Successor Liability In New Jersey: Am I Buying A Lawsuit?

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Traditional Rule of Successor Liability

Before Jackson v. Diamond T. Trucking Co., 100 N.J. Super. 186 (Law Div. 1968), no New Jersey court had been called upon to make a comprehensive statement of the law in the area of successor liability. In Jackson, Plaintiff, George J. Jackson (Jackson) was an employee of Phillips Specials (Phillips), a trucking company wholly owned by Ujay, Inc. (Ujay). After Plaintiff sustained a compensable work-related injury for which he received a worker's compensation award against Phillips, Wallace T. Taylor (Taylor) entered into a contract with Ujay to purchase the capital stock and assets of Phillips for Diamond T. Trucking (Diamond T). Pursuant to the contract, Taylor was the buyer, although provisions were made for the assignment and transfer of the rights and assets covered by the contract to Taylor's corporate nominee, Diamond T. The contract included the following highlights: $100,000 consideration for the Phillips stock; $12,436 in consideration for its assets; an $80,000 promissory note executed or to be executed by Diamond T and guaranteed by Taylor individually; the creation of a seller's security interest in the Interstate Commerce Commission (I.C.C.) operating license; seller's permission to liquidate, merge or consolidate Phillips; resignations by Phillips' old officers and directors, and releases by them of any claims they might have against the corporation. Ujay further agreed to pay the debts and liabilities of Phillips of any kind, absolute or contingent, existing on the date of closing. Furthermore, Ujay agreed to indemnify and save Taylor harmless from all actions, suits, proceedings, demands, assessments, judgments, costs and expenses incident to any failure of Ujay in fulfilling any terms of the sale contract. Attached to the contract and made a part thereof was a list of certain outstanding obligations of Phillips. Included on this list was Jackoson's compensation claim beneath which Ujay declared its obligation to accept liability with regard thereto. After the franchise was transferred, the trucks and other operating equipment were registered in Diamond T's name. All operations performed by Phillips were thereafter performed by and under the name of Diamond T. Although Phillips was not statutorily dissolved it was left with no assets in New Jersey and no longer conducted any activities. Jackson, supra, 100 N.J. Super. at 188-90.

Jackson asked the court to render a judgment of liability with interest and costs against Diamond T for the worker's compensation award rendered against Phillips because Diamond T was a continuation in law and fact of Phillips. In rendering his decision Judge Pindar found where no statement of law existed the State would adopt the formulation set forth in *Fletcher Cyclopedia Corporations*. Per Fletcher's formulation:

> Generally where one corporation sells or otherwise transfers all of its assets to another corporation, the latter is not liable for the debts and liabilities of the transferor, except: (1) where the purchaser expressly or impliedly agrees to assume such debts; (2) where the transaction amounts to a consolidation or merger of the corporation; (3) where the purchasing corporation is merely a continuation of the selling corporation; and (4) where the transaction is entered into fraudulently in order to escape liability for such debts. Jackson, 100 N.J. Super. at 192 (quoting 15 *Fletcher, Cyc. Corporations*, § 7122, p. 187 (1961 Perm. Ed.)).

Judge Pindar also relied on five older New Jersey equity cases from the New Jersey Court of Errors and Appeals and the Chancery Division. He ultimately ruled that Fletcher's formulation and the equity cases did not support plaintiff's proposition that a transferee corporation was responsible for the liabilities of its transferor whenever the transferee continued the business operations of the transferor with the latter's assets. Nor was he prepared to adopt such a sweeping statement, when, such a conclusion was unnecessary for what he believed was the

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correct disposition of the case. He therefore found Diamond T liable based on five elements which were common to the five older equity cases and fit Fletcher's formulation: (1) Phillips' transfer of corporate assets (2) for less than adequate consideration (3) to Diamond T a company with the same President (Taylor) (4) which continued the business operation of Phillips, (5) rendering Phillips incapable of paying its creditors. Jackson, 100 N.J. Super. at 196-97.

Product Line Exception

Notably, such was the law in New Jersey for almost fifteen years. Accordingly, absent the transaction falling into the four exceptions set forth in Fletcher's formulation, when one corporation sold or otherwise transferred its assets to another corporation, the latter was not liable for the debts and liabilities of the former. However in 1981, the New Jersey Supreme Court in Ramirez v. Armsted Industries, Inc., 86 N.J. 332 (1981), decided to reevaluate the traditional approach adopted by Judge Pindar in Jackson. In Ramirez, Efrain Ramirez (Ramirez) was injured while operating a power press manufactured by Johnson Machine and Press Company (Johnson). Through a purchase agreement, Amsted Industries, Inc. (Amsted) obtained Johnson's trade name, physical plant, manufacturing equipment, inventory, manufacturing designs, patents and customer lists. After discovery, Amsted moved for summary judgment on the ground that the mere purchase of Johnson's assets for cash did not carry with it tort liability for damages arising out of defects in products manufactured by Johnson. The trial court granted Amsted's motion for summary judgment, holding that pursuant to the traditional corporate approach, there was no assumption of liability when the successor purchases the predecessor's assets for cash and when the provisions of the purchase agreement between the selling and purchasing corporations indicated an intention to limit the purchaser's assumption of liability. Ramirez, supra, 86 N.J. at 335-36.

