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Reporting on Significant Court of Appeals Opinions and Developments in New York Practice

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CASE LAW DEVELOPMENTS

Are Large Industrial Coke Ovens "Products" for Strict Liability Purposes?

Majority of Court of Appeals Insists That the Size and Physical Characteristics of the Ovens Were Not Determinative

The issue presented in *Matter of Eighth Jud. Dist. Asbestos Litig.*, 2019 N.Y. Slip Op. 04640 (June 11, 2019), was whether the defendant carried its burden on summary judgment to establish that large industrial coke ovens situated in the decedent's workplace were *not* "products" for strict liability purposes, so as to absolve the defendant of a duty to warn. A split Court of Appeals ruled that it did not meet its burden.

The plaintiff, as administrator of the decedent's estate, was seeking damages for injuries allegedly sustained as a result of the decedent's exposure, as a Bethlehem Steel employee, to coke oven emissions. The plaintiff sued the defendant, Honeywell International, Inc. (Honeywell), as successor in interest to Wilputte Coke Oven Division of the Allied Chemical Corporation (Wilputte), which designed and built coke oven batteries. A coke oven burns coal to create coke, which is used as a fuel in steel production. A coke oven is roughly 13 feet high and 1.5 feet wide. A coke oven battery is a series of individual ovens situated in a row to create a wall of the battery structure in which the ovens are housed. The coke oven battery construction process here took over 18 months, entailing almost 1.5 million labor hours to complete. The batteries were situated on the coke oven plant grounds, which included other structures.

Honeywell moved for summary judgment, arguing that the coke ovens were not products, and thus it could not be strictly liable as a products manufacturer. In addition, it maintained that Wilputte's contract to design and build the ovens was a service contract, not subject to strict products liability. The trial court denied the motion, but the Appellate Division reversed.

A majority of the Court of Appeals reversed the Appellate Division. It noted that while products liability theories include design defect, manufacturing defect, and failure to warn claims, here they were only dealing with the failure to warn; there is no clear definition of a "product" under the case law, but, in many cases, industrial machines have been assumed to be products; and the physical characteristics of a machine are *not* the sole criteria in determining whether it is a "product."

The Court instead was concerned with whether the defendant manufacturer owed a duty to warn, which focuses on "factors such as a defendant's control over the design of the product, its standardization, and its superior ability to know – and warn about – the dangers inherent in the product's reasonably foreseeable uses or misuses." *Id*. at*3 (citation omitted). Here, the Court emphasized that Wilputte was an expert designer and manufacturer in the marketing and selling of coke ovens; the oven designs were "complex and unique to Wilputte's enterprise"; it exerted full control over how the coke ovens were built; and the process employed was a standard one despite any requests or alterations (as to the scale or specifications of the battery) that Bethlehem may have made. In addition, Wilputte placed the ovens into the stream of commerce and "derived financial benefit from its role in the production process." It was the sole distributor of its ovens and was a manufacturer in this context.

The majority added that Wilputte "was in the best position to assess the safety of the coke ovens because of its superior knowledge regarding the ovens' intended functionality," a significant factor in determining whether there is a duty to warn. *Id*. at *4. Conversely, there was no evidence that Bethlehem or the decedent was in a better position to understand the coke ovens' inherent dangers. The Court rejected defendant's arguments that the plaintiff's failure to identify a specific oven component part as defective rendered the allegations insufficient (the alleged defect is "in the failure to warn of the whole product's dangerous 'intended use or a reasonably foreseeable unintended use'"); that there is a bright line distinction between products and the buildings here (real property can be subject to strict li-

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ability claims); and that the contract between Bethlehem and Wilputte, which was alleged to be a predominantly service-oriented one, precluded liability here (a service component in a sale "does not mean that the furnished item is not a product to which a duty to warn may apply").

The dissent, however, focused on the physical characteristics of the coke ovens, which it asserted "strongly militate" in favor of its conclusion that they were not products. It pointed out that "unlike any item this Court has previously considered," coke ovens are not mass produced, marketed, or distributed and are only sold to large steel companies. Moreover, coke ovens cannot be viewed as individual separate products in that they cannot function outside of coke oven batteries (each containing dozens of coke ovens).

