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Products Liability: An Argument for Product Line Liability in Texas

Charles E. Cantú
St. Mary's University School of Law, ccantu@stmarytx.edu

David S. Goldberg

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PRODUCTS LIABILITY: AN ARGUMENT FOR PRODUCT LINE LIABILITY IN TEXAS***

CHARLES E. CANTU*
DAVID S. GOLDBERG**

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I. INTRODUCTION

In 1985, the ABC Corporation ("ABC") designed, manufactured, and placed into the stream of commerce a product called the "Wonder Widget."[1] Fred Consumer bought a Wonder Widget in 1986. Later that year, ABC was "bought out" by Gigantic, Incorporated

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* Professor of Law, St. Mary's University School of Law. B.A., University of Texas; J.D., St. Mary's University; M.C.L., Southern Methodist University; Fulbright Scholar, Universidad de Rene Gabriel Moreno, Santa Cruz, Bolivia; LL.M., University of Michigan.

** Associate, Haynes and Boone, Fort Worth, Texas; B.S., Texas Christian University, J.D., St. Mary's University.

1. The scenario presented here is solely for illustrative purposes, and no reference is intended toward any parties now or at any time in the past.

("Gigantic"), and ABC dissolved shortly thereafter. However, the successor corporation,[2] Gigantic, continued to manufacture the identical product and marketed the widgets under the original trade name. After ABC's dissolution, Fred Consumer was using his widget and was severely injured when it unexpectedly malfunctioned. Consumer's medical bills began to mount, and as a result of the injury sustained, he could no longer work full time. The resulting financial pressures led Consumer to consult his attorney about the feasibility of a products liability suit. After some brief research, the attorney called Consumer to give him the bad news: Consumer's Wonder Widget was manufactured by the ABC Corporation, which had completely dissolved in 1986. State law precluded any suit against Gigantic, Incorporated because, although Gigantic was a successor in fact, it was not a successor as a matter of law. Furthermore, since Consumer's injuries occurred after the dissolution of ABC, ABC could not be sued by Consumer. Fred Consumer had therefore become a rarity in the law of torts: He was a severely injured plaintiff with no available means of seeking compensation for the harm he had sustained.

While the above scenario is fictitious, unfortunately the plight of similarly situated plaintiffs today is not. In the fast-paced climate of today's business world, buy-outs, takeovers, mergers, and other acquisitions of various forms are common occurrences.[3] As a consequence of this corporate turnover, the consumer plaintiff injured while using a defective product may find that a search for the proper defendant is futile, simply because the product is now marketed by a different legal entity. Generally, the consumer has no recourse against the manufacturer of the particular product which caused the injury if that manufacturer has since dissolved.[4] The critical issue becomes whether the

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2. The term "successor corporation" is used here and throughout this article to mean any corporation which has acquired some or all of the assets of another corporation. The term generally applies, however, to a corporation which has legally succeeded to the rights and the burdens of a predecessor corporation. *See* International Ass'n of Machinists v. Shawnee Indus., 224 F. Supp. 347, 352 (W.D. Okla. 1963).

3. *See generally* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441 (1982)(describing business circumstances under which successor corporations should be liable for product defects).

4. *See, e.g.*, Ray v. Alad Corp., 560 P.2d 3, 9 (Cal. 1977)(even where judgment against dissolved corporation obtained, collection not possible from former stockholders); Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1111 (Ill. App. Ct. 1982)(plaintiff's loss of remedy because of corporation's dissolution is problem, not solution). *But see* Naugher v. Fox River Tractor Co., 446 F. Supp. 1281, 1283 (N.D. Miss. 1977)(remedy available against dissolved corporation under liberal construction of pertinent statute). *See gener-*

successor corporation should be held liable. Typically, courts have resorted to the law of corporations in answering this question.[5] There are essentially three methods of transferring the corporate ownership of a business,[6] and each of the three methods of corporate transfer has a different impact on the liabilities of the corporations involved. The effect of judicial reliance on corporate law has been that a plaintiff's ability to recover is determined by the manner in which the change in corporate ownership is accomplished.[7]

The first method of transfering corporate ownership is a statutory merger or consolidation, which now is strictly regulated in virtually all jurisdictions.[8] Stated in simple terms, a merger is accomplished by one corporation merging into and becoming a part of another existing corporation.[9] A consolidation occurs when two corporations combine

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ally Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 593-95 (1977)(remedies available to plaintiffs virtually worthless); Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 444-46 (1982)(discussing successor's liabilities as consideration in selecting method of corporate transfer).

5. *See* Pelc v. Bendix Mach. Tool Corp., 314 N.W.2d 614, 618 (Mich. Ct. App. 1981)(stating traditional rules and exceptions of successor liability); *see also* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 443, 447 (1982)(noting shift in judicial attitudes toward traditional rules); *cf.* Jones v. Johnson Mach. and Press Co., 320 N.W.2d 481, 484 (Neb. 1982)(citing cases abandoning traditional corporate analysis); *Manh Hung Nguyen*, 433 N.E.2d at 1109 (stating that traditional corporate law should not be ignored).

6. *See generally* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 585 (1977)(three methods of transfer); Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 444 (1982)(introducting three methods of transfer).

7. Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 880 (Mich. 1976)(avoidance of product liability may be only reason to choose cash purchase of assets over merger); *see also* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 590-93 (1977)(acquisition may be structured as assets purchase to avoid product liability); Heitland, *Survival of Products Liability Claims in Assets Acquisitions*, 34 BUS. LAW. 489, 498-99 (1979)(recommending that acquired corporation be set up as subsidiary to protect buying corporation from potential liability); *cf.* Shannon v. Samuel Langston Co., 379 F. Supp. 797, 803 (W.D. Mich. 1974)(corporations not permitted to avoid liability by manipulation of corporate entities).

8. *See* H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 346, at 983 (3d ed. 1983)("[a]ll current statutes authorize mergers . . . ."). *See generally* TEX. BUS. CORP. ACT ANN. art. 5.06 (Vernon Supp. 1988).

9. *See, e.g.*, Leannais v. Cincinnati, Inc., 565 F.2d 437, 439 (7th Cir. 1977)(one corporation absorbs another); Jacobs v. Lakewood Aircraft Serv., 512 F. Supp. 176, 180 (E.D. Pa. 1981)(one corporation loses existence as separate entity); *Manh Hung Nguyen*, 433 N.E.2d at 1110 (one corporate entity merges into another). *See generally* N. LATTIN, THE LAW OF CORPORATIONS § 170, at 613 (2d ed. 1971)(describing processes of merger and consolidation).

to form a third corporation which did not exist prior to the transaction.[10] By statute, the surviving or consolidated corporation assumes all debts and liabilities, including those based on tort, of the "disappearing" entity.[11] The second means of transferring corporate ownership is through the sale of stock by the shareholders.[12] Since the corporate structure and entity are left undisturbed by a merger, consolidation, or transfer of stock, the tort liabilities of the corporation are also unaffected.[13] As a result, neither of the first two methods of transferring ownership affects the injured consumer's right to a remedy.

The third means by which corporate ownership is changed, however, is the one which is of immediate concern to our injured hypothetical consumer. Under this method, ownership is transferred when one corporation sells all, or substantially all, of its assets to another business.[14] Under the traditional corporate law rule, a corporation which purchases the assets of another legal entity does not assume the debts and liabilities of the selling company.[15] Instead, the seller remains liable for settling its own debts prior to its dissolution.[16] This

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10. *See* N. LATTIN, THE LAW OF CORPORATIONS § 170, at 613 (2d ed. 1971)(corporation created for purpose of consolidation).

11. *See* H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 346, at 982 (3d ed. 1983). Most statutes provide that the "surviving" corporation in a merger is to assume the rights and obligations of the "constituent" corporations which are merged into it. *See, e.g.*, CAL. CORP. CODE ANN. § 1107(a) (Deering 1977); TEX. BUS. CORP. ACT ANN. art. 5.06(A)(3) (Vernon Supp. 1988); REVISED MODEL BUSINESS CORP. ACT § 11.06(a)(3) (1984).

12. *See* H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 341, at 966 (3d ed. 1983).

13. *See id.* at 966 n.30 (purchasing corporation indirectly assumes seller's liabilities); *see also* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 588 (1977)(purchaser indirectly liable by becoming shareholder in selling corporation).

14. *See generally* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 445 (1982).

15. *See, e.g.*, Bazan v. Kux Mach. Co., 358 F. Supp. 1250, 1251 (E.D. Wis. 1973); Schwartz v. McGraw-Edison Co., 92 Cal. Rptr. 776, 783 (Cal. Ct. App. 1971); Comstock v. Great Lakes Distrib. Co., 496 P.2d 1308, 1311 (Kan. 1972).

16. Nardis Sportswear v. Simmons, 147 Tex. 608, 612-13, 218 S.W.2d 451, 453 (corporate president and directors act as trustees to settle corporate business), *modified on other grounds*, 219 S.W.2d 779 (1949); *cf.* Armour-Dial, Inc. v. Alkar Eng'g Corp., 469 F. Supp. 1198, 1202 (E.D. Wis. 1979)(transfer of assets by insolvent seller corporation "unable to meet its obligations to creditors" may be deemed fraud); Lamb v. Leroy Corp., 454 P.2d 24, 27 (Nev. 1969)(selling corporation has obligation to pay creditors). *See generally* 15 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §§ 7122-7123 (rev. perm. ed. 1983)(describing general rule and exceptions).

rule will be applied by the courts unless the facts and circumstances of the sale warrant the application of some judicially-created exception.[17] Traditionally, four exceptions to the above stated rule have been recognized and result in the successor's liability:[18] (1) where the successor corporation expressly or impliedly assumes the obligations of the predecessor;[19] (2) where the purchase is found to be fraudulent because it is made in an attempt to avoid the liabilities of the predecessor;[20] (3) where the transaction results in the successor corporation being the "mere continuation" of the predecessor;[21] and (4) where the alleged sale of assets is found to be a de facto merger or consolidation.[22]

Originally, corporate law addressed itself to questions regarding the contractual and tax liabilities of the predecessor.[23] However, corpo-

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17. *See, e.g.*, Alexander & Baldwin, Inc., v. Peat, Marwick, Mitchell & Co., 385 F. Supp. 240, 243 (S.D.N.Y. 1974)(nature and consequences of the transaction may result in liability); Pelc v. Bendix Mach. Tool Corp., 314 N.W.2d 614, 618 (Mich. Ct. App. 1981)(factual determination essential to imposition of successor liability); Jones v. Johnson Mach. and Press Co., 320 N.W.2d 481, 484 (Neb. 1982)(circumstances may warrant succession to liabilities of predecessor).

18. Numerous cases have stated the general rule and listed the traditional exceptions. *E.g.*, Knapp v. North Am. Rockwell Corp., 506 F.2d 361, 363-64 (3d Cir. 1974), *cert. denied*, 421 U.S. 965 (1975); Cyr v. B. Offen & Co., 501 F.2d 1145, 1152 (1st Cir. 1974); Kloberdanz v. Joy Mfg., 288 F. Supp. 817, 820 (D. Colo. 1968); Tift v. Forage King Indus., 322 N.W.2d 14, 15 (Wis. 1982).

19. *See, e.g.*, Leannais v. Cincinnati, Inc., 565 F.2d 437, 438 (7th Cir. 1977)(successor assumed liability for five years following acquisition); Bouton v. Litton Indus., 423 F.2d 643, 651 (3d Cir. 1970)(successor impliedly assumed predecessor's liabilities by broad language in purchase contract).

20. *See, e.g.*, Armour-Dial, Inc. v. Alkar Eng'g Corp., 469 F. Supp. 1198, 1202 (E.D. Wis. 1979)(assets purchase which renders selling corporation insolvent may be deemed fraud); Lamb v. Leroy Corp., 454 P.2d 24, 27 (Nev. 1969)(stock paid to shareholders to exclusion of creditors may be deemed constructive fraud).

21. *See, e.g.*, *Cyr*, 501 F.2d at 1152 (successor held liable under mere continuation exception); Bergman & Lefkow Ins. Agency v. Flash Cab Co., 249 N.E.2d 729, 737 (Ill. App. Ct. 1969)(applying mere continuation exception); Haney v. Bendix Corp., 279 N.W.2d 544, 545-46 (Mich. Ct. App. 1979)(successor held liable as mere continuation where 90% of sales and production staff same as predecessor).

22. *See, e.g.*, Sanders v. CEG Corp., 157 Cal. Rptr. 252, 257 (Cal. Ct. App. 1979)(grounds for liability based on merger transaction); Shannon v. Samuel Langston Co., 379 F. Supp. 797, 803 (W.D. Mich. 1974)(applying de facto merger theory in product liability action).

23. *See* Alexander & Baldwin, Inc., v. Peat, Marwick, Mitchell & Co., 385 F. Supp. 240, 243 (S.D.N.Y. 1974)(while rule applies to contracts and tax debts, also long applied to tort liability). *See generally* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 444-46 (1982)(describing evolution of corporate law rules to satisfy transferor's creditors).

rate law has also been applied to tort issues, including products liability.[24] Consequently, the purchasing or successor corporation has been held immune from liability for injuries caused by defective products manufactured and marketed by its predecessor, in the absence of facts justifying one of the above exceptions to the general rule.[25] The traditional corporate law rule of successor non-liability and its exceptions were designed to protect the interests of shareholders and purchasing corporations while simultaneously guarding the interests of existing creditors.[26] Unfortunately, the corporate law rule leaves the victim of an accident caused by a defective product in a uniquely disadvantageous position.

