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BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

B. D. Lithograph, Inc., dba Gardner Lithograph and Sterling Business Credit, Inc., Complainant, vs. Southern California Edison Company, Defendant.	Case 88-04-035 (Filed April 13, 1988)

Lincoln Gardner, Attorney at Law, for Gardner Lithograph, Inc., and Sterling Business Credit, Inc., complainants.
Phillip Walsh, Attorney at Law, for Southern California Edison Company, defendant.

OPINION

Complainants B. D. Lithograph, Inc. (BD Litho) and Sterling Business Credit, Inc. (Sterling) allege the following:

In 1986, Sterling provided financing to Gardner/Fulmer Lithograph, Inc. (G/F Litho), acquiring in return, a security interest in G/F Litho's equipment, inventory, work in progress, accounts receivable, trade names, etc.

In March 1987, G/F Litho defaulted on its loan payments to Sterling and on March 6, 1987 Sterling, with permission of G/F Litho, entered the premises and took peaceful possession of the secured collateral. After taking possession of the collateral, Sterling contacted Southern California Edison Company (Edison), informing Edison that it had repossessed its collateral at G/F Litho and as secured creditor in possession, requested electric service in its own name so that it could proceed with an orderly liquidation of the collateral in order to preserve the value of the collateral.

On March 9, 1987, Edison sent Sterling a notice to make a deposit, checking the box marked "Initial deposit request--for your convenience, we turned the electric service on prior to receiving your service deposit."

On March 11, 1987, Edison sent a letter to Sterling advising that it would not change service over to the name of Sterling. The letter further advised that since the business was still operating as G/F Litho, previous and current bills incurred by G/F Litho were still owing to Edison and that future energy consumption would remain in the account of G/F Litho until proof of a new identity accepting responsibility for the electric service was made.

On March 12, 1987 G/F Litho filed a Chapter 11 bankruptcy. On that same date, Sterling sent a letter along with a check to defendant stating that it was paying the amount demanded under protest.

In April 1987, after obtaining relief from stay in the bankruptcy court, Sterling conducted a sale of the assets of G/F Litho to satisfy the debt owed to Sterling. The assets were sold to David Gardner (Gardner) on behalf of BD Litho which was organized as a startup corporation by Gardner to re-engage in the lithographic business.

As part of the purchase agreement between BD Litho and Sterling for the assets of G/F Litho, BD Litho paid Sterling the cost of the payments demanded by and paid to Edison by Sterling and Sterling assigned its rights to the contested moneys paid Edison to BD Litho.

BD Litho had no relationship whatsoever with G/F Litho other than the fact that it purchased the assets of G/F Litho from Sterling and that up to approximately 12 to 15 months prior to March 6, 1987, Gardner, principal shareholder of BD Litho, was a shareholder in G/F Litho. However, after selling his entire stock interest in G/F Litho to Edward Yeager (Yeager) in 1986, Gardner had no further ownership interest in G/F Litho.

Complainants contend that the $13,500 which Sterling was ordered to pay to Edison reflected the amounts due Edison by G/F Litho, and that neither Sterling nor BD Litho were liable for any debts owed to Edison by G/F Litho prior to Sterling taking possession of the assets of G/F Litho.

Sterling and BD Litho request that Edison be ordered to reimburse them the sum of $13,500, reflecting the amount the utility demanded Sterling pay on the past due debt of G/F Litho.

Edison's answer to the complaint states the following:

On March 9, 1987 it notified Sterling that it was turning the requested electric service on prior to receiving a service deposit and asked Sterling to make such deposit.

Two days later, Edison sent a letter to Sterling advising that it would not change electric service over to the name of Sterling after determining that the business was still operating as G/F Litho. Sterling was advised that the account would remain in the prior name until proof of a new entity accepting responsibility for the electric service was furnished.

Sterling has never provided Edison with any proof or documentation that the subject business or the assets thereof were transferred from one legal entity to another.

Edison takes the position that the subject business has continued to be operated as the same business and that Edison has properly applied the deposit paid to it by Sterling against the outstanding debt owed Edison by G/F Litho.

