When US Subsidiaries Are Ordered to Produce Documents From Their Non-US Parents: the Risks and Some Responses

Key Points

- A US subsidiary may be ordered to produce documents from its non-US parent in US litigation even if the non-US parent is not a party to the case and is not subject to US jurisdiction.
- A court can order production of parent documents if it finds that the documents are in the subsidiary's "control" or if the subsidiary is an agent or alter-ego of the parent.
- Appropriate document control policies at the sub and parent can reduce the risk that the sub will be ordered to produce parent company documents.

Nearly every non-US company involved in international commerce knows and fears the reach of US courts and the scope of US discovery. There is good reason for that concern. US-style discovery can be expensive, burdensome, time-consuming and intrusive. There is nothing analogous in most countries.

Companies do many things to protect themselves from becoming subject to US jurisdiction. They avoid doing business directly in the US and work through subsidiaries and distributors. They carefully structure their relationships with their US subsidiaries and deal with US subs on arm's-length terms. But having taken all the right steps to avoid becoming subject to US *jurisdiction*, has a non-US company done all it can to avoid having to produce documents in a US litigation?

The answer is "No." Even if a company cannot be made a party to a US suit, its documents and information may still be subject to discovery in US litigation in which its subsidiary is involved.

A US Sub Must Produce Its non-US Parent's Documents If They Are in the Sub's Control

Under US court rules, parties to a case – plaintiffs and defendants – can be required to produce documents in their "possession, custody or control." When the US subsidiary of a non-US company is sued, plaintiffs often attempt to obtain parent company documents

from the subsidiary on the basis that the parent's documents are within the sub's "*possession, custody or control*."[1]

If a non-US company entrusts copies of its documents to its US subsidiary – if, for example, the parent's documents are in file cabinets in the US – the subsidiary can be compelled to produce those documents on the basis that they are in the sub's possession. The subsidiary cannot resist production by arguing that the documents belong to the parent.

Digitally stored information is usually held to be in a sub's possession as long as the sub can access it. A parent's electronically stored data that is directly accessible to its US sub, such as emails or documents stored in a shared system, may be subject to production even if it is accessed on a server in Japan.

A subsidiary is generally understood to have control over documents or information possessed by its parent if the subsidiary has the legal right to obtain the documents on demand. Many US courts also find that a sub has control of parent documents if the sub has the "practical ability" to obtain the documents in the ordinary course of business, even if it has no legal right to them.[2]

The ability to obtain something upon request might seem to suggest a lack of control. Nonetheless, many US courts, sometimes with little reflection, interpret evidence that a sub obtained documents on request in the past or would likely have obtained them if it requested them as evidence of "control" for purposes of ordering the sub to produce parent documents. That the parent might refuse to produce the documents when asked to provide them for purposes of the litigation is not evidence that the sub does not control them, and does not relieve the sub of its obligation to produce them.

A sub's control over parent documents is generally shown through two types of evidence. The plaintiff may try to show (i) that the parent has provided similar kinds of documents

[1] If the non-US parent is not subject to US jurisdiction itself, the US court cannot directly order the parent to produce discovery for the US litigation. But the subsidiary can be ordered to obtain documents from the parent. If the parent refuses to provide them, the subsidiary can be financially penalized and its case weakened.

[2] *See* The Sedona Conference, *The Sedona Conference Commentary on Rule 34 and Rule 45 "Possession, Custody or Control,"* 17 SEDONA CONF. J. 467, 492 (2016) (courts in the First, Third, Fourth, Fifth, Sixth, Seventh, Eighth, Ninth, Tenth, and Eleventh Circuits have applied a version of the "legal right" standard, while courts in the Second, Fourth, Eighth, Tenth, Eleventh, and D.C. Circuits have applied the "practical ability" standard).

in the past; or (ii) that the corporate relationship between parent and sub is sufficiently close that documents available to one are available to the other.[3]

Evidence of Document-Sharing Practices Can Establish "Control"

In a typical case, a plaintiff had been injured in a jet ski accident.[4] The plaintiff sued the US sub of the Japanese manufacturer; the parent was not subject to US jurisdiction. The plaintiff asked in discovery for information about the jet ski's compliance with safety standards. A sub executive testified that he sometimes requested and received information about testing and product specifications from the Japanese parent. The court concluded that the requested information fell within a general type of information that the subsidiary could obtain on request and ordered the subsidiary to produce it.

