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Piercing the Corporate Veil in Federal Courts: Is Circumvention of a Statute Enough?

A strong public policy exists in the United States to protect shareholders from a corporation's debts. This is accomplished by employing the legal fiction that the corporation is an entity, separate and distinct from its shareholders.¹ The policy is often referred to as "limited liability."² Shareholders are allowed to make capital contributions to corporations without subjecting their personal wealth to the risks of the business³ and are subject only to losing the amount of capital they have actually invested in the corporation.⁴

In appropriate circumstances, however, the court will cast aside this legal fiction and disregard the corporate entity, thereby holding shareholders liable for the corporation's debts.⁵ While the rationale for disregarding the corporate entity varies, the decision is supported when to hold otherwise would promote fraud, illegality, or injustice or would defeat public policy.⁶ The action taken by the courts has been termed "piercing the corporate veil."⁷ In theory, the piercing doctrine applies

1. See H. BALLANTINE, CORPORATIONS §122, at 293 (rev. ed. 1946); 1 W. FLETCHER, CYCLOPEDIA OF CORPORATIONS §25, at 100 (rev. ed. 1974) [hereinafter cited as FLETCHER]; H. HENN, LAW OF CORPORATIONS §146, at 251 (2d ed. 1970) [hereinafter cited as HENN].

2. HENN, *supra* note 1, §73; Campbell, *Limited Liability for Corporate Shareholders: Myth or Matter of Fact*, 63 KY. L.J. 23 n.43 (1974); Manne, *Our Two Corporation Systems: Law and Economics*, 53 VA. L. REV. 259, 262 (1967); Meiners, Mofsky & Tollison, *Piercing the Veil of Limited Liability*, 4 DEL. J. CORP. L. 351, 353 (1979).

3. Subscribers and shareholders will normally be liable to the corporation or its creditors for the full consideration for which its shares are issued. MODEL BUSINESS CORP. ACT §25 (1979).

4. These liabilities are essentially for the members' debts, not the corporation's. A. CONRAD, CORPORATIONS IN PERSPECTIVE §270 (1976) [hereinafter cited as CONRAD].

5. See *Hay v. Commissioner*, 145 F.2d 1001, 1005 (4th Cir. 1944), *cert. denied*, 324 U.S. 863 (1945); *Southern Electric Sec. Co. v. State*, 91 Miss. 195, 207 44 So. Rptr. 785, 790 (1907); BALLANTINE, *supra* note 1, §122, at 293; FLETCHER, *supra* note 1, §41.

6. The classic statement used by many courts was that made by Judge Sanborn in *United States v. Milwaukee Refrigerator Transit Co.*, 142 F. 247, 255 (E.D. Wis. 1905):

If any general rule can be laid down in the present state of authority, it is that a corporation will be looked upon as a legal entity as a general rule, and until sufficient reason to the contrary appears; but, when the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud, or defend crime, the law will regard the corporation as an association of persons.

7. 1A H. BALLANTINE & G. STERLING, CALIFORNIA CORPORATION LAWS §295 (4th ed. 1981); HENN, *supra* note 1, §146, at 250. Other catchwords used by judges include "alter ego," "instrumentality," "dummy," "mere agent," "device," "corporate double," and "tool." Hamilton, *The Corporate Entity*, 49 TEX. L. REV. 979, 983 (1971). It was precisely such a flood of images and terminology that prompted Judge Cardozo to declare that the area "is enveloped in the mists of

to both publicly-held and closely-held or family corporations,⁸ although case law reveals the doctrine is primarily applied to closely-held corporations.⁹

The decision of when to pierce the corporate veil varies from state to state¹⁰ as well as within the federal court system.¹¹ Confusion in both state and federal courts in disregarding the corporate entity is the result of different tests employed by the courts and different factors required by the particular tests.¹² The result of this inconsistent application of the piercing doctrine in the federal courts is of particular significance in the Medicare program, specifically as it has been applied recently in the limited area of Medicare's right to reimbursement from extended care facilities,¹³ commonly referred to as skilled nursing facilities.¹⁴ During the past few years at least five decisions were handed down by federal courts on the issue of Medicare's right to recoup overpayments from the shareholders of corporate providers pursuant to Title XVIII of the Social Security Act.¹⁵ Although the factual situations were nearly identical, application of the appropriate law with regard to piercing the corporate veil was unclear, inconsistent, and confusing.¹⁶ Two cases failed to mention whether state law was to be incorporated into the federal rule or whether federal common law was to be applied;¹⁷ two cases applied state law as the appropriate federal rule;¹⁸ and one case formulated a federal uniform rule of decision.¹⁹

The purpose of this comment will be to examine the confusion in federal courts regarding the decision to adopt either the state law as the controlling federal piercing law or to formulate a uniform rule of decision. This perplexity in the federal courts will be illustrated further by

metaphor" and that "metaphors in law are to be narrowly watched, for starting as devices to liberate thought, they end often by enslaving it." *Berkey v. Third Ave. Ry. Co.*, 244 N.Y. 84, 94, 155 N.E. 58, 61 (1926).

8. HENN, *supra* note 1, §146, at 252. However, the general rule becomes less subject to exceptions as the number of shareholders increases. HENN, *supra* note 1, §146, at 252 n.12.

9. *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421, 424 (D. Mass. 1977) (citing *Francis O'Day Co. v. Shapiro*, 267 F.2d 669, 673 n.11 (D.C. Cir. 1959)); HENN, *supra* note 1, §146, at 252.

10. See notes 59-86 and accompanying text *infra*.

11. See notes 31-33, 87-94 and accompanying text *infra*.

12. See notes 57-62 and accompanying text *infra*.

13. *United States v. Pisani*, 646 F.2d 83 (3d Cir. 1981); *United States v. Thomas*, 515 F. Supp. 1351 (W.D. Tex. 1981); *Woodland Nursing Home Corp. v. Harris*, 514 F. Supp. 110 (S.D.N.Y. 1981); *United States v. Healthwin-Midtown Convalescent Hosp. and Rehabilitation Center, Inc.*, 511 F. Supp. 416 (C.D. Cal. 1981); 428 F. Supp. at 421.

14. *United States v. Gravette Manor Homes, Inc.*, 642 F.2d 231, 232 (8th Cir. 1981); 514 F. Supp. at 112; *see also* 42 U.S.C. §1395x(j) (1976 & Supp. III 1979).

15. See note 13 *supra*.

16. See note 13 *supra*.

17. 515 F. Supp. at 1351; 428 F. Supp. at 421.

18. 514 F. Supp. at 110; 511 F. Supp. at 416.

19. 646 F.2d at 83.

demonstrating the inconsistent application of the piercing doctrine in the state courts and the effect of these inconsistencies on the federal courts' decisions. The focus of this comment will be the piercing doctrine as it has been applied to Medicare's right to reimbursement and the impact of a uniform rule of decision on the piercing doctrine in this area. This discussion will include an analysis of the need for a uniform rule of decision, the essence of the uniform rule of decision pursuant to existing case law, and the potential impact of these determinations on California corporations. To provide background for the piercing decision, this comment will begin with an examination of the piercing doctrine and the application of this doctrine in the United States.

PIERCING THE CORPORATE VEIL

The general rule is that a corporation will be looked upon as a legal entity, separate and distinct from its shareholders.²⁰ This separation of legal entity from beneficial ownership has evolved into the principle of limited liability.²¹ Although limited liability historically was not a benefit to incorporating in the United States,²² over the years it has been adopted primarily to encourage capital growth and investment.²³ Today limited liability is fundamental to the law of every jurisdiction.²⁴

The doctrine of limited liability, however, has been introduced for purposes of convenience and to achieve justice in a particular situation.²⁵ When the doctrine is invoked for a purpose beyond the scope of this policy, courts will disregard the corporate form and pierce the protective "corporate veil."²⁶ A corporation and its shareholders will be treated as one and the same,²⁷ thereby subjecting the individual shareholders to personal liability for the debts and obligations of the corpo-

20. See note 1 and accompanying text *supra*.

21. See note 2 and accompanying text *supra*.

22. Comment, *Inadequate Capitalization as a Basis for Shareholder Liability: The California Approach and a Recommendation*, 45 S. CAL. L. REV. 823, 830-33 (1972) [hereinafter cited as *Inadequate Capitalization*].

23. *Inadequate Capitalization*, *supra* note 22, at 830, 833-34; see also Douglas & Shanks, *Insulation from Liability Through Subsidiary Corporations*, 39 YALE L.J. 193, 193-94 (1929); Comment, *Should Shareholders be Personally Liable for the Torts of Their Corporation?*, 76 YALE L.J. 1190, 1190-91 (1967).

24. Krendl & Krendl, *Piercing the Corporate Veil: Focusing the Inquiry*, 55 DEN. L.J. 1, 2 (1978) [hereinafter cited as Krendl & Krendl]; see Quinn v. Butz, 510 F.2d 743, 758 (D.C. Cir. 1975).

25. *Western Battery & Supply Co. v. Hazelett Storage Battery Co.*, 61 F.2d 220, 230 (8th Cir. 1932).

26. In a court of equity, substantial rights rather than mere matter of organization will be given controlling effect, and disregard of the corporate entity may be invoked if this is necessary to preserve, protect or enforce such rights. *Riverdale Cotton Mills v. Alabama & Ga. Mfg. Co.*, 198 U.S. 188, 199 (1905).

