KANE KESSLER, P.C.

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About Kane Kessler...

Kane Kessler is a midsize law firm located in Midtown Manhattan, serving clients throughout the United States and globally. Kane Kessler has been in the business of providing exceptional legal services to its clients for over 80 years, with experienced and specialized lawyers practicing in many areas of the law. At Kane Kessler, we take pride in delivering personal attention to each and every client and in our ability to offer a wide range of experience and knowledge in many legal specialties to help your business grow and prosper.

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The Editors,

Judith A. Stoll
Gary E. Ostroff

NY Court Puts the Brakes on Overreaching Creditors

Reprinted from *Law360*, November 7, 2014 – In times of economic turmoil, when businesses are failing and cash-flow is tight, creditors often seek to cast a wide net to reach entities other than the company for whom the creditor has provided services and which contractually owes the obligation. Recently the Commercial Division of the New York County Supreme Court issued a pair of decisions curbing creditors' efforts to reach beyond the contracting party to capture entities or individuals with whom it was not in privity.

In American Media Inc. et al. v. Bainbridge & Knight Laboratories LLC et al., 2014 NY Slip Op. 32481(U) (Sup. Ct. N.Y. Co. Sept. 19, 2014), the plaintiff creditor sought to recover a debt against an individual who was the owner, chief executive officer, president, chairman, secretary, treasurer and director of the company that contracted for $1.3 million in advertising services.

Frustrated that the company could no longer pay its debts due to business misfortunes, the plaintiff sued the individual under alter ego, fraud and debtor/creditor law theories. However, the court granted the individual defendant's motion to dismiss, in part upholding the principle that an officer is not liable for the debt of his company just because he made decisions while acting on behalf of the corporation that caused the company to be unable to pay its debts. Moreover, conclusory allegations that the corporate form is a sham will not suffice to overcome a motion to dismiss, or even to warrant discovery.

As to the fraud allegations, the alleged assurances that the company would pay and the individual would invest additional capital were found not to be collateral to the contract for advertising services, but concerned the very performance of those services.

The court also found plaintiff's claims under the New York Debtor and Creditor Law too speculative and conclusory to support the relief requested. The court observed that since plaintiff was not seeking the equitable remedy of voiding any

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purported fraudulent conveyance, but was in essence seeking a money judgment for the amount due under its contract, this claim was merely duplicative of the contract cause of action. The court also cautioned that a sophisticated business entity like the plaintiff could not justifiably rely on the alleged misrepresentations concerning capitalization and financial ability without conducting its own due diligence to verify the promises allegedly made.

Because courts are reluctant to pierce the corporate veil without compelling proof, creditors who seek to pursue individual liability on an alter ego theory need to be diligent in gathering every fact they can muster to suggest that that individual has so dominated the corporation so as to have abused the privilege of doing business in the corporate form. Sufficient facts need to be alleged in the complaint to provide enough detail to persuade the court to allow discovery rather than grant outright dismissal.

Ironically, these very facts of corporate domination and abuse typically lie within the exclusive knowledge of the company and its individual owners/officers, but without a cogent presentation, the complaint will face the same fate it did in the case discussed above. The decision of the Commercial Division in the case is on appeal.

So long as the corporate form is respected and an asset sale is not tainted by fraudulent conduct, the courts will generally not permit creditors to draw into the web of litigation nonparties to the contract such as owners/officers or acquiring corporations.

A companion case was also decided by the Commercial Division that same month. Although it involved different parties and different legal theories, it reflects the common theme of a plaintiff-creditor seeking to impose contract liability upon an entity other than the contracting party.

In Oorach Inc. v. Covista Communications Inc., et al., 2014 NY Slip Op. 32498(U)(Sup. Ct. N.Y. Co. Sept. 25, 2014), the court granted the motion to dismiss by a purchaser of corporate assets that was being sued on a successor liability theory. Once again, the plaintiff was frustrated in failing to recover against its contracting party, so it sought to impose contract liability upon a purchaser that acquired customer accounts, accounts receivable and communication equipment, and thereby left the seller as a shell company with no assets to pay plaintiff's debt once the purchase price funds were used for other purposes. The successor liability claim asserted against the purchaser included theories of de facto merger, fraud and implied assumption of liabilities.

