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# Tort Law - New Mexico Adds the Product-Line Exception to Successor Company Liability - Garcia v. Coe Manufacturing Co.

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# TORT LAW—New Mexico Adds the Product-Line Exception to Successor Company Liability—*Garcia v. Coe Manufacturing Co.*

## I. INTRODUCTION

In *Garcia v. Coe Manufacturing Co.*,[1] the New Mexico Supreme Court was faced with the difficult legal question of choosing which of two innocent parties should bear the financial burden of a wrongful death. Ms. Altagracia Garcia (Garcia), a widow suing individually and representing the estate of her deceased husband, asked the court to hold the Coe Manufacturing Company (Coe) liable for her husband's death.[2] Garcia wanted Coe held liable even though Washington Iron Works, Inc. (WIW), an entity separate and distinct from Coe, was the manufacturer of the product that caused Mr. Garcia's death.[3] Garcia's theory was that Coe should be liable as the successor to WIW. New Mexico law at the time, however, did not impose liability on successor companies for their predecessors' liabilities, except under four limited exceptions.[4] Mrs. Garcia's claim did not fit within any of the exceptions.[5]

The *Garcia* court decided to reconsider the existing rule of nonliability because the New Mexico Supreme Court had never analyzed the rule's implications on tort claims involving predecessor and successor liability.[6] The *Garcia* court concluded that the controversial[7] product-line exception should be added to the list of exceptions.[8] Thus, it added a fifth exception to the general rule of nonliability for successor companies. This note will: (1) discuss the *Garcia* decision; (2) explain the basis for the court's rationale; and (3) explore the implications of the *Garcia* decision on companies doing business in New Mexico.

## II. STATEMENT OF THE CASE

In 1982, Montana de Fibra (Montana), a fiberboard manufacturing company, purchased boardline equipment[9] from WIW.[10] The contract required WIW to assist in the installation of the equipment. WIW was still in the process of installing and making the equipment operational when Coe purchased WIW's assets in 1984.

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1. 123 N.M. 34, 933 P.2d 243 (1997).
2. *See id.* at 35, 933 P.2d at 244.
3. *See id.* at 35-36, 933 P.2d at 244-45.
4. *See id.* at 36, 933 P.2d at 245. The four exceptions under New Mexico law include: (1) when the successor company expressly or implicitly contracts to assume the liability; (2) when the successor company mergers or consolidates with the predecessor company; (3) when the successor company is a virtual continuation of the predecessor company; and (4) when the successor company uses fraudulent tactics to avoid liability. *See id.* at 38, 933 P.2d at 247.
5. *See id.* at 37-39, 933 P.2d at 246-48.
6. *See id.* at 38, 933 P.2d at 247.
7. *See id.* "We note that . . . [the] product-line exceptions have been rejected by many courts that have considered them." *Id.* at 40, 933 P.2d at 249.
8. *See id.* at 40, 933 P.2d at 249. The product-line exception imposes liability on a successor company when it produces the same product as its predecessor. Its premise is that liability should be imposed to provide an injured plaintiff with a remedy, even though it was the predecessor company who manufactured the defective equipment. *See id.* at 38, 933 P.2d at 247.
9. Boardline equipment takes pulp material and compresses it into thin sheets.
10. Unless otherwise cited, all subsequent references to the facts are paraphrased from *Garcia*, 123 N.M. 35-37, 933 P.2d 244-46 (1997).

These assets included manufacturing plants, equipment, patents, and use of the WIW trade name. The deal did not require Coe to take on WIW's liabilities. Instead, WIW indemnified Coe by purchasing insurance for six years from the acquisition date to cover any suits against manufactured products.[11] Coe informed WIW's customers that it was purchasing WIW and that Coe would honor their warranty agreements. Coe's commitment to honor these agreements included Montana's purchase of WIW equipment. Coe's employees, formerly WIW employees, were sent to complete the installation of the equipment.

Coe continued to have business dealings with Montana even after its warranty obligations expired in January 1985. Coe sold Montana some equipment and parts. One Coe employee, Bird, inspected the boardline during two days in April 1986. Another employee, Penner, observed the boardline at work. Penner noted that the start-up mechanism did not have a safety delay and that consequently someone could start it without being able to see whether another employee was in a dangerous position.[12]

Medite, a fiberboard manufacturing company, purchased Montana and its WIW equipment. On December 17, 1990, a Medite employee, Curtis Garcia, was cleaning the elevated conveyor while the equipment was shut-off. Another employee, unaware of Mr. Garcia's proximity to the conveyor, restarted the boardline. Mr. Garcia was pulled by the conveyor into a roller and crushed to death.

