OPINION NO. 1580

Syllabus:

1. In enforcing paragraph (H), Section 1151.292, Revised Code, the superintendent of building and loan associations may not as a matter of course disregard the corporate entity of a borrowing corporation whose officers or stockholders are officers, directors or employees of the lending building and loan association.

2. The superintendent of building and loan associations may disregard the corporate entity in a specific case when in his judgment such action is necessary to enforce the policy of paragraph (H), Section 1151.292, Revised Code.

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To: Lyle L. Herbold, Superintendent of Division of Building and Loan Assoc., Columbus, Ohio

By: William B. Saxbe, Attorney General, December 7, 1964

I am in receipt of your request for my opinion which is as follows:

> "In order to properly administer the affairs of building and loan associations chartered by the State of Ohio, it is my desire to submit to you for opinion the following questions:
>
> "Is a building and loan association authorized to make a mortgage loan to a corporation when a director, officer, attorney, or employee of the association owns eighty percent of the corporation's total outstanding stock, without obtaining the written approval of the Superintendent of Building and Loan Associations pursuant to Section 1151.292 (H) of the Revised Code?
>
> "Is a building and loan association authorized to make a mortgage loan to a corporation when two directors of the association own all of the corporation's total outstanding stock, without obtaining the written approval of the Superintendent of Building and Loan Associations pursuant to Section 1151.292 (H) of the Revised Code?"

Paragraph (H), Section 1151.292, Revised Code, provides:

> "(H) Without the written approval of the superintendent, no association shall make any loan on real estate to any of its officers, directors, or employees, or buy from or sell to them any real estate, mortgage loan, or other kind of investment, except that with

> the approval of the directors not interested in such loan except as directors, any director, officer, or employee of the association may be granted a loan on his own home. For purposes of this division 'employee' includes any attorney or firm of attorneys regularly serving the association in the capacity of attorney at law."

It will be seen that the restriction in the paragraph reaches, on its face, only loans by a building and loan association to its officers, directors or employees. In each of the two hypothetical situations you present the proposed loan is not to officers, employees or directors of the building and loan association but is to a corporation whose directors or officers or employees are also directors or officers or employees of the building and loan association. A corporation is by law an entity separate and distinct from its stockholders and officers and employees and it would ordinarily seem that the loans, under any of the hypothetical situations presented, may be made without the approval of the superintendent of building and loan associations. The question you raise of course is whether under these circumstances the corporate entity may be disregarded and the loans considered as being directly to the officers or stockholders as the case may be.

The doctrine of "disregard of the corporate entity" or, as it is sometimes referred to, "piercing the corporate veil" is a legal theory introduced in appropriate cases for purposes of public convenience and to protect against wrong. It was first used in this country in Bank of the United States v. Deveaux, 5 Cranch 61, 3 L.ed. 38 (1809), in which it was concluded that a corporation cannot be a citizen for purposes of determining the jurisdiction of the courts of the United States. Since the Deveaux case the doctrine has become a part of the law in all states including Ohio. E.g. State, ex rel. Watson v. Standard Oil Co., 49 Ohio St., 137; Auglaize Box Board Co. v. Hinton, 100 Ohio St., 505. While it is not within the scope of this opinion to catalog the many cases in which the corporate entity has been disregarded, broadly speaking the courts have done so when: (1) to treat the acts as those of the corporation alone would cause an inequitable result; (2) the corporate form is used to evade the effect of a statute or law. If the corporate structure is to be disregarded in the application of the provisions of paragraph (H), Section 1151.292, supra, it is on the basis that not to disregard the entity would circumvent these provisions.

Despite the willingness of most courts to disregard the corporate entity, it is clear that this theory is to be relied on only in special circumstances. See North v. Higbee Co. 131 Ohio St., 507; United States v. Elgin, Joliet and Eastern Ry., 298 U.S. 492; 26 Iowa L.R., 350. The reason is of course that it is in direct conflict with the basic principle upon which the whole law of corporations is based. In addition, where the question is of a statutory violation the result sought by disregarding the corporate structure could be as easily -- and in most instances more logically--reached by legislative change.

