

April 2014

Reverse Piercing of the Corporate Veil: A Straightforward Path to Justice

Nicholas B. Allen

Follow this and additional works at: <https://scholarship.law.stjohns.edu/lawreview>

Recommended Citation

Allen, Nicholas B. (2011) "Reverse Piercing of the Corporate Veil: A Straightforward Path to Justice," *St. John's Law Review*: Vol. 85 : No. 3 , Article 6.

Available at: <https://scholarship.law.stjohns.edu/lawreview/vol85/iss3/6>

This Note is brought to you for free and open access by the Journals at St. John's Law Scholarship Repository. It has been accepted for inclusion in St. John's Law Review by an authorized editor of St. John's Law Scholarship Repository. For more information, please contact selbyc@stjohns.edu.

REVERSE PIERCING OF THE CORPORATE VEIL: A STRAIGHTFORWARD PATH TO JUSTICE

NICHOLAS B. ALLEN[†]

INTRODUCTION

It is textbook law that a stockholder's exercise of control over a corporation does not create liability beyond the assets of that corporation.¹ This concept of limited liability for corporations is "deeply ingrained" in both American legal and economic systems.² Indeed, judicial acknowledgement of a corporation as a separate and distinct entity is a cornerstone of American enterprise, and benefits such as encouraging shareholder investment by limiting investor risk exposure are essential.³

However, limited liability has its limits. When a corporation is used as a shield for liability or for an illegitimate business purpose, courts will exercise their equitable power in applying the "equally fundamental principle" of piercing the corporate veil.⁴ Piercing the corporate veil allows one to puncture the "veil" of limited liability in order to hold a shareholder liable for the corporation's conduct.⁵

[†] Notes & Comments Editor, *St. John's Law Review*; J.D. Candidate, 2012, St. John's University School of Law; B.S., 2009, University of Miami.

¹ See *United States v. Bestfoods*, 524 U.S. 51, 61–62 (1998).

² *Id.* at 61 (quoting William O. Douglas & Carrol M. Shanks, *Insulation from Liability Through Subsidiary Corporations*, 39 *YALE L.J.* 193, 193 (1929)) (internal quotation marks omitted).

³ See Gregory S. Crespi, *The Reverse Pierce Doctrine: Applying Appropriate Standards*, 16 *J. CORP. L.* 33, 34 (1990).

⁴ *Bestfoods*, 524 U.S. at 62.

⁵ See *id.*; see also *Anderson v. Abbott*, 321 U.S. 349, 362 (1944). This principle has remained largely unchanged for over a century of corporate jurisprudence. See, e.g., *First Nat'l Bank of Chi. v. F. C. Trebein Co.*, 52 N.E. 834, 837 (Ohio 1898) (Courts have confined "[t]he fiction by which an ideal legal entity is attributed to a duly-formed incorporated company, existing separate and apart from the individuals composing it . . . to the purposes for which it was adopted,—convenience in the transaction of business . . . —and have repudiated it in all cases where it has been insisted on as a protection to fraud or any other illegal transaction.").

While exact definitions vary by state, courts will disregard the corporate entity—or pierce the corporate veil—when it is shown that a corporation is an “alter ego.” A corporation is an alter ego when it is used as a “mere instrumentality for the transaction of [the shareholders’] affairs without regard to separate and independent corporate existence.”⁶ The “paramount goal” of traditional veil piercing⁷ (“traditional piercing”) is to achieve an equitable result.⁸ Traditional piercing jurisprudence is well established and, despite some differences in formulation, universally followed throughout American courts.

The practice of reverse piercing the corporate veil is less established.⁹ Where it is available, both corporate insiders and outside third parties have the opportunity to reverse pierce the corporate veil.¹⁰ In outside reverse piercing, a third-party creditor seeks either to recover debts owed by a corporation’s owner from the corporation itself or to recover debts owed by a parent corporation from a subsidiary corporation.¹¹ Although several states have expressly rejected the doctrine,¹² there is a growing trend toward recognizing reverse piercing as a theory of recovery.¹³ Even still, the approaches taken in states that have

⁶ *Phillips v. Double B Trading Co.*, 893 P.2d 1357, 1362 (Colo. App. 1994).

⁷ “Traditional Piercing” involves a claim brought against the shareholders of a corporation in their individual capacities resulting from a wrong procured by the corporation. For more information concerning traditional piercing see *infra* Part I.A.

⁸ *Connolly v. Englewood Post No. 322 Veterans of Foreign Wars of the U.S., Inc. (In re Phillips)*, 139 P.3d 639, 644 (Colo. 2006) (en banc).

⁹ See 1 WILLIAM MEADE FLETCHER ET AL., *FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS* § 41.70 (perm. ed. 2011).

¹⁰ When performed by an insider, it is called “inside reverse piercing.” Similarly, when performed by a third party, it is called “outside reverse piercing.” This Note focuses on outside reverse piercing; for more information in regards to both inside and outside reverse piercing see *infra* Part I.B.

¹¹ See, e.g., *Goya Foods, Inc. v. Unanue-Casal*, 982 F. Supp. 103, 108 (D.P.R. 1997); *In re Phillips*, 139 P.3d at 645; *supra* Part I.B.

¹² See, e.g., *Postal Instant Press, Inc. v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96, 98 (Ct. App. 2008) (refusing to adopt reverse piercing); *Acree v. McMahan*, 585 S.E.2d 873, 874 (Ga. 2003) (rejecting reverse piercing); *McIntyre v. Nice*, No. CV-99-727, 2001 WL 1708832, at *6 (Me. May 17, 2001) (noting that the court has never recognized reverse piercing and has stated the weight of authority is against the doctrine), *rev’d on other grounds*, 786 A.2d 620 (2001); *Transamerica Cash Reserve v. Dixie Power & Water, Inc.*, 789 P.2d 24, 26 (Utah 1990) (refusing to apply reverse piercing to current case, without directly rejecting doctrine).

¹³ See *Litchfield Asset Mgmt. Corp. v. Howell*, 799 A.2d 298, 312 (Conn. App. Ct. 2002) (noting there is “a growing recognition of the doctrine of reverse piercing of the corporate veil”).

allowed reverse piercing are far from uniform.¹⁴ The various approaches reflect attempts to weigh the interests of the plaintiff, innocent shareholders, and other corporate creditors.¹⁵ These approaches are unlike traditional piercing where the shareholder is held liable for her proactive role in creating the wrong; there, the corporation, its creditors, and other shareholders are not adversely affected. The conflicting interests implicated by reverse piercing mandate that any allowance of reverse piercing delicately balance the needs of all involved parties to adequately protect all involved.

This Note argues that while outside reverse piercing should not be the norm, there are instances when application of the doctrine is the only way to ensure justice. Because of the competing interests that reverse piercing implicates, this Note proposes that the doctrine be permitted against both legal and equitable owners, but only when traditional, less intrusive remedies are insufficient. Additionally, any innocent shareholders should be permitted a capital exemption prior to payment of the plaintiff's claim when that claim would liquidate the corporation's assets. Finally, dilemmas amongst creditors should be dealt with under preexisting priority laws. Part I discusses both traditional and outside reverse veil piercing. Part II discusses the arguments for and against the various methods of outside reverse piercing through a case law analysis. Finally, Part III advances a solution that safeguards the interests of all involved parties by first identifying the shortcomings of more traditional remedies and then proposing a new approach.

¹⁴ Compare *In re Phillips*, 139 P.3d at 641 (holding Colorado law requires proof that no innocent shareholders or creditors would be prejudiced by reverse piercing), with *State v. Easton*, 169 Misc. 2d 282, 287–90, 647 N.Y.S.2d 904, 908–10 (Sup. Ct. Albany Cnty. 1995) (holding that New York only requires a showing that a corporation is the alter ego of the individual and failure to disregard the corporate entity would procure a fraud to plaintiff), with *Towe Antique Ford Found. v. IRS*, 999 F.2d 1387, 1390 (9th Cir. 1993) (holding Montana Law does not require a showing of fraud to allow reverse piercing, at least in tax collection cases).