27. See note 5 and accompanying text *supra*.

ration.²⁸ Thus, the courts are torn between two competing policies—the necessity of limiting liability to promote growth of the corporate style of doing business and the desire to do justice in a particular case.²⁹ Since this “piercing” remedy is essentially equitable in nature and requires contradicting the strong public and economic policies of encouraging capital growth and investment, the courts reluctantly, inconsistently, and quite often unclearly determine when to pierce the corporate veil.³⁰

This inconsistency and confusion in the application of the piercing doctrine is quite apparent in federal courts.³¹ The source of this confusion, however, is twofold. First, whenever a case is required to be taken into the federal court system, a decision must be made regarding the rule to be adopted as the controlling federal law.³² The decision requires the federal court to apply either the law of the state in which it presides or to follow other federal cases and formulate a uniform rule of decision—essentially federal common law.³³ Second, if the federal court determines that state law is to be adopted as the controlling federal law, further complexities arise due to the inconsistent application of the piercing doctrine in the individual states. In order to fully understand the source of this confusion, it is necessary to trace the historical background of federal common law and its development in the modern federal piercing dilemma.

THE FEDERAL OPTION: STATE LAW OR A UNIFORM RULE OF DECISION

Erie R.R. Co. v. Tompkins,³⁴ decided in 1938, effectively ended the regime of federal common law in the area of diversity of citizenship cases by holding that a federal court was bound to apply state law.³⁵ *Erie* stated that no general federal common law existed and that Congress had no power to declare substantive rules of common law applicable in a state.³⁶ *Hinderlider v. La Plata River & Cherry Creek Ditch Co.*,³⁷ decided on the same day as *Erie*, however, clearly stated that federal common law still existed in cases when federal jurisdiction was

28. See note 5 and accompanying text *supra*.

29. Dobbyn, *A Practical Approach to Consistency in Veil-Piercing Cases*, 19 U. KAN. L. REV. 185, 185 (1971) [hereinafter cited as Dobbyn].

30. Krendl & Krendl, *supra* note 24, at 7.

31. See note 13 *supra*.

32. *United States v. Pisani*, 646 F.2d 83, 85-87 (3d Cir. 1981).

33. *Id.*

34. 304 U.S. 64 (1938).

35. *Id.* at 80.

36. *Id.* at 78.

37. 304 U.S. 92 (1938).

based on a federal question.³⁸ This proposition was clarified five years later in *Clearfield Trust Co. v. United States*.³⁹ The Court held that when the United States disburses its funds or pays its debts in exercising a constitutional function or power, absent an applicable act of Congress, the federal courts should fashion the governing rule of law according to their own standards.⁴⁰ The enduring contribution of the *Clearfield* holding is its clear establishment of power in the federal courts to select the governing law in matters related to ongoing operations of the national government.⁴¹

Nevertheless, federal courts often adopt the state law as the relevant federal rule when to do so is reasonable and no contrary federal policy exists.⁴² The decision is a matter of judicial wisdom dependent upon the nature of the interests involved, as well as upon the impact of the use of a particular rule on these interests.⁴³ Essentially, the "adoption decision" requires a balancing test that seeks to determine whether the federal interests can be effectuated better by adoption of a uniform federal rule or by adoption of the state rule as the controlling federal law.⁴⁴ Courts have articulated various factors to aid in this determination. These factors include the extent to which: (1) a need exists for national uniformity;⁴⁵ (2) a federal rule would disrupt commercial relationships predicated on state law;⁴⁶ (3) application of state law would frustrate specific objectives of the federal program;⁴⁷ (4) implementation of a particular rule would cause administrative hardships or would aid in administrative conveniences;⁴⁸ (5) the regulations lend weight to the application of a uniform rule;⁴⁹ (6) the action in question has a direct effect on financial obligations of the United States;⁵⁰ and

38. *Id.* at 110. Perhaps the language in *Erie* can be distinguished on the basis of "general federal common law" as opposed to merely "federal common law." C. WRIGHT, LAW OF FEDERAL COURTS §60, at 279 (3d ed. 1977).

39. 318 U.S. 363 (1943).

40. *Id.* at 366-67. But see Wechsler, *The Political Safeguards of Federalism: The Role of the United States in the Composition and Selection of the National Government*, 54 COLUM. L. REV. 543 (1954).

41. Mishkin, *The Variousness of "Federal Law": Competence and Discretion in the Choice of National and State Rules for Decision*, 105 U. PA. L. REV. 797, 833 (1957) [hereinafter cited as Mishkin].

42. *United States v. Polizzi*, 500 F.2d 856, 907 (1974).

43. *United States v. Standard Oil Co.*, 332 U.S. 301, 310 (1947); see also Mishkin, *supra* note 41, at 805.

44. *Southern Pac. Transp. Co. v. United States*, 462 F. Supp. 1193, 1208 (E.D. Cal. 1978).

45. *United States v. Pisani*, 646 F.2d 83, 86 (3d Cir. 1981).

46. *Id.*

47. *Id.*

48. *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 733 (1979); *United States v. Dansby*, 509 F. Supp. 188, 193 (N.D. Ohio 1981).

49. This analysis is the modern or so-called "implied" preemption approach. See, e.g., *Pennsylvania v. Nelson*, 350 U.S. 497, 501-06 (1956); *Pennzoil Co. v. Federal Energy Regulatory Comm'n*, 645 F.2d 360, 385 n.52 (5th Cir. 1981).

50. *Holbrook v. Pitt*, 643 F.2d 1261, 1270 n.16 (7th Cir. 1981).

(7) substantial federal interest in the outcome of the litigation exists.⁵¹

Even with the use of these factors, however, whether state law will be adopted as the federal rule or a unique federal uniform rule of decision will be formulated remains unclear. The courts have failed to either mention the applicable law⁵² or to state the underlying rationale for their choice of which law to apply.⁵³ Moreover, the decision is complicated further since the federal court is faced with the additional dilemma of interpreting the particular state's law on piercing before it can ascertain whether federal interests can be effectuated by its use. The piercing doctrine has evolved differently in the individual states and a considerable amount of confusion exists regarding the requirements that must be fulfilled to allow for disregarding the corporate entity.⁵⁴ This confusion and inconsistent application of the piercing doctrine among the states amplifies the confusion already existing in federal courts.

A. Piercing the Corporate Veil According to State Law

Early courts looked directly to bad faith and to the injustice of the shareholder's conduct towards third persons to justify disregarding the corporate entity.⁵⁵ After 32 years of dealing with the inadequacies of a rule emphasizing the conduct of the shareholder directly affecting third persons, courts added a second line of reasoning to their piercing rationales.⁵⁶ This new aspect was an "instrumentality" or "identity" relationship between the shareholder and the corporation.⁵⁷ The end product in each jurisdiction was a rule that combined two distinct elements: (1) injustice or inequity in the relationship between the plaintiff and the shareholder and (2) unity of interest and ownership⁵⁸ between

51. *In re "Agent Orange" Product Liability Litigation*, 635 F.2d 987, 990 (2d Cir. 1980).

52. *United States v. Thomas*, 515 F. Supp. 1351 (W.D. Tex. 1981); *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421 (D. Mass. 1977).

53. *Woodland Nursing Home Corp. v. Harris*, 514 F. Supp. 110 (S.D.N.Y. 1981); *United States v. Healthwin-Midtown Convalescent Hosp. and Rehabilitation Center, Inc.*, 511 F. Supp. 416 (C.D. Cal. 1981).

54. Dobbyn, *supra* note 29, at 186.

55. Dobbyn, *supra* note 29, at 185.

56. Dobbyn, *supra* note 29, at 185-86.

57. California set the stage for other courts to follow in *Minifie v. Rowley*, 187 Cal. 481, 487, 202 P. 673, 676 (1921):

First, that the corporation is not only influenced and governed by that person, but that there is such a unity of interest and ownership that the individuality, or separateness, of the said person and corporation has ceased; second, that the facts are such that an adherence to the fiction of the separate existence of the corporation would, under the particular circumstances, sanction a fraud or promote injustice.

58. This unity of interest element essentially means that the corporation is merely the alter ego of the shareholders, notwithstanding compliance with all statutory requirements for the creation of a corporation. 1A H. BALLANTINE & G. STERLING, *CALIFORNIA CORPORATION LAWS* §295 (4th ed. 1981).

the shareholder and the corporation.⁵⁹

The confusion in this area today is a result of the various methods jurisdictions use in defining the importance of these two elements, as well as the factors necessary to establish their existence. For example, courts have used a "scatter-gun" approach regarding the unity of interest requirement and have placed each and every available fact which might possibly indicate unity of interest or control in their opinions, regardless of its relevance to the particular issue in dispute.⁶⁰ Consequently, courts espouse numerous tests to justify disregarding corporateness,⁶¹ while at the same time their rationales are frequently devoid of substance and dominated by loaded terminology.⁶² Thus, the deciding and differentiating factors used in a piercing the corporate veil case are often impossible to determine.⁶³

New York and California courts appear to be on opposite extremes regarding the evidence necessary to allow for piercing the corporate veil.⁶⁴ Historically, New York has generated many of the most important corporate veil cases, and other jurisdictions have followed the restrictive view of New York courts toward disregarding the corporate entity.⁶⁵ The basic position of these decisions is that the corporate veil should not be readily pierced.⁶⁶ In furtherance of this position, New York and other states adopting this view require a strong showing of fraud or other improper purpose.⁶⁷ In an attempt to prove this improper purpose, courts look to various factors such as complying with corporate formalities, regardless of whether compliance is the cause of

59. Dobbyn, *supra* note 29, at 187. Compare this analysis with the application of Powell's three-legged test in *Lowendahl v. Baltimore & Ohio R.R. Co.*, 247 A.D. 144, 157-62, 287 N.Y.S. 62, 75-81 (1936).

60. Conrad, *supra* note 4, §277, at 432; Dobbyn, *supra* note 29, at 188; see *Rosen v. Losch Co.*, 234 Cal. App. 2d 324, 333-35, 44 Cal. Rptr. 377, 382-84 (1965); *Associated Vendors, Inc. v. Oakland Meat Co.*, 210 Cal. App. 2d 825, 837-42, 26 Cal. Rptr. 806, 812-16 (1962); *Berkey v. Third Ave. Ry. Co.*, 244 N.Y. 84, 94-95, 155 N.E. 58, 61 (1926).

