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A New Way to Pierce the Corporate Veil: Disgorging Profit From Corporate Affiliates

Update

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The US Supreme Court has recently granted *certiorari* on the issue of whether a corporation can be held liable for the conduct of its affiliate without first satisfying the well-settled standards for piercing the corporate veil. While the case concerns the discretion afforded courts to fashion a remedy under the Lanham Act, the US Court of Appeals for the Fourth Circuit's approach to veil-piercing could have broad implications. In particular, the Fourth Circuit held that the trademark-infringing defendant must disgorge not only its profits, but also those of its non-defendant affiliates. If the Fourth Circuit's decision is affirmed or extended by the Supreme Court, the ruling could create a new avenue for piercing the corporate veil, beyond the traditionally required showing that the affiliated entities have engaged in fraud or other similar wrongdoing.[1]

Background

The parties to the action, Dewberry Engineers, Inc. and Dewberry Group, Inc., are both in the real estate development business, and have a history of trademark litigation over the name "Dewberry." The present dispute arose when the Dewberry Group designed new insignias using the "Dewberry" name as part of a corporate rebrand, and Dewberry Engineers sued for trademark infringement and contract violation in the district court in the US District Court for the Eastern District of Virginia.[2] The District Court sided with Dewberry Engineers, granting summary judgment and awarding more than $42 million in profit disgorgement against Dewberry Group, along with attorneys' fees.

At the center of the dispute that has now made its way to the Supreme Court is the broad equitable discretion afforded federal courts with respect to the extent of damages awards under the Lanham Act. Under Section 1117(a) of the Act, courts are authorized to grant a plaintiff an award of profit disgorgement based

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on the defendant's profits earned from the disputed trademark.[3] If a court finds that the profits-based recovery is either inadequate or excessive, "the court may in its discretion enter judgment for such sum as the court shall find to be just."[4]

Applying an approach that could have broad implications if adopted by the Supreme Court, the District Court in the Dewberry case calculated the damages award based not only on Dewberry Group's profits, but also on the profits of Dewberry Group's corporate affiliates, which were separate corporate entities and not parties to the case. Dewberry Group itself claimed that it earned no profits from the trademark infringement, because it simply produced the infringing branding, while its corporate affiliates are the parties who profited from the use of the branding on business and promotional materials.

The Fourth Circuit Decision

In a split decision, the Fourth Circuit majority upheld the District Court's approach.[5] The Fourth Circuit distinguished the District Court's approach from a typical corporate veil-piercing analysis. Specifically, the majority noted, "rather than pierce the corporate veil, the [District Court] considered the revenues of entities under common ownership with Dewberry Group in calculating Dewberry Group's true financial gain from its infringing activities that necessarily involved those affiliates."[6]

Thus, the Fourth Circuit majority concluded that the District Court did not abuse its discretion when it considered the profits of the Dewberry Group corporate affiliates in calculating the profit disgorgement remedy. The court emphasized, "admonishing courts for using their discretion in this fashion risks handing potential trademark infringers the blueprint for using corporate formalities to insulate their infringement from financial consequences."[7]

The Fourth Circuit's majority opinion was paired with a dissent in part from Judge Quattlebaum. The dissent said that remedies under the Lanham Act are limited to the profits of the infringing parties, and the non-party corporate affiliates were not shown to be infringing parties in this case. In the dissent's view, the affiliates were entirely separate and non-party entities, and no facts were presented to support the idea that any profits were passed on to these affiliates from Dewberry Group.

Supreme Court Showdown

The Supreme Court granted *certiorari* on this issue on June 24, 2024.[8] Notably, the federal government has sought time to present its own oral argument on the public policy implications at issue in the case. Earlier this

month, the Supreme Court granted the federal government ten minutes to argue its position at oral argument.

In its amicus brief to the Supreme Court, the federal government argued for a middle road between the Fourth Circuit's opinion and a more limited treatment of non-party affiliates under the Lanham Act charted in other circuits.[9] The government offers an approach that takes into consideration the "economic realities" of a party's profit, outside of specialized accounting or tax treatment. According to this approach, "a defendant may be fairly considered to have profited from a transaction if the defendant's conduct has generated (or helped to generate) the funds and the defendant controls their disposition."[10]

The government's amicus brief identifies two scenarios where, under this proposed approach, the measurement of a corporate defendant's liability may include the profits of its affiliates. First, profits of an affiliate may be attributed to a party when that party received "indirect payments" as a result of the trademark infringement. Second, a court could look to whether an infringing party would have received profits from an infringing transaction but directed those profits to be paid elsewhere (i.e., to its affiliates).

It remains to be seen whether the Supreme Court will affirm the more expansive approach adopted by the Fourth Circuit or take one of the more limited approaches outlined by the federal government or other circuit courts. The oral argument, scheduled for December 11, 2024, may provide clues as to the future of the corporate veil-piercing doctrine.

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[1] Judicial standards for piercing the corporate veil vary by jurisdiction, but courts generally consider the following three factors: (1) complete control and domination of a corporate entity by a defendant; (2) the defendant's use of that control to engage in fraud or other wrongdoing; and (3) injury or harm as a result of the control and wrongdoing. 1 Carol A. Jones, *Fletcher Cyclopedia of the Law of Corporations* § 41, at 156-165 (2015 rev. vol.)*; see also Cortlandt St. Recovery Corp. v. Bonderman,* 31 N.Y.3d 30, 47 (N.Y. 2018); *Bhole, Inc. v. Shore Invs., Inc.*, 67 A.3d 444, 452, fn. 35 (Del. 2013).

[2] *Dewberry Eng'rs Inc. v. Dewberry Grp., Inc.*, No. 1:20-CV-610-LO-IDD, 2022 WL 1439105 (E.D. Va. May 6, 2022), *aff'd*, 77 F.4th 265 (4th Cir. 2023), *cert. granted*, 144 S. Ct. 2681 (2024).

[3] 15 U.S.C. § 1117(a) (2008).

[4] *Id*.

[5] *Dewberry Eng'rs v. Dewberry Grp., Inc*., 77 F.4th 265 (4th Cir. 2023), *cert. granted*, 144 S.Ct. 2681 (2024).

[6] *Id*. at 292.

[7] *Dewberry Eng'rs,* 77 F.4th at 293.

[8] *Dewberry Eng'rs v. Dewberry Grp., Inc*, 144 S.Ct. 2681 (2024) (order granting cert).

[9] Brief for the United States as Amicus Curiae Supporting Neither Party, *Dewberry Eng'rs v. Dewberry Grp., Inc*, 144 S.Ct. 2681 (2024) (No. 23-900).

[10] *Id*. at *13.

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