¹⁵ See *In re Phillips*, 139 P.3d at 645; see also *Cascade Energy & Metals Corp. v. Banks*, 896 F.2d 1557, 1577 (10th Cir. 1990).

I. OVERVIEW OF VEIL PIERCING: TRADITIONAL AND REVERSE

Because reverse piercing is a variation of traditional piercing, Part I begins by detailing traditional piercing case law and analyzing the various approaches before delving into reverse piercing.

A. *Traditional Veil Piercing*

All corporations exist behind the “corporate veil” and are entitled to a legal assumption that the acts of the corporation are independent from the acts of its shareholders. This ensures that shareholders or another corporation are exempt from liability for the corporation’s actions.¹⁶ This assumption of limited liability is “the rule, not the exception.”¹⁷

Piercing the corporate veil, however, places an outer limitation on this assumption.¹⁸ Veil piercing is not a separate cause of action against a corporation, but “rather . . . an assertion of facts and circumstances which will persuade the court to impose the corporate obligation on its owners.”¹⁹

While small differences exist between states,²⁰ a traditional veil piercing claim generally requires that (1) the owners exercised complete domination of the corporation in respect to the transaction attacked, and (2) such domination was used to commit a fraud or wrong against the plaintiff.²¹ Although some

¹⁶ See BLACK'S LAW DICTIONARY 390–91 (9th ed. 2009).

¹⁷ *United States v. Bestfoods*, 524 U.S. 51, 61 (1998) (quoting *Anderson v. Abbott*, 321 U.S. 349, 362 (1944)).

¹⁸ See *Easton*, at 288, 647 N.Y.S.2d at 908.

¹⁹ *Id.* at 169 Misc. 2d at 287, 647 N.Y.S.2d at 908.

²⁰ For instance, California and Illinois require ownership as a prerequisite to alter ego liability. See *S.E.C. v. Hickey*, 322 F.3d 1123, 1128 (9th Cir. 2003); see also *Trossman v. Philipsborn*, 869 N.E.2d 1147, 1171 (Ill. App. Ct. 2007) (holding that to permit reverse piercing an insider must own “all, or substantially all, of the stock”). But see *Easton*, 169 Misc. 2d at 289, 647 N.Y.S.2d at 909 (holding that an equitable owner can satisfy the domination requirement; “legal” ownership is not a requirement).

²¹ See *Easton*, 169 Misc. 2d at 288–89, 647 N.Y.S.2d at 908–09; see also *Sea-Land Serv., Inc. v. Pepper Source*, 941 F.2d 519, 520 (7th Cir. 1991) (holding that under Illinois law there are two requirements that must be satisfied to permit veil piercing). “[F]irst, there must be such unity of interest and ownership that the separate personalities of the corporation and the individual [or other corporation] no longer exist; and second, circumstances must be such that adherence to the fiction of separate corporate existence would sanction a fraud or promote injustice.” *Id.* (alterations in original) (quoting *Van Dorn Co. v. Future Chem. & Oil Corp.*, 753 F.2d 565, 569–70 (7th Cir. 1985)).

states require that three elements be satisfied before allowing a plaintiff to pierce the veil—the third element being a causation or equitable results prong—the analysis is nearly identical to the two-prong test.²² If a plaintiff proves these elements, the court imposes liability on the individual because the corporation is a mere “instrumentality” or “alter ego” of its owner.²³

The first prong of piercing the corporate veil, domination, is met when the owners use the corporate form to further their own personal goals.²⁴ The control that accompanies stock ownership and management is not enough to show domination.²⁵ Instead, the actions taken need to circumvent legitimate corporate purposes, so as to make the corporation a mere “alter ego.”²⁶ States are split as to who can dominate a corporation, though many take a liberal approach, allowing both legal and equitable owners.²⁷ The vast majority of cases involving reverse piercing implicate closely held organizations,²⁸ not publicly traded companies.²⁹ This Note only addresses reverse piercing in the context of closely held corporations.

²² See, e.g., *Connolly v. Englewood Post No. 322 Veterans of Foreign Wars of the U.S., Inc. (In re Phillips)*, 139 P.3d 639, 646 (Colo. 2006) (en banc) (stating that Colorado law has three elements: (1) the insider and the corporation are alter egos, (2) that justice requires recognizing the substance of the relationship over the form because adherence would sanction a fraud, and (3) that an equitable result be achieved by piercing).

²³ See *WM. Passalacqua Builders, Inc. v. Resnick Developers S., Inc.*, 933 F.2d 131, 134 (2d Cir. 1991) (emphasis omitted). Accordingly, veil-piercing is often referred to as the “alter ego” theory.

²⁴ *Easton*, 169 Misc. 2d at 289, 647 N.Y.S.2d at 909.

²⁵ See *Angelo Tomasso, Inc. v. Armor Constr. & Paving, Inc.*, 447 A.2d 406, 411 (Conn. 1982); see also *Aoki v. Atto Corp. (In re Aoki)*, 323 B.R. 803, 811 (B.A.P. 1st Cir. 2005); *In re Plantation Realty Trust*, 232 B.R. 279, 282 (Bankr. D. Mass. 1999).

²⁶ *Easton*, 169 Misc. 2d at 289, 647 N.Y.S.2d at 909.

²⁷ See *supra* note 20 and accompanying text.

²⁸ A closely held corporation is generally described as “a corporation with a few shareholders and whose corporate shares are not generally traded on a securities market.” *DiPasquale v. Costas*, 926 N.E.2d 682, 707 (Ohio Ct. App. 2010) (quoting *Crosby v. Beam*, 548 N.E.2d 217, 218 (Ohio 1989)).

²⁹ This is in part because most publicly traded companies adhere to corporate formalities, thus making it difficult to satisfy the domination element of the alter ego theory. For an example of a reverse piercing case involving a publicly traded company see *Cascade Energy & Metals Corp. v. Banks*, 896 F.2d 1557, 1577 (10th Cir. 1990). A cursory assessment would suggest that any reverse piercing action against a publicly traded company would necessarily implicate innocent shareholders and should accordingly fail. All subsequent references to a corporation refer to a closely held corporation unless explicitly stated otherwise.

While a finding that a corporation is an alter ego necessarily depends on the facts of each case, courts have identified certain factors that provide evidence of domination: (1) the absence of corporate formalities; (2) inadequate capitalization; (3) commingling funds; (4) overlap in ownership, officers, directors, and personnel; and (5) shared address, office space, and other similar indicia.³⁰ A finding of domination depends on the totality of the circumstances, so no one factor is dispositive.³¹

Once domination is established, a plaintiff attempting to pierce the veil must prove that a shareholder exercised her domination to commit a fraud or wrong against the plaintiff.³² Stated differently, a plaintiff must show that a Court's adherence to the corporation's separate existence would further the defendant's fraud or promote injustice.³³ This element does not require actual fraud, complete with a showing of intent.³⁴ Rather, plaintiffs only need to show that retention of the corporate form would produce inequitable consequences.³⁵ Inequitable consequences can be the violation of a statute or other positive legal duty, a dishonest or unjust act in contravention of a plaintiff's legal rights,³⁶ or a manifest abuse of the corporate form, including intent to use the corporation as a

³⁰ See *WM. Passalacqua Builders, Inc. v. Resnick Developers S., Inc.*, 933 F.2d 131, 139 (2d Cir. 1991). Additional factors include the amount of business discretion displayed by the dominated corporation; whether related corporations deal at "arms length," whether corporations are treated as independent profit centers, personal payment or guarantee of corporate debts, or guarantees by other corporations; and whether the corporation in question had property used by an owner or another corporation as if it were its own. See *id.* For other factors courts have relied on, see *Associated Vendors, Inc. v. Oakland Meat Co.*, 26 Cal. Rptr. 806, 813-15 (Dist. Ct. App. 1962). See also *Robert's Haw. Sch. Bus, Inc. v. Laupahoehoe Transp. Co.*, 982 P.2d 853, 870-72 (Haw. 1999).

³¹ See generally *Fantazia Int'l Corp. v. CPL Furs N.Y., Inc.*, 67 A.D.3d 511, 889 N.Y.S.2d 28 (1st Dep't 2009); *Meshel v. Ohev Sholom Talmud Torah*, 869 A.2d 343 (D.C. 2005).