Creditors are protected because the predecessor corporation must satisfy its existing debts and contractual obligations prior to dissolving the corporation;[27] the products liability plaintiff, however, has no such protection. As illustrated by our hypothetical scenario, a product's defect may remain undiscovered until long after the predecessor corporation has been dissolved, and our injured plaintiff may be left without a legal remedy.[28] This apparent unfairness, coupled with an increase in litigation of this nature over the last decade, has led to the judicial recognition of a fifth exception to the traditional corporate

24. *See* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 444-46 (1982); *see also* Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 886 (Mich. 1976)(Coleman, J., dissenting)(general rule of non-liability includes liability for tortious conduct). *But see* Bazan v. Kux Mach. Co., 358 F. Supp. 1250, 1251 (E.D. Wis. 1973)(citing old cases holding torts *not* covered by exceptions to general rules of non-liability). *See generally* Hill, *Products Liability of a Successor Corporation—Acquisition of "Bad Will" with Good Will*, 23 IDEA 9, 10-12 (1982).

25. *See* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 446-47 (1982)(discussing traditional application of corporate rule and current changes in judicial approach).

26. *See Turner*, 244 N.W.2d at 878 (corporate law rule and exceptions for benefit of creditors and shareholders); *see also* Note, *Continued Expansion of Corporate Successor Liability in the Products Liability Arena*, 58 CHI.-KENT L. REV. 1117, 1121 (1982).

27. *See, e.g.*, Armour-Dial, Inc. v. Alkar Eng'g Corp., 469 F. Supp. 1198, 1202 (E.D. Wis. 1979)(transfer of assets by insolvent seller corporation unable to fulfill obligations to creditors may be deemed fraud); Lamb v. Leroy Corp., 454 P.2d 24, 27 (Nev. 1969)(selling corporation has obligation to pay creditors); *see also* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 446 (1982)(corporate law rule developed to satisfy known creditors at time of transaction).

28. *See* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 592-93 (1977)(cause of action may not accrue until after dissolution); *see also id.* at 593 n.46 (discussing availability of cause of action for personal injury and property damage).

law rule—the so-called "product line" exception.[29] This fifth exception, which is our principle subject, encompasses a fact situation in which the successor corporation has purchased more than the physical assets of the seller. Rather, the successor has purchased the entire business and continues to manufacture the original product and place it into the stream of commerce. The courts which have applied this new exception have departed significantly from the traditional corporate law rule and have recognized public policy considerations which are similar to those underlying the theory of strict products liability.[30]

Texas courts have chosen not to adopt the product line exception.[31] Instead, Texas courts have followed the traditional corporate law rule of successor non-liability and have adopted some of the above-mentioned exceptions.[32] As illustrated in our hypothetical, the problem that remains unresolved by the Texas approach is that certain consumers injured by defective products are denied the right to seek a remedy in a court of law. This result seems to defy some of the most fundamental principles underlying the law of products liability.

Before presenting arguments for adoption of the product line exception, this article will review the corporate law rule and its original four exceptions. A determination of whether or not Texas courts should adopt the exception must be based upon a careful examination of its underlying policy considerations, as well as of the changing marketplace in recent times, and of the resulting impact on the individual consumer.

II. The Traditional Corporate Rule and Its Exceptions

Absent statutes to the contrary, whenever one corporate entity

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29. *See* Ray v. Alad Corp., 560 P.2d 3, 11 (Cal. 1977).

30. *See, e.g.*, *Ray*, 560 P.2d at 8-9 (considering whether policy supporting strict liability justified special exception to general rule of non-liability of successor corporation); *Turner*, 244 N.W.2d at 877 ("Products liability law must govern" as matter of social policy); Ramirez v. Amsted Indus., 431 A.2d 811, 816 (N.J. 1981)(strict liability law to be applied because traditional corporate law rule too narrow). *But see, e.g.*, Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1109 (Ill. App. Ct. 1982)(corporate law principles apply in cases of successor liability); Jones v. Johnson Mach. and Press Co., 320 N.W.2d 481, 484 (Neb. 1982)(public policy behind products liability not necessarily applicable to successor corporations).

31. *See, e.g.*, Mudgett v. Paxson Mach. Co., 709 S.W.2d 755, 759 (Tex. App.—Corpus Christi 1986, writ ref'd n.r.e.)(following *Griggs*); Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 294 (Tex. App.—Austin 1985, writ ref'd n.r.e.)(rejecting product line theory).

32. *See generally infra* text accompanying notes 223-48.

purchases all, or substantially all, of the assets of another concern, the traditional corporate law rule has been interpreted so as to impose no tort liability upon the successor corporation. This position has been justified as a "fundamental principle of justice and fairness, under which the law imposes responsibility for one's own act and not for the totally independent acts of others."[33] In the context of corporate or contract law, this justification is probably very sound. The rule protects the bona fide purchaser of assets who in good faith has given adequate consideration with no intent to defraud the creditors of the transferring entity.[34] In short, the rule ensures that when one entity purchases the assets of another, the purchaser will not be saddled with a liability that was not bargained for in the exchange.

The rule, however, loses its validity in transactions encompassing more than a mere sale of corporate assets.[35] The courts have implicitly recognized this shortcoming and, as a result, have formulated four exceptions to the traditional corporate law rule. These exceptions have evolved to take notice of the substance rather than the form of many corporate acquisitions.[36] Examining each exception, however, reveals that although each may provide effective protection to the existing creditors of a corporate entity, no exception is fully responsive to the needs of an injured plaintiff.[37] If a plaintiff is seeking redress

33. Leannais v. Cincinnati, Inc., 565 F.2d 437, 439 (7th Cir. 1977).

34. *See generally* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 591-92 & n.42 (1977)(discussing bona fide purchaser's good faith and lack of notice of prior claims).

35. *See id.* at 591 (corporate structure modified in merger or consolidation). The rule is valid in sale of assets transactions because the selling corporation is theoretically able to meet its own obligations. *See id.* at 592.

36. The four exceptions to the traditional corporate law rule apply to transactions which take the form of an asset purchase, but which are in substance or effect a merger, a continuing enterprise, or an attempt to defraud creditors. *Cf.* Jacobs v. Lakewood Aircraft Serv., 512 F. Supp. 176, 180-81 (E.D. Pa. 1981)(considering whether substance of transaction constituted de facto merger); Shannon v. Samuel Langston Co., 379 F. Supp. 797, 803 (W.D. Mich. 1974)(liability of entity cannot be avoided by changing form of property ownership); Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 875 (Mich. 1976)(cause of action may arise where continuity of enterprise shown from totality of transaction).

37. *E.g.*, Ray v. Alad Corp., 560 P.2d 3, 9-10 (Cal. 1977)(plaintiff's remedy destroyed because dissolution "insuperable obstacle" to recovery); Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1111 (Ill. App. Ct. 1982)(plaintiff denied recovery under corporate law); *Turner*, 244 N.W.2d at 878 (plaintiff's only relief from successor); *see also* Note, *Continued Expansion of Corporate Successor Liability in the Products Liability Arena*, 58 CHI.-KENT L. REV. 1117, 1144 (1982)(comparing strict liability law and purpose of providing remedy for plaintiff).

for injuries caused by a defective product placed into the stream of commerce by a corporation which is no longer in existence, the traditional corporate law rule of successor non-liability and its exceptions often offer little hope.

A. *Assumption of Liabilities*

The first exception is the most straightforward of the four. It takes effect whenever, as part of the purchase agreement, the successor corporation expressly agrees to assume not only the existing contractual obligations of the predecessor, but also its contingent obligations or liabilities.[38] The disadvantage to this approach, however, is that the courts will not find such an assumption of tort liability unless the succeeding corporation has expressly and unambiguously assumed it.[39] Furthermore, any clause in a purchase agreement which expressly excludes the assumption of liability for defective products is generally honored by the courts.[40] Under this exception, therefore, purchasing corporations may, through careful drafting of the purchase agreement, avoid any and all liability for defective products even though expressly assuming all of the seller's other obligations.[41] Predictably, under this exception, successor corporations are rarely held responsi-

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38. *See* Bippus v. Norton Co., 437 F. Supp. 104, 106 (E.D. Pa. 1977)(holding successor corporation liable for future product liability claims per terms of agreement of sale).

39. *E.g.*, Kloberdanz v. Joy Mfg. Co., 288 F. Supp. 817, 821 (D. Colo. 1968)(assumption of specified liabilities did not implicitly include tort liability); Schwartz v. McGraw-Edison Co., 92 Cal. Rptr. 776, 783 (Cal. Ct. App. 1971)(assumption of predecessor's warranties not implied assumption of product liability when purchase agreement made before inception of strict products liability); Husak v. Berkel, Inc., 341 A.2d 174, 178-79, 179 n.2 (Pa. Super. Ct. 1975)(assuming "all liabilities" not specific enough to include assumption of strict product liability, especially when strict liability not yet adopted at time of purchase).

40. *See, e.g.*, Leannais v. Cincinnati, Inc., 565 F.2d 437, 438-40 (7th Cir. 1977)(clause limiting liability to five years honored by court); National Dairy Prod. Corp. v. Borden Co., 363 F. Supp. 978, 980 (E.D. Wis. 1973)(successor's refusal to assume liability for patent infringement accepted without question by court because only specific liabilities assumed under agreement). *But see* Cyr v. B. Offen & Co., 501 F.2d 1145, 1153 (1st Cir. 1974)(specific exclusion of tort liability insured purchaser's right of recovery over from predecessor but not binding on third party plaintiff); Hoche Prods., S.A. v. Jayark Films Corp., 256 F. Supp. 291, 295-96 (S.D.N.Y. 1966)(that defendant had assumed predecessor's liabilities either implied from statements by employee and attorney or found by de facto merger theory).

41. *Compare* Bouton v. Litton Indus., 423 F.2d 643, 652 (3d Cir. 1970)(assumption of product liability claims implied where agreement assumed seller's liabilities) *with* Kloberdanz v. Joy Mfg., 288 F. Supp. 817, 821 (D. Colo. 1968)(even though successor assumed seller's liability, tort liability not included).

ble for their predecessors' tort liability.[42] Consequently, this first exception affords little relief, if any at all, to the injured consumer in our hypothetical scenario.

B. *Fraudulent Transfer of Assets*

Similarly, the second exception to the traditional corporate law rule of successor non-liability rarely provides a remedy in a products liability suit.[43] This exception, designed to prevent a fraudulent transfer of assets from one legal entity to another, was formulated primarily to protect existing creditors of the selling corporation.[44] The exception is generally applied whenever a transfer of assets is made from one corporation to another for inadequate or no consideration.[45] If such an exchange leaves the predecessor without available means to satisfy its debts, the transaction is deemed to operate as a fraud upon the creditors of the selling company.[46] The purchasing entity, charged with constructive knowledge of the fraud due to the inadequate consideration given, is held liable to the defrauded creditors.[47] Obviously, this exception would afford much protection to the existing

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42. *See generally* Note, *Continued Expansion of Corporate Successor Liability in the Products Liability Arena*, 58 CHI.-KENT L. REV. 1117, 1120-22, 1128-30 (1982)(general discussion of limited application of the exceptions to the rule); Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 596 & n.64 (1977)(limited application of the assumption exception).

43. Hill, *Products Liability of a Successor Corporation—Acquisition of "Bad Will" with Good Will*, 32 DEF. L.J. 55, 58 (1983); *see also* Wolff v. Shreveport Gas, Elec. Light & Power Co., 70 So. 789, 794-95 (La. 1916)(gas company held liable for injury due to explosion from leaking pipe where subsequent transfer of corporate assets found fraudulent for lack of consideration).

44. *See* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 597 (1977).

45. *See* Economy Ref. & Serv. Co. v. Royal Nat'l Bank, 97 Cal. Rptr. 706, 710 (Cal. Ct. App. 1971)(new corporation held liable where transfer without consideration was attempt to defraud creditor).

46. *See, e.g.*, Armour-Dial, Inc. v. Alkar Eng'g Corp., 469 F. Supp. 1198, 1202 (E.D. Wis. 1979)(transaction rendering seller insolvent may be deemed fraud); Bazan v. Kux Mach. Co., 358 F. Supp. 1250, 1252 (E.D. Wis. 1973)(defendant buyer's case stronger because rights of seller's creditors not impaired); Lamb v. Leroy Corp., 454 P.2d 24, 27 (Nev. 1969)(constructive fraud may be found where buyer issues stock to seller's stockholders to detriment of creditors); *see also* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 597 (1977)(inadequate consideration for corporate assets essence of fraudulent transfer).

47. *See* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 597 n.69 (1977)(citing Lamb v. Leroy Corp., 454 P.2d 24, 27 (Nev. 1969)).

creditors of a going concern, but by its nature is of little use to the consumer who is injured after the manufacturing corporation is dissolved.

These first two exceptions to the traditional corporate rule of successor non-liability are of limited use in an action wherein a plaintiff seeks to impose tort liability on a successor corporation. The last two exceptions, however, are somewhat more useful to an injured plaintiff.

C. *Mere Continuation*

The third exception, the so-called "mere continuation" exception, generally is acknowledged whenever the successor corporation more closely resembles a reorganized version of its predecessor than an entirely new corporate entity.[48] Where a corporation is merely continuing the same business under the different name of a successor, it can be charged with the legal obligations incurred prior to its reorganization.[49] This would, by necessity, include liability for injuries caused by defective products. In order to recognize a continuing enterprise of this sort, courts often look for the presence of certain factors which would indicate a common identity between the successor corporation and the legal entity which preceded it.[50] Such evidence of common identity would include, but not be limited to, the existence of identical stockholders, the same officers, and similar directors.[51] As in the case of fraudulent transfers, the court will also question the adequacy of

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48. *See, e.g.*, *Armour-Dial*, 469 F. Supp. at 1201-02 (mere continuation exists where new corporation merely "new hat" for old entity); City of Altoona v. Richardson Gas & Oil Co., 106 P. 1025, 1025 (Kan. 1910)(liability of successor grounded on "continuance of the original corporation under a new guise"); Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 892 (Mich. 1976)(Coleman, J., dissenting)(continuity of shareholders is, in effect, corporate reorganization).

