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New York Appellate Court Limits Application of "Separate Entity Rule" in Post-Judgment Discovery Context

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In *In re B&M Kingstone, LLC v. Mega International Commercial Bank Co., Ltd.*,[1] the New York Supreme Court, Appellate Division, First Department, held that the "separate entity rule" does not insulate a non-US bank's New York branch from the obligation to disclose information and documents relating to customer assets held outside the US, in the foreign bank's non-US branches in response to post-judgment subpoenas served on the branch in New York. The Appellate Division held that the non-US bank's consent to necessary regulatory oversight in return for permission to operate a branch in New York was sufficient to subject the bank to the jurisdiction of the Court such that it could be compelled to comply with the post-judgment discovery demands.

The Court limited its ruling to situations where the non-US bank did not claim that responding to such information requests would be onerous or unduly expensive, or that the requested information was not accessible by the US branch (e.g., through electronic searches performed there). However, the decision undercuts the scope of the recent opinion of the New York Court of Appeals in *Motorola Credit Corporation v. Standard Chartered Bank*,[2] which held a judgment creditor's service of a restraining notice on a foreign bank's New York branch ineffective to freeze assets held outside the US in the bank's foreign branches. Pointing to public policy interests in broad post-judgment discovery and technological innovations that enable New York bank branches to more easily find information about judgment creditors' assets located in foreign branch accounts, the First Department held that the narrow holding of *Motorola* did not extend to subpoenas seeking information and documents obtainable by the New York branches.

Background

Plaintiff B&M Kingstone, LLC ("B&M") is a judgment creditor seeking to satisfy judgments totaling in excess of $39 million against various individual and corporate entities, arising from acts of counterfeiting, civil theft and misappropriation of proprietary information.[3] Mega International Commercial Bank Co. Ltd. ("Mega ICBC") is a bank organized under the laws of Taiwan, with its principal place of business in Taipei City, which operates a single branch in New York City.[4]

1 2015 WL 4726634 (N.Y. App. Div. 1st Dep't Aug. 11, 2015)

2 23 N.Y.3d 149 (N.Y. 2014)

3 2015 WL 4726634, at *1-2

4 Id.

Believing that Mega ICBC held bank accounts for the benefit of the judgment debtors and was in possession of assets belonging to the judgment debtors, B&M served Mega ICBC with an information subpoena, a subpoena *duces tecum*, and a questionnaire seeking records of any account at Mega ICBC anywhere in the world in which each judgment debtor may have had an interest and whether the judgment debtor was indebted to Mega ICBC in any manner.[5]

In response to the subpoenas, Mega ICBC stated that its New York branch was not in possession of any of the judgment debtors' assets, that its New York Branch was not holding any account or other property for the judgment debtors, and that the judgment debtors were not indebted to it.[6] Mega ICBC stated that it could not and would not access accounts maintained outside of New York, and objected to the subpoena *duces tecum* to the extent it sought records outside of New York.[7] B&M then brought a petition seeking an order compelling compliance with the subpoenas and questionnaire, and restraining any accounts held by judgment debtors.[8] The lower court held that it did not have jurisdiction over Mega ICBC, and denied the petition to the extent that it sought to restrain the judgment debtors' accounts outside the US.[9] However, finding that the New York branch could access information concerning accounts outside of the US, the court ordered Mega ICBC to comply with B&M's information subpoena.[10]

Before the First Department, Mega ICBC argued that B&M could not exercise general jurisdiction over Mega ICBC because it was not fairly regarded as being "at home" in New York.[11] Mega ICBC further argued that the separate entity rule precluded enforcement of subpoenas and restraining notices as to Mega ICBC branches outside New York.[12] Finally, the bank argued that considerations of international comity precluded compelling compliance with the subpoenas, contending that such compliance could require Mega ICBC to violate banking regulations in foreign jurisdictions.[13]

Ruling

The First Department, relying on the US Supreme Court's decision in *Daimler AG v. Bauman*,[14] agreed that a foreign bank may not be subject to general jurisdiction, (i.e., all-purpose jurisdiction, with respect to its non-US operations if the bank's contacts with New York are not so continuous and systematic as to render it essentially "at home" in the State). Nevertheless, the First Department ruled that by virtue of a foreign bank's consent to necessary regulatory oversight in return for permission to operate a bank branch in New York, a foreign bank does subject itself to New York jurisdiction requiring it to participate as a third party in lawsuits involving assets under its management, such as by complying with appropriate information subpoenas.[15] Accordingly, the essential issue raised in *In re B&M Kingstone* is whether the separate entity rule circumscribes the scope of a New York court's jurisdiction over the non-US operations of a non-US bank operating in New York such that the court may not compel the New York branch of a non-US bank to produce information pertaining to assets of judgment debtors on deposit at the bank's branches outside the US.[16]