³² See *State v. Easton*, 169 Misc. 2d 282, 288 647 N.Y.S.2d 904, 908 (Sup. Ct. Albany Cnty. 1995).

³³ See *Sea-Land Servs., Inc. v. Pepper Source*, 941 F.2d 519, 520 (7th Cir. 1991) (citing *Van Dorn Co. v. Future Chem. & Oil Corp.*, 753 F.2d 565, 569-70 (7th Cir. 1985)).

³⁴ See *Shamrock Oil & Gas Co. v. Ethridge*, 159 F. Supp. 693, 696 (D. Colo. 1958).

³⁵ See *id.*

³⁶ See *Fischer Inv. Capital v. Catawba Dev. Corp.*, 689 S.E.2d 143, 147 (N.C. Ct. App. 2009).

shield for fraud.³⁷ Mere inability to collect on a judgment is not an inequitable consequence as this risk is inherent in all dealings with a corporate entity.³⁸

B. Reverse Piercing Generally

Whereas traditional piercing holds an individual liable for the acts of a corporation, or a parent liable for the acts of a subsidiary, reverse piercing imposes liability on a corporation for the obligations of an individual shareholder, or on a subsidiary corporation for the acts of a parent corporation.³⁹ Despite the differences, reverse piercing initially requires the same two-pronged analysis of domination and promotion of fraud or injustice.⁴⁰ There are two types of reverse piercing: inside⁴¹ and outside—depending on the relationship of the party attempting to pierce the corporate veil.⁴² The two types of reverse piercing

³⁷ *Walk-In Med. Ctrs., Inc. v. Breuer Capital Corp.*, 778 F. Supp. 1116, 1123 (D. Colo. 1991) (citing *Ward v. Cooper*, 685 P.2d 1382, 1383 (Colo. App. 1984)).

³⁸ *Shamrock*, 159 F. Supp. at 696.

³⁹ See *Connoley v. Englewood Post No. 322 Veterans of Foreign Wars of the U.S., Inc. (In re Phillips)*, 139 P.3d 639, 644 (Colo. 2006) (en banc).

⁴⁰ See *State v. Easton*, 169 Misc. 2d 282, 289, 647 N.Y.S.2d 904, 909 (Sup. Ct. Albany Cnty. 1995). For states like Colorado that require a three-pronged analysis for traditional piercing, the same three-pronged test is carried over in reverse piercing cases. See *In re Phillips*, 139 P.3d at 646. For a discussion on additional elements courts have imposed in reverse piercing cases see *infra* Part II.

⁴¹ Insider reverse piercing claims involve a corporate insider attempting to pierce the corporate veil to take advantage of corporate claims that she would be unable to bring in her individual capacity. See *In re Phillips*, 139 P.3d at 644–45. For an example of inside piercing see *Roepke v. Western National Mutual Insurance Co.*, 302 N.W.2d 350, 353 (Minn. 1981). In *Roepke*, the court allowed a corporate insider to pierce the veil so that she could “stack”—redeem multiple insurance policies—six insurance policies, instead of only receiving the benefits of only one policy. *Id.* The ability to “stack” was only available to the corporation itself. *Id.* While not widely accepted, several states have allowed inside reverse piercing claims. See, e.g., *id.*; *Earp v. Schmitz*, 79 N.E.2d 637, 641 (Ill. App. Ct. 1948); *U.S. Gypsum Co. v. Mackey Wall Plaster Co.*, 199 P. 249, 252 (Mont. 1921). *But see, e.g., Feldman v. Trs. of Beck Indus. (In re Beck Indus.)*, 479 F.2d 410, 418 (2d Cir. 1973); *Terry v. Yancey*, 344 F.2d 789, 790 (4th Cir. 1965); *Messick v. PHD Trucking Serv., Inc.*, 678 P.2d 791, 794–95 (Utah 1984). Those states that have rejected inside veil piercing claims have done so because it allows a corporation’s owner to “have it both ways” by limiting the owner’s liability, while allowing her to capitalize on the benefits of the corporate form. *Beck Indus.*, 479 F.2d at 418 (holding that a parent corporation could not inside pierce the veil of its subsidiary, commenting that the veil “will not be disregarded where those in control have deliberately adopted the corporate form in order to secure its advantages”). For a more comprehensive analysis on inside reverse piercing, see Crespi, *supra* note 3, at 38–55.

⁴² See *In re Phillips*, 139 P.3d at 644–45.

implicate different interests and diverse policy concerns. To permit a comprehensive analysis, this Note only addresses outside reverse piercing,⁴³ unless stated otherwise.

In an outside reverse piercing claim, the plaintiff, an "outside" third party, seeks to pierce the corporate veil to impose liability on the corporation in order to satisfy the debt of an individual shareholder.⁴⁴ The "outsider" is asserting a claim against the corporation, not for a harm procured by the corporation itself, but rather for the actions of an individual shareholder.⁴⁵ Similarly, outside reverse piercing is used to impose liability on a subsidiary corporation for the debts of a parent corporation,⁴⁶ or to hold one controlled corporation liable for the debts of an affiliated corporation.⁴⁷

The concept of reverse piercing⁴⁸ first arose in the landmark case⁴⁹ of *Kingston Dry Dock Co. v. Lake Champlain Transportation Co.*,⁵⁰ decided by Judge Learned Hand. In *Kingston*, the plaintiff, Kingston, repaired a ship owned by the defendant Champlain's subsidiary.⁵¹ Champlain, not the subsidiary, requested the repairs, and Plaintiff entered into the agreement with Champlain.⁵² Champlain and its subsidiary shared nearly identical boards, but both companies kept separate identities, with decisions made independently.⁵³ Following default by Champlain, Kingston attached the boats to satisfy the

⁴³ Outsider reverse piercing is also referred to as "[r]everse alter ego." See *Acree v. McMahan*, 585 S.E.2d 873, 874 (Ga. 2003) (quoting *Estate of Daily v. Title Guar. Escrow Serv., Inc.* 178 B.R. 837, 845 (D. Haw. 1995)).

⁴⁴ See *Crespi*, *supra* note 3, at 37.

⁴⁵ See *In re Phillips*, 139 P.3d at 645.

⁴⁶ See *FMC Fin. Corp. v. Murphree*, 632 F.2d 413, 421 (5th Cir. 1980).

⁴⁷ Gary J. Mennitt, *Reverse & Triangular Piercing of the Corporate Veil*, N.Y. L.J., Mar. 20, 2000, at col. 1. This is also referred to as triangular piercing because liability moves up from one affiliate to the dominant individual and then flows back down to the second affiliate. *Id.*

⁴⁸ "Reverse piercing," from here on, refers to outside reverse piercing, unless specifically stated otherwise.

⁴⁹ See *Postal Instant Press, Inc. v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96, 101 (Ct. App. 2008) ("Perhaps the oldest reverse piercing case is *Kingston*.").

⁵⁰ 31 F.2d 265 (2d Cir. 1929) While Judge Hand described the facts of a typical outside reverse pierce case, he did not use the term "reverse pierce." See *id.* The first mention of the term "reverse pierce" came forty-five years later in a Georgia case. See *Kingston Dev. Co. v. Kenerly*, 208 S.E.2d 118, 122 (Ga. Ct. App. 1974).

⁵¹ 31 F.2d at 266.