On December 14, 1993, Mrs. Altagracia Garcia (Garcia), individually and representing the estate, sued Coe, not WIW,[13] in negligence and strict liability. Garcia had a variety of legal theories including: (1) negligent design, manufacture and installation; (2) negligence in allowing an unreasonably dangerous working condition; (3) liability under the continuation exception;[14] (4) liability under the continuing enterprise exception;[15] and (5) liability under the product-line exception.[16] Coe answered that it was not responsible for WIW's defective equipment and that it did not have a legal duty to warn Medite of any potential defects. The trial court granted Coe's summary judgment motion and Garcia appealed to the New Mexico Court of Appeals. The court of appeals recognized that

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11. The court later concluded that this was an example of good lawyering but was insufficient because six years was too short of a term. *See id.* at 41, 933 P.2d at 250.

12. Penner's observation was particularly relevant because "prior to joining WIW he had designed control systems for boardline plants which incorporated delayed start-up mechanisms." *Id.* at 37, 933 P.2d at 246.

13. *See id.* Mrs. Garcia's attorney attempted to locate WIW. Since WIW was a Washington state based company, the attorney contacted the Washington State Corporation Commission and they informed him that WIW had liquidated all of its assets. *See* Telephone Interview with Philip C. Gaddy, attorney at Gaddy & Hall (Oct. 23, 1997) (notes on file with author) [hereinafter Oct. 23, 1997 Telephone Interview]. The plaintiff named Medite as a defendant in its original complaint, but the district court dismissed them as a party. It concluded that Medite could only be sued under an employer/employee relationship. *See* Telephone Interview with Philip C. Gaddy, attorney at Gaddy & Hall (Dec. 2, 1997) (notes on file with author) [hereinafter Dec. 2, 1997 Telephone Interview].

14. *See Garcia*, 123 N.M. at 38, 933 P.2d at 247. "Generally, a continuation of the transferor corporation occurs where there is: (1) a continuity of directors, officers, and shareholders; (2) continued existence of only one corporation after the sale of the assets; and (3) inadequate consideration for sale of the assets." *Id.* The continuation exception is one of the four traditional exceptions to the general rule of nonliability. *See id.*

15. *See id.* "Under this exception, various factors are considered, such as whether the successor utilizes the same production and supervisory personnel, the same corporate officers and directors, the same managerial personnel, the same methods of production, and the same name." *Id.* The continuing enterprise exception is not one of the four traditional exceptions to the general rule of nonliability. *See id.*

16. *See id.*

Garcia was asking for a modification of the existing general rule of nonliability and sent a certification order to the New Mexico Supreme Court. The supreme court granted certiorari.[17]

## III. HISTORICAL PRECEDENT

### A. *Introduction*

The *Garcia* court relied primarily on two cases: *Brooks v. Beech Aircraft Corp.*[18] and *Ray v. Alad Corp.*[19] *Brooks* provided the *Garcia* court with an analytical device, a public policy balancing scale, to help it resolve the competing policy arguments on expanding successor liability. *Ray*, the seminal case involving the creation of the product-line exception, provided the substantive analysis which tilted the scale toward adopting the new exception. Both cases expanded product liability by embracing the public policy principle that companies can shoulder the burden better than victims because companies can ultimately shift the costs of liability to consumers.[20]

### B. *The Former General Rule of Nonliability in New Mexico Case Law*

*Pankey v. Hot Springs National Bank*[21] incorporated into New Mexico case law the common law general rule that, with four exceptions, unaffiliated successor companies are not liable for their predecessors' liabilities.[22] The rationale behind this general rule was that nonliability promotes the alienability of companies.[23] This means that the assets of a company are more likely to be transferred if the purchaser does not have to assume the predecessor's liability. The original four exceptions to nonliability were:

> (1) Where the purchaser expressly or impliedly agrees to assume such debts; (2) where the transaction amounts to a consolidation or merger of the corporations; (3) where the purchasing corporation is merely a continuation of the selling corporation and (4) where the transaction is entered into fraudulently in order to escape liability for such debts.[24]

These exceptions stood as the sole exceptions to the general rule for more than fifty years in New Mexico.

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17. *See id.* at 37, 933 P.2d at 246. The court of appeals can certify issues of first impression to the supreme court under N.M. STAT. ANN. 1978, § 34-5-14(C)(2) (Repl. Pamp. 1997); *See also* N.M. R. APP. P. 12-606 (establishing procedure for certification to the supreme court by the court of appeals).

18. 120 N.M. 372, 902 P.2d 54 (1995).

19. 560 P.2d 3 (Cal. 1977).

20. *See Brooks*, 120 N.M. at 375, 902 P.2d at 57 (citing to general principles established in Greenman v. Yuba Power Prods., Inc., 377 P.2d 897 (Cal. 1962) (in bank) and Escola v. Coca Cola Bottling Co., 150 P.2d 436 (Cal. 1944) (Traynor, J., concurring)).

21. 46 N.M. 10, 119 P.2d 636 (1941).

