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Comments and Casenotes

Due Process Objection To Jurisdiction Over Foreign Corporations Not "Doing Business" Within The State

*Erlanger Mills, Inc. v. Cohoes Fiber Mills, Inc.*¹

Erlanger Mills, Inc., a North Carolina Corporation engaged in the manufacturing of textile products, sent certain agents to call upon Cohoes Fiber Mills, Inc., located in Cohoes, New York, for the purpose of discussing the possible purchase of rayon garnet manufactured by Cohoes. Subsequent to this visit, Erlanger placed its order with Cohoes. Every part of the transaction took place in New York, including the technical delivery to the buyer through the shipment of the goods f.o.b. Cohoes, New York. Erlanger began to use the rayon garnet, but shortly thereafter it complained that the yarn was defective. After several communications between the parties, the general manager of Cohoes, one Crowther, agreed to visit Erlanger and discuss the complaint. While in North Carolina, Crowther was served with a summons against Cohoes. Erlanger conceded the fact that Cohoes, up to this transaction, had never done any business in North Carolina, nor with a North Carolina citizen or corporation, but it claimed that service upon Crowther was valid under the North Carolina statute,² the relevant portion of which provides as follows:

"Jurisdiction over foreign corporations not transacting business in this State — (a) Every foreign corporation shall be subject to suit in this State, by a resident of this State or by any person having a usual place of business in this State, whether or not such foreign corporation is transacting or has transacted business in this State and whether or not it is engaged exclusively in interstate or foreign commerce on any cause of action arising as follows: . . .

"(3) Out of the production, manufacture, or distribution of goods by such corporation with the *reasonable expectation that those goods are to be used or con-*

¹ 239 F. 2d 502 (4th Cir., 1956).

² GEN. STATS., NORTH CAROLINA (1955 Cum. Supp. §55-38.1.

sumed in this State and are so used and consumed, regardless of how or where the goods were produced, manufactured, marketed, or sold or whether or not through the medium of independent contractors or dealers;"³

Cohoes moved to quash the service on the ground that this statute was a denial of due process of law under the Fourteenth Amendment to the Constitution. The service was quashed in the Federal District Court, and, on appeal, the United States Court of Appeals for the Fourth Circuit affirmed.

The primary question involved in this case was whether or not a state may validly pass a statute which would give it jurisdiction over a foreign corporation upon a single sale, consummated completely without the state, but with the reasonable expectation that those goods were to be used in the state. Erlanger contended that the "minimum contacts" test which was laid down in *International Shoe Co. v. Washington*⁴ liberalized the law to a degree sufficient to allow a state to maintain jurisdiction over a foreign corporation which does no more than to ship its product into North Carolina on one occasion for use in that state. The Court agreed that the "minimum contacts" test, did have liberalizing tendencies, but it still could not justify jurisdiction on the minimal contacts that Cohoes had with North Carolina. Therefore, the North Carolina statute, as applied to this case, was found to be invalid.

Though the recent trend in interpreting state statutes providing for jurisdiction over foreign corporations indicates increasing liberality, in no other case on this point have there been so few contacts between the foreign corporation and the state. In every other case — whether a tort action or for breach of contract — the cause of action arose out of an act which was committed or performed within the state in which the suit was initiated. Even in the far reaching case of *Smyth v. Twin State Improvement Corp.*,⁵ the Vermont Court, showing just how little activity

³ Italics supplied by the Court, *supra*, n. 1, 504.

⁴ 328 U. S. 310, 161 A. L. R. 1057 (1945).