Judicial disregard of the corporate entity in the enforcement of public law has, generally speaking, been based ostensibly on the presence of two conditions. The first is a unity of interest such that the individuality of the corporation and its officers and stockholders has ceased. The second is the formation of the corporation for the purpose of evading the law. See Auglaize Box Board Co. v. Hinton, supra; The State, ex rel. The Johnson and Higgins Co. v. Safford, 117 Ohio St., 576; Pearson v. All Borg, 23 F. Supp., 837,842. Despite their rationale, analysis of the decisions indicates that in most instances the presence of either or both of these conditions is not alone determinative of the application of the doctrine. Cases based on unity of interest seem actually explainable on a theory of agency. While those purportedly based on intent to evade the law seem by expression to beg the question. The corporate structure was invented--and is sanctioned in law--to take advantage of privileges unvailable to individuals, and it seems anomolous to destroy its efficacy because of this intent alone.

The real test and the one actually applied by the courts in this area appears to be whether preserving the corporate aegis will defeat the policy of the law. This of course depends upon the purpose for the law, and it means that each law presents a separate problem in itself.

It should be noted that paragraph (H), Section 1151.292, supra, does not prohibit loans in which the officers, directors or employees of the lending institution have an interest, it merely places a condition on such loans. Which suggests to me that the purpose for this section is to prevent poor risk loans occasioned by the personal interest of the officers or directors of the building and loan association. This being so the degree of interest of a building and loan officer, etc. in a loan, or the purpose for which the corporate borrower was formed, is less important than the financial position of the borrowing corporation. For example, an adequately secured loan to a corporation owned entirely by an officer of the building and loan association would not do violence to the result sought by this statutory restriction, while a loan to a financially unsound corporation owned in part by an officer of the lending institution would. It has been determined that undercapitalization is a basis for disregarding the corporate entity. Automotziz Del Golfo De California v. Resnick. 47 Cal. 2d 792, 306 P. 2d 1. See also 51 Har. L.R., 1373.

While consideration to this point has been of judicial use of the doctrine of disregard of the corporate entity, I am of the opinion that it may be used by the superintendent of building and loan associations, in appropriate cases, where necessary to "see that the laws relating to building and loan associations * * * are executed and carried out" within the meaning of Section 1155.02, Revised Code.

You have asked me specific hypothetical questions which I am unable to answer. The conditions under which the corporate entity may be disregarded in enforcing this statute will necessarily vary according to the circumstances of each case. A determination can only be made on the basis of all of the facts. And while generalization is difficult I can advise you that you are justified in disregarding the corporate structure where

not to do so in a specific case will alter the effect of the law.

I am cognizant that this places a rather onerous burden upon the division of building and loan associations but I cannot for this reason conclude that you may sweep the corporate veil aside in every case.

To this point I have made no reference to my prior opinion, Opinion No. 1155, Opinions of the Attorney General for 1957, the second branch of the syllabus of which reads:

> "2. Where the superintendent of building and loan associations finds that a corporation, chartered for real estate development or other purposes, whose officers, directors and shareholders are substantially the same as those of an Ohio chartered building and loan association, was organized or is being used to evade or circumvent the requirement of Section 1151.292, (H), Revised Code, that the written approval of the superintendent be given before an association loans money to or enters into other specified transactions with its officers, directors or employees, he may properly conclude that such transactions without the written approval of the superintendent are in violation of said sections."

The hypothesis upon which this conclusion was predicated indicated that the corporation was but the "alter ego" or agent of the officers and stockholders. This remains my conclusion under these circumstances. I merely add here by way of explanation that the superintendent should examine each case from the standpoint of whether the policy of this provision will otherwise be destroyed.

Therefore, it is my opinion and you are advised that:

1. In enforcing paragraph (H), Section 1151.292, Revised Code, the superintendent of building and loan associations may not as a matter of course disregard the corporate entity of a borrowing corporation whose officers or stockholders are officers, directors or employees of the lending building and loan association.

2. The superintendent of building and loan associations may disregard the corporate entity in a specific case when in his judgment such action is necessary to enforce the policy of paragraph (H), Section 1151.292, Revised Code.