⁵² See *id.*

⁵³ See *id.*

debt owed by Champlain.⁵⁴ The trial court permitted Plaintiff's attachment, but Judge Hand reversed.⁵⁵ In doing so, Judge Hand greatly limited the potential scope of the reverse piercing holding: while it may "be too much to say that a subsidiary can never be liable for a transaction done in the name of a parent . . . such instances, if possible at all, must be extremely rare."⁵⁶

Following Judge Hand's admonition in *Kingston*, courts refused to entertain reverse piercing cases for nearly thirty years. The doctrine finally reemerged and gained acceptance in a marital property case, *W.G. Platts, Inc. v. Platts*.⁵⁷ In *Platts*, the plaintiff sought to impose liability on her husband's corporation in order to satisfy her share of the assets per their divorce decree.⁵⁸ The court held the corporation was an alter ego of the husband and permitted piercing in order to satisfy the divorce decree.⁵⁹ This opinion offered little precedential value for reverse piercing, however, as the court relied heavily on the fact that the ex-husband voluntarily proffered the corporation's assets for inclusion in the decree and a subsequent avoidance of that offering by his alter ego corporation "would be unconscionable and a denial of justice."⁶⁰

Just two years after *Platts*, a district court in Colorado adopted a broad definition of reverse piercing in *Shamrock Oil & Gas v. Ethridge*.⁶¹ There, a third-party creditor held an unsatisfied judgment against the Defendant corporation's owner in his individual capacity.⁶² Plaintiff attached the corporation's main asset, an oil-drilling rig, in order to satisfy his judgment.⁶³ The court permitted this reverse piercing since the corporation was a "mere dummy" of the individual Defendant who shifted his assets to the corporation and habitually commingled funds.⁶⁴

⁵⁴ *See id.*

⁵⁵ *Id.* at 267.

⁵⁶ *Id.*

⁵⁷ 298 P.2d 1107 (Wash. 1956).

⁵⁸ *See id.* at 1108.

⁵⁹ *See id.* at 1109.

⁶⁰ *Id.* at 1111.

⁶¹ 159 F. Supp. 693 (D. Colo. 1958).

⁶² *See id.* at 694–95.

⁶³ *See id.* at 695.

⁶⁴ *Id.* at 698.

The court stressed that “[t]he abstraction of the corporate entity *should never* be allowed to bar out and pervert the real and obvious truth.”⁶⁵

Reverse piercing has met the least resistance when invoked by the government, most commonly to obtain payment of taxes owed by individuals. The government first attempted reverse piercing in 1976 in *G.M. Leasing Corp. v. United States*.⁶⁶ The individual was not an incorporator, director, or officer of G.M. Leasing, but the court still permitted reverse piercing after finding that the individual was an equitable owner.⁶⁷ *Valley Finance, Inc. v. United States* furthered the acceptability of reverse piercing by holding the government’s inability to satisfy legitimate tax debts provides a “sound basis” for reverse piercing the corporate veil.⁶⁸ Today, reverse piercing is a “well-established theory” in federal tax cases as the IRS routinely uses the remedy to attach assets of a corporation to satisfy debts owed by individual shareholders.⁶⁹

II. MIXED REVIEWS: HOW COURTS HAVE APPLIED REVERSE PIERCING AND WHY SOME HAVE REJECTED IT

Section A of Part II provides an in-depth analysis of two different approaches courts have taken in implementing reverse piercing.⁷⁰ Section B of Part II discusses the various reasons put forth by courts in rejecting reverse piercing.

⁶⁵ *Id.* at 696 (emphasis added). Following *Shamrock*, reverse piercing claims became more frequent, albeit with mixed success. *See, e.g.,* *Olympic Capital Corp v. Newman*, 276 F. Supp. 646 (C.D. Cal. 1967) (rejecting outside reverse piercing); *Divco-Wayne Sales Fin. Corp. v. Martin Vehicle Sales, Inc.*, 195 N.E.2d 287 (Ill. App. Ct. 1963) (denying an outside reverse piercing claim); *Cent. Nat’l Bank & Trust Co. of Des Moines v. Wagener*, 183 N.W.2d 678 (Iowa 1971) (allowing a third-party creditor of an individual to reverse pierce a corporation in which he was a majority shareholder).

⁶⁶ *See* 514 F.2d 935 (10th Cir. 1975), *rev’d in part on other grounds*, 429 U.S. 338 (1977).

⁶⁷ *See id.* at 939.

⁶⁸ 629 F.2d 162, 172 (D.C. Cir. 1980).

⁶⁹ *United States v. Scherping*, 187 F.3d 796, 803 (8th Cir. 1999).

⁷⁰ While much of what is to come does apply equally to both inside and outside reverse piercing, not all does. *See supra* note 48.

A. *All in Favor . . . Reasons Supporting Courts' Various Approaches to Reverse Piercing*

Courts have taken two approaches to reverse piercing. This Note refers to the first method as the “inverse method.” The inverse method simply takes the requirements of traditional veil piercing and applies them in the context of a reverse pierce.⁷¹ The second method is the “equitable results” approach. Rather than simply carrying over the requirements of traditional veil piercing, the equitable results approach imposes additional requirements to better protect the diverse interests implicated by reverse piercing.

This Note uses a hypothetical along with case law to allow for an “apples to apples” comparison between various theories and remedies while highlighting the nuances of each. The hypothetical is as follows: Lady X (“Lady”) wants to form X Corporation (“X Corp.”), a wholesale health supplement distribution company. She needs \$35,000 in start up. To get the money, she liquidates her life savings of \$5,000. She convinces her longtime friend (“Friend”) and brother (“Brother”) to contribute \$5,000 each. Lady also gets two separate loans from two different banks (“Bank One” and “Bank Two”), for \$10,000 each. Bank One decides to secure the loan by acquiring a UCC Article 9 lien on X Corp’s inventory; Bank Two does not secure its loan. With her capital in hand, Lady forms X Corp., an S corporation,⁷² and assumes the role of president. Lady does not receive any shares in X Corp.—instead those shares are split equally between Friend and Brother. In addition to the shares, Friend and Brother are given positions on the Board of Directors. Despite Friend and Brother’s stake in X Corp., they receive no dividends or disbursements, do not inquire as to the dealings of the business, and do not attend board meetings as none are regularly held. Lady conducts business in the name of X Corp., which has several monthly retail customers. Lady purchases a

⁷¹ Reverse piercing does necessitate some slight alterations to the traditional veil piercing methodology. *See infra* Part II.A.1.

⁷² An S-Corporation is a regular corporation that has between one and one hundred shareholders and passes through net income or losses to shareholders to be taxed as dividends paid to the shareholders. *See* William Perez, What Is an S Corporation?: Definition & Requirements, ABOUT.COM, available at http://taxes.about.com/od/scorporations/qt/scorp_criteria.htm. There are additional limitations placed on who the shareholders of an S Corporation can be. *See infra* note 167 and accompanying text.

new car and condominium in the X Corp.'s name, though they are solely for her personal use. She also uses X Corp.'s revenue to pay all of her personal expenses. Despite her work for X Corp., Lady takes no salary. Judgment Creditor ("JC"), after finding Lady to be insolvent, attempts to satisfy his \$150,000 judgment—stemming from a tort claim against Lady—by securing assets from X Corp. X Corp. has \$3,000 in inventory, the condominium and car Lady purchased, two computers worth \$4,000 each, and \$1,500 in a bank account.⁷³

1. The "Inverse Method" of Reverse Piercing

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.⁷⁴ This approach permits recovery in a wide variety of cases because of its limited analysis into interests outside of the plaintiff's; when applied to the Lady X hypothetical, this method permits JC to recover on his claim.

Behind the inverse method of reverse piercing is the view that, despite the different corporate interests implicated, the remedy is a logical extension of traditional veil piercing because the underlying equitable goals remain unchanged.⁷⁵ These cases

⁷³ All subsequent applications of the "Lady X hypothetical" will assume that the domination and fraud or injustice requirement have been satisfied to highlight the impact subsequent conditions, or a lack thereof, have on the interests of shareholders, corporate creditors, and the judgment creditor.