22. *See id.* at 16, 119 P.2d at 640. *Pankey* involved a judgment creditor attempting to recover his money against a successor bank after a predecessor bank liquidated its remaining assets. The court held that the general rule of nonliability applied and that plaintiff's claim did not fit into any of the exceptions. *See id.* at 13-17, 119 P.2d at 638-41.

23. *See* Garcia v. Coe Mfg. Co., 123 N.M. 34, 39, 933 P.2d 243, 248 (1997).

24. *Pankey*, 46 N.M. at 16, 119 P.2d at 640; *see also supra* text accompanying note 4.

### C. *California Creates a New Exception Based on Policy Considerations*

In *Ray v. Alad Corp.*,[25] the California Supreme Court created a fifth exception to the general rule of nonliability. The *Ray* court based its decision on policy considerations of fair distribution of costs and the protection of innocent plaintiffs.[26] In *Ray*, the plaintiff, Herbert Ray (Ray) alleged that he fell from a defective ladder.[27] Alad (Alad I) had made the ladder, but had been succeeded by the Alad Corporation (Alad II) at the time of the accident.[28] Ray sued Alad II because Alad I had dissolved.[29] Ray then alleged that Alad II was the mere continuation of Alad I and thus was liable under the third exception to the general rule of nonliability.[30] Ray alleged that Alad II had continued to produce the same ladders under the same trade name without any indication of change of ownership.[31] Alad II, however, had not agreed to assume Alad I's liability.[32] Alad II asserted that it had not manufactured the defective ladder and moved for summary judgment.[33]

The *Ray* court began its review with an analysis of whether any of the exceptions were applicable.[34] It concluded that: (1) Alad II had not contracted to assume liability; (2) Alad II had not merged with Alad I; (3) Alad II was not a continuation of Alad I because of a change in stock ownership; and (4) that there was no fraudulent activity.[35] This meant that the current rule of nonliability with its exceptions could not remedy the plaintiff's claim.[36] The *Ray* court concluded that public policy considerations should be factored into defective product cases in order to achieve more equitable results.[37]

The court ruled that protecting the plaintiff justified imposing liability on successor manufacturers because the manufacturers were better able to spread the economic burden throughout society.[38] When Alad II acquired Alad I's assets, it also acquired the part of Alad I's financial resources that had been available to deal

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25. 560 P.2d 3 (Cal. 1977).
26. *See id.* at 8-9.
27. *See id.* at 5.
28. *See id.*
29. *See id.* at 6.
30. *See id.* at 7. The third exception applies when the successor company is merely the continuation, with the same stockholders and executives, of the predecessor company. *See supra* text accompanying note 14.
31. *See Ray*, 560 P.2d at 5.
32. *See id.* at 6.
33. *See id.* at 5.
34. *See id.* at 7.
35. *See id.*
36. *See id.* at 8.
37. *See id.*
38. *See id.* at 8-9.

> 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 rule, 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 the business.

*Id.*

with the consequences of defective ladders.[39] Alad II now had the same capacity as its predecessor to estimate the risks and obtain insurance.[40] Therefore, the *Ray* court reversed the lower court's judgment and assigned liability to Alad II for Alad I's defective products based on strict liability grounds.[41] Alad II was liable because it had continued to produce the same product-line and had the same capacity to deal with defective products as its predecessor.[42]

### *D. New Mexico Uses a Policy Balancing Test for Design Defects Liability*

The New Mexico Supreme Court used a similar public policy rationale to conclude in *Brooks v. Beech Aircraft Corp.*[43] that a company is subject to strict liability in a defective design product liability claim.[44] The court overruled *Duran v. General Motors Corp.*,[45] which held that if a plaintiff alleges that the defective product enhanced the injury, the plaintiff can only sue in negligence.[46] A claim alleging strict liability was now an option.

In *Brooks*, the wife of a deceased pilot sued Beech Aircraft Corporation (Beech) alleging that its Musketeer aircraft was defective, causing the plane crash and her husband's resulting death.[47] Mrs. Brooks (Brooks) alleged that the Musketeer lacked a shoulder harness and this enhanced her husband's injuries.[48] Beech argued that the plaintiff failed to demonstrate that their company had committed any negligence and moved for summary judgment.[49] The motion was granted and Brooks appealed directly to the New Mexico Supreme Court.[50]

The *Brooks* court addressed the larger issue of whether design defect claims should be limited to allegations of negligence.[51] It construed a balancing scale where it considered the policies supporting the limitation[52] against the policies supporting an expansion to a strict liability standard.[53] The court found the

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39. *See id.* at 10.

40. *See id.*

41. *See id.* at 11.

42. *See id.* "[A] party which acquires a manufacturing business and continues the output of its line of products under the circumstances here presented assumes strict tort liability for defects in units of the same product line previously manufactured and distributed by the entity from which the business was acquired." *Id.*

43. 120 N.M. 372, 902 P.2d 54 (1995).

44. *See id.* at 383, 902 P.2d at 65.

