PRESERVING LIMITED LIABILITY: MITIGATING THE INEQUITIES OF REVERSE VEIL PIERCING WITH A COMPREHENSIVE FRAMEWORK

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ABSTRACT

Reverse veil piercing—a controversial exception to the traditional notion of limited liability—has enjoyed increased recognition in recent years. By facilitating access to a corporation's assets for satisfaction of a wrongdoing-shareholder's personal debt, courts have enabled a doctrine that implicates many third parties: nonculpable shareholders, corporate creditors, and the corporation's other constituencies. Unrestricted application of reverse veil piercing may prejudice these parties, impair the corporation's ability to secure credit, and thwart the policies underlying limited liability. In response, courts and commentators have suggested and adopted several approaches that seek to mitigate these inequities. None, however, are sufficient to both account for the conflicting interests of all involved parties and ensure that devious shareholders cannot hide personal assets behind the cloak of limited liability.

This Note proposes a framework that is rooted in a strong default presumption of limited liability, but allows for a narrow window of recovery within strict parameters: claimants must demonstrate commingling of assets between the wrongdoing shareholder and the corporation; recovery is limited to the corporation's surplus account, subject to an innocent shareholder exemption; and punitive damages may not be recovered from the corporation. In turn, courts complete the inquiry by balancing the claimant's interests in recovery against those of the corporation's other constituents. This approach accounts for the interests of all implicated parties, without wholly precluding recovery.

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INTRODUCTION

The American corporation is a fiction. Founded upon the notion that "corporate existence and corporate functions are distinct from that of the stockholders," this artificial legal entity operates behind a thin cloak of limited liability.[1] Thin as it is, "this distancing of individual from corporation has been referred to as the cornerstone of American business law."[2] Limited liability

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[1] Paul v. Univ. Motor Sales Co., 278 N.W. 714, 720 (Mich. 1938).

[2] Michael Richardson, *The Helter Skelter Application of the Reverse Piercing Doctrine*, 79 U. CIN. L. REV. 1605, 1607 (2011); *see also* Note, *Piercing the Corporate Law Veil: The Alter Ego Doctrine Under Federal Common Law*, 95 HARV. L. REV. 853, 854 (1982).

ensures that "shareholders in a corporation are not liable for the obligations of the enterprise beyond the capital that they contribute in exchange for their shares."[3]

Limited liability is not, however, absolute. If "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" and set aside the protections of limited liability.[4] Criticized by Benjamin Cardozo as a notion entirely "enveloped in the mists of metaphor,"[5] courts' willingness to look beyond the corporate fiction has a storied history, eventually earning the distinction of a metaphor-laden nomenclature: piercing the corporate veil.[6]

Like most equitable doctrines, the doctrine of veil piercing is a true balancing of interests. In deciding whether to set aside the corporate fiction, courts "attempt to uphold legitimate investor expectations of limited liability exposure while preventing the use of the corporate form to promote fraud, illegality, or other injustice."[7] Despite courts' increasing conviction that the veil should be drawn aside under the right circumstances, there is little consensus as to which circumstances are the right ones.[8] Rather, "[e]ach court adopts its own test in determining when it is appropriate to apply the doctrine."[9]

Notwithstanding the erratic application of veil piercing, courts often look to several common factors, organized under two general prongs of inquiry.[10] The first is unity of interest and ownership: often described as alter ego theory, courts are unwilling to adhere to the corporate fiction when "the corporation is the mere 'alter ego' of its shareholders,"[11] such that "the separate personalities of the corporation and the individual no longer exist."[12] Courts look for key indicators of impropriety between the shareholder and the corporation—cleverly coined as "[i]ndicia of alter ego"[13]: undercapitalization;[14] "commingling corporate and

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[3] Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036, 1039 (1991).
[4] *Paul v. Univ. Motor Sales Co.*, 278 N.W. at 720.
[5] Berkey v. Third Ave. Ry. Co., 155 N.E. 58, 61 (N.Y. 1926).
[6] *See, e.g.*, Weisser v. Mursam Shoe Corp., 127 F.2d 344, 348 (2d Cir. 1942).
[7] Gregory S. Crespi, *The Reverse Pierce Doctrine: Applying Appropriate Standards*, 16 J. CORP. L. 33, 34 (1990).
[8] *See* Kathryn Hespe, *Preserving Entity Shielding: How Corporations Should Respond to Reverse Piercing of the Corporate Veil*, 14 J. BUS. & SEC. L. 69, 75–76 (2013).
[9] *Id.* at 73.
[10] *See id.*; *see also* Note, *supra* note 2, at 866.
[11] Jonathan Macey & Joshua Mitts, *Finding Order in the Morass: The Real Justifications for Piercing the Corporate Veil*, 100 CORNELL L. REV. 99, 100 (2014).
[12] Note, *supra* note 2, at 854.
[13] Electro Source, LLC v. Nyko Tech., Inc., Nos. CV 01-10825 DT (BQRx), CV 02-520 DT (BQRx), 2002 WL 34536682, at *9 (C.D. Cal. Apr. 15, 2002).
[14] *See, e.g.*, Harris v. Curtis, 87 Cal. Rptr. 614, 618–19 (Cal. Ct. App. 1970).

personal funds";[15] "nonpayment of dividends";[16] "insolvency of the subservient corporation";[17] failure to observe corporate formalities, such as absence of corporate records;[18] treating the corporation as "merely a façade for the operations of the dominant stockholder";[19] using the corporation form "to promote fraud, injustice, or illegalities."[20]

Second, courts look to whether "an inequitable result will follow" if the corporate fiction is upheld.[21] Though "less well-defined" than alter ego theory, this prong allows the court to evaluate individual circumstances and flex its equitable muscles in determining whether veil piercing is necessary to prevent an injustice.[22]

While traditional veil piercing is controversial in its own right, the last several decades have seen "a growing recognition of the doctrine of *reverse* piercing of the corporate veil"—an even broader erosion of limited liability.[23] This "peculiar development"[24] merely reverses the direction of the pierce: instead of seeking access to shareholder assets to satisfy a judgment against the corporation, "either a corporate insider or a person with a claim against a corporate insider is attempting to have the insider and the corporate entity treated as a single person for some purpose."[25]

Just as in traditional veil piercing, a litigant's most common objective in pursuing this theory is to broaden "the pool of assets available to satisfy legal liabilities."[26] Reverse veil piercing is also consistent "with traditional piercing in its goal of preventing abuse of the corporate form."[27] Functionally, its scope is

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[15] Lamar v. Am. Basketball Ass'n, 468 F. Supp. 1198, 1204 (S.D.N.Y. 1979); *see also* MP Nexlevel of Cal., Inc. v. CVIN, LLC, No. 1:14-cv-288-LJO-GSA, 2014 WL 5019639, at *11 (E.D. Cal. Oct. 7, 2014) (listing several factors that "militate[] towards finding alter ego liability," including "commingling of assets" and "treatment of the assets of the corporation as the individual's own . . . .").

[16] Ost-West-Handel Bruno Bischoff GmbH v. Project Asia Line, Inc., 970 F. Supp. 471, 478 (E.D.V.A. 1997).

[17] *Id.* at 479.

[18] *See, e.g.*, *Electro Source, LLC*, 2002 WL 34536682, at *9; MP Nexlevel of Cal., Inc., 2014 WL 5019639, at *11.

[19] Energy Marine Servs., Inc. v. DB Mobility Logistics AG, Civil Action No. 15-24-GMS, 2016 WL 284432, at *3 (D. Del. Jan. 22, 2016); *see also* Ost-West-Handel Bruno Bischoff, 970 F. Supp. at 479 ("Such indicia include . . . complete control by a dominant stockholder.").

[20] Macey & Mitts, *supra* note 11, at 100.

[21] Hespe, *supra* note 8, at 73.

[22] Note, *supra* note 2, at 855.

[23] Litchfield Asset Mgmt. Corp. v. Howell, 799 A.2d 298, 312 (Conn. App. Ct. 2002) (emphasis added).

[24] Larry E. Ribstein, *Reverse Limited Liability and the Design of the Business Association*, 30 DEL. J. CORP. L. 199, 200 (2005).

[25] Crespi, *supra* note 7, at 36.

[26] Sam F. Halabi, *Veil-Piercing's Procedure*, 67 RUTGERS U. L. REV. 1001, 1010 (2015).

[27] LFC Mktg. Grp., Inc. v. Loomis, 8 P.3d 841, 846 (Nev. 2000).

largely "limited to closely held firms in which a single insider, or a small group of insiders acting in concert, holds all or virtually all economic claims."[28]

Although there is a lack of consistency among the "principles that govern the reverse veil piercing theory,"[29] there is a standardized set of inequities that give courts pause in applying the doctrine—most notably, the potential for prejudice against nonculpable shareholders and corporate creditors.[30] The chaotic legal landscape of reverse veil piercing coupled with these inequities demands a comprehensive and structured approach to reverse veil piercing.[31]

This Note proposes a framework that is rooted in a strong presumption of limited liability. However, claimants may rebut this presumption by satisfying four elements of the proposed test. Courts finalize the analysis by weighing the competing interests presented by the case at hand before deciding to impose liability.

To make the case for this proposal, this Note proceeds in four parts. Part I discusses the unruly judicial landscape of reverse veil piercing. Part II illustrates the potential adverse consequences of unrestricted reverse piercing. Part III describes the shortcomings of various judicial approaches and other proposals. Part IV outlines this Note's proposed solution: the imposition of liability in a narrow category of cases. Finally, Part V addresses counterarguments and explains why they are not persuasive.

To best illustrate both the equitable challenges and potential solutions, this Note utilizes a hypothetical situation throughout, in which a claimant seeks to reverse pierce two related corporations. Barbara, a thriving businesswoman, owns significant equity interest in two companies. Consolidated Holdings, a closely held corporation, is owned and operated in equal part by Amy, Barbara, and

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[28] Crespi, *supra* note 7, at 69; *see also* Hespe, *supra* note 8, at 82 ("[C]ourts have only allowed reverse veil piercing in close corporations, never in public corporations.").

[29] Elham Youabian, *Reverse Piercing of the Corporate Veil: The Implications of Bypassing "Ownership" Interest*, 33 SW. U. L. REV. 573, 577 (2004).

[30] *See* Nicholas B. Allen, *Reverse Piercing of the Corporate Veil: A Straightforward Path to Justice*, 85 ST. JOHN'S L. REV. 1147, 1163–64 (2011) ("These courts cite several common objections.").

