How Can My Corporate Veil Be Pierced? The Bullet Point: Volume 2, Issue 14

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The Bullet Point is a biweekly update of recent, unique, and impactful cases in Ohio state and federal courts in the area of commercial litigation.

Ohio v. American Express Co., Slip. Op. No. 16-1454 (June 25, 2018).

Several states sued American Express for violating the anti-steering provisions of the Sherman Antitrust Act. American Express is a credit card company that provides a "two-sided platform" – that is, it provides services to two groups, cardholders and merchants, that both rely on American Express to intermediate between them. This relationship requires a balancing act of the prices charged to each group, in order to maximize the service that American Express offers and to allow it to compete with rivals. To compete, American Express focused on cardholder spending and offered a significant rewards program; however, the program required American Express to continually invest in it, leading the company to charge merchants more. This created tension with merchants, who, to avoid the higher fees, would sometimes dissuade cardholders from using American Express cards at the point of sale, known as "steering." To combat this practice, American Express placed an anti-steering provision in its merchant contracts.

Various states sued for this practice, contesting the anti-steering provision as a violation of the Sherman Antitrust Act. The district court agreed but the Second Circuit Court of Appeals reversed. The United States Supreme Court then affirmed that decision, finding that the anti-steering provision did not violate the Sherman Antitrust Act.

The Bullet Point: Section 1 of the Sherman Act prohibits "unreasonable restraints" on trade. Restraints may be unreasonable in one of two ways—unreasonable per se or unreasonable as judged under the "rule of reason." The rule of reason requires courts to conduct a fact-specific assessment of "market power and market structure . . . to assess the [restraint]'s actual effect" on competition. The goal is to "distinguis[h] between restraints with anticompetitive effect that are harmful to the consumer and restraints stimulating competition that are in the consumer's best interest." Courts apply a three-step, burden-shifting test to see if a restraint violates the rule of reason. First, the plaintiff has the initial burden to prove that the challenged restraint has a substantial anticompetitive effect that harms consumers in the relevant market. If the plaintiff carries its burden, then the burden shifts to the defendant to show a procompetitive rationale for the restraint. If the defendant makes this showing, then the burden shifts back to the plaintiff to demonstrate that the procompetitive efficiencies could be reasonably achieved through less anticompetitive means. Here, the Court found that plaintiffs failed to carry their initial burden because the plaintiffs only focused on the increased fees to merchants and ignored the other side of the two-sided platform and the benefits that were afforded to cardholders under the program.

City of Cleveland v. Embassy Realty Investments, Inc., 8th Dist. Cuyahoga No. 105091, 2018-Ohio-2513.

This was an appeal of a trial court's decision to grant the city of Cleveland judgment against a company and its owner for violating various housing code ordinances. The appellant registered the trade name Embassy Realty Investments (Embassy) and used that company to purchase vacant commercial buildings. He purchased a former church that had been declared a public nuisance by the city a few years prior. Once he bought the property, the City began sending him notices of condemnation and demolition. Thereafter, he incorporated Embassy and then transferred title of the disputed property to it. After a number of legal disputes, the City eventually demolished the property. It then filed suit against Embassy and Appellant individually for the costs associated with the demolition. Regarding Appellant, the City sought to hold him liable under a "piercing the corporate veil" theory. The trial court eventually granted the City's motions and the Appellant appealed.

On appeal, the Eighth Appellate District affirmed in part and reversed in part. Specifically, the court found that the trial court erred in finding Appellant individually liable under a piercing the corporate veil theory, noting that there was a factual dispute as to whether the Appellant exercised control over the company as required to be held individually liable.

The Bullet Point: "[A] fundamental rule of corporate law is that, normally, shareholders, officers, and directors are not liable for the debts of the corporation." In *Dombroski v. WellPoint, Inc.*, 119 Ohio St.3d 506, 2008-Ohio-4827, 895 N.E.2d 538, the Ohio Supreme Court explained the exception to this general principle, noting that shareholders are not absolutely immune from liability for the actions of their corporations, and that the "veil" of a corporation may be pierced where it would be unjust to allow a shareholder to hide behind corporate protections. Piercing the corporate veil is a rare exception and usually reserved for cases of fraud or other exceptional circumstances. Three elements must be met to pierce the corporate veil: (1) control over the corporation by those to be held liable was so complete that the corporation has no separate mind, will, or existence of its own; (2) control over the corporation by those to be held liable was exercised in such a manner as to commit fraud or an illegal act against the person seeking to disregard the corporate entity; and (3) injury or unjust loss resulted to the plaintiff from such control and wrong.

By design, it is very difficult to pierce the corporate veil, so companies should be very wary when attempting to do so. If you are concerned about future collectability or liability, securing a personal guarantee may be more effective.