61. In 1925, Professor Ballantine stated that courts usually pierced the corporate veil upon a showing of (1) agency or (2) the use of the corporation as an instrumentality to sanction a fraud or promote injustice. See Ballantine, *Separate Entity of Parent and Subsidiary Corporations*, 14 CAL. L. REV. 12, 20 (1925). Douglas and Shanks in 1929 stated that courts would pierce the veil under circumstances they categorized as (1) inadequacy of capital; (2) direct intervention which ignores the normal and orderly procedure of corporate control; or (3) avoiding an inequitable result. See Douglas & Shanks, *Insulation from Liability Through Subsidiary Corporations*, 39 YALE L.J. 193, 218 (1929). For recent attempts to categorize the factors, see Dobbyn, *supra* note 29, at 190; Hamilton, *The Corporate Entity*, 49 TEX. L. REV. 979, 985 (1971).

62. CONRAD, *supra* note 4, §277, at 432; Dobbyn, *supra* note 29, at 189.

63. See notes 60-62 *supra*.

64. See Dobbyn, *supra* note 29, at 192; Krendl & Krendl, *supra* note 24, at 14.

65. Krendl & Krendl, *supra* note 24, at 14.

66. *Kingston Dry Dock Co. v. Lake Champlain Transp. Co.*, 31 F.2d 265, 267 (2d Cir. 1929); *Eskimo Pie Corp. v. Whitelawn Dairies, Inc.*, 266 F. Supp. 79, 83 (S.D.N.Y. 1967); *Bartle v. Home Owners Cooperative*, 309 N.Y. 103, 106, 127 N.E.2d 832, 833 (1955); *Lowendahl v. Baltimore & Ohio R.R. Co.*, 247 A.D. 144, 154, 287 N.Y.S. 62, 72 (1936); Krendl & Krendl, *supra* note 24, at 18.

67. See note 66 *supra*.

an injury in question;⁶⁸ holding a controlling interest in one or more corporations and handling them so that they have ceased to represent separate enterprises;⁶⁹ and adequately capitalizing the corporation at the outset to provide for payment of reasonably foreseeable creditors' claims.⁷⁰ Although something more than mere ownership or control must be proven, the improper purpose need not rise to the level of common law fraud.⁷¹

In comparison, California courts appear to be quite liberal in their application of the piercing doctrine.⁷² At least in theory, California is the only state to rely on inadequate capitalization in the piercing decision to the exclusion of all other factors and elements, including improper purpose and unjust results.⁷³ In *Minton v. Cavaney*,⁷⁴ the California Supreme Court elevated inadequate capitalization from a mere factor⁷⁵ to be considered in the "piercing" decision to an *independent ground* for imposing shareholder liability.⁷⁶ Although *Minton* was the last case to be decided by the California Supreme Court on the matter, at least two subsequent California appellate court cases have retreated from the holding in *Minton*,⁷⁷ thereby obscuring the weight California courts will accord to this theory.⁷⁸

In *Harris v. Curtis*,⁷⁹ the court explicitly held that undercapitalization was merely a factor to be considered,⁸⁰ along with all other factors present in the case. The court treated the language in *Minton* that inadequate capitalization is an independent ground for piercing as mere dictum.⁸¹ Notwithstanding that this holding constituted a retreat from

68. *De Witt Truck Brokers v. W. Ray Flemming Fruit Co.*, 540 F.2d 681, 687 (4th Cir. 1976); 309 N.Y. at 106, 127 N.E.2d at 833; R. HAMILTON, CORPORATIONS, CASES AND MATERIALS, 210-15 (2d ed. 1981).

69. *Walkovsky v. Carlton*, 18 N.Y.2d 414, 418, 223 N.E.2d 6, 8-9, 276 N.Y.S.2d 585, 588-89 (1966); Berle, *The Theory of Enterprise Entity*, 47 COLUM. L. REV. 343, 348 (1947).

70. 540 F.2d at 684.

71. *Schattner v. Girard*, 668 F.2d 1366, 1369-70 (D.C. Cir. 1981).

72. *See Minton v. Cavaney*, 56 Cal. 2d, 576, 579, 364 P.2d 473, 475, 15 Cal. Rptr. 641, 643 (1961).

73. *Id.*

74. 56 Cal. 2d 576, 364 P.2d 473, 15 Cal. Rptr. 641 (1961).

75. In *Automotriz Del Golfo De California v. Resnick*, 47 Cal. 2d 792, 796-97, 306 P.2d 1, 4 (1957), the court clearly indicated that inadequate capitalization was merely a factor to be considered in the decision to pierce the corporate veil. Quoting from *Carlesimo v. Schwebel*, 87 Cal. App. 2d 482, 493, 197 P.2d 167, 174 (1948), the court held:

[T]he proper rule is that inadequate financing, where such appears, is a factor, and an important factor, in determining whether to remove the insulation to stockholders normally created by the corporate method of operation.

47 Cal. 2d at 797, 306 P.2d at 4.

76. 56 Cal. 2d at 579, 364 P.2d at 475, 15 Cal. Rptr. at 643.

77. *Pearl v. Shore*, 17 Cal. App. 3d 608, 95 Cal. Rptr. 157 (1971); *Harris v. Curtis*, 8 Cal. App. 3d 837, 87 Cal. Rptr. 614 (1970).

78. *Inadequate Capitalization*, *supra* note 22, at 824-26.

79. 8 Cal. App. 3d at 837, 87 Cal. Rptr. at 614.

80. *Id.* at 843, 87 Cal. Rptr. at 619.

81. *Id.* at 841, 87 Cal. Rptr. at 617-18. The court stated: "Appellants would have us declare

Minton, the petition for a hearing by the California Supreme Court was denied.⁸²

A second case, *Pearl v. Shore*,⁸³ also indicates a weakening of *Minton*. The appellate court explicitly stated that the requirements of unity of interest and inequitable result must both be present to disregard the corporate form.⁸⁴ Primary emphasis was placed on the plaintiff's inability to show that failure to pierce the corporate veil would result in inequities.⁸⁵ Moreover, in dictum the court referred to *Harris* and indicated that the issue of whether undercapitalization alone was sufficient for disregarding the corporate form had not been settled.⁸⁶

As a result of the inconsistent approaches the individual states take regarding the elements and factors necessary to allow "piercing," clearly, if federal courts adopt the laws of the states in which they preside as the appropriate federal rule, the piercing doctrine may differ from state to state even when applied to essentially similar claims. In addition, a uniform rule of decision on disregarding the corporate entity formulated by federal courts may differ substantially from the law of the state in which the federal court presides. In order to understand the potential impact of the federal court applying a uniform rule of decision as opposed to state law, it is necessary to analyze the substance of the federal common law piercing doctrine.

B. *The Federal Common Law Piercing Doctrine*

Once a federal court determines that a uniform rule of decision on piercing should be applied, the court is then faced with the problem of identifying what other federal courts have held in the area, and, based on these judicial opinions, the court must formulate an appropriate rule to apply to the particular facts of the case. A considerable amount of confusion exists regarding the applicable federal common law in this area. Many federal courts simply apply the two elements of the state doctrine—unity of interest and injustice in the particular situation—thereby equating the federal piercing doctrine to that applied by the states.⁸⁷ One federal court, in the Central District in California, chose

that per se inadequate capitalization renders the shareholders, officers and directors liable for the obligations of the corporation. They cite no case so holding, and we know of none." *Id.*

82. *Id.* at 843; see also *Inadequate Capitalization*, *supra* note 22, at 830.

83. 17 Cal. App. 3d at 608, 95 Cal. Rptr. at 157.

84. *Id.* at 618, 95 Cal. Rptr. at 163.

85. *Id.*

86. *Id.* at 616-17, 95 Cal. Rptr. at 162; see also *Inadequate Capitalization*, *supra* note 22, at 830 n.26.

87. See *DeWitt Truck Brokers v. W. Ray Flemming Fruit Co.*, 540 F.2d 681, 684-87 (4th Cir. 1976); *Lakota Girl Scout Council, Inc. v. Havey Fund-Raising Management, Inc.*, 519 F.2d 634, 637-38 (8th Cir. 1975); *G.M. Leasing Corp. v. United States*, 514 F.2d 935, 939-40 (10th Cir. 1975);

to apply state piercing law to the particular facts based on the premise that federal law was undeveloped in the piercing area.⁸⁸ Another court, in the District of Columbia, found federal law on piercing to encompass a general rule that "a corporate entity may be disregarded in the interests of public convenience, fairness and equity."⁸⁹

Still other federal courts have incorporated the two elements of injustice and unity of interest used by the states into a federal rule of decision, while at the same time adding another element to the piercing doctrine. Theoretically, this new element alone justifies disregarding the corporate entity.⁹⁰ This independent ground for piercing was most recently articulated as an alternative holding in the federal court cases of *United States v. Normandy House Nursing Home, Inc.*⁹¹ and *United States v. Pisani*,⁹² wherein circumvention of a statute or avoidance of a clear legislative purpose was held sufficient to pierce the corporate veil.⁹³ The holdings in these cases allow the corporate entity to be disregarded and permit personal liability to be placed upon the shareholder or shareholders of the corporation *whenever the failure to pierce would frustrate a statutory aim*.⁹⁴ The particular statute involved in both cases required the United States government to be reimbursed for overpayments made to providers under the Medicare program.⁹⁵ The mere inability of corporations to pay warrants piercing, notwithstanding the absence of fault or inequities. This interpretation is further substantiated in a recent United States appellate court decision, *Town of Brookline v. Gorsuch*.⁹⁶ There the court stated its understanding of the general federal rule on piercing to be that a corporate entity may be disregarded in the interests of public convenience, fairness, and equity.⁹⁷ In applying this rule, the court required a close scrutiny of the

Delchamps, Inc. v. Borkin, 429 F.2d 417, 418-19 (5th Cir. 1970); Zubik v. Zubik, 384 F.2d 267, 272-75 (3d Cir. 1967).