[31] This Note focuses almost exclusively on reverse piercing the traditional corporate form. For a more nuanced illustration of the specific challenges presented by reverse piercing a limited liability partnership, see Larry E. Ribstein, *Reverse Limited Liability and the Design of the Business Association*, 30 DEL. J. CORP. L. 199 (2005). *See also* Elizabeth S. Miller, *Are There Limits on Limited Liability? Owner Liability Protection and Piercing the Veil of Texas Business Entities*, 43 TEX. J. BUS. L. 405, 426–45 (2009). Occasionally, this Note will nonetheless reference cases that address reverse piercing of partnerships or other alternative corporate forms, as there is significant overlap of the equitable issues, though mitigating them may require a much broader approach in these nontraditional contexts. *See* Ribstein, *supra*, at 218–19, 228. Conversely, "whether an entity is an LLC or a corporation is a distinction without a difference for purposes of applying veil piercing principles." Miller, *supra*, at 415 (discussing the Court's holding in *In re* Moore, 379 B.R. 284, 289 n.4 (Bankr. N.D. Tex. 2007)).

Cooper. This real estate investment firm has fifteen full-time employees, and holds long-term contracts with a law firm, an accounting firm and a property management firm. The firm also owns two mixed-use apartment complexes, with several hundred residential tenants and a handful of commercial tenants each.

Barbara also sits at the helm of Barb Holdings, Inc., as the sole shareholder and President. Barb Holdings owns several parcels of undeveloped real property and has no employees. Over the years, Barbara advanced money to Barb Holdings from her own assets, receiving unsecured demand promissory notes in return. Barbara received no salary or dividends from Barb Holdings, but frequently borrowed large sums from the company, interest-free. Additionally, she utilized a business credit card in the corporation's name to pay for most of her personal expenses.

Driving home one night while intoxicated, Barbara struck a pedestrian, Peter, with her car. Barbara was subsequently held liable for tortious conduct in the amount of two million dollars in compensatory damages, and an additional one million dollars in punitive damages. Recognizing that Barbara's personal assets are likely insufficient to satisfy this judgment, Peter now seeks to attach the assets of both Barb Holdings and Consolidated Holdings, under the theory of reverse veil piercing.[32]

I. REVERSE VEIL PIERCING: BACKGROUND AND JUDICIAL APPROACHES

A. Background

Under the predominant classification system, reverse veil piercing is divided into two categories: insider and outsider. The distinction between insider and outsider reverse piercing turns on "the relative position of the persons seeking corporate disregard and their opponents."[33]

Insider reverse piercing occurs when the controlling shareholder wishes to "take advantage of corporate claims that she would be unable to bring in her individual capacity."[34] The Minnesota Supreme Court, for example, allowed individual farm owners to claim a homestead exemption from judgment creditors, despite having placed the land into a family farm corporation.[35] Though not as controversial as outsider piercing, courts nonetheless "find breaking with

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[32] The fact pattern of this hypothetical is based in part on those in Sea-Land Servs., Inc. v. Pepper Source, 941 F.2d 519, 521–22 (7th Cir. 1991) and *In re* Fett Roofing & Sheet Metal Co., 438 F. Supp. 726, 728–29 (E.D. Va. 1977).

[33] Crespi, *supra* note 7, at 37; *see also In re* Howland, 516 B.R. 163, 166 (Bankr. E.D. Ky. 2014).

[34] Allen, *supra* note 30, at 1153 n.41.

[35] *See* Cargill, Inc. v. Hedge, 375 N.W.2d 477, 478 (Minn. 1985).

traditional entity theory a difficult task," even when the shareholder seeks corporate disregard, rather than an unrelated third party.[36]

By contrast, the direction of the pierce flips in an outsider reverse pierce claim. Here, a third party claimant seeks to pierce the veil between the corporate insider and the corporation in order to "subject corporate assets to this claim"[37] and, consequently, "satisfy the debt of an individual shareholder."[38] Although the alleged wrongdoing may be related to the target corporation, more often the claimant seeks remedy "not for a harm procured by the corporation itself, but rather for the actions of an individual shareholder."[39]

Because "[t]he policies underlying the presumption of separate entity status in the outsider reverse piercing context differ . . . from the policies implicated in the insider reverse piercing context," this Note focuses primarily on outsider reverse veil piercing and its unique challenges.[40] Accordingly, the hypothetical used in this Note illustrates an outsider piercing claim: Peter seeks access to Consolidated Holdings' and Barb Holdings' assets to satisfy Barbara's personal debt to him.

Reverse veil piercing has enjoyed broad application, with courts contemplating this novel approach in many contexts. In perhaps its most successful iteration, reverse veil piercing has frequently been sought by—and granted to—the Internal Revenue Service (IRS) "for recovery of taxpayer's delinquent tax liability."[41] In *Shades Ridge Holding Co. v. United States*, for

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36 Michael J. Gaertner, *Reverse Piercing the Corporate Veil: Should Corporation Owners Have It Both Ways?*, 30 WM. & MARY L. REV. 667, 688 (1989).

37 Crespi, *supra* note 7, at 37.

38 Allen, *supra* note 30, at 1154.

39 *Id.*

40 Crespi, *supra* note 7, at 64. The equitable ramifications between the two also diverge, due to the relative position and ultimate goals of those seeking corporate disregard. Indeed, the foremost commentator to distinguish between the two types noted that, "In an insider reverse pierce, it is the shareholder or other insider that is actively seeking corporate disregard; consequently, allowance of such claims will not undermine the security of investor expectations of limited liability exposure." *Id.* at 50. Additionally, insider reverse piercing often focuses not on accessing corporate assets, but rather accessing the privilege of certain doctrines and defenses that the corporation enjoys but are unavailable to the individual shareholder. *See* Gaertner, *supra* note 36, at 696–97 (discussing a case in which the Court was faced with deciding "whether the parent [corporation] was entitled to statutory immunity" under insider reverse veil piercing). For a discussion on the distinct equitable challenges presented by insider reverse veil piercing, see Crespi, *supra* note 7, at 50–55, and Gaertner, *supra* note 36, at 681–96.

41 Youabian, *supra* note 29, at 578 (discussing Towe Antique Ford Found. v. IRS, 999 F.2d 1387 (9th Cir. 1993)); *see also* Allen, *supra* note 30, at 1156 ("Reverse piercing has met the least resistance when invoked by the government, most commonly to obtain payment of taxes owed by individuals."); *see, e.g.*, United States v. Scherping, 187 F.3d 796, 803 (8th Cir. 1999) (noting that "reverse piercing is a well-established theory in the federal tax realm."). *But see* Floyd v. IRS, 151 F.3d 1295 (10th Cir. 1998) (refusing to reverse pierce a taxpayer's corporation for the purposes of collecting delinquent tax dues).

example, the Eleventh Circuit Court of Appeals allowed the IRS to collect the taxpayer's tax liability from the assets of a corporation he "truly controlled."[42] Observing that under Supreme Court precedent, "[p]roperty of the nominee or alter ego of a taxpayer is subject to the collection of the taxpayer's tax liability," the Court found that the corporation was, in fact, the taxpayer's alter ego.[43] Notably, the Court disregarded the veil even though the taxpayer owned no stock in the company, rather relying on the fact that the taxpayer had "total control" over the corporation.[44]

Creditors of shareholders' individual debts, such as in bankruptcy proceedings, have enjoyed similar success in using reverse veil piercing to access a corporation's assets.[45] Some courts are influenced by the nature and legitimacy of the corporate form in deciding whether to pierce, valuing substance over form.[46] Others have demonstrated a seemingly excessive willingness to reverse pierce in bankruptcy proceedings "even when it is undisputed that the debtor did not intend to defraud any creditors and when the formal elements of a fraudulent conveyance are not addressed."[47]

Family law has also witnessed an influx of reverse veil piercing cases.[48] Often observed in divorce proceedings, reverse veil piercing allows "the court to reach corporate assets and divide them as part of the community estate."[49] This approach usually takes the form of one spouse seeking to attach the other's "alter ego" corporation.[50] Finally, tort plaintiffs have at times invoked reverse veil piercing in the hopes of satisfying their judgment against a shareholder-wrongdoer.[51] Some courts have even noted greater willingness to reverse pierce for an involuntary tort creditor than for consensual contract creditors.[52]

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42 Shades Ridge Holding Co. v. United States, 888 F.2d 725, 729 (11th Cir. 1989).

43 *Id.* at 728–29 (discussing G.M. Leasing Corp. v. United States, 429 U.S. 338 (1977)).

44 *Id.* at 729.

45 *See, e.g.*, Goya Foods, Inc v. Unanue-Casal, 982 F. Supp. 103 (D.P.R. 1997); Shamrock Oil & Gas Co. v. Ethridge, 159 F. Supp. 693 (D. Colo. 1958).

46 *See In re* Schuster, 132 B.R. 604, 612 (D. Minn. 1991) (reverse piercing the corporate veil in order to disallow "a legal fiction—the facade of the family corporation—to triumph over substance—Debtor's accrual and retention of nonexempt wealth, in the face of his insolvency and discharge from debt.").

47 Richardson, *supra* note 2, at 1618 (discussing *In re* Mass, 178 B.R. 626 (M.D. Pa. 1995)).

48 *See, e.g.*, Zisblatt v. Zisblatt, 693 S.W.2d 944 (Tex. App. 1985); W. G. Platts, Inc. v. Platts, 298 P.2d 1107 (Wash. 1956).

49 Miller, *supra* note 31, at 415.

50 Youabian, *supra* note 29, at 591.

51 *See* Crespi, *supra* note 7, at 34.

52 *See id.* at 62; *see also* Allen, *supra* note 30, at 1164.

