Testimony of

Victor E. Schwartz, Esq.
Partner, Shook, Hardy & Bacon, LLP
On behalf of the Institute for Legal Reform
Of the U.S. Chamber of Commerce

Before the
Subcommittee on Commercial and Administrative Law
of the
U.S. House of Representatives Committee on the Judiciary

Hearing on H.R. 5913,
"Protecting Americans from Unsafe Foreign Products Act"
2141 Rayburn House Office Building

May 1, 2008
9:30AM

Submitted by:
Victor E. Schwartz, Esq.
Shook, Hardy & Bacon, LLP
600 14th Street, NW – Suite 800
Washington, D.C. 20005
Phone: 202-783-8400
Fax: 202-783-4211
Email: vschwartz@shb.com

TESTIMONY OF VICTOR E. SCHWARTZ
BEFORE THE
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW
OF THE
COMMITTEE ON THE JUDICIARY
U.S. HOUSE OF REPRESENTATIVES

Hearing on H.R. 5913,
"Protecting Americans from Unsafe Foreign Products Act"
May 1, 2008

Chairwoman Sanchez, and Ranking Member Cannon, and members of the Subcommittee, thank you for your invitation to testify today on the topic of holding foreign manufacturers accountable for defective products. Last November, I had the opportunity to testify before the Subcommittee on this topic. I am pleased to revisit this issue with you in the context of a proposal that has moved from the conceptual phase into legislation.

My background for addressing these issues includes practical experience as both a plaintiff and defense lawyer. I am a former law professor and law school dean, and co-author the leading torts casebook in the United States, Prosser, Wade & Schwartz's Cases and Materials (11th ed. 2005). In addition, I have authored the leading texts on multi-state litigation and comparative negligence.

While I have the privilege to testify today on behalf of the Institute for Legal Reform of the U.S. Chamber of Commerce, the views expressed are my own in light of my experience with these important topics.

Background

Major foreign manufacturers who do business in the United States, such as large foreign-based auto manufacturers, are subject to our legal system. Their products are priced accordingly. If they sell a considerable amount of their products in other countries where there is less liability exposure than in the United States, then they may be able to reduce their costs. Nevertheless, if one of their products proves defective and injures a person in this country, they are subject to liability here and the costs associated with such liability. The interesting impact of this phenomenon, though, is that a foreign-based company that can inappropriately avoid these costs can reduce its

price accordingly and place those companies who are subject to the full effects of the U.S. legal system at a competitive disadvantage. They could avoid this "tort tax." Every other manufacturer pays it.

The U.S. legal system should be consistent with the principle that those who are deemed culpable and responsible for a harm should be subject to liability to the degree of their responsibility. Accordingly, foreign manufacturers who deliberately avail themselves of the U.S. marketplace, but inappropriately avoid subjecting themselves to the U.S. legal system, should be held accountable for the harms caused by their defective products. Currently, there is a disparity between those foreign manufacturers who escape accountability and the domestic and foreign manufacturers who do not. The net result can impact international trade, the pricing of products, and most importantly, incentives for safety.

The Concept

H.R. 5913, the "Protecting Americans from Unsafe Foreign Products Act," has the worthwhile goal of ensuring that a foreign manufacturer whose defective products injure people in the United States does not escape responsibility because they are beyond the reach of our judicial system. While product liability is guided by state law, the Due Process Clause of the Constitution of the United States only permits a state to exercise personal jurisdiction over a defendant if that entity has "minimum contacts" with that specific state. In some instances, a foreign manufacturer may do business throughout the United States, or in a limited number of states, but its product may injure a U.S. resident in a state in which its business does not rise to a level permitting a state court to constitutionally exercise jurisdiction over it.

The Supreme Court of the United States addressed such a situation in *Asahi Metal Industry Co. Ltd. v. Superior Court*, 480 U.S. 102 (1987). Asahi is frequently characterized as a suit between a California plaintiff, who was injured when a tire blew, and a tire manufacturer. This was not the actual dispute before the Supreme Court. The dispute before the Supreme Court involved an indemnity claim brought by a Taiwanese manufacturer, Cheng Shin Rubber Industrial Co. ("Cheng Shin"), which made the defective tire, and Asahi, a Japanese manufacturer of a component part, a

valve, that allegedly played a part in the driver's injury. The injured California resident did have jurisdiction over Cheng Shin. Justice Sandra Day O'Connor's opinion relied on the fact that the plaintiff was not a California resident and that "[t]he dispute between Cheng Shin and Asahi is primarily about indemnification rather than safety." *Id*. at 115. The Court was persuaded in its decision by the fact that it was unclear whether California law would apply in what was a contract dispute and that Cheng Shin could easily have had the dispute heard in either a Taiwanese or Japanese judicial forum. *Id*.