⁵ 116 Vt. 569, 80 A. 2d 664, 25 A. L. R. 2d 1193 (1951). In this case the defendant, a foreign corporation, came into Vermont to repair plaintiff's roof. The job was done in a negligent manner, and the court held that jurisdiction could be had in Vermont, under the Vermont statute, for this singular act which took place in Vermont. The court sets forth the reason for their decision at page 668:

"No sound reason appears to exist why foreign corporations may not be held responsible in Vermont for wrongful acts done in Vermont. If a foreign corporation voluntarily elects to act here, it should be

was required for the purpose of subjecting a foreign corporation to local jurisdiction, still pointed out the fact that the tort was committed within the state in which the suit was initiated.⁶

In 1937, the Maryland Legislature enacted a statute⁷ allowing Maryland residents, or persons having their usual place of business in the state, to bring suit against a foreign corporation for any contract made *within* the state or for any liability incurred for acts done *within* the state.⁸ Subsequent to the passage of this statute, the first of its kind, several articles were written speculating upon whether or not this "unique" subsection of the statute could be legally sustained against objections based upon the due process clause of the Fourteenth Amendment.⁹ An article,¹⁰ written in Maryland by Professor Reiblich, reasoned that the statute should be valid in its entirety and stated as to this part of the statute, "It is submitted, that whatever the theoretical or conceptual argument that may need to be raised to support it, subdivision (d) represents a sound social policy and should be sustainable against the due process objection."¹¹

answerable here and under our laws. The consequences imputed to it lie within its own control, since it need not act within this state at all, unless it so desires."

⁶ For a full discussion of the power of a state to subject a foreign corporation to the jurisdiction of its courts on the sole ground that the corporation committed a tort within the state, see the annotation under that heading in 25 A. L. R. 2d 1202.

⁷ Md. Code (1924), Art. 23, Sec. 118(d), as amended, Laws 1937, Ch. 504. This section of Article 23 was subsequently changed to section 119(d) in Md. Code (1939), and is presently referred to as Article 23, Section 88(d), Md. Code (1951).

⁸ The exact wording of the relevant subsection is as follows:

"Section 88 (Suits Against Foreign Corporations) . . . (d) Every foreign corporation shall be subject to suit in this State by a resident of this State or by a person having a usual place of business in this State on any cause of action arising out of a contract made within this State or liability incurred for acts done within this State, whether or not such foreign corporation is doing or has done business in this State."

In subsections (a), (b) and (c), the suit to be brought is qualified as being against foreign corporations doing or having done intrastate, interstate, or foreign business within the State of Maryland.

⁹ Myerberg, *Revision of the Maryland Corporation Law*, the *Daily Record*, Oct. 15, 1937; Reiblich, *Jurisdiction of Maryland Courts Over Foreign Corporations . . .*, 3 Md. L. Rev. 35 (1938); Note, *Revision of the Maryland Foreign Corporation Law: An Advance*, 38 Col. L. Rev. 1060 (1938). All wholeheartedly approved of the statutory jurisdiction over a foreign corporation for acts done within the state, and the latter concludes with the following on page 1078: "The concept embodied in the subsection is at best embryonic, but may soon find expression in the cases."

¹⁰ Reiblich, *ibid.* A discussion as to the probable validity of the particular subsection concerned is found on pages 67-72.

¹¹ *Ibid.*, 71.

Relatively few states¹² have passed similar statutes, possibly because of the fear that Maryland had exceeded its police powers by enacting a statute that might be found to be unconstitutional as a denial of due process of law. Because of this, judicial interpretation on this subject is also extremely limited, and most of the important decisions on point seem to have arisen under our own Maryland statute.¹³

The first case in which the specific subsection¹⁴ of the Maryland statute was mentioned was some six years after the statute was passed. In that case,¹⁵ the United States District Court, found that the foreign corporation *was* doing business in Maryland, and, therefore, declined to rule upon the constitutionality of subsection (d). However, the Court expressed some doubt as to whether this section of the statute would survive attack upon the basis of a denial of due process, stating in part:

“We will add, however, that if the conclusion which we have reached in this opinion be correct, it is difficult to see how the broad provisions in the Maryland law just referred to can be upheld in the face of the requirements for due process upon which our conclusion is based. We have been referred to no reported decision of the Maryland Court of Appeals or of any other Court which has interpreted that provision.”¹⁶

It is to be noted, however, that this case preceded the *International Shoe Co. v. Washington*¹⁷ case, and the Court was still laboring under the old jurisdictional doctrines of “constructive presence” and “doing business” when the above quoted statement of doubt was expressed.