B. Judicial Approaches

Though varied, courts' attitudes towards and responses to reverse veil piercing can be loosely categorized into four distinct approaches. The first, and most straightforward, is a complete bar on this controversial doctrine. Most notably, the Tenth Circuit Court of Appeals has categorically rejected reverse veil piercing.[53] This is true even in tax cases, where courts have historically been most comfortable applying the doctrine.[54] Hawaiian courts are also wary of the doctrine, generally refusing to reverse pierce.[55]

In rejecting reverse veil piercing, courts often cite concerns about "the potential harm reverse piercing could bring to both innocent shareholders and corporate creditors."[56] Additionally, courts argue that the doctrine "violates normal judgment collection procedures," noting that "other, more traditional, remedies exist to provide plaintiffs with redress without resorting to the drastic remedy of reverse piercing the corporate veil."[57] Some even speculate that reverse piercing "could damage businesses [sic] ability to obtain credit as a result of the greater fear of losing assets."[58]

In jurisdictions that acknowledge reverse veil piercing, the "inverse method" is perhaps the most common.[59] Looking to function over form, courts simply invert the traditional two-pronged veil piercing test to determine whether the corporate form should be disregarded, reasoning that "the direction of the piercing was immaterial where the general tests supporting it had been met."[60] Accordingly, the claimant must demonstrate unity of interest and ownership (typically by pointing to the various indicia of alter ego) and prove that an inequitable result would follow if the court refuses to impose liability.[61] Courts recognizing the inverse method cite "the need for the court to 'avoid an over-rigid preoccupation with questions of structure . . . and apply the preexisting and

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[53] *See* Susan A. Kraemer, *Corporate Law*, 76 DENV. U. L. REV. 729, 737–41 (1999); *see also* Cascade Energy & Metals Corp. v. Banks, 896 F.2d 1557 (10th Cir. 1990); Floyd v. IRS, 151 F.3d 1295 (10th Cir. 1998).

[54] *See* Floyd v. IRS, 151 F.3d 1295 (10th Cir. 1998); Allen, *supra* note 30, at 1156.

[55] *See* Youabian, *supra* note 29, at 588.

[56] Allen, *supra* note 30, at 1163–64.

[57] *Id.* at 1164.

[58] Richardson, *supra* note 2, at 1615.

[59] Allen, *supra* note 30, at 1158 ("The inverse method of reverse piercing has been, by far, the most widely accepted approach to reverse piercing, with at least ten states utilizing the same test for both traditional and reverse veil piercing.").

[60] Litchfield Asset Mgmt. Corp. v. Howell, 799 A.2d 298, 311 (Conn. App. Ct. 2002); *see* Allen, *supra* note 30, at 1158–59.

[61] *See supra* notes 11–22 and accompanying text.

overarching principle that liability is imposed to reach an equitable result'" when the traditional test is satisfied.[62]

Because the traditional veil piercing test consists of a stunning plethora of assessments, inquiries, and factors, this necessarily means that courts applying reverse piercing under the same test they use for traditional piercing are equally scattered in their methods.[63] One consequence is that when the unity prong of the traditional test requires a showing of domination—that the shareholder exercised total control over the corporation—the inverse test "would impose on a plaintiff the seemingly impossible task of showing that a corporation dominated an individual or that a subsidiary dominated its parent corporation."[64] Indeed, the earliest known opinion to contemplate reverse piercing[65] imposed a unity of interest and control requirement identical to that of traditional veil piercing, even while noting its improbability[66]: *Kingston Dry Dock Co. v. Lake Champlain Transportation Co.* stood "for the proposition that the highly unusual circumstance of a subsidiary dominating its parent is a virtual prerequisite for finding the kind of unity of interest that would allow an outsider reverse pierce in an inter-corporate relationship context."[67]

As one leading scholar noted, "[i]f the [inverse method] and the Tenth Circuit doctrine can be seen as opposite ends of the spectrum, state courts and the federal courts applying their law have explored nearly every shade in between."[68] Rather than completely rejecting the doctrine or adopting the rigid and highly structuralized inverse method, many courts have instead taken a more flexible equitable results approach, by "craft[ing] a remedy that could protect the interests of judgment creditors, innocent shareholders, and corporate creditors alike."[69]

Some courts have accomplished this by explicitly adding an additional requirement onto the traditional veil piercing test—that "an equitable result is achieved by piercing."[70] In applying this additional criterion, some courts conduct a case-by-case inquiry into whether "innocent shareholders or creditors would be

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[62] *Litchfield Asset Mgmt. Corp.*, 799 A.2d at 312 (quoting LiButti v. United States, 107 F.3d 110, 119 (2d Cir. 1997)).

[63] *See* Hespe, *supra* note 8, at 73.

[64] Allen, *supra* note 30, at 1159.

[65] *See* Crespi, *supra* note 7, at 56.

[66] *See* Kingston Dry Dock Co. v. Lake Champlain Transp. Co., 31 F.2d 265, 267 (2d Cir. 1929).

[67] Crespi, *supra* note 7, at 67.

[68] Richardson, *supra* note 2, at 1616.

[69] Allen, *supra* note 30, at 1160–61; *see, e.g.*, Century Hotels v. United States, 952 F.2d 107, 112 (5th Cir. 1992) (quoting Krivo Indus. Supply Co. v. Nat'l Distillers & Chem. Corp., 483 F.2d 1098, 1102–03 (5th Cir. 1973)) ("[T]he courts will look through the forms to the realities of the relation between the companies as if the corporate agency did not exist and will deal with them as the justice of the case may require.").

[70] *In re* Phillips, 139 P.3d 639, 646 (Colo. 2006).

prejudiced by outside reverse piercing."[71] Others evaluate many "different factors in determining where to draw the line between acceptable and unacceptable reverse piercing of the corporate veil,"[72] often looking to "issues that are specifically implicated in the reverse piercing situation, such as the impact on innocent third parties."[73]

Ultimately, the equitable results approach can be most succinctly summarized as a "balancing of the relevant interests."[74] Though it is difficult to generalize with such an unstructured approach, courts applying an equitable lens over the traditional test seem to be more willing to reverse pierce when "no other corporate shareholders were involved and no other creditors were in line to collect."[75] On the other end of the spectrum, however, some have gone so far as to eschew an ownership requirement altogether.[76] Ownership is an integral part of the traditional alter ego test, yet "some courts have ignored this factor and found alter ego liability based on control" only.[77] For example, the Court in *LFC Marketing Group v. Loomis* allowed the plaintiffs to reverse pierce a corporation controlled by the defendant, even though it was wholly owned by his non-culpable brother.[78]

Finally, some jurisdictions have simply not addressed reverse veil piercing at all.[79] Though many jurisdictions have acquiesced to this departure from "traditional corporate law notions of limited liability," the doctrine is by no means ubiquitous.[80] Delaware, for example—home of "the most important corporation law in the United States"[81]—has never expressly acknowledged reverse veil piercing.[82]

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[71] *Id.*
[72] Richardson, *supra* note 2, at 1616.
[73] Hespe, *supra* note 8, at 80; *see, e.g.*, C.F. Trust, Inc. v. First Flight L.P., 580 S.E.2d 806, 811 (Va. 2003) ("[A] court considering reverse veil piercing must weigh the impact of such action upon innocent investors . . . . [and] innocent secured and unsecured creditors.").
[74] Gaertner, *supra* note 36, at 687.
[75] Youabian, *supra* note 29, at 580.
[76] *See, e.g.*, LFC Mktg. Grp., Inc. v. Loomis, 8 P.3d 841, 847 (Nev. 2000) ("Although ownership of corporate shares is a strong factor favoring unity of ownership and interest, the absence of corporate ownership is not automatically a controlling event.").
[77] Youabian, *supra* note 29, at 592.
[78] *See LFC Mktg. Grp., Inc.*, 8 P.3d at 847–48.
[79] *See* Hespe, *supra* note 8, at 77 n.69.
[80] Kraemer, *supra* note 53, at 736.
[81] Curtis Alva, *Delaware and the Market for Corporate Charters: History and Agency*, 15 DEL. J. CORP. L. 885, 889 (1990)).
[82] *See* Sky Cable, LLC v. Cooley, No. 5:11cv00048, 2016 WL 3926492, at *13 (W.D. Va. July 18, 2016); Hespe, *supra* note 8, at 77 n.69.

II. THE INEQUITIES OF HAPHAZARD REVERSE VEIL PIERCING

Courts and commentators alike have expressed unease about the many potential consequences that flow from a haphazard application of reverse veil piercing. The most obvious and common concern that arises from this controversial doctrine is the potential harm to innocent shareholders. Specifically, "if other, non-culpable shareholders of the corporate entity exist, they will be unfairly prejudiced if the creditors of a corporate insider can directly attach the corporate assets."[83]

Another related concern is that reverse veil piercing may "undermine the shareholders' expectation of the risks and liabilities that their individual investments in the corporation will be exposed to when the corporation is held liable for another shareholder's debt."[84] Shareholders are expected to base investment decisions on a corporation's perceived profitability, as well as the risk that "that the actual financial reward will differ from the expected one."[85] Shareholders primarily (if not exclusively) consider economic concerns, such as the company's past performance, corporate structure, leverage ratio, and other financial variables.[86] By contrast, investors are incapable of taking into account personal endeavors of existing (and future) shareholders that could one day result in personal liability.[87] Unexpected exposure to such indeterminate risks may

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[83] Crespi, *supra* note 7, at 67.

[84] Youabian, *supra* note 29, at 574.

[85] Dennis S. Corgill, *Securities as Investments at Risk*, 67 TULANE L. REV. 861, 871 (1993); *see also* Virginia Harper Ho, *Risk-Related Activism: The Business Case for Monitoring Nonfinancial Risk*, 41 J. Corp. L. 647, 650 (2016) ("[R]isk matters to all investors because firm profitability and investment returns depend on the associated risk.").

[86] *See* Dennis S. Corgill, *Securities as Investments at Risk*, 67 TULANE L. REV. 861, 871 (1993). Federal securities laws, for example, acknowledge risk management as an important part of shareholder decision-making and seek to facilitate it by mandating disclosure of financial information. *See What We Do*, U.S. SEC. & EXCHANGE COMMISSION, https://www.sec.gov/about/whatwedo.shtml (last visited Mar. 8, 2017) ("The laws and rules that govern the securities industry in the United States derive from a simple and straightforward concept: all investors, whether large institutions or private individuals, should have access to certain basic facts about an investment prior to buying it, and so long as they hold it. To achieve this, the SEC requires public companies to disclose meaningful financial and other information to the public. This provides a common pool of knowledge for all investors to use to judge for themselves whether to buy, sell, or hold a particular security."); *see also In re* Universal Camera Corp., Securities Act Release No. 3076, 1945 WL 26104, at *7 (June 28, 1945) ("The Act leaves it to the investor, on the basis of the facts disclosed, to weight the earning prospects of a registered security against the risks involved and to judge for himself whether he wishes to invest his money in it.").