Phoenix Lighting Group LLC v. Genlyte Thomas Group LLC, 9th Dist. Summit No. 28082, 2018-Ohio-2393.

The owner and operator of two lighting companies entered into negotiations with two employees to sell Phoenix, one of the companies. The parties entered into confidentiality agreements during the negotiating process. During that process, confidential information about Phoenix was disclosed. While the negotiations were ongoing, the employees started their own lighting agency. As part of that process, the company for which they would be selling lights in the Cleveland market asked for a business plan. The employees utilized information they learned in negotiating with Phoenix for their plan and also contemplated hiring various employees of Phoenix. When Phoenix's owner found out, the employees ultimately resigned and proceeded with their lighting agency.

Phoenix then filed suit, alleging various business-related torts. The matter then proceeded to a jury trial that eventually found for Phoenix on a number of claims. Specifically, the jury found that the new lighting agency had tortiously interfered with Phoenix's business relationships, misappropriated Phoenix's trade secrets, and participated in a civil conspiracy to tortiously interfere with Phoenix's business relationships, to breach a duty of loyalty owed to Phoenix, and to misappropriate Phoenix's trade secrets. Ultimately, the jury awarded Phoenix in excess of $1.6 million in compensatory damages and more than $7 million in punitive damages. The trial court reduced that amount to $2.7 million and awarded almost $4 million in attorneys' fees. The defendants appealed and on appeal, the Ninth Appellate affirmed in part and reversed in part. In so ruling, the court affirmed various findings by the jury that the defendants had tortiously interfered with business relationships, misappropriated trade secrets, and engaged in a conspiracy. It reversed the trial court's application of a punitive damages cap because it had applied the wrong one under statute.

The Bullet Point: "The elements of 'tortious interference with a business relationship are: (1) a contractual or business relationship; (2) knowledge of the relationship by the tortfeasor; (3) an intentional and improper act by the tortfeasor preventing formation of a contract, procuring breach of a contract, or termination of a business relationship; (4) lack of privilege on the part of the tortfeasor; and (5) resulting damage.'" "Tortious interference with a business relationship does not require the breach of contract, rather it is sufficient to prove that a third party does not enter into or continue a business relationship with the plaintiff." However, the tortfeasor must act maliciously before a party can recover under a theory of tortious interference with a business relationship.

To that end, courts consider the following factors: (a) the nature of the actor's conduct, (b) the actor's motive, (c) the interests of the other with which the actor's conduct interferes, (d) the interests sought to be advanced by the actor, (e) the social interests in protecting the freedom of action of the actor and the contractual interests of the other, (f) the proximity or remoteness of the actor's conduct to the interference, and (g) the relations between the parties.

Boehm v. Black Diamond Casino Events LLC, 1st Dist. Hamilton No. C-170339, 2018-Ohio-2379.

This was an appeal of a trial court's decision to grant a motion for involuntary dismissal by the plaintiff. Black Diamond operates a casino-games-themed events business for corporate and private parties. Roger Boehm, Jr., a former employee of Black Diamond, approached the owners about buying two of the four members' interests in Black Diamond. During the due diligence process, Mr. Boehm signed a nondisclosure agreement. He then obtained confidential information from Black Diamond, such as customer lists and tax and financial information. Mr. Boehm eventually decided to move forward with the purchase, but members of Black Diamond refused to sell. Mr. Boehm sued, and Black Diamond filed counterclaims for breach of contract and violation of the Ohio Uniform Trade Secrets Act. At a bench trial, the trial court orally granted a request for dismissal by Mr. Boehm, and Black Diamond appealed. The First Appellate District reversed, finding that the trial court erred in finding that Black Diamond's client lists and financial information were not trade secrets.

The Bullet Point: Under Ohio law, a trade secret is defined as information, including the whole or any portion or phase of any scientific or technical information, design, process, procedure, formula, pattern, compilation, program, device, method, technique, or improvement, or any business information or plans, financial information, or listing of names, addresses, or telephone numbers, that satisfies both of the following:

(1) It derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use.

(2) It is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

The following factors should be considered when analyzing a trade secrets claim: (1) The extent to which the information is known outside the business; (2) the extent to which it is known to those inside the business, i.e., by the employees; (3) the precautions taken by the holder of the trade secret to guard the secrecy of the information; (4) the savings effected and the value to the holder in having the information as against competitors; (5) the amount of effort or money expended in obtaining and developing the information; and (6) the amount of time and expense it would take for others to acquire and duplicate the information.

Customer lists are an intangible asset that is presumptively a trade secret when the owner takes measures to prevent its disclosure in the ordinary course of business. Likewise, taxes and quarterly profit-and-loss statements could constitute trade secrets assuming they are not known to those outside the business, not available to other people outside the business absent a nondisclosure agreement, and were kept confidential by a company.