88. *United States v. Healthwin-Midtown Convalescent Hosp. and Rehabilitation Center, Inc.*, 511 F. Supp. 416, 418 (C.D. Cal. 1981). This decision was based on the holding in *Matter of Christian and Porter Aluminum Co. v. Titus*, 584 F.2d 326, 337 (9th Cir. 1978).

89. *Capital Telephone Co. v. F.C.C.*, 498 F.2d 734, 738 (D.C. Cir. 1974).

90. *United States v. Pisani*, 646 F.2d 83, 88-89 (3d Cir. 1981); *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421, 424-25 (D. Mass. 1977). Although the law in regard to this new element was clearly addressed in these cases and their progenitors, there were always facts sufficient to justify piercing the corporate veil absent the use of this additional piercing element. See generally *Quinn v. Butz*, 510 F.2d 743 (D.C. Cir. 1975); *Bruhn's Freezer Meats of Chicago, Inc. v. United States Dept. of Agriculture*, 438 F.2d 1332 (8th Cir. 1971); *Maley v. Carroll*, 381 F.2d 147 (5th Cir. 1967); *H.R. Lambert Co. v. Secretary of the Treasury*, 354 F.2d 819 (1st Cir. 1965); *Mansfield Journal Co. v. F.C.C.*, 180 F.2d 28 (D.C. Cir. 1950).

91. 428 F. Supp. 421 (D. Mass. 1977).

92. 646 F.2d 83 (3d Cir. 1981).

93. *Id.* at 88-89; 428 F. Supp. at 424-25.

94. 646 F.2d at 88-89; 428 F. Supp. at 424-25.

95. 646 F.2d at 85; 428 F. Supp. at 42.

96. 667 F.2d 215 (1st Cir. 1981).

97. *Id.* at 221.

purpose of the federal statute to determine whether the statute placed importance on the corporate form.⁹⁸ The court further held that this inquiry accorded less respect to the corporate form than the strict common law alter ego doctrine applied by the state courts.⁹⁹

In essence, the decisions of the federal courts in *Normandy*, *Pisani*, and *Town of Brookline* imposed different requirements on state piercing doctrines and federal common law piercing doctrines.¹⁰⁰ The federal courts, applying a federal rule of decision, required a lesser burden of proof to disregard the corporate entity than that traditionally demanded by the individual states.¹⁰¹ The nearest reference to this circumvention of a statutory aim as a ground for disregarding the corporate entity at the state level is the language that a corporation should be disregarded "whenever justice or public policy demand it. . . ."¹⁰² This broad language, however, is consistently qualified by the requirement of specific factors which are regarded as essential to the "piercing" determination.¹⁰³ Thus, even though states differ considerably in the application of the piercing doctrine, nothing akin to the federal circumvention of a statutory purpose as an independent ground for piercing exists at the state level. The results of the inconsistent application of the piercing doctrine in federal courts can be understood by an examination of the application of the doctrine in the area of Medicare's right to reimbursement from extended care facilities pursuant to Title XVIII of the Social Security Act.¹⁰⁴

MEDICARE AND THE PIERCING DOCTRINE

Recently, five decisions have been published by federal courts on the issue of Medicare's right to reimbursement from extended care facilities.¹⁰⁵ The situations were nearly identical, but the analyses and the applications of the law by the courts were inconsistent and confusing. A review of the historical background of the policies and procedures of the Medicare Program is required to comprehend the factual composition of these five cases.

98. *Id.*

99. *Id.* See note 58 and accompanying text *supra*.

100. See notes 90-99 and accompanying text *supra*.

101. See notes 59, 90-99 and accompanying text *supra*.

102. *Tucker v. Binstock*, 310 Pa. 254, 263, 165 A. 247, 250 (1933).

103. See note 61 *supra*.

104. See note 13 *supra*.

105. See note 13 *supra*.

A. Background on the Medicare Program

Title XVIII of the Social Security Act,¹⁰⁶ commonly known as Medicare, was enacted in 1965 to provide health care services to the aged, blind, and disabled.¹⁰⁷ The program was enacted by Congress for the specific purpose of providing modern medical care through a coordinated and comprehensive federal health insurance plan.¹⁰⁸ The Medicare program is substantively divided into two parts.¹⁰⁹ This comment will deal exclusively with Part A,¹¹⁰ which provides for hospital insurance benefits through direct payments to hospitals, nursing homes, clinics, or home health agencies for inpatient services.¹¹¹

In general, under Part A of the program providers of medical services are reimbursed by the federal government¹¹² for the "reasonable cost"¹¹³ of services actually rendered to eligible Medicare beneficiaries.¹¹⁴ Reasonable costs are the costs actually incurred by the provider, excluding any part thereof found unnecessary in the efficient delivery of needed health services.¹¹⁵ These costs are determined in accordance with regulations establishing the method or methods to be used and the items to be included in ascertaining costs for various types of classes of institutions, agencies, and services.¹¹⁶ The overriding policy to be implemented by the regulations is to ensure that costs attributable to Medicare beneficiaries are not borne by nonbeneficiaries and, conversely, that the Medicare program does not reimburse providers for costs which are properly attributable to non-Medicare patients.¹¹⁷

These actual costs, however, cannot be identified until the end of the

106. 42 U.S.C.A. §§1395-1395ss (West Supp. 1974-1979).

107. Individuals covered under the program include:

(1) individuals who are age 65 or over and are eligible for retirement benefits under subchapter II of this chapter or under the railroad retirement system; (2) individuals under age 65 who have been entitled for not less than 24 months to benefits under subchapter II of this chapter or under the railroad retirement system on the basis of a disability; and (3) certain individuals who did not meet the conditions specified in either clause (1) or (2) but who are medically determined to have end stage renal disease.

42 U.S.C. §1395c (1976 & Supp. III 1979).

108. *Turecamo v. Commissioner*, 554 F.2d 564, 571 (2d Cir. 1977); *Rastetter v. Weinberger*, 379 F. Supp. 170, 172 (D.C. Ariz. 1974), *aff'd*, 419 U.S. 1098 (1975).

109. 554 F.2d at 571.

110. 42 U.S.C. §§1395c-1395i (1976 & Supp. III 1979). Part A is entitled "Hospital Insurance Benefits for Aged and Disabled." The second substantive section of the act, Part B, deals with supplementary medical insurance benefits for the aged and disabled. *Id.* §§1395j-1395w. Part C of Title XVIII is a definitional section. 42 U.S.C.A. §§1395x-1395ss (West Supp. 1974-1979).

111. See note 110 *supra*.

112. In reality, the Secretary has assigned the daily operation of the program to "fiscal intermediaries." *Beverly Enterprises v. Mathews*, 432 F. Supp. 1073, 1075 (D.D.C. 1976).

113. 42 U.S.C. §§1395f(b), 1395x(v) (1976 & Supp. III 1979); see also 42 C.F.R. §405.402 (1980).

114. See generally 42 C.F.R. §§405.401-405.454 (1980).

115. 42 U.S.C. §1395x(v)(1)(A) (1976); 42 C.F.R. §405.454 (1980).

116. 42 U.S.C. §§1395f(b)(2), 1395x(v)(1)(A) (1976).

117. 42 C.F.R. §405.454 (1980); see also 42 U.S.C. §1395x(v)(1)(A) (1976).

reporting year, when the cost reports are filed and verified.¹¹⁸ Providers, therefore, must be reimbursed according to an "estimated" cost basis throughout the year.¹¹⁹ These estimated cost payments are made on an interim basis to providers at least once a month¹²⁰ to guarantee that they have an adequate cash flow and are reimbursed as quickly as possible.¹²¹ A retroactive adjustment, based on actual costs determined pursuant to an audit, is made at the end of the annual accounting period.¹²² If the audit reveals that the estimated cost basis exceeds the actual costs incurred by the provider, then Medicare may recover these overpayments.¹²³ Recoupment of these overpayments by the government under the Medicare program has led to numerous controversies that often result in litigation.¹²⁴ When viewing these controversies it is necessary to understand the origin and nature of the claims involved.

B. Current Application of the Piercing Doctrine

The source of the claims involved in Medicare's right to recoup overpayments from providers confers federal courts with jurisdiction over the matter.¹²⁵ The Constitution provides that federal courts may be given jurisdiction over cases in law and equity arising under the Constitution, the laws of the United States, and treaties made, or which shall be made, under their authority.¹²⁶ Clearly, the power to recoup overpayments under the Medicare program has its origin in the statutes of the United States and is not dependent on the laws of any particular state.¹²⁷ Furthermore, the litigation of this matter necessarily raises questions regarding the unique federal nature of the relationships involved.¹²⁸

As previously mentioned, however, whenever a case is heard by federal courts, a decision must be made regarding the rule to be adopted as

118. 42 C.F.R. §405.405 (1980).

119. *Id.*

120. 42 U.S.C. §1395g(a) (1976).

121. 42 C.F.R. §405.454(f)(2) (1980).

122. *Id.*

123. *Szekely v. Florida Medical Ass'n*, 517 F.2d 345, 349 (5th Cir. 1975), *cert. denied*, 425 U.S. 960 (1976); *Mount Sinai Hospital of Greater Miami, Inc. v. Weinberger*, 517 F.2d 329, 337-39 (5th Cir. 1975), *cert. denied*, 425 U.S. 935 (1976); *United States v. Thomas*, 515 F. Supp. 1351, 1353 (W.D. Tex. 1981); *see also* 42 C.F.R. §405.454(f) (1980).