¹² These states are Arkansas, Missouri, and Vermont, and the statutes, in chronological order are as follows: Miss. CODE ANN., Sec. 1437 (1940); ARK. STAT., Sec. 27-340 (1947); VT. REV. STAT., Sec. 1562 (1947). However, there were other states that either had or later enacted statutes providing for jurisdiction over non-residents or foreign corporations which were limited to specialized fields. Cf. *Hess v. Pawloski*, 274 U. S. 352 (1927) (use of state highways); *Travelers Health Assn. v. Virginia*, 339 U. S. 643 (1950) (sale of insurance within the state); *Doherty & Co. v. Goodman*, 294 U. S. 623 (1935) (sale of securities within the state).

¹³ *Supra*, n. 7.

¹⁴ *Supra*, n. 8.

¹⁵ *Edgewater Realty Co. v. Tennessee Coal, Iron and Railroad Co.*, 49 F. Supp. 807 (D. C. Md., 1943).

¹⁶ *Ibid.*, 816.

¹⁷ 326 U. S. 310, 161 A. L. R. 1057 (1945). In this case the entire doctrine of jurisdiction over foreign corporations was changed, and the use of the liberalizing key phrases of “minimum contacts” and “traditional notions of fair play and substantial justice” first came into use.

There was another lapse of seven years before the specific subsection in question was finally interpreted in *Johns v. Bay State Abrasive Products Co.*,¹⁸ a 1950 case. That case involved two foreign corporations, Bay State and Reed Roller Bit Co., as codefendants. Plaintiff, a Maryland resident, was injured when a grinding wheel manufactured by Bay State shattered while being used on a machine manufactured by Reed Roller, the latter having recommended the particular type of wheel to be used on its machine. Neither defendant was "doing business" in Maryland, and the machine and grinding wheel were both purchased from an independent machinery company in Baltimore; nor did either defendant have an office, telephone listing, bank account, or warehouse in Maryland. The United States District Court held that service under section 119(d)¹⁹ of Article 23 was a denial of due process under the Fourteenth Amendment when that section was applied to Bay State, since there had been no contract or transaction within the State of Maryland. As to Reed Roller, however, the Court held that they did have jurisdiction over this company since there was more than mere solicitation — there was an agent living in Maryland with a Maryland registered automobile, and it was this company that had negligently recommended the use of the Bay State grinding wheel to be used with its own product. The Court concluded by stating that there would be factual situations in which the application of the subdivision of this statute would be inconsistent with due process of law.²⁰

This view that a single tort or contract within the state might not be sufficient to subject the foreign corporation to the jurisdiction of the state, was short lived. In the next relevant case,²¹ the Maryland Court of Appeals held that a

¹⁸ 89 F. Supp. 654 (D. C. Md., 1950).

¹⁹ Again, it is necessary to observe that Art. 23, Sec. 119(d), has been amended in the Md. Code (1951), and is presently Sec. 88(d) of Art. 23. See n. 7, *supra*.

²⁰ "Without unduly extending this opinion, the result of my reflection about the statute is that it can properly be given valid application to a *limited extent*. Consistent with the approach adopted by Chief Justice Stone in the Shoe Company case . . . I think it will be necessary to test the proper application of the statute by a process of inclusion and exclusion hereafter to the several factual situations as they are presented. The conclusion in each case must be based upon a fair consideration of all the relevant factors, including, among others, the nature and extent of the corporation's actual activities within the state . . ." *Supra*, n. 18, 662. (Italics supplied.)