45. 101 N.M. 742, 688 P.2d 779 (Ct. App. 1983), *cert. denied*, 101 N.M. 555, 685 P.2d 963 (1984).

46. *See Brooks*, 120 N.M. at 374, 902 P.2d at 56 (citing *Duran*, 101 N.M. at 745, 688 P.2d at 782).

47. *See id.* at 373, 902 P.2d at 55.

48. *See id.*

49. *See id.*

50. *See id.* This direct appeal was based on the court's former jurisdiction over direct appeals on contract claims. This provision was repealed in a 1995 amendment. *See* N.M. R. APP. P. 12-102(A)(1) (Compilers Annotations).

51. *See Brooks*, 120 N.M. at 374, 902 P.2d at 56.

52. *See id.* at 374-75, 902 P.2d at 56-57. There were three main reasons to support the limitation: (1) there was no way to objectively judge defects or mistakes in design so a court should examine whether the manufacturer made an effort to produce a safe design; (2) a plaintiff who could too easily prove that a product was defectively designed could wipe out an entire product and thus an entire company; and (3) old planes that were designed to meet the safety standards of the past should not be judged by safety standards of the present generation. *See id.*

53. *See id.* at 375-76, 902 P.2d at 57-58. There were four main reasons to expand to strict liability: (1) the manufacturer could better distribute the added costs; (2) the plaintiff had difficulty proving negligence; (3) strict liability created an incentive for suppliers to look for and work with responsible manufacturers; and (4) strict liability was more fair to the victims because it moved the burden from those who were injured to those who made

arguments and policies supporting strict liability more convincing[54] and concluded that an innocent victim should have relief. The court remanded the case to allow Mrs. Brooks' claims to be judged under a strict liability standard.[55] The *Brooks* court further noted that its four reasons for imposing strict liability in this case were consistent with the general policies behind the establishment of strict liability.[56]

### *E. The Position of the Majority of Jurisdictions*

The majority of jurisdictions that have faced this issue have refused to adopt the product-line exception.[57] In *Niccum v. Hydra Tool Corp.*,[58] the Minnesota Supreme Court summarized the reasons for rejecting the product-line exception:

> (1) the exception is *inconsistent with* elementary products liability principles, and *strict liability principles* in particular, in that it results in an imposition of liability without a corresponding duty; (2) the *exception threatens small successor businesses* with economic annihilation because of the difficulty involved in obtaining insurance for defects in a predecessor's product; and (3) the exception is essentially a *radical change* in the principles of corporation law, and, as such, *should be left to legislative action.*[59]

Many of these jurisdictions have concluded that they must closely adhere to Section 402A of the Restatement (Second) of Torts (Restatement § 402A),[60] which limits strict liability to the seller.[61] The seller has been interpreted to include the actual seller or manufacturer of the product and not the successor company.[62] A company is subject to strict liability only when it has a duty as the actual manufacturer or seller to provide a safe product to the consumer.[63] Therefore, the imposition of successor liability on a company without such a duty undermines the concept of strict liability.[64]

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money off the product. *See id.*

54. *See id.* at 377-79, 902 P.2d at 59-61.

55. *See id.* at 383, 902 P.2d at 65.

56. *See id.* at 379, 902 P.2d at 61; *see also supra* text accompanying note 20.

57. *See* Howard L. Shecter & David W. Pollak, *Successor Liability in Asset Acquisitions, in* ACQUIRING OR SELLING THE PRIVATELY HELD COMPANY at 97-99 (PLI Corp. Law & Practice Course Handbook Series No. 947, 1996). These states include: Arizona, Colorado, Florida, Georgia, Illinois, Iowa, Kansas, Massachusetts, Michigan, Minnesota, Missouri, Nebraska, New Hampshire, North Dakota, Ohio, Oklahoma, South Dakota, Texas, Vermont, Virginia, Wisconsin. *See id.*

58. 438 N.W.2d 96 (Minn. 1989).

59. *Id.* at 99-100 (emphasis added).

60. The Restatement reads: "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 . . . ." RESTATEMENT (SECOND) OF TORTS § 402A (1965).

61. *See* Bernard v. Kee Mfg. Co., 409 So. 2d 1047, 1050 (Fla. 1982); Guzman v. MRM/Elgin, 567 N.E.2d 929, 932 (Mass. 1991); Downtowner, Inc. v. Acrometal Prods., Inc., 347 N.W.2d 118, 123 (N.D. 1984).

62. *See Guzman*, 567 N.E.2d at 932.

63. *See Downtowner*, 347 N.W.2d at 123.

64. *See Guzman*, 567 N.E.2d at 932. "To impose liability on a successor corporation which did not manufacture, sell, or market the product would be contrary to this principle." *Id.* (citing Simoneau v. South Bend Lathe, Inc., 543 A.2d 407, 409 (N.H. 1988)).