[87] Notably absent from federal securities registration requirements, for example, is any information about other shareholders. *See Form S-1: Registration Statement Under the Securities Act of 1933*, U.S. SEC. & EXCHANGE COMMISSION, https://www.sec.gov/about/forms/forms-1.pdf (last visited Mar. 8, 2017).

reduce investors' appetite for purchasing corporate ownership.[88] Chief among these, of course, is the risk that innocent shareholders may lose "their entire investment because essential assets were sold off to pay the debts of a majority owner."[89]

This concern is not exclusive to shareholders. Corporate creditors expect even greater security for their investments; debts are contractually safeguarded and assets are often pledged as collateral in case of breach to provide maximum assurance that creditors' investments will be reasonably protected.[90] Reverse veil piercing undermines these expectations: "[C]reditors who extended credit to the corporation in reliance on its assets would be left unprotected if those assets were sold off to satisfy a judgment unrelated to the corporation."[91]

"[T]he possibility of losing their collateral to an individual shareholder's creditors" may even impact creditors' willingness to issue loans in the first place.[92] Even if not altogether reluctant, lenders may "take steps to shield themselves from this increased risk" by applying "altered risk calculations to spread the cost of individual misdeeds across all small businesses."[93] Lenders can mitigate increased risk of default and loss of collateral, but only with a commensurate increase in compensation.[94] "[T]he result could be a general chilling of the ability of small businesses with few owners to receive financing," thus adversely affecting corporations' effectiveness in securing credit.[95] Taken together with shareholders' reluctance, reverse veil piercing carries the potential to impair both the corporation's ability to take on debt and its ability to raise equity capital.

Unlike the doctrine's effect on shareholders and creditors, discussed at length by many, few have explored its impact on the corporation's other constituencies. Like the other inequities, concern for constituencies is a mere continuation of the common sentiment that reverse veil piercing "fails to protect innocent third parties that would suffer a detriment if the corporation's assets

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[88] *See* Allen, *supra* note 30, at 1164 ("[L]osing out to an individual shareholder's creditors will ultimately reduce the effectiveness of corporations as a means of raising capital, through the extension of credit.").

[89] Richardson, *supra* note 2, at 1624.

[90] *See* Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89, 91 (1985); Ann E. Conaway Stilson, *Reexamining the Fiduciary Paradigm at Corporate Insolvency and Dissolution: Defining Directors' Duties to Creditors*, 20 DEL. J. CORP. L. 1, 104 (1995); Mark E. Van Der Weide, *Against Fiduciary Duties to Corporate Stakeholders*, 21 Del. J. Corp. L. 27, 46 (1996).

[91] Allen, *supra* note 30, at 1164.

[92] Youabian, *supra* note 29, at 587–88 (discussing the reasoning behind the Court's decision to reject the doctrine in Floyd v. IRS, 151 F.3d 1295 (10th Cir. 1998)).

[93] Richardson, *supra* note 2, at 1628.

[94] *See* Youabian, *supra* note 29, at 588.

[95] Richardson, *supra* note 2, at 1628.

were attached."[96] Third parties, however, comprise more than just shareholders and creditors. While the corporation's legal priorities lie with these primary constituents, companies are regularly engaged with a secondary set of constituencies: the workers they employ, the customers they conduct business with, and the communities they operate in. Contemplating theories of management, corporations themselves note "the need for 'balancing' the interests of 'shareholders, customers, employees, vendors, and the community we live in.'"[97] Some even view for-profit corporations as community citizens who engage in productive activity that possesses an important social value.[98] Indeed, corporations have gradually become cognizant of their role in solving various "public goods problems,"[99] and have assumed "more and more responsibilities as social institutions."[100] To this end, community involvement, such as giving research grants, contributing to charity, and implementing community development programs has become "accepted business practice"[101]; corporations increasingly look "upon such 'socially responsible' behavior as a way to improve the general business climate."[102]

By threatening the corporation's continued viability, reverse veil piercing might indirectly harm these secondary constituents. The workforce may be reduced, charity could fall by the wayside, and community involvement would likely fall victim to the immediate priority of restoring the company. Though perhaps intangible, this impact could be pronounced if judgment recoveries significantly deplete corporations' assets.

Ultimately, these inequities demand a wary approach in deciding when to reverse pierce. On the other hand, "[f]ailure to allow reverse piercing in certain instances . . . essentially provides 'a roadmap' to debtors on how to avoid payment of their outstanding obligations by crafting the outer limits of traditional remedies and placing action outside those limits beyond the reach of judicial intervention."[103] Consequently, any comprehensive approach to reverse veil

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[96] Hespe, *supra* note 8, at 77.

[97] Greg Urban, *Why For-Profit Corporations and Citizenship?*, *in* CORPORATIONS AND CITIZENSHIP 1, 26 (Greg Urban ed., 2014).

[98] *See* Nien-hê Hsieh, *Can For-Profit Corporations Be Good Citizens? Perspectives from Four Business Leaders*, *in* CORPORATIONS AND CITIZENSHIP 289, 299 (Greg Urban ed., 2014).

[99] Lynn Sharp Paine, *Corporate Power and the Public Good*, *in* CORPORATIONS AND CITIZENSHIP 31, 35–36 (Greg Urban ed., 2014).

[100] Margaret M. Blair, *Whose Interests Should Corporations Serve?*, *in* THE CORPORATION AND ITS STAKEHOLDERS 47, 53 (Max B.E. Clarkson ed., 1998).

[101] *Id.* at 53.

[102] *Id.* at 54.

[103] Allen, *supra* note 30, at 1166 (quoting C.F. Trust, Inc. v. First Flight L.P., 140 F. Supp. 2d 628, 642 (E.D. Va. 2001), *aff'd*, 338 F.3d 316 (2003)); *see also* Hespe, *supra* note 8, at 82 (describing "steps that corporations can take that may make them less likely to be pierced.").

piercing must balance "the conflicting interests of all involved parties" and simultaneously provide structure and certainty.[104]

III. EXISTING APPROACHES ARE INADEQUATE AT ACHIEVING A BALANCE OF INTERESTS

In addition to the judicial approaches, commentators have proposed several tests, hoping to mitigate the acknowledged inequities of reverse veil piercing. Each of these proposals falls short of successfully balancing all parties' interests.

A. Complete Bar

At first glance, the Tenth Circuit's complete bar on reverse veil piercing may be appealing.[105] It is logical to assume that prohibiting this controversial doctrine automatically eliminates all concerns about prejudiced third parties. A careful analysis of alternative recovery methods, however, shows otherwise. Under traditional judgment collection procedures in which the defendant's corporate shares may be attached as assets, the creditor either "takes control of the shares or they are sold to a third party with the proceeds going the creditor."[106] In order to recover on the judgment beyond the shares' market resell value, however, the judgment creditor would need to dissolve the corporation or sell its assets.[107] After attaching the shares, the creditor "is a full owner of the shares, including its management rights, and rights to share in the control of distributions."[108] As a result, he or she "would then be able to force a sale of the attached assets belonging to the corporation" in order to satisfy the full judgment.[109]

This drastic result arguably has a more negative impact on the corporation's viability than structuring a narrow path to direct recovery against the corporation. Even though "other shareholders would be guaranteed their proportional share of the dissolved corporation,"[110] dissolution would

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[104] Allen, *supra* note 30, at 1166.

[105] *See supra* notes 53–58 and accompanying text. For additional commentary advocating for a complete bar on reverse veil piercing, see generally Richardson, *supra* note 2, David Cabrelli, *The Case Against "Outsider Reverse" Veil Piercing*, 10 J. CORP. L. STUD. 343, 366 (2010) (favoring complete abolition of the doctrine or, alternatively, a highly constrained version that "operates within much more restricted parameters"), and STEPHEN M. BAINBRIDGE, CORPORATION LAW AND ECONOMICS 166–68 (2002).

[106] Richardson, *supra* note 2, at 1624.

[107] *See id.*

[108] Ribstein, *supra* note 24, at 203.

[109] Allen, *supra* note 30, at 1164.

[110] Richardson, *supra* note 2, at 1624.

significantly impact the corporation's other constituencies (for example, its employees). It also follows that a forced sale of corporate assets that doesn't fully rise to dissolution would fail to protect non-culpable shareholders' rights by way of mandatory proportional distribution.

This approach's "refusal to look beneath the surface of the corporate form blatantly exalts form over substance" and "places excessive emphasis on the importance of limited liability in situations in which the concept does not belong."[111] Even the Tenth Circuit, in rejecting the doctrine, "recognized that the problems associated with a reverse pierce are less serious where there is only a single shareholder because no other shareholders would be unfairly prejudiced," conceding that the Court's concerns are at least theoretically mitigatable under the right circumstances.[112]

Ultimately, however, the most significant concern with this approach is an equitable one: under a complete bar, "a plaintiff could be left sitting with an unsatisfied judgment while the wrongdoer is free to continue living off the funds hidden in an alter ego corporation."[113] Applied to the hypothetical described above, the complete bar approach would, unsurprisingly, preclude Peter from recovering against either Consolidated Holdings or Barb Holdings. The preclusion would likely protect Amy and Cooper's interests, as well as those of Consolidated Holdings' creditors, employers, business partners, and tenants. It would also shield Barb's personal assets behind the corporate veil of Barb Holdings, leaving Peter with an unsatisfied judgment.

B. Inverse Method

As discussed above, many jurisdictions rationalize that reverse veil piercing "is a logical extension of traditional veil piercing because the underlying equitable goals remain unchanged and so the test should remain the same."[114] Thus, "[t]he direction of the piercing is immaterial where the general rule has been met."[115]

This approach is simultaneously too rigid and "[e]ssentially void of definite standards."[116] Courts have applied and considered countless tests and factors within the context of traditional veil piercing; the inverse method, therefore, operates within the same chaotic framework.[117] The "[l]ack of consensus in the area results in substantial confusion," with courts often

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111 Gaertner, *supra* note 36, at 694.
112 Youabian, *supra* note 29, at 588 (discussing Floyd v. IRS, 151 F.3d 1295 (10th Cir. 1998)).
113 Allen, *supra* note 30, at 1179.
114 Hespe, *supra* note 8, at 79–80.
115 *Id.* at 80 (quoting State v. Eason, 647 N.Y.S.2d 904, 909 (N.Y. Sup. Ct. 1995)).
116 Gaertner, *supra* note 36, at 695.
117 *See supra* note 63 and accompanying text.

considering "factors irrelevant to the reality of the situation."[118] Moreover, "judgment creditors and victims of torts may be given preference over consensual creditors if reverse piercing is allowed with a simple two-prong test."[119]

By contrast, the one nearly universal element of this test creates a rigid and unworkable structure that renders this approach functionally meaningless and akin to the complete bar. Under the domination requirement, plaintiffs are held to the near-insuperable task of demonstrating that the corporation (or subsidiary) exercised total control over the shareholder (or parent corporation).[120] Both courts and commentators recognize that "only in extremely rare instances, if ever, will a corporation exercise sufficient domination over its parent or other insider to justify holding it liable for claims against the insider."[121] By this measure, Peter cannot recover against Barb Holdings in the hypothetical because inverse domination cannot be shown, despite the overwhelming indicia of alter ego.