124. *See* note 13 *supra*.

125. *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 726-27 (1979); *Wallis v. Pan Am. Petroleum Corp.*, 384 U.S. 63, 69 (1966); *United States v. Pisani*, 646 F.2d 83, 86 (3d Cir. 1981).

126. U.S. CONST. art. III, §2.

127. 42 U.S.C. §1395g (1976 & Supp. III 1979); *see also* 42 C.F.R. §405.405(b), (c) (1980).

128. *Cf. Clearfield Trust Co. v. United States*, 318 U.S. 363, 366-67 (1943); *In re "Agent Orange" Product Liability Litigation*, 635 F.2d 987, 990 (2d Cir. 1980); *Boyster v. Roden*, 628 F.2d 1121, 1125 (8th Cir. 1980) (Each of these cases discussed the unique nature of particular federal programs.).

the controlling law.¹²⁹ In the application of the piercing doctrine, choice of controlling law is implicitly, inconsistently, or unclearly made.¹³⁰ For example, in *Normandy*, the federal district court in Massachusetts made no mention of which rule was to be the governing law, *i.e.*, the state rule or a federal rule of decision. The court merely articulated alternative holdings¹³¹ without specifying whether the law to be applied was that of the state in which the court was presiding or federal common law. On the one hand, the court discussed the alter ego doctrine requiring unity of interest and equitable considerations as applied generally by the states.¹³² The court found the facts of the case justified going beyond the corporate entity and, accordingly, denied the motion to dismiss.¹³³ On the other hand, the court embarked on a unique approach to disregarding the corporate entity.¹³⁴ Specifically, the court held that the corporate veil could be pierced when failure to do so would lead to circumvention of a statute or avoidance of a clear legislative purpose,¹³⁵ both of which were present in the case. Although the court failed to mention whether state or federal law governed, that federal common law was controlling can be inferred from reliance on this holding in a later federal court opinion applying federal common law.¹³⁶

In a subsequent decision, *U.S. v. Healthwin-Midtown Convalescent Hospital and Rehabilitation Center, Inc.*,¹³⁷ the federal court in the Central District of California stated that the alter ego claim was to be analyzed in accordance with state law.¹³⁸ The court based this holding on the conclusion of a federal circuit court that since there appeared to be no special rule concerning the burden of proof in alter ego cases in federal courts, California law should be applied.¹³⁹ The court then stated the necessity of the presence of unity of interest and inequitable results, as well as various factors to be taken into consideration in determining the existence of these two elements.¹⁴⁰ The court concluded by holding that in the present situation failure to pierce the corporate

129. See notes 43-45 and accompanying text *supra*.

130. See note 13 and accompanying text *supra*.

131. *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421, 424-25 (D. Mass. 1977).

132. *Id.* at 424.

133. *Id.*

134. *Id.* at 424-25.

135. *Id.* at 424.

136. This inference is made possible by later reference to the alternative holding of this case in *United States v. Pisani*, 646 F.2d 83, 88 (3d Cir. 1981) and in *United States v. Thomas*, 515 F. Supp. 1351, 1357 (W.D. Tex. 1981).

137. 511 F. Supp. 416 (C.D. Cal. 1981).

138. *Id.* at 418.

139. *Id.* See note 88 and accompanying text *supra*.

140. 511 F. Supp. at 418-20.

veil would be unjust.¹⁴¹

The federal court in the Southern District of New York also applied the state rule as the controlling federal law in the case of *Woodland Nursing Home Corp. v. Harris*.¹⁴² Although the court explicitly stated that New York law was to govern the case, it supplied no basis for this decision.¹⁴³ Applying the alter ego theory, the court found that despite the absence of proof of fraudulent intent, failure to pierce the corporate veil would produce an unjust result.¹⁴⁴ The court did not cease its analysis here, but continued on to state that "[e]quity and, in particular, policy considerations under the Medicare statute may provide a basis for the same result."¹⁴⁵ Moreover, the court cited *Normandy* and stated that "to permit Woodland Corporation to avoid liability for Woodland Associate's debts would be contrary to an important policy underlying the Medicare program which is to insure that the government not be charged for more than the reasonable costs of services being rendered."¹⁴⁶ While the court applied New York law to allow for piercing the corporate veil, inclusion of the language regarding policies underlying the Medicare program as well as the court's reference to *Normandy* indicates an awareness of the existence of the federal uniform rule of decision in this area.¹⁴⁷ Only the federal common law piercing doctrine places genuine significance on the policies and statutes underlying a particular program.¹⁴⁸ In addition, it appears that the court in *Woodland Nursing Home* actually used the federal rule to substantiate its decision to pierce based upon state law.¹⁴⁹

Pisani was the first case to distinguish between the use of state law and federal common law in the area of piercing the corporate veil and Medicare's right to reimbursement.¹⁵⁰ In deciding which law to adopt as the federal rule for the case, the United States Third Circuit Court of Appeals relied on *United States v. Kimbell Foods, Inc.*,¹⁵¹ and analyzed three factors: (1) whether a need for national uniformity existed in this area, (2) whether a federal rule would disrupt commercial relationships predicated on state law, and (3) whether the application of state law would frustrate specific objectives of the federal program.¹⁵² The

141. *Id.* at 420.

142. 514 F. Supp. 110 (S.D.N.Y. 1981).

143. *Id.* at 113.

144. *Id.* at 114.

145. *Id.* at 113.

146. *Id.* at 114.

147. *Id.*

148. See notes 90-99 and accompanying text *supra*.

149. 514 F. Supp. at 114.

150. *United States v. Pisani*, 646 F.2d 83, 85-88 (3d Cir. 1981).

151. 440 U.S. 715 (1979).

152. 646 F.2d at 86; *see also* 440 U.S. at 728.

Pisani court found that state law could frustrate the specific objectives of the Medicare program to furnish prompt reimbursements to providers¹⁵³ and to pay only for the reasonable costs of services supplied.¹⁵⁴ Based upon these findings, as well as upon the finding that application of the laws of the different states would frustrate HEW's only control for overpayments,¹⁵⁵ the court held that the formulation of a federal uniform rule of decision was necessary.¹⁵⁶ The court then discussed the contents of this federal uniform rule through the use of alternative holdings.¹⁵⁷ Initially, the court discussed the alter ego theory as used in *DeWitt Truck Brokers v. W. Ray Flemming Fruit Co.*¹⁵⁸ The *Pisani* opinion detailed the factors necessary to show unity of interest between the shareholder and the corporation.¹⁵⁹ Further, the court stated that the factual situation must present an element of injustice or fundamental unfairness,¹⁶⁰ thereby equating the federal rule of decision with the traditional piercing doctrine applied by the states.¹⁶¹ Based on this alter ego doctrine, the court held that piercing the corporate veil was appropriate.¹⁶² As an alternative to this rule, however, the court carefully rearticulated the holding in *Normandy* that the corporate veil could be pierced to prevent circumvention of a statute or avoidance of a clear legislative purpose.¹⁶³ The court found that Dr. Pisani fell within the purview of this alternative holding as well as the alter ego rationale since the Medicare statute could be circumvented if he were not found personally liable.¹⁶⁴

The most recent case decided in this area was *United States v. Thomas*.¹⁶⁵ Although the United States district court did not mention which rule was to be adopted as the appropriate law, the court's reference to the holding in *Pisani*¹⁶⁶ that clearly applied a federal uniform rule of decision, infers that federal common law was controlling upon

153. 646 F.2d at 86.

154. *Id.* at 86-87.

155. *Id.* at 87.

156. *Id.*

157. *Id.* at 88-89.

158. 540 F.2d 681 (4th Cir. 1976).

159. Factors important to the determination of the existence of an alter ego include: (1) gross undercapitalization for its purposes; (2) failure to observe corporate formalities; (3) non-payment of dividends; (4) insolvency of the debtor corporation at the time; (5) siphoning of funds of the corporation by the dominant stockholders; (6) nonfunctioning of other officers or directors; (7) absence of corporate records; and (8) the fact that the corporation is merely a facade for the operations of the dominant stockholder or stockholders. Also the situation must present an element of injustice or fundamental unfairness. 646 F.2d at 88; see also 540 F.2d at 686-87.

160. See note 159 *supra*.

161. See text accompanying note 59 *supra*.

162. 646 F.2d at 88.

163. 646 F.2d at 88-89.

164. *Id.*

165. 515 F. Supp. 1351 (W.D. Tex. 1981).

166. *Id.* at 1357.

the piercing issue. From the holding in *Thomas*, however, the weight accorded to the uniform rule of decision stated in *Pisani* as well as in *Normandy* is not evident. The majority of the opinion of the court focused on the so-called trust fund doctrine and its applicability to the facts.¹⁶⁷ The court found there were sufficient facts to warrant imposing personal liability on the sole shareholder to the extent the judgment was not satisfied by the corporation.¹⁶⁸ In the alternative, the court opined that sufficient facts existed to justify piercing the corporate veil¹⁶⁹ based on the general rule that corporate existence should be disregarded to prevent fraud, illegality, or injustice or when recognition of the corporate entity would defeat public policy.¹⁷⁰ In applying this rule, the court further stated that pursuant to *Pisani* and *Normandy* circumvention of the Medicare recoupment statute through the insolvency of the provider violated public policy.¹⁷¹ Accordingly, the court appeared to refer to the federal rule of decision on piercing rather than to the traditional state doctrines requiring the existence of both unity of interest and injustice in the particular situation.¹⁷² Nevertheless, the court also discussed factors from *DeWitt Truck Brokers* as being relevant to the decision to impose personal liability for corporate debts.¹⁷³ This analysis was quite similar to the alter ego alternative holding in the *Pisani* decision.¹⁷⁴ The court concluded by holding that the facts were sufficient to warrant summary judgment on the issue of personal liability.¹⁷⁵ This decision was based on an unclear application of *Normandy* accompanied by alter ego factors¹⁷⁶ as well as on the trust fund doctrine.