Many of these jurisdictions have also chosen to defer to their legislature's judgment on whether successor liability should be expanded.[65] "The question of whether or not strict liability in tort policy should be substantially altered by also changing established principles of corporate succession transactions involves broad public policy issues which are more appropriately left to legislative determination."[66] Legislatures, according to this reasoning, are better equipped to invite all interested parties to the table, hold hearings, gather opinions and act as fact-finders.[67]

Some of these jurisdictions have expressed concern over the impact of successor liability on small companies.[68] Smaller companies can be at a disadvantage because they do not have the same options as larger companies. They may be unable to afford liability insurance.[69] Their insurance rates are often higher because insurance companies have difficulty calculating risks and writing policies for smaller companies.[70] Smaller companies are also often unable to raise the prices on their goods to cover this added cost and still compete with larger companies.[71]

## IV. RATIONALE

The New Mexico Supreme Court decided to adopt the product-line exception based on policy concerns. In doing so, it used the *Brooks* balancing scale and weighed the arguments supporting and opposing the need for the new product-line exception. The court examined three arguments, taken largely from *Ray*, supporting the new exception: (1) a plaintiff should not be left without a possible remedy; (2) successor companies can assess the risks just as well as their predecessor and can shift the cost to consumers; and (3) successor companies gain the loyalty of their predecessors. Thus, successor companies should also be prepared to assume the burden of providing safe products to consumers.[72] The court considered three arguments opposing the new exception: (1) the successor company had nothing to do with the defective product and thus should not be held liable; (2) the successor company did inherit the consumers' loyalty to the predecessor company but this was not enough to hold the successor liable; and (3) small companies would face economic annihilation because they could not bear the cost of strict liability.[73]

The *Garcia* court concluded that the arguments supporting the product-line exception were more convincing because a "successor is positioned to assess the risks before purchasing the assets, and to then decide whether to assume the potential burden associated with its acceptance of the predecessor's goodwill by

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65. *See* Johnston v. Amsted Indus., Inc., 830 P.2d 1141, 1145 (Colo. Ct. App. 1992); Manh Hung Nguyen v. Johnson Mach. & Press Co., 433 N.E.2d 1104, 1110 (Ill. App. Ct. 1982); *Guzman*, 567 N.E.2d at 933; Jones v. Johnson Mach. & Press Co., 320 N.W.2d 481, 484 (Neb. 1982); *Downtowner*, 347 N.W.2d at 125.

66. *Jones*, 320 N.W.2d at 484.

67. *See Manh Hung Nguyen*, 433 N.E.2d at 1111.

68. *See Johnston*, 830 P.2d at 1144; *Manh Hung Nguyen*, 433 N.E.2d at 1111.

69. *See* Debra A. Schiff, 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, 1024 (1980).

70. *See id.* at 1025.

71. *See Manh Hung Nguyen*, 433 N.E.2d at 1111.

72. *See* Garcia v. Coe Mfg. Co., 123 N.M. 34, 39, 933 P.2d 243, 248 (1997).

73. *See id.* at 40, 933 P.2d at 249.

continuing to produce the same product-line."[74] The court concluded that a successor was capable of assessing these risks and thus should not be allowed to take the good (the customers' loyalty inherited from the predecessor) without any of the bad (the potential liability inherited from the predecessor).[75] The *Garcia* court followed the same reasoning used in *Ray v. Alad Corp.*[76] As a result, it remanded the case in order for Mrs. Garcia's claim to be judged under the new exception.[77]

## V. ANALYSIS

The *Garcia* decision is controversial because the product-line exception to the general rule of nonliability for successor companies has been repeatedly rejected throughout the country.[78] The court's decision reflects its concern with providing a remedy for innocent and injured plaintiffs.[79] The court's decision also reflects a willingness to make what other courts have viewed as a radical change[80] and to act where other courts have deferred to the legislative branch.[81] Therefore, the court could be seen as overstepping its boundaries and exercising judicial activism.

The *Garcia* court's acceptance of the product-line exception means that New Mexico is now one of five jurisdictions that differs from the majority position.[82] There is an explanation for the difference of opinion over the concept of strict liability. New Mexico case law does not require a close adherence to Restatement Section 402A.[83] New Mexico courts have rejected the Restatement's requirement that a company must control the manufacture or sale of a defective product before it can be subject to strict liability.[84] This precedent enabled the *Garcia* court to impose liability without relying on the Restatement's conception of duty.

The *Garcia* court did not explain or try to justify its assertiveness. The court did not make any reference to the legislative branch in its opinion. There was also little mention of the possible problems for small companies. Instead, the *Garcia* court cursorily summed up its position on all of the concerns expressed by other jurisdictions. Its answer was simply: "[w]e believe, however, that these concerns

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74. *Id.*

75. *See id.* at 41, 933 P.2d at 250.

76. 560 P.2d 3 (Cal. 1977).