Consequently, the inverse method also implicates the same equitable concern as the complete bar: strategic shareholders could be unjustly enriched at the plaintiff's expense by shuttling assets into a limited liability vehicle, even under the inverse method.

C. Equitable Results Approach

With nearly as many variations as the traditional veil piercing test, the flexible equitable results approach suffers from being "inherently standardless."[122] On the one hand, this approach has been discredited by some as "creating requirements that 'essentially eliminate the outside reverse piercing doctrine as a practical matter'"[123]:

Indeed, if all the requirements of outside reverse piercing are met, its application would be unnecessary to protect the judgment creditor. Judgment collection procedures offer judgment creditors adequate protection in situations where outside reverse piercing would not harm innocent shareholders and creditors, legal remedies are inadequate, and the traditional requirements of

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118 Gaertner, *supra* note 36, at 695 ("Whether a subsidiary is listed as a division on the parent's stationery should have no bearing on whether to pierce the veil between the two entities.").
119 Richardson, *supra* note 2 at 1627.
120 *See supra* notes 65–67 and accompanying text.
121 Crespi, *supra* note 7, at 66–67 (discussing Judge Learned Hand's observation in Kingston Dry Dock Co. v. Lake Champlain Transp. Co., 31 F.2d 265 (2d Cir. 1929) and noting that "it is virtually impossible for a subsidiary to interpose itself decisively in the conduct of its parent's affairs.").
122 Gaertner, *supra* note 36, at 695; *see supra* notes 69–78 and accompanying text.
123 Allen, *supra* note 30, at 1165 (quoting Postal Instant Press, Inc. v. Kaswa Corp., 77 Cal. Rptr. 3d 96, 106 (Cal. Ct. App. 2008)).

proving alter ego are met. By levying on the debtor's shares, the judgment creditor could place itself in the same position as the shareholder.[124]

By categorically refusing to pierce where the doctrine implicates even a single nonculpable party, this approach would likely preclude recovery in most circumstances, while leaving the plaintiff with an unsatisfied judgment. Suppose Barbara, in the hypothetical, caused Barb Holdings to sell just a few shares of stock to her younger sister, deliberately contriving an equitable concern that would dissuade the court from setting aside the corporate veil behind which she is hiding. Even though Barbara has treated Barb Holdings as her alter ego, courts applying the strictest iteration of the equitable results approach would refuse to pierce altogether, because piercing would prejudice one nonculpable shareholder's investment.[125]

On the other end of the spectrum, some courts have reverted to justice for the plaintiff as the ultimate equitable guideline.[126] While a noble goal, the plaintiff is but one character in this judicial drama; any test that focuses exclusively on promoting justice for the plaintiff effectively and unjustifiably subordinates the interests of absent parties, without a corresponding opportunity for shareholders, creditors, and other corporate constituents to defend their interests. Moreover, this could lead to situations in which the corporate entity is disregarded even if the wrongdoer is not a shareholder.[127] In *LFC Marketing Group v. Loomis*, for example, the court superficially considered "whether the rights of innocent shareholders or creditors are harmed by the pierce" and concluded—without explanation—that the sole non-culpable shareholder would not be harmed.[128] This holding demonstrates the ease with which a court may overlook the inequity of reverse piercing a corporation with innocent shareholders, based on its own subjective notion of harm.

In an even less structured approach, at least one court has held that "if disregarding the corporate entity would advance important state policies, an insider reverse piercing claim will be sustained . . . even if a corporate creditor is thereby prejudiced or many corporate formalities have been observed."[129] Not

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[124] *Postal Instant Press, Inc.*, 77 Cal. Rptr. 3d at 106.

[125] *See supra* note 75 and accompanying text.

[126] *See, e.g.*, LFC Mktg. Grp., Inc. v. Loomis, 8 P.3d 841, 846 (Nev. 2000) ("[R]everse piercing is appropriate in those limited instances where the particular facts and equities . . . require that the corporate fiction be ignored so that justice may be promoted.").

[127] *See* Youabian, *supra* note 29, at 592–95 (illustrating "[t]he Many Problems Implicated by Reverse Piercing when 'Ownership' Interest is Bypassed").

[128] *LFC Mktg. Grp., Inc.*, 8 P.3d at 847. The Court agreed to reverse pierce based on its conclusion that the defendant, though not a shareholder, exhibited sufficient control over the corporation to satisfy the alter ego test—a conclusion that is problematic in its own right. *See id.* at 847–48.

[129] Crespi, *supra* note 7, at 42 (discussing Cargill, Inc. v. Hedge, 375 N.W.2d 477, 478–79 (Minn. 1985)).

only is this problematic because of the "injustice visited upon non-culpable parties," but it also demonstrates the unpredictability of a vague and ever-fluctuating equitable results approach.[130] Thus, it is the court's responsibility to not only promote justice for the plaintiff and further public policies, but to also act as a proxy for these absent parties in crafting the most equitable remedy.

D. Degree of Shareholder Ownership or Control

Some commentators focus on the degree of shareholder ownership as a reliable guideline for determining whether reverse piercing is appropriate in a given circumstance. The corporate fiction may be set aside, many propose, "if one individual owns 'all, or practically all' of the stock of the corporation and the equities so require."[131]

Although it directly targets one of the doctrine's greatest inequities, this approach presents a line-drawing challenge. At one end of the spectrum, "the presence of corporate shareholders other than the insider against whom the outsider is asserting the primary claim . . . . would militate strongly against granting the equitable remedy of corporate disregard."[132] Not only would this preclude recovery in all but the most exceptional circumstances, but it would also create an enticing and formulaic roadmap for devious shareholders to sidestep liability and shield their assets from personal creditors, just as Barbara did in the example above.[133]

On the other hand, some commentators "*mandate* judicial acceptance o [sic] the reverse pierce" as long as the corporation owners exhibit sufficient control over the entity, without regard for collateral consequences.[134] As one court noted wryly, "[the majority shareholder] was not deterred by the fact that he did not hold all of the stock of Tie–Net; why should his creditors be?"[135] On either end, the pendulum swings too far; at once too preclusive and too lax, this approach relies on shareholder control to the detriment of creditors and other

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[130] *Id*. at 65.

[131] *Id*. at 39; *see also* Youabian, *supra* note 29, at 588 ("[T]he problems associated with a reverse pierce are less serious where there is only a single shareholder because no other shareholders would be unfairly prejudiced.").

[132] Crespi, *supra* note 7, at 65.

[133] *See* Allen, *supra* note 30, at 1166; *see also* Hespe, *supra* note 8, at 82 (describing "steps that corporations can take that may make them less likely to be pierced.").

[134] Gaertner, *supra* note 36, at 669, 703 (emphasis added). This article does not distinguish between insider and outsider reverse piercing, but it does appear to generally apply the analysis to situations in which the Court addresses "the corporation owner's plea to reverse pierce." *See id.* at 668. Consequently, this test may have limited application in outsider reverse pierce cases, but nonetheless illustrates the deficiencies inherent in an approach that focuses exclusively on ownership and control.

[135] Sea-Land Servs., Inc. v. Pepper Source, 941 F.2d 519, 521–22 (7th Cir. 1991).

constituencies, but prohibits recovery even when minority shareholders' interests are only "cosmetic."[136]

Yet any intermediate measure of ownership (such as "practically all"[137]) is not a quantifiable guideline, but rather invites the court to engage in the arbitrary task of determining just how many innocent shareholders renders this remedy inappropriate. Are Amy's and Cooper's interests in the hypothetical sufficient to preclude Peter's recovery against Consolidated Holdings? Should Barb Holdings' assets be drained to the detriment of its creditors, simply because the only shareholder is Barbara herself? The unstructured analysis necessary to answer these questions makes clear that "a more doctrinally sound and predictable approach is needed."[138]

E. Capital Exemption

In an effort to account for the interests of innocent shareholders, some scholars have proposed a capital exemption scheme, under which every non-culpable shareholder "would be entitled to receive a return on his initial investment amount prior to any disbursement to the plaintiff, ensuring the shareholder does not sustain a loss due to reverse piercing."[139] This reimbursement "would only be triggered when a plaintiff's claim would drain the corporation of *all* its assets."[140]

Although this proposal seeks to "protect the interests of both the shareholders and plaintiffs," it does not wholly mitigate the potential harm to shareholders.[141] Shareholders own more than just their initial capital contribution; the nature of equity investment is such that the shareholders' true ownership interest is defined not by the amount they invested, but rather by their right to a share of the corporation's surplus assets, proportionate to their stock ownership.[142] If the corporation has thrived since shareholders' initial stock purchase, it follows that their ownership interest would be far greater than their investment. If, however, the corporation has since declined in profitability, their ownership interest would be less valuable. Thus, allowing shareholders merely a capital exemption can be both insufficient and excessive, depending on the state of the corporation's surplus account at the time of judgment collection.

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[136] Youabian, *supra* note 29, at 586 ("[A]lthough there were other non-culpable shareholders involved, loss of a ten dollar investment was hardly unfair prejudice.").
[137] Crespi, *supra* note 7, at 39.
[138] Gaertner, *supra* note 36, at 696.
[139] Allen, *supra* note 30, at 1183.
[140] *Id.* (emphasis added).
[141] *Id.* at 1182.
[142] *See generally* Rebecca C. Cavendish & Christopher W. Krammerer, *Determining the Fair Value of Minority Ownership Interests in Closely Held Corporations*, 82 FLA. B. J. 10 (2008).

Moreover, under this remedy, the capital exemption doesn't protect innocent shareholders unless "enforcement of a judgment would liquidate the alter ego corporation."[143] Innocent shareholders are left unprotected in all other, less extreme situations that nonetheless undermine their ownership rights. Notably, the only situation in which this scheme is applicable is also one in which dissolution of the corporation is likely—an outcome that would undoubtedly prejudice corporate creditors and all other constituents, as well as the economy and community at large.

Ultimately, none of the existing approaches adequately balance the conflicting interests implicated by reverse veil piercing. Some are limited in their ability to account for all affected parties (including non-primary constituencies). Other approaches are chaotic and unpredictable. Still others are deficient because they fail to promote justice for wronged plaintiffs, while the wrongdoer is unjustly enriched.