G/F Litho, BD Litho dba Gardner Lithograph, and Sterling represent alter egos of Gardner and as such should be treated as a sole entity for purposes of payment of its electric bill.

Edison contends that any change in ownership of G/F Litho was done for purposes of defrauding Edison and therefore such a transfer should be disregarded.

Any purchase by BD Litho of the subject business represents a continuation of the business of the selling entity and that since the subject business has been conducted on a continuing basis by the same parties, any technical change in ownership should be disregarded.

Even if Sterling, and later BD Litho, were new customers, the claim is greatly inflated in that most of the deposit paid has been applied to bills which accrued subsequent to March 12, 1987.

Edison alleges therefore that the complaint is without merit and should be dismissed.

Following notice, public hearing in the matter was held in Los Angeles on June 27, 1988 before Administrative Law Judge William A. Turkish, and the matter was submitted upon the receipt of concurrent briefs on July 15, 1988.

Three witnesses were called to testify on behalf of complainants. Two witnesses testified for defendant.

Frederick Bae, employed as a consultant for Sterling, testified on behalf of complainants essentially as follows:

1. During the period March 6 through approximately the middle of April, 1987, his duties included management of the G/F Litho account with Sterling, and as manager of the account for purposes of liquidation, he had his office at the G/F Litho printing facility as well as at the Sterling office.

2. Sterling is a small commercial finance company, securing the assets of small companies as collateral when granting them loans. G/F Litho was one of many borrowers in a creditor-debtor relationship with Sterling. Prior to entering into such creditor-debtor relationship with G/F Litho, Sterling had no other affiliation with G/F Litho in terms of ownership or any

other interest in the company. G/F Litho was simply a borrower from Sterling which put up its assets as collateral for its loans from Sterling.

3. On March 26, 1986, Sterling and Yaeger, president and principal shareholder of G/F Litho executed a financing statement, under the Uniform Commercial Code, which was filed with the Secretary of State on March 26, 1986, in which the assets of G/F Litho was pledged as collateral for the financing provided by Sterling. Yaeger, president of G/F Litho signed the financing statement on behalf of G/F Litho. Yaeger owned G/F Litho at the time.

4. On or about March 12, 1987, G/F Litho filed bankruptcy proceedings and on April 1, 1987 G/F Litho and Sterling entered into a stipulation, approved by the Court, whereby Sterling should be given immediate relief from the automatic stay arising from 11 United States Code (U.S.C.) Sect. 362(a) in order to enforce any and all rights and remedies Sterling may have with respect to the collateral pledged as security by G/F Litho to Sterling.

5. After Sterling took possession of the assets of G/F Litho he contacted Edison to explain the takeover of the assets of G/F Litho. Edison was informed that Sterling would continue to operate the business until the assets could be sold and he was told by Edison that they would send someone over to read the meter and that Sterling would be responsible for the account from that point on. Thereafter, Sterling received two notices from Edison to make a credit deposit. The exchange of letters-from Edison to Sterling dated March 11 and the letter from Sterling to Edison dated March 12, 1987, followed.

6. In the March 12th letter, Sterling informed Edison that it was a financial institution with no interest in the printing business; that it had repossessed its collateral at G/F Litho and that service would be needed

through the auction date which at that point was set for April 15. Sterling further went on to notify Edison that it had taken possession on Friday, March 6, 1987 and that they had notified Edison the following Monday morning requesting new service under the Sterling name. The letter further made reference to the additional $5,500 demanded by Edison in its March 11th letter resulting from an alleged payment agreement made on March 5, 1987 by G/F Litho to Edison and Sterling indicated that it would pay that amount under protest to forestall the cutting off of power by Edison.

7. After taking possession of the assets of G/F Litho, Edison demanded deposits totalling $13,500 plus the $5,500 payment owing to Edison on the delinquent G/F Litho accounts as a condition of allowing power to be furnished to the premises. Sterling then paid the $19,000 total demanded by Edison on March 12, 1987.