Although in each of the preceding five cases¹⁷⁷ the decision to pierce was reached, the use of implicit, vague, different, or inconsistent explanations concerning which rule to apply could rapidly lead to inequitable results as well as manipulation of the Medicare system. For

167. *Id.* at 1356-57.

168. *Id.*

169. *Id.* at 1357.

170. *Id.*

171. *Id.*

172. See text accompanying note 59 *supra*.

173. 515 F. Supp. at 1357. See note 159 and accompanying text *supra*.

174. See *United States v. Pisani*, 646 F.2d 83, 88 (3d Cir. 1981).

175. 515 F. Supp. at 1357.

176. In *Thomas* the court appeared to rely on the *Normandy* court's interpretation of the piercing doctrine, and yet the court also discussed *DeWitt Truck Brokers*. The court in *DeWitt Truck Brokers* held the decision

to disregard the corporate entity may not, however, rest on a single factor, whether undercapitalization, disregard of corporation's formalities, or what-not, but must involve a number of such factors; in addition it must present an element of injustice or fundamental unfairness.

DeWitt Truck Brokers v. W. Ray Flemming Fruit Co., 540 F.2d 681, 687 (4th Cir. 1976).

177. See note 13 *supra*.

example, the *Pisani* and *Normandy* courts stated that circumvention of a statutory purpose alone was sufficient to disregard the corporate entity.¹⁷⁸ In *Thomas* the court also appeared to rely on this element,¹⁷⁹ although it is not clear that this reliance was exclusive.¹⁸⁰ On the other hand, the court in *Healthwin-Midtown Convalescent Hospital* applied the alter ego theory of California.¹⁸¹ Likewise, the court in *Woodland Nursing Home* applied the alter ego piercing law of New York to the facts of the case¹⁸² and used the uniform rule articulated by the *Pisani* and *Normandy* courts merely to substantiate its decision based on state law.¹⁸³ The application of these different rules to the same general factual situation indicates that the piercing doctrine might be employed inconsistently.¹⁸⁴ The issue remains whether the state rule or a uniform rule of decision *should* be adopted as the appropriate federal law to avoid this potential inconsistent application of the piercing doctrine in the area of Medicare's right to reimbursement.

THE FUTURE APPLICATION OF PIERCING IN MEDICARE'S RIGHT TO REIMBURSEMENT

The determination to adopt state law or a uniform rule of decision as the controlling federal law in regard to piercing and Medicare's right to recoup overpayments from providers should be based on a thorough analysis of the relevant factors previously set forth in this comment.¹⁸⁵ These factors have been used by federal courts in areas other than those limited to piercing to decide if the adoption of a uniform rule is necessary. In essence, the choice of appropriate law involves a balancing of state and federal interests.

A. Controlling Law: Federal Rule of Decision or State Law

Primary and often competing considerations in determining the need to formulate a federal rule of decision as opposed to using state law are the need for uniformity to effectuate the objectives of the federal program and the intrusion into established state commercial practices and relationships.¹⁸⁶ An analysis of the need for uniformity includes

178. 646 F.2d at 88-89; *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421, 424-25 (D. Mass. 1977).

179. 515 F. Supp. at 1357.

180. *Id.*

181. *United States v. Healthwin-Midtown Convalescent Hosp. and Rehabilitation Center, Inc.*, 511 F. Supp. 416, 418 (C.D. Cal. 1981).

182. *Woodland Nursing Home Corp. v. Harris*, 514 F. Supp. 110, 113 (S.D.N.Y. 1981).

183. *Id.* at 114.

184. See notes 177-183 and accompanying text *supra*.

185. See notes 45-51 and accompanying text *supra*.

186. *United States v. Dansby*, 509 F. Supp. 188, 192 (N.D. Ohio 1981).

strictly scrutinizing the potential frustration of specific objectives of federal programs, the effect of a particular decision on the financial obligations of the United States, and the existence of a substantial federal interest in the outcome of the litigation.¹⁸⁷

The purpose of the Medicare legislation includes ensuring that modern medical care is available on a coordinated and comprehensive basis to covered individuals throughout the country.¹⁸⁸ The system is designed to pay providers on a monthly¹⁸⁹ basis as an incentive for them to participate in the Medicare program.¹⁹⁰ Moreover, providers are to be paid only for the "reasonable costs" actually incurred in furnishing health care services to Medicare beneficiaries. The return of overpayments is crucial to guarantee the fulfillment of this goal and to allow the program to continue to pay providers on an interim, estimated cost basis.¹⁹¹ The federal government has a substantial interest in maintaining the program's current operating structure.¹⁹²

Application of the Medicare program is indistinguishable from nationwide acts of the federal government originating in a single form from a single source.¹⁹³ The scope, nature, legal incidents, and consequences of the relation between providers and Medicare are derived from federal sources and governed by federal authority.¹⁹⁴ Payments are made under a uniform statutory scheme,¹⁹⁵ and the only control is the "day of reckoning" for overpayments.¹⁹⁶ Because of the differences between state and federal law in this area,¹⁹⁷ if federal courts fail to apply a uniform rule of decision, this control could be frustrated.¹⁹⁸ Regardless of the state in which the federal court is presiding, the federal rule of decision on piercing is more lenient than the rule applied by the states.¹⁹⁹ If federal courts were to apply a uniform rule of decision

187. *Id.* at 192-95.

188. *Turecamo v. Commissioner*, 554 F.2d 564, 571 (2d Cir. 1977); *Rastetter v. Weinberger*, 379 F. Supp. 170, 172 (D.C. Ariz. 1974), *aff'd*, 419 U.S. 1098 (1975).

189. 42 U.S.C. §1395g(a) (1976); 42 C.F.R. §405.454(a), (b) (1980).

190. *Monmouth Med. Center v. Harris*, 646 F.2d 74, 76 (3d Cir. 1981); *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421, 423 (D. Mass. 1977); *see also* 42 C.F.R. §405.402(b)(1) (1980).

191. *United States v. Pisani*, 646 F.2d 83, 86 (3d Cir. 1981). The court further stated:

If Congress intended that Medicare be a welfare program for doctors and hospitals, then the return of overpayments would not be so important. The overpayments would be going to those Congress intended to benefit. We believe however, that Medicare was intended solely to assist patients.

Id. at 86-87; *see also* 42 C.F.R. §405.454(b) (1980).

192. *See* 646 F.2d at 86.

193. *See id.* at 76; 428 F. Supp. at 423; *see also* 42 C.F.R. §405.402(b)(1) (1980).

194. 646 F.2d at 76; 428 F. Supp. at 423; *see also* 42 C.F.R. §405.402(b)(1) (1980).

195. 646 F.2d at 76; 428 F. Supp. at 423; *see also* 42 C.F.R. §405.402(b)(1) (1980).

196. 646 F.2d at 87.

197. *See* notes 63-71, 88-99 and accompanying text *supra*.

198. *See* notes 63-71, 88-99 and accompanying text *supra*.

199. *See* notes 59, 90-99 and accompanying text *supra*.

on piercing in one case and the state piercing doctrine in a similar case, the results might not be the same.²⁰⁰ Furthermore, if federal courts adopt the law of the state in which they preside in all cases, essentially similar claims, although based upon the same statutory authority, could be treated differently.²⁰¹ The likelihood of this becomes clear when contrasting the "conservative" piercing doctrine of New York with the "liberal" piercing doctrine of California.²⁰² The application of different laws would directly affect the financial status of the United States by limiting its ability to impose personal liability on the individual shareholders of an insolvent corporation.²⁰³ Conceivably, the use of these inconsistent laws, whether state or federal, involving providers and the Medicare program identically situated in all relevant respects, could allow for piercing in one case and not in another. This would subject the rights and duties of the United States to exceptional uncertainty.²⁰⁴

On the other hand, states traditionally have had a strong interest in applying their own laws in the area of piercing the corporate veil.²⁰⁵ The reason for the strong state concern is to promote capital investment and economic growth within the particular state by employing the legal fiction that the corporation is an entity, separate and distinct from its shareholders.²⁰⁶ The use of a federal uniform rule of decision will adversely affect the state's ability to apply its own piercing doctrine and to further its own particular goals. Since the uniform rule of decision applied to the facts is less restrictive than a particular state's law, this rule will allow piercing more readily. This will conflict with the state's desire to promote the corporate form of doing business, since the protection of limited liability would no longer exist in this specific area.

Conversely, the adoption of a special rule could serve to benefit the states in a significant way. Presently, states with stricter piercing doctrines, for example, may be attractive to providers who conduct their business in a marginal manner²⁰⁷—perhaps bordering on bankruptcy or insolvency. A uniform rule would put all states on an equal footing

200. See notes 90-99 and accompanying text *supra*.

201. See *In re "Agent Orange" Product Liability Litigation*, 635 F.2d 987, 990 (2d Cir. 1980); *United States v. State Box Co.*, 219 F. Supp. 684, 688 (N.D. Cal. 1963), *aff'd*, 321 F.2d 640 (9th Cir. 1963). See notes 60-62 and accompanying text *supra*.

202. See notes 64-73 and accompanying text *supra*.

203. *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 733 (1979); *Clearfield Trust Co. v. United States*, 318 U.S. 363, 367 (1943); 646 F.2d at 87. See note 191 and accompanying text *supra*.