49. *E.g.*, *In re* Johnson-Hart Co., 34 F.2d 183, 184 (D. Minn. 1929)(where new corporation is mere continuation of old business, it assumes liability for predecessor's debts); *Richardson Gas & Oil Co.*, 106 P. at 1025 (successor liable where new corporation mere continuation of old).

50. *See, e.g.*, *Armour-Dial, Inc.*, 469 F. Supp. at 1201 (continuity based on "common identity" of predecessor and successor)(quoting Leannais v. Cincinnati, Inc., 565 F.2d 437, 440 (7th Cir. 1977)); Bergman & Lefkow Ins. Agency v. Flash Cab Co., 249 N.E.2d 729, 737 (Ill. App. Ct. 1969)(same officers, shareholders, location supported finding of liability for predecessor's fraudulent representations).

51. *E.g.*, Jacobs v. Lakewood Aircraft Serv., 512 F. Supp. 176, 181 (E.D. Pa. 1981); Lopata v. Bemis Co., 383 F. Supp. 342, 345 (E.D. Pa. 1974), *vacated and remanded on other grounds*, 517 F.2d 1398 (3d Cir. 1975); Tift v. Forage King Indus., 322 N.W.2d 14, 17 (Wis. 1982). *See generally* 1 L. FRUMER & M. FREIDMAN, PRODUCTS LIABILITY § 2.06[2][c] (1987)(summarizing mere continuation exception).

the consideration given in the exchange.[52] Such factors have been critical in determining whether the succeeding business entity is an entirely new going concern or a mere continuation of the preceding corporate entity. Curiously enough, however, in the leading products liability case applying the mere continuation exception, these elements were missing.[53]

In *Cyr v. B. Offen & Co.*,[54] the court found that the existing corporation was, for purposes of tort liability for a defective product, a mere continuation of its predecessor.[55] In the case, the B. Offen Company, a sole proprietorship, manufactured and marketed printing presses and ovens.[56] In 1959, Rumford Printing Company purchased one of Offen's products.[57] Following the death of Mr. Offen in 1962, several of his former employees formed a corporation which purchased all of the sole proprietorship's assets.[58] The sales agreement was supported by adequate consideration,[59] and included a provision that the newly formed corporation would operate in substantially the same manner as the preceding business.[60] The contract also expressly excluded the successor's assumption of the predecessor's tort liabilities.[61] The new company, however, continued its operations at the same location and with virtually the same employees and managers.[62] It also represented itself in all advertising as an ongoing operation[63] and, in addition, honored all existing contractual and service obligations, which happened to include servicing and

52. *See* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 600 (1977)(adequacy of consideration most important aspect of mere continuation exception).

53. *See* Cyr v. B. Offen & Co., 501 F.2d 1145 (1st Cir. 1974). The predecessor was a sole proprietorship whose owner had died. *See id.* at 1151. Thus there was no continuity of stockholders or directors. Additionally, the consideration given was apparently adequate. *See id.* at 1152 ("good faith sale at arm's length").

54. 501 F.2d 1145 (1st Cir. 1974).

55. *See id.* at 1154 (successor a mere continuation "in the most real sense").

56. *See id.* at 1151.

57. *See id.*

58. *See id.*

59. *See id.* at 1152.

60. *See id.* at 1151 (same business policies and practices continued). The products were by agreement to be manufactured by the new corporation in the same manner as they had been by the sole proprietorship. *See id.*

61. *Id.*

62. *See id.*

63. *See id.* (company's advertisements claimed business forty years old).

renovating the equipment sold to Rumford.[64]

In 1969, ten years after the equipment had been purchased and seven years after the new corporation had come into existence, two employees of the Rumford Printing Company were injured while cleaning an allegedly defective oven which had been purchased from the B. Offen sole proprietorship.[65] In imposing liability on the successor corporation for these injuries, the court in *Cyr* stressed that this result was brought about because the new company was nothing more than a mere continuation of the prior business.[66] Furthermore, the court concluded that the same policy considerations which support strict products liability as promulgated by the Restatement of Torts section 402A[67] would also support the imposition of tort liability upon a successor corporation in a case of this sort. The court stated:

> The manufacturer's successor, carrying over the experience and expertise of the manufacturer, is likewise in a better position than the consumer to gauge the risks and the costs of meeting them. The successor knows the product, is as able to calculate the risk of defects as the predecessor, is in position to insure therefor and reflect such cost in sale negotiations, and is the only entity capable of improving the quality of the product.[68]

From this case, it seems clear that in situations where one business entity is a mere continuation of another, the courts may overlook the traditional corporate law rule of successor non-liability and impose tort liability for injuries caused by defective products. This position, which considers all relevant facts and circumstances, acknowledges the substance of the transaction over its form. The exception allows an injured party relief where there is in fact no remedy, and, in this respect, the exception operates as a measure of equitable relief. The courts, nevertheless, justify this position for the same reasons that they impose strict liability.

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64. *See id.* Defendant serviced Rumford Press's old dryers, but was not under contract to do so. *Id.*

65. *See id.* at 1148. The employees contended that the ovens were defective for lack of "fail-safe" safety features. *See id.* at 1149.

66. *See id.* at 1154.

67. *See id.* The court enumerated the same policy reasons as those underlying section 402A of the Restatement without specifically identifying the sources. *See infra* text accompanying note 68; *see also* RESTATEMENT (SECOND) OF TORTS § 402A comment c (1965).

68. *See Cyr*, 501 F.2d at 1154.

D. *De Facto Merger or Consolidation*

The finding of a de facto merger or consolidation is the fourth and final traditional exception to the corporate law rule of successor non-liability. Courts apply this theory to transactions which purport to encompass the sale of corporate assets but which in fact have elements more characteristic of a merger or consolidation.[69] It is important to make a distinction between these two actions because in a merger, the successor corporation assumes the liabilities of its predecessor,[70] whereas, as already noted, in an ordinary purchase agreement the corporate law rule of successor non-liability becomes applicable.

The reasons for this important difference are traceable to the differing nature and consequences of the two types of transfers. Whenever the assets of one corporation, for example, are purchased by another corporation, the two entities theoretically remain intact.[71] Both before and after the sale, the corporations are "strangers,"[72] and as such, each has an ability as well as an obligation to satisfy its own respective debts and obligations.[73] A merger or consolidation, on the other hand, presupposes the concurrent dissolution of the selling cor-

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69. *See, e.g.*, Jacobs v. Lakewood Aircraft Serv., 512 F. Supp. 176, 180 (E.D. Pa. 1981)(plaintiff alleged de facto merger because assets sale resembled de jure merger); Shannon v. Samuel Langston Co., 379 F. Supp. 797, 800-01 (W.D. Mich. 1974)(de facto merger found where transaction was something "other than an ordinary purchase of assets"); Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 892 (Mich. 1976)(Coleman, J., dissenting)(de facto merger to be found where result of asset sale same as statutory merger).

70. *See generally* H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 346, at 982 (3d ed. 1983)(assumption of liability in merger acquisitions prescribed by state's corporate statutes).

71. In actions alleging de facto merger, the continued existence of the predecessor corporation for even a short period of time following the sale has often defeated a finding in favor of the claimant. *E.g.*, Leannais v. Cincinnati, Inc., 565 F.2d 437, 440 (7th Cir. 1977)(no dissolution where corporation's distinct identity maintained); Bazan v. Kux Mach. Co., 358 F. Supp. 1250, 1252 (E.D. Wis. 1973)(no dissolution where entity operated as independent company for ten months after sale); Schumacher v. Richards Shear Co., 451 N.E.2d 195, 198 (N.Y. 1983)("meagre" entity surviving sale precludes finding mere continuation).

72. *E.g.*, *Jacobs*, 512 F. Supp. at 181; Kloberdanz v. Joy Mfg., 288 F. Supp. 817, 821 (D. Colo. 1968); *Turner*, 244 N.W.2d at 881-82; McKee v. Harris-Seybold Co., 264 A.2d 98, 104 (N.J. Super. Ct. Law Div. 1970), *aff'd*, 288 A.2d 585 (N.J. Super. Ct. App. Div. 1972).

73. Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 591-92 (1977). Implicit in the general rule of non-liability is the selling corporation's ability to settle its own debts prior to dissolution. *E.g.*, Armour-Dial, Inc. v. Alkar Eng'g Corp., 469 F. Supp. 1198, 1202 (E.D. Wis. 1979)(sale of assets by insolvent seller corporation unable to fulfill obligations to creditors may be deemed fraud); Lamb v. Leroy Corp., 454 P.2d 24, 27 (Nev. (1969)(selling corporation has obligation to pay creditors).

poration.[74] The original entity is dissolved upon completion of the transaction or as soon thereafter as possible,[75] and, as a result, the selling corporation relinquishes its separate identity and becomes part of the successor.[76] This means that all debts, obligations, and, for purposes of this discussion, tort liabilities become the responsibility of the surviving corporate entity.[77] The successor's assumption of liability derives in part from the fact that in a merger or consolidation the shareholders of the selling corporation usually surrender their stock in exchange for shares in the new company.[78] This exchange creates the expectation that even though the predecessor will be dissolved, the operation will continue to exist as a different entity but with the same shareholders.[79] Therefore, it is logical that the existing obligations continue as well.

The underlying distinction between these two types of transactions becomes very important in a scenario such as the hypothetical one presented at the beginning of this discussion, for if the transfer in question is a sale of assets, the traditional corporate law rule of suc-

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74. *See, e.g.*, Shannon v. Samuel Langston Co., 379 F. Supp. 797, 801 (W.D. Mich. 1974)(merger requires absorption and "practically contemporaneous" dissolution of acquired entity)(citing *McKee*, 264 A.2d at 103). Merger statutes generally provide for the dissolution of the entity which is absorbed. *See, e.g.*, TEX. BUS. CORP. ACT ANN. art. 5.06(A)(2) (Vernon Supp. 1988); REVISED MODEL BUSINESS CORP. ACT § 11.06(a)(1) (1984); *see also* H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 346, at 980 (3d ed. 1983)(one corporation disappears).

75. *See* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 444 (1982)(absorbed corporation loses "corporate identity").

76. *See, e.g.*, TEX. BUS. CORP. ACT ANN. art. 5.06(A)(1)-(A)(2) (Vernon Supp. 1988). The statute continues: "Such surviving or new corporation shall have all the rights, privileges, immunities, and powers and shall be subject to all the duties and liabilities of a corporation organized under this Act." *Id.* at (A)(3).

77. *See, e.g.*, TEX. BUS. CORP. ACT ANN. art. 5.06(A)(5) (Vernon Supp. 1988); REVISED MODEL BUSINESS CORP. ACT § 11.06(a)(3) (1984); *see also* Hoche Prods., S.A. v. Jayark Films Corp., 256 F. Supp. 291, 296 (S.D.N.Y. 1966)(stating rule under New York corporation statute); H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 346, at 982 (3d ed. 1983)(liability assumed by absorption). *See generally* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 587 (1977)(general discussion of effects of merger and significance to product liability complainant).

78. *See* H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 346, at 982 (3d. 1983)(surviving corporation buys shares of disappearing corporation); *see also* REVISED MODEL BUSINESS CORP. ACT § 11.06(a)(6) (1984).

79. *See* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 444 (1982). By absorption into another corporation, the acquired business continues its existence as a constituent part of the entity which has "survived" the acquisition. *Id.*

cessor non-liability applies and our injured plaintiff remains remediless. If, on the other hand, the transfer is a merger, the remaining entity remains liable for all obligations, including the tort liability, of the selling company.

Confronted with a transfer of assets which is alleged to be a sale/purchase agreement, the courts will deem the transfer a de facto merger and impose liability accordingly if the evidence is sufficiently characteristic of a merger.[80] To arrive at this conclusion, however, it is necessary to establish four definite patterns in each proceeding.[81] First, there must be a continuation of the enterprise.[82] For example, the successor must retain essentially the same management team and personnel, operate the business in the same general manner, and remain in the same location.[83] Secondly, there must be a continuity of

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80. *See, e.g.*, Jacobs v. Lakewood Aircraft Serv., 512 F. Supp. 176, 180 (E.D. Pa. 1981)(de facto merger not found where transaction did not resemble merger); Shannon v. Samuel Langston Co., 379 F. Supp. 797, 801 (W.D. Mich. 1974)(transaction resembling merger held de facto merger); Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 888 (Mich. 1976)(Coleman, J., dissenting)("corporate merger in fact" can be achieved without complying with merger statute)(quoting Applestein v. United Board & Carton Corp., 159 A.2d 146, 152 (N.J. Super. Ct. Ch. Div.), *aff'd*, 161 A.2d 474 (N.J. 1960)). *See generally* H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 341, at 963 n.16 (3d ed. 1983).

81. Opinions discussing the de facto merger exception in a number of jurisdictions list all four requirements discussed in the text. *E.g.*, *Shannon*, 379 F. Supp. at 801 (citing McKee v. Harris-Seybold Co., 264 A.2d 98, 103-05 (N.J. Super. Ct. Law Div. 1970)); Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1106-07 (Ill. App. Ct. 1982); *Turner*, 244 N.W.2d at 879 (citing *Shannon*, 379 F. Supp. at 801). Other jurisdictions, however, emphasize only some of the factors or some aspects of one or more factors. *See infra* note 88.