A non-US company can open the door to broad discovery of its documents by providing documents to its sub to assist the sub in defending itself. The US subsidiary of a Korean manufacturer was sued for damage caused by a washing machine.[5] In response to a document request, the subsidiary produced a diagram of the washing machine's circuit board. The sub had obtained the document from the Korean parent in the course of preparing to defend the case. The plaintiff moved to compel production of all similar and related parent documents. The sub protested that it did not control these documents. The court held that by obtaining the single circuit board diagram, the subsidiary "has demonstrated its ability to obtain the requested information and documents" and hence was in "control" of them.

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[3] *See, e.g.*, *Estate of Colomb ex rel. Colomb v. Nissan N. Am., Inc.*, No. 4:08-CV-76-F(3), 2009 WL 10705311, at *3-4 (E.D.N.C. Oct. 2, 2009) (finding control where the parent and subsidiary had overlap in the membership of their respective boards, did not distinguish between the corporate identities of the parent and subsidiaries, and regularly shared documents, databases, and information related to the requested materials).

[4] *Lutes v. Kawasaki Motors Corp., USA*, No. 3:10CV1549 WWE, 2014 WL 7185469, at *5 (D. Conn. Dec. 16, 2014).

[5] *Slabaugh v. State Farm Fire & Cas. Co.*, No. 1:12-CV-01020-RLY, 2013 WL 4777206, at *6 (S.D. Ind. Sept. 5, 2013). *But see Princeton Digit. Image Corp. v. Konami Digit. Ent. Inc.*, 316 F.R.D. 89, 94 (D. Del. 2016) (finding no control and refusing to require the US company to produce a document from its non-US sister company where there was no evidence of the relationship between the companies or the role of the non-US company in the US litigation, even though the US company had obtained documents from the non-US company and produced them in the litigation).

Evidence of Corporate Relationships Can Establish "Control"

Courts often assume that a parent company has control of documents in its sub's possession in virtue of the corporate relationship between them.[6] There is no reason to think that the opposite presumption should apply: subs seldom control their parents.

But courts do sometimes conclude that a parent is so pervasively involved in the activities of its sub and so dominates the sub's affairs that there is no real distinction between them. In that situation, the court may find that the sub can obtain information from its parent. This concept is similar to the principle that when a parent mingles its business with its subsidiary's without regard for the corporate form, the two become "alter-egos" and can be responsible for each other's liabilities. In many US courts, a parent's control over a subsidiary's day-to-day activities need not rise to the level required to establish alter-ego liability to show that the parent's documents are in the subsidiary's control. Some courts find that a sub controls its parent's documents based on features that are characteristic of most parent-subsidiary relationships. In many cases, analysis of corporate relationships is combined with consideration of past document-sharing practices to establish the sub's control of parent documents.

A patent infringement case demonstrates how courts can take into consideration both corporate structure and direct evidence of the subsidiary's ability to obtain documents from the parent in finding control.[7] The plaintiff asked the court to compel a US subsidiary to produce the documents of its German parent, which had designed and manufactured the allegedly infringing items. The subsidiary's directors were all officers of the parent; the CEO of the subsidiary was the head of an operating division at the parent, which paid his salary; and the head of the parent's finance department oversaw the subsidiary's finances. The parent appeared to control the litigation itself: it assigned patents to the sub after the suit commenced and then filed counterclaims based on them without the knowledge of the sub's board. The parent had already provided several documents to the sub that the sub produced in the litigation. The court held that the relationship between the companies and their history of sharing documents demonstrated sufficient control to require the sub to produce its parent's documents.