8. After Sterling took over the assets of G/F Litho it used the name "Gardner/Fulmer Lithograph/Sterling Business Credit Inc., creditor in possession."

9. Sterling was not interested in operating the G/F Litho business. Their intent was to just keep it going to finish up various jobs that were in progress when it took over the assets of G/F Litho and then to liquidate the assets through sale.

10. From the time Sterling took over the G/F Litho assets, it did not accept any new business. It merely continued to fill the existing orders in progress. Approximately one-half the employees were let go and the remaining production workers were paid by Sterling from its own bank account.

11. In April, 1987 most of the assets of G/F were sold by Sterling to BD Litho for $641,000. The amount of the debt owed to

Sterling by G/F Litho at the time of the sale to BD Litho was $600,000.

12. Gardner was never involved in any dealings between Sterling and G/F Litho.

Janet Gonser (Gonser), a credit administrator for Edison during the relevant periods herein, called as a witness by BD Litho and Sterling, testified essentially as follows:

1. The balance of Account No. 8420 owed by G/F Litho at the beginning of January 1987 was $4,551.27. On January 15, 1987, G/F Litho was billed $3,842.64 on this account. On February 13, 1987 G/F Litho was billed $4,892.98. From February 13, 1987 to March 6, 1987, the estimate of the bill for electricity used by G/F Litho was in the amount of $3,198.93. Payments on the account from January to March 6 totaled $8,393.41, leaving a balance owing on March 6 of $8,091.84 (sic).

2. The balance of Account No. 4063 owed by G/F Litho on January 9, 1987, was $2,105.51. On January 21, Edison rendered a bill for $1,805.43. On February 28, 1987 G/F Litho was billed $2,032.07. From that billing period until March 6, 1987 the consumed energy was estimated at $853.58. Payments on the account from January 9, to March 6, 1987 totalled $3,911.22, leaving a balance owed by G/F Litho, on March 6, 1987 of $2,885.37. Adding that amount to the 8420 Account totals $10,977.21 owed by G/F Litho.

3. Of the $19,000 paid by Sterling on March 12, $8,022.49 was applied toward electric energy used by Sterling after March 6, 1987. The remaining $10,977.21 was applied against the outstanding G/F Litho obligation.

4. On March 5, 1987, Gonser negotiated a payment plan with G/F Litho on their outstanding debt, in lieu of requiring them to post a cash deposit of $13,500. A payment of $5,500 was to be paid on

March 12, 1987. Until she received the letter from Sterling dated March 12, 1987, Gonser had no knowledge that the business had ceased operating as G/F Litho.

David Gardner (Gardner), called as a witness by BD Litho and Sterling, testified essentially as follows:

1. Gardner is president and sole shareholder of BD Litho. Gardner was formerly president and a 50% shareholder of G/F Litho from 1959, when that company was incorporated, until March of 1986. In March 1986, both Gardner and Orbie Fulmer (Fulmer), the other principal shareholder of G/F Litho, sold their entire shares in the company to a Mr. Ed Yeager (Yeager). The terms of the sale included an employment contract with the company. Following the sale to Yeager, neither Gardner nor Fulmer retained any interest in G/F Litho. Gardner was initially employed as sales manager and thereafter became a salesman for the company. He introduced the Declaration of Purchase Intent dated March 15, 1986 (Exhibit 5) signed by buyer Edward J. Yeager, and sellers David G. Gardner and Orbie Fulmer.

2. Prior to the time that Gardner and Fulmer sold their shares in G/F Litho to Yeager, G/F Litho never had any business dealings with Sterling.

3. On March 6, 1987 representatives of Sterling came to the offices of G/F litho and took possession of all the assets. Gardner was asked by the representatives to stay on and assist them in preserving the value of the assets. Since Gardner had a great many customers from whom he had taken printing orders, he felt it was in the best interest of everyone that such work be completed in order to protect the assets and his customers' confidence in him. Gardner assisted Sterling in completing work that was already in progress when Sterling took over.

