

Indemnities And Jurisdiction

When corporations sell subsidiary businesses, it is common for the seller to indemnify the buyer for certain liabilities. An unfortunate byproduct of this is the growing phenomenon of third party tort claimants suing the seller directly, practically because the seller may be in better financial position but technically on claims that the tort plaintiff is a third party beneficiary to the indemnity agreement. That claim is suspect on the merits, but in many cases, the threshold issue is whether the court has personal jurisdiction over the indemnitor, the former parent of the business that was sold. We analyze this issue.

A Short Primer on Personal Jurisdiction

There are two general bases for asserting jurisdiction over a company. The doctrines are referred to as general jurisdiction and specific jurisdiction. While the two doctrines are closely related,

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there are meaningful differences. The former doctrine allows a court to assert jurisdiction over a corporation if it has "minimum contacts" with the State such that the corporation had "fair warning" that it might be required to defend itself in that jurisdiction. In this circumstance, it does not matter if there is any connection between the event giving rise to the lawsuit and the location of the lawsuit. All that matters is that the defendant conducts business regularly in the forum state. Specific jurisdiction, on the other hand, arises when the corporation's actions, while not sufficient to create general jurisdiction, actually give rise to the claim at issue. A holding company parent, by way of example, has the requisite "minimum contacts" at the very least with the state in which it is incorporated and the state where it maintains its principal place of business. It may not have "minimum contacts" with any other jurisdiction if it does not sell products or otherwise do business in other states. A company that places product into the stream of commerce will be subject to both general and specific jurisdiction wherever that product is sold, used or causes injury. A service provider, on the

other hand, may find itself subject to specific jurisdiction only in areas where it has performed services.

Legacy Liabilities and Jurisdiction

Here is the typical fact pattern: Buyer acquires the assets of an operating business in a transaction involving the operating business and its parent. The seller and parent agree to indemnify buyer for liability claims associated with conduct that occurred prior to the date of the transaction. Over time, the selling corporation is merged into other subsidiaries and is not easily located. Third party claimants sue the seller's parent in a state other than that where the company is incorporated or has business operations. The rationale for suing the parent is its deep pockets. The articulated theory is that the former parent is the successor to the seller and therefore responsible for seller's liabilities. While that theory will be contested at an appropriate time, the first issue is jurisdiction. There is no doubt that the seller, were it still in existence, would be subject to jurisdiction in the forum court. There also is no doubt that the parent would not be subject to jurisdiction absent the indemnity agreement. The question, then, is whether the indemnity agreement is enough to create specific jurisdiction based on the allegations of the complaint.

Jurisdiction Is Probably Not Created By An Indemnity Agreement

Very few courts have ruled on this issue, but those that have seem to conclude that the indemnity obligation does not create jurisdiction. The Texas Court of Appeals for the First District recently issued a ruling in a case involving a fact pattern very similar to that outlined above. The trial court had found the indemnity provision to be a sufficient basis for jurisdiction. The appellate court reversed, relying both on its conclusion that the indemnity provision is a contract between buyer and seller and does not confer rights on the plaintiff, but also on its conclusion that the plaintiff's claim does not arise out of the indemnity agreement but rather the actions of the seller. See *Koll Real Estate*

Company v. Purseley, 2003 WL 22382623 (Tex. App. [Houston], October 16, 2003). The court held that “even if we assume that Koll, as corporate successor to Henley II, has a contractual obligation to indemnify Dresser (pursuant to the Purchase Agreement), ... we do not believe such a contractual obligation, alone, is sufficient to support an assertion of personal jurisdiction over Koll in this case.” The court relied on a Texas Supreme Court ruling that a reinsurance contract did not provide a basis for jurisdiction for a claim by the insured, since the reinsurer agreed only to cover losses by the insurer, not the insured.

New York likewise has found indemnity agreements to be an inadequate foundation for jurisdiction. In *Media Corp. of America v. Motif Manufacturing Co.*, 524 F. Supp. 86,87 (SDNY 1981), the court stated that “the rule in New York is clear that an indemnity agreement alone does not provide a sufficient contact with New York simply because the underlying events that trigger the indemnification occur in New York.”

Illinois is another state where this issue has been tested. Illinois law also holds that a mere indemnification obligation does not give rise to personal jurisdiction. In *Kerr v. Conrail*, 103 Ill. App. 3d 61 (5th Dist. 1981), the court considered the issue of whether a circuit court had jurisdiction over a non-resident based on a contractual agreement to indemnify another. The court found that jurisdiction did not exist in such circumstances and stated,

Neither can the indemnity provision in the transportation services contract between Center Cabs and defendant serve as a basis for finding that Center Cabs voluntarily submitted to the court’s jurisdiction....In the absence of an express contractual understanding that Center Cabs would voluntarily submit to the court’s jurisdiction, *the indemnity provision cannot be so construed*. Therefore, we find that Center Cabs did not consent to jurisdiction of the courts of Illinois.

Other cases reach the same conclusion. See *Lopez v. Huber, Hunt & Nichols, Inc.*, 1985 WL 1868, *2 (N.D. Ill. 1985) (“Defendants’ position as potential indemnitors of other defendants over who the court does have jurisdiction does not bring them within the court’s personal jurisdiction.”); *Rohde v. Central R.R. of Indiana*, 930 F.Supp.

1269, 1273 n.4 (N.D. Ill. 1996) (the mere fact that a defendant has taken on indemnification obligations does not create contacts sufficient to support jurisdiction).

This result follows from the fact that many such indemnity agreements are structured as “net of insurance” agreements. That is, an indemnity obligation arises only when available insurance coverage no longer exists to cover such claims. Understanding that indemnity obligations frequently are conditional, courts would be wise to avoid expanding the contractual rights and obligations created by the parties to the contract.

Lessons Learned

In litigating this issue recently, certain lessons emerged. First, agreements that provide indemnities should be clear and unambiguous that the intended beneficiary is only the contracting party and that third parties are not considered to be beneficiaries under the Agreement. Second, conditions on the indemnity, including sunset provisions or net of insurance provisions, must be clearly articulated. Third, if the selling subsidiary survives the transaction, the parties should make clear the intent that the parent’s indemnity obligation is triggered only if all avenues of recovery from the selling entity are exhausted, including seeking indemnity directly from the seller in the first instance.

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