82. The "continuation of the enterprise" factor seems to have caused some blurring of the distinctions between the "mere continuation" exception and the de facto merger doctrine, since it is a requirement under both theories. For instance, courts and commentators are in disagreement as to the classification or basis of the decision in *Turner v. Bituminous Casualty Co.*, 244 N.W.2d 873 (Mich. 1976). *Compare* Schumacher v. Richards Shear Co., 451 N.E.2d 195, 198 (N.Y. 1983)(continuity of enterprise) *and* Jones v. Johnson Mach. and Press Co., 320 N.W.2d 481, 484 (Neb. 1982)(continuity of enterprise) *and* Pelc v. Bendix Mach. Tool Corp., 314 N.W.2d 614, 618 (Mich. Ct. App. 1981)(continuity of enterprise) *and* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 449 & n.66 (1982)(mere continuation exception) *with Manh Hung Nguyen*, 433 N.E.2d at 1107 (de facto merger) *and Turner*, 244 N.W.2d at 888 (Coleman, J., dissenting)(majority found de facto merger) *and* Note, *Products Liability—Successor Corporations—Liability for Defects in Predecessor's Products*, 33 U. KAN. L. REV. 791, 796 (1985)(de facto merger).

83. *E.g.*, Travis v. Harris Corp., 565 F.2d 443, 447 (7th Cir. 1977)(considering retention of employees and managers); *Jacobs*, 512 F. Supp. at 181 (no liability under de facto merger where officers and employees not made available to purchasing corporation); Bazan v. Kux Mach. Co., 358 F. Supp. 1250, 1252 (E.D. Wis. 1973)(no liability because no commonality of

shareholders.[84] This is usually the case when the purchasing corporation pays for the assets of the other company with its own stock,[85] resulting in the predecessor's shareholders becoming owners of the successor corporation.[86] Thirdly, there must be a dissolution of the predecessor as soon as legally and practically possible after the "sale" of its assets.[87] Fourthly, the successor must assume those liabilities and obligations of the predecessor as are needed to ensure a normal, uninterrupted continuation of the business.[88] The presence of these

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executives, management personnel, or officers); Kloberdanz v. Joy Mfg., 288 F. Supp. 817, 822 (D. Colo. 1968)(de facto merger requires "mixture" of shareholders and officers).

84. *See, e.g.*, Leannais v. Cincinnati, Inc., 565 F.2d 437, 439-40 (7th Cir. 1977)(no de facto merger unless purchaser corporation makes payment in stock); *Kloberdanz*, 288 F. Supp. at 822 (de facto merger requires "mixture" of shareholders and officers of selling and purchasing corporations); *Manh Hung Nguyen*, 433 N.E.2d at 1111 (shareholder continuity most important element of de facto merger); Tift v. Forage King Indus., 322 N.W.2d 14, 21 (Wis. 1982)(de facto merger requires that selling corporation's shareholders receive shares of purchaser's stock).

85. Jacobs v. Lakewood Aircraft Serv., 512 F. Supp. 176, 181 (E.D. Pa. 1981)(no de facto merger unless purchasing corporation pays with its own stock); Armour-Dial, Inc. v. Alkar Eng'g Corp., 469 F. Supp. 1198, 1201 (E.D. Wis. 1979)(de facto merger found only if consideration given for seller's assets is shares of purchaser's stock). However, whether the consideration is to be entirely of stock is not clear. *Compare* Ray v. Alad Corp., 560 P.2d 3, 7 (Cal. 1977)(transaction de facto merger where entire consideration is shares of buying corporation's stock) *with* Wilson v. Fare Well Corp., 356 A.2d 458, 466 (N.J. Super. Ct. Law Div. 1976)(de facto merger upheld even though successor purchased predecessor's assets with both cash and stock).

86. Once the stock transfer is made, the stockholders of the selling corporation, or predecessor, become owners or shareholders of the new corporation. *See Travis*, 565 F.2d at 447 (no continuity of shareholder interests without stock transfer); *Turner*, 244 N.W.2d at 890 (Coleman, J., dissenting)(stock transfers create continuity of shareholder interest from selling company to purchasing company).

87. *See, e.g.*, Shannon v. Samuel Langston Co., 379 F. Supp. 797, 801 (W.D. Mich. 1974) (merger requires absorption and "practically contemporaneous" dissolution of acquired entity) (citing McKee v. Harris-Seybold Co., 264 A.2d 98, 103 (N.J. Super. Ct. Law Div. 1970)); *Bazan*, 358 F. Supp. at 1252 (selling corporation's dissolution after ten months not immediate enough for de factor merger); Schumacher v. Richards Shear Co., 451 N.E.2d 195, 198 (N.Y. 1983)(successor corporation not liable under corporate law exceptions where predecessor survived the purchase but discontinued operations). *But see Ray*, 560 P.2d at 6-7 (dissolution of predecessor one month following purchase apparently insignificant factor in considering de factor merger). Courts have also found that where a predecessor was in the process of foreclosure or liquidation prior to the assets sale, the buying corporation is not liable for the obligations of the sellers. *E.g.*, Comstock v. Great Lakes Distrib. Co., 496 P.2d 1308, 1312-13 (Kan. 1972); Pelc v. Bendix Mach. Tool Corp., 314 N.W.2d 614, 618-19 (Mich. Ct. App. 1981).

88. Menacho v. Adamson United Co., 420 F. Supp. 128, 133 (D.N.J. 1976); *Shannon*, 379 F. Supp. at 801 (citing *McKee*, 264 A.2d at 103-05); Freeman v. White Way Sign & Maintenance Co., 403 N.E.2d 495, 502 (Ill. App. Ct. 1980)(citing Hernandez v. Johnson Press Corp., 388 N.E.2d 778, 780 (Ill. App. Ct. 1979)); *Pelc*, 314 N.W.2d at 618 (enumerating list of elements in *Turner*, 244 N.W.2d at 879, but characterizing *Turner* decision as based on mere

four factors in a sale of assets may lead to a finding of de facto merger for purposes of product liability.[89] The absence of any one element can be fatal to a plaintiff's case,[90] with the result that the injured individual, such as the one in our hypothetical scenario, is left without a remedy.

These principles are well exemplified in *Shannon v. Samuel Langston Company*.[91] In that case, the plaintiff, Shannon, was injured on the job in 1967 by a machine that had been manufactured by the Samuel M. Langston Company.[92] In 1966, a corporation called Harris Intertype Corporation had purchased all of the assets as well as the name of The Langston Company,[93] paying for the transfer entirely with its own stock.[94] The federal district court found that all elements of a de facto merger were present in this "purchase" and held that the successor was liable for the injuries caused by the defective product placed into the stream of commerce by the predecessor.[95] First, the court determined that the general business operation of the

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continuation theory). Assuming such obligations is another indication of an intent to continue the enterprise without pause. *See Shannon*, 379 F. Supp. at 801 n.1. Some courts (most notably those of California) have failed to consider this factor in discussions of de facto merger, perhaps because it is unnecessary to do so in the absence of other elements. *See, e.g.*, *Jacobs*, 512 F. Supp. at 180-81 (assumption of obligations in de facto merger context not discussed where continutiy of enterprise and shareholders and immediate dissolution of predecessor absent)(applying California law); Kloberdanz v. Joy Mfg., 288 F. Supp. 817, 820 (D. Colo. 1968)(de facto merger criteria not satisfied in absence of common officers and where separate entities existed after transfer) (applying California law); *Ray*, 560 P.2d at 7 (only element of de facto merger mentioned concerned inadequate consideration or stock as consideration); Ortiz v. South Bend Lathe, 120 Cal. Rptr. 556, 558 (Cal. Ct. App. 1975)(de facto merger not found in absence of common officers and where separate entities existed after transfer).

89. *E.g.*, Knapp v. North Am. Rockwell Corp., 506 F.2d 361, 369 (3rd Cir. 1974), *cert. denied*, 421 U.S. 965 (1975); *Shannon*, 379 F. Supp. at 801.

90. *See, e.g.*, Travis v. Harris Corp., 565 F.2d 443, 447 (7th Cir. 1977)(transaction not merger absent continuity of shareholders); Leannais v. Cincinnati, Inc., 565 F.2d 437, 439 (7th Cir. 1977)(where payment not in stock, de facto merger elements not satisfied); Lamb v. Leroy Corp., 454 P.2d 24, 26 (Nev. 1969)(no de facto merger where both companies maintained separate identities). *But see* Long John Silver's Inc. v. Architectural Eng'g Prods. Co., 520 F. Supp. 753, 758-59 (W.D. Pa. 1981)(while dissolution of predecessor is required, continuity of business enterprise may not be). "Not all of these factors are needed to demonstrate a merger; rather, these factors are only indicators that tend to show a de facto merger." Menacho v. Adamson United Co., 420 F. Supp. 128, 133 (D.N.J. 1976).

91. 379 F. Supp. 797 (W.D. Mich. 1974).

92. *See id.* at 798 (employee lost left arm while working with cardboard printer-slotter).

93. *Id.* at 799.

94. *See id.* at 799, 801 (Harris stock used to satisfy predecessor's debts and distributed to predecessor's shareholders).

95. *See id.* at 801-03.

purchased entity had continued in the same location with the same personnel, and had been operated under the same management.[96] Also, the Harris Intertype stock used to purchase the Langston assets had been distributed to Langston's shareholders after the company's debts had been satisfied. This created a continuity of ownership.[97] The third element was also present in that the predecessor changed its name and discontinued ordinary business operations soon after the sale.[98] Finally, the court found that Harris Intertype had expressly assumed all of Langston's debts necessary to continue the normal uninterrupted cycle of business operations.[99] On these facts, the court reasoned that Harris Intertype had received all of the benefits of a going concern and should therefore also assume its ordinary costs.[100] These costs included liability for damages caused by defective products placed into the stream of commerce by the predecessor.[101] Moreover, the court noted that the successor had "deliberately evaded" statutory merger requirements by shaping the acquisition as a purchase of assets,[102] and that avoiding liability by manipulation of corporate entities was against public policy.[103] This case presents an example of a de facto merger pure and simple. The facts and circumstances presented a "perfect" opportunity for the court's imposition of the fourth exception to the traditional corporate rule of successor non-liability.

Two years after the *Shannon* decision, however, the Michigan Supreme Court expanded the de facto merger doctrine as it applied to products liability actions by eliminating an element which previously had been regarded as essential: In *Turner v. Bituminous Casualty Company*,[104] the court dispensed with the requirement of an exchange of stock.[105] Instead, the court determined that the basic continuity of

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96. *See id.* at 801.

97. *See id.*

98. *See id.* at 799, 801.

99. *Id.* at 801.

100. *Id.* at 802.

101. *See id.* (sales price includes projected products liability insurance premiums).

102. *Id.*

103. *See id.* at 802-03 ("enlightened social policy" not contrary to "favorable corporate climate").

104. 244 N.W.2d 873 (Mich. 1976).

105. *See id.* at 880 (absence of stock as consideration not dispositive); *see also id.* at 883 (cash payment rather than stock transfer mere difference in degree).

the enterprise should be the determining factor.[106] In that case, the plaintiff Turner, like Shannon, was injured on the job by a machine whose manufacturer had been acquired by Harris Intertype Corporation.[107] The purchase agreement and circumstances were also substantially the same as those in *Shannon*.[108] There was, however, one major difference. In *Turner*, Harris had acquired the company for cash instead of stock.[109] As previously noted, the traditional position has been that a de factor merger may not be found without a transfer of stock. The *Turner* court, however, found the absence of an exchange of stock inconclusive.[110] The majority decided that where other circumstances showing a continuity of the enterprise are so pervasive as to dominate the transaction, the form of payment should have no effect on the successor's tort liability.[111] To the injured plaintiff, technical distinctions as to the form of acquisition are meaningless;[112] the more cogent inquiry is whether the successor held itself out to the public as a continuing enterprise.[113] Accordingly, the *Turner* court stated that even absent an exchange of stock, a successor should be held liable for the predecessor's defective products where the purchasing corporation held itself out as a continuing enterprise and where other elements of de facto merger are present.[114]

Shannon and *Turner* offer ample authority for the proposition that when confronted with a transfer of assets that is alleged to be a sales/purchase agreement, some courts will now look to a variety of factors in determining whether a de facto merger should be imposed. Some of the most important of these factors are the continuity of the enterprise, the rapid dissolution of the predecessor, the assumption of debts necessary to continue uninterrupted operations, and whether the successor has held itself out as a continuing concern. Moreover,

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106. *See id.* at 882 ("continuity is the watch word").

107. *See id.* at 875 (plaintiff's hands amputated as result of injury from power press manufactured by T.W. & G.B. Sheridan Co.).

108. *See generally id.* at 875-76 (summarizing terms of purchase agreement).

109. *See id.* at 876 (consideration was $6.38 million).

110. *See id.* at 880. Noting that the actual shareowners at the time the product was manufactured are likely not the same shareowners as at the time of the corporation's sale, the court stated that "continuity" of shareholders is more theoretical than real. *Id.*

111. *See id.* at 882 (justice offended if liability avoided where business property, operations, policy, and personnel continuous).

112. *See id.* at 878.

113. *See id.* at 882 (corporation must be successor for both sales and liabilities).

114. *See id.* at 883-84.

both *Turner* and *Shannon* reflect a growing emphasis on the public policy supporting strict products liability law[115] and its insistence on compensation of injured plaintiffs. The court in each decision noted that traditional corporate law principles governing successor liability were originally designed to protect creditors, shareholders, and corporate entities,[116] but that these general non-liability principles could also be manipulated so as to cut off any available remedy for the product liability plaintiff.[117] This conundrum, however, has had positive results. It was instrumental in bringing about the newest exception to the corporate law rule of successor non-liability, the product line exception.

