
In Washington, with four narrow exceptions, a company that acquires the assets of another company is not liable for the latter's debts and liabilities.¹ Courts developed these rules of "successor liability" from theories underlying debtor-creditor relationships. Because the transactions arise out of arms-length bargaining, the parties' liabilities reflect their legitimate expectations.² Yet, when the claim is raised by a victim of the predecessor's defective product rather than a creditor, the liability of a successor cannot rest on the expectations of the parties. Modern products liability³ rests on a public policy that mandates that society bear the costs associated with technological innovation without regard to the parties' expectations.⁴ Courts address—


² The term "successor" as used in this note is defined as an entity that purchases or otherwise acquires substantially all of its assets directly from another entity, as opposed to a "transferee" or "acquiring" corporation, which may acquire assets from a nonentity, such as an individual or trust. The terms "transferor" and "predecessor" will be used interchangeably throughout this text as entities that sell or otherwise transfer their assets either in their own right or in the right of a related party. See Meisel v. M & N Modern Hydraulic Press Co., 97 Wash. 2d 403, 645 P.2d 689 (1982).


ing the issue of successor liability for the defective product of the predecessor face a dilemma: whether to follow the traditional corporate rules or develop new rules to effectuate the policy of products liability doctrine. 6

Addressing this problem, courts have reached varying results. Some courts apply traditional successor liability law, disregarding the conflict between the considerations underlying those rules and the rules of products liability. 7 Other courts attempt to fashion new rules within the framework of traditional successor liability principles. 8 A third group of courts have developed a modern law exception to the traditional rule for

6. At common law, the Washington courts have ruled that strict liability applies to all products liability claims regardless of whether the theory is construction defect, design defect, or inadequate warning. See, e.g., Seattle-First Nat'l Bank v. Tabert, 86 Wash. 2d 145, 542 P.2d 774 (1975) (no distinction should be made between construction defect or design defect and strict product liability should apply); Little v. PPG Indus., Inc., 92 Wash. 2d 118, 594 P.2d 911 (1979) (strict liability analysis should apply in adequacy of warning cases).

As of July 26, 1981, the Washington Legislature limited a manufacturer's strict liability to construction defects and breach of warranty. See Wash. Rev. Code § 7.72.030 (1981). Apparently, the Senate Select Committee on Tort Reform thought prior cases involving design defects and inadequate warnings, even though framed in strict liability terms, were more appropriately analyzed in negligence terms. See Washington State Senate Select Committee on Tort & Product Liability Reform Final Report, 47th Legis., Reg. Sess. 26, reprinted in 1 Senate Journal 37, Reg. & 1st Ex. Sess. (1981). Although the legislature attached the label of negligence to design defects and inadequate warning, the new statute's effect on the earlier common law holdings is still unclear.

7. See, e.g., Woody v. Combustion Eng'g, Inc., 463 F. Supp. 817 (E.D. Tenn. 1978); Bernard v. Kee Mfg. Co., 409 So. 2d 1047 (Fla. 1982); Domine v. Fulton Iron Works, 76 Ill. App. 3d 253, 395 N.E.2d 19 (1979). In Woody, the court declined to depart from the corporate rules, holding that an acquiring corporation bears no closer relationship to a defective product produced by a predecessor than does any other company in the industry which is producing the same product. Moreover, the entity that benefited from the sale of the defective product was the predecessor, since it received the profits. The court concluded that holding an acquiring corporation liable is unfair and greatly burdens business transfers. Cf. Ramirez v. Amsted Indus., Inc., 86 N.J. 332, 431 A.2d 811 (1981); Dawejko v. Jorgensen Steel Co., 209 Pa. Super. 15, 434 A.2d 106 (1981).

strict tort liability cases. Exemplifying this third group, the California Supreme Court in Ray v. Alad Corp., ruled that an acquiring corporation assumes a predecessor's products liability when the acquiring corporation receives the business and continues the predecessor's same product line. Courts following this modern exception recognize that the traditional corporate rules ignore the policy supporting modern products liability. While rejecting the traditional rule's applicability to product liability claims, the modern exception nonetheless accounts for both the expectations of the successor corporation and the needs of the public.

In Meisel v. M & N Modern Hydraulic Press Co., the Washington Supreme Court had its first opportunity to address the problem of reconciling the traditional successor corporation rules and products liability doctrine. Rather than take a determinative posture, the court dodged the issue and instead placed Washington successor liability law in question. Though in dicta the Meisel court recognized the Ray rule and noted its consistency with the court's prior holdings, the court narrowly read the successor classification. The court held that a corporation acquiring a business through a transfer of leased assets and continuing the transferor's product line will not be liable for the transferor's products liability. In misinterpreting what constitutes a transfer of assets, the Meisel ruling effectively subverts the modern rule and provides an easy method for successor corporations to avoid products liability through commonly utilized corporate designs. Ultimately, the court's holding frustrates the recognized public policy that seeks to spread the cost of injury from defective products throughout society rather than force individual consumers to bear the burden.