4. Shortly thereafter, Gardner formed BD Litho (he and his wife are the sole shareholders) and entered into negotiations with Sterling for the purchase of some of the equipment of G/F Litho. Gardner also purchased two pieces of equipment from two other creditors of G/F Litho. In order to finance the purchase of the assets Gardner had to refinance his home to obtain the necessary cash required in addition to obtaining a loan from Sterling for the balance.

5. As a result of G/F Litho losing its assets and ceasing to exist, Gardner lost $200,000 on an unsecured note received from Yeager when Gardner sold his stock in the company to Yeager.

6. Since BD Litho purchased the equipment from Sterling it has been engaged in the printing business at the same location. It has been paying its electric bills regularly and faithfully.

7. After Sterling assumed the assets of G/F Litho no new printing work was accepted by Sterling. The only work performed while Sterling was in possession was the completion of orders that were previously obtained by G/F Litho.

Discussion

The issues presented are:

1. Whether a secured creditor in possession of a defaulting corporate debtor's assets is liable for the debts of the defaulting corporate debtor; and

2. Whether a new corporate entity engaged in the same type of business and occupying the same premises as a defaulting corporate debtor is liable for the debts of the defaulting debtor where none of the shareholders or officers of the new corporation are shareholders or officers of the defaulting corporation.

The general rule is that where one corporation sells or otherwise transfers all of its assets to another corporation, the latter is not liable for the debts and liabilities of the transferor. There are four well recognized exceptions to this general rule under which the purchasing corporation becomes liable for the debts and liabilities of the selling corporation:

> (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.

We conclude that the facts of this case are insufficient to warrant bringing them within any of the four settled exceptions of the general nonliability rule.

There was no contract, expressed or implied, on the part of Sterling or BD Litho to pay the debts of G/F Litho. The taking of the assets of G/F Litho by Sterling was neither a consolidation nor a merger. Likewise, we find no fraud on the part of Sterling. Nor can it be said that the taking of the assets by Sterling was without adequate consideration in view of the fact that G/F Litho had received considerable financing from Sterling and had defaulted on said loans. Finally, it cannot be stated that because Sterling took possession of the assets of G/F Litho and completed work in progress, that Sterling was a mere continuation or reincarnation of the former corporation.

Sterling is in the financial business and not in the printing business and only completed work already in progress when it took over the assets in order to enhance the accounts receivable assets of G/F Litho which it held as collateral for the defaulted loan. We find no considerations of public policy, on the facts here shown, that would compel the imposition of G/F Litho's liability to Edison upon Sterling.

In considering the facts relative to BD Litho or Gardner, we likewise find no basis upon which liability for the debts of G/F Litho can be imposed upon BD Litho or Gardner. BD Litho is a newly formed corporation which purchased some of the assets of G/F Litho from Sterling for a valuable consideration. The facts do not support a finding of any exception to the general rule with respect to BD Litho. From March 15, 1986 when Gardner sold his entire share of stock in G/F Litho to Yaeger and thereafter became an employee salesman of G/F Litho, he never assumed, either expressly or impliedly, the liability of G/F Litho.

The $5,500 payment made by Sterling to Edison was not the result of any agreement entered into between Sterling and Edison, but rather an agreement entered into between officials of G/F Litho and Edison, prior to the takeover of G/F Litho's assets by Sterling. The fact that Sterling took over the assets of G/F Litho the day following the payment agreement between Edison and G/F Litho does not impose any obligation upon Sterling. Thus the $5,500 payment demanded of and paid by Sterling on March 12, 1987 should be returned. Likewise, Sterling is entitled to a return of the $13,500 credit deposit paid to Edison on March 12, 1987, less any amount owing to Edison on and after March 6, 1987 for electric energy used by Sterling.

Comments to the ALJ proposed decision were filed by Edison. Edison commented that Ordering Paragraph 1 could be interpreted as requiring the payment of interest on the entire amount paid by Sterling and that it should be made clear that the money paid by Sterling that was applied to electric consumption by Sterling is to be deducted from the total before computing interest. In addition, Edison points out that Ordering Paragraph 1 makes reference to amounts owing Edison by Sterling for electric energy consumption from March 6, 1987 to April 14, 1987 while there is no specific ending date in the reference on page 11 of the decision. As Edison's comments are valid, the Conclusion of Law and Ordering Paragraph 1 below will be changed to reflect these comments.