III. Product Line Liability: The "New" Exception

The mere continuation rule, the third exception to the corporate law rule of successor non-liability discussed above[118] and enunciated in *Cyr v. B. Offen & Company*,[119] was further extended by the Supreme Court of California in *Ray v. Alad Corporation*.[120] *Ray* is the seminal case in which the "product line" exception was formulated and stands for the proposition that in some cases liability should be imposed upon a successor corporation for a defective product sold by the predecessor.[121] This exception focuses not upon whether the existing company is a mere continuation of the former one, but instead upon whether the predecessor's actual product line has been continued.[122] In other words, this exception differs from the mere continuation rule by focusing specifically upon the continuation of the product instead of upon the continuity of the business.

In *Ray*, the plaintiff was injured when he fell from a defective ladder which had been manufactured by the Alad Corporation (Alad

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115. *See id.* at 877-79; 882-83 (discussing evolution of products liability law in legislatiure and courts); *see also* Shannon v. Samuel Langston Co., 379 F. Supp. 797, 802-03 (W.D. Mich. 1974)(analyzing social and economic policies).

116. *See* Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 878 (Mich. 1976); *see also* *Shannon*, 379 F. Supp. at 802.

117. *Cf. Turner*, 244 N.W.2d at 882-83 (corporation may employ piecemeal divestiture to escape liability); *Shannon*, 379 F. Supp. at 802-03 (corporation may attempt to avoid liability by "shuffling paper").

118. *See supra* text accompanying notes 48-53.

119. 501 F.2d 1145 (1st Cir. 1974); *see also supra* text accompanying notes 54-68.

120. 560 P.2d 3, 7-8 (Cal. 1977)(discussing limitations of mere continuation exception).

121. *See id.* at 11.

122. *See id.* at 10-11; *see also* Ramirez v. Amsted Indus., 431 A.2d 811, 822 (N.J. 1981).

I).[123] Prior to the damaging event, however, Alad I had sold all of its assets to the Lighting Maintenance Corporation (Alad II) and subsequently dissolved as a business entity.[124] In accordance with their purchase plan, Alad II had continued to manufacture and place into the stream of commerce the identical ladders, using the original "Alad" trade name.[125] The injured plaintiff filed suit, seeking to impose strict tort liability upon the successor corporation.[126] Analyzing the facts and applying the law under the traditional corporate law rule, the trial court granted Alad II's motion for summary judgment.[127]

On appeal, the California Supreme Court reversed the trial court's judgment.[128] In reaching this decision, the court first examined the rationale underlying the general corporate law rule of successor non-liability[129] and proceeded to give an extensive analysis of the prior case law.[130] The court's conclusion was that none of the four traditional exceptions applied to the particular transaction in this case.[131] In addition, the court concluded that it was not prepared to expand these existing theories, nor did the court find that an additional *corporate law* exception was warranted.[132] Instead, the court decided to abandon the traditional approach in favor of a products liability analysis.[133] Examining prior cases, including the landmark decision of *Greenman v. Yuba Power Products*,[134] the court determined that policy considerations supporting products liability for manufacturers and sellers were equally applicable to successor corporations.[135] Conse-

123. *See Ray*, 560 P.2d at 5 (plaintiff fell from ladder during course of employment).

124. *See id.* at 5-6. Alad I sold all its assets, including the manufacturing plant, machinery, raw materials, semi-finished goods, and office fixtures to Alad II. *See id.*

125. *See id.* at 6.

126. *See id.* at 4.

127. *See id.* at 5 (successor had not manufactured ladder); *see also infra* text accompanying notes 129-31.

128. *See* Ray v. Alad Corp., 560 P.2d 3, 11 (Cal. 1977).

129. *See generally id.* at 7-8.

130. *See generally id.* at 7-9.

131. *Id.* at 8.

132. *See id.*

133. *See id.* at 8 (policies supporting strict tort liability may justify exception to corporate law of successor non-liability).

134. 377 P.2d 897 (Cal. 1963)(landmark case recognizing strict products liability cause of action).

135. *See* Ray v. Alad Corp., 560 P.2d 3, 8 (Cal. 1977). The court reasoned that "the protection of otherwise defenseless victims of manufacturing defects and the spreading

quently, a new exception *based upon principles of tort* rather than corporate law was appropriate. The court then held that "a party which acquires a manufacturing business and continues the output of its line of products . . . assumes strict tort liability for defects . . . of the same product line previously manufactured and distributed by the entity from which the business was acquired."[136] The court reasoned:

> Justification for imposing strict liability upon a *successor* to a manufacturer under the circumstances here presented rests upon (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 business.[137]

Like the *Shannon* decision discussed above,[138] *Ray* placed great emphasis on the "good will" justification, stating:

> Finally, the imposition upon Alad II of liability for injuries from Alad I's defective products is fair and equitable in view of Alad II's acquisition of Alad I's trade name, good will, and customer lists, its continuing to produce the same line of ladders, and its holding itself out to potential customers as the same enterprise. This deliberate albeit legitimate exploitation of Alad I's established reputation as a going concern manufacturing a specific product line gave Alad II a substantial benefit which its predecessor could not have enjoyed without the burden of potential liability for injuries from previously manufactured units. Imposing this liability upon successor manufacturers in the position of Alad II not only causes the 'one who takes the benefit [to] bear the burden . . .' but precludes any windfall to the predecessor that might otherwise result from (1) the reflection of an absence of such successor liability in an enhanced price paid by the successor for the business assets and (2) the liquidation of the predecessor resulting in avoidance of its responsibility for subsequent injuries from its defective products.[139]

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throughout society of the cost of compensating them" properly justifies successor liability. *Id.* (quoting Price v. Shell Oil Co., 466 P.2d 722, 725-26 (Cal. 1970)(en banc)).

136. *Id.* at 11.

137. *Id.* at 8-9 (emphasis in original).

138. *See* Shannon v. Samuel Langston Co., 379 F. Supp. 797 (W.D. Mich. 1974); *see also supra* text accompanying notes 91-103.

139. *See Ray*, 560 P.2d at 10-11 (citations omitted). The exception enunciated in *Ray* was expanded a step further in *Rawlings v. D.M. Oliver, Inc.*, 159 Cal. Rptr. 119 (Cal. Ct. App.

The "new" exception was born. Since *Ray*, the product line exception has become well established in California, but has not yet been widely accepted by other jurisdictions.[140] In 1981, the product line exception was adopted by the courts of Pennsylvania and New Jersey.[141] Both tribunals suggested that the new theory, founded upon the policies supporting strict products liability,[142] was preferable to a judicial expansion of the traditional corporate law exceptions.[143] When adopting the exception, the Pennsylvania court also expanded the significant factors that should be examined in applying the exception to a particular set of facts.[144] At least two other jurisdictions, Washington and New York, have implicitly supported this new exception, but have not yet adopted it.[145] The Washington Supreme Court, while recognizing the product line exception as being consistent with Washington law, was reluctant to adopt the new theory under inappropriate circumstances.[146] Similarly, the New York Court of Appeals evinced some degree of approval of the exception's

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1979). In *Rawlings*, the court imposed successor corporation liability despite the fact that the successor did not continue to manufacture the identical product. *See id.* at 124. The court stated that "where one takes the benefit one ordinarily should bear the burden" and, furthermore, "unlike plaintiff, [the successor] was in a position to protect itself from loss by expressly providing for that risk in the bargain it made with [the] sellers." *Id.*

140. *See* Sell, *Successor Corporation's Liability for Defective Products of Its Transferor—The Product Line Exception*, 4 J.L. & COM. 65, 71 n.29 (1984). The courts of Alabama, Florida, Illinois, Indiana, Michigan, Nebraska, Ohio, and Wisconsin, among others, have rejected the product line exception. *Id.*

141. *See* Ramirez v. Amsted Indus., 431 A.2d 811, 825 (N.J. 1981); Dawejko v. Jorgensen Steel Co., 434 A.2d 106, 110 (Pa. Super. Ct. 1981); *see also* Nieves v. Bruno Sherman Corp., 431 A.2d 826, 830 (N.J. 1981)(companion case to *Ramirez* which also adopted product line exception).

142. *See Dawejko*, 434 A.2d at 111 (citing *Ramirez*, 431 A.2d at 825).

143. *See id.*; *see also Ramirez*, 431 A.2d at 819 (focus should be continuity of manufacturing operation rather than continuity of ownership and management).

144. *See Dawejko*, 434 A.2d at 111 (combining the *Cyr, Turner, Knapp*, and *Ray* requirements). The court determined that the following factors were significant to its imposition of product line liability:

> whether the successor corporation advertised itself as an ongoing enterprise; or whether it maintained the same product, name, personnel, property, and clients; or whether it acquired the predecessor corporation's name and good will, and required the predecessor to dissolve.

Id. (citations omitted). The court further noted that whether the *Ray* three-part test was met would be a consideration. *Id.*

145. *See* Schumacher v. Richards Shear Co., 451 N.E.2d 195, 198 (N.Y. 1983); Meisel v. M & N Modern Hydraulic Press Co., 645 P.2d 689, 692 n.1 (Wash. 1982)(rule of *Ray* salutary).

146. *See Meisel*, 645 P.2d at 692 n.1.

underlying policy rationale but declined to adopt it.[147] Finally, as noted above,[148] the Supreme Court of Michigan emulated *Ray*'s product liability rationale in *Turner v. Bituminous Casualty Co.*,[149] but, instead of adopting the product line exception, chose to expand the de facto merger exception.[150] In no way can these examples of recognition of the product line exception be designated as overwhelming.[151] Yet, both the very definite advantages as well as the negative aspects of this theory should be considered.

IV. Product Line Liability: "Pros and Cons"

The difficulty encountered by courts in determining whether or not to impose product line liability is that they are analyzing and balancing two competing policy goals from two separate and distinct bodies of law.[152] The corporate common law on the one side seeks to ensure the orderly transfer of assets in a market economy,[153] while the tort law on the other seeks to compensate the injured victim of a damaging event.[154] In other words, the courts are confronted with a classic ex-

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147. *See Schumacher*, 451 N.E.2d at 198 (N.Y. 1983)("We do not adopt the rule of [*Ray*] but note that [it is] factually distinguishable in any event.").

148. *See supra* text accompanying notes 104-14.

149. 244 N.W.2d 873 (Mich. 1976).

150. *See id.* at 883. The *Turner* court cited *Ray*'s application of tort law with approval, but made no comment as to the adoption of the product line exception. *See id.* at 879 n.4, 882 (*Ray* part of trend toward finding successor liability).

151. *See, e.g.*, Tucker v. Paxson Mach. Co., 645 F.2d 620, 625 (8th Cir. 1981)(product line liability not part of Missouri law); Travis v. Harris Corp., 565 F.2d 443, 448 (7th Cir. 1977)(neither Indiana nor Ohio follow successor liability); Mudgett v. Paxson Mach. Co., 709 S.W.2d 755, 759 (Tex. App.—Corpus Christi 1986, writ ref'd n.r.e.)(adopting product line theory a legislative choice); Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 292 (Tex. App.—Austin 1985, writ ref'd n.r.e.)(judicial restraint appropriate in considering such a radical theory); *see also* Sell, *Successor Corporation's Liability for Defective Products of Its Transferor—The Product Line Exception*, 4 J.L. & Com. 65, 71 (1984)(thirteen states have considered product line liability, two have adopted such theory, two have left the issue unresolved, nine have rejected the theory).

152. A number of legal writers have addressed the issue of conflict between corporate and product liability law. *See generally* Fegan, *Successor Corporations and Strict Liability in Tort—A Convergence of Two Opposing Doctrines*, 69 Ill. B.J. 142 (1980); Note, *Continued Expansion of Corporation Successor Liability in the Products Liability Arena*, 58 Chi.-Kent L. Rev. 1117, 1117-21 (1982); Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 Ohio St. L.J. 441, 446-47 (1982).

153. *See* Kadens, *Practitioner's Guide to Treatment of Seller's Products Liabilities in Assets Acquisitions*, 10 Toledo L. Rev. 1, 4 & n.5 (1978)(successor non-liability matter of "economic utility").

154. *See* W. Keeton, D. Dobbs, R. Keeton, & D. Owen, Prosser and Keeton on the Law of Torts § 1, at 6 (5th ed. 1984).

ample of adding up apples and oranges. It is for this reason that the courts should carefully analyze the relative strengths and weaknesses of the arguments both for and against adoption of this new theory. The courts imposing product line liability and those courts rejecting such liability have advanced numerous legal and policy arguments to support their respective positions.[155] They nevertheless follow similar patterns of reasoning.

A. *Product Liability Analysis: Pro*

The major, and perhaps the strongest, argument in support of the product line exception was advanced in the *Ray* decision. The California court, always a pioneer in the field of strict products liability,[156] reasoned that a plaintiff is entitled to seek compensation from a successor corporation because he has no remedy against the dissolved predecessor.[157] As we have seen, corporate law imposes no duty upon a dissolved corporation to provide for future product liability claims. The result of this rule is that the cost of a defective product is shifted totally to the injured plaintiff.[158] The transferring of economic bur-

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155. *See, e.g.*, Andrews v. John E. Smith's Sons Co., 369 So. 2d 731, 785 (Ala. 1977); Pelc v. Bendix Mach. Tool Corp., 314 N.W.2d 614, 620 (Mich. Ct. App. 1981)(Alabama and Michigan reject product line theory because each state bases product liability recovery on negligence, not strict liability theory). Some courts reject the product line theory because it holds companies liable for defective products which they did not manufacture. *See* Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1108-09 (Ill. App. Ct. 1982); Jones v. Johnson Mach. and Press Co., 320 N.W.2d 481, 484 (Neb. 1982). Similarly, other courts reject the product line exception because the successor corporation was not in a position to eliminate the risk of injury, and such liability would defeat one policy consideration supporting strict products liability—modification of the manufacturer's behavior. *See* Bernard v. Kee Mfg., 409 So. 2d 1047, 1050 (Fla. 1982)(court also apprehensive about impact of product line liability on small business, particularly regarding insurability against such liability). One federal court, interpreting Texas law, concluded that product line liability was too radical a departure from Texas products liability law. *See* Rhynes v. Branick Mfg. Corp., 629 F.2d 409, 410 (5th Cir. 1980); *see also* Mudgett v. Paxson Mach. Co., 709 S.W.2d 755, 759 (Tex. App.—Corpus Christi 1986, writ ref'd n.r.e.)(decision whether to adopt product line exception proper for legislature, not judiciary).