IV. THE SOLUTION: A NARROW EXCEPTION TO THE STRONG DEFAULT PRESUMPTION OF LIMITED LIABILITY

More so than even traditional veil piercing, the reverse unquestionably abrogates the central tenet of the corporate entity—limited liability. To reflect the continuing importance of limited liability in corporate law, courts should abide by a strong default presumption against reverse veil piercing. Nevertheless, to preclude reverse piercing in all cases would be a circumvention of justice, rewarding strategic shareholders for shuttling assets into an alter ego corporation—"[t]he abstraction of the corporate entity should never be allowed to bar out and pervert the real and obvious truth."[144] To account for the interests of all implicated parties, this Note proposes a comprehensive multi-part test that targets each potential inequity by limiting both the availability and the permissible amount of recovery against a corporation. "The corporate cloak is not lightly thrown aside"—indeed, to overcome the default presumption, the burden must be on the judgment creditor to show that each element of the inquiry has been met.[145] As Judge Learned Hand noted at the very inception of this doctrine, "such instances, if possible at all, must be extremely rare."[146]

Before contemplating whether and to what extent reverse piercing is appropriate, courts must address an essential prerequisite: to avoid being deemed a shortcut around traditional judgment collection procedures, it is necessary that the claimant first exhaust the traditional remedies. "[S]ince reverse piercing is an equitable remedy, it should only be granted 'in the absence of adequate remedies

[143] Allen, *supra* note 30, at 1182.
[144] Paul v. Univ. Motor Sales Co., 278 N.W. 714, 721 (Mich. 1938).
[145] LFC Mktg. Grp., Inc. v. Loomis, 8 P.3d 841, 846 (Nev. 2000).
[146] Kingston Dry Dock Co. v. Lake Champlain Transp. Co., 31 F.2d 265, 267 (2d Cir. 1929).

at law.'"[147] In traditional veil piercing, claimants must generally exhaust corporate assets first, before piercing the veil to collect against shareholders.[148] The same should be true for claimants seeking to reverse pierce. After the defendant's liability is established, the claimant must first attempt to execute the judgment against the defendant-shareholder; if it is then returned wholly or partially unexecuted, the court may entertain a reverse piercing claim.[149]

If the shareholder's personal assets are insufficient to fully satisfy the judgment, the Court may proceed with the inquiry to determine whether the creditor may supplement judgment collection by reverse piercing the shareholder's corporation. The first part of the analysis sets forth four elements that delineate the creditor's ability to recover against the corporation. The second part focuses on an additional independent factor for courts to weigh after considering the more formulaic elements.

A. Part I: The Scope and Availability of Recovery

1. Commingling of Assets

There are many ways for claimants to convince a court to pierce the corporate veil in the traditional direction—any number of improprieties and indicia can form the basis of alter ego liability.[150] For reverse piercing, however, claimants should be held to a more specific standard of proof. Since the corporation's liability is often based not on its undesirable conduct, but rather on the relationship between the shareholder's assets and those of the corporation, the test must be narrower than merely any indicia of alter ego.[151] Instead, the court should fixate on the aspect of the improper shareholder-corporation relationship most relevant to reverse veil piercing: commingling of assets. Indeed, several courts have already recognized that "[i]t is particularly appropriate to apply the alter ego doctrine in 'reverse' when the controlling party uses the controlled

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[147] Youabian, *supra* note 29, at 588 (quoting Floyd v. IRS, 151 F.3d 1295 (10th Cir. 1998)).

[148] *See, e.g.*, Fourth Nat'l Bank v. Francklyn, 120 U.S. 747, 755 (1887); Eskimo Pie Corp. v. Whitelawn Diaries, Inc., 266 F. Supp. 79, 82–83 (S.D.N.Y. 1967); Abercrombie v. United Light & Power Co., 7 F. Supp. 530, 535 (D. Md. 1934).

[149] This is modeled after the New York recovery rule for traditional veil piercing. *See, e.g.*, *Eskimo Pie Corp.*, 266 F. Supp. at 82–83 ("[C]reditors of a corporation may not recover from a parent corporation or its stockholders 'until they have exhausted their legal remedy against the corporation by recovery of a judgment against it, and return of an execution wholly or partly unsatisfied, unless they show that this was impossible or would have been useless.'" (quoting 13 FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 6320 (Sept. 2016 update)).

[150] *See, e.g.*, Electro Source, LLC v. Nyko Tech., Inc., Nos. CV 01-10825 DT (BQRx), CV 02-520 DT (BQRx), 2002 WL 34536682, at *9 (C.D. Cal. Apr. 15, 2002).

[151] *See* Richardson, *supra* note 2, at 1628 ("Reverse piercing is commonly invoked in purely personal cases, including satisfaction of tax debts and settling marital assets in a divorce.").

entity to hide assets or secretly to conduct business to avoid the pre-existing liability of the controlling party."[152]

To prevail on a reverse piercing claim, a creditor must demonstrate that the shareholder is using its corporation to shield personal assets. Strong indicators of improper asset commingling include consistently shuttling personal assets into (and out of) the corporation, advancing funds to the corporation as loans (particularly if there is no repayment agreement or if the terms deviate from market norms), treating the corporation as a personal checking account, utilizing the corporation as a "personal investment vehicle[],"[153] and moving funds freely among various entities owned by the wrongdoing shareholder.[154]

Applying this element to the hypothetical, Peter should have no difficulty demonstrating that Barb Holdings is merely an asset-shielding entity for Barbara. Barbara "loaned" money to Barb Holdings over a sustained period of time but received only unsecured promissory notes payable on demand in return. Rather than receiving earnings as a salary or through dividends, Barbara periodically borrowed large sums from Barb Holdings and even used a business credit card for unrelated personal expenses. Without addressing any other indicia of alter ego, it is evident that Barbara has been using Barb Holdings to shield her personal assets, withdrawing money when personal needs arose.

On the other hand, there appears to be no or little commingling of assets between Barbara and Consolidated Holdings. Even if there were improprieties, inobservances of corporate formalities, or other indicia of alter ego, it would be unjust to deplete Consolidated Holdings' assets to satisfy Barbara's personal debts if she did not use the shared company to shield her funds.

2. Recovery Must be Limited to the Corporation's Surplus Account

A corporation's surplus account is both a legal term and an accounting principle, reflecting an "excess of net asset values over the legal capital."[155] Net

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[152] LFC Mktg. Grp., Inc. v. Loomis, 8 P.3d 841, 846 (Nev. 2000) (quoting Select Creations, Inc. v. Paliafito Am., Inc., 852 F. Supp. 740, 774 (E.D. Wis. 1994)).

[153] NetJets Aviation, Incl. v. LHC Commc'ns, LLC, 537 F.3d 168, 182 (2d Cir. 2008).

[154] *See, e.g.*, *id.* at 180–82 ("[R]ecords show numerous transfers of money by [shareholder] to [corporation], as well as numerous transfers of money from [corporation] to [shareholder]."); Sea-Land Servs., Inc. v. Pepper Source, 941 F.2d 519, 521–22 (7th Cir. 1991); Macaluos v. Jenkins, 420 N.E.3d 461, 466–67 (Ill. App. Ct. 1981).

[155] JAMES D. COX & THOMAS LEE HAZEN, 3 TREATISE ON THE LAW OF CORPORATIONS § 19:7 (3d ed. 2016); *see, e.g.*, DEL. CODE. ANN. tit. 8, § 154 (2010). Legal (or stated) capital refers to the aggregate par value of all outstanding shares or, alternatively, a designated portion of the consideration received for those shares if the corporation does not assign par value. *See* COX & HAZEN, *supra*, § 16:24. Because there are many legal consequences associated with altering the amount allocated to this account, this Note does not contemplate dismantling stated capital for the purpose of broadening the pool of assets available to shareholders' personal creditors. *See id.* ("Legal capital fixes the margin of net assets or value that must be retained in the business and

assets, in turn, refer to "the amount by which total assets exceed total liabilities."[156] It follows that if there is no amount allocated to a corporation's surplus account, then the corporation has at least as many outstanding liabilities as it does assets.

To avoid creating further inequities, it would be unjust for courts to prioritize the individual shareholders' creditors over the corporation's other creditors by allowing recovery in excess of the surplus account.[157] Consequently, if the corporation has no surplus, reverse veil piercing should not be permitted. This limitation prevents corporate creditors from superseding judgment creditors and ensures that corporate creditors' expectations are not undermined. Similarly, limiting recovery to the surplus ensures that corporations' ability to secure credit will not be impaired because of risk-averse creditors.

Assuming Peter prevails through the first series of inquiries, he would have access to only that which can be properly classified as Barb Holdings' surplus. This excludes any of the company's outstanding liabilities. Even if recovery from Consolidated Holdings was not precluded by the first element, Peter could only recover out of its net assets, after deducting the many debts it has likely incurred (including mortgages on the investment properties). The importance of this limitation is particularly evident where the company has incurred significant debt, with unlimited recovery potentially impairing any number of creditors, legitimate business operations, and the continued viability of the company.

Additionally, courts may find the doctrines of subordination and recharacterization useful in applying the surplus limitation. Ordinarily, a corporate insider (such as a majority or sole shareholder) may permissibly loan funds to the corporation, "recoverable to the same extent as if made to the corporation by any other lender."[158] Such transactions, however, are subject to rigorous judicial scrutiny to ensure that the loan was advanced in good faith and

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restricts the distribution of assets to the shareholders."). As an increasingly archaic and criticized doctrine, however, many jurisdictions, along with the Model Business Corporation Act, have abolished the stated capital system entirely or allowed corporations to allocate to surplus the entire consideration received for shares (or, alternatively, assign a par value of zero to each share, thus accomplishing an identical result). *See id.* Thus, the exclusion of a corporation's capital account from the available pool of assets is not a significant limitation for claimants seeking corporate disregard.

[156] DEL. CODE. ANN. tit. 8, § 154 (2010).

[157] Most states' corporation statutes define surplus using the traditional terminology, though "[c]urrent accounting terminology has discarded the surplus terminology in favor of designations such as 'retained earnings,' 'contributed capital,' and 'paid-in capital in excess of par.'" *See* COX & HAZEN, *supra* note 155, § 19:7. Courts applying the law of states whose corporation statute does not define surplus may consider any method that ultimately yields a determinate amount representing the excess of assets over outstanding liabilities.