⁷⁴ While not exhaustive, states that have adopted the inverse method of piercing include Connecticut, Idaho, Illinois, Iowa, Kentucky, Nevada, New York, Oregon, Texas, Virginia and Wisconsin. *See* *Bollore S.A. v. Import Warehouse, Inc.*, 448 F.3d 317 (5th Cir. 2006) (citing *Zahra Spiritual Trust v. United States*, 910 F.2d 240 (5th Cir. 1990)); *C.F. Trust, Inc. v. First Flight Ltd. P'ship*, 140 F. Supp. 2d 628 (E.D. Va. 2001) (citing *Greenberg v. Commonwealth*, 499 S.E.2d 266 (Va. 1988) (rejecting reverse piercing not because Virginia law precluded the remedy but only because Plaintiff failed to show corporation was in fact an alter ego of individual debtor)); *Litchfield Asset Mgmt. Corp., v. Howell*, 799 A.2d 298 (Conn. App. Ct. 2002); *Minich v. Gem State Developers, Inc.*, 591 P.2d 1078 (Idaho 1979); *Crum v. Krol*, 425 N.E.2d 1081 (Ill. App. Ct. 1981); *Cent. Nat'l Bank & Trust Co. of Des Moines v. Wagener*, 183 N.W.2d 678 (Iowa 1971); *Nutrition Rich Prods. v. Nutritional Res., Inc.*, No. 99-CI-00483, 2003 WL 1339309 (Ky. Ct. App. Feb. 21, 2003); *LFC Mktg. Grp., Inc. v. Loomis*, 8 P.3d 841 (Nev. 2000); *New York v. Easton*, 169 Misc. 2d 282, 647 N.Y.S.2d 904 (Sup. Ct. Albany Cnty. 1995); *Amfac Foods, Inc., v. Int'l Sys. & Controls Corp.*, 654 P.2d 1092 (Or. 1982); *Am. Petrol. Exch., Inc. v. Lord*, 399 S.W.2d 213 (Tex. Civ. App. 1966); *Olen v. Phelps*, 546 N.W.2d 176 (Wis. Ct. App. 1996).

⁷⁵ *See* *Postal Instant Press v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96, 104–05 (Ct. App. 2008).

place emphasis on the function of the corporation, rather than the form. In accepting reverse piercing, a Connecticut court stressed “the need for [courts] to ‘avoid an over-rigid preoccupation with questions of structure . . . and apply the preexisting and overarching principle that liability is imposed to reach an equitable result.’”⁷⁶ The status as a separate entity granted to corporations was introduced to subserve the ends of justice, not subvert them.⁷⁷ These arguments all stand for the proposition that in the event of potential misuse the courts will flex their equitable powers by circumventing limited liability, from either direction, by viewing a corporation as nothing more than a collection of individuals.

Equitable similarities aside, there are some differences that have precluded courts from simply copying the traditional veil piercing test for reverse piercing. The biggest difference is the definition of “domination.”⁷⁸ As discussed above, “domination” requires an exercise of control to such an extent that the corporation or subsidiary has become a mere “alter ego” or “instrumentality” for the controlling party or corporation.⁷⁹ Applied to reverse piercing, this 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.⁸⁰ To avoid imposing this insurmountable burden on plaintiffs, courts have adopted a lesser standard of control based on the same factors considered in traditional piercing cases.⁸¹

Certain factors relevant in analyzing traditional piercing, while often cited, should also be reconsidered when assessing whether a corporation is an alter ego for reverse veil piercing purposes. One such example is that of undercapitalization. In traditional veil piercing, alter ego corporations often operate with insufficient assets, precluding a judgment creditor

⁷⁶ *Litchfield*, 799 A.2d at 312 (quoting *LiButti v. United States*, 107 F.3d 110, 119 (2d Cir. 1997)).

⁷⁷ *Shamrock Oil & Gas Co. v. Ethridge*, 159 F. Supp 693, 697 (D. Colo. 1958).

⁷⁸ See *infra* Part II.A.2 for an alternative view on how to deal with domination in a reverse piercing context.

⁷⁹ See *supra* notes 24–29 and accompanying text.

⁸⁰ See *FMC Fin. Corp. v. Murphree*, 632 F.2d 413, 422 (5th Cir. 1980) (“[T]here is factually no way that the subsidiary can interpose itself in the conduct of the parent’s affairs.”).

⁸¹ See *id.*

from satisfying a judgment against the corporation. In reverse piercing, it is more than likely that a third-party creditor is alleging that an individual is incapable of satisfying a debt because she has divested all her assets into a corporate alter ego. Thus, overcapitalization of a corporate alter ego could provide evidence of fraud and serve as a basis for reverse piercing the corporate veil.⁸²

To better understand the implications of the inverse method of reverse piercing, consider it in light of the Lady X hypothetical. To show domination, JC would point to the level of control Lady exerted over X Corp., including the intermingling of corporate and personal funds, sharing her personal and business address, lack of corporate formalities, and overcapitalization. JC would argue that by divesting her assets to, and purchasing assets with, X Corp., Lady has sheltered her assets in the corporation, rendering herself judgment-proof. Under the inverse method, satisfaction of those two elements would entitle JC to a judgment against X Corp. The court would disregard the potential claims of the innocent shareholders, Brother and Friend, and Bank Two,⁸³ because if Lady “was not deterred by the fact that [she] did not hold all of the stock . . . why should [her] creditors be?”⁸⁴

2. The “Equitable Results” Approach⁸⁵

The Colorado Supreme Court directly confronted the common criticisms of reverse piercing⁸⁶ and acknowledged that when “inartfully performed,” reverse piercing can negatively impact innocent third parties.⁸⁷ Rather than use the doctrinal shortcomings as support for an outright rejection of the doctrine, however, the court tried to craft a remedy that could protect the interests of judgment creditors, innocent shareholders, and

⁸² See *Pac. Dev., Inc. v. United States*, C.A. No. 77-0690, 1979 WL 1283, at *2 (D.D.C. Jan. 3, 1979).

⁸³ Because Bank One secured its loan under Article 9, it would have priority over Lady's claim even under this approach.

⁸⁴ *Sea-Land Servs., Inc. v. Pepper Source*, 941 F.2d 519, 521–22 (7th Cir. 1991).

⁸⁵ This Note will refer to the three-pronged approach taken by the Colorado Supreme Court in *In re Phillips* as the “equitable results” approach because it is the third element, an equitable results condition, which distinguishes the method of reverse piercing from the inverse method.

⁸⁶ For a detailed discussion of the criticisms of reverse piercing see *infra* Part II.B.

⁸⁷ *Connolly v. Englewood Post No. 322 Veterans of Foreign Wars of the U.S., Inc.* (*In re Phillips*), 139 P.3d 639, 645 (Colo. 2006) (en banc).

corporate creditors alike. The reality of their effort swung the pendulum too far in the opposite direction.⁸⁸ The shortcomings of the equitable results approach—as interpreted through subsequent case law—make it ill suited to deal with the factual situations presented in many reverse piercing cases. The Lady X hypothetical reaffirms that assertion, as this method would prevent JC from recovering. This Subsection first analyzes the additional factor imposed by this method and then surveys subsequent case law to better define the conditions it imposes, before ultimately applying this approach to the Lady X hypothetical.

In addition to the requirements of domination and a showing of fraud or injustice, Colorado requires that “an equitable result [be] achieved by piercing.”⁸⁹ The court defined “equitable result[s]” to mean that neither innocent shareholders nor corporate creditors would be prejudiced by allowing reverse piercing.⁹⁰ This requires an analysis to assess the availability of other, less intrusive remedies, and discourages reverse piercing when such remedies are viable alternatives.⁹¹ In *Phillips v. Englewood Post No. 322 Veterans of Foreign Wars of the U.S., Inc.*, the court found that because the shareholder’s personal creditors were identical to the corporation’s creditors, no harm would come to the creditors by reverse piercing.⁹² Similarly, reverse piercing did not injure innocent shareholders, as the individual Defendant owned the corporation outright.⁹³ The court left further decisions to determine whether any injury, no matter how minute, to creditors or shareholders would be sufficient to overrule a reverse piercing claim.

Since *Phillips*, there have been just four reverse piercing cases in Colorado. These cases have failed to contribute objective methodology to the lip service *Phillips* paid to equitable results. The subsequent cases forego the in-depth analysis necessary to

⁸⁸ As the subsequent application will reveal, JC would be unable to recover from Lady X under this method.

⁸⁹ See *In re Phillips*, 139 P.3d at 641. The requirement that an equitable result be achieved also exists in traditional veil piercing cases, though Courts routinely incorporated this requirement into the second prong, which requires a showing of fraud or injustice.

⁹⁰ See *id.* at 646.