Types of Parent Company Information That a Subsidiary Can Be Ordered to Produce

A subsidiary of a non-US company can be required to produce documents from its parent and to respond to interrogatories – written questions – concerning its parent. The type of documents that a sub can be ordered to provide, in US state or federal court, includes

[6] *See, e.g., In re: Ski Train Fire of Nov. 11, 2000 Kaprun Austria*, No. MDL 1428(SAS)THK, 2006 WL 1328259, at *6-*8 (S.D.N.Y. May 16, 2006) (German company subject to US jurisdiction ordered to produce documents from its Austrian subsidiary).
[7] *Afros S.P.A. v. Krauss-Maffei Corp.*, 113 F.R.D. 127, 132 (D. Del. 1986).

electronically stored information, letters, contracts, emails and cell phone records. Data that is maintained in databases or only preserved in back-up tapes may also have to be produced. The Federal Rules require parties to produce:

> any designated documents or electronically stored information – including writings, drawings, graphs, charts, photographs, sound recordings, images, and other data or data compilations – stored in any medium from which information can be obtained either directly or, if necessary, after translation by the responding party into a reasonably usable form.[8]

A subsidiary generally cannot be ordered to provide an employee of the parent company to testify at a deposition, unless the individual is also an employee of the sub.[9] Depositions can sometimes be used to obtain parent company information in one situation. A corporate party can be deposed through a corporate representative, who is required to testify about information known or reasonably available to the corporation. When a subsidiary is found to have control over parent company information, the sub's corporate representative may be required to testify about information held by its foreign parent company that is subject to the sub's control. One court stated: "if a corporate [party] controls information possessed by a nonparty foreign affiliate, the knowledge is subject to the . . . deposition notice . . . [and the] corporate designee may be compelled to testify about information possessed by a foreign corporate affiliate."[10]

Designing Document Control Policies to Reduce Non-US Parents' Exposure To US Discovery Through Their US Subs

The most important step a non-US parent company and its US subsidiary can take to limit the risk that the subsidiary will be required to produce parent company information is to implement document control policies limiting document and information sharing between the companies. Policies should be adopted by the parent and made known to the sub as appropriate.

An effective document control policy must be tailored to the particular circumstances of each company; there is no "one size fits all" solution. A document control policy should protect above all the parent's most sensitive documents and information, whatever that may be. But document control policies must also be practical. They must address the

[8] "Translation" here means conversion from one form of data, such as a relational database, to a more usable form. The burden of translating materials into English usually rests on the party requesting production.

[9] Depositions are a means of taking the sworn testimony of a witness in a proceeding that is conducted between lawyers with no judge present. Depositions are often preserved in video recordings that can be played at trial.

[10] *In re: Benicar (Olmesartan) Prods. Liab. Litig.*, 2016 WL 5817262 at *5 (D.N.J. Oct. 4, 2016); *see Sanofi-Aventis v. Sandoz, Inc.*, 272 F.R.D. 391, 394-95 (D.N.J. 2011) (collecting cases); *but see In re: Ski Train Fire*, 2006 WL 1328259, at *9 (refusing to require a corporate representative to "acquire all of the knowledge of the subsidiary on matters in which the parent was not involved").

reality of day to day workplace interaction. A document control policy that looks "perfect" on paper but is unworkable in practice is useless. An effective document control policy requires careful thought and design; guidance from counsel experienced with discovery battles in US litigation seeking non-US parent company documents can be helpful in creating a practical and effective policy. It also must be remembered that applicable legal standards are not consistent across US jurisdictions: procedures that are appropriate in one jurisdiction may be inadequate in another.