This note examines the problem of products liability in the context of modern corporate practice. First, this note will

12. See supra text accompanying note 10.
13. See supra note 5.
address products liability doctrine and its underlying rationale.\textsuperscript{14} Next, discussion will focus on the conflict between the policies underlying the products liability doctrine and the traditional successor liability rules. Finally, this note will examine the manner in which the modern rule resolves this inherent conflict and Meisel's effect on that rule, concluding that the Washington courts should adopt the modern rule without limitations.

In \textit{Meisel v. M & N Modern Hydraulic Press Co.}, the facts showed that M & N Modern Hydraulic Press Company (M & N) had been founded in 1955 by Nicholas Brodsky.\textsuperscript{15} Brodsky was the sole owner of the corporation and, in his individual capacity, owned all the manufacturing capital equipment, the land, and the building necessary to M & N's operation.\textsuperscript{16} He leased these assets to M & N. Brodsky died in 1974, and his son, Nicholas Brodsky, Jr., inherited all the leased assets from his father along with nearly sole stock ownership of the corporation.\textsuperscript{17} In June 1976, Nicholas formed a new corporation named Modern Hydraulic Corporation (Modern).\textsuperscript{18} After incorporating Modern, he evicted M & N from use of the leased assets, divested himself of his M & N ownership, then leased all the business assets to Modern.\textsuperscript{19} With Nicholas as president and sole shareholder, Modern continued to manufacture hydraulic presses. Without the leased business assets, M & N continued to run as a service company, repairing presses. Shortly thereafter M & N dissolved.\textsuperscript{20} Prior to both M & N's eviction from the leased assets and M & N's dissolution, however, M & N had manufactured and sold a 20 ton press that, in March 1979, malfunctioned and severed Marie Meisel's hand.\textsuperscript{21} Plaintiff Meisel argued that Modern Corporation should be held liable as a successor under

\textsuperscript{14} See \textit{supra} notes 6 & 11.


\textsuperscript{16} \textit{Id.}

\textsuperscript{17} \textit{Id.} at 404, 645 P.2d at 690. Nicholas Brodsky, Jr. received 99\% ownership of M & N with his mother, Anna Brodsky, recieving the final 1\% ownership.

\textsuperscript{18} \textit{Id.} at 410, 645 P.2d at 693. Nicholas Jr.'s reason for forming the new corporation (Modern) was his mother's nagging. See Brief for Appellant at 3, Meisel v. M & N Modern Hydraulic Press Co., 97 Wash. 2d 403, 645 P.2d 689 (1982).

\textsuperscript{19} \textit{Meisel}, 97 Wash. 2d at 404, 645 P.2d at 690.

\textsuperscript{20} \textit{Id.} at 405, 645 P.2d at 690. Although the M & N Company existed without physical assets up until the time of the suit, the Washington State Supreme Court assumed for summary judgment purposes that M & N existed as no more than a corporate shell.

\textsuperscript{21} \textit{Id.}
Ray's analysis.\textsuperscript{22}

The modern rule that the plaintiff asked the court to apply was forged from the conflicting policies represented by the rules of modern products liability and traditional corporate successor liability. The doctrine of modern products liability expands beyond traditional tort liability the scope of a manufacturer's liability to consumers for injuries caused by defective products.\textsuperscript{23} In Washington, a product manufacturer is subject to strict liability if the product is not reasonably safe in construction or if the product does not conform to the manufacturer's express or implied warranties, and the construction or warranty defects caused plaintiff's harm.\textsuperscript{24} The rationale of modern products lia-

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\item \textsuperscript{22} Id.
\item \textsuperscript{23} The doctrine of strict products liability originated as a hybrid of the two traditional causes of action: negligence and breach of warranty. The history of products liability has been characterized by the constant abolition of various bars to recovery presented by the traditional causes of action. The bars stemming from breach of warranty include absence of privity, disclaimer, absence of reliance on warranty, and lack of notice of breach. The bars stemming from negligence include the burden of proof for establishing all the elements of a negligence action and the absence of contributory negligence. The doctrine of strict products liability was adopted largely in response to the inequities that resulted from the application of the traditional product dissatisfaction causes of action. See generally Prosser, The Fall of the Citadel (Strict Liability to the Consumer), 50 MINN. L. REV. 791 (1966); Prosser, The Assault Upon the Citadel, 69 YALE L.J. 1099 (1960); Traynor, The Ways and Meanings of Defective Products and Strict Liability, 32 TENN. L. REV. 363 (1965).
\item Under the traditional product dissatisfaction causes of action, injured plaintiffs had no remedy against acquiring corporations. In breach of warranty, lack of privity barred injured victims' claims against acquiring corporations. Under negligence theory, lack of negligence on the part of the acquiring corporation barred injured plaintiffs from recovery. However, strict liability is founded on a no fault system that promotes compensation of victims and holds manufacturers responsible for the allocation of product dissatisfaction costs throughout society. See supra note 5 and accompanying text. Because proof of fault is not required in strict products liability actions the traditional bars of privity and fault are inapplicable. Moreover, under the analysis in Ray v. Alad Corp., 19 Cal. 3d 22, 580 P.2d 3, 136 Cal. Rptr. 574 (1977), when an acquiring corporation has a sufficiently close relation with the defective product line, the policies underlying strict products liability are promoted equitably by holding the acquiring corporation liable. Id. at 31, 560 P.2d at 8, 136 Cal. Rptr. at 579.
\item \textsuperscript{24} WASH. REV. CODE § 7.72.060 (1980). The Preamble to the Act states:

\begin{quote}
The purpose of the amendatory act is to enact further reforms in the tort law to create a fairer and more equitable distribution of liability among parties at fault.
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It is the intent of the legislature that the right of the consumer to recover for injuries sustained as a result of an unsafe product not be unduly impaired. It is further the intent of the legislature that retail businesses located primarily in the State of Washington be protected from the substantially increasing product liability insurance costs and unwarranted exposure to product liability
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bility is that manufacturers who place their goods in the stream of commerce impliedly represent their goods as safe for their intended use. The purpose is to place the responsibility for the costs of injuries resulting from defective products on the manufacturer who put such products on the market, rather than on the injured persons who are powerless to protect themselves.

Modern products liability doctrine recognizes the relative abilities of the consumer and manufacturer to bear the risk of loss from defective products. Because the general consumers in a technological society lack the ability to weigh the risks of danger and the costs associated with defective products, they should not bear the loss for injuries from those products. Moreover, the consumer is generally ill-equipped to handle the overwhelming cost of an injury. Manufacturers, however, are better able to discern risks associated with products. When forced to compensate those injured, they will also have an incentive to make their


25. See supra note 23. See also Ramirez v. Amsted Indus., Inc., 86 N.J. 332, 350-53, 431 A.2d 811, 820-22 (1981). In Ramirez, plaintiff was injured while operating an allegedly defective punch press. The machine involved was manufactured by Johnson Machine & Press Co. more than 25 years prior to the injury. Before the accident, there had been three separate transfers of substantially all of the assets, and each intervening entity had held itself out as the same business enterprise. Id. at 337-40, 431 A.2d at 812-15. The court realized that the traditional corporate rules were inconsistent with the rapidly developing principles of strict liability in tort and unresponsive to the legitimate interests of products liability plaintiffs. Furthermore, the court recognized that the traditional corporate rules, which were developed to protect creditors and minority shareholders, place unwarranted emphasis on the form of the transfer rather than the practical effect of the transaction. Id. at __, __, 431 A.2d at 815-17. The court ultimately held Amsted liable under Ray's modern rule, see supra note 10 and accompanying text, reasoning that the imposition of liability on Amsted is consistent with the public policy of spreading the risk to society at large for the cost of injuries from defective products. Id. at __, 431 A.2d at 820-22. The court further justified the imposition as a burden necessarily attached to its enjoyment of Johnson's trade name, good will, and continuation of the manufacturing enterprise. Id. at __, __, 431 A.2d at 822-23. But see generally Comment, A Search for the Outer Limits to Successor Corporation Liability for Defective Products of Predecessors, 51 U. Cinn. L. Rev. 117 (1982).

26. See Note, Postdissolution Product Claims and the Emerging Rule of Successor Liability, supra note 8, at 862.

27. See supra note 5.
products safe. Moreover, with his superior knowledge of the product and its risks, the manufacturer is in a more cost-effective position to spread the risk of harm. On one hand, the manufacturer can acquire insurance at a fair price. On the other hand, with or without liability insurance the manufacturer can pass the cost of products liability claims on to customers, thus placing the risk of loss finally on society as a whole, the ultimate beneficiary of technological innovation. The modern products liability doctrine, therefore, shifts the cost of defective products to society in order to assure that the individual is compensated for this innocent loss.

In contrast to the products liability rules, the traditional rule of successor liability does not seek to assure recovery for products liability plaintiffs. The traditional rule seeks, rather, to effectuate the legitimate expectations of the parties to particular transactions.

At common law, the general rule is that a business entity may purchase, or otherwise acquire, the assets of another business entity without acquiring its debts or obligations. In the context of corporate structures, liability adheres to the fictional corporate entity regardless of the severing of the business assets. By forcing the corporate entity to retain its liabilities, the traditional rule assures that creditors and minority shareholders can look to the entity with whom they dealt for satisfaction of their obligations. Moreover, by freeing the acquiring corporation from liability for the transferring corporation's obligations, the rule facilitates the transfer of capital. Freed from the possibility of judgment awards and other types of unascertainable debts, the purchaser can accurately assess the value of the purchase.