⁹¹ See *id.* at 647.

⁹² See *id.* at 646.

⁹³ See *id.*

obtain “equitable results,” opting instead for a mechanical application of the elements.⁹⁴ The first case, *Stimpson v. Goldberg*,⁹⁵ misinterpreted the third prong of the reverse piercing test, finding the defendant’s ability to move assets beyond the plaintiffs’ reach “manifestly inequitable and unfair” in satisfaction of the third prong.⁹⁶ Two years later in *GRY Partners LLP v. Tabernash Meadows Water & Sanitation District*,⁹⁷ the court, in authorizing reverse piercing, noted that the limited liability partnership had no creditors and the only other partner was the individual Defendant’s wife, who contributed no capital to the partnership.⁹⁸ This holding begged the question of whether a capital investment would have prevented Plaintiff from reverse piercing the corporation.

The last of the *Phillips* progeny, *Shem, LLC v. Buhler*,⁹⁹ provides an answer to the question posed by *GRY Partners*.¹⁰⁰ Here, the plaintiff attempted to reverse pierce all the corporations in which the individual Defendant was involved, but succeeded only on those that the Defendant wholly owned.¹⁰¹ The depthless analysis proffered by the court in these cases falls far short of that required to ensure equitable results.

Using the equitable results approach, JC would not be able to recover against Lady—as he did under the inverse method. As a preliminary matter, there is a split as to whether Lady—an equitable owner—can be found to have dominated X Corp., though *Shem* seems to mandate that she cannot. The fact that she does not own any shares would prevent a finding of domination.¹⁰² Assuming, *arguendo*, she could, the question then

⁹⁴ In the most recent case, *Carreras v. Lemon*, No. 07-cv-00739-MSK-KMT, 2008 WL 3895527, at *2 (D. Colo. Aug. 22, 2008), the court dismissed Plaintiff’s claim for reverse piercing for failure to provide any factual basis as to any of the three elements.

⁹⁵ No. 2004CV1563, 2006 WL 3949633 (D. Colo. Nov. 8, 2006).

⁹⁶ *Id.* at *10.

⁹⁷ No. 2006CV220, 2008 WL 5597587 (D. Colo. June 12, 2008).

⁹⁸ *Id.* at *8.

⁹⁹ No. 06 CV 687, 2008 WL 4532827 (D. Colo. June 27, 2008), *aff’d*, No. 08CA2138, 2009 WL 2810330 (Colo. App. Sept. 3, 2009).

¹⁰⁰ *See id.* at *2–6.

¹⁰¹ *See id.* at *1, *5–6. The court did no further analysis as to the corporations’ involvement with or relations to the other shareholders, finding their mere existence to be sufficient to override Plaintiff’s interest in reverse piercing. *Id.*

¹⁰² In *Shem*, Plaintiff was not allowed to reverse pierce a company where the individual Defendant owned seventy percent and the other thirty percent consisted of various family members each with a five percent or less interest. *See id.*

turns to whether Brother and Friend's investments would serve as a bar to reverse piercing, a question unanswered in *GRY Partners*. The court could respond to Brother's and Friend's capital investment in one of three ways: (1) hold that their investments serve as an absolute bar to reverse piercing, (2) deduct the total amount of their investments from the corporation's total assets and allow JC to recover, or (3) allow JC to reverse pierce and ignore their investments entirely. Based on the logic of *Shem*, the court would presumably choose the first approach, barring JC from recovery since Brother and Friend each invested in X Corp. and each owned fifty percent of X Corp.¹⁰³

Thus, the "equitable results" approach fails to achieve just that. By not analyzing the effects, impact and involvement of innocent shareholders and creditors, courts give blind deference to a corporation's form rather than its substance. They are withholding justice from rightful plaintiffs on the chance that others may be adversely affected. Such precautions are wholly unnecessary as the facts of any case reveal whether such "chance" is present. Such deference to form obviates the need for reverse piercing by essentially precluding judgment for a plaintiff against any well-counseled defendant who has added shareholders to prevent such claims.

B. All Opposed . . . Reasons Supporting Courts' Rejection of Reverse Piercing

Rather than adopt either the inverse or equitable results method, many courts simply reject reverse piercing.¹⁰⁴ These courts cite several common objections. First, they say reverse piercing violates normal judgment collection procedures.¹⁰⁵ Second, courts point out the potential harm reverse piercing

¹⁰³ *See id.*

¹⁰⁴ States that have expressly rejected reverse piercing include California, Georgia, and Utah. *See* *Postal Instant Press v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96, 102 (Ct. App. 2008); *Acree v. McMahan*, 585 S.E.2d 873, 874 (Ga. 2003); *Transamerica Cash Reserve, Inc. v. Dixie Power & Water, Inc.*, 789 P.2d 24, 26 (Utah 1990). The Tenth Circuit has also rejected the doctrine. *See* *Cascade Energy & Metals Corp. v. Banks*, 896 F.2d 1557, 1577 (10th Cir. 1990) (rejecting reverse piercing under Utah law; decided before *Transamerica*); *see also* *Floyd v. IRS*, 151 F.3d 1295, 1298–1300 (10th Cir. 1998) (rejecting reverse piercing under Kansas law).

¹⁰⁵ *See, e.g., Cascade*, 896 F.2d at 1577. For a rejection of the arguments against veil piercing see *infra* Part III.A.

could bring to both innocent shareholders and corporate creditors.¹⁰⁶ Third, they argue that other, more traditional, remedies exist to provide plaintiffs with redress without resorting to the drastic remedy of reverse piercing the corporate veil.¹⁰⁷ Fourth, courts refuse to lessen the "domination" standard adopted in *FMC Finance Corp. v. Murphree*,¹⁰⁸ instead agreeing with Judge Hand that "outside reverse piercing is only appropriate in the rare case of a subsidiary dominating its parent."¹⁰⁹ Finally, several courts have expressed added disdain for reverse piercing when the plaintiff is a voluntary, contractual creditor as opposed to an involuntary, tort creditor.¹¹⁰

Normal judgment collection procedures permit a judgment creditor to attach an individual defendant's stock in a corporation.¹¹¹ Reverse piercing, however, allows an individual to skip this step by levying directly against the corporation's assets.¹¹² If successful in a reverse piercing action, the plaintiff would then be able to force a sale of the attached assets belonging to the corporation.

Courts highlight the negative effects that selling off the assets of a corporation could have. They stress the impact on non-culpable shareholders who would witness the value, and potentially the earning capacity of their corporation be sold off due to the actions of one individual shareholder.¹¹³ Additionally, creditors 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.¹¹⁴ These arguments, taken to their extremes, lead the courts to conclude that the unnerving prospect of losing 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.¹¹⁵ While the equitable results approach takes account

¹⁰⁶ See, e.g., *Cascade*, 896 F.2d at 1577.

¹⁰⁷ See *Floyd*, 151 F.3d at 1300.

¹⁰⁸ 632 F.2d 413, 422 & n.8 (5th Cir. 1980).

¹⁰⁹ *Floyd*, 151 F.3d at 1299-1300 (citing *Kingston Dry Dock Co. v. Lake Champlain Transp. Co.*, 31 F.2d 265, 267 (2d Cir. 1929)).

¹¹⁰ See *id.*

¹¹¹ See, e.g., *Cascade*, 896 F.2d at 1577.

