

At Last Sportswear, Inc. v Newport News Holding Corp.

2010 NY Slip Op 32792(U)

October 5, 2010

Supreme Court, New York County

Docket Number: 602208/2009

Judge: Joan A. Madden

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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: Hon. Jack A. M. ...

PART 11

Index Number : 602208/2009

AT LAST SPORTSWEAR

vs
NEWPORT NEWS, INC.

Sequence Number : 002

DISMISS

INDEX NO. _____
MOTION DATE _____
MOTION SEQ. NO. _____
MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to for dismissal
+ cross motion to amend

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

Answering Affidavits — Exhibits _____

Replying Affidavits _____

PAPERS NUMBERED

Cross-Motion: Yes No

Upon the foregoing papers, It is ordered that this motion is decided in accordance with the approved Memorandum Decision ~~Order~~ + Order.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

FILED
OCT 07 2010
NEW YORK
COUNTY CLERK'S OFFICE

Dated: October 5, 2010

[Signature]
J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION
Check if appropriate: DO NOT POST REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK : IAS PART 11

-----x
AT LAST SPORTSWEAR, INC.,
d/b/a/ Eva Blue

Plaintiff,

-against-

Index No. 602208/2009

NEWPORT NEWS HOLDING CORPORATION
and SIGNATURE STYLES, LLC d/b/a Newport News,

Defendant

-----x
Joan A. Madden, J.

Defendant, Signature Styles, LLC (“Signature”) moves to dismiss the claims against it. Plaintiff, At Last Sportswear, Inc. (“At Last”), opposes the motion, and separately cross-moves to amend its amended complaint to, *inter alia*, include a claim against Signature based on successor liability.

Background

At Last is a New York corporation that manufactures women’s dresses. Defendant Newport News Holding Corporation (“Newport”), is a Delaware corporation specializing in mail order and on-line sales of women’s clothing. In or about February 2009, Newport agreed to buy certain women’s dresses from At Last for \$112, 701. At Last alleges that Newport paid \$79,765.58, thus leaving an outstanding balance of \$32,935.42. In June 2009, Newport defaulted on its loans. On June 15, 2009, all of Newport’s assets were sold to Signature, a Delaware corporation. After Signature refused to pay the outstanding balance, At Last commenced this action.

The amended complaint¹ asserts claims against Signature for piercing the corporate veil, and conversion, and against Newport for breach of contract, goods sold and delivered and an account stated.

At Last now cross-moves to amend the amended complaint and submits a proposed Second Verified Amended Complaint, which inter alia, adds a claim of successor liability against Signature. Signature does not oppose the cross-motion to amend. Thus, the court will consider the allegations as they pertain to Signature's liability set forth in the Second Verified Amended Complaint.

Discussion

On a motion to dismiss pursuant to CPLR §3211(a)(7), the court is limited to ascertaining whether a pleading states any cause of action and not whether there is any evidentiary support for the complaint. Guggenheimer v Ginzburg, 43 N.Y.2d 268, 275 (1977). The complaint must be liberally construed in a light most favorable to the plaintiff, and all factual allegations must be accepted as true. Id. At the same time, “[i]n those circumstances where the legal conclusions and factual allegations are flatly contradicted by documentary evidence, they are not presumed to be true or accorded every favorable inference,” and dismissal is appropriate pursuant to CPLR §3211(a)(1). Morgenthau & Latham v. Bank of New York Company, Inc., 305 A.D.2d 74, 78 (1st Dep’t 2003), quoting, Biondi v. Beekman Hill House Apt. Corp., 257 A.D.2d 76, 81 (1st Dep’t 1999) aff’d, 94 N.Y.2d 659 (2000). In such case, the criterion becomes “whether the proponent of the pleading has a cause of action, not whether he has stated one.” Id., quoting Guggenheimer v Ginzburg, 43 N.Y.2d at 275.

¹ The original complaint asserted claims against Newport and the XYZ Corp. d/b/a Newport. By order dated December 29, 2009, the Court permitted At Last to amend the Complaint to inter alia, add Signature as a defendant in the place of XYZ Corporation.

However, dismissal based on documentary evidence may only result when the documentary evidence “utterly refutes [a] plaintiff’s allegations, conclusively establishing a defense as a matter of law.” It is under this standard that the court will review each allegation set forth against Signature in the Second Verified Amended Complaint.

