| **Fogel v American Intl. Indus. for Clubman** |
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| 2017 NY Slip Op 30129(U) |
| January 18, 2017 |
| Supreme Court, New York County |
| Docket Number: 1900093/2016 |
| Judge: Peter H. Moulton |
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SUPREME COURT OF THE STATE OF NEW YORK: Part 50
ALL COUNTIES WITHIN THE CITY OF NEW YORK
----------X Index 1900093/2016
IN RE NEW YORK CITY ASBESTOS LITIGATION
----------X,
LESLIE FOGEL and CATHERINE FOGEL

Plaintiffs

-against- Motion Seq. 001

AMERICAN INTERNATIONAL INDUSTRIES FOR CLUBMAN et al

Defendants

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PETER H. MOULTON, J.S.C.:

Plaintiffs commenced this action against multiple defendants, including defendant American International Industries ("All") as the successor to Neslemur Company, the manufacturer of Clubman brand talc. All moves for summary judgment dismissing all claims and cross-claims against it on the basis that plaintiff alleges exposure to talc during the period 1958-1986, but defendant did not have any involvement with Clubman talc until it purchased the brand in 1987. To support the motion, defendant submits the affidavit Charles Loveless, defendant's Executive Vice President, who has been with the company for approximately 25 years.

Plaintiffs maintain that summary judgment must be denied because under an Asset Purchase Agreement (the "Agreement") defendant assumed tort liability pertaining to the use or sale of Clubman products prior to defendant's purchase of the brand in 1987.[1] Plaintiffs also maintain that summary judgment should be denied because as a result of the sale, a de facto merger occurred. Plaintiffs further maintain that defendant's purchase of the Clubman brand constituted a mere continuation of Neslemur's business subjecting defendant to liability as a successor. Plaintiffs also assert that Charles Loveless' affidavit is conclusory and is not based on personal knowledge, and,

[1]The Agreement is dated August 13, 1987 and is between defendant and the sellers Neslemur Company ("Neslemur") and its parent, Kleer-Vu Industries, Inc. ("Kleer-Vu").

that issues of fact exit for trial. Furthermore, plaintiffs maintain that the motion is premature because no discovery has been conducted on the successor liability issue.

Defendant's motion is granted to the extent of dismissing plaintiffs' claim against defendant for successor liability predicated on the Agreement and is otherwise denied, with leave to renew upon completion of discovery on the issue of successor liability.

Arguments Regarding Liability Under The Purchase Agreement

The crux of the dispute centers around Section 2 and Section 8 of the Agreement. Defendant points to Section 2.3 (entitled "Assumption of Liabilities") which defendant maintains sets forth the entire universe of liabilities that defendant assumed when it purchased the Clubman brand. Defendant maintains that it assumed only the following liabilities (noting that tort liabilities are not included in the list): (1) $1,391,000 of financial liabilities and $3,700,000 of indebtedness then owed to the Third National Bank in Nashville (Section 2.3[a]) and, (2) liabilities arising out of contractual agreements and licenses (Section 2.3[b]). Defendant stresses that Section 2.3(c) states that "[t]he Purchaser shall not assume or be obligated in respect of any liabilities or obligations of the Seller, except those assumed pursuant to Section 2.3(a) and Section 2.3 (b)."

Plaintiffs assert that while Section 2.3 (c) limits defendant's obligations, the limitation is only with respect to *contracts*. Plaintiffs point out that tort liabilities are not discussed in Section 2.3. However, plaintiffs assert that they are discussed in Section 8 (entitled "Indemnification"). Section 8.1(b) states in relevant part:

> [E]ach of the Seller (Neslemur) and Kleer-Vu hereby agrees to indemnify and hold the Purchaser (All)...harmless against any and all claims, liabilities or obligations which may arise out of or result from the use of any products or goods sold by the Seller (Neslemur) before the Closing, and against all actions, suits, proceedings, judgments, costs and expenses connected with any of the foregoing; provided, however, that the Purchaser shall timely notify the Seller and Kleer-Vu of any such claims and shall permit the Seller and Kleer-Vu, at their election, to negotiate and settle such claim, and shall provide such records and witnesses as may be necessary

to litigate such claim.[2]