The courts have recognized, however, that the traditional rule may allow a transferring corporation, under certain circum-

28. Id.
29. The term "entity" refers to the formalized corporate existence brought about through proper statutory procedures and also to sole proprietorships and partnerships. The term "enterprise" refers to the nature of the business conducted by any particular entity. For purposes of simplicity, corporate entities will be discussed throughout this comment, but for discussion of sole proprietorship and partnership successor liability see Rawlings v. D.M. Oliver, Inc., 97 Cal. App. 3d 890, 159 Cal. Rptr. 119 (1979); Tift v. Forage King Indus., Inc., 108 Wis. 2d 72, 322 N.W.2d 14 (1982).
31. Unascertainable debts include potential liability for obligations such as products dissatisfaction claims. See Note, The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel, supra note 3, at 593-94 (1977).
stances, effectively to avoid its obligations to the detriment of creditors and minority shareholders.\textsuperscript{33} The courts have identified four circumstances where this may occur: first, where the acquiring entity expressly or impliedly assumes the transferor’s liabilities,\textsuperscript{33} second, where the transfer amounts to a consolidation\textsuperscript{34} or de facto merger,\textsuperscript{35} third, where the acquiring corporation is

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  \item 33. The rationale for holding the acquiring corporation liable when it assumes the liabilities of its predecessor is that the two entities have bargained at arm’s length and have thus devalued the assets according to the liabilities assumed. Therefore, if consideration is not sufficient, creditors should have a right to claim their obligations from the entity undertaking their debtor’s responsibilities. Note, though, that an acquiring corporation rarely expressly assumes the products liability of another entity. Moreover, courts have been reluctant to find an implied assumption of liability between the bargaining entities. See Adams v. General Dynamics Corp., 405 F. Supp. 1020 (N.D. Cal. 1975) (successor’s disclaimer of any undisclosed debts was determinative as not expressly or impliedly assuming products liability arising from predecessor’s defective products). \textit{But see} Bouton v. Litton Indus., Inc., 423 F.2d 643 (3d Cir. 1970) (purchase agreement that included assumption of broad categories of liabilities was sufficient to hold acquiring corporation liable for transferor’s products liability).
  \item 34. In a consolidation two entities form one new entity; in a merger the two combine leaving one of the two entities as the survivor. \textit{Black’s Law Dictionary} 891 (rev. 5th ed. 1979). For purposes of this article, however, both consolidation and merger will be discussed as mergers.
  \item 35. Where one corporation merges with another according to statutory requirements, the survivor corporation is responsible for the liabilities of the nonexistent corporation. \textit{Wash. Rev. Code} § 23A.20.060 (1981). The rationale for statutory merger is that since one entity is absorbing another and since an entity consists of assets and liabilities the surviving corporation receiving the benefit of the dissolving corporation’s assets must also receive the burden of its liabilities. The statutory requirements with which merging companies must comply were designed to protect the rights of creditors and minority shareholders of the dissolving entity. The creditors are protected by a transfer of liabilities to the survivor. The dissenting minority shareholders are protected by appraisal rights that entitle them to the fair market value for their shares. \textit{Wash. Rev. Code} § 23A.24.040 (1981). When a corporation sold its assets for the acquiring corporation’s stock, creditors and minority shareholders traditionally were not afforded any of the protections offered by statutory merger. See \textit{supra} notes 1-3 and accompanying text. The courts developed the de facto merger doctrine which provides that a transaction closely resembling a statutory merger, such as a sale of assets for the acquiring corporation’s stock, should be subject to the same legal consequences as a surviving corporation under statutory merger. The rationale for de facto merger is that acquiring entities should not be allowed to circumvent the predecessor’s liabilities because of the form of the transaction if the transaction has the indicia of a statutory merger. The traditional elements of de facto merger include: (1) consideration for the purchased assets paid in the form of the acquiring corporation’s stock, which ensures that the transferor’s shareholders will retain ownership in the acquiring corporation, (2) some identity of management, and (3) prompt extinction of predecessor. These are the basic elements present in a statutory merger where the surviving corporation as a matter of law is liable for seller corporation obligations. See Menacho v. Adamson United Co., 420 F. Supp. 128 (D.N.J. 1976); Kloberdanz v. Joy Mfg. Co., 288 F. Supp. 817 (D. Colo. 1968); McKee v. Harris-Seybold Co., 109 N.J. Super. 555, 264 A.2d 98 (Law Div. 1970), \textit{aff’d per curiam}, 118 N.J. Super. 480,
merely a "continuation" of the transferee, fourth, where the transferor entered into the transfer agreement fraudulently in order to escape liability. In any one of these four circumstances, courts will find that the acquiring entity is a "successor" to the liabilities and obligations of the selling corporation. The theory supporting this "successor liability" rests on the consideration the purchaser provides to the seller. Where none of the circumstances identified by the four exceptions exist, it is likely that the seller has received consideration from the purchaser adequate to cover the seller's liabilities. In turn, creditors and shareholders can recover their obligations upon the seller's dis-


36. The "continuation" theory is the most nebulous concept. It, like the de facto merger theory, reflects the concepts of "separate entities" and adequate consideration. Liability will be transferred from the transferor to the transferee when the latter is, in effect, a reincarnation of the former. The common law elements include: (1) common identity of officers, directors and shareholders, and (2) insufficiency of consideration in light of assets transferred. See, e.g., Kloberdanz v. Joy Mfg. Co., 288 F. Supp. 817 (D. Colo. 1968); Seipp v. Stetson Ross Mach. Co., 32 Wash. App. 224, 646 P.2d 783 (1982). The rationale for the continuation theory is continuation of the corporate entity, not continuation of the business enterprise. See National Dairy Prods. Corp. v. Borden Co., 363 F. Supp. 978 (E.D. Wis. 1973). Thus, again, ascertainable creditors at the time of dissolution are protected by a right against the predecessor if adequate consideration has been received, or a right against the transferee where continuation is found. Yet, unlike ascertainable creditors, products liability plaintiffs who rely on outward continuation of a business enterprise, are not protected where "continuation" of the corporate entity cannot be shown.