However, on appeal the Supreme Court reasoned that the traditional corporate approach was inconsistent with the rapidly developing principles of strict liability in tort and was unresponsive to the legitimate interests of the products liability plaintiff. It opined that the traditional rule of non-liability was developed not in response to the interests of parties to products liability actions, but rather to protect the rights of commercial creditors and dissenting shareholders following corporate acquisitions, as well as to determine successor corporation liability for tax assessments and contractual obligations of the predecessor. Ramirez, 86 N.J. at 341.

It also found that strict interpretation of the traditional corporate law approach led to a narrow application of the exceptions to non-liability, and placed unwarranted emphasis on the form rather than the practical effect of a particular corporate transaction. Indeed, it held that the principal exceptions to non-liability outlined in McKee v. Harris-Seybold Co., Div. of Harris-Intertype Corp., 109 N.J. Super. 555 (Law Div. 1970), incorrectly conditioned successor liability on a determination of whether the transaction could be labeled as a merger or a de facto merger, or whether the purchasing corporation could be described as a mere continuation of the selling corporation. Ramirez, 86 N.J. at 341.

It reasoned that:

> To the injured persons the problem of recovery is substantially the same, no matter what corporate process led to transfer of the first corporation and/or its assets. Whether the corporate transaction was (1) a traditional merger accompanied by exchange of stock of the two corporations, or (2) a de facto merger brought about by the purchase of one corporation's assets by part of the stock of the second, or (3) a purchase of corporate assets for cash, the injured person has the same problem, so long as the first corporation in each case legally and/or practically becomes defunct. He has no place to turn for relief except to the second corporation. Therefore, as to the injured person, distinctions between types of corporate transfers are wholly unmeaningful. Ramirez, 86 N.J. at 3432-43 (quoting Turner v. Bituminous Cas. Co., 244 N.W.2d 873, 878 (1976)).

Consequently, in an effort to arrive at the standard most consistent with the principles underlying the New Jersey law of strict products liability, the Court adopted the "product-line" approach to successor liability. In adopting this standard, the Supreme Court of New Jersey relied upon and incorporated the three policy consideration

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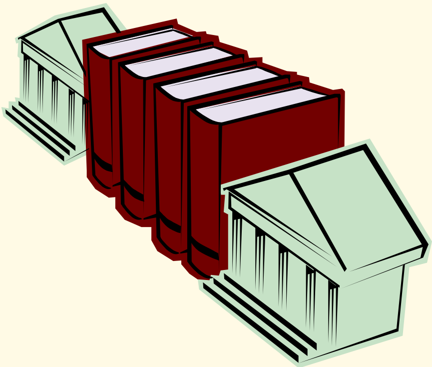
annunciated by the Supreme Court of California in Ray v. Alad, 19 Cal. 3d 22, 31 (1977). These three considerations, which stood as a justification for the imposition of potential liability on a successor corporation which acquired the assets and continued the manufacturing operation of its predecessor, included:

> (1) The virtual destruction of the plaintiff's remedies against the original manufacturer caused by the successor's acquisition of the business, (2) the successor's ability to assume the original manufacturer's risk-spreading role, and (3) the fairness of requiring the successor to assume a responsibility for defective products that was a burden necessarily attached to the original manufacturer's good will being enjoyed by the successor in the continued operation of the business. Ramirez, 86 N.J. at 347 (quoting Ray, supra, 19 Cal. 3d at 31).



By adopting these three considerations the Ramirez court extended the already well-established principle that strict liability for injuries caused by defective products placed into the stream of commerce continued so long as the defective product is present on the market. Santor v. A.M. Karagheusian, Inc., 44 N.J. 52, 65 (1965). However, it found in contrast to traditional successor liability principles that where the original manufacturer is no longer viable, the corporation that acquired all or substantially all of the manufacturing assets of another corporation and undertook essentially the same manufacturing operation as the selling corporation, is strictly liable for injuries caused by defects in units of the same product line, even if these units were previously manufactured and distributed by the selling corporation. It reasoned where a successor received the benefits from trading its product line on the name of the predecessor and takes advantage from its accumulated good will, business reputations and established customers, it must, also bear the burden. Ramirez, 86 N.J. at 352-58.

Until today, the products-liability principles set forth in Ramirez are controlling in New Jersey. As such, in addition to making sure any purchase agreements clearly express that the purchaser will not assume any of the seller’s liabilities, because of Ramirez, an additional indemnity clause within the purchase agreement should be included. Potential purchasers should also analyze potential sources of liabilities before the purchase in order to determine whether any product previously sold by the seller may give rise to post-purchase liability, in order to properly evaluate the purchase price. Once this information is gathered, purchasers should invest in insurance which will cover such products, and should require copies of the seller’s historical liability insurance contracts. Purchasers, as a result of Ramirez, could in the purchase agreement also require the selling corporation to maintain their corporate existence post-purchase and to obtain additional post-purchase insurance policies or maintain future occurrences accounts for any post-purchase liability claims; therefore, continuing to render the original manufacturer viable.

*** Daniel Kuszmerski and Jason Gosnell are both associates of the law firm Hoagland, Longo, Moran, Dunst & Doukas, LLP in New Brunswick, NJ. This article is the first in a series which will discuss many of the issues they have encountered concerning successor liability including: intermediary successors, original manufacturer viability, product line continuation, and supplier successor liability. Should you wish to contact Daniel or Jason please do so at dkuszmerski@hoaglandlongo.com or jgosnell@hoaglandlongo.com.**