Where the acquired company is effectively merged into the purchaser, equity will intervene to require the successor to be responsible for the predecessor's liabilities. The hallmarks of a de facto merger include: (1) continuity of ownership, (2) cessation of ordinary business and dissolution of the acquired corporation, (3) the successor's assumption of liabilities ordinarily necessary for the uninterrupted continuation of the acquired business and (4) continuity of management, personnel, physical location, assets and general business operations.

While the plaintiff adequately pleaded some of these hallmarks for purposes of defeating a motion to dismiss, it failed to show the essential hallmark of continuity of ownership. Plaintiff failed to demonstrate that an actual merger occurred under the guise of an asset sale where the seller's owners did not also become owners of the acquiring corporation.

The court recognized that the reality of an asset sale also doomed plaintiff's fraud claim – the asset sale was not intended to shield the selling company from its creditors, even though the result was to strip the seller of any remaining assets other than the purchase price, which funds were gone before the case could ever reach resolution. Since there was no manifestation of any intention on the part of the buyer to pay the debts of the seller, the theory of implied assumption of liabilities was rejected as well.

These cases illustrate the difficulties a creditor faces when it seeks to extend liability beyond the contracting party. They also demonstrate judicial reluctance to erode the principle of corporate separateness that insulates individual representatives from personal liability and judicial reluctance to impede commerce where companies buy and sell assets in the regular course of business.

So long as the corporate form is respected and an asset sale is not tainted by fraudulent conduct, the courts will generally not permit creditors to draw into the web of litigation nonparties to the contract such as owners/officers or acquiring corporations. As a matter of policy, the litigation burdens placed upon such nonparties not in contractual privity are not outweighed by a rote incantation of the legal elements of a claim bereft of evidentiary facts. As reflected by these recent decisions, the courts will diligently act as gatekeepers to exclude complaints that do not contain sufficient detail to warrant further proceedings.

Kane Kessler represented the prevailing defendants in each of the cases discussed in this article. Kane Kessler's **Litigation practice group** has extensive experience representing clients in commercial litigation matters.

Jeffrey H. Daichman is a Partner in and Co-chairman of the Firm's **Litigation practice group**. Jeffrey can be reached at (212) 519-5142 or jdaichman@kanekessler.com.

CONFIDENTIALITY AGREEMENTS May Violate Whistleblower Rules

In a widely reported development, the Securities and Exchange Commission brought an enforcement against global and engineering company KBR, Inc., alleging that certain of its confidentiality agreements violated the whistleblower provisions of the Dodd-Frank Act. The whistleblower rules are designed to encourage reporting of regulatory violations by providing protective provisions and financial incentives for reporting individuals.

Rule 21-F17(a) under the Securities Exchange Act of 1934 provides that "no person may take any action to impede an individual from communicating…about a possible securities law violation, including enforcing or threatening to enforce a confidentiality agreement." In prior public statements, the SEC has indicated that it intends to focus on any confidentiality agreement that could be understood as an attempt to impede a potential whistleblower's effort to communicate with the SEC. In bringing its action against KBR, the SEC noted that the company had required present and former employees involved with certain internal investigations that involved allegations of securities violations to sign confidentiality agreements prohibiting them from discussing the investigation with anyone outside the company without prior approval, and threatening sanctions, including dismissal, for failure to comply.