37. The common law tests for this exception include: (1) a showing of fraud or actions otherwise lacking good faith, (2) insufficient consideration for the assets, and (3) predecessor left unable to respond to creditor's claims. The rationale for this exception is that a corporation may not absolve itself of its liabilities through fraudulent transfer under the protection of the separate existence of entities. See, e.g., Wolff v. Shreveport Gas, Electric Light & Power Co., 138 La. 743, 70 So. 789 (1916); McKee v. Harris-Seybold Co., 109 N.J. Super. 555, 264 A.2d 98 (Law Div. 1970), aff'd per curiam, 118 N.J. Super. 480, 288 A.2d 585 (App. Div. 1972), overruled, Wilson v. Fare Well Corp., 140 N.J. Super. 476, 356 A.2d 458 (Law Div. 1976).


solution. If one of the four circumstances is present, however, the consideration is most likely insufficient to meet the seller’s obligations. The exceptions assure that creditors and shareholders can pursue the acquiring corporation as a successor for recovery of outstanding liabilities from which the acquiring corporation did not purchase its freedom.  

Although the common law exceptions protect commercial creditors, they frequently leave the products liability plaintiff without a remedy. Since an acquiring corporation will generally purchase the transferor’s assets for consideration adequate to avoid those known liabilities that the traditional rule seeks to protect (i.e., traditional debts and obligations), the traditional rule looks to the transferor as the source of recovery. If, however, the transferor has dissolved, and if more than two years have elapsed from the time of dissolution, the injured plaintiff is left without a remedy. Thus, while the traditional rules of corporate law satisfy the needs of traditional creditors whose claims arise before or soon after the predecessor’s dissolution, those rules provide no adequate remedy for the typical products liability plaintiff whose claims frequently arise years after the product’s purchase.

The failure of the traditional rules of successor liability to meet the needs of the products liability plaintiff results from the rule’s limited purpose. The rule’s purpose is to protect persons having obligations against a business entity. Although a products liability plaintiff falls into that class of person, the traditional rule was fashioned to meet the needs of only those claimants whose claims were clearly identifiable at the time of the transfer. Fashioned long before the advent of the modern products liability doctrine, the traditional rule did not anticipate the social policies underlying the new doctrine. Consequently, the application of the traditional rule frustrates the policies of mod-

40. See supra note 39.
41. Washington’s postponement abatement statute, WASH. REV. CODE § 23A.28.250 (Supp. 1982), allows suits against the dissolvee corporation within two years from the date of dissolution. The claim sued upon, however, must have arisen before the corporation dissolved. Id. At common law, a corporation’s ability to be sued terminated when the corporation was legally dissolved. See 16A W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §§ 8127, 8142-8143 (rev. perm. ed. 1962).
42. See supra notes 3 & 38 and accompanying text.
43. See Note, The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel, supra note 3, at 590-93. See also supra note 3.
44. See supra note 23.
ern products liability.

Realizing the inequities that resulted from applying the corporate successor liability rule to products liability claimants, several courts attempted to expand the scope of the de facto merger and continuation exceptions, under which products liability claimants generally attempt to recover.46 In Turner v. Bituminous Casualty Co.,48 and Knapp v. North American Rockwell Corp.,47 the courts expanded the de facto merger exception by eliminating some of the traditional elements and replacing them with new elements based on the public policy underlying strict products liability. The traditional elements of the de facto merger include: (1) consideration for the purchased assets in the form of the acquiring corporation's stock, (2) some identity of management, and (3) prompt extinction of the predecessor.48 The Turner court eliminated the stock consideration element and instead looked to the continuation of the enterprise.49 In Knapp, the court excluded the prompt extinction of predecessor element in favor of weighing the relative ability of the successor to bear the loss.50 Two other decisions, Tift v. Forage King Industries, Inc.51 and Cyr v. B. Offen & Co.,52 expanded the traditional continuation theory by virtually eliminating all of the traditional elements and replacing them with new elements fashioned from strict products liability policy. The traditional elements of continuation include: (1) common identity of officers, directors and shareholders, and (2) inadequate consideration for the assets transferred.53 These two courts eliminated both traditional elements and replaced them with the continuation of business enterprise as seen by the general public.54 The Tift and Cyr courts relaxed the narrow exceptions which adequately protected creditors and minority shareholders to include products liability claimants when justice required.