The dissent similarly emphasized that

> [i]n contrast with the typical consumer of mass-produced products, Bethlehem—as a large steel manufacturer that employed engineers specializing in coke oven battery operations—was uniquely situated to understand the hazards associated with coke production. Bethlehem's engineers dictated to Wilputte the number of ovens and total production required for its Lackawanna plant, provided input on the design plans, and approved or rejected the design and construction plans submitted by Wilputte. . . . The practical reality is that both Wilputte and Bethlehem were sophisticated entities, with extensive knowledge about the use and construction of these structures. . . . Bethlehem was in a superior position to control the use of the ovens by its employees, as well as to absorb the risk of loss by procuring insurance to cover any resulting injuries. Further, Bethlehem had an equal, if not greater, incentive to minimize liability and danger to its employees (citations omitted).

Id. at *9.

The dissent expressed its fear that the majority's opinion will expand products liability "leading to future claims that the builders of single-use facilities or structures are all manufacturers of products, a result that would unreasonably expose builders of such structures to previously uncontemplated liability and that would be completely divorced from the public policy considerations underlying our products liability jurisprudence." *Id*.

Insurers Can Withhold Payment of Assigned No-Fault Claims to Medical Service Corporation Improperly Controlled by Non-Physicians

No Requirement That Insurers Prove Common-Law Fraud

In *State Farm Mut. Auto. Ins. Co. v. Mallela*, 4 N.Y.3d 313, 319 (2005), the New York Court of Appeals ruled (on a certified question from the Second Circuit Court of Appeals) that under no-fault, insurers can "withhold payment for medical services provided by fraudulently incorporated enterprises to which patients have assigned their claims." The Court found that there was a "willful and material failure to abide by" licensing and incorporation statutes. *Id*. at 321.

More recently, in *Andrew Carothers, M.D., P.C. v. Progressive Ins. Co*., 2019 N.Y. Slip Op. 04643 (June 11, 2019), the Court clarified its *Mallela* holding, concluding that it did *not* require that there be a common-law fraud finding in order for an insurer to rightfully withhold payments to a medical service corporation that was improperly controlled by non-physicians.

The plaintiff, Andrew Carothers, M.D., P.C., was a professional service corporation formed by a radiologist, Andrew Carothers, providing MRI services. It subleased three MRI facilities and rented its equipment at "exorbitant fees" from companies owned and operated by a non-physician, Hillel Sher, who had the sole right to terminate the leases. Sher also introduced Carothers to another non-physician, Irina Vayman, who was hired by Carothers as his executive secretary and who wrote all checks from plaintiff's bank account. The Court noted that "Carothers's oversight of the provision of medical services was practically nonexistent"; that there was no "quality control" in the practice; and that plaintiff had no books or records. *Id*. at *1.

Most of the scans performed were of patients allegedly injured in car accidents, who assigned their right to receive first-party no-fault insurance benefits to the plaintiff. In turn, the plaintiff then billed insurance companies on the assigned claims to recover payment. Plaintiff entered into a loan and security agreement with Medtrex, again introduced by Sher. Vayman, not Carothers, acted as the authorized borrower's representative. Medtrex advanced loans to the plaintiff weekly, and insurance company payments were used to pay Medtrex loans. Carothers's salary was less than Vayman's, and huge amounts were funneled through plaintiff to Sher and Vayman.

When the insurance companies stopped paying, the plaintiff brought thousands of actions to recover unpaid claims of assigned benefits, including this action against Progressive Insurance Company. The defendants claimed that the plaintiff could not seek reimbursement because it was controlled by unlicensed non-physicians. They also relied on *Mallela*, arguing that Carothers was the plaintiff's nominal owner, and that the professional corporation was really owned and controlled by Sher and Vayman. Finally, the defendants asserted that Carothers did not personally engage in the practice of medicine through the plaintiff.

