SUPERIOR COURT
OF THE
STATE OF DELAWARE

E. SCOTT BRADLEY
JUDGE

SUSSEX COUNTY COURTHOUSE
1 The Circle, Suite 2
GEORGETOWN, DE 19947

September 19, 2011

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RE: Magnolia's at Bethany, LLC v. Artesian Consulting Engineers, Inc.
C.A. No. S11C-04-013-ESB
Letter Opinion

Date Submitted: September 16, 2011

Dear Counsel:

This is my decision on Defendant Artesian Consulting Engineers, Inc.'s Motion to Dismiss the complaint filed against it by Plaintiff Magnolia's at Bethany, LLC in this case involving a condominium with a leaking roof. Magnolia's complaint alleges that Artesian is the successor-in-interest to Meridian Architects and Engineers, LLC and is therefore responsible for Meridian's negligent design of the condominium developed by Magnolia's. Meridian is an architectural and engineering firm that designed the condominium for Magnolia's. Artesian purchased some of Meridian's assets and assumed some of its liabilities two years after Magnolia's completed the condominium. It did not assume Meridian's liabilities related to the condominium. Magnolia's is now the defendant in a lawsuit filed against it by the condominium's unit owners. It filed this separate lawsuit against Artesian seeking indemnification and contribution for any monies it may have to

pay to the condominium's unit owners. The estimated cost to repair the condominium is $2,000,000. The general rule on successor corporate liability in a matter involving the sale of assets is that a corporation that purchases the assets of another corporation is not responsible for that corporation's liabilities.[1] There are four exceptions to this rule.[2] They apply where the purchaser assumed the seller's liabilities, the transaction was a *de facto* merger or consolidation, the purchaser operates as a mere continuation of the seller, and fraud.[3] Each of these exceptions consists of certain elements that must be pled.[4] I have granted Artesian's Motion to Dismiss because Magnolia's did not adequately plead in its complaint the elements of the alleged exceptions to the general rule on successor corporate liability.

Statement of Facts

Magnolia's is the developer of Magnolia's Resort Condominiums at Bethany, a single-building, three-story, 35 unit condominium with a swimming pool on the roof. Meridian is an architectural and engineering firm owned by Darin A. Lockwood, a licensed professional engineer. It provided architectural and engineering services to Magnolia's for the condominium. The condominium was completed in 2006. Artesian is also an architectural and engineering firm. It purchased some of Meridian's assets in 2008. The

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[1] *Fountain v. Colonial Chevrolet Co.,* 1988 WL 40019, at *7 (Del. Super. April 13, 1988) (Citing *Fehl v. S. W.C. Corp.*, 433 F. Supp. 939, 945 (D. Del. 1977)); *Elmer v. Tenneco Resins, Inc.*, 698 F. Supp. 535, 540 (D. Del. 1988).

[2] Id.

[3] *Id.*

[4] Superior Court Civil Rule 8.

sale of assets was governed by an Asset Purchase Agreement between Artesian, Meridian and Lockwood dated June 6, 2008. Artesian acquired for $130,000 Meridian's uncompleted contracts and accounts receivable and permits related to the uncompleted contracts, computers, office equipment and furniture, motor vehicles, and the use of Meridian's name. Artesian only assumed Meridian's liabilities related to the uncompleted contracts and permits. Meridian's employees did become employees of Artesian after the asset sale closed. Lockwood signed a 10-year consulting agreement with Artesian. Meridian subleased its premises to Artesian for $5000 per month for five years. Artesian later displayed on its Facebook page a number of projects, including Magnolia's condominium, on May 12, 2009. Artesian Resources Corporation, the parent company of Artesian, on behalf of itself and a number of subsidiaries, paid Lockwood $800,000 on August 6, 2010 to terminate all contracts and agreements between Lockwood, Artesian and a number of related entities. Magnolia's, the condominium's unit owners, and the general contractor and various subcontractors for the condominium are now embroiled in separate litigation over defects in the condominium. The chief defect seems to be that water is leaking through the flat roof from the areas around and beneath the swimming pool. The condominium's unit owners filed their lawsuit against Magnolia's and the contractors on August 22, 2009. Magnolia's filed its lawsuit against Artesian on April 12, 2011.