156. The California Supreme Court was the first to impose strict products liability in *Greenman v. Yuba Power Products*, 377 P.2d 897 (Cal. 1963). This decision was made the year before the American Law Institute adopted the concept of strict products liability in section 402A of the Restatement of Torts. *See* W. KEETON, D. DOBBS, R. KEETON, & D. OWEN, PROSSER AND KEETON ON THE LAW OF TORTS § 98, at 694 (5th ed. 1984).

157. *See* Ray v. Alad Corp., 560 P.2d 3, 9 (Cal. 1977).

158. *See id.* at 10; *see also* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 601 (1977)(injured person without adequate remedy under traditional rule).

dens to the injured victim not only violates fundamental doctrines of tort law,[159] but also contradicts one of the fundamental precepts of strict products liability.[160]

Traditionally, another major goal of strict products liability law has been to spread the cost of the individual plaintiff's injury to the entire group of consumers.[161] A purchasing corporation could accomplish this by obtaining liability insurance to cover contingent liability for any defective products placed into the stream of commerce by the predecessor.[162] By simply adjusting the purchase price of the assets downward to reflect the cost of such insurance, the purchasing corporation would shift a portion of the burden of insurance costs onto the business entity now dissolved.[163] As such, an equitable distribution of costs between both corporations would be achieved, and one of the reasons for imposing strict products liability[164] would be satisfied.

Three other basic policy considerations also support a products liability analogy. First, concerns for public health and safety demand that the law accommodate society by compensating plaintiffs injured

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159. *See generally* W. KEETON, D. DOBBS, R. KEETON, & D. OWEN, PROSSER AND KEETON ON THE LAW OF TORTS § 1, at 6 (5th ed. 1984)(discussing tort principles).

160. *See* Greenman v. Yuba Power Prods., 377 P.2d 897, 901 (Cal. 1963)(purpose of strict tort liability is to ensure that cost of injuries resulting from defective product borne by manufacturers rather than "powerless" injured person); *see also* McKisson v. Sales Affiliates, 416 S.W.2d 787, 789 (Tex. 1967)(adopting RESTATEMENT (SECOND) OF TORTS § 402A (1965)).

161. *See* Escola v. Coca Cola Bottling Co., 150 P.2d 436, 441 (Cal. 1944)(Traynor, J., concurring)(manufacturer should insure against costs of injuries caused by defective products as cost of doing business).

162. Some courts imposing liability on successor corporations have presumed the successors' ability to insure against loss. *See, e.g.*, Cyr v. B. Offen & Co., 501 F.2d 1145, 1154 (1st Cir. 1974)("hazards of insuring for risk better borne by manufacturer than consumer); Shannon v. Samuel Langston Co., 379 F. Supp. 797, 802 (W.D. Mich. 1974)(in practice, acquiring corporation continues predecessor's insurance); Ray v. Alad Corp., 560 P.2d 3, 9 (Cal. 1977)(Alad II's capacity to insure same as Alad I's). *But see* Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1111 (Ill. App. Ct. 1982)(cannot assume availability of product liability insurance).

163. Some commentators have suggested the alternative of requiring the seller to indemnify the buyer for future product liability claims. *E.g.*, Heitland, *Survival of Products Liability Claims in Assets Acquisitions*, 34 BUS. LAW. 489, 498 (1979). This can be accomplished by placing a portion of the purchase price into an interest-bearing escrow account as security. *Id.*; *see also* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 458-59 (1982)(discussing disadvantages of escrow accounts).

164. *See* RESTATEMENT (SECOND) OF TORTS § 402A comment a (1965)(putting product in stream of commerce implies special responsibility to consuming public).

by unreasonably dangerous products.[165] Second, the risk of injury should be placed on the business entity because, whether the product is defective or not, it is the corporation that profits from the sale.[166] Third, the entity placing a product into the stream of commerce, rather than the injured plaintiff, is in a better position to discover and correct potential defects.[167]

Judicial emphasis on public safety encourages manufacturers to improve the quality and safety of their goods. Having the threat of strict products liability over them provides companies with an incentive to invest more in safety research and in quality control of their production.[168] The ultimate result is that fewer defective and unsafe products will be placed into the stream of commerce.[169] These broad concerns of public policy stressing health and safety should not be diminished simply because one manufacturer has transferred its operation to another going concern. The bottom line for proponents of the product line exception is that health and safety goals are best served by imposing the same strict liability standards on a successor corporation as would have been imposed upon its predecessor.[170]

A second products liability policy argument is based on the fact that the sale of a product earns a profit for the manufacturer. Since strict products liability seeks to shift the cost of injuries caused by

165. *See* Note, *Expanding the Products Liability of Successor Corporations*, 27 HASTINGS L.J. 1305, 1323 (1976).

166. *See id.* (corporation enjoying commercial advantage should bear losses as cost of business).

167. *See* Note, *Continued Expansion of Corporate Successor Liability in the Products Liability Arena*, 58 CHI.-KENT L. REV. 1117, 1127 (1982)(manufacturer best able to prevent risks).

168. Codling v. Paglia, 298 N.E.2d 622, 628 (N.Y. 1973); Ellithorpe v. Ford Motor Co., 503 S.W.2d 516, 521 (Tenn. 1973); *see also* O. HOLMES, THE COMMON LAW 117 (1881)("safest way to secure care is to throw the risk upon the person who decides what precautions shall be taken"); *cf.* Escola v. Coca Cola Bottling Co., 150 P.2d 436, 441 (Cal. 1944)(Traynor, J., concurring)("It is to the public interest to discourage the marketing of products having defects that are a menace to the public.").

169. A basic policy justification for strict products liability is its deterrent effect. Two arguments against this view are that (1) liability based on negligence is an equally effective deterrent, and (2) strict liability will discourage experimentation with new products. *See* W. KEETON, D. DOBBS, R. KEETON, & D. OWEN, PROSSER AND KEETON ON THE LAW OF TORTS § 98, at 693 (5th ed. 1984).

170. One author has advised acquiring corporations to "attempt to discover the extent of danger created by the [predecessor's] products . . ." and to advise past buyers of those hazards in order to protect themselves against future liability. Heitland, *Survival of Products Liability Claims in Assets Acquisitions*, 34 BUS. LAW. 489, 498 (1979). The fact that legal advisors are giving such advice seems to provide some support for the deterrent theory.

defective products to those parties that economically benefit from the product's sale, the maker and seller should bear the burden of a product's attendant risks.[171] Moreover, a successor corporation which continues to produce and market the identical product, using the same trade name or trademark, realizes a benefit in the form of "good will" and reputation generated from prior sales.[172] New sales are generated for the succeeding company in part because consumers recognize the trade name as that of a reliable, quality product. A successor corporation likely will attempt to capitalize on that reputation by holding itself out as a continuing enterprise having all of the knowledge and expertise of the predecessor.[173] A purchasing corporation in many cases deliberately and meticulously creates the impression of an on-going business, and consumers are unaware of any changes in corporate ownership. From the consumer's perspective, there is no difference in either product or manufacturer.[174] This perception works to the advantage of the current manufacturer, who enjoys more sales and more profits because of consumers' continuing reliance on the reputation of the product.[175] Advocates of the product line exception contend that the benefit thus derived justifies placing the corresponding burden of liability on the succeeding entity.[176] The same rationale which supports the imposition of strict products liability on the manufacturer who gleans profits from the sale also supports the imposition of product line liability on the successor corporation.[177] If one has made a profit, he should bear the cost of injuries caused by the product.

The third justification for a products liability analysis is that the

171. *See* Greenman v. Yuba Power Prods., 377 P.2d 897, 901 (Cal. 1963).

172. *E.g.*, Shannon v. Samuel Langston Co., 379 F. Supp. 797, 802 (W.D.Mich. 1974); Ray v. Alad Corp., 560 P.2d 3, 10, 11 (Cal. 1977); Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 882 (Mich. 1976).

173. *See* Cyr v. B. Offen & Co., 501 F.2d 1145, 1151-53 (1st Cir. 1974)(successor exploits good will accumulated by past sales of products).

174. *See id.* at 1152.

175. *See Turner*, 244 N.W.2d at 882 (general discussion of business and sales advantages of continuity of enterprise).

176. *See* Hill, *Products Liability of A Successor Corporation—Acquisition of "Bad Will" with Good Will*, 32 DEF. L.J. 55, 59-60 (1983)(citing *Ray*, 560 P.2d at 10-11).

177. This conclusion is founded on the view that one who voluntarily places himself in the shoes of a predecessor should accept the burdens as well as the benefits of the transaction, and is as capable as the predecessor of protecting against unreasonable claims. *See Ray*, 560 P.2d at 10; Ramirez v. Amsted Indus., 431 A.2d 811, 816 (N.J. 1981); Dawejko v. Jorgensen Steel Co., 434 A.2d 106, 108 (Pa. Super. Ct. 1981)(citing *Cyr*, 501 F.2d at 1154).

manufacturer is in the best position to discover potential defects.[178] The manufacturer is also in the best position to estimate the product's cost and, if the product does cause injury, to shift and spread the burden of this damaging event among all consumers.[179] The same inferences apply to a successor corporation: Having voluntarily placed itself in the same position as the predecessor, the successor should have the same ability not only to discover defects but also to estimate costs and shift the burden of injuries to the consuming public.[180] The successor also should be capable of economically protecting itself from any contingent liability attributable to the predecessor's product.[181]

B. *Product Liability Analysis: Con*

While its advocates argue that product line liability is merely a logical extension of the law of strict products liability, its opponents contend that the underlying policy goals are impracticable and unworkable in the realm of corporate acquisitions.[182] For example, a principle argument against holding a successor corporation liable for injuries caused by its predecessor's defective products is that such liability restricts the free availability and transferability of corporate assets.[183] Critics of product line liability complain that accurately predicting the extent of future claims resulting from defective products already placed into the stream of commerce is virtually impossible[184] and prevents a reasonable determination of a purchase price for

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178. Escola v. Coca Cola Bottling Co., 150 P.2d 436, 440-41 (Cal. 1944)(Traynor, J., concurring)(manufacturer can anticipate hazards); *see also* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 442-43 (1982)(often only manufacturer in position to detect defects)(citing Codling v. Paglia, 298 N.E.2d 622, 627 (N.Y. 1973)).

179. *See generally* W. KEETON, D. DOBBS, R. KEETON, & D. OWEN, PROSSER AND KEETON ON THE LAW OF TORTS § 98, at 692-93 (5th ed. 1984)(discussing "risk-bearing economic" theory).

180. *E.g.*, *Ray*, 560 P.2d at 10; *Ramirez*, 431 A.2d at 816; *Dawejko*, 434 A.2d at 108.

181. *See supra* text accompanying notes 161-63. *See generally* Heitland, *Survival of Products Liability Claims in Assets Acquisitions*, 34 BUS. LAW. 489, 497-99 (1979)(enumerating techniques to avoid successor liability); Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 458-60 (1982)(discussing methods of self-protection for successors).

182. *See generally* Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 458-61 (1982)(criticizing successor liability).

183. *Id.* at 458. *But see* Shannon v. Samuel Langston Co., 379 F. Supp. 797, 802 (W.D. Mich. 1974)(liability would not result in artificial restraints on corporate acquisitions).

184. *See* Note, Ray v. Alad Corporation: *Imposing Liability on the Successor Corporation*

the seller's business.[185] Predicting and guarding against future liability, however, is part of the regular conduct of business.[186] Predicting liability should be no less certain when one entity is acquiring the assets of another; if the predecessor was capable of estimating future liabilities, the successor should be equally competent.[187] Furthermore, the necessity of predicting this kind of potential loss has had no apparent effect in transactions where one corporation's assets are transferred to another corporation by means of a statutory merger or consolidation.[188] Since the difficulty of determining future claims resulting from defective products has had no effect on one type of corporate transfer, it should have no effect on a different type of transfer.[189] The alleged difficulty of calculating a suitable purchase price is apparently not great enough to impose serious limitations on the proposed transferability of corporate assets. Therefore, one of the major arguments against product line liability is defeated.

Arguing further against the product line exception, some courts and commentators contend that the corporate purchaser is entitled to the same protections as a bona fide purchaser of property.[190] These

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for the Defective Products of the Predecessor Corporation, 15 CAL. W.L. REV. 338, 357-58 (1979)(amount of contingent liabilities cannot be accurately determined in corporate negotiations).

185. *See* Recent Cases, *Strict Product Liability—Successor Corporations Are Strictly Liable in Tort for Defective Products Manufactured by Its Predecessor Corporation*, 18 SANTA CLARA L. REV. 556, 558 (1978)(Ray v. Alad Corp., 560 P.2d 3 (Cal. 1977) will require successor corporations to calculate cost of strict products liability in tort for predecessor's products when determining purchase price). At least one court has rejected the product line theory because it did not want corporate acquisitions to become "traps for unwary successor corporations." *See* Woody v. Combustion Eng'g, 463 F. Supp. 817, 821 (E.D. Tenn. 1978).

186. Any manufacturer must be able to calculate the probability of product liability. The predecessor would have had the "burden of potential liability" had it not sold its business. Ray v. Alad Corp., 560 P.2d 3, 10-11 (Cal. 1977). An opponent of successor liability stated this very simply: "Obviously, a corporation is subject to liability for defective products which it manufactures and sells itself, regardless of whether it is a predecessor or successor corporation." Jones v. Johnson Mach. & Press Co., 320 N.W.2d 481, 484 (Neb. 1982).