77. *See Garcia*, 123 N.M. at 41, 933 P.2d at 250. In the suit's secondary issue, the court also remanded Mrs. Garcia's allegation that Coe had a duty to warn Montana and Medite of any product defects. The general rule is: "[A] duty arises only when there is a nexus between the successor corporation, its predecessor's customers, and the allegedly defective product." *Id.* The court acknowledged that Coe and Montana conducted several business interactions but it was not clear whether Coe had actually had notice that there were defects with the WIW equipment. *See id.* at 42, 933 P.2d at 251. The suit, however, was later settled for an undisclosed amount. *See* Dec. 2, 1997, Telephone Interview, *supra* note 13.

78. *See* Shecter & Pollack, *supra* note 57, at 97-99. Some states, such as Alabama and Ohio, have added the continuing enterprise exception, which is an expansion of the third traditional exception (when successor company is merely the continuation of the predecessor company). *See id.* at 91.

79. *See Garcia*, 123 N.M. at 38, 933 P.2d at 247.

80. *See supra* note 59 and accompanying text.

81. *See id.*

82. *See* Ray v. Alad Corp., 560 P.2d 3 (Cal. 1977); Ramirez v Amsted Indus., 431 A.2d 811 (N.J. 1981); Dawejko v. Jorgensen Steel Co., 434 A.2d 106 (Pa. 1981); Martin v. Abbott Lab., 689 P.2d 368 (Wash. 1984).

83. *See* Garcia v. Coe Mfg. Co., 123 N.M.34, 40, 933 P.2d 243, 249 (1997) (citing Stang v Hertz Corp., 83 N.M. 730, 497 P.2d 732 (1972), where the state supreme court turned away from the RESTATEMENT (SECOND) OF TORTS § 402A (1965) and held a lessor strictly liable for a defective automobile).

84. *See Garcia*, 123 N.M.at 40, 933 P.2d at 249.

may be allayed by application of the principles established in *Ray* and *Brooks*, and we therefore adopt the product-line exception."[85]

In a recent speech, Chief Justice Gene E. Franchini, who concurred on the *Garcia* decision, tried to diffuse the charge that his court has been exercising judicial activism.[86] Chief Justice Franchini explained that since New Mexico is such a young state, the appellate courts face many areas of law that have not been decided by prior courts.[87] The *Garcia* court viewed itself as such: "We have not had the opportunity to analyze the application of the rule and its exceptions in the context of a tort claim against a successor corporation."[88] Chief Justice Franchini commented in his speech that when a court resolves an area of law for the first time it does not necessarily mean that it is guilty of judicial activism.[89] He explained that when a court faces such an issue, it looks to how other states have handled the issue.[90] The court then picks what "we think is the best rule for New Mexico because it is the best reasoned rule."[91] Therefore, the *Garcia* court looked to California's *Ray* decision and concluded that it was the best rule for New Mexico because it was the best reasoned rule.

Whether the *Ray* decision was the best reasoned rule available is a debatable proposition. The *Ray* decision appeared to handle the question of who should bear the burden between two innocent parties through a process of elimination. The *Ray* court reasoned that since the injured plaintiff could not bear the burden of costly medical treatment, the successor company had to bear these costs.[92] It did not thoroughly examine whether successor companies could handle this burden.[93]

A more thorough examination of whether successor companies could bear this burden should have done. Yet, the *Garcia* court assumed that successors were capable of factoring this burden into their business planning decisions[94] and that they could protect themselves against potential claims through insurance coverage.[95] Indeed, a company can protect itself through purchasing insurance in several

85. *Id.* 123 at 40, 933 P.2d at 249.

86. *See* Chief Justice Gene E. Franchini, Address at the Federalist Society's Speakers Series at the University of New Mexico School of Law (Dec. 3, 1997) (notes on file with author)[hereinafter Franchini Address]. Chief Justice Franchini stated: "My definition of a judicial activist (is) a judge who knowingly departs from legal precedent in a judicial decision for the purpose of advancing his or her personal, political, philosophical, moral, or religious beliefs as part of the law in his or her jurisdiction." *Id.*

87. *See id.*

88. *Garcia*, 123 N.M. at 38, 933 P.2d at 247.

89. *See* Franchini Address, *supra* note 86.

90. *See id.*

91. *Id.*

92. *See* Ray v. Alad Corp., 560 P.2d 3, 8-9 (Cal. 1977).

93. *See id.* at 10.