45. See supra note 8.
46. 397 Mich. 406, 244 N.W.2d 873 (1976).
48. See supra note 35.
51. 108 Wis. 2d 72, 322 N.W.2d 14 (1982).
52. 501 F.2d 1145 (1st Cir. 1974).
53. See supra note 36.
54. See Cyr v. B. Offen & Co., 501 F.2d 1145, 1152-54 (1st Cir. 1974); Tift v. Forage King Indus., Inc., 108 Wis. 2d 72, 76-82, 322 N.W.2d 14, 16-18 (1982).
The efforts of these four courts have stretched the traditional corporate rule beyond its purpose in a piecemeal and often inconsistent manner. Their rationales do nothing to reconcile the inherently distinct circumstances in which the traditional rules arise. In fact, under the Tift holding, creditors and shareholders are now granted even more protection as a result of the relaxed standards.

Rather than broadly read a rule designed for limited purposes, the California Supreme Court correctly recognized the inherent incompatibility of traditional successor liability rules and the modern products liability policy, and adopted a modern rule that addresses the problem. In Ray v. Alad Corp., the court developed an exception for successor liability specifically designed to deal with products liability claims. It did so by examining both products liability policies and the traditional corporate principles, concluding that the traditional rules could not adequately protect products liability plaintiffs.

In Ray, the plaintiff was injured by a defective ladder and brought suit for damages. Prior to the claim, however, the manufacturer had sold its assets for cash and then dissolved. A new and separately owned corporation acquired the plant, equipment, inventory, trade name, personnel, customer lists, and goodwill of the manufacturer, and continued the same line of business under the same corporate name. There was no intervening manufacturing hiatus during or after the sales transac-

55. Tift, 108 Wis. 2d at 104, 322 N.W.2d at 29 (Callow, J., dissenting). Judge Callow stated in his dissent, "[b]ecause the majority has not cited any authority in support of its [continuation and de facto merger theory] conclusion, I can only believe that it seeks not to apply the law as it is; it seeks to mold the law in the image it wishes it to be." Id. at 87, 322 N.W.2d at 20. See also Note, The Extension of Products Liability to Corporate Asset Transferees—An Assault on Another Citadel, supra note 3, at 607; Note, Postdissolution Product Claims and the Emerging Rule of Successor Liability, supra note 26, at 864.

56. See Tift v. Forage King Indus., Inc., 108 Wis. 2d 72, 322 N.W.2d 14 (1982) (court refashioned and broadened the traditional elements without justification or distinction between tort and contract creditors).


58. See Ray, 19 Cal. 3d at 31, 560 P.2d at 8, 136 Cal. Rptr. at 579.

59. Id. at 25, 560 P.2d at 5, 136 Cal. Rptr. at 576.

60. Id. at 25-26, 560 P.2d at 5-6, 136 Cal. Rptr. at 576-77.

61. Id. at 24-28, 560 P.2d at 5-6, 136 Cal. Rptr. at 576-77.
The court recognized that if it applied the traditional successor liability rule, the victim would be without a remedy because the predecessor had received adequate consideration for its assets, distributed the consideration to its shareholders, and dissolved before the plaintiff's claim arose. Strict products liability policy, however, mandated a remedy. Recognizing the undesirability of modifying the traditional corporate rules, the Ray court formulated a new test based on the policies underlying manufacturer's strict products liability: the compensation of injured victims and the allocation of product dissatisfaction costs throughout society.

The court ruled that a corporation which acquires a manufacturing business and continues its product line assumes strict products liability for defects in products produced and distributed by the entity from which the business was acquired. The court based its holding on three underlying rationales. First, the transferee's acquisition of the business enterprise effectively destroyed plaintiff's remedies in obtaining compensation from the predecessor corporation. Second, the transferee could easily assume the cost spreading role by passing costs onto its consumers. Third, where the transferee has benefited from the continued operation of the predecessor's business, it is fair to impose liability.

The traditional corporate exceptions upon which products liability plaintiffs have relied differ from the Ray rule in many respects. The Ray rule focuses on the continuation of the enterprise, not the entity. Instead of focusing on the internal formalities of the transfer of assets, as traditional corporate rules do, the modern rule looks to the external realities of the transfer.

The courts' first duty under the modern rule is to determine whether the transferee has acquired substantially all the transferor's assets, leaving the transferor no more than a corporate

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62. *Id.* at 34, 560 P.2d at 11, 136 Cal. Rptr. at 582.
63. *Id.* at 28, 560 P.2d at 7, 136 Cal. Rptr. at 578.
64. *Id.* at 31, 560 P.2d at 8, 136 Cal. Rptr. at 579.
65. *Id.* at 34, 560 P.2d at 11, 136 Cal. Rptr. at 582.
66. *Id.* at 31, 560 P.2d at 9, 136 Cal. Rptr. at 580.
67. See supra note 29.
68. The term "substantially all of the assets" means the assets the transferring entity uses to carry on the business enterprise. See generally Gimbel v. Signal Co.'s, 316 A.2d 599 (Del. Ch. 1974), aff'd per curiam on limited grounds, 316 A.2d 619 (Del. 1974). These assets generally include physical assets, such as machinery and buildings, and
shell. Second, the court must determine whether the transferee is holding itself out to the general public as the same corporation as the transferor by producing the same product line under a similar name. Finally, the court must determine whether the transferee is benefiting from the goodwill of the transferor. If these three criteria are met, the transferee is deemed to be in the best position to exact costs for insurance from its predecessor and its customers in order to protect innocent consumers. These three criteria also provide guidelines by which acquiring corporations may set up their transfer agreements. The Ray court has therefore, developed a modern successor liability exception for strict products liability claims that both adequately protects the needs of an injured consumer and provides acquiring corporations guidelines with which to structure their transactions.