The KBR case is notable because there does not appear to be any instance of the company actually attempting to prevent its employees from communicating with the SEC. It was the mere existence of the provisions at issue in the confidentiality agreement that the SEC concluded was sufficient to have the effect of deterring a potential whistleblower from reporting illegal activity to the SEC. And while the relatively modest penalty against KBR of $130,000 with no admission of misconduct is not particularly notable, this case is being understood as an indication of the SEC's intent and willingness to take strong action in this area in the future. Because the SEC has not delineated specific rules regarding which confidentiality agreements may be in violation of Rule 21F-17, and the SEC's public comments have not revealed any intent to limit the rule only to situations involving internal investigations, such as with KBR, it is entirely possible that the SEC may take the position that any type of agreement seeking confidentiality (including employment agreements, separation agreements, settlement agreements and non-compete agreements), may be subject to the rule.

All existing confidentiality agreements with current and former employees and consultants, as well as codes of conduct, internal reporting and compliance policies, and separation and termination agreements, should be reviewed for compliance with Rule 21F-17...

In light of this decision, we are encouraging all of our clients that are subject to the provisions of Dodd-Frank to consult with counsel to determine what steps are appropriate to ensure compliance with the provisions of Dodd-Frank, while continuing to use confidentiality agreements to address legitimate business concerns. All existing confidentiality agreements with

current and former employees and consultants, as well as codes of conduct, internal reporting and compliance policies, and separation and termination agreements, should be reviewed for compliance with Rule 21F-17, including whether any provisions in such documents could be deemed to impliedly cause violation. And consideration should be given to specifically excluding from the definition of confidential information in these agreements any whistleblower-type communications with the SEC. Possible language that can be used includes the following:

"Nothing in this agreement shall be deemed to prohibit me from reporting possible violations of laws or regulations to any government agency or entity including the Securities and Exchange Commission, Congress, any agency Inspector General or from making disclosures or communications that are protected under the whistleblower provisions or federal law or regulation."

In addition, all company personnel administering confidentiality agreements, such as human resource departments, should be educated about the requirements of Rule 21F-17, and communication of any changes to existing agreements should be made to all counterparties to such agreements.

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ALERT

New York City Bans Use of Employment Credit Checks

Following a growing national trend, on April 16, 2015, the New York City Council passed Intro. No. 261-A, 2014, into law, which prohibits employers from discriminating against employees and job applicants based on their credit history. The bill, which becomes effective on September 4, 2015, provides that applicants and employees with poor credit are now among the list of protected classes under the New York City Human Rights Law.

> Specifically, New York City Administrative Code §8-107(23) has been amended as follows:
>
> …[I]t is an unlawful discriminatory practice for an employer, labor organization, employment agency or licensing agency to request or to use for employment purposes information contained in the consumer credit history of an applicant for employment or to retaliate or otherwise discriminate against an applicant or an employee with regard to hiring, termination, promotion, demotion, discipline, compensation or the terms, conditions or privileges of employment based on information in the consumer credit history of the applicant or employee.

The purpose of this law is to ensure that individuals with poor credit history due to unpaid medical bills, student loans, etc. are not denied employment opportunities for which the person may otherwise be qualified. Despite the breadth of this ban, employers still retain the right to run credit checks on candidates for top-level executive positions with fiduciary responsibilities, law enforcement personnel and other security-sensitive positions.

For instance, employers may request credit history for nonclerical positions having regular access to "trade secrets," positions that have signing authority over third-party funds or assets of $10,000 or more (or that involve fiduciary responsibility to the employer with authority to enter financial agreements on behalf of the employer for $10,000 or more), and computer security positions where the regular duties allow the employee to modify digital security systems in place to prevent the unauthorized use of an employer's or client's networks or databases.

The New York City law follows a trend among other states and localities that have banned the use of credit checks for hiring purposes. States that have enacted such a ban include California, Colorado, Connecticut, Hawaii, Illinois, Maryland, Nevada, Oregon, Vermont and Washington, and more states and localities are likely to follow suit. While several states allow credit checks for any position that handles money, New York City's law is more restrictive.

New York City employers should no longer obtain credit checks for applicants or employees, except for those positions specifically exempted by the new law, and should review their hiring practices accordingly. Kane Kessler's **Labor and Employment Law practice group** has experience advising employers on employment practices, including employment applications, testing, interviewing and related matters. Please contact us if you have any questions about whether a particular applicant or employee is still subject to a legal credit check.