Standard of Review

Artesian argues that Magnolia's complaint fails to state a claim for which relief may be granted. The standards for a Rule 12(b)(6) motion to dismiss in Delaware are clearly

defined. The Court must accept all well pled allegations as true.[5] The Court must then determine whether a plaintiff may recover under any reasonable set of circumstances that are susceptible of proof.[6] Dismissal will not be granted if the complaint "gives general notice as to the nature of the claim asserted against the defendant."[7] A claim will not be dismissed unless it is clearly without merit, which may be either a matter of law or fact."[8] Vagueness or lack of detail in the pleaded claim are insufficient grounds upon which to dismiss a complaint under Rule 12(b)(6).[9] If there is a basis upon which the plaintiff may recover, the motion is denied.[10]

Discussion

Magnolia's alleges in its complaint that Artesian is the successor-in-interest to Meridian because it (1) impliedly assumed responsibility for Meridian's liabilities, (2) engaged in a transaction with Meridian that amounts to a *de facto* merger of Meridian into Artesian, and (3) operates as a mere continuation of Meridian. In Delaware when one company sells or otherwise transfers all of its assets to another company, the buyer generally is not responsible for the seller's liabilities, including claims arising out of the seller's tortuous conduct. In limited situations, where avoidance of liability would be unjust,

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[5] *Spence v. Funk*, 396 A.2d 967, 968 (Del. 1978).

[6] *Id.*

[7] *Diamond State Telephone Co. v. University of Delaware*, 269 A.2d 52, 58 (Del. 1970).

[8] *Id. at 58.*

[9] *Id.*

[10] *Id.*

exceptions may apply to enable the transfer of liability to the seller. These exceptions include: (1) the buyer's assumption of liability; (2) *de facto* merger or consolidation; (3) mere continuation of the predecessor under a different name; or (4) fraud.[11] I will discuss each exception raised by Magnolia's separately.

1. The Buyer's Assumption of Liabilities

Magnolia's complaint alleges that Artesian has impliedly assumed responsibility for Meridian's liabilities for the condominium by holding itself out publicly as the architect and engineer for the condominium. This allegation is based on a Facebook page that Artesian displayed on May 12, 2009. Artesian was advertising on its Facebook page a number of projects, one of which was Magnolia's condominium. Artesian certainly did not expressly assume Meridian's liabilities for the claims related to Magnolia's condominium, leaving Magnolia's to allege that Artesian impliedly assumed them. "Implied" is used in the law in contrast to "express" where the intention in regard to the subject matter is not manifested by explicit and direct words, but is gathered by implication or necessary deduction from the circumstances, the general language, or the conduct of the parties.[12] The subject matter in dispute is the assumption of Meridian's liabilities related to Magnolia's condominium. Artesian's Facebook page is an advertisement that was obviously designed to solicit business, not an expression of its intent to assume Meridian's liabilities for the condominium. Indeed, Artesian's Facebook page did not even mention Meridian, let alone

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[11] *Fountain v. Colonial Chevrolet Co.,* 1988 WL 40019, at *7 (Del. Super. April 13, 1988) (Citing *Fehl v. S. W.C. Corp.*, 433 F. Supp. 939, 945 (D. Del. 1977)); *Elmer v. Tenneco Resins, Inc.*, 698 F. Supp. 535, 540 (D. Del. 1988).

[12] Black's Law Dictionary 754 (6th ed. 1990).

the assumption of its liabilities. To conclude otherwise completely fails to recognize the obvious context and purpose of the Facebook page. No one would interpret it to mean that Artesian had assumed Meridian's liabilities for the condominium. Moreover, the Facebook page ran a full three months before the condominium's unit owners filed their lawsuit against Magnolia's. Thus, it is unlikely that Artesian was even aware of Meridian's liabilities at the time it allegedly assumed them. Therefore, Magnolia's has failed to state a claim of implied assumption of liabilities for which relief can be granted.

2. *De Facto* Merger

A traditional merger under Delaware law involves two or more entities existing under Delaware law merging into a single corporation.[13] Typically, the selling entity is merged into the purchasing entity and ceases to exist.[14] The elements necessary to create a *de facto* merger under Delaware law are the following: (1) one corporation transfers all of its assets to another corporation; (2) payment is made in stock, issued by the transferee directly to the shareholders of the transferring corporation; and (3) in exchange for their stock in that corporation, the transferee agreeing to assume all the debts and liabilities of the transferor.[15] Magnolia's has failed to allege in its complaint the elements of a *de facto* merger. Magnolia's does not, and can not, allege that Artesian acquired all of Meridian's assets because, pursuant to the terms of the Asset Purchase Agreement, Artesian only acquired some of Meridian's assets. Magnolia's does not, and can not, allege that Artesian

[13] 8 *Del.C.* § 251(a).