Findings of Fact

1. Gardner and Fulmer were the two principal shareholders of G/F Litho from 1959 until March 1986.

2. In March 1986 Gardner and Fulmer sold their entire shares of stock in G/F Litho to Yaeger. After the sale neither Gardner or Fulmer retained any interest in G/F Litho.

3. After the sale of stock to Yaeger, Gardner was retained by the corporation as a salesman.

4. On March 25, 1986, Yaeger, president of G/F Litho, and Farhad Motia, president of Sterling, executed a financing statement pursuant to the California Uniform Commercial Code for the financing given G/F Litho by Sterling in which all of the assets of G/F Litho were pledged as collateral for such financing.

5. On March 6, 1987, the amount of money owing to Edison for consumed electrical energy by G/F Litho was $10,977.21.

6. Following notice to Edison, Sterling took possession of the assets of G/F Litho due to the default of G/F Litho on the debt owed to Sterling.

7. After taking possession of the assets of G/F Litho, Sterling laid off most of the employees of G/F Litho, but retained some employees in order to complete work already in progress. This was done to protect its security interest in the accounts receivable of G/F Litho.

8. On March 12, 1987, Sterling paid Edison the sum of $19,000, as demanded by Edison, in order to complete the work which was in progress when it took possession of the assets of G/F Litho.

9. In April 1987, Sterling sold some of the assets it possessed to BD Litho for $641,000. The president and principal shareholder of BD Litho is Gardner.

10. Neither Sterling, BD Litho, or Gardner assumed any liability, either expressed or implied, for the debts of G/F Litho.

Conclusion of Law

Since Sterling, BD Litho, nor Gardner ever assumed the liabilities of G/F Litho, and the facts do not fall within any of the exceptions to the general rule of liability of successor entities so as to impose liability upon them, the moneys paid by Sterling to Edison should be reimbursed to Sterling less any charges for electrical energy used by Sterling from March 6, 1987.

ORDER

IT IS ORDERED that:

1. Southern California Edison Company (Edison) shall reimburse the sum of $19,000 to Sterling Business Credit, Inc. (Sterling), less any amounts owing Edison by Sterling for electric energy consumption on and after March 6, 1987, plus interest on any remaining balance.

2. The complaint is granted as set forth above.

This order becomes effective 30 days from today.

Dated NOV 9 1988, at San Francisco, California.

STANLEY W. HULETT
President
DONALD VIAL
FREDERICK R. DUDA
G. MITCHELL WILK
JOHN B. OHANIAN
Commissioners

I CERTIFY THAT THIS DECISION WAS APPROVED BY THE ABOVE COMMISSIONERS TODAY.

Victor Weisser, Executive Director

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2. Prior to the time that Gardner and Fulmer sold their shares in G/F Litho to Yeager, G/F Litho never had any business dealings with Sterling.

3. On March 6/1987 representatives of Sterling came to the offices of G/F litho and took possession of all the assets. Gardner was asked by the representatives to stay on and assist them in preserving the value of the assets. Since Gardner had a great many customers from whom he had taken printing orders, he felt it was in the best interest of everyone that such work be completed in order to protect the assets and his customers' confidence in him. Gardner assisted Sterling in completing work that was already in progress when Sterling took over.

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5. As a result of G/F Litho losing its assets and ceasing to exist, Gardner lost $200,000 on an unsecured note received from Yeager when Gardner sold his stock in the company to Yeager.

6. Since BD Litho purchased the equipment from Sterling it has been engaged in the printing business at the same location. It has been paying its electric bills regularly and faithfully .

7. After Sterling assumed the assets of G/F Litho no new printing work was accepted by Sterling. The only work performed while Sterling was in possession was the completion of orders that were previously obtained by G/F Litho.