The B&B Hardware Case: HOW THE SUPREME COURT HAS UPPED THE ANTE IN TRADEMARK TTAB ACTIONS

The recent United States Supreme Court decision in B&B Hardware, Inc. v. Hargis Industries, Inc. has raised the stakes of filing trademark opposition and cancellation proceedings before the Trademark Trial and Appeal Board (TTAB). In the March 2015 B&B Hardware decision, the Court held that a finding by the TTAB as to likelihood of confusion between two marks will, at least under certain circumstances, preclude a federal court from coming to a different conclusion in a separate trademark infringement lawsuit (between the same parties regarding the same marks). The Court based this holding on long-standing principles of issue preclusion, finding that "[s]o long as the ordinary elements of issue preclusion are met, when the usages adjudicated by the TTAB are materially the same as those before a district court, issue preclusion should apply." Although the B&B Hardware holding was not entirely surprising or unexpected to trademark practitioners, the decision no doubt clarified the law of the land regarding the preclusive effect of TTAB proceedings.

This issue would become relevant in the following circumstances, among others: When an application to register a trademark passes the initial examination phase, it proceeds to the publication phase, at which point any third party which believes it would be damaged by registration of the applied-for mark (e.g., because it is confusingly similar to its own registered mark) can challenge the application by filing an opposition before the TTAB. If the TTAB agrees with the opposing party that a likelihood of confusion exists, the TTAB will deny registration of the applied-for mark. However, the TTAB does not have the power to award monetary damages to the successful opponent or stop the applicant from continuing to use the mark; the TTAB solely decides the issue of whether the mark may register. A trademark owner seeking to stop use of a trademark or be awarded money damages must commence an action in federal court.

Because the TTAB may not stop use of a trademark, some companies have in the past hesitated to start opposition and cancellation proceedings at the TTAB, reasoning that a TTAB proceeding was in many cases not worth the effort because at the end of the day any decision would still be subject to a federal court's determination of the confusion issue. But now, because of B&B Hardware, a TTAB proceeding (which is generally more streamlined and less costly to pursue than federal court litigation) may be more worthwhile, given that a finding of likelihood of confusion by the TTAB might under appropriate circumstances preclude the other company from arguing anew that a mark is not confusingly similar. The flip side of course is also true; if a potential opposing party does not have a strong case of confusing similarity, it should think hard about commencing an opposition or cancellation proceeding because the ramifications are now potentially more severe.

While it remains to be seen exactly what circumstances will allow a court to readjudicate issues determined by the TTAB, one thing is for sure: the B&B Hardware decision has changed the stakes in TTAB proceedings. Depending on the circumstances, companies concerned about the registration and use of trademarks confusingly similar to their own should rethink their TTAB strategies and, at appropriate times, use TTAB proceedings to their greater advantage.

Kane Kessler's **Intellectual Property practice group** has extensive experience in TTAB practice and trademark litigation.

Adam M. Cohen is a Partner and Chair of and **Linda M. Dougherty** is an Associate in the Firm's **Intellectual Property practice group**. Adam can be reached at (212) 519-5146 or acohen@kanekessler.com and Linda can be reached at (212) 519-5144 or ldougherty@kanekessler.com.

UPDATE: On June 9, 2015, the New York City Council passed a "Ban the Box" law which is similar to the New Jersey law and is currently awaiting signature by Mayor DeBlasio. More information will be published in the next issue of the newsletter.

NEW JERSEY'S OPPO

"Ban the Box" and other si

This past summer, the State of New Jersey adopted legislation establishing certain employment rights for persons with a criminal record. The purpose of this legislation, designated the "Opportunity to Compete Act," is to remove obstacles to employment for individuals who are arrested, charged with and/or convicted of crimes, while also increasing the productivity, health and safety of New Jersey communities.