In this context, the Court's plurality opinion found that the manufacturer lacked the necessary "minimum contacts" with California because it did not have an office, an agent, employees, or property in the state, it did not advertise or solicit business in the state, it did not create or control the distribution system that sent its product into the state, and it did not purposely seek to send products into the California market. Mere foreseeability that the product would end up being sold in the United States, the Court found, was insufficient to establish jurisdiction. Again, in this context, the Court stated that minimum contacts requires a "substantial connection" between the defendant and the forum state that is demonstrated by "an action of the defendant purposefully directed toward the forum State." *Id*. at 112.

In a footnote to *Asahi*, Justice O'Connor, perhaps concerned with an overly broad reading of the decision, provided a not-so-subtle invitation for Congress to expand jurisdiction over foreign manufacturers who purposefully send their products into the United States, but may not have sufficient contact with any particular state to allow that state to establish a "substantial connection." In *dicta*, meaning language that was not necessary as a basis for its opinion, Justice O'Connor volunteered the following:

> We have no occasion here to determine whether Congress could, consistent with the Due Process Clause of the Fifth Amendment, authorize *federal court* personal jurisdiction over alien defendants based on the aggregate of *national* contacts, rather than on the contacts between the defendant and the State in which the federal court sits.

Id. at 113 (emphasis in original). In other words, Justice O'Connor suggested that Congress might, by statute, authorize federal courts to hear product liability cases involving foreign defendants who direct their products into the United States as a whole, even if they do not have a substantial connection to the state in which the injury

occurred. This language appears to be the basis for the Protecting Americans from Unsafe Foreign Products Act, which would establish federal jurisdiction (but go further to provide state jurisdiction) over foreign manufacturers on the basis of contacts with the United States, whether or not such contacts occurred in the place where the injury occurred.

Questions and Concerns

While I commend the general purpose of the legislation and its attempts to clarify the actual meaning of the *Asahi* decision, some of the specific provisions of H.R. 5913 raise several substantial concerns that need to be addressed to ensure that the bill does not have unintended adverse consequences on the federal judiciary or domestic litigants, and falls within the bounds of the Constitution.

Scope. While the apparent purpose of the legislation is to address defective products sent into the United States from abroad that cause injury to U.S. residents, Section 2 goes well beyond that scope. It applies this new jurisdiction to an "injury that was sustained in the United States and that *relates to* the purchase or use of a product, or a component thereof, that is manufactured outside the United States. . . ." (emphasis added). This "relates to" language is cause for concern. It could be interpreted by courts as establishing jurisdiction far broader than product liability cases, to include *any* case that merely involves a product manufactured outside the United States. This could include a contract dispute between two foreign manufacturers, as was the case in *Asahi*, or a dispute between a manufacturer and distributor, among any other number of potential claims related to a product. Such expansive jurisdiction could burden the U.S. judicial system and its ability to promptly handle the cases of American citizens.

Constitutionality. Two aspects of the proposed legislation would likely be invalidated as unconstitutional.

First, the legislation authorizes jurisdiction when the foreign manufacturer "knew or reasonably should have known that the product or component part (or the product) would be imported for sale or use in the United States" *or* "had contacts with the United States." This language is significantly more relaxed than the Supreme Court's instruction in *Asahi* as to the sufficiency of contacts needed to reasonably and

constitutionally assert personal jurisdiction under the Due Process Clause. The legislation should recognize that a foreign manufacturer must have "purposefully directed its sale of products toward sale in the United States" *and* had "sufficiently aggregated contacts with the United States" to be subject to federal jurisdiction. Without such language, foreign companies that have made as much as an international phone call into the United States unrelated to the product at issue could unconstitutionally be hauled across the sea into the American liability system.