Piercing the Corporate Veil

Regarding the claim for piercing the corporate veil, the Second Verified Amended Complaint alleges that Signature exercises complete dominion and control over Newport as it “continues to do business utilizing the name, goodwill, all business accounts, all or substantially all of the employees and directors, physical location and continues to maintain other indicia of Newport...” Second Amended Verified Complaint ¶27. It further alleges that Signature purchased the assets of Newport in order to use the corporate structure to defraud the rights of At Last and other creditors, and due to Signature’s “complete domination of Newport ... Plaintiff has sustained injuries.” *Id.* ¶ 28, 29.

Signature argues that Delaware law governs as both Signature and Newport are incorporated in Delaware and that under Delaware law, the Second Verified Amended Complaint fails to state a claim for piercing the corporate veil as it alleges no facts showing domination or control, particularly as Signature was formed only days before Newport sold its assets. Furthermore, Signature argues that the conclusory allegations of fraud are insufficient to satisfy the piercing requirements under New York or Delaware law. At Last counters that New York law should be applied and not Delaware law and that under the law of either jurisdiction, it has adequately stated a claim.

A party seeking to pierce the corporate veil must plead, “(1) the owners exercised complete domination of the corporation in respect to the transaction attacked; and (2) that such

domination was used to commit a fraud or wrong against the plaintiff which resulted in plaintiff's injury." Matter of Morris v New York State Dept. of Taxation and Finance, 82 NY2d135, 41 (1993). Delaware law similarly requires that a defendant exercise domination and control over the corporation and that such domination and control be used "to effectuate fraud or similar injustice." See LaSalle Nat'l Bank v. Perelman, 82 F. Supp 2d 279, 295 (D. Del. 2000).

Here, under either New York or Delaware law, the conclusory allegations of domination and control for the purposes of defrauding creditors are insufficient to state a claim for piercing the corporate veil. Sheridan Broad Corp. v. Small, 19 AD3d 331 (1st Dept 2005); Gillen v 397 Prop. LLC, 2002 WL 259953 ** 1-2 (Del. Ch. 2002). In fact, as asserted by Signature, any purported fraud with respect to the February 2009 contract to purchase the dresses could not have involved Signature, which was not formed until June 2009. Moreover, allegations related to Signature's continuity of business using Newport's name, goodwill, physical location and the same business accounts relate to Signature's liability as a successor-in-interest and are not a basis for piercing the corporate veil. See Cargo Partner AG v. Albatrans Inc., 352 F. 3d 41, 44-45 (2nd Cir. 2003)(noting that successor liability and piercing the corporate veil are separate doctrines). Accordingly, the motion to dismiss the claim for piercing the corporate veil is granted.

Successor Liability

Regarding the claim for successor liability, the Second Verified Amended Complaint alleges, upon information and belief, that Signature "has expressly or impliedly assumed all or substantially all obligations of Newport ...and is conducting business as a mere continuation of the Newport in a fraudulent effort to avoid all liability of Newport News." Second Verified Amended Complaint ¶ 33. It is further alleged that "upon information and belief that the

* 6]

transaction between Signature ... resulted in the assumption of the obligations of Newport... as Signature ... is conducting business as a mere continuation of Newport in a fraudulent effort to avoid liabilities of Newport...[and] that Signature ... has deliberately effected various transactions to acquire, *inter alia*, the Merchandise in order to defraud its creditors and in wrongful derogation of the rights of the Plaintiff and other Creditors.” Id. ¶ 35-36.² It is also alleged that the purchase of Newport’s assets constitutes a de facto merger as Signature continues to do business utilizing Newport’s name, goodwill, business accounts, all or substantially all the same employees and directors, same physical location and other indicia of Newport. Id. ¶ 37. It is further alleged the “acquisition of Newport’s assets constituted a consolidation and/or merger of Signature...and Newport.” Id. ¶38.

Signature argues that this claim must be dismissed as successor liability based on the de facto merger doctrine requires a showing of continuity of ownership. Signature argues that the allegation of continuity of ownership cannot be supported since the documentary evidence shows that consideration for the sale was cash, not stocks, and therefore the prior owners received no interest in the new company.