Among the Act's most important provisions is the so-called Ban the Box rule, which prohibits employers from inquiring into an applicant's criminal record until after the initial employment application process. The initial employment application process is defined as the time period beginning when an applicant makes a first inquiry into prospective employment (or when the employer makes an inquiry of an applicant about prospective employment) until the employer conducts a first interview and determines that the applicant is the top choice to fill the vacant position. The law also proscribes employers from posting job openings which indicate that individuals with criminal records will not be considered for employment.

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Though prospective employers may probe into an applicant's criminal history after this initial stage, other provisions of the Act work to limit the adverse impact of information such an examination might reveal. Specifically, employers are prohibited from making adverse employment decisions based on an arrest, a record which has been erased or expunged, a conviction for a disorderly persons offense occurring five (5) or more years ago, or a conviction for a crime in the first through fourth degrees occurring ten (10) or more years ago. However, despite the breadth of this rule, certain crimes such as homicide, burglary, arson and sex offenses, among others, are not subject to these post-initial-process restrictions.

This Act, which covers employers with fifteen (15) or more employees, also lays out factors employers are to consider when weighing the influence an applicant's criminal background has on his/her application. The factors include any information provided

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by the applicant regarding the accuracy of a criminal record or degree of rehabilitation. Employers shall also consider the nature of the offense, how long ago the offense occurred, and the duties and settings of the job. While employers are not expressly required to actually meet with an applicant to discuss criminal history, the law does require a "good faith effort" to do so.

Employers found to violate the provisions of this Act are subject to penalties ranging from $1,000 to as high as $10,000 per violation. The Act does not provide applicants or employees with a private right of action and employers are protected from negligent hiring claims based on an employee's criminal history unless the employer is found to be grossly negligent.

In order to best avoid any conflict with the provisions of this Act, New Jersey employers should avoid making any inquiry into an applicant's criminal record until after the first interview or after a conditional offer of employment is made. All inquiries on employment applications about the application's conviction history should be omitted. Recordkeeping processes should also be implemented so as to allow employers to articulate the impact of an applicant's criminal record, if any, on an employer's employment decision.

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New Jersey is not alone in passing this type of legislation. A number of states have passed similar "Ban the Box" laws, including California, Colorado, Connecticut, Delaware, Hawaii, Illinois, Maryland, Massachusetts, Minnesota, Nebraska, New Mexico and Rhode Island. The New York State legislature has expressed interest in following suit, and certain local cities including Buffalo and Rochester have already passed comparable laws. New York employers may want to consider omitting inquiries about criminal conviction on their employment applications in anticipation that a "Ban the Box" law will be enacted in New York in the not too distant future.

Kane Kessler's **Labor and Employment practice group** has extensive experience advising employers on their employment applications and application processes, including how to handle criminal background checks.

Judith A. Stoll is a Partner and **Michael C. Lydakis** is an Associate in the Firm's **Labor and Employment practice group**. Judith can be reached at (212) 519-5165 or at jstoll@kanekessler.com and Michael can be reached at (212) 519-5163 or mlydakis@kanekessler.com.

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Firm News...

ACHIEVEMENTS

The Firm's **Real Estate practice group** represented a NYC property developer in the purchase of development rights from an adjacent neighbor; in addition to monetary compensation, this neighbor was provided a long-term lease to a portion of the commercial space in the developer's new building along with the right to acquire the space as a condominium unit should the developer complete its plans to convert the building to a condominium regime.

The Firm's **Real Estate practice group** represented a restaurant group in connection with the negotiation of a lease for an 18,000-plus-square-foot restaurant to be located in a building to be constructed.

The Firm's **General Business practice group** represented a restaurant group in raising convertible debt for the expansion of a fast/casual dining concept.

The Firm's **Real Estate practice group** represented a NYC property developer in the negotiation of access agreements with multiple neighboring property owners, to grant the developer access to such neighboring properties in connection with the construction of the new development, as well as for protecting the neighboring properties during such construction.