Plaintiffs assert that once a claim arises against defendant stemming for the use of any products sold before the closing date, defendant may seek indemnification from the sellers for these same liabilities- - thus, defendant assumed the liabilities but defendant can pass them on through the indemnification clause. Plaintiffs argue that the indemnification provisions would be superfluous or meaningless unless defendant and the sellers intended that defendant actually assume tort liabilities. Plaintiffs conclude that "[r]ead carefully, Section 8 of the Agreement reveals the parties' intention to transfer the liabilities arising from products sold before the closing date to All, and upon a demonstration of four conditions, once met, would require the sellers to contractually indemnify All for such liabilities. Thus, All's argument rests on an illogical premise, since indemnification with conditions precedent would be entirely unnecessary unless the liabilities indeed transferred to All." Plaintiffs also cite *Grant-Howard Assoc. v General Housewares Corp.* (63 NY2d 291 [1984]) for the proposition that defendant's argument that the indemnification provisions evidence that defendant is not a successor, suffers from the fatal flaw of reliance on the "faulty premise . . . that the doctrine of successor corporations is related to theories of indemnification." Plaintiffs then cite *Vigilant Ins. Co. v Federal Ins. Co.* (163 AD2d 202 [1st Dept 1990]) for the proposition that liability based on contractual indemnification does not control the existence of common law liabilities.[3]

Defendant counters that the indemnification provisions do not create any ambiguity. Defendant argues that Section 8 of the Asset Purchase Agreement does not deal with the assumption

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[2]Plaintiffs note that Section 8.2 contains a reciprocal provision whereby defendant agreed to defend and indemnify the sellers for claims "arising out of the use of any products or goods sold by All after the Closing".

[3]It is not clear why plaintiffs cite *Vigilant Ins. Co.* While the *Vigilant* Court noted that common law indemnity can exist outside of a contract, plaintiffs' central argument is based on the contract, and not the common law. Presumably, this argument does not relate to plaintiffs' second argument (that defendant is liable as a successor corporation) because, as plaintiffs note, *Grant-Howard Assoc.* explains that the doctrine of successor liability is unrelated to contractual indemnification.

of liabilities, which is only addressed in Section 2.3. Defendant counters plaintiffs' argument that the indemnity provisions would be superfluous or meaningless if defendant did not assume the tort liability in the first instance. Defendant's counsel maintains that the indemnification provisions were inserted because "not all jurisdictions follow New York's approach to successor liability thereby creating a risk that the parties' intent would not be effectuated in every jurisdiction where the Clubman brand was used and sold." Defendant's counsel observes that in 1977, in California, (defendant's headquarters), courts applied a rule known as the "product-line exception" to successor liability years before the Agreement was drafted.[4] Thus, defendant claims that because of "the existence of the product-line exception and its application in numerous jurisdictions, including the one where All was based at the time of the Asset Purchase Agreement's execution (1987), the indemnification provisions are nothing more than procedural safeguards to ensure that Neslemur/Kleer-Vu remained responsible for tort liabilities related to the use of Clubman brand products prior to 1987." Furthermore, defendant argues that the indemnification provisions actually support defendant's argument because they evidence an intent to ensure that the sellers are financially responsible for products manufactured or used during the time that the sellers owned the company, while defendant is financially responsible for claims for products manufactured or used after the sale.

Arguments Regarding Successor Liability

Defendant argues that the purchase was not a de facto merger, especially given that the purchase was for cash and there was no continuity of ownership between predecessor and successor entities, the sine qua non of a merger. Citing the Loveless Affidavit, defendant asserts that no

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[4]Defendant's counsel cites *Ray v. Alad Coro.* (19 Cal 3d 22, 560 P2d 3 [1977]), which held that under the product-line exception, an entity which acquires a manufacturing business and continues the output of its line of products can be held liable in tort even where the acquiring entity disclaimed liability for the predecessor's active torts. Defendant's counsel also notes that the product-line theory was applicable in New Jersey and Washington State, citing *Ramirez v. Amsted Industries. Inc.* (86 NJ 332, 431 A2d 811 [1981]) and *Martin v. Abbot Laboratories* (102 Wash 2d 581 [1984]).

