THE CONSEQUENCES OF REMOVAL AND REMAND GONE AWRY

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Although we suspected that something might be amiss, we were utterly unprepared for the revelation that concealed collusion had resulted in our denial of jurisdiction in federal court. The truth only came to light due to the forcefulness of a state judge who ordered corporate counsel to bring his entire file to court during the middle of trial, and the fact that corporate counsel printed his emails without having read them; otherwise, the deception would have remained concealed forever. However, the impact of the deception was not, and could not have been, remedied without considerable expense and delay. In other words, the potential remedies available under state and federal law at that time were inadequate—the damage had been done.

There are many reasons defendants avail themselves of the jurisdiction of federal courts through removal. Some believe the forum is more neutral. Others prefer the requirement of a unanimous jury verdict. Still others favor the resources available to federal judges. Whatever the reason, an order remanding a case to state court following a defendant's removal can have a profound impact on the trajectory of the case and can leave the defendant without adequate relief in the event of misconduct. This is a bad thing, which undermines our system of justice and gives individuals and businesses even more reason to be skeptical of the legal system.

Our clients (the defendants and counterclaimants) are residents of Ohio and collectively held a 50 percent ownership interest in the Iowa corporation at the center of the dispute. The plaintiff, an Iowa resident, allegedly held the other 50 percent ownership interest. Regrettably, the parties never completed all of the usual corporate documentation, which aggravated a fractured situation.[1]

The company at issue provided services related to energy conservation through a combination of a software product and training services. The company was supported financially for many years by our clients through an Ohio company that they owned and controlled, which was also named as a defendant. In short, our clients invested in a nascent startup in Iowa that was to focus on the development of a software support program for energy training services. By 2014, after about six years of slow development, the company at issue was losing money and the Iowa plaintiff was in dire financial straits. It was at this point that he decided to try to extort $1 million from his fellow shareholders (our clients) by cutting off services to their Ohio company, whose customers would then suffer. When that plan was implemented but did not result in payment to him, he pursued a legal attack by filing a derivative complaint in Iowa state court, naming the Iowa corporation as a plaintiff. He alleged in the complaint that the acting CEO of the company, hired because of the disagreements among the shareholders, had refused his demand as a shareholder to proceed with litigation against our client.[2]

In response, we filed a notice of removal on the basis of diversity to the U.S. District Court for the Southern District of Iowa.[3] We believed this would be a more expeditious path to the dismissal of the case.

After consenting to disposition by a U.S. magistrate judge, a scheduling order was issued, setting trial for January 2016. Shortly thereafter, the court held a status conference at which it sought to "clarify the alignment of the parties" because it was puzzled by the Iowa corporation having been named as a plaintiff. Although we suspected that corporate counsel and the plaintiff were in cahoots, we had no proof at that time. To that end, the defendants served a document request upon the plaintiff that called for production of any and all documents that referenced the lawsuit including, but not limited to, communications with third parties. That document request, if responded to properly, would have made it clear that the Iowa corporation was aligned with the plaintiff and that complete diversity existed. But the documents that ultimately surfaced in court were not produced at that time.[4]

In May 2015, the U.S. magistrate judge *sua sponte* remanded the matter to state court in reliance on the allegations of the complaint that the corporation was antagonistic to the plaintiff. Ironically, the court relied on case law in which a court had held extensive hearings to determine the proper alignment of the parties.[5] We had not requested a hearing because we were never provided with the non-privileged documents that would have revealed the collusion that gave rise to the remand order. Nor was the federal court privy to this information.

After almost two years of litigation in state court, the case proceeded to trial in February 2017. Although we had already issued a subpoena to corporate counsel and obtained what we now know were incomplete documents during discovery, we nevertheless issued a trial subpoena to corporate counsel to bring his file and appear to testify at the trial. After legal arguments and testimony related to the applicability of the attorney-client privilege, the court ordered corporate counsel to appear with his entire file.[6] It was at that point, as Shakespeare wrote in Hamlet, "In this upshot, purposes mistook / Fall'n on th' inventors' heads."

Corporate counsel appeared in court the next day with a banker's box of documents. The number of documents far exceeded that which he originally produced. We adjourned for the afternoon to review these newly produced documents prior to examining the next witness.[7]

The first surprise was a non-privileged email from the plaintiff's litigation counsel to corporate counsel, stating:

> [Corporate counsel], attached is our proposed petition for our shareholder derivative lawsuit. We have the inclination and intention to file this today unless you have major objections. As you review this, please also consider whether you believe we are missing something. Our plan is to file immediately but not serve right away to take advantage of time for possible negotiations.[8]

Yes, this really is an email from a lawyer for the plaintiff asking corporate counsel in a derivative action to bless or edit the proposed derivate complaint that was included for his review. This document alone precluded a realignment of the parties, and those aware of this information had a duty to so inform the U.S. magistrate judge and not to take advantage of her remand order.

A second surprise was a non-privileged email written and sent by corporate counsel to the plaintiff and plaintiff's litigation counsel, stating:

The shareholder issue persists and there may be two or more options concerning that issue:

1. Do nothing regarding [Defendants]. Any [corporation] "profit" can be taken by [Plaintiff] and John as salary. Eventually the software will run its course and the company can fade away.
2. Offer to sell a copy of the software to [the Ohio company] for a reasonable price, such as $1. Then also sell a copy to Newco called ESI Energy (owned by [Plaintiff] & [acting CEO] for $1. Allow [the corporation] to go dormant and Sec of State administratively dissolve it.[9]

This email is, in fact, direct evidence of collusive behavior between the plaintiff and corporate counsel to oppress the interests of our clients through the use of a legal proceeding based on a false premise. This behavior was later described by the state court judge as "advocacy by deception."[10] Had the plaintiff or plaintiff's litigation counsel disclosed this information to the magistrate judge, the federal court would have been compelled to retain jurisdiction and dismiss the derivative complaint.