The Firm's **Corporate and Securities practice group** represented a provider of rapidly deployable expeditionary equipment in the successful completion of its approximately $36 million sale of substantially all of its assets to a leading provider of solutions for government, military, commercial and industrial customers.

The Firm's **Corporate and Securities practice group** represented a leading global provider of a diverse range of safety and survivability products designed for the public safety, military, professional and outdoor markets in the successful completion of its approximately $14.5 million acquisition of a leading distributor of equipment and uniforms for public safety professionals.

The Firm's **Corporate and Securities practice group** represented a NYSE global public company in the successful completion of a $1.1 billion and €350 million private offering of Senior Notes.

The Firm's **Corporate and Securities practice group** represented a provider of diverse consumer products in the successful completion of an amendment to its senior credit facility providing for refinancing certain of its U.S. dollar term and U.S. and multicurrency revolver facilities.

The Firm's **Corporate and Securities practice group** represented a global public company in the successful completion of a $750 million facilities increase under its senior credit facility, providing for incremental increases to term and revolver facilities in dollars and euros.

The Firm's **Corporate and Securities practice group** represented a private equity fund in the successful acquisition of a bourbon distillery.

The Firm's **Labor and Employment practice group** represented the Hotel Association of New York City, Inc., during contract talks with the New York Hotel & Motel Trades Council, AFL-CIO. The negotiations resulted in the successful extension of the New York City industry Wide Collective Bargaining Agreement through June 30, 2026. The Collective Bargaining Agreement covers approximately 30,000 employees working in more than 150 hotels in New York City.

SPEAKING ENGAGEMENT

David R. Rothfeld, head of the Firm's **Labor and Employment Law practice group**, was a speaker at the 9th Annual National H.R. in Hospitality Conference and Expo, held March 16–18, 2015, in Las Vegas, Nevada. David addressed recent developments under the National Labor Relations Act.

JOINED THE FIRM

Jonathan M. Sabin has joined the Firm as an associate in its **Litigation practice group**. Jonathan has experience representing clients in complex litigation before both state and federal courts. Prior to joining the firm, Jonathan was a litigation associate in the New York office of an international law firm and subsequently at a litigation boutique specializing in the trial of complex commercial cases. During law school, Jonathan was editor in chief of the *Journal of Law and Policy*.

Jonathan received his J.D., magna cum laude, in 2010 from Brooklyn Law School. He is admitted to the Bar of the State of New York and to the U.S. District Courts for the Southern and Eastern Districts of New York.

Brendan P. Harney has joined the Firm as an associate in its **Corporate and Securities practice group**. Brendan has experience representing clients in complex merger and acquisition transactions, SEC reporting compliance, equity and debt transactions, public securities offerings, initial public offerings, corporate governance guidance and other general corporate matters. His practice also includes advising public company officers and directors as to their Section 16 reporting obligations and compliance with insider trading regulations.

Prior to joining the firm, Brendan was General Counsel and Corporate Secretary of a NASDAQ-listed healthcare IT company that completed an initial public offering transaction in July 2014.

Brendan received his J.D. from Rutgers School of Law in 2010, and is admitted to practice in the states of New York and New Jersey.

Victor I. Cohen has joined the Firm as an associate in its **Corporate and Securities practice group**. Victor has experience representing clients in complex corporate finance and securities matters.

Prior to joining the firm, Victor represented privately held companies and investors with respect to a wide variety of corporate transactions that included acquisitions, equity and debt placements, joint ventures, consulting and employment agreements, and other general corporate matters. He also represented companies with respect to compliance and reporting requirements to the SEC, FINRA and OTC Markets.

Victor received his J.D. in 2011 from Brooklyn Law School (graduating with a Certificate in Intellectual Property, Media and Information Law) and is admitted to practice in the State of New York.

PRACTICE GROUPS

Bankruptcy, Reorganization and Creditors' Rights
Corporate and Securities
Corporate Investigations
General Business
Intellectual Property
Labor and Employment Law
Litigation
Matrimonial
Mediation
Real Estate
Trusts, Estates and Taxation

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