While non-parties Sher and Vayman were both deposed, they invoked their Fifth Amendment privilege and refused to answer almost all the questions posed. The Civil Court conducted a consolidated joint trial, including 54 insurers, at which Sher's and Vayman's deposition testimony, including their repeated Fifth Amendment invocations, was read to the jury. (It was agreed that they were "unavailable" to testify under CPLR 3117(a)(3).) Multiple witnesses testified that (i) the "plaintiff's profits were funneled to Sher and Vayman, through grossly inflated equipment lease payments to Sher's companies and through the transfer of plaintiff's funds to personal accounts" (*Id*. at *2); (ii) Carothers was not in control of the plaintiff and had no real involvement with the company's management; and (iii) the lease agreements were not mutually beneficial to the parties and were thus not made at arm's length. Carothers could not account for the transactions described by these insurance company witnesses.

In summation, the insurance company lawyers repeatedly referred to Sher's and Vayman's invocation of the Fifth Amendment at their depositions. The trial court denied the plaintiff's counsel's request for a "traditional elements

of fraud" jury instruction, including fraudulent intent. The trial court charged the jury that it could draw an adverse inference against the plaintiff based on Sher's and Vayman's Fifth Amendment invocation. It also gave the jury a list of 13 factors to consider in determining whether Vayman and Sher "were de facto owners of or exercised substantial control over the plaintiff." *Id*.

The jury found for the defendants, and the trial court denied plaintiff's motion to set aside the verdict and for a judgment as a matter of law or alternatively to set aside the verdict as against the weight of the evidence or in the interest of justice and for a new trial. *See* CPLR 4404(a).

The Court of Appeals noted here that a professional service corporation can be owned or controlled only by licensed professionals; that New York law "prohibits unlicensed individuals from organizing a professional service corporation for profit or exercising control over such entities"; and that such corporate practice of medicine can "create ethical conflicts and undermine the quality of care afforded to patients." *Id*. at *3.

The Court held that the trial court did not err in *not* instructing the jury that it had to find fraudulent intent, or, at least, conduct "tantamount to fraud." It insisted that nothing in the relevant regulations or in *Mallela* required an insurance company to prove that the professional service corporation engaged in common-law fraud.

> A corporate practice that shows "willful and material failure to abide by" licensing and incorporation statutes may support a finding that the provider is not an eligible recipient of reimbursement under 11 NYCRR 65-3.16 (a) (12) without meeting the traditional elements of common-law fraud. Nor is a jury required to evaluate the extent to which corporate misconduct approximates fraud. The no-fault insurance regulations make providers ineligible for reimbursement when their violations of the cited statutes are more than merely technical and "rise to the level of" a grave violation such as fraud. . . . Here, the jury's finding that plaintiff was in material breach of the foundational rule for professional corporation licensure — namely that it be controlled by licensed professionals — was enough to render plaintiff ineligible for reimbursement under 11 NYCRR 65-3.16 (a) (2) (citations omitted).

Id. at *4.

Court Punts on Whether Nonparty's Invocation of Fifth Amendment Can Trigger Adverse Inference Against a Party in a Civil Action

Some of you may be wondering about the trial court's charge in *Andrew Carothers*, permitting the jury to draw an adverse inference against the plaintiff based on Sher's and Vayman's invocation of the Fifth Amendment. An individual can refuse to answer questions in a *civil* action, if the answers could incriminate that person in a future *criminal* proceeding. However, a party's failure to answer questions in a civil case "may be considered by a jury in assessing the strength of the evidence offered by the opposite party on the issue which the witness was in a position to controvert." *Marine Midland Bank v. John E. Russo Produce Co.*, 50 N.Y.2d 31, 42 (1980). Thus, a party's invocation of the Fifth Amendment privilege against self-incrimination may be used to draw an adverse inference against that party in the civil action.

What the Court of Appeals has not previously ruled on concerned the situation in our case: whether a *nonparty's* invocation of the Fifth Amendment can result in an adverse inference against a *party*. The Appellate Division had held that no such inference could be drawn. However, it found the trial court's error to be harmless. While the Court of Appeals agreed with the Appellate Division that the error was harmless because there was "no reasonable view of the evidence under which plaintiff could have prevailed," it felt it had "no occasion" to finally resolve the underlying issue. *Andrew Carothers, M.D., P.C.*, 2019 N.Y. Slip Op. 04643 at *5.