In Meisel, the plaintiff argued that the Washington court should adopt the more appropriate Ray rule. Meisel’s claim was based on the fact that M & N, the original manufacturer, was left as no more than a corporate shell after the transfer of assets. Second, Modern had the ability to assume the original manufacturer’s risk spreading role. Finally, considering the continuity of product line and corporate name, it would be fair to hold Modern liable. In dicta, the Meisel court accepted plaintiff’s theory, recognizing that the modern rule was beneficial and not inconsistent with Washington’s products liability policy. The court,

intangible assets, such as trade name, trademark, and goodwill. Moreover, when substantially all of these have been transferred, the transferor is generally left as a corporate shell, existing mainly to wind up corporate affairs prior to dissolution. Dawejko v. Jorgensen Steel Co., 209 Pa. Super. 15, 434 A.2d 106 (1981).


70. Meisel, 97 Wash. 2d at 407, 645 P.2d at 691. After formation, Modern continued to use the Los Angeles Machinery Broker as its distributor. In fact, the Los Angeles distributor thought Modern had only undergone a name change and was the same entity as M & N. Id. at 407, 645 P.2d at 690.

71. Id. at 408 n.1, 645 P.2d at 692 n.1. The Ray court fashioned its modern rule in the context of strict products liability. Since many states embrace strict products liability doctrine they can easily adopt the modern Ray rule. In Washington, the new products
nevertheless, held that Modern was not a successor by narrowly defining what constitutes a transfer of assets. In order for a transfer to give rise to a successor corporation, the court noted, there must be a direct transfer of assets from one entity to its own right to another entity in its own right. Therefore, a transfer by a related party, such as an officer or majority shareholder of a corporate entity, in his personal capacity, to another entity, will not satisfy Meisel's entity-to-entity requirement. Here, because the president was sole owner of the business assets at all times, the court found there was no actual transfer of assets by M & N to Modern, and therefore, no successor.\(^7\) Thus, the court

\(^7\) Meisel, 97 Wash. 2d at 407-08, 645 P.2d at 691-92. See also 15 W. Fletcher,
held that a corporation that leases its business assets, which were formerly leased by a different corporation, cannot be classified as a successor corporation regardless of the reality of the transaction. Consequently, the acquiring corporation will not be held liable for the transferor's products liability obligations.

In narrowly defining what constitutes a transfer of assets, the Washington Supreme Court failed to recognize the practicalities of corporate existence and misinterpreted the scope of the modern rule. The court drew a distinction between leased and owned assets based solely on the facts of the cases plaintiff had cited as authority, without examining whether there was a practical difference between leased and owned assets worthy of a distinction. Further, the court failed to examine whether a distinction between leased and owned assets was justified by the policies underlying the modern products liability doctrine and the modern rule. In a practical sense, the difference between a corporation leasing its assets and owning them outright is an artificial distinction.73 A corporate director's decision to lease or purchase physical assets typically rests on financial capacity and tax considerations.74 The court's removal of liability from the transfer of leased assets as opposed to wholly-owned assets will only serve to make a distinction on the basis of how a transferring entity holds its assets. Consequently, a decision that once rested on financial considerations will now be based on the desire to avoid products liability.75

supra note 3, at §§ 7122-23.

73. Although a detailed tax analysis of the consequences of holding business assets was beyond the scope of Meisel, and is beyond the scope of this article, it is well accepted that the leasing of assets has significant tax advantages. See generally 39 Inst. on Fed. Tax. (Matthews Bender) § 35.06 (1981); Sales and Leasebacks, Tax MGMT (BNA) No. 36-3d (Dec. 28, 1981).