As explained by the state trial judge in his opinion finding in favor of the defendants:

> It is axiomatic that in a shareholder derivative case the corporation is antagonistic to the plaintiff and not a confederate. This evidence, coupled with additional evidence produced by [corporate counsel] during the middle of trial in February 2017, reflect that [corporate counsel] was working on behalf of [Plaintiff] and not [the corporation] and this suit was not properly filed. Simply put, [the corporate counsel] failed to act in the best interest of [the corporation] or properly represent the company; rather [the corporate counsel] worked with [Plaintiff] to deprive [Defendants] of their ownership interest in [the corporation].[11]

The state trial judge further advised:

> The court is further troubled that [Plaintiff], his previous attorneys, [corporate counsel] and [corporate counsel's] firm all withheld the fact that they were working hand-in-hand to file this action against Defendants, as well as other evidence that directly bear upon the claims and defenses in this action, from the court and the federal court, despite their obligation to disclose the evidence…. But for this court ordering [corporate counsel] to appear with his file during the middle of the trial in February 2017 and [corporate counsel] hurriedly printing emails from his account and producing the next day without first reading them, Defendants and this court would never have been made aware of these key facts.[12]

Due to the newly produced documents during trial, the court continued the trial until the summer of 2017. It issued an opinion finding in favor of the defendants on all counts in April 2018—over two years after the original trial date set in federal court.[13]

The plaintiff's and corporate counsel's behavior cost the defendants over two years of the life of the corporation at issue. The time and expense for any business or shareholder in the throes of litigation is substantial and detrimental. In our case, the bad actors remained in control of the corporation until the misconduct was

revealed. Although the defendants have sought and are expecting relief for the discovery mischief, it won't be enough.

Asking the state court to re-remove the case to federal court during the middle of trial was not a practical option. The damage had been done to our clients.

Seeking relief from the federal court was similarly not in our clients' best interest. The general rule is that a defendant cannot appeal or otherwise request a review of an order remanding a case to the state court from which it was removed.[14] While there is a limited exception allowing a federal court to vacate a remand order obtained through what is tantamount to fraud, this exception is extremely narrow and can be challenging to prove.[15]

Therefore, even if a defendant could successfully prove fraudulent conduct and obtain an order vacating the remand order, doing so would add significant cost to the client, as well as delay the ultimate resolution of the underlying dispute. Nor is this approach beneficial if the misconduct is not discovered until years into the proceedings. In our case, requesting that the district court vacate its remand order and resume proceedings over the case approximately three years after the remand order was issued and when we were in the midst of trial was not a practical solution. It would have only served to increase the costly litigation and the executive and employee time related to the defense of the case.

What happened to our clients is as wrong as wrong can be. While the rationale behind the finality of remand orders and the corresponding jurisdictions of federal and state courts is well-meaning and important, its practical effect is that defendants in situations such as our clients are left without an adequate remedy. Unless the misconduct is discovered almost immediately after the remand order is issued, and the client has the funds to prove that fraudulent conduct occurred, there appears to be no way to restore the status quo and allow the defendant to rightfully proceed in federal court.

The removal process is an important aspect of our legal system. Unfortunately, Congress has not provided any practical solution or remedy for this type of misconduct. As a result, we respectfully suggest that federal courts exercise great care and due diligence when issuing remand orders and hold parties and their counsel accountable for their misstatements or concealment of critical facts. While it is, of course, incumbent upon counsel to fulfill their ethical obligations in remand situations, sadly, this does not always happen. We hope that highlighting our experience will remind readers of the significance of remand orders and encourage federal courts to stay ever vigilant against the abuse of this process. ⊙

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Endnotes

[1]*See* Findings of Fact, Conclusions of Law and Order of Judgment, Case No. EQCE076363, April 12, 2018, Iowa District Court, Polk County, *available at* https://www.iowacourts.state.ia.us/Efile.

[2]*See id*.

[3]*See* Notice of Removal, *Hanes v. Nat'l Comfort Ivst.,* Case No. 4:14-cv-00217-CFB (S.D. Iowa June 5, 2014) (ECF No. 1), *available at* https://www.iasd.uscourts.gov.

[4]*See id*. generally; Findings of Fact, Conclusions of Law and Order of Judgment, *supra* note 1.

[5]*See* Removal Order, *Hanes v. Nat'l Comfort Ivst.,* Case No. 4:14-cv-00217-CFB (S.D. Iowa May 5, 2015) (ECF No. 46).

[6]*See* Findings of Fact, Conclusions of Law and Order of Judgment, *supra* note 1.

[7]*See id.*

[8]*See id.* at 15-16.

[9]*See id.* at 10.

[10]*See id.* at 13.

[11]*See id.* at 16.

[12]*See id.* at n.79.

[13]*See id.* generally.

[14]28 U.S.C. § 1447(d).

[15]*Barlow v. Colgate Palmolive Co.*, 772 F.3d 1001 (4th Cir. 2014).