Court Unanimously Holds That College Abused Its Discretion as a Matter of Law in Refusing to Grant Petitioner a Three-Hour Adjournment of Administrative Hearing to Permit Counsel to Attend

Reverses Appellate Division Order

The Court of Appeals decision in *Matter of Bursch v. Purchase Coll. of the State Univ. of N.Y.*, 2019 N.Y. Slip Op. 04449 (June 6, 2019), is very brief, so resorting to the Appellate Division decision is necessary, especially in view of the rather troubling fact pattern.

On September 24, 2014, the petitioner, a Purchase College student, was charged with four violations of the student code of conduct, arising out of allegations that he sexually assaulted another student. The violations included one instance of underage drinking and three instances of sexual assault. The maximum administrative punishment facing the petitioner was expulsion. The next day, the petitioner met with Melissa Jones, Purchase's Director for Community Standards, admitted that he was responsible for underage drinking, but sought an administrative hearing for the other charges before a board consisting of three faculty and/or professional staff. Petitioner was advised that he had the right to have an "advisor" of his choice at the hearing, which could be an attorney or a parent. If an attorney was chosen, however, he or she could only interact with the petitioner. On September 30, Jones emailed the petitioner that her office was having trouble scheduling the hearing that week "due to witness unavailability and the Jewish holiday." Twenty minutes later, petitioner's attorney contacted Purchase to advise that he had been retained. Two days later, on October 2, in the afternoon, petitioner was notified of the hearing time, October 7 at 9:00 a.m., a little more than two business days after the notice was sent. Within four hours, petitioner's attorney called the college, but Jones refused to speak to him until the petitioner signed and returned a Family Education Rights and Privacy Act of 1974 (FERPA) release form. Petitioner's attorney's call to the college the next day was also refused. On Sunday, October 5, 2014, the petitioner sent the form in, and his attorney again contacted Purchase to request a three-hour delay of the hearing due to a scheduling conflict. That request was denied. Ultimately, the hearing proceeded without the petitioner's attorney and without live testimony from petitioner's fact witnesses – they were compelled to provide written statements – because they were in class at the time of the hearing. All the

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complainant's character witnesses appeared in person at the hearing, which took less than two hours. Less than five hours after the start of the hearing, the disciplinary hearing's findings were transmitted to the petitioner, finding petitioner responsible for all the disciplinary charges. He was permanently expelled from the college and directed to leave the campus within three days, at which time he would be subject to criminal arrest.

Petitioners brought this article 78 proceeding alleging that the college's summary denial of his request for a three-hour adjournment to permit counsel to attend the hearing constituted an abuse of discretion and violated his due process rights. Pursuant to CPLR 7804(g), the Supreme Court transferred the proceeding to the Appellate Division.

In a split decision, a majority of the Appellate Division held that:

> Due process does not require colleges to provide accused students with legal representation at disciplinary hearings. Purchase's rules, the legality of which the petitioner does not challenge, allow for an attorney to be present and advise an accused student at a disciplinary hearing, but not to represent the student or interact with anyone at the hearing other than the accused student. Here, the petitioner had hired an attorney as of September 30, 2014. As noted above, the petitioner was notified on September 30, 2014, that the hearing would likely be scheduled for October 6 or 7, and was informed of the exact time of the hearing on October 2, 2014. He alleges that he did not request an adjournment until 'on or about' October 5, 2014, which was two days before the date of the hearing. Under these circumstances, contrary to the suggestion of our dissenting colleagues, the petitioner was not denied the opportunity to have an attorney present at the hearing (citations omitted).

164 A.D.3d 1324, 1328–29 (2d Dep't 2018).

The dissent found that the college had "violated the petitioner's right to due process and abused its discretion when it denied his timely request for a three-hour adjournment of the administrative hearing so that his attorney could attend. Given the gravity of the administrative charges facing the petitioner, and the threat of additional criminal charges stemming from an active police investigation, the petitioner's right to secure the assistance of his designated attorney at the administrative hearing was fundamental." *Id*. at 1329.

The Court of Appeals unanimously reversed the Appellate Division order, finding that the college abused its discretion as a matter of law by failing to grant petitioner's request for a three-hour adjournment. Thus, the Court remitted the matter to the Appellate Division with directions to remand to the college for a new disciplinary hearing.

I would like to thank you for your meaningful and encouraging comments and suggestions. They are greatly appreciated. Wishing you and your families, a restful, peaceful and enjoyable summer.

David

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