74. See supra note 73.

75. Id. See also Warehouse Indem. v. Ariz. Dep't of Econ. Sec., 128 Ariz. 504, 627 P.2d 235 (1981). This was a labor relations case governed by a successor statute which stated that "an organization . . . , which in any manner acquires the trade . . . or business, or substantially all of the assets thereof, shall be liable, . . . for any contributions, interest and penalties due . . . and unpaid by such predecessor employer . . . ." Id. at 506, 627 P.2d at 237. This case had a fact situation similar to that in Meisel. In Warehouse Indem., the acquiring corporation acquired substantially all of the leased assets of the predecessor and carried on the same line of business. Moreover, it held itself out to the public as the same business. The court held the acquiring corporation liable under the statute because the statute did not focus on the internal form of the transaction; rather, it focused on the external substance of the transaction. Thus, it was unimportant that there was no direct transfer of assets between entities. What was important was the transfer and continuation of the business enterprise. Id. at 506, 627 P.2d at 237. Further-
Even assuming that a distinction between the holding of leased and wholly-owned assets could be made, the *Meisel* court misinterpreted the scope of the modern rule. The court, in deciding the case, examined the internal structure of the transfer—how the assets were held, which party transferred the assets, and which party received the assets—concluding that the transfer of assets must be from one entity to another entity in order for products liability to also transfer. The modern rule, however, focuses on the content of the transfer and the party's post-transfer conduct, which bear no relation to the manner in which the entity's assets are held. The inquiry centers on the type of assets used in manufacturing, the product line produced, and the business name and trademark used. Thus, even though the acquiring corporation is a different entity by law, it was held liable when it purchased or otherwise acquired the business assets of another and held itself out to the general public as the same business enterprise. Thus, under the modern rule, the business enterprise is determined by the nature of the business conducted, not by either the legal niceties that have defined the corporate entity, or the manner by which it holds assets.

The practical effects of the *Meisel* court's misinterpretation are many. First, the court relieved a manufacturer properly held liable under the same modern rule that the court ostensibly recognized as proper. In *Meisel*, Modern took possession of substantially all the physical assets formally leased by M & N, including the plant and capital equipment.76 Modern also received the benefits of the trade name and goodwill of M & N.77 Furthermore, Modern continued the same product line without interruption.78 These factors show continuation of the corporate enterprise from M & N to Modern. Under the modern rule, liability would follow.

On a broader level, the *Meisel* ruling will emasculate the modern rule, once it is formally recognized by the court. The Washington State Supreme Court's distinction based on the internal form of the holding of the business assets and its misinterpretation of the modern rule may result in even fewer injured products liability plaintiffs receiving a recovery. The effect of

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77. *Id.* at 407, 645 P.2d at 691.
78. *Id.*

more, note that the California Supreme Court formulated the modern rule from a labor relations context. See Ray, 19 Cal. 3d at 30, 560 P.2d at 8, 136 Cal. Rptr. at 579.
Meisel is to allow corporate owners to dissolve for any tenuous business purpose and reform under a new corporate entity, producing the same product, thereby circumventing successor liability altogether. Following Meisel, any corporation can effectively rid itself of its projected future products liability claims by a simple three-step transaction. First, the original entity arranges a typical sale and leaseback transaction with a related party, such as a majority shareholder or principal officer. Second, the original entity's directors and shareholders, for some business purpose, form a new corporate entity, with a similar name and then dissolve the original entity. Third, the related party that now owns the business assets leases them back to the new entity, which can now continue the same product line as the original entity without responsibility for the original entity's products liability. If corporations go through this process of reformation every few years, they could virtually prevent the great majority of, if not all, injured plaintiffs from recovering on any products dissatisfaction claims. The sole factor underlying this ability is the Meisel court's artificial distinction between leased and owned assets.

By focusing on the single artificial lease/own characterization, the Meisel rule provides directors and controlling stockholders with a new incentive to operate with leased assets alone. The corporate world may now base its lease/purchase decisions on the basis of projected liability, as well as the financial and tax considerations that properly ground such decisions. Rather than assure recovery by legitimate products liability plaintiffs, Meisel legitimizes a process designed specifically to frustrate that recovery. Because of the Washington Supreme Court's interpretation, the modern rule may protect even fewer injured plaintiffs by providing corporations with a simple three-step transaction to circumvent products liability altogether.

Because the Meisel court declined to rule on the adoption of the modern rule, Washington courts are still faced with the dilemma of how to best treat products liability plaintiffs who

79. See Wall Street J., Sept. 27, 1982, at 27, col. 3-6. The Wall Street Journal report states how one manufacturer, Forty-Eight Insulations, Inc., leased its business assets to a new entity under private ownership, and now exists solely to handle its asbestos products liability claims. The purpose of the move was to shield the business enterprise from the asbestos claims.

80. See generally Sales and Leasebacks, Tax. Mgmt. (BNA) No. 36-3d, at 1-9, (Dec. 28, 1981). See also supra note 73.
generally are left without recovery under the traditional successor liability rules. The corporate rules were designed to protect creditors and minority shareholders. The modern rule has presented Washington with a beneficial rule, consistent with Washington products liability policy and one which balances the needs of the corporate world against the needs of the general public.

The Washington Supreme Court improperly held that Modern Corporation was not a successor for the purposes of products liability. The Court failed to recognize the practical realities of corporate existence and the scope of the modern rule. Rather than look at the form of the corporate transfer, as the Meisel court did, the court should focus on the continuity of the enterprise: acquisition of all, or substantially all, of the predecessor’s assets, continuity of the product line, and dissolution of the predecessor.81 Under that rule, liability will properly follow a continuing enterprise, thus protecting the general public’s health and safety by assuring recovery for injury from defective products, and providing incentive to manufacturers to produce safe products. In this day and age, where corporate acquisitions are becoming an everyday occurrence, the courts must not lose sight of the injured consumer, who, under the traditional corporate rules, is left without compensation.

Robert C. Manlowe

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