shareholders, directors or managers from Neslemur or Kleer-Vu joined All after the transaction was consummated. Defendant cites *Matter of New York City Asbestos Litig.* (15 AD3d 254, 256 [1st Dept 2005] ["it has been held that, because continuity of ownership is the essence of a merger, it is a necessary element of any de facto merger finding" and continuity of ownership exists only where "the shareholders of the predecessor corporation become direct or indirect shareholders of the successor corporation"]). Defendant also cites *Matter of TBA Global, LLC v. Fidus Partners, LLC*, 132 AD3d 195 [1st Dept 2015] ["[w]e agree with the Second Circuit that, under New York Law, continuity of ownership is the touchstone of the de facto merger concept and thus a necessary predicate to a finding of a de facto merger"] and *Oorah, Inc, v. Covista Communications, Inc.*, 139 AD3d 444 [1st Dept 2016] ["Continuity of ownership is an essential element of de factor merger"]).

Defendant also concedes that it acquired many assets from Neslemur under the Agreement, but citing the Loveless affidavit, asserts that defendant did not acquire any physical plant locations or other such real estate. Moreover, defendant asserts that it was not a mere continuation of either Neslemur and/or Kleer-Vu because under *Schumacher v. Richards Shear Co., Inc.* (59 NY2d 239 [1983]) "[t]he mere continuation exception "refers to corporate reorganization...where only one corporation survives the transaction." Under *Greenlee v. Sherman* (142 AD2d 472 [3d Dept 1989]), defendant maintains that the mere continuation exception can only apply where the successor-buyer does not exist prior to the purchase of the predecessor's assets. Here, defendant maintains that it existed, and was not affiliated with either Neslemur or Kleer-Vu, prior to purchase of the Clubman brand. Defendant asserts that it was an ongoing concern which merely purchased the assets of another entity that continued to exist after the transaction. Defendant also makes much of the fact that Neslemur was not dissolved as a result of the asset purchase. However, as plaintiffs correctly point out, a company need not be actually dissolved if it is essentially shorn of its assets.

In opposition, plaintiffs point to page 70-73 of the Agreement and exhibits and note that defendant purchased from the sellers: all inventories of products whether complete, work-in progress, and raw materials; furniture and fixtures and office equipment; right, title and interest for prepaid advertising; all seller's patents, trademarks, service marks, logos and related art work,

copyrights and registrations, trade names, names or slogans; all knowhow, processes, trade secrets, technology, information, designs, films, plates, art work, maps used to produce packaging supplies and advertising materials; all customer records; the business of the seller including their phone number; and all machinery, equipment, tooling, or parts. Plaintiffs point to page 76 of the Agreement indicating that defendant also purchased Neslemur's goodwill. Plaintiffs also attempt to read out any continuity of ownership requirement because, after the sale, "as a practical matter, it simply owned an empty shell. Thus, whatever continuity of ownership exists, must lie with defendant All." Plaintiffs further stress that "[w]hile All claims that no shareholder, directors or managers from Neslemur or Kleer-Vu joined All after the purchase (based on the self-serving affidavit of Charles Loveless), there has been little if any discovery provided by All in this regard pertaining to who from Neslemur was retained to run the company." Plaintiffs conclude that defendant is liable because it admitted in depositions that it was in the business of buying companies with existing brands and selling those very same products using everything defendant acquired from the sellers.

Discussion

Liability Under The Purchase Agreement

*Grant-Howard Assoc.*, 63 NY2d 291, *supra,* upon which plaintiffs rely, is instructive. In that case the Court held that parties may allocate risk for injuries among themselves, irrespective of whether a corporation is liable as a successor. In *Grant-Howard Assoc.*, like here, "[n]o express reference was made to contingent tort liability" in a purchase agreement provision (*id.* at 295). The purchase agreement also contained an indemnification provision providing that the defendant was not responsible for liabilities which the defendant did not assume under the agreement. The case is instructive because the Court looked only to the assumption of liabilities provision to determine the liability issue, noting that indemnification between a seller and purchaser relates to the "ordering of relations between the two contracting parties, not guaranteeing that some third party has recovery

against a tort-feasor" (*id.* at 297).[5] The *Grant-Howard* Court further commented on the plaintiff's "faulty premise : that the doctrine of successor corporations is related to theories of indemnification" (*id.*).