204. See 318 U.S. at 367.

205. See notes 20-24 and accompanying text *supra*.

206. See notes 23-24 and accompanying text *supra*.

207. The strict piercing doctrines will make it less likely that the shareholders will be held personally liable for the corporation's debts and obligations.

regarding the piercing doctrine as applied to the Medicare program, thereby protecting a particular state from the abuse of having providers incorporate there for the purpose of escaping liability.²⁰⁸ Further, those states with more lenient piercing doctrines, *i.e.*, those that more readily subject the corporate members to personal liability, furnish an incentive for providers to incorporate elsewhere. Under a uniform rule, the deterrent element would be eliminated and the prospects for economic growth of a particular state would be advanced.

Another important factor in determining the applicable rule is the administrative hardship or convenience in using one rule as opposed to another. In the case of Medicare's right to reimbursement, the ability of the government to coordinate, administer, and control the program would be enhanced greatly by a uniform rule.²⁰⁹ The use of various state piercing schemes presents a serious danger of conflict with the effective administration of the federal program by hampering the uniform enforcement of the program with sporadic local prosecutions and undefined guidelines.²¹⁰

A final important factor is whether the pertinent regulations provide for specific measures that aid in determining the appropriate rule.²¹¹ The comprehensive regulations that implement the Medicare program demonstrate that the program is to be run on a national level.²¹² The scheme of the federal regulations, including guidelines for recouping overpayments from providers, is so pervasive as to indicate a congressional objective that cannot be attained without the application of federal common law.²¹³ When Congress has not explicitly spoken in an area comprised of issues substantially related to an established program of governmental operation, the holding in *Clearfield* directs federal courts to fill the interstices of federal legislation according to their own standards.²¹⁴ The federal nature of the issue, in the absence of a statute, requires that federal judge-made law be applied to resolve the

208. *Cf. Pennzoil Co. v. Federal Energy Regulatory Comm'n*, 645 F.2d 360, 385-86 (5th Cir. 1981) (The court stated that uniformity of result was not assured by the creation of federal common law in this situation since identical language in different contracts could be interpreted to have different meanings.).

209. *Cf. Pennsylvania v. Nelson*, 350 U.S. 497, 505-06 (1956) (The court examined the danger of enforcing state sedition acts in regard to the administration of the federal program.).

210. *Id.*

211. See note 49 and accompanying text *supra*.

212. See 42 C.F.R. §§405.401-405.454 (1980); *Cf. United States v. Dansby*, 509 F. Supp. 188, 194-95 (N.D. Ohio 1981) (The court, applying policy considerations to the FMHA loan program, reached a contrary result since a uniform federal rule was not necessary to reasonably achieve the obligations of the program.).

213. *Cf. 645 F.2d at 385* (The court held that a contract subject to federal regulation does not by itself demonstrate that Congress intended federal rather than state law to govern all aspects of its performance.).

214. *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 727 (1979); *Clearfield Trust Co. v. United States*, 318 U.S. 363, 367 (1943); see also *Mishkin*, *supra* note 41, at 800.

controversy.²¹⁵

Considering the above factors, *i.e.*, the need for national uniformity, the disruption of commercial relationships predicated on state law, the frustration of specific objectives of the Medicare program, the administrative hardship involved by failing to use one rule, the uniform statutory scheme of the program, the direct effect on financial obligations of the United States, and the substantial federal interest in the outcome of the litigation, the balance weighs heavily in favor of a federal uniform rule of decision in this area.²¹⁶ Although a uniform rule may intrude into established state commercial practices and relationships and may conflict with the individual desire of a state to apply their own piercing doctrines to further their own particular interests,²¹⁷ the decision to formulate a uniform rule may be supported by more decisive factors. The deciding factor should be the purpose behind a specific program and the rule that most accurately promotes that purpose.²¹⁸ Medicare's right to reimbursement could be severely hindered and the entire Medicare system could suffer without the use of a uniform rule. The efficient and effective operation of the program requires the exercise of judge-made law to protect and to effectuate the dominant federal scheme.²¹⁹ The exact parameters of this uniform rule must be addressed to facilitate understanding of the implications of its use.

B. Federal Uniform Rule of Decision: What is the Rule?

Once a determination is made that a federal uniform rule of decision should be applied in this area, further examination of *Pisani*, *Normandy*, *Thomas*, and *Town of Brookline*, as well as their progenitors, is necessary to define the substance of the rule. In *Normandy*, the earliest decision, the federal district court set forth an alternative holding whereby the corporate entity could be disregarded when failure to do so would lead to circumvention of a statute or avoidance of a clear legislative purpose.²²⁰ Although the main holding of the case was

215. 318 U.S. at 367.

216. *United States v. Pisani*, 646 F.2d 83, 87 (3d Cir. 1981). See generally *Holbrook v. Pitt*, 643 F.2d 1261 (7th Cir. 1981); *In re "Agent Orange" Product Liability Litigation*, 635 F.2d 987 (2d Cir. 1980); *Boyster v. Roden*, 628 F.2d 1121 (8th Cir. 1980); *First S. Fed. Sav. v. First S. Sav.*, 614 F.2d 71 (5th Cir. 1980); *Rust v. Johnson*, 597 F.2d 174 (9th Cir. 1979); *Schlake v. Beatrice Production Credit Ass'n*, 596 F.2d 278 (8th Cir. 1979); *United States v. Carson*, 372 F.2d 429 (6th Cir. 1967); *United States v. Sommerville*, 324 F.2d 712 (3d Cir. 1963); *United States v. Dansby*, 509 F. Supp. 188 (N.D. Ohio 1981); *United States v. Chatlin's Dept. Store, Inc.*, 506 F. Supp. 108 (E.D. Penn. 1980); *City of New Orleans v. United Gas Pipe Line Co.*, 390 F. Supp. 861 (E.D. La. 1974).

217. See notes 20-24 and accompanying text *supra*.

218. 646 F.2d at 86 (The most important factor in the adoption decision is whether state law would frustrate specific objectives of the federal program.).

219. See note 216 and accompanying text *supra*.

220. *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421, 424 (D. Mass. 1977).

based on an alter ego theory, the language used by the court makes it clear that the same result would be obtained in the case under the circumvention of a statute approach.²²¹ If the government were unable to recoup overpayments from the provider, one of the goals of the Medicare program would be frustrated—namely, that the government not be charged for more than the reasonable cost of services rendered.²²² The *Normandy* court was not the first court to state that the protective corporate veil could be pierced based on an act which served to undermine a substantial legislative purpose, absent a showing of the unity of interest and injustice elements normally required.²²³ Other cases relied upon by the court in *Normandy* included *Quinn v. Butz*,²²⁴ *Bruhn's Freezer Meats of Chicago, Inc. v. United States Department of Agriculture*,²²⁵ *Maley v. Carroll*,²²⁶ *H.P. Lambert Co. v. Secretary of the Treasury*,²²⁷ and *Mansfield Journal Co. v. F.C.C.*²²⁸

In *Quinn*, the United States District of Columbia Circuit Court of Appeals placed primary emphasis on the traditional unity of interest and injustice requirements.²²⁹ Specifically, the court urged that the corporate veil be pierced primarily to avoid injustice.²³⁰ Nevertheless, the court went on to quote from *Lambert* and stated that regardless of the importance of the corporate form, it could not be used to stand in the way of regulatory procedures.²³¹ The *Quinn* court further quoted from *Mansfield* and held that “[t]o carry out statutory objectives, it is frequently necessary to seek out and to give weight to the identity and characteristics of the controlling officers and stockholders of a corporation.”²³² The court in *Normandy* interpreted this language to allow disregarding the corporate entity when an act by the corporation served to undermine a substantial federal legislative purpose regardless of the existence of any wrongful conduct.²³³ The United States Third Circuit Court of Appeals reinforced the *Normandy* interpretation in *Bruhn's Freezer Meats* by holding that “an order limited in its application only to the corporate petitioners probably would prove futile as the corporations could be dissolved and the individual petitioners could then,

221. *Id.* at 424-25.

222. *Id.* at 425.

223. *Id.* at 424-25. See note 90 and accompanying text *supra*.

224. 510 F.2d 743 (D.C. Cir. 1975).

225. 438 F.2d 1332 (8th Cir. 1971).

226. 381 F.2d 147 (5th Cir. 1967).

227. 354 F.2d 819 (1st Cir. 1965).

228. 180 F.2d 28 (D.C. Cir. 1950).

229. 510 F.2d at 758-59.

230. *Id.* at 759.

231. *Id.*; see also 354 F.2d at 822.

232. 510 F.2d at 758-59; see also 180 F.2d at 37.

233. *United States v. Normandy House Nursing Home, Inc.*, 428 F. Supp. 421, 424-25 (D. Mass. 1977).

under the cloak of new corporations, engage in the proscribed activities and thereby frustrate the purposes of the Act."²³⁴ The court in *Bruhn's Freezer Meats* also stated that "[t]he law is well settled that the corporate entity may be disregarded when the failure to do so would enable the corporate device to be used to circumvent a statute."²³⁵

The *Maley* court focused primarily on the alter ego theory as a basis for disregarding the corporate entity.²³⁶ The federal appellate court held that before equity will destroy rights, "there must be evidence of clear fraud, use of a corporation as an alter ego, infidelity of a fiduciary, *purposeful* avoidance of a statutory duty, or a similar species of such genera."²³⁷ Although this language appears to leave room for the *Normandy* interpretation that circumvention of a statutory purpose is enough to allow for disregarding the corporate entity, the requirement of "purposeful avoidance" of a statutory duty mandates a stricter standard than that subsequently required in *Normandy*. According to the court in *Normandy*, no fraudulent intent or wrongful conduct was required. Rather, any act that frustrated a clear legislative purpose permitted piercing the corporate veil.²³⁸

The interpretation in *Normandy* of these cases was later followed in *Pisani* wherein the court merely restated the alternative holding in *Normandy*.²³⁹ In addition, the federal district court in *Thomas* supported the use of circumvention of a statute or avoidance of a clear legislative purpose as an independent ground for piercing by holding that circumvention of a statute violated public policy and that the corporate form should be disregarded when recognition would defeat public policy.²⁴⁰ Finally, in *Town of Brookline*, the United States First Circuit Court of Appeals required the federal courts to look closely at the purpose of the federal statute to see whether the statute placed importance on the corporate form, an inquiry that gave less respect to the corporate form

234. *Bruhn's Freezer Meats of Chicago, Inc. v. United States Dept. of Agriculture*, 438 F.2d 1332, 1343 (8th Cir. 1971).