The following considerations are often relevant to the design of an effective document control policy:

- The policy should be written and made known to parent personnel with contact with the sub. Employees may be required to sign to acknowledge that they have read the policy and will comply with it.

- A document control policy describes both types of information that will be provided to the sub and information that will not be provided. Information provided to the sub should be limited to what is necessary to perform the sub's business functions.

- Care should be taken to consider the particular needs and risks of the business and areas of heightened sensitivity. Bright-line rules that are easy to follow and to enforce can be put in place, with an exception process if necessary.

- A document policy may make certain types of documents available to a sub on request – *e.g.*, "Sub may request such employee records as it requires." But such rules should be written with the knowledge that some US courts may interpret them as giving the sub control over all documents within a broad category, not just those the sub requested.

- If practical, the sub should ideally have little or no direct access to the parent company's systems, records, databases, document management systems, or email files.

    - The parent may be able to configure its electronic systems so that the sub is automatically blocked from accessing the parent's data. If the sub requires access to a limited category of information relevant to its business functions, that category can be defined in the document control policy and the business purpose recorded.

    - If possible, sub employees should not be able to search parent systems. Sub IT personnel should be subject to the same limits on parent system access.

- The risks presented by two-hat employees should often be expressly addressed. Two-hat employees are all but inevitable: parents almost always have representatives on a sub's board, and often have employees acting in other capacities at the sub.

    - Because any information to which the two-hat employee has access is at heightened risk of disclosure, the two-hat employee should be given access to no more parent company information than is needed to perform his or her job. It may be possible to wall off the two-hat employee through automatic means such as electronic barriers from categories of sensitive parent data or documents that the employee does not need.

    - Two-hat employees nonetheless are likely to come into possession of information or documents in their capacity as parent company employees that they should not make available to subsidiary employees. Written policies, acknowledged by the employee, can make clear that safeguarding the parent's confidential information from disclosure to the sub is a requirement of the employee's terms of employment.

- Short-term secondees present similar risks.

    - They may join a US sub with confidential information from their prior position in their possession. Their access to systems or information relating to their prior position at the company that is unnecessary to their job at the sub can be cut off and they can be required to return any documents in their possession before they take up their position with the sub.

    - Because their tenure at the sub is short-term, they pose a particular risk of viewing themselves as owing reporting obligations primarily to parent employees. Written policies can make clear that it is an obligation of their job to avoid obtaining or divulging information to parent employees through back-channels that evade subsidiary reporting structures and procedures.

- Document control policies should be known and followed. Compliance with the document control policy can be documented. The document control policy can be mentioned in job descriptions and office procedures.

- Document control policies should be practical. They should include procedures that can be followed in the ordinary course of business without undue burden or distraction. More demanding procedures are appropriate for ensuring that highly sensitive information is not shared with a sub.

Avoiding a finding that the sub and parent are alter egos, or that their businesses are so comingled that asking for documents from the sub is no different from asking the parent, raises broader issues than merely limiting discovery risk. An alter-ego finding can subject the parent company to US jurisdiction and even lead to parent company liability for a subsidiary's actions. Steps taken to limit the risk of jurisdictional and liability exposure will decrease discovery exposure as well.

When Litigation Arises Involving a US Sub

When a sub is sued and plaintiffs start requesting parent documents, a well-executed document control policy shows its value. The sub should be able to demonstrate that the parent has placed systematic limitations on the sub's access to parent documents. If limited discovery from the parent occurs – discovery to show that there is no basis for discovery – the parent will be prepared to produce a written document control policy limiting the sub's access to documents and evidence that the policy was known, acknowledged and followed by employees.

Parent companies also need to proceed with caution when a sub is sued. Among other risks, being forthcoming in providing documents to the sub to assist in its defense could lead to court orders that the sub must provide all similar documents from the parent. When significant litigation arises involving a US sub, risk can be reduced by relying on counsel experienced in US litigation and involving them in communications with the sub concerning the litigation.

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