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1. Whether a secured creditor in possession of a defaulting corporate debtor's assets is liable for the debts of the defaulting corporate debtor; and

2. Whether a new corporate entity engaged in the same type of business and occupying the same premises as a defaulting corporate debtor is liable for the debts of the defaulting debtor where none of the shareholders or officers of the new corporation are shareholders or officers of the defaulting corporation.

The general rule is that where one corporation sells or otherwise transfers all of its assets to another corporation, the here shown, that would compel the imposition of G/F Litho's liability to Edison upon Sterling.

In considering the facts relative to BD Litho or Gardner, we likewise find no basis upon which liability for the debts of G/F Litho can be imposed upon BD Litho or Gardner. BD Litho is a newly formed corporation which purchased some of the assets of G/F Litho from Sterling for a valuable consideration. The facts do not support a finding of any exception to the general rule with respect to BD Litho. From March 15, 1986 when Gardner sold his entire share of stock in G/F Litho to Yaeger and thereafter became an employee salesman of G/F Litho, he never assumed, either expressly or impliedly, the liability of G/F Litho.

The $5,500 payment made by Sterling to Edison was not the result of any agreement entered into between Sterling and Edison, but rather an agreement entered into between officials of G/F Litho and Edison, prior to the takeover of G/F Litho's assets by Sterling. The fact that Sterling took over the assets of G/F Litho the day following the payment agreement between Edison and G/F Litho does not impose any obligation upon Sterling. Thus the $5,500 payment demanded of and paid by Sterling on March 12, 1987 should be returned. Likewise, Sterling is entitled to a return of the $13,500 credit deposit paid to Edison on March 12, 1987, less any amount owing to Edison on and after March 6, 1987 for electric energy used by Sterling.

<u>Findings of Fact</u>

1. Gardner and Fulmer were the two principal shareholders of G/F Litho from 1959 until March 1986.

2. In March 1986 Gardner and Fulmer sold their entire shares of stock in G/F Litho to Yaeger. After the sale neither Gardner or Fulmer retained any interest in G/F Litho.

3. After the sale of stock to Yaeger, Gardner was retained by the corporation as a salesman.

4. On March 25, 1986, Yaeger, president of G/F Litho, and Farhad Motia, president of Sterling, executed a financing statement pursuant to the California Uniform Commercial Code for the financing given G/F Litho by Sterling in which all of the assets of G/F Litho were pledged as collateral for such financing.

5. On March 6, 1987, the amount of money owing to Edison for consumed electrical energy by G/F Litho was $10,977.21.

6. Following notice to Edison, Sterling took possession of the assets of G/F Litho due to the default of G/F Litho on the debt owed to Sterling.

7. After taking possession of the assets of G/F Litho, Sterling laid off most of the employees of G/F Litho, but retained some employees in order to complete work already in progress. This was done to protect its security interest in the accounts receivable of G/F Litho.

8. On March 12, 1987, Sterling paid Edison the sum of $19,000, as demanded by Edison, in order to complete the work which was in progress when it took possession of the assets of G/F Litho.

9. In April 1987, Sterling sold some of the assets it possessed to BD Litho for $641,000. The president and principal shareholder of BD Litho is Gardner.

10. Neither Sterling, BD Litho, or Gardner assumed any liability, either expressed or implied, for the debts of G/F Litho.

<u>Conclusion of Law</u>

Since Sterling, BD Litho, or Gardner never assumed the liabilities of G/F Litho, and the facts do not fall within any of the exceptions to the general rule of liability of successor entities so as to impose liability upon them, the moneys paid by Sterling to Edison should be reimbursed to Sterling less any charges for electrical energy used by Sterling from March 6, 1987 to the date of sale of the assets to BD Litho, on April 14, 1987.

ORDER

IT IS ORDERED that:

1. Southern California Edison Company (Edison) reimburse the sum of $19,000 to Sterling Business Credit, Inc. (Sterling), plus interest and less any amounts owing Edison by Sterling for electric energy consumption from March 6, 1987 to April 14, 1987.

2. The complaint is granted as set forth above.

This order becomes effective 30 days from today.

Dated ____________________, San Francisco, California.