Second, the legislation authorizes jurisdiction over foreign entities by virtue of their *national* contacts in both federal and *state* courts. It is long-standing judicial precedent that state courts may only assert personal jurisdiction over defendants who purposefully establish minimum contacts with that forum State. *See, e.g., International Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945). Those minimum contacts permitting jurisdiction in a state court must have a basis in "some act by which the defendant purposefully avails itself of the privilege of conducting activities in the forum State, thus invoking the benefits and protections of its laws." *Asahi*, 480 U.S. at 109 (O'Connor, J. joined by Rehnquist, C.J., Powell and Scalia, JJ.) (quoting *Burger King Corp. v. Rudzewucz*, 471 U.S. 462, 475 (1985)). The legislation's test for minimum contacts should be strengthened to increase its likelihood of passing constitutional muster, particularly given that "[t]he unique burdens placed upon one who must defend oneself in a foreign legal system should have significant weight in assessing the reasonableness of stretching the long arm of personal jurisdiction over national borders. *Id*. at 114 (O'Connor, J. joined by Rehnquist, C.J., and Brennan, White, Marshall, Blackmun, Powell, and Stevens, JJ.). In addition, the legislation should be amended to authorize personal jurisdiction over foreign defendants on the basis of national contacts only in federal courts, as suggested by Justice O'Connor in *Asahi*.

As we may recall from law school, the Supreme Court of the United States in *Erie R.R. v. Tompkins*, 304 U.S. 64 (1938) held that when a federal court decides a case arising under state substantive law, it must apply the law of the state in which the federal court sits. In a subsequent decision, *Klaxon Co. v. Stentor Electric Mfg. Co*., 313 U.S. 487 (1941), the Supreme Court held that a state's choice of law rules were part of the substantive law of the state and that for *Erie* purposes a federal court must

follow those rules. Now legal scholars have long debated whether *Erie* was based on the Constitution of the United States or was merely a federal rules advisory opinion. If *Erie* was indeed a constitutional ruling, Section 3 of the bill cannot stand.

Litigation Tourism. The current legislative language would permit plaintiffs' lawyers to forum shop their cases against foreign defendants to what they perceive as the most favorable or substantially anti-corporate state court in the United States. Experience dating back to the Class Action Fairness Act has shown that certain local courts could become magnets for claims against foreign defendants. This "litigation tourism" would encourage lawyers to bring claims from across the country and the world to plaintiff-friendly state courts, burdening local litigants and juries.

Effect on domestic defendants. While the legislation is clearly targeted at foreign manufacturers, it may also have the consequence of expanding federal jurisdiction or changing choice of law rules for domestic manufacturers, distributors, or retail product sellers.

The legislation would permit a plaintiff to sue a foreign entity in a federal or state court in any state in which the entity "resides, is found, has an agent, or transacts business." This might also have the effect of subjecting domestic distributors to lawsuits in any federal or state court in the United States. In addition, the bill provides that the "law of the State where the injury occurred shall govern *all issues concerning liability and damages.*" (emphasis added). Thus, it would appear that if a product manufactured outside of the United States forms the basis of jurisdiction (even if the claim is not related to a product defect, as discussed above), any other issue involved in the suit will be subject to the law of the place of injury. This language would appear to subject any domestic entity that is pulled into the lawsuit to the law of that same state even if common law choice of law rules or a contract between the parties would otherwise require application of another state's law.

In addition to clarifying that the scope of the new federal jurisdiction is limited to claims involving an alleged defect in a product manufactured by a foreign citizen, the intent of the legislation should be further clarified by adding a rule of construction. A new Section 4 might provide: "Sec. 4. RULE OF CONSTRUCTION.—Nothing in this Act shall be construed to affect personal jurisdiction, choice of law, or liability of any

entity that is not a citizen or subject of a foreign state." This language would convey Congress's intent that the law does not expand jurisdiction over or change choice of law rules with respect to domestic defendants. The purpose of the law is solely to subject foreign manufacturers that send defective products into the United States to the jurisdiction of federal courts.

Conclusion

These questions and concerns are based on a preliminary review of the legislation. It is important to note that the extent to which foreign manufacturers should be subject to the U.S. tort system is an area of which there is not clear consensus in the business community. However, there is consensus that the U.S. tort system can "overheat" and impose liability that is above and beyond what is reasonable. Furthermore, the cost of the American liability system can significantly increase the prices of products that are subject to it. For these reasons, it is particularly important that the bill not inadvertently expand jurisdiction or liability for American employers.

In conclusion, I respectfully suggest that before H.R. 5913 moves forward, this Subcommittee:

- Strengthen language on the extent of contacts necessary to establish personal jurisdiction;
- Apply the new, expanded jurisdiction to authorize claims based on *national* contacts only in *federal* courts;
- Examine whether the choice of law provision conflicts with the principles of *Erie v. Tompkins*; and
- Include a rule of construction clarifying that the legislation does not impact jurisdiction, choice of law, or liability as applied to domestic defendants.

Thank you for the opportunity to testify today and I look forward to your questions.