²¹ There was one intervening case, *Park Beverage Co. v. Goebel Brewing Co.*, 197 Md. 369, 79 A. 2d 157 (1951), but the court in this case had no need to use the statute because the final contract was not consummated within the state. If, therefore, the North Carolina statute used in the *Erlanger v. Cohoes* case, had been the same as the Maryland statute, there would

single transaction within the state was sufficient to obtain jurisdiction over the foreign corporation. This far reaching decision, rendered in 1954, was *Compania de Astral v. Boston Metals Co.*²² Even though the ships to be purchased by Astral were in Maryland, an escrow fund was established here, and Astral inspected the ships and signed the contract of purchase here, the Court found that all of these acts amounted to "what was but a single transaction . . ."²³ While pointing out that there were insufficient contacts in or with Maryland to say that Astral was "doing business" here, the Court stated that "the contacts of Astral with the State of Maryland were sufficient to sustain a suit against it in this State under the test of due process stated in *International Shoe Co. v. Washington* . . ."²⁴ The holdings of this and of the *Smyth* case,²⁵ make it apparent that a state may validly obtain jurisdiction over a foreign corporation which has performed or committed a single act *within* the state, whether that act be one of contract or tort, without first obtaining actual or fictional consent from the foreign corporation being sued.²⁶ These two decisions appear to represent the most liberal stand taken by the courts. The theory upon which the courts have relied in upholding the constitutionality of these statutes is best summed up in the *International Shoe Co.*²⁷ case, where it was said:

"But to the extent that a corporation exercises the privilege of conducting activities *within a state*, it enjoys the benefits and protection of the laws of that state. The exercise of that privilege may give rise to obligations, and so far as those obligations arise out of or are connected with the activities *within the State*, a procedure which requires the corporation to respond to a suit brought to enforce them can, in most instances, hardly be said to be undue."²⁸

probably have been little doubt that the case would have been dismissed without question, since the contract was made without the state of the forum, *i.e.*, North Carolina.

²² 205 Md. 237, 107 A. 2d 357 (1954), *cert. den.* 348 U. S. 943 (1955).

²³ *Ibid.*, 261. For a complete annotation on the validity of statutes subjecting a foreign corporation to jurisdiction for a contract made within the state, see 49 A. L. R. 2d 668.

²⁴ *Ibid.*, 265.

²⁵ 116 Vt. 569, 80 A. 2d 664, 25 A. L. R. 2d 1193 (1951).

²⁶ *Olberding v. Illinois Central R.R. Co.*, 346 U. S. 338 (1953), noted in 14 Md. L. Rev. 62 (1954).

²⁷ *Supra*, n. 17.

²⁸ *Ibid.*, 319. Italics supplied.

This brings us to the very essence of the problem presented in the *Erlanger* case, *i.e.*, did the particular section of the North Carolina statute in question violate the Fourteenth Amendment through a denial of due process of law? It was the opinion of the Court that it did. The single interstate shipment of goods to be used in North Carolina was held not to be sufficient contact to allow the North Carolina court to obtain jurisdiction over Cohoes. But for this bare association with North Carolina, Cohoes had no contacts whatsoever with North Carolina. It was Erlanger who came to New York to negotiate the purchase, the contract of sale was signed in New York, and the goods were shipped f.o.b. New York, thereby making Erlanger the owner of the property before the goods ever left the state. The Court was unwilling to hold that Cohoes had even a "minimum contact" with North Carolina under these facts.

Accordingly, since Erlanger came to Cohoes, it is difficult to see how it can be said that Cohoes had any benefit or protection from North Carolina. This tends to defeat one of the primary reasons for allowing a state to obtain jurisdiction over a foreign corporation, *i.e.*, since the corporation would be protected by the state laws, it should be subject to the state laws as well. Even though it is true that the recent trend had been towards a broader exercise of jurisdiction over foreign corporations through the enactment of statutes, criticism²⁹ of the existing statutes suggests that the outside limits may already have been reached in the *Astral* case,³⁰ relating to contracts, and in the *Smyth* case,³¹ relating to torts. If the North Carolina statute were to be sustained, the doctrine of "minimum contacts" would afford a foreign corporation little protection, for it could be required to defend suits initiated in any state into which its goods were shipped. The question must be answered, ultimately by the Supreme Court, whether such a result offends the "traditional notions of fair play and substantial justice" as set out in the *International Shoe Co.* case.³²

The question is a close one, and not all of the weight lies with the decision of the instant case. The state has, under its police powers,³³ power to enact such legislation as will

²⁹ See 40 Va. L. Rev. 1083 (1954) and 27 Notre Dame Lawyer 117 (1951).

