Piercing The Corporate Veil, Alter Ego And Successor Liability

2017

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Presenter Background

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- The views expressed are solely those of the presenter, and should not be attributed to the presenter’s firm or its clients.
- This presentation does not constitute legal advice; nor does it constitute solicitation of an attorney/client relationship.
Exceptional Remedy


• “Basic tenet” of American corporate law is that “the corporation and its shareholders are distinct entities.”

• “Piercing” is a “rare exception,” applied in the case of fraud and other “exceptional circumstances.”

• Applied on a “case by case basis.”
Focus On Corporate Boundaries


• Parent corporation not liable for torts of subsidiary unless it has “disregarded the separate identity” of the subsidiary

• Rejecting view that parent is liable merely because it could “exert pressure” on subsidiary to act responsibly.
“Complete Domination” Plus Fraud/Wrongful Conduct


• Must show corporate owners “exercised complete domination of the corporation in respect to the transaction attacked”
• Must show that “such domination was used to commit a fraud or wrong against the plaintiff which resulted in plaintiff’s injury”
• Actual fraud: some jurisdictions require proof
Common Factors Considered


• Lack of corporate formalities (director meetings, minutes, stock certificates)
• Common officers/directors; common office space; common use of resources
• Lack of business discretion displayed by dominated corporation
• Under-capitalization
• Diversion of profits
• Commingling/shuttling of funds
• Payment by one corporation of salaries/vendors of another corporation
• Failure to deal at arm’s length
Proof of Actual Fraud


- “Badges of fraud:” multiple potential factors
- Secret/hasty transactions
- Use of dummies/fictitious parties
- Close relationship among parties
No “Form Over Substance”


• Separate accounting; separate tax returns may give appearance of corporate separateness

• Focus on reality of separate activity and corporate control
“Reverse” Piercing


• “Rare” but possible to hold subsidiary liable for obligations of parent
• Dominating corporation puts assets out of reach in subsidiary, but does not maintain true corporate separateness
• “Lateral” piercing also theoretically possible (sibling corporations)
Fraudulent Transfer


• Proof of actual intent to defraud not required
• Transfer of assets without fair consideration, where: (1) debtor insolvent at time of transfer; or (2) debtor made insolvent by the transfer
• Remedy: return of asset (or its value)
Asset Purchase: Four Possible Bases For Liability Of Successor


- Successor corporation “expressly or implied assumes its predecessor’s tort liability”
- There exists a “consolidation or merger of seller and purchaser”
- Purchasing corporation is a “mere continuation of the selling corporation”
- Transaction is “entered into fraudulently,” to escape obligations
“De Facto” Merger

Cargo Partner AG v. Albatrans Inc., 352 F.3d 41 (2d Cir.)

- Continuity of ownership
- Cessation of business activity of acquired corporation
- Assumption of some obligations, necessary to continuity of business
- Continuity of management
“Mere Continuation” Of Business

Cargo Partner AG v. Albatrans Inc., 352 F.3d 41 (2d Cir.)

• Purported cessation of business and asset sale is in effect a corporate reorganization

• Factors: (1) common identity of owners; (2) common identity of directors; (3) only one corporation exists after transaction
“Product Line” Theory

Ray v. Alad Corp., 19 Cal.3d 22 (1977)

• Where party acquires a manufacturing business and continues the output of its line of products, it assume strict liability in tort for defects

• “[V]irtual destruction of the plaintiff’s remedies against the original manufacturer”

• “[S]uccessor’s ability to assume the original manufacturer’s risk-spreading role”

• “Fairness” of requiring successor to assume the responsibility, which is “necessarily attached” to the original manufacturer’s “good will.”

• Rejected in Semenetz (NY 2006): threatens “economic annihilation” to small businesses; could deter transactions
Bankruptcy Asset Sale

• 11 U.S.C. Sec. 363
• May be “free and clear” of debts/obligations of debtor entity
• Creditors gain assets (cash), in exchange for release of claims (by bankruptcy court order)
• Bankruptcy court retains authority to enforce its order, to prevent future litigation. See In re Motors Liquidation Co., 829 F.3d 135 (2d Cir. 2016)
“Single Employer” Theory (Labor Law)

Turley v. ISG Lackawanna, Inc., 774 F.3d 140 (2d Cir. 2014)

• “Conceptually distinct” from piercing theory

• Must show: corporate parent’s involvement was “sufficient and necessary to the total employment process, even absent total control or ultimate authority”

• Held: Sufficient evidence, where parent negotiated collective bargaining agreement, and plaintiff’s employment ended when corporate parent shut down plant and sold assets.
Questions?

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