In general, when one corporation sells or otherwise transfers all of its assets to another corporation, the acquiring corporation is not liable for the debts and liabilities of the transferor unless (1) the successor has expressly or impliedly assumed the predecessor’s liability, (2) there was a consolidation or merger of seller and purchaser, (3) the purchasing corporation was a mere continuation of the selling corporation, or (4) the transaction is entered into fraudulently to escape such obligations. Schumacher v. Richards Shear Co., Inc., 59 NY2d 239, 2440245 (1983); Sweatland v Park Corp., 181 AD2d 243, 245 (4th Dept 1992). “[A] transaction structured

² The paragraphs of the Second Verified Amended Complain are incorrectly numbered, and the court is assuming that the paragraphs were intended to be numbered consecutively.

as a purchase-of-assets may be deemed to fall within this exception as a 'de facto' merger, even if the parties chose not to effect a formal merger." In re New York City Asbestos Litigation, 15 A.D.3d 254 (2005).

To determine if there has been a de facto merger, the court is to assess if the following factors are present: (1) continuity of ownership; (2) cessation of ordinary business operations as soon as possible after the transaction; (3) the buyer's assumption of the liabilities ordinarily necessary for the uninterrupted continuation of the seller's business; and (4) continuity of management, personnel, physical location, assets and general business operations. Fitzgerald v. Fahnestock & Co., 286 AD2d 573, 574 (1st Dept 2001). At the same time, "not all of these factors are needed to demonstrate merger rather these factors are only indicators that tend to show de facto merger." See Sweatland v. Park Corp., 181 AD2d at 245(internal quotations and citations omitted).

That being said, however, under New York law, it has been held that "because continuity of ownership is 'the essence of merger,' it is a necessary element of any de facto merger finding although not sufficient to warrant a finding by itself." New York City Asbestos Litigation v. A.W. Chesterton Co., 15 AD3d 254, 256 (1st Dept 2005), quoting Cargo Partner AG v Albatrans Inc., 352 F3d 41, 47 (2nd Cir. 2003). "Continuity of ownership describes a situation where the parties to the transaction 'become owners together of what formerly belonged to each.'" Id., quoting Cargo Partner AG v Albatrans Inc., 352 F3d at 47.

However, "the de facto merger test requires *continuity*, not uniformity of ownership, and nominal changes in the ownership structure of a corporate entity do not undermine the finding of de facto merger." Miller v. Forge Mench Partnership, Ltd., 2005 WL 267551, * 8 (SD NY 2005)(emphasis in the original). In addition, "[t]he requirement of ownership continuity does

not exalt form over substance. The fact that the seller's owners retain their interest in supposedly sold assets (through their ownership interest in the purchaser) is the 'substance' which makes the transaction inequitable." Cargo Partner AG v Albatrans Inc., 207 F.Supp2d 86, 104 (SD NY 2002), aff'd, 352 F3d 41, 47 (2nd Cir. 2003).

Here, Signature argues that allegations of continuity of ownership by At Last are insufficient to state a claim since the consideration for the sale of Newport's assets was cash and not stock thus precluding the owners of Newport from receiving an interest in the Signature. In support of its argument, Signature provides a copy of the sales agreement and cites to case law holding that the continuity of ownership factor is not satisfied when the assets are purchased solely for cash and the shareholders of the predecessor corporation did not become shareholders of the successor corporation. See e.g. New York City Asbestos Litigation v. A.W. Chesterton Co., 15 AD3d at 256 ("there is no continuity of ownership between Old H-T and New H-T since New H-T paid for Old H-T's assets with cash and not stock and neither Old H-T or any of its shareholders has become a shareholder of New H-T"); Desclafani v. Pave-Mark Corp., 2008 WL 3914881, *4, 5 (SD NY 2008). Signature also points to a limitation of liability clause in the sales agreement, to support its position that Signature did not intend to assume Newport's liabilities.

However, that "the transaction was structured as an asset purchase for cash and the agreement expressly sought to limit the purchaser's liability" are not dispositive. Nettis v. Levitt, 241 F3d 186, 194 (2d Cir 2001), overruled on other grounds by, Slayton v. Am. Express Co., 460 F3d 186, 193-194 (2d Cir 2006). Notably, while Signature submits proof apparently showing that Newport was sold to Signature by its secured creditors in an all cash deal, it provides no evidence regarding the identity of Newport's shareholders before the purchase and whether they were the same as the owners of Signature. Nor does Signature provide an affidavit

or other evidence to refute the statements of At Last's Certified Financial Officer that Signature is "composed of, directly or indirectly of some or all of the same owners as Newport."