94. *See* Garcia v. Coe Mfg. Co., 123 N.M. 34, 40, 933 P.2d 243, 249 (1997). This proposition is debatable because successor companies require the certainty of knowing their potential liabilities for effective business planning. *See also* Janet B. Fierman, Note, *Assumption of Products Liability in Corporation Acquisitions*, 55 B.U. L. REV. 86 (1975). "[C]orporate law and policy . . . require settled rules of successor liability in order to facilitate planning." *Id.*

95. *See Garcia*, 123 N.M. at 41, 933 P.2d at 250.

different forms. A successor company can purchase product liability insurance[96] or it can self-insure itself by setting aside money for possible judgments.[97] This money can also come from a product liability premium added onto the cost of its products.[98] A successor company can always work with the predecessor company. The two can negotiate a long-term indemnification and insurance provision in the purchase contract[99] or the predecessor company can agree to put aside money for the successor company in an escrow account.[100]

The cost of this insurance may discourage companies from purchasing the assets of predecessor companies. The cost of insurance depends on the type of product being manufactured. If the cost is prohibitive, a successor company could take the risk and not buy insurance.[101] The cost may also discourage normal underwriters from writing the policy.[102] A successor may have to go to a surplus line insurer to write a high risk policy.[103]

On the other hand, the *Garcia* decision may not have such a significant impact on New Mexico companies. A successor company may be able to pursue several strategies that will allow them to avoid falling within the scope of the new product-line exception. One such strategy is to distinguish the successor company from its predecessor. This might be done by modifying the product design[104] or by presenting the successor company as a different company to the customers.[105]

The *Garcia* decision, however, did not clearly explain what characteristics will be crucial to set apart a successor's output from its predecessor. The court only held: "[w]hen, as here, the successor continues to *produce* and *market* the same product, using the *same designs*, *equipment*, and *name* . . . [and] when, as here, the successor corporation succeeds to a position of *market prominence because of the goodwill* developed by the predecessor" then liability can be imposed.[106] It is unclear which of these factors, or all of them, are crucial. The *Garcia* court's

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96. *See id.* There are three main types of product liability insurance: the general liability policy, the completed operations policy and products liability only policy. *See generally* Richard C. Ausness, *An Insurance-Based Compensation System for Product-Related Injuries*, 58 U. PITT. L. REV. 669 (1997) (explaining the features of the insurance system and suggesting ideas for improvements).

97. *See* Michael G. Kadens, *Practitioner's Guide to Treatment of Seller's Products Liabilities in Assets Acquisitions*, 10 U. TOL. L. REV. 1, 36 (1978).

98. *See* Brooks v. Beech Aircraft Corp., 120 N.M. 372, 378, 902 P.2d 54, 60 (1995).

99. *See* Kadens, *supra* note 97, at 45. "If such liabilities are imposed by law there is little successors can do to avoid liability except to negotiate lengthy indemnity periods or make sure their insurance coverage, if any, is in order." *Id.* As mentioned earlier, the *Garcia* court found that six years was too short of a term. *See supra* text accompanying note 10.

100. *See* Schiff, *supra* note 69, at 1022.

101. *See* Telephone Interviews with staff members of Alexander & Alexander, Inc., Insurance Consultants (Dec. 2, 4, 5, 1997) [hereinafter Alexander Interviews](notes on file with author); *see also* Telephone Interviews with staff members of Gerding, McMahon, Padon & Koller, Inc., Kemper Insurance Agents (Dec. 2, 1997) [hereinafter Gerding Interviews](notes on file with author). These interviews do not represent the official positions of these companies. These interviews were only designed to provide the author with background information on the insurance market.

102. *See* Alexander Interviews, *supra* note 101.

103. *See id.* A surplus line insurer is a national company (out-of-state) that writes high risk policies. These insurers are regulated under New Mexico state law. *See* N.M. STAT. ANN. § 59A-14-1 to -18 (1995 Repl. Pampl. 1997)

104. *See* Schiff, *supra* note 69, at 1020.

105. *See id.*

106. Garcia v. Coe Mfg. Co., 123 N.M. 34, 41, 933 P.2d 243, 250 (1997) (emphasis added).

statement is more ambiguous than the *Ray* court's final conclusion that "[a] party which acquires a manufacturing business and continues the output of its line of products *under the circumstances here presented* assumes strict tort liability."[107]

The *Garcia* court did appear to be particularly offended by the notion that a successor company might market the exact same product and present itself as the exact same company and then avoid any potential liability.[108] Therefore, if a successor looks and acts like the predecessor and benefits from looking like the predecessor, the successor may invite the imposition of liability. A successor's best strategy may be to make itself distinct from its predecessor and a lawyer's best strategy may be to list as many items as possible that make the successor distinct from the predecessor. A successor company should avoid presenting itself as the same company to the consuming public in order to avoid falling within the new exception to the general rule of nonliability.[109]

The successor company may also consider acquiring the predecessor company through a subsidiary company.[110] Absent piercing the corporate veil, the parent company is shielded from the subsidiary's liability.[111] Therefore, if a plaintiff wins a judgment against the subsidiary because of a defective product produced by the predecessor, the parent company's liability cannot exceed the amount it has invested in the subsidiary company.[112]

The *Garcia* court's conclusion that successor companies are liable for their predecessor appears to follow the standard business practices of the insurance industry. The standard policy for manufacturing companies is an occurrence policy.[113] An occurrence policy is one in which the policy holder at the date of the occurrence/accident is the one who must deal with the claim.[114] These policies do not require the holder of the policy to be the manufacturer of the product.[115]