¹¹² See *id.*

¹¹³ See *id.*

¹¹⁴ See *id.*

¹¹⁵ See *Acree v. McMahan*, 585 S.E.2d 873, 874-75 (Ga. 2003).

of these interests, it was discredited by a California court as creating requirements that “essentially eliminate the outside reverse piercing doctrine as a practical matter.”¹¹⁶

Courts further contend that reverse piercing and its associated risks are unnecessary given the availability of alternative, more traditional, remedies.¹¹⁷ Often-cited alternatives include conversion, fraudulent conveyance, respondeat superior, and conventional agency law.¹¹⁸ With such a wide gamut of remedies already available, courts insist there is no need to invent a new theory of liability.¹¹⁹

Additionally, in relying on Judge Hand’s reasoning in *Kingston*, some courts claim reverse piercing is only appropriate in the rare instance that a subsidiary corporation dominates its parent.¹²⁰ Agreeing with Judge Hand, they argue that the nature of the parent-subsidary relationship makes it nearly, if not completely, impossible for a subsidiary to interject itself in the affairs of a parent to the extent necessary to make the parent a mere instrumentality or alter ego.¹²¹ Courts hold that traditional veil piercing mandates this standard be served, and further believe lessening the standard with the potential downsides presented by reverse piercing would be unduly fair to a creditor of the corporation.¹²² Indeed, Justice Hand’s labeling such an instance as this “extremely rare” seems correct.¹²³ If courts apply this standard, most, if not all, reverse piercing claims would be denied.¹²⁴

Lastly, several courts who have considered reverse piercing also criticize a doctrine that would permit voluntary creditors of an individual, or corporation, to recover from another corporation.¹²⁵ At a minimum, courts suggest a distinction

¹¹⁶ See *Postal Instant Press, Inc. v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96, 106 (Ct. App. 2008).

¹¹⁷ See, e.g., *Floyd v. IRS*, 151 F.3d 1295, 1300 (10th Cir. 1998).

¹¹⁸ See, e.g., *id.*

¹¹⁹ See *id.*

¹²⁰ See *Acree*, 585 S.E.2d at 875 (citing *Kingston Dry Dock Co. v. Lake Champlain Transp. Co.*, 31 F.2d 265, 267 (2d Cir. 1929)).

¹²¹ See *Kingston Dry Dock*, 31 F.2d at 267.

¹²² See *Floyd*, 151 F.3d at 1299.

¹²³ *Kingston Dry Dock*, 31 F.2d at 267.

¹²⁴ See *Crespi*, *supra* note 3, at 68.

¹²⁵ See *Cascade Energy & Metals Corp. v. Banks*, 896 F.2d 1557, 1577 (10th Cir. 1990) (“[T]he analysis of corporate veil issues is different in a consensual

between voluntary and involuntary creditors given the distinct public policy issues each raises.¹²⁶ Judge Hand articulated this fear in *Kingston* writing, “[a]ll that has really happened is that the [plaintiff], being dissatisfied with the credit of the company with which [he] dealt now seeks to involve its creature.”¹²⁷ These courts contend that because voluntary creditors choose the parties with whom they deal, they can take precautions necessary to protect their interests and to permit reverse piercing would only reward a creditor’s failure to take such precautions, at the expense of other creditors.¹²⁸

III. THE NEED FOR REVERSE PIERCING: HOW A HYBRID APPROACH CAN PROTECT THE INTERESTS OF ALL PARTIES

When “inartfully performed,” the disadvantages of reverse piercing—such as injuries to innocent shareholders and corporate creditors—easily outweigh the benefits—allowing a judgment creditor to recover.¹²⁹ Failure to allow reverse piercing in certain instances, however, 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.¹³⁰ Part III first provides a brief overview of commonly cited alternative remedies and their shortcomings. It then proposes an alternative balancing test for reverse piercing that weighs the conflicting interests of all involved parties.

transaction, such as a breach of contract case, than in a nonconsensual transaction . . .”).

¹²⁶ See *id.*; see also *Edwards Co. v. Monogram Indus.*, 730 F.2d 977, 980–84 (5th Cir. 1984) (discussing the differences between tort and contract cases in veil piercing context); Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89, 112 (1985) (discussing the economic reasons for making a tort or contract distinction when piercing the corporate veil).

¹²⁷ *Kingston Dry Dock*, 31 F.2d at 267.

¹²⁸ See *Postal Instant Press, Inc. v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96, 105 (Ct. App. 2008); see also *Cascade*, 896 F.2d at 1577.

¹²⁹ *Connolly v. Englewood Post No. 322 Veterans of Foreign Wars of the U.S., Inc. (In re Phillips)*, 139 P.3d 639, 645 (Colo. 2006) (en banc).

¹³⁰ *C.F. Trust, Inc. v. First Flight Ltd. P’ship*, 140 F. Supp. 2d 628, 642 (E.D. Va. 2001).

A. *The Inadequacy of Alternative Remedies*

1. Fraudulent Conveyance

Courts often cite fraudulent conveyance as an adequate alternative to reverse piercing. While it may suffice in many situations, however, there are instances where the fraudulent conveyance doctrine alone proves insufficient to promote justice. The existence of a separate corporate entity can allow a debtor to circumvent the transfer requirement by utilizing corporate assets as a personal piggybank instead of transferring personal assets to the corporation, thus making it hard to prove fraudulent intent. Employment of fraudulent conveyance to the Lady X hypothetical brings this shortcoming to the forefront as fraudulent conveyance proves useless to JC.¹³¹ This Subsection discusses the scope and requirements of fraudulent transfer law, before applying it to the Lady X hypothetical. The remedy is then applied to *Postal Instant Press, Inc. v. Kaswa Corp.* to show that, despite the court's assertion to the contrary, the fraudulent conveyance doctrine did not serve as an adequate alternative to reverse piercing.

Fraudulent conveyance law has remained largely unchanged¹³² for five hundred years¹³³ and entitles creditors to avoid transfers made either “(1) with actual intent to hinder, delay, or defraud any creditor of the debtor; or (2) without receiving a reasonably equivalent value in exchange for the transfer or obligation” when other conditions¹³⁴ are met.¹³⁵ To aid

¹³¹ For a description of the elements giving rise to fraudulent conveyance see *infra* note 134 and accompanying text. See also UNIF. FRAUDULENT TRANSFER ACT § 4(a), 7A U.L.A. pt. 2, at 58 (1948).

¹³² See *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 540–41 (1994).

¹³³ The prototypical, and most often cited, fraudulent conveyance case is *Twyne's Case*, where Pierce, a debtor with a creditor's action pending, created a secret deed gifting all his personal property to Twyne, to whom Pierce also owed money. Twyne v. KB, [1601] 76 Eng. Rep. 809, 811–14. Following the transfer, Pierce continued to use his property, even branding and selling the sheep he had “gifted.” *Id.* at 811. The court held that while the transfer as payment of the debt owed to Twyne could ordinarily constitute valid consideration, the circumstances surrounding this transfer made it fraudulent. *Id.* at 812–13.

¹³⁴ The other conditions require that the debtor either “(i) was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or (ii) intended to incur, or believed or reasonably should have believed that he [or she] would incur, debts beyond his [or her] ability to pay as they became due.” UNIF.

in determining "actual intent," the Uniform Fraudulent Transfer Act ("UFTA") includes eleven "badges of fraud."¹³⁶ The UFTA created a four year statute of limitations for fraudulent conveyance actions, although many states have either increased or decreased this statutory period.¹³⁷

Even if the elements of fraudulent conveyance are satisfied, the doctrine provides a plaintiff with very limited remedies. The primary remedy is avoidance of the fraudulent transfer.¹³⁸ Some states also permit attachment or other provisional remedies against the asset transferred.¹³⁹ Additionally, a plaintiff is entitled to the value of the asset transferred when a

FRAUDULENT TRANSFER ACT § 4(a)(2)(i), 7A U.L.A. pt. 2, at 58 (1984) (alterations in original).

¹³⁵ UNIF. FRAUDULENT TRANSFER ACT § 4(a), 7A U.L.A. pt. 2, at 58 (1984). The UFTA has been adopted in forty-three states and the District of Columbia.

¹³⁶ *BFP*, 511 U.S. at 535, 541. The eleven badges of fraud are:

(1) the transfer or obligation was to an insider; (2) the debtor retained possession or control of the property transferred after the transfer; (3) the transfer or obligation was disclosed or concealed; (4) before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit; (5) the transfer was of substantially all the debtor's assets; (6) the debtor absconded; (7) the debtor removed or concealed assets; (8) the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred; (9) the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred; (10) the transfer occurred shortly before or shortly after a substantial debt was incurred; and (11) the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

UNIF. FRAUDULENT TRANSFER ACT § 4(b), 7A U.L.A. pt. 2, at 57-58 (1984). These badges of fraud are not presumptions of fraud, but merely relevant evidence. *See id.* at cmt. 5, 7A U.L.A. pt. 2, at 59-60.