[158] J. Francis Hock & Co. v. Strohm, 170 A. 738, 739 (Md. 1934).

is inherently fair to the corporation, especially in the bankruptcy context.[159] Transactions that fail this scrutiny may fall victim to either equitable subordination or "recharacterization of loans as equity rather than debt"—in effect, disregarding the shareholder's claim to these assets.[160]

Relying primarily on equitable considerations, courts invoke subordination when the shareholder has "engaged in some type of inequitable conduct," so long as "[t]he misconduct . . . resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant."[161] Qualifying inequitable conduct includes "(1) fraud, illegality or breach of fiduciary duty; (2) undercapitalization; [or] (3) use of the debtor as an instrumentality or alter ego."[162] The test for recharacterization differs slightly, focusing more on the degree of convergence between the terms of the loan and commercial standards, as well as the corporation's use of the advanced funds.[163]

Applying these related doctrines to the surplus limitation, courts may "disregard the outward appearances of the transaction and determine its actual character and effect," in order to prevent fraudulent classification of equity as debt by devious shareholders seeking to shield their assets from creditors.[164] Barbara's loans to Barb Holdings, for example, are perfectly suited for recharacterization: Barbara described her advances to Barb Holdings as loans,

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159 *See In re* Fett Roofing & Sheet Metal Co., 438 F. Supp. 726, 729 (E.D. Va. 1977).

160 Markus C. Stadler, *Treatment of Shareholder Loans to Undercapitalized Corporations in Bankruptcy Proceedings*, 17 J. L. & Com. 1, 10 (1997) ("Equitable subordination does not affect the character of the shareholder loan as corporate debt, but merely changes the priority of corporate debts. Recharacterization challenges the character of the loan as corporate debt and treats it instead as a property interest. The practical effect of this distinction is in most cases immaterial.").

161 *In re* Mobile Steel Co., 563 F.2d 692, 700 (5th Cir. 1977). Courts also demand that subordination is not "inconsistent with the provisions of the Bankruptcy Act." *See id.*

162 Stadler, *supra* note 160, at 17; *see also* Pepper v. Litton, 308 U.S. 295, 309–10 (1939) (noting that subordination has been invoked when the corporation "has been used merely as a corporate pocket of the dominant stockholder, who, with disregard of the substance or form of corporate management, has treated its affairs as his own.").

163 *See In re* AutoStyle Plastics, Inc., 269 F.3d 726, 749–50 (6th Cir. 2001). Specifically, the factors are:

> "(1) the names given to the instruments, if any, evidencing the indebtedness; (2) the presence or absence of a fixed maturity date and schedule of payments; (3) the presence or absence of a fixed rate of interest and interest payments; (4) the source of repayments; (5) the adequacy or inadequacy of capitalization; (6) the identity of interest between the creditor and the stockholder; (7) the security, if any, for the advances; (8) the corporation's ability to obtain financing from outside lending institutions; (9) the extent to which the advances were subordinated to the claims of outside creditors; (10) the extent to which the advances were used to acquire capital assets; and (11) the presence or absence of a sinking fund to provide repayments."

Id. at 750.

164 *In re Fett Roofing & Sheet Metal Co.*, 438 F. Supp. at 729.

placing those funds beyond Peter's reach during the initial recovery from her personal assets. These assets would ordinarily be untouchable even through a reverse pierce, if categorized as a liability on the balance sheet and thus excluded from surplus. The loans, however, had no maturity date, were unsecured, and had no schedule for repayments—strong indicators of improperly classified debt.[165] Recharacterization of the loans as equity would bring those funds back within Peter's grasp by calculating surplus without regard to Barbara's advances. Subordination and recharacterization are therefore essential for ensuring that the surplus limitation is a meaningful one.

3. Innocent Shareholder Exemption from Surplus

Building on the foregoing proposal of a capital exemption for innocent shareholders, this framework expands the scheme to cover not only the shareholders' initial investment, but rather their entire pro rata ownership interest.[166] In the context of shareholder buyouts, it is well-established that the "fair value" of a shareholder's ownership interest is "the value of the oppressed shareholder's proportionate interest in the corporation."[167] Along with other, more amorphous valuation factors, courts generally look to the corporation's net asset value as an authoritative measure of shareholders' ownership interest.[168] The difficulty of "determining an entity's value absent a market," however, renders this analysis "more an art than a science."[169]

A more precise valuation can be found in the context of dissolution. Each shareholder of a corporation facing judicially ordered dissolution is entitled to "receive his full, pro rata share of the corporation's net assets."[170] "[S]ubject to any applicable liquidation preferences and other rights," equity owners "share proportionately in the net assets remaining after the satisfaction of corporate

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[165] *See In re AutoStyle Plastics, Inc.*, 269 F.3d at 50 ("The absence of a fixed maturity date and a fixed obligation to repay is an indication that the advances were capital contributions and not loans.").

[166] *See supra*, Section III.E.

[167] James H. Eggart, *Replacing the Sword with a Scalpel: The Case for a Bright-Line Rule Disallowing the Application of Lack of Marketability Discounts in Shareholder Oppression Cases*, 44 ARIZ. L. REV. 213, 219 (2002). Within the minority shareholder buyout context, this proportionate share is sometimes modified or discounted to reflect lack of control and the illiquidity of shares within a close corporation, but the overarching principle is instructive in fashioning a more accurate definition of ownership within the reverse piercing context. *See id.* at 214; *see also* Cavendish & Krammerer, *supra* note 142, at 13.

[168] *See* Joshua M. Henderson, *Buyout Remedy for Oppressed Minority Shareholders*, 47 S.C. L. REV. 195, 221 (1995).

[169] James H. Eggart, *Replacing the Sword with a Scalpel: The Case for a Bright-Line Rule Disallowing the Application of Lack of Marketability Discounts in Shareholder Oppression Cases*, 44 ARIZ. L. REV. 213, 219 (2002).

[170] *Id.* at 220.

creditors."[171] Surplus is also used to determine the amount from which distributions to shareholders may be made in the ordinary course of business, further illustrating the idea that shareholders' true ownership interest encompasses a proportionate share of the net assets, not just the stated capital or their initial contribution.[172]

To more accurately reflect the law's perception of corporate ownership, this Note proposes echoing the dissolution process and limiting claimants' recovery to the wrongdoing shareholder's pro rata share of the corporation's surplus—his or her true ownership interest. Rather than receiving a reimbursement for their initial capital investment, innocent shareholders would be entirely unaffected by the reverse veil pierce; it is the claimant's burden to establish the portion of the surplus available for recovery. For example, notwithstanding the inequities of piercing Consolidated Holdings under the other elements of this framework, Peter's recovery would be limited to one third of its surplus account—the pro rata share of net assets properly attributed to Barbara's ownership interest. This would protect Amy's and Cooper's share in the company, reflecting their non-culpability. Alternatively, Peter would have access to the entire surplus account of Barb Holdings, as Barbara is the sole shareholder.

This constraint eliminates the "risk of innocent third parties losing their entire investment because essential assets were sold off to pay the debts of a majority owner" by accounting for their interests even in their absence from the suit.[173] Rather than wholly precluding corporate disregard when the circumstances call for it, the surplus exemption simultaneously protects innocent shareholders and effectively mitigates the control issue noted by some commentators.[174] If the defendant is not a true owner of the corporation, the entire surplus would be removed from the claimant's reach: every shareholder would receive an exemption, leaving no portion of the surplus for judgment collection. Of course, the court need not proceed through any portion of this inquiry if the defendant is not a shareholder. Under this proposal, lack of equity interest in the corporation is a de facto bar on reverse veil piercing. "Reverse alter ego is an equitable doctrine; it stretches the imagination, not to mention the equities, to

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171 HARRY G. HENN & JOHN R. ALEXANDER, HANDBOOK OF THE LAW OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES 992 (3d ed. 1983).

172 *See, e.g.*, DEL. CODE. ANN. tit. 8, § 170 (2010) ("The directors of every corporation, subject to any restrictions contained in its certificate of incorporation, may declare and pay dividends upon the shares of its capital stock . . . [o]ut of its surplus, as defined in and computed in accordance with §§ 154 and 244 of this title.").

173 Richardson, *supra* note 2, at 1624.

174 *See* Youabian, *supra* note 29, at 592–595 (emphasizing that reverse piercing should not be applied unless the shareholder has a true equity ownership interest in the corporation, not just control or domination).

conceive of how someone wholly outside the corporation may be used to pierce the corporate veil."[175]

The surplus exemption also dispenses with the difficult fact-finding burden of determining whether any additional shareholders' interests are "genuine and not merely cosmetic"—a standard some courts have adopted in order to ensure that corporations are not escaping liability by mechanically adding innocent shareholders to dissuade the courts from piercing.[176] Similarly, it eliminates the need for courts to denote a bright line for "how many innocent creditors must be present before the court will refuse to pierce the veil."[177] Cosmetic or not, innocent shareholders will receive an automatic proportional exemption from the surplus, to which they rightfully assert an ownership claim—precluding both the situation in which a single shareholder thwarts an otherwise justifiable recovery, and the one in which recovery is permitted at the expense of the innocent shareholder's investment.

4. Prohibition on Recovery of Punitive Damages

Unlike compensatory damages, which seek to compensate the plaintiff for the injury, punitive damages seek to punish the wrongdoer, for the purpose of "retribution and deterring harmful conduct."[178] Punishing the corporation, however, by dismantling its assets through reverse veil piercing, neither punishes the shareholder nor achieves retribution. This doctrine is, at its heart, an equitable one: both traditional and reverse veil piercing were developed to ensure that an injustice to the plaintiff would not occur because devious defendants cleverly shielded their assets behind the veil of limited liability.[179] Punitive damages, while awarded to the plaintiff, essentially carry out a public service function, incompatible with the equitable nature of corporate disregard—punishing the defendant and setting an example for future potential wrongdoers.[180] Allowing recovery of punitive damages out of the corporation's assets perhaps indirectly punishes the defendant as a shareholder, but ultimately punishes the corporate entity and its constituents.

If the claimant prevails on each preceding element, the shareholder's personal assets would first be aggregated towards compensatory damages. Any remaining unsatisfied portion of compensatory damages may be recovered from the corporation's surplus. In the hypothetical, Peter would be limited to recovering up to two million dollars in compensatory damages only from Barb

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[175] Estate of Daily v. Title Guar. Escrow Serv., Inc., 178 B.R. 837, 845 (D. Haw. 1995).
[176] Youabian, *supra* note 29, at 594.
[177] Hespe, *supra* note 8, at 87.
[178] Exxon Shipping Co. v. Baker, 554 U.S. 471, 492 (2008).
[179] *See* Youabian, *supra* note 29, at 575–76.
[180] *See Exxon Shipping Co.*, 554 U.S. at 492–93.