187. As noted in *Ray*, the successor has purchased from the predecessor the means and sources for determining liability. *Ray*, 560 P.2d at 10; *see also* Cyr v. B. Offen & Co., 501 F.2d 1145, 1154 (1st Cir. 1974)(where resources, employees, and facility identical, ability to predict should be identical).

188. *See* Turner v. Bituminous Casualty Co., 244 N.W.2d 873, 882-83 (Mich. 1976)(noting lack of logic in view that potential liability unmanageable in assets sales but not in mergers)(citing Chase v. Michigan Tel. Co., 80 N.W. 717, 719 (1899)).

189. *See id.* at 882.

190. *See, e.g.*, Kloberdanz v. Joy Mfg., 288 F. Supp. 817, 820-21 (D. Colo. 1968); Pierce v. Riverside Mortgage Sec. Co., 77 P.2d 226, 230-31 (Cal. Dist. Ct. App. 1938); American Ry. Express Co. v. Commonwealth, 228 S.W. 433, 437 (Ky. 1920); *see also* Comment, *The Exten-*

authorities assert, for example, that the purpose of the traditional corporate law rule was to provide security from unknown perils.[191] The concept of bona fide purchaser, however, historically was designed to protect the uninformed and unsophisticated buyer.[192] A business entity familiar with the intricacies of commercial transactions cannot be said to fall into this category. This is especially true since, in many instances, a transfer of assets is specifically structured to avoid liability for injuries caused by defective products already in the stream of commerce.[193] Therefore, the analogy fails to provide a basis for persuasive argument.

Another objection to the product line concept is that it is a major expansion of strict liability theory uncontemplated by the writers of the Restatement of Torts.[194] Section 402A,[195] for example, specifi-

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sion of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel, 10 LOY. L.A.L. REV. 584, 591 (1977); *cf.* Recent Cases, *Strict Product Liability—Successor Corporations Are Strictly Liable in Tort for Defective Products Manufactured by Its Predecessor Corporation,* 18 SANTA CLARA L. REV. 556, 558 (1978)(*Ray* should not extend to purchaser which continues trade name, but not product line). A corporate purchase is generally characterized as "bona fide" where the consideration is adequate to satisfy the seller's debts. *E.g.*, Jacobs v. Lakewood Aircraft Serv., 512 F. Supp. 176, 180 (E.D. Pa. 1981); *Kloberdanz*, 288 F. Supp. at 821 & n.2. A transferee must also be without notice of prior claims. Frankish v. Federal Mortgage Co., 87 P.2d 90, 97 (Cal. Dist. Ct. App. 1939). Under California law, the surviving corporation in a merger, for example, is presumed to have notice of creditors' claims, so that bona fide purchaser status in a merger context is impossible to achieve. Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel,* 10 LOY. L.A.L. REV. 584, 591-92 n.42 (1977)(citing Treadaway v. Camellia Convalescent Hosps., 118 Cal. Rptr. 341, 348 (Ct. App. 1974)). The rules of corporate law pertaining to successor liabilities within the context of corporate acquisitions have been influenced significantly by concerns for creditor protection. Note, *Assumption of Products Liability in Corporate Acquisitions,* 55 B.U.L. REV. 86, 91 (1975). *See generally* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel,* 10 LOY. L.A.L. REV. 584, 591-92 (1977)(discussing creditor's security in sale of assets).

191. *See* Note, *Assumption of Products Liability in Corporate Acquisitions,* 55 B.U.L. REV. 86, 91 (1975)(successor non-liability facilitates sales of corporate assets by permitting avoidance of contigent or unknown liabilities).

192. The great protections afforded the bona fide purchaser of property were evolved not under the common law, but in a commercial setting under the Uniform Commercial Code. Under the common law, between an innocent purchaser and an innocent owner of property, the owner prevailed. *See generally* C. SMITH & R. BOYER, SURVEY OF THE LAW OF PROPERTY 480 (2d ed. 1971).

193. *See* Turner v. Bituminous Casaulty Co., 244 N.W.2d 873, 880 (Mich. 1976)(where avoidance of product liability only reason to choose cash purchase of assets, non-liability under corporate law rule not in public interest).

194. This argument is founded upon a literal reading of section 402A of the Restatement (Second) of Torts, which states that "[o]ne who sells any product . . . is subject to liability for physical harm thereby caused to the . . . user or consumer . . . ." RESTATEMENT (SECOND) OF

cally states that strict liability is to be imposed on "[o]ne who sells" an unreasonably dangerous and defective product.[196] Opponents of successor liability argue that since the defendant corporation did not manufacture or market the product in question, it should not be held liable for the alleged injuries.[197] This argument is simple and straightforward: since the successor corporation did not "sell" the product causing the injury, it should not be held liable. A literal interpretation of section 402A tends to support this view.[198] The Restatement, however, is not substantive law and need not be strictly construed. Restatement formulations may be adapted judicially to accommodate the dynamic policy considerations underlying modern tort law. This is exemplified in many cases construing this very same phrase—"one who sells"—to mean "one who places into the stream of commerce."[199] As a result of this construction, individuals who have not

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TORTS § 402A (1965). Numerous courts have adopted this approach. *E.g.*, Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1111 (Ill. App. Ct. 1982); Jones v. Johnson Mach. and Press Co., 320 N.W.2d 481, 484 (Neb. 1982); Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 292 (Tex. App.—Austin 1985, writ ref'd n.r.e.).

195. *See* RESTATEMENT (SECOND) OF TORTS § 402A (1965).

196. *See id.* The Restatement provides:

> (1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if
>
> (a) the seller is engaged in the business of selling such a product, and
>
> (b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.
>
> (2) The rule stated in Subsection (1) applies although
>
> (a) the seller has exercised all possible care in the preparation and sale of his product, and
>
> (b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

Id.

197. Some courts contend that the successor did not create the risk and should not be held liable for the harm caused by its predecessor's products. *E.g.*, Leannais v. Cincinnati, Inc., 565 F.2d 437, 439 (7th Cir. 1977); Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1111 (Ill. App. Ct. 1982); Jones v. Johnson Mach. & Press Co., 320 N.W.2d 481, 484 (Neb. 1982).

198. *See supra* text accompanying note 194.

199. *See* First Nat'l Bank of Mobile v. Cessna Aircraft Co., 365 So. 2d 966, 967 (Ala. 1978).

> Not only does decisional authority emphasize the stream of commerce' in fixing liability, but it is also the more reasonable view. When a product is placed in the stream of commerce,' the marketing cycle as it were, whether by demonstration, lease, free sample or sale, the doctrine should attach. In each of these situations the profit motive of the manufacturer is apparent whether or not a sale' in the strict sense takes place. Moreover, the manufacturer who enters the market is in a better position to know and correct defects in

sold but instead have rented,[200] or released the product into the marketplace by bailment,[201] free sample,[202] or otherwise have been held strictly liable for injuries caused by defects in such products. In any case, the true issue is whether the policy considerations supporting section 402A[203] outweigh the literal language of the Restatement. If so, then a literal interpretation which frustrates the policy goals is contradictory and undesirable. Viewed from this perspective, the product line theory does not expand strict product liability, but instead furthers its goals. Again, the argument fails.

The contention that a corporation should not be held liable for what it could not control may also be answered by reference to section 402A. Strict products liability is not based upon fault,[204] but instead upon the premise that those parties who receive the benefits of selling a product should also accept responsibility for harm caused by that product.[205] While this view is arguably unfair to the successor corporation, denying the liability of a successor corporation is equally, if not more, harsh to the injured plaintiff portrayed in our initial scenario. As previously mentioned, successor non-liability violates one of the fundamental doctrines of tort law[206] and contradicts one of the fundamental precepts of strict products liability[207] when it fails to compensate this injured person.

Finally, opponents of successor liability strenuously assert that,

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> his product and as between him and his prospective consumers should bear the risk of injury to those prospective consumers when any such defects enter the market uncorrected.

Id. at 968.

200. *Id.* at 967 (citing Cintrone v. Hertz Truck Leasing & Rental Serv., 212 A.2d 769 (N.J. 1965)).

201. *Id.* (citing Delaney v. Towmotor Corp., 339 F.2d 4 (2d Cir. 1964)).

202. *Id.* (citing McKisson v. Sales Affiliates, Inc., 416 S.W.2d 787 (Tex. 1967)).

203. *See generally* Cowan, *Some Policy Bases of Products Liability*, 17 STAN. L. REV. 1077, 1084-94 (1965).

204. *See* Phipps v. General Motors Corp., 363 A.2d 955, 958 (Md. 1976)(manufacturer's conduct irrelevant).

> [I]n an action founded on strict liability in tort, as opposed to a traditional negligence action, the plaintiff need not prove any specific act of negligence on the part of the seller. The relevant inquiry in a strict liability action focuses not on the conduct of the manufacturer but rather on the product itself.

Id.

205. *Id.* at 963.

206. *See supra* text accompanying notes 158-59.

207. *See supra* text accompanying note 160.

contrary to the position of its proponents,[208] insurance against liability is neither readily attainable nor affordable for some successors.[209] This would be especially true in situations involving small businesses.[210] If, as the opponents argue, insurance is not available, then there would be some resulting unfairness to the defendant business entity. Many courts and commentators have concluded that to deal fairly with the several policy considerations raised by the issue of insurability, state legislatures should resolve the problem.[211] Any question of fairness to the corporation, however, also raises the question of fairness to the injured consumer. No one could argue that this individual is in a better position to insure himself against such contingencies. Consequently, when we compare the innocent injured victim to the going business concern which either placed the product into the stream of commerce or acquired the entity that did, there is no question who should bear the burden. Insurable or not, the acquiring company should pay.

For all the reasons stated, both pro and con, it would seem that the logical conclusion and the best position for all concerned would be the adoption of product line liability. The beginning of this discussion stressed that the difficulty encountered by the courts in determining whether or not to impose product line liability was that the courts are

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208. The court in *Ray*, for example, assumed that a successor corporation could obtain insurance to cover contingent liabilities associated with the predecessor's defective products. Ray v. Alad Corp., 560 P.2d 3, 9 (Cal. 1977).

209. Tift v. Forage King Indus., 322 N.W.2d 14, 24-25 (Wis. 1982)(Callow, J., dissenting); *see also Product Liability Insurance (Part 1): Hearings Before the Subcommittee on Capital, Investment and Business Opportunities of the House Committee on Small Business*, 95th Cong., 1st Sess. 4 (1977)(testimony of Charles W. Whalen, Jr., Edward W. Pattison, Donald J. Pease, Joel Pritchard, & Newton I. Steers, Jr.)(product liability premiums increased 5.8 times more than annual sales between 1970 and 1977); SENATE SELECT COMM. ON SMALL BUSINESS, 28TH ANNUAL REPORT, S. REP. NO. 629, 95th Cong., 2d Sess. 167 (1978)(between 1975 and 1977, product liability insurance premiums increased 100 to 1,000 percent).

210. *See* Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1111 (Ill. App. Ct. 1982)(insurance costs make competition difficult for small businesses); *see also* Heitland, *Survival of Products Liability Claims in Assets Acquisitions*, 34 BUS. LAW. 489, 497 (1979)(some insurance policies now on "claims made" basis, precluding coverage for claims after dissolution of predecessor).

211. *E.g.*, Manh Hung Nguyen v. Johnson Mach. & Press Corp., 433 N.E.2d 1104, 1111 (Ill. App. Ct. 1982); Jones v. Johnson Mach. and Press Co., 320 N.W.2d 481, 484 (Neb. 1982); Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 292-93 (Tex. App.—Austin 1985, writ ref'd n.r.e.); *see also* Comment, *Products Liability and Successor Corporations: Protecting the Product User and the Small Manufacturer Through Increased Availability of Products Liability Insurance*, 13 U.C. DAVIS L. REV. 1000, 1026 (1980).

in fact analyzing and balancing two competing policy goals, using two separate and distinct bodies of law.[212] The corporate common law on the one side seeks to ensure the orderly transfer of assets in a market economy, while the tort law on the other side seeks to compensate the injured victim of a damaging event.[213] When the strengths and weaknesses of product line liability are considered, however, and the function of the judicial system taken into account, it seems clear that the time has arrived for implementation of this theory. It is fair, and taking all factors into consideration, it is a position that best serves society, business, and the injured plaintiff.

V. SUCCESSOR LIABILITY IN TEXAS

A. *Statutory Authority*

Currently, there are three provisions in the Texas Business Corporation Act which relate to the issue of successor corporation liability.[214] The first of these, article 5.06, entitled "Effect of Merger or Consolidation of Domestic Corporation," states:

> Such surviving or new corporation shall thenceforth be responsible and liable for all liabilities and obligations of each of the corporations so merged or consolidated; and any claim existing or action or proceeding pending by or against any of such corporations may be prosecuted as if such merger or consolidation had not taken place, or such surviving or new corporation may be substituted in its place.[215]

This passage is typical of most statutory enactments in the United States today in that it provides that the "surviving" or "new" corporation may be held responsible for the obligations of the merging entities.[216]

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212. *See generally* Comment, *The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel*, 10 LOY. L.A.L. REV. 584, 584-85 (1977)(corporate law supports "predictability" in business transactions while product liability law shifts losses from the consumer); Comment, *A Restoration of Certainty: Strict Products Liability and Successor Corporations*, 43 OHIO ST. L.J. 441, 446-47 (1982)(corporate rule promotes commerce while tort law compensates victims).