The *Ray* and *Garcia* courts should have conducted a more thorough examination of the impact of their decisions on successor companies. The potential for problems

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107. Ray v. Alad Corp., 560 P.2d 3, 11 (Cal. 1977) (emphasis added). The *Garcia* court did not cite to the *Ray* court's final conclusion but a lawyer might be able to argue that the language in *Garcia* ("when, as here") is equivalent to the language in *Ray* ("under the circumstances presented here"). *See id.*; *see also Garcia* 123 N.M. at 41, 933 P.2d at 250. If this argument is persuasive, a New Mexico court might opine that all of the listed characteristics are crucial and therefore a successor could fall outside the scope of the product-line exception if the facts of its case are distinguishable from just one of *Garcia*'s factual characteristics. This can be a two dimensional argument, however, with difference in kind and difference in degree, which can lead to even more unanswered questions: (a) how much of a modification in the product is sufficient? (b) is it a systematic change or a slight change in degree? (c) will judges be forced to become engineers or marketing experts? These questions are still unsettled and may have to be resolved through future litigation.

108. *See Garcia*, 123 N.M. at 41, 933 P.2d at 250.

109. The Alad Corporation (Alad II) made the mistake of assuming that by only redesigning the logo on its letterhead and labels it had distinguished itself from its predecessor. *See Ray*, 560 P.2d at 6. In addition, "the manufacturer's representatives *were not instructed* to notify customers of the change." *Id.* at 6-7 (emphasis added). New Mexico businesses should probably do more than redesign their logo and they should instruct their employees and salespeople to notify the customers of the change in companies.

110. *See* Schiff, *supra* note 68, at 1020-1021.

111. *See id.* at 1021.

112. *See id.* The *Garcia* court did not discuss the subsidiary option. The court also did not discuss "piercing the corporate veil", a concept recently discussed by the New Mexico Court of Appeals in *Garcia v. Coffman*, 946 P.2d 216 (Ct. App. 1997). Which involved a medical breach of fiduciary duty.

113. *See* sources cited *supra* note 101.

114. *See id.*

115. *See id.*

still exists, but *Garcia*'s legacy will likely be its positive impact on injured plaintiffs. Therefore, the *Ray* decision and the product-line exception may well be the best rule, despite its repudiation throughout the country.

## VI. IMPLICATIONS

The *Garcia* decision may temper a multi-state corporation's enthusiasm for moving into New Mexico and purchasing the assets of New Mexican businesses. Although companies may be able to remain outside the scope or co-exist with the product-line exception, they may choose to avoid dealing with this situation. The lack of a national uniform standard might create too much havoc for their legal departments.[116]

Successor companies will also have to make changes to avoid liability (such as changing marketing schemes or product design). These changes will cost money. Even if these costs can be passed to the consumer, they may cause waste and inefficiency if the changes are made solely to avoid product-line successor liability.

These changes, however, could possibly spur advances in the industry. A company now has an incentive to spend money on research and development because it needs to modify the product to distinguish itself from its predecessor.[117] This may produce a better product and result in a long term benefit to the industry.

Finally, the lower courts' interpretation of the product-line exception should be monitored. The *Garcia* court did not include any set of factual limiting principles. This is potentially problematic because product liability suits require fact-dependent analyses. Some unorthodox and inconsistent decisions could result. Public policy makers may want to revisit this issue if it becomes unmanageable.[118]

## VII. CONCLUSION

The *Garcia* court has added a fifth exception to the general rule of nonliability for successor companies in New Mexico. The court relied on public policy considerations to reach a three part conclusion that: (a) injured plaintiffs should be protected; (b) successor companies can adequately bear the burden; and (c) this burden is not onerous because companies have tools available to mitigate the cost. Therefore, it is a point of symmetry. A successor company that continues to market and manufacture the same product-line as its predecessor company should prepare itself to accept the good, the consumer's loyalty, along with the bad, the predecessor's liability.

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116. *See* Shecter & Pollack, *supra* note 57, at 102. Amsted Industries "has litigated the issue of successor liability ten times, once each under the laws of California, Colorado, Michigan, Illinois, New Jersey, New York, New Hampshire, Nebraska and twice under the law of Wisconsin. Amsted has won seven times and lost three times." *Id.* at 104.

117. *See* Schiff, *supra* note 69, at 1020. "[C]ourts, in an attempt to encourage corporations to improve old designs and produce a safer product, might, as a matter of policy, refuse to apply the Alad doctrine when a corporation makes design changes." *Id.*

118. The Colorado State Legislature passed a law that limited liability, much like that discussed in § 402A of the *Restatement (Second) of Torts*, to the actual manufacturer. *See* Colo. Rev. Stat. § 13-21-402(2) (1997).