Plaintiffs focus on the Court's statements that "[a] sale of assets does not vitiate the original company's liability"; that a sale "may" allow an injured plaintiff to proceed against a successor corporation; and that an injured parties' right to proceed against the defunct corporation, the successor corporation, or both "cannot be altered per se by the corporations. . . The companies can regulate how such liability will be allocated among themselves, but they cannot affect the rights of a stranger to their contract" (*id.*). However, plaintiffs' main argument regarding defendant's assumption of liabilities is based on the Agreement. Plaintiffs attempt to use the indemnification provision as evidence that defendant assumed liability, but *Grant-Howard* illustrates that the doctrine of successor corporations is unrelated to theories of indemnification. Even assuming the correctness of plaintiffs argument (that the assumption of liability provisions are limited only to contracts given that they only mention contracts and are silent as to tort liability), liability assumed under a contract cannot be predicated on silence. Plaintiffs point to no other provision in the Agreement where defendant agreed to assume tort liability for the sale or use of products, whether before or after the closing. Plaintiffs assert that the mere fact that the sellers agreed to indemnify defendant for claims arising from the use or sale of products prior to the closing implies that defendant assumed the liability in the first instance (otherwise, plaintiffs question, why would you need an indemnification clause). However, plaintiffs cannot look to the indemnification provisions to create liability when *Grant-Howard Assoc* holds that indemnification provisions relate to the allocation of responsibility, not issues of liability. Nor can plaintiffs look to the indemnification provisions to create an ambiguity for the same reasons (*compare American Standard, Inc. v OakFabco, Inc.*, 14 NY3d 399,

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[5]The assumption of liability clause provided that defendant "[agreed] to assume, perform and discharge (i) all of the obligations and liabilities of [Holt Howard] which exist at the Closing Date, except for such of those liabilities as are excluded from this assumption by the following Section 6(c)" (*id.* at 297). Section 6(c) contained a general and specific enumeration of those matters.

401 [2010] [liabilities assumed by defendant under a purchase agreement included a claim brought by a plaintiff who was injured after the closing date by asbestos-containing boilers installed prior to the closing date, where defendant's purchase included "all debts, liabilities, and obligations and commitments . . . existing and outstanding at the Closing Date"]).[6] Accordingly, the motion is granted to the extent of dismissing plaintiffs' claim against defendant for successor liability predicated on the Agreement

Successor Liability

Generallly, a corporation which acquires the assets of another is not liable for the torts of its predecessor (*Schumacher*, 59 NY2d at 244, *supra*). An exception exists where there has been "a consolidation or merger of seller and purchaser" (*id.* at 245). 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, if the following factors are present: (1) continuity of ownership; (2) cessation of ordinary business operations and the dissolution of the selling corporation 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 operation (*see Fitzgerald v Fahnestock & Co.*, 286 AD2d 573, 574 [2001]).

Although plaintiffs attempt to read out the continuity of ownership requirement, that is "the touchstone of the [de facto merger] concept" and "thus a necessary predicate to a finding of a de facto merger" (*Matter of TBA Global, LLC,* 132 AD3d at 210, *supra* [internal citations omitted] [there was no continuity of ownership between seller and buyer which would require the buyer to arbitrate because it was undisputed that none of seller's owners acquired a direct or indirect interest in the buyer as a result of the transaction]). The purpose of requiring continuity of ownership is to

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[6]Plaintiffs assert that defendant is liable as a successor under common law, which could explain why the parties ordered the liability under the Agreement in the manner that they did. However, the Court need not determine the parties' undisclosed intent, for the reasons stated.