³⁰ *Supra*, n. 22.

³¹ *Supra*, n. 25.

³² 326 U. S. 310, 316, 161 A. L. R. 1057 (1945).

³³ Constitution of the United States of America, Tenth Amendment. Also, see the *International Shoe* case, *supra*, n. 32, 325:

"Nor can I stretch the meaning of due process so far as to authorize this Court to deprive a State of the right to afford judicial protection to its citizens on the ground that it would be more 'convenient' for the corporation to be sued somewhere else."

protect the welfare of its citizens.³⁴ The foreign corporation, should there be a hardship in being brought into a state court under such a statute, could have the case removed from the state court to a federal court,³⁵ and then file a motion of *forum non conveniens* to transfer the case to another federal court.³⁶ Of significance is the modern trend in defining *due process* of law: "a trend from emphasis on the territorial limitations of courts, to emphasis on providing notice and an opportunity to be heard."³⁷ In the *Erlanger* case both were present: notice directly to the general manager of Cohoes, and an opportunity to be heard in North Carolina.

Nevertheless, the Fourth Circuit found that, taking all of the facts of the *Erlanger* case into consideration, shipping goods into North Carolina for use there under one sale, fully consummated in New York, was not sufficient "minimum contact" with North Carolina to sustain jurisdiction of its courts. Until reversed, or overruled, *Erlanger* suggests summarizing the law as being that unless the transaction or act from which the suit arose actually took place *within* the state,³⁸ or the foreign corporation has had "minimum contacts" with a state or its citizens greater than mere use of goods from one out of state sale,³⁹ a state cannot subject a foreign corporation to a suit within its jurisdiction.⁴⁰

Whether this decision stands or not, the constitutionality of the Maryland statute⁴¹ probably will not be affected. In order to subject the foreign corporation to its jurisdic-

³⁴ The foreign corporation has been held to have constructive knowledge of such laws. See Md. Code (1951), Art. 23, Sec. 85:

"Every foreign corporation doing intrastate or interstate or foreign business in this State shall be deemed thereby to have assented to all the provisions of the laws of this State."

³⁵ 28 U. S. C. A., Sec. 1441(b) (1952).

³⁶ *Ibid.*, Sec. 1404(a).

³⁷ Note, *The Growth of the International Shoe Doctrine*, 16 U. of Chi. L. Rev. 523, 536 (1949).

³⁸ That is, unless the final contract was consummated *within* the state (Astral case, *supra*, n. 22) or the tort actually occurred within the state (Smyth case, *supra*, n. 25).

³⁹ *Cf.* *Travelers Health Association v. Virginia*, 339 U. S. 643 (1950). In this case a Nebraska mail order health insurance company was held to be subject to Virginia jurisdiction under the rules stated in *International Shoe Co.* case, even though the defendant had no other contacts with Virginia than the continual sending of policies into that state.

⁴⁰ It is interesting to note that the Court in the *Erlanger* case concluded by stating that "the North Carolina statute *as applied to this case* is invalid". 239 F. 2d 502, 509 (4th Cir., 1956). (Italics supplied.) From language such as this one may only speculate as to whether or not the use of goods shipped into a state on more than one occasion would be sufficient minimum contact to bring a foreign corporation within the jurisdiction of the court under a statute similar to the North Carolina statute in question.

⁴¹ Md. Code (1951) Art. 23, Sec. 83(d).

tion, the Maryland statute requires an act to be performed or committed *within* the state. The cases reviewed herein show almost conclusively that such an act within the state constitutes sufficient "minimum contact" to satisfy the requirements of due process of law.

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