

# Piercing the Corporate Veil

Business owners and entrepreneurs form corporations and LLCs as protection from debts tied to the business. However, piercing the corporate veil can make these individuals liable for debts the company owes. Learn more about the process and how to protect your business from this practice. Schedule a consultation by calling 555-555-5555 to discuss your legal options with XYZ Law Firm.

## What Happens When a Court Pierces the Corporate Veil?

According to the Internal Revenue Service, sole proprietorships and corporations are the most common business entities. Many business owners and individuals set up business entities to help protect themselves from personal liability. In many cases, the business is separate from the individual, with different bank and tax accounts.

Many believe this is a fool-proof way to shield themselves from business debts, but a legal business structure is not enough to offer complete protection. Piercing the corporate veil is a legal term describing the action that holds members, stakeholders, and owners personally liable for any business debts. In short, the courts completely disregard the corporate structure. This process allows an individual’s property interests, bank accounts, and investments to be at risk of financial loss.

While it may seem alarming to hear this term, not everyone has to worry about this liability process. The court system only imposes personal liability on those parties responsible for the fraudulent actions of the LLC or corporation. Any innocent parties will not be liable for paying back debts due to another person’s poor or irresponsible decisions. Find out how to protect your business by scheduling a consultation with XYZ Law Firm.

## What Is Required to Pierce the Corporate Veil?

All LLCs and corporations are legal entities. While many individuals believe these entities provide complete legal liability protection, they only offer limited personal liability for the debts of the business. Typically, the persons who operate the company are not personally responsible for the debt, but there are a few exceptions.

Small LLCs and closely held corporations are more likely to have their corporate veil pierced. A court can impose personal liability on the personal assets of members of the LLC or corporation in the following situations:

### No Proof of Personal and Business Separation

Business owners create these entities for a reason: to separate the business and personal assets of the owners. When the owners do not keep their personal and business finances separate, the court could determine that the individuals and corporation/LLC are acting as one entity. All LLCs and corporations must follow specific rules. The owners cannot pay the company’s bills out of their personal checking accounts or make decisions without shareholder meetings.

The courts must determine whether the legal entity was fraudulent in those cases. If the judge or courts cannot see documented proof of separation, the owners are no longer afforded the right to the limited liability of the business structure.

### Creditors Suffered an Unjust Loss of Income

Many LLCs or corporations need services or goods from outside providers. Those providers expect payment for their products or services. In the case of a non-payment, the provider can head to civil court to collect the debt or judgment. But that is not always successful. Sometimes, the company that owes the debt has ceased operations with no remaining assets. The owners may try to hide assets to start up another business or keep them away from creditors. With that, the owed provider can go through the court system and seek payment from the personal assets of the company’s owners, stakeholders, or managers.

### The Company Participated in Fraudulent or Wrong Activities

Unfortunately, some corporation or LLC owners or members may act unlawfully. They may have made deals knowing they could not pay back creditors, recklessly borrowed money, or behaved in other fraudulent ways. In those situations, the court can determine that the company committed financial fraud, meaning limited liability protection will not apply to those parties responsible for the wrongful actions.

## How to Prevent Piercing the Veil

Individuals may avoid these issues by taking extra steps to protect the business. Choosing the proper legal structure for the company is crucial. According to the United States Small Business Association, the business structure affects every part of the company. Often, some individuals may choose an entity that is convenient for them at the moment without looking at the long-term legal implications.

Whether operating as a corporation or LLC, there are still rules and legal obligations to follow. Businesses must file taxes every quarter, and they need to keep all personal and corporate finances separate from each other. While LLCs are simple to manage, some corporate structures may require scheduling board of director meetings and paying dividends to shareholders. Not following these requirements could lead to liability issues.

Corporations and LLCs also need proper documentation. Without it, there may not be proof that the expenses or profits were kept separate from the personal account. The documentation also notes whether a creditor received payment on time. Any member or owner of the LLC or corporation must be professional and act within the laws. In most situations, illegal activities allow the courts to become involved in these matters, making them pierce the corporate veil. Any signs of wrongdoing set businesses up for legal ramifications down the road.

## Piercing the Corporate Veil Remains a Rare Occurrence

No businesses want their corporate veils pierced. However, engaging in unethical or egregious behavior may lead to losing personal assets because of a business’s actions. That said, corporations and LLCs still need to follow the regulations and formalities of the legal entity structure. Failing to adhere to their legal obligations can leave businesses vulnerable to these issues.

## Contact an Experienced San Francisco Business Attorney Today

Piercing the corporate veil can be financially devastating for many business owners. Many assets, property holdings, and investments could be at risk and required to pay debts from a corporation or LLC. Finding the proper business structure for your business may help prevent most of these problems. Schedule your consultation with a dedicated California business lawyer at XYZ Law Firm by calling 555-555-5555 to determine the best steps for structuring and protecting your business.