Holdings (assuming that Consolidated Holdings is ineligible for corporate disregard). As evident from the example, this proposal does not guarantee that injured parties will be fully compensated; the suggested framework operates to limit recovery in a way that mitigates the potential injustices of unchecked reverse piercing, while still allowing plaintiffs some recovery beyond the wrongdoer's personal assets, however minimal. Part II of the analysis plays an additional role in striking the appropriate balance between these competing interests.

B. Part II: Balancing the Claimant's Interests Against Those of the Corporation's Other Constituencies

Should a claimant prevail on the preceding elements, courts must complete the analysis by balancing the plaintiff's interest in a satisfied judgment against possible prejudice to the corporation's other constituencies. Each preceding element targets potential injustice to innocent shareholders, corporate creditors, and the corporation's ability to raise capital. The corporation's far-reaching influence on other parties, however, can only be identified on a case-by-case basis, reflecting on the totality of the circumstances.[181]

It would be both undesirable and untenable to create a bright line test for courts to apply in considering the corporation's non-statutory constituencies. For example, one could posit that a corporation with less than fifty employees does not present a significant equitable challenge, such that a court should disallow recovery. Courts are understandably wary of such bright-line tests; an unrefined judicial axe of this sort may produce asymmetric and arbitrary results.[182] Moreover, an employee-based judicial test fails to account for the other ways in which a corporation impacts its community.

Instead, courts must carefully consider the size of the company and its workforce, customers, and vendors, as well as the magnitude of the judgment relative to the corporation's assets and its impact on the corporation's solvency and viability. If the corporation is an active participant in its community, courts must appraise the judgment's effect on these valuable societal benefits.[183] Additionally, courts should consider whether the corporation is of the kind that serves an important public policy, such as pension funds, charitable foundations, and other benefit funds. Ultimately, if the claimant's interest in a satisfied judgment is outweighed by the consequences for these other constituents, the court should deny access to the corporation's assets.

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[181] *See supra* notes 96–102 and accompanying text for a detailed discussion of how reverse veil piercing might indirectly harm these secondary constituents.

[182] *See, e.g.*, United States v. Christie, 717 F.3d 1156, 1162 (10th Cir. 2013).

[183] Examples include corporations that offer research grants, contribute to charity, or facilitate community development programs.

In weighing these competing interests, courts might find guidance in the irreparable harm standard, borrowed from the context of injunctive relief—a well-established equitable remedy.[184] Irreparable harm is "a noncompensable injury for which there is no legal measurement of damages or for which damages cannot be determined with a sufficient degree of certainty."[185] Under this standard, an injunction may only be granted in the face of "injury which is 'both great and immediate,'"[186] harm that is "*likely*," not merely possible or speculative.[187] Applied specifically to commercial contexts, "courts have found irreparable harm where, for example, the moving party will lose customers, goodwill, or business."[188]

A highly fact specific inquiry, the irreparable harm standard may serve as a guiding principle for the uncharted legal territory of this final inquiry.[189] Claimants who prevail under the four elements would be entitled to recovery against the corporation, unless the court finds that it would cause irreparable harm to other constituencies. For example, a court may find irreparable harm where recovery against the corporation would likely result in the loss of a primary employer or the sole provider of needed services in a community—injuries that go beyond merely monetary harm. Allowing the court equitable leeway places this delicate decision in the hands of experienced judges, who are better positioned to evaluate the extent of any collateral ramifications and, if necessary, ultimately bar reverse veil piercing, even if all other elements are satisfied.

In this Note's hypothetical, one could reasonably conclude that Consolidated Holdings' constituencies are so extensive that reverse veil piercing would irreparably harm their interests. Between the long-term contracts and the hundreds of tenants, a multi-million dollar decrease in assets would impair Consolidated Holdings' ability to continue fulfilling its duties as a landlord. Depending on its solvency, Consolidated Holdings may need to resort to extreme measures in order to preserve its continued viability, such as overleveraging or pursing risky mergers. Barb Holdings, on the other hand, has few such constituencies. Its properties are undeveloped, it employs no workers, there are no long-term creditors, and the company is not an active participant in the

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[184] *See generally* Winter v. Nat. Res. Def. Council, Inc., 555 U.S. 7, 20–23 (2008).

[185] Thermatool Corp. v. Borzym, 575 N.W.2d 334, 338 (Mich. Ct. App. 1998).

[186] O'shea v. Littleton, 414 U.S. 488, 499 (1974) (quoting Younger v. Harris, 401 U.S. 37, 46 (1974)).

[187] *Winter*, 555 U.S. at 22.

[188] Daniel N. Adams & Daniel. W. Linna Jr., *The Availability of Injunctive Relief in Commercial Disputes: Clarifying Michigan's Preliminary-Injunction Standard*, 91 Mich. B.J. 36, 38 (2012). *But see Thermatool Corp.*, 575 N.W.2d at 339 ("A relative deterioration of competitive position does not in itself suffice to establish irreparable injury.").

[189] *See* Groupe SEB USA, Inc. v. Euro-Pro Operating LLC, 774 F.3d 192, 205 (3d Cir. 2014) ("[C]ourts considering whether to grant injunctive relief must exercise their equitable discretion in a case-by-case, fact-specific manner.").

community. In this scenario, the harm to others is likely not irreparable. Particularly in light of this alternative, a court could easily conclude that Peter's interest in recovering against Consolidated Holdings pales in comparison to the likely harm that would result to its employees, business partners, tenants, and the community.

V. COUNTERARGUMENTS

A. Counterargument 1: Reverse Veil Piercing Is a Shortcut Around Traditional Judgment Collection Measures

Critics of reverse veil piercing often note that "the doctrine ignores normal judgment collection procedures." [190] The initial prerequisite that the shareholder's personal assets be insufficient to satisfy the judgment prevents claimants from abusing reverse veil piercing as a tool of convenience. Rather, the narrow exception crafted by this Note's proposed solution serves as the ultimate safeguard against inequity, when traditional judgment collection procedures are insufficient. Additionally, as noted above, relying exclusively on "the intermediary step of seizing the defendant's interest in the corporation" as an indirect way of reaching the corporation's assets can lead to sweeping consequences far beyond those implicated by the workaround.[191] Although some speculate that "[t]he new holder would have an incentive to make economically rational decisions that benefit the corporation or resell the shares for value,"[192] claimants seeking immediate satisfaction of their judgment are more likely to pursue an extensive sale of assets or even forced dissolution, impeding on the interests of nonculpable shareholders, creditors, and other constituents.

Moreover, this concern was particularly emphasized in cases where liability was found based on mere control, rather than ownership.[193] The innocent shareholder exemption from the corporation's surplus creates a de facto preliminary requirement that the defendant is, in fact, a shareholder of the corporation—a requirement that effectively mitigates this concern.

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[190] Hespe, *supra* note 8, at 77; *see also* Richardson, *supra* note 2, at 1605–06 ("[P]laintiffs attempt to increase the ease of collecting on their judgment by skipping the intermediary step of seizing the defendant's interest in the corporation."); Youabian, *supra* note 29, at 595–96 ("In adopting the reverse pierce theory, courts must consider the . . . problems associated with bypassing normal judgment collection procedures . . . .").

[191] Richardson, *supra* note 2, at 1605–06; *see supra* notes 106–110 and accompanying text.

[192] *Id.* at 1624.

[193] *See* Youabian, *supra* note 29, at 593 (expressing concern that if alter ego liability is based on control rather than ownership, "the corporation's assets, which belong to the corporation and not the controlling party, are used to satisfy the controlling party's debts," which violates traditional judgment collection procedures).

B. Counterargument 2: Reverse Veil Piercing Impairs the Corporation's Ability to Obtain Credit

Critics note that reverse veil piercing undermines corporate creditors' expectations, whose loans are secured by corporate assets.[194] Widespread application of the doctrine could thus lead to decreased willingness to lend to small business or a correlating increase in risk premium to account for the possibility of losing their collateral to individual shareholders' creditors.[195]

Because of the extremely stringent circumstances under which a corporation's surplus account would actually be subjected to recovery, creditors are unlikely to account for such a remote possibility by imposing an unduly burdensome premium on the "increased risk of default posed by reverse piercing claims."[196] Limiting recovery to surplus protects the outstanding debt itself, thereby reducing the creditors' need to rely on collateral. If the corporation retains its ability to fulfill its obligations, then the creditor will not need to resort to secured assets.

Even without the mitigating effect of the surplus limitation, an exodus of willing lenders may not be as inevitable as some fear. Leaving aside widespread corporate disregard, "loans to closely held corporations are made despite the nearly infinite grounds upon which a corporation could face its own action."[197] It is therefore unlikely that "the risk of judgment against a corporation, stemming from an action against an individual, would deter loans to closely held corporations."[198] Notably, "unsecured creditors already face some risks from reverse piercing by the IRS, as the doctrine has widespread acceptance in federal tax cases," yet nonetheless fearlessly lend to businesses.[199] The safeguards imposed by the surplus limitation should be sufficient to alleviate creditors' anxieties.

CONCLUSION

Under the guise of preventing injustice, the corporate cloak has been thrown aside with much abandon in recent decades. The ramifications of courts' chaotic and unpredictable approaches to reverse veil piercing are far and wide, exacting harm on innocent shareholders, corporate creditors, and other secondary

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194 *See, e.g.*, Floyd v. IRS, 151 F.3d 1295, 1299 (10th Cir. 1998); Youabian, *supra* note 29, at 587–88.

195 *See Floyd*, 151 F.3d at 1299 ("Corporate creditors are likely to insist on being compensated for the increased risk of default posed by outside reverse-piercing claims, which will reduce the effectiveness of the corporate form as a means of raising credit.").

196 Youabian, *supra* note 29, at 593–94.

197 Allen, *supra* note 30, at 1185.

198 *Id.*

199 *Id.*

constituencies. At the same time, plaintiffs are left unsatisfied when courts seek to mitigate these inequities by permitting devious shareholders to shield their personal assets behind the veil of limited liability. Preserving the fundamental principle of limited liability while balancing the interests of all implicated parties requires a structured and comprehensive approach.

This Note proposes a multi-part test for courts to apply when contemplating whether to reverse pierce. It permits a narrow window of recovery against corporations by forcing courts to act as a proxy for the interests of unrepresented third parties, without precluding this equitable remedy altogether. Although this approach does not yield the predictability of a rigid, formulaic rule, "[t]he logical consistency of a juridical conception will indeed be sacrificed at times, when the sacrifice is essential to the end that some accepted public policy may be defended or upheld."[200]

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[200] Berkey v. Third Ave. Ry. Co., 155 N.E. 58, 61 (N.Y. 1926).