213. *See* W. KEETON, D. DOBBS, R. KEETON, & D. OWEN, PROSSER AND KEETON ON THE LAW OF TORTS § 1, at 6 (5th ed. 1984); Kadens, *Practitioner's Guide to Treatment of Seller's Products Liabilities in Assets Acquisitions*, 10 TOLEDO L. REV. 1, 4 & n.5 (1978).

214. TEX. BUS. CORP. ACT ANN. arts. 5.06, 5.10, 7.12 (Vernon Supp. 1988).

215. *Id.* art. 5.06(A)(5).

216. *See e.g.*, ARIZ. REV. STAT. ANN. § 10-076(B)(5)(1977); ILL. ANN. STAT. ch. 32, para. 11.50(5) (Smith-Hurd 1985); N.M. STAT. ANN. § 53-14-6(E) (1983). Many state corpo-

The second statutory provision, article 7.12, entitled "Limited Survival After Dissolution," is also typical in that it provides that existing obligations may not be avoided by dissolving a corporation.[217] The statute states that the mere dissolution of a company does not terminate or impair any existing remedy available against the business entity prior to that date.[218] Article 7.12 goes on to provide that the dissolved corporation remains liable for such existing claims for three years after the date of dissolution.[219] This would mean, however, that if the claim arises after the date of dissolution, or if the claim is not made within three years, the claimant would be completely barred from any recovery.

The third and final relevant section of the Act, article 5.10, entitled "Disposition of Assets Requiring Special Authorization of Shareholders," explicitly states that de facto mergers and consolidations are not authorized under Texas law.[220] Consequently, at least one of the avenues open to injured consumers seeking a remedy in most jurisdictions is closed.[221] In Texas, apparently, unless the acquisition is a statutory merger or consolidation, a corporation which acquires the business operation of another is liable only for those obligations which

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ration statutes are patterned after the Model Business Corporation Act, which provides in pertinent part:

> When a merger takes effect . . . the surviving corporation has all liabilities of each corporation party to the merger . . . .

REVISED MODEL BUSINESS CORP. ACT § 11.06(a)(3) (1984). *But see* Hamilton, *Reflections of a Reporter*, 63 TEX. L. REV. 1455, 1455 n.4 (1985)(influential states such as Delaware, California, New York, and Pennsylvania developed original state corporation statutes, reducing influence of model act).

217. *See* TEX. BUS. CORP. ACT ANN. art. 7.12(A)(2) (Vernon Supp. 1988).

218. *See id.*

219. *See id.*

220. *See id.* art. 5.10(B). The pertinent language states:

> A disposition of any, all, or substantially all, of the property and assets of a corporation, whether or not it requires the special authorization of the shareholders of the corporation, effected under Section A of this article or under Article 5.09 of this Act or otherwise:
>
> (1) is not considered to be a merger or consolidation pursuant to this Act or otherwise; and
>
> (2) Except as otherwise expressly provided by another statute, does not make the acquiring corporation responsible or liable for any liability or obligation of the selling corporation that the acquiring corporation did not expressly assume.

Id.; *see also* Mudgett v. Paxson Mach. Co., 709 S.W.2d 755, 758 (Tex. App.—Corpus Christi 1986, writ ref'd n.r.e.)(de facto merger doctrine not recognized under Texas law).

221. *See generally supra* text accompanying notes 69-117 (discussing de facto merger or consolidation).

it expressly assumes.[222]

B. *Case Authority*

Because of the relative clarity of the Texas Business Corporation Act, the Texas judiciary has been unwilling to question the legislature's intent or to deviate from the statutory limitations. Texas courts, for example, do not recognize the de facto merger.[223] At least two courts of appeals also expressly rejected the product line exception.[224] In the leading case of *Griggs v. Capitol Machine Works*,[225] the plaintiff claimed to have been injured by a defective product manufactured by Capitol Machine Works.[226] Three years before the injury occurred, the company had voluntarily dissolved and transferred all of its assets to another corporation.[227] The injured plaintiff, however, proceeded to trial and pleaded four causes of action, one of which was based upon the product line theory of recovery.[228] The Austin Court of Appeals stated that the issue involved was whether:

> the common law affirmatively impose[s] upon a corporation strict liability for personal injuries caused by an unreasonably dangerous product manufactured and sold by another corporation, when the former has purchased all the assets and going business of the latter and continues to make and supply the same product line as that which includes the unreasonably dangerous product.[229]

The court then took note of the *Ray*,[230] *Ramirez*,[231] and *Dawejko*[232]

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222. Decisions are conflicting as to the issue of whether or not "mere continuation" is accepted in Texas. *Compare* Western Resources Life Ins. Co. v. Gerhardt, 553 S.W.2d 783, 786 (Tex. Civ. App.—Austin 1977, writ ref'd n.r.e.)(recognizing "mere continuation" exception to traditional corporate law rule) *with Mudgett*, 709 S.W.2d at 758 (since de facto merger exception contrary to public policy so is mere continuation exception because it is "even more liberal").

223. *Mudgett*, 709 S.W.2d at 758; Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 292 (Tex. App.—Austin 1985, writ ref'd n.r.e.); *see also supra* text accompanying notes 220-22.

224. Although the Texas Supreme Court has yet to rule on the issue of product line liability, two different courts of appeals have rejected it. *See Mudgett*, 709 S.W.2d at 759; *Griggs*, 690 S.W.2d at 294.

225. 690 S.W.2d 287 (Tex. App.—Austin 1985, writ ref'd n.r.e.).

226. *See id.* at 288 (product causing injury not described in court's opinion).

227. *Id.* at 288-89.

228. *See id.* at 289; *see also id.* at 291 (product line theory is "imputed" liability).

229. *Id.* at 290-91.

230. *See supra* text accompanying notes 120-39.

231. *See supra* text accompanying note 141.

232. *See supra* text accompanying notes 141-44.

decisions and the social policies underlying the theory of strict products liability.[233] The court's conclusion was that the product line theory is a "judicially created . . . common law tort"[234] and that the analysis upon which the theory is founded is "light indeed and the scope . . . astonishing."[235]

The *Griggs* decision, which strictly interpreted the language of section 402A, was based on three general principles. First, the court reasoned that the product line theory advances none of the social policies underlying strict products liability; instead, the theory contradicts the fundamental limitation which the Restatement imposes upon this type of situation.[236] In other words, the court was adhering to the language of section 402A which states that liability is applicable only to "one who sells any product." Construing the rule otherwise, in the court's view, would be tantamount to imposing upon the successor the legal duty to prevent the injury.[237] Secondly, the court asserted that its decision was controlled by Texas precedent.[238] Interestingly,

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233. *See* Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 291-92 (Tex. App.—Austin 1985, writ ref'd n.r.e.)(applying policy considerations to question of successor liability).

234. *Id.* at 291.

235. *Id.* The court noted that no social policy is advanced by imposing liability upon a party who did not put a product "into the channels of commerce." *Id.* The court further complained that such a theory could equally impose liability upon corporate directors, officers, employees, suppliers, or indeed any persons "vaguely" found to benefit from the predecessor's good will, to control the risk, or to have the ability to purchase product liability insurance. *Id.* at 292.

236. *Id.* The court stated:

> Where then may one find the real basis for imposing tort liability upon a person who could not possibly conduct himself so as to avoid the specific injury suffered by a particular plaintiff? The reported decisions adopting the "product line" theory supply no real or explicit basis apart from their misplaced reliance upon § 402A of the Restatement (Second) of Torts. Really, those decisions merely declare a result. The liability they find simply floats between earth and sky, buoyed perhaps by the salutary policy that one should have reparation for his injuries but disregarding nevertheless the fundamental proposition that there is no pre-existing legal principle declaring that liability for such reparation shall descend and fasten upon the purchasing corporation, as opposed to any other person in the universe. Recognizing the want of legal precedent, they embrace but find rejection in § 402A of the Restatement. We find in such decisions patently insufficient analysis and justification for the raw judicial legislation they illustrate so vividly.

Id. at 293.

237. *See id.* at 292 ("legal duty" is duty to make one whole).

238. *See id.* at 293. The court cited as "controlling" precedent *Denison Light & Power Co. v. Patton*, 105 Tex. 621, 154 S.W. 540 (1913); *Mexican Nat'l Const. Co. v. Middlegge*, 75 Tex. 634, 13 S.W. 257 (1890); *Southwestern Gas, Light & Power Co. v. Jay*, 275 S.W. 735 (Tex. Civ. App.—El Paso 1925, writ ref'd n.r.e.). *See id.* at 293-94 (purchaser not a proper defendant for tortious acts committed prior to purchase).

these allegedly binding Texas cases were decided forty years before the inception of section 402A.[239] Finally, the court concluded that since public policy and not legal theory served as the analytical basis for product line liability, the issue more properly should be addressed by the legislature.[240]

Shortly after *Griggs*, the Corpus Christi Court of Appeals, in *Mudgett v. Paxson Machine Company*,[241] was confronted with the same issue.[242] Deferring to *Griggs*, the *Mudgett* court rejected not only the product line theory,[243] but also the de facto merger and mere continuation exceptions to the traditional corporate law rule of successor non-liability.[244] The court reasoned that "the successor cannot be said to have created the risk associated with a product manufactured by its predecessor,"[245] and that if such a "far-reaching change" is required, the legislature rather than the judiciary should make the change.[246] Once again a Texas court opted to have the entire matter decided by the legislative branch of government.

These two cases make it clear that under the present state of Texas law, a corporation which acquires another is liable only for those obligations which it expressly assumes, unless an acquisition is a statutory merger or consolidation.[247] Considering the reasoning of the courts in these decisions, it is not surprising that Texas courts have rejected product line liability.[248] Their argument that numerous competing public policy issues are involved and that the problem should be addressed by the legislature is a persuasive one. Since there are indeed numerous economic and social issues involved, the legislature proba-

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239. The American Law Institute accepted section 402A of the Restatement (Second) of Torts in 1964. W. KEETON, D. DOBBS, R. KEETON, & D. OWEN, PROSSER AND KEETON ON THE LAW OF TORTS § 98, at 964 (5th ed. 1984).

240. *See* Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 294 & n.5 (Tex. App.—Austin 1985, writ ref'd n.r.e.)(judiciary "uniquely ill-suited" to address successor product liability issue). *But cf.* Duncan v. Cessna Aircraft Co., 665 S.W.2d 414, 429 (Tex. 1984)(supreme court created comparative causation due to legislative inaction).

241. 709 S.W.2d 755 (Tex. App.—Corpus Christi 1986, writ ref'd n.r.e.).

242. *See id.* at 758 (plaintiff asked court to adopt product line liability).

243. *Id.* at 759.

244. *Id.* at 758 (de facto and mere continuation exceptions contrary to public policy).

245. *Id.* at 759.

246. *Id.*

247. *See id.* at 758-59; Griggs v. Capitol Mach. Works, 690 S.W.2d 287, 294 (Tex. App.—Austin 1985, writ ref'd n.r.e.); *see also* TEX. BUS. CORP. ACT ANN. art. 5.10(B)(2) (Vernon Supp. 1988).

248. *See generally supra* text accompanying notes 236-40, 245-46.

bly can address the issue of successor liability more effectively than the judiciary. There is, however, one important aspect to this position that must be addressed. If the legislature fails to act, what happens to the injured plaintiff?

VI. CONCLUSION

An individual injured by a defective product placed into the stream of commerce must be compensated for the damages sustained.[249] This is a basic tenet of tort and product liability law. The Texas Legislature should enact a statute which effectively balances the competing corporate and tort considerations discussed above and, at the same time, formulate an equitable means for allowing injured parties to receive adequate compensation. If, however, the legislature fails to act, it would leave "the supreme court no reasonable alternative except to resolve [this] issue when next called upon to do so."[250] "Sooner or later, and the sooner the better, we must bring products liability cases within a manageable format."[251] It is time not only to recognize the changing marketplace illustrated in our initial scenario, but also to take note of the resulting impact that this change has brought upon the individual consumer.[252] The product line theory of liability would serve this function as a logical extension of present product liability law. Furthermore, to deny the adequate redress of an injury solely on the basis of a "corporate technicality" is the very antithesis of the function of modern day courts. In following this present course, we are denying injured plaintiffs their day in court.[253]

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249. This philosophy pervades the entire specter of American tort law.

250. Edgar, *Products Liability in Texas*, 11 TEX. TECH L. REV. 23, 50 (1979)(author calling for adoption of comparative negligence in Texas strict products liability cases).

251. Boatland of Houston, Inc. v. Bailey, 609 S.W.2d 743, 751 (Tex. 1980)(Pope, J., concurring)(misuse of a product is in fact contributory negligence and as such should diminish an individual's recovery in a strict products liability suit).

252. The initial scenario presented illustrates how in some cases an individual may have no cause of action for injuries sustained from a defective product placed into the stream of commerce.

253. Denying an injured plaintiff access to the courts deprives him of due process. *See generally* Note, *The Right of Access to Civil Courts Under State Constitutional Law: An Impediment to Modern Reforms, or a Receptacle of Important Substantive and Procedural Rights?* 13 RUTGERS L.J. 399 (1982). Lack of access to the courts may also violate the open courts doctrine. *See* Neagle v. Nelson, 685 S.W.2d 11, 12 (Tex. 1985)(statute of limitations precluding plaintiff from bringing suit for sponge left in abdomen more than two years after surgery was unconstitutional as violative of Texas's open courts doctrine). The Texas Constitution provides in pertinent part: "All courts shall be open, and every person for an injury done him, in his

For all of these reasons, it seems that the best solution to this predicament is the adoption in Texas of the product line exception.

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lands, goods, person or reputatuion, shall have remedy by due course of law." TEX. CONST. art. I, § 13. "The open courts provision . . . protects a citizen . . . from legislative acts that abridge [an injured party's] right to sue before he has a reasonable opportunity to discover the wrong and bring suit." *Neagle*, 685 S.W.2d at 12.