identify situations where the shareholders of a seller corporation retain some ownership interest in their assets after cleansing those assets of liability (*id.*). It is the fact that the seller's owners retain their interest in the supposedly sold assets (through their ownership interest in the purchaser) that makes the transaction inequitable (*id.*). Where a buyer pays a bona fide, arms-length price for the assets, there is no unfairness to creditors in limiting recovery to the proceeds of the sale (*id.*). That is because the cash or other consideration roughly equal to the value of the purchased assets takes the place of the purchased assets as a resource for satisfying the seller's debts (*id.*) [7] Otherwise, creditors may collect against the purchasers of insolvent debtors' assets, which would give the creditors a windfall by increasing the funds available compared to what would have been available if no sale had taken place (*id.*). This concept has been applied in asbestos tort cases (*Matter of New York City Asbestos Litig.*, 15 AD3d 254, *supra* [buyer was not liable for seller's torts given that two of the four factors required for de facto merger were lacking: continuity of ownership and dissolution, which was absent because the seller continued existence in a meaningful way]).

In *State of New York v National Serv. Indus., Inc.* (460 F 3d 201 [2d Cir 2006]), cited by defendant and by *Matter of TBA Global, LLC*, 132 AD3d 195, *supra,* then Circuit Judge Sonia Sotomayor found that continuity of ownership is required under New York law, especially because New York rejected the product line theory of successor liability in *Semenetz v Sherling & Walden, Inc.* (7 NY3d 194 [2006] [product line exception rejected because it would deter the purchase of ongoing manufacturing businesses, force sellers to liquidate, and would place liability upon a party that did not place the product in the stream of commerce]). Judge Sotomayor found that the rejection of the product line exception in *Semenetz* signaled that the policy considerations at issue in tort cases were not sufficient to justify the departure from the common-law standards that would be necessary to find the existence of a de facto merger, in the absence of any evidence of continuing ownership.[8]

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[7]Of course in the tort context, where the product involves a long latency period, the funds may no longer be available due to the passage of time.

[8]Judge Sotomayor also stated that "[t]his does not mean, however, that the court might not read those standards flexibly in tort cases and that other indicia of control over or continuing benefit from the sold assets might not be sufficient to satisfy the continuity of ownership factor"

Thus, contrary to plaintiffs' argument, successor liability cannot be predicted on the mere fact that defendant was in the business of buying companies with existing brands and selling those very same products using everything defendant acquired from the sellers - a perfectly acceptable scenario under *Semenetz*.

However, as plaintiffs note, while Charles Loveless has been with defendant a long time, he was not employed by defendant in 1987 when the Agreement was executed. Loveless' terse affidavit does not state how he knows that there was no continuity of ownership, or other facts disproving successor liability. He does not refer to any corporate or public records that might be admissible to demonstrate that no shareholder, directors or managers from Neslemur or Kleer-Vu joined defendant after the purchase. The affidavit is insufficient to demonstrate, as a matter of law, that successor liability will not lie. Moreover, because this action is in its nascent stages, discovery on the issue of successor liability is appropriate.

It is hereby

ORDERED that defendant's motion is granted to the extent of dismissing plaintiffs' claim against defendant for successor liability predicated on the Agreement; and it is further

ORDERED that defendant's motion is otherwise denied, with leave to renew upon completion of discovery on the issue of successor liability.

This constitutes the Decision and Order of the Court.

**Dated:** January 18, 2017

**New York, New York**

**J.S.C.**
**PETER H. MOULTON**

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(*id.* at n 5). Thus, she cited an example of a continuing benefit involving a purchase agreement which required the purchasing corporation to retain the president of the seller as a consultant and to pay him a $ 60,000 annual consulting fee (*id.*). It is unnecessary to decide at this time whether a de facto merger can only occur in a tort case where there is a stock transfer (see *Matter of New York City Asbestos Litig.*, 15 AD3d 254, *supra* [in a tort action, the transaction was paid for in cash, and there was no evidence that any seller became a shareholder in the buyer]; *Oorah, Inc., supra*, 139 AD3d 444 [in a breach of contract action, the evidence demonstrated that the transaction was paid for in cash and plaintiff did not allege overlapping owners or executives or offices]).