In deciding this question, the Court observed that the separate entity rule establishes a narrow exception, as recognized in *Motorola*, to a non-US bank's obligation to participate as a third party in a lawsuit seeking to recover assets from a judgment debtor by preventing the restraint or turnover of assets located in foreign bank branches.[17] However, the Court held that, despite this exception, New York courts retain personal jurisdiction over a non-US bank's New York branch by virtue of the bank's consent to necessary regulatory oversight in exchange for operating here, and, as a consequence, can compel the New York branch to produce

5 Id. at *2
6 Id.
7 Id.
8 Id. at *2-3
9 Id. at *4
10 Id.
11 Id. at *3; *see Daimler AG v. Bauman*, 134 S.Ct. 746 (2014)
12 Id.
13 Id.
14 134 S.Ct. 746 (2014)
15 Id. at *4-5
16 Id. at *5
17 Id.

information (and documents) that can be found through electronic searches performed in New York.[18] Thus, the First Department held that the lower court could compel the production of information from the New York branch of Mega ICBC concerning its foreign branches (i.e., accounts maintained by depositors in other branches or at the home office) as long as compliance with that order would not be onerous or unduly expensive and the information was accessible by the New York branch in New York.[19] In the First Department's view, the "onerous or unduly expensive" standard was not met, notwithstanding Mega ICBC's concerns that Taiwanese and Panama laws generally limit such disclosure.

On this latter point, the First Department upheld the lower court's finding that principles of international comity did not warrant a different result where Mega ICBC's submissions were insufficient to show that the bank could face liability for violation of any foreign banking laws, or to demonstrate that any other state or country had an interest more compelling than New York's interest in enforcing its judgments and regulating banks operating within its jurisdiction.[20]

Implications

In re B&M Kingstone demonstrates that, despite the Court of Appeal's fealty to the well-established separate entity rule,[21] New York courts are willing to interpret *Motorola* narrowly in order to preserve their ability to compel non-US banks operating in New York to leverage the operational interconnectivity of their individual branches in service of New York's public policy interest in enforcing its judgments through broad post-judgment discovery. Ironically, while the separate entity rule as articulated in *Motorola* prohibits judgment creditors from compelling the turnover or restraint of assets held in foreign branches merely through the service of a restraining notice or turnover order on the New York branch of a non-US bank, that decision will not insulate the New York branches of foreign banks from being compelled to disclose information (and documents) pertaining to assets of judgment debtors held by the bank outside the US, even where the New York branch conducts "narrow and limited" operations in the State.[22] In effect, the First Department is facilitating indirectly what the Court of Appeals has constrained New York courts from directly doing in *Motorola* by helping judgment creditors to gain the information needed to freeze assets held outside the US in a non-US bank's foreign branches.

Moreover, this decision could encourage non-US banks operating in New York to fully segregate customer information relating to their US banking business from customer information arising from their non-US banking business in order to insure that information about non-US banking activities is inaccessible from the US and, thus, beyond the reach of New York courts. This behavior—which would be a natural response to *In re B&M Kingstone*—would make it more difficult for US banking regulators to do their jobs and to gain access to the type of information necessary to obtain a full picture of the worldwide operations of a non-US bank with US branch operations.

Further, such behavior would potentially create an unworkable morass for non-US banks seeking to comply with, among other legal and safety and soundness considerations, USA PATRIOT Act requirements to "know your customer" by understanding the full extent of a US branch customer's relationship with the entire foreign bank organization (e.g., with respect to accounts opened by or for the benefit of the customer at other branches of the bank outside the US), if the US branch cannot gain access to complete information about the customer's other relationships with the bank outside of the US. These important obligations under US law would be hindered and obstructed by the non-US bank's legitimate concern with protecting its customers' confidential account information as required by law in many non-US banking systems and the bank's fear of running afoul of contradictory legal and/or regulatory obligations. In addition, as a result of this decision, the number of information subpoenas served on the New York branches of foreign banks by judgment creditors seeking to obtain information about the assets of judgment debtors held by foreign branches of those banks will surely increase, giving rise to a significant increase in litigation (with its attendant costs) relating to such subpoenas.

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18 Id. at *6

19 Id.

20 Id.

21 Id. at *5

22 Id. at *2

For these reasons, the *In re B&M Kingstone* decision can be seen as undercutting the important protections afforded by the separate entity rule to non-US banks operating branches in the US as recognized by the Court of Appeals in *Motorola*. Non-US banks with New York branches must carefully consider how this decision impacts their operational activities in the State going forward. The importance of these issues to New York's vital international banking industry may also draw the attention of New York's Court of Appeals making this decision a significant candidate for review.

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