In the absence of such evidence, At Last should be permitted to conduct discovery regarding the ownership of the two companies particularly as it is alleged that Signature acquired all the assets of Newport and is utilizing Newport's name, business accounts and good will, and that Signature has many of the same employees and officers as Newport including the President Chief Executive Officer, and Director of Finance and it is alleged that Signature moved into Newport's Offices and has the same website. See Sweatland v. Park Corp., 181 AD2d at 245 (requiring further discovery regarding whether there was de facto merger when defendant "acquired all of [the seller's] fixed assets and many of its intangible assets such as good will, engineering, patents, copyrights, and customer lists"); Nettis v. Levitt, 241 F3d at 194 (finding that the district court erred in refusing to permit the addition of defendants to the complaint to allege successor liability where the purchase agreement involved the wholesale acquisition of the seller's business even though the agreement was structured as an asset purchase for cash and sought to limit the purchaser's liability); compare Washington Mutual Bank, F.A. v. SB Mortgage Corp., 21 AD3d 953 (2nd Dept 2005)(dismissing the complaint seeking to hold defendant liable for its predecessors debt where the terms of the employment agreement established lack of continuity of ownership as a matter of law).

Accordingly, the motion to dismiss the fourth cause of action alleging Signature's successor liability is denied.

Conversion

Regarding the claim for conversion, the Second Verified alleges that "Newport... and Signature have intentionally exercised dominion and control over the merchandise, title to and ownership of which belongs to At Last." Second Amended Verified Complaint ¶45.

Signature argues that the conversion claim must be dismissed since under New York Uniform Commercial Code § 2-401, title to goods generally passes upon their delivery and that at most, At Last has a breach of contract claim. At Last counters that it retained title pursuant to an agreement with Newport, citing New York UCC § 2-401(2). In reply, Signature argues that even if there were an agreement that title to the dresses did not pass to Newport upon delivery, pursuant to New York UCC §2-401 (1), At Last only maintains a security interest in the goods, and such security is not a sufficient basis for a claim for conversion.

To properly plead a cause of action for conversion, it is incumbent upon the plaintiff to allege facts establishing that he owned or had a superior right to the materials in question, that plaintiff demanded their return, and that defendant refused to deliver them. See Weider v Chemical Bank, 202 AD2d 168 (1st Dept), ly denied 83 NY2d 759 (1994). Here, as At Last cannot show it had a superior right to the dresses than Signature, its claim for conversion must be dismissed.

Under New York's UCC § 2-401, absent an agreement to the contrary, title to the goods passed upon delivery. Here, counsel for At Last conceded at oral argument that there was no express agreement that At Last would retain title to the dresses after their delivery to Newport, but asserted the such an agreement could be inferred by the course of dealings between At Last and Newport. In any event, even if such an agreement could be inferred, under UCC § 2-401(1) "[a]ny retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited to effect a security interest." See also Shanghai Changhong Intern. Trading Co. v. K& d Logistics Co., LTD., 2002 WL 1732807 (ED NY 2002).

Here, even assuming *arguendo* that At Last has a security interest in the property, such interest, which At Last does not claim it perfected, would be insufficient to provide a basis for a conversion claim here since Signature has shown that Newport's secured creditors which sold

the property at issue to Signature had a perfected security interest in property. As At Last has not shown a superior interest in the property at the conversion claim must be dismissed. See Burns v. Bank of America, 655 FSupp2d 240, 257 (SD NY 2008)(rejecting conversion claim where bank conducted a lawful foreclosure sale); see also, Anderson on the Uniform Commercial Code § 2-401:138 (2010).

Conclusion

In view of the above, it is

ORDERED that the motion to dismiss by defendant Signature Styles LLC is granted to the extent of dismissing the third cause of action (piercing the corporate veil) and the fifth cause of action (conversion) against it and is otherwise denied; and it is further

ORDERED that the remainder of the causes of actions shall continue; and it is further

ORDERED that the cross-motion for leave to amend the complaint is granted; and it is further

ORDERED that the proposed Second Amended Verified Complaint in the form annexed to the cross motion is deemed served; and it is further

ORDERED that the defendants are directed to serve an answer to the remaining claim in the Second Amended Verified Complaint within 30 days of the date of this decision and order; and it is further

ORDERED that the parties shall appear in Part 11, room 351 on November 18, 2010 at 9:30 am for a preliminary conference.

Dated: October 5, 2010

FILED
J.S.C.
OCT 07 2010
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