[14] *In re Asbestos Litigation (Bell)*, 517 A.2d 697, 699 (Del. Super. 1986).

[15] *Drug, Inc. v. Hunt*, 168 A. 87, 96 (Del. 1933).

transferred its stock directly to Lockwood because, pursuant to the terms of the Asset Purchase Agreement, Artesian transferred $130,000 to Meridian for its assets and no stock to Lockwood. Magnolia's does not, and can not, allege that Artesian assumed all of Meridian's debts and liabilities because, pursuant to the terms of the Asset Purchase Agreement, Artesian only assumed some of Meridian's debt and liabilities. Therefore, Magnolia's has failed to state a claim of *de facto* merger for which relief can be granted.

3. Continuation Theory

The continuation theory of successor corporate liability has been narrowly construed by the Delaware courts.[16] Mere continuation requires that the new company be the same legal entity as the old company. "The test is not the continuation of the business operation; rather, it is the continuation of the corporate entity."[17] Imposition of successor liability is appropriate only where the new entity is so dominated and controlled by the old company that separate existence must be disregarded.[18] The primary elements of continuation include the common identity of the officers, directors, or stockholders of the predecessor and successor corporations, and the existence of only one corporation at the completion of the transfer.[19] Magnolia's has not alleged sufficient facts to support a finding that Artesian is "the same legal person" as Meridian. Artesian and Meridian were two unrelated business entities in 2008 and remain so today. Meridian was and is owned by Lockwood.

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[16] *Fountain,* 1988 WL 40019, at *8.

[17] *Fountain,* 1988 WL 40019, at *9.

[18] *Elmer,* 698 F. Supp. at 542.

[19] *In re Asbestos Litigation,* 517 A.2d at 699.

Artesian was and is a wholly-owned subsidiary of Artesian Resources. There is simply no reason to believe that the sale of Meridian's assets to Artesian was anything but an arm's length transaction between the parties. The cash consideration for the assets went from Artesian to Meridian. Artesian and Meridian signed a sub-lease, providing that Artesian would pay $5,000 per month to Meridian for its office space. The ownership of Meridian and Artesian did not change as a result of the transaction and Lockwood did not become an officer, director or shareholder of Artesian. Both Meridian and Artesian continued to exist as separate legal entities after the closing on the sale of assets. Indeed, Magnolia's and Meridian were involved with the lawsuit filed by the condominium's unit owners. The elements of the continuation theory of liability are wholly absent. Therefore, Magnolia's has failed to state a claim of continuation liability for which relief may be granted.

Conclusion

Magnolia's has failed to adequately plead in its complaint the elements of the three allegedly applicable exceptions to the general rule on successor corporate liability. There are a core set of facts that have to be alleged in order to adequately set forth the various exceptions to the general rule that a corporation that purchases another corporation's assets is not liable for the selling corporation's liabilities. They are simply not present in this case. Artesian did not engage in any conduct that suggested it impliedly assumed Meridian's liabilities related to the condominium. Its mere running of an advertisement on a Facebook page can only be interpreted as a solicitation for new business, not the assumption of Meridian's liabilities, particularly where the advertisement did not even mention Meridian or its liabilities. Artesian did not engage in a *de facto* merger with

Meridian because it did not acquire all of Meridian's assets, did not transfer its stock directly to Lockwood, and did not assume all of Meridian's debts and liabilities. Lastly, Artesian is not the mere continuation of Meridian because the two entities did not have common officers, directors and shareholders and because Meridian and Artesian both remained as separate legal entities after the asset sale. The facts are that Meridian and Artesian were two separate legal entities with different owners, officers and directors both before and after the asset sale. Artesian paid Meridian $130,000 for some of Meridian's assets. It did not transfer any of its stock to Lockwood. Artesian only assumed certain liabilities of Meridian's. It did not expressly assume the balance of them and it did not impliedly assume them by running an advertisement for business on a social networking site. It is these undisputed facts that make Magnolia's unable to properly plead the necessary elements for successor corporate liability. Therefore, I have granted Defendant Artesian Consulting Engineers, Inc.'s Motion to Dismiss the complaint filed against it by Plaintiff Magnolia's at Bethany, LLC.

IT IS SO ORDERED.

Very truly yours,

/S/ E. Scott Bradley

E. Scott Bradley

oc: Prothonotary's Office