235. *Id.*; see, e.g., *Schenley Distillers Corp. v. United States*, 326 U.S. 432, 437 (1945); *United States v. Lehigh Valley R. R.*, 220 U.S. 257, 259 (1911); *Kavanaugh v. Ford Motor Co.*, 353 F.2d 710, 717 (7th Cir. 1965); *Joseph A. Kaplan & Sons, Inc. v. F.T.C.*, 347 F.2d 785, 787 n.4 (D.C. Cir. 1965); see also *Fletcher*, *supra* note 1, §45 (1963).

236. *Maley v. Carroll*, 381 F.2d 147, 152-54 (5th Cir. 1967).

237. *Id.* at 155 (emphasis added). In dictum, the court expressed the proper standard for disregarding the corporate entity:

While corporate entities may be disregarded where they are made the implement for avoiding a clear legislative purpose, they will not be disregarded where those in control have deliberately adopted the corporate form in order to secure its advantages and where no violence to the legislative purpose is done by treating the corporate entity as a separate legal person.

Id. (quoting *Schenley Distillers Corp. v. United States*, 326 U.S. 432, 437 (1946)).

238. 428 F. Supp. at 424-25.

239. *United States v. Pisani*, 646 F.2d 83, 88-89 (3d Cir. 1981).

240. *United States v. Thomas*, 515 F. Supp. 1351, 1357 (W.D. Tex. 1981).

than the strict common law alter ego theory.²⁴¹

Thus, when federal courts apply federal common law in the case of Medicare's right to reimbursement, they are applying essentially the traditional state test of unity of interest and injustice in the particular situation.²⁴² Another element, however, has been added to this traditional test by the federal courts. This element, circumvention of a statutory objective, serves as an independent ground for piercing the corporate veil.²⁴³ The test is based solely on an interpretation of the purpose of the federal scheme in order to assure that relevant aims are not obviated by the actions of corporations and individuals.²⁴⁴ This single element approach substantially alleviates the government's burden of proof in actions seeking to impose shareholder liability for the debts of the corporation.²⁴⁵ Consequently, this uniform rule could have a substantial impact on corporations throughout the United States. These potential ramifications could be felt even in California, a state considered quite liberal in terms of disregarding the corporate entity.

C. Impact of A Uniform Rule of Decision on California Corporations

The use of circumvention of a statutory purpose as an independent ground to justify piercing the corporate veil could seriously affect California corporations. Applying this federal uniform rule of decision in cases involving Medicare's right to reimbursement, as opposed to using the traditional state piercing doctrines, will justify disregarding the corporate entity when a clear statutory purpose is frustrated.²⁴⁶ Nothing akin to this test for piercing exists at the state-level.²⁴⁷ Although California is considered to be liberal in its application of the piercing doctrine,²⁴⁸ this federal circumvention of a statute approach to piercing requires an even lesser burden of proof than that required by *Minton* wherein theoretically inadequate capitalization alone was enough to justify piercing the corporate veil. The potential difference in result is further amplified by the fact that at least two subsequent California appellate courts have failed to follow the proposition in *Minton*.²⁴⁹ The

241. *Town of Brookline v. Gorsuch*, 667 F.2d 215, 221 (1st Cir. 1981).

242. See notes 229-241 and accompanying text *supra*.

243. 646 F.2d at 88; 428 F. Supp. at 424.

244. 646 F.2d at 88; 428 F. Supp. at 424.

245. *Marget, Shareholder Liability—Lakota Girl Scout Council, Inc. v. Havey Fund-Raising Management, Inc.—A Single-Factor Test?*, 3 J. CORP. L. 219, 234 (1977).

246. See notes 90-99 and accompanying text *supra*.

247. See notes 6, 61, 90-99 and accompanying text *supra*.

248. See *Dobbyn*, *supra* note 29, at 192; *Krendl & Krendl*, *supra* note 24.

249. *Pearl v. Shore*, 17 Cal. App. 3d 608, 95 Cal. Rptr. 157 (1971); *Harris v. Curtis*, 8 Cal. App. 3d 837, 87 Cal. Rptr. 614 (1970).

effect of these two holdings is that the piercing doctrine in California may not be as liberal as case law has appeared to suggest.

The federal uniform rule of decision on piercing requires finding only that a statute has been circumvented.²⁵⁰ There is no requirement that the individual shareholders have dominion over a corporation so that for all practical purposes the separate personalities are negated, nor is there a requirement that failure to pierce the veil produce an unjust result.²⁵¹ Furthermore, this rule of decision does not require a finding that a particular corporation is inadequately capitalized.²⁵² In fact, the provider corporation may be adequately capitalized, may adhere to all corporate formalities, and may be entirely without fraudulent intent or wrongful conduct, and yet the mere inability to pay the Medicare program may require imposing personal liability on the individual shareholder or shareholders.²⁵³ As a result, the traditional doctrine of limited liability could be significantly weakened in this area.

The implications of this uniform rule of decision easily could be extended into areas other than Medicare's right to reimbursement from providers. Although avoidance of a statutory aim, absent a showing of fraud or other improper purpose, has been perhaps carried to its extreme position in the limited area of Medicare's right to reimbursement under a special regulatory payment scheme, the language used by the courts does not confine the use of the rule to this specific area.²⁵⁴ Rather, a fair reading of the cases reveals that this uniform piercing rationale may be used in any situation in which the federal government is a party representing the interests of a nationwide program.²⁵⁵ The extension of this rule to other areas could significantly hinder the corporate entity. Conceivably, California would no longer be able to protect individual shareholders from personal liability in any situation when the corporation was dealing with a national government program.²⁵⁶ The government could control the determination of individual liability in all areas involving a substantial federal program through the creation of a comprehensive statutory scheme.²⁵⁷ California corporations would be required to closely abide by the rules and regulations of these federal programs to prevent circumvention of a statutory purpose and to guarantee that the individual shareholders are not held personally liable for the debts of an insolvent corporation.

250. 646 F.2d at 88; 428 F. Supp. at 424.

251. 646 F.2d at 88; 428 F. Supp. at 424.

252. 646 F.2d at 88; 428 F. Supp. at 424.

253. 646 F.2d at 88; 428 F. Supp. at 424.

254. See notes 219-241 and accompanying text *supra*.

255. See notes 219-241 and accompanying text *supra*.

256. See notes 219-241 and accompanying text *supra*.

257. See notes 219-241 and accompanying text *supra*.

CONCLUSION

Limited liability has become a concept which is fundamental to the law of every jurisdiction in the United States. When the doctrine is used beyond its reason and policy, however, courts will disregard the corporate entity and hold the shareholders personally liable for the debts and obligations of the corporation. Confusion surrounds the decision whether the corporate veil will be pierced. Application of the doctrine varies from state to state, and at times, even within a particular state. This ambiguity is then coupled with an unclear determination of whether state law or a uniform rule of decision is to be used in a case where federal law is controlling. Perhaps the most perplexing aspect of the problem is an analysis of the factors and elements employed by the federal courts in their decision to disregard the corporate entity.

This comment has examined the criteria relevant to the decision of whether state law or federal law should govern in the limited area of Medicare's right to reimbursement from providers under the program. The national character of the program, as well as the federal statutory right to reimbursement, requires that federal law be applied. In ascertaining the need for a uniform rule as opposed to using state law, numerous factors have been established and evaluated. *Pisani* is the authority in this area and correctly applies a uniform rule of decision as the governing federal law.

Nevertheless, the real impact of the decision to apply a uniform rule on the traditional piercing doctrine is dependent upon the substance of the federal rule. *Pisani* and *Normandy* establish that circumvention of a statute or avoidance of a clear legislative purpose may serve as independent grounds to justify piercing the corporate veil. This new element, existing only in the federal courts, places new importance on the decision by the federal courts either to apply the state rule or to formulate a uniform rule of decision. Since nothing akin to this new ground for disregarding the corporate entity exists at the state level, particularly in California, the effect of a uniform piercing rule on California corporations could be substantial. This new uniform rule of decision allows piercing absent a showing of wrongful conduct, fraudulent intent, inadequate capitalization, apparent injustices, or other traditional piercing factors. Consequently, the government's burden of proof in a particular case could be significantly lessened.

Although this uniform rule of decision only has been applied to a special regulatory payment system under the Medicare program, the language used by the courts indicates that this uniform piercing doctrine could be extended outside of this limited area to encompass virtu-

ally any situation in which the federal government is a party representing the interests of a nationwide program. The use of this piercing rule in areas other than Medicare could have far reaching ramifications on the corporate style of conducting business. Since the federal common law rule more readily disregards the corporate entity, it is conceivable that the doctrine of limited liability will be considerably weakened by the use of this rule. Corporations will be held to a higher standard in regard to performing their business obligations, at least whenever they engage in activities involving a substantial federal program. It becomes extremely difficult to ensure that shareholders will not be held liable for the debts of an insolvent corporation. Thus, in an attempt to maintain limited liability protection, officers, directors, and shareholders of a corporation must closely abide by pertinent rules and regulations of the various federal programs they deal with in a corporate capacity.

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