¹³⁷ *See, e.g.*, FLA. STAT. ANN. § 56.29(6)(a) (West 2011) (creating a one year statute of limitations when a judgment has already been obtained); N.Y. C.P.L.R. § 213 (McKinney 2011) (establishing a six year statute of limitations for fraudulent transfers). Federal Bankruptcy Law covers any transfers made within two years of the filing of a petition. *See* 11 U.S.C § 548 (2006). Regardless of the timeframe, the statute of limitations begins running when the claim or transfer occurs and not when the plaintiff's claim has been reduced to judgment. *See Sands v. New Age Family P'ship, Ltd.*, 897 P.2d 917, 920 (Colo. App. 1995) (citing *Fish v. East*, 114 F.2d 177 (10th Cir. 1940)).

¹³⁸ *See* UNIF. FRAUDULENT TRANSFER ACT § 7(a)(1), 7A U.L.A. pt. 2, at 58; *see also id.* at cmt. 2, 7A U.L.A. pt. 2, at 59.

¹³⁹ *See* UNIF. FRAUDULENT TRANSFER ACT § 7 cmt. 2, 7A U.L.A. pt. 2, at 58. While attachment is available, practical considerations weigh against attachment prior to the conveyance being set aside. *See Peter A. Alces & Luther M. Dorr, Jr., A Critical Analysis of the New Uniform Fraudulent Transfer Act*, 1985 U. ILL. L. REV. 527, 545.

fraudulent transferee subsequently transfers the asset.¹⁴⁰ This right, however, is lost when the transferee, without knowledge of the fraud, purchased the asset for fair consideration.¹⁴¹

Applied to the Lady X hypothetical, the doctrine of fraudulent conveyance provides JC with little help. Under fraudulent conveyance law, JC would not be able to seek attachment on either the apartment or the car owned by the corporation since those assets were acquired by the corporation, and not transferred to it. Even though Lady uses them for personal use, it is corporate property and JC's judgment is against Lady. The only potential basis for a fraudulent transfer action would be Lady's investing her life savings in the corporation, as it is this transfer that made her insolvent. This claim would fall under UFTA § 4(a)(1), requiring JC to show actual intent.¹⁴² Here the only badge of fraud that could support JC's claim would be Lady's transfer of all her personal assets—her life savings—to an insider, Corp. X.¹⁴³

Even if deemed an insider, it is equally probable—and, arguably more likely—that this badge of fraud will be found as a valid investment in Lady's company—her first step down the road of entrepreneurship—and not an illegal transfer. Lady's argument will likely succeed because the badges of fraud are only presumptions, and her motive could easily rebut the presumption of fraudulent intent. Furthermore, no single presumption is dispositive, and here JC can only point to one of the eleven badges. The only scenario that would permit Lady's investment in X Corp. to be found a fraudulent transfer would be if the "investment" came after she had already been sued, or had been threatened with such a lawsuit. In that scenario, especially given Lady's retained use of the property to pay her expenses,

¹⁴⁰ UNIF. FRAUDULENT TRANSFER ACT § 8(b), 7A U.L.A. pt. 2, at 178–79. The plaintiff is also entitled to any depreciation in value of the asset while in possession of the fraudulent transferee. *See id.* at § 8(c), 7A U.L.A. pt. 2, at 178–79.

¹⁴¹ *Id.* at § 8(a), 7A U.L.A. pt. 2, at 178–79.

¹⁴² The party seeking to avoid the transfer must show there was a transfer to an insider made with "actual intent to hinder, delay, or defraud any creditor of the debtor." UNIF. FRAUDULENT TRANSFER ACT § 4(a)(1), 7A U.L.A. pt. 2, at 58.

¹⁴³ There would also be an issue as to whether the corporation is in fact an insider, since Lady is an equitable, not legal, owner. This analysis has been omitted because even if X Corp. is an insider, the remedy proves inadequate.

there would likely be enough to show actual intent to defraud given the pending litigation. As the facts are, however, JC would be unable to use this remedy to recover against Lady.

A look at the complicated facts of *Postal Instant Press*¹⁴⁴ shows that even in less “prototypical” reverse piercing cases, fraudulent conveyance alone can fall short of achieving equitable results.¹⁴⁵ In *Kaswa*, the defendant, Mr. Rangoonwala, purchased a Postal Instant Press (“PIP”) franchise from a third party.¹⁴⁶ PIP consented to the assignment and was a party to the agreement.¹⁴⁷ Following the purchase, Rangoonwala and a friend ran the franchise as general partners.¹⁴⁸ After several years of operating as partners, Rangoonwala created Kaswa Corp. (“Kaswa”) for the sole purpose of operating the PIP franchise.¹⁴⁹ Thus, Kaswa, and not Rangoonwala, owned all the franchise assets.¹⁵⁰ Kaswa later merged with another company called The Print Works, but maintained the name Kaswa.¹⁵¹ Upon being sued, Kaswa sold the assets to another company for fair value.¹⁵² After obtaining a judgment against Rangoonwala for non-payment of franchise fees, PIP attempted to levy against the franchise assets, but learned of the transfer and sale of the assets.¹⁵³ PIP attempted to add Kaswa as a judgment debtor under the theory of reverse piercing.¹⁵⁴ The court rejected PIP’s argument and refused to add Kaswa as a judgment debtor, in part because of the availability of other remedies such as a

¹⁴⁴ *Postal Instant Press, Inc. v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96 (Ct. App. 2008).

¹⁴⁵ The facts of *Kaswa* also presents two additional issues: (1) harm to an innocent shareholder and (2) a distinction between a voluntary creditor and an involuntary creditor. While these are factors that should be considered in any reverse piercing action, they are omitted from discussion in this Subsection, which focuses solely on the adequacy of fraudulent conveyance as a substitute remedy for reverse piercing. For a discussion on the rights voluntary creditors, involuntary creditors, and innocent shareholders should have in reverse piercing actions, see *infra* Part III.B.1–2, respectively.

¹⁴⁶ *Postal Instant Press*, 77 Cal. Rptr. 3d at 98.

¹⁴⁷ *See id.*

¹⁴⁸ *See id.*

¹⁴⁹ *See id.* at 99.

¹⁵⁰ *See id.*

¹⁵¹ *See id.*

¹⁵² *See id.*

¹⁵³ *See id.* at 98–99.

¹⁵⁴ *See id.* at 100–01.

fraudulent conveyance action.¹⁵⁵ An analysis, however, shows PIP would have likely been unable to recover under fraudulent conveyance law.

One way of showing a fraudulent transfer would be to prove actual intent to hinder or defraud a creditor. There seems to be no problems with the initial transfer of the franchise assets to Kaswa. The corporation was capitalized and also had the franchise assets as collateral. It seems unlikely Rangoonwala had fraudulent intent as he requested permission from PIP to add Kaswa to the franchise agreement. Again, the only “badge of fraud” that seems applicable was that the transfer was to an insider as defined in the UFTA.¹⁵⁶ Because these factors are only presumptive, it is unlikely that showing just one would convince a trier of fact of fraud.

The other way to prove a fraudulent transfer would be to show the transfer was made without an exchange of equivalent value if also accompanied by one of two other conditions. PIP could likely prove this element as Rangoonwala transferred the equipment from himself to his corporation without receiving a reasonably equivalent value in exchange. However, the exchange of value may not have been required as Rangoonwala, at the time, was the president and sole owner of Kaswa. His control of the transferee, makes this different from an exchange to a third party for less than reasonable value. Assuming Rangoonwala’s transfer to Kaswa did satisfy the equivalent value element, PIP would still have to prove Rangoonwala was either (1) engaged in or about to engage in a transaction with unreasonably small assets in relation to that transaction or (2) that he intended to incur debts beyond his ability to pay.¹⁵⁷

The first option is inapplicable here because (1) even after the transfer, Rangoonwala had sufficient assets to cover the only transaction he was then engaged in—the Franchise Agreement—and (2) Rangoonwala did not enter into any further transactions in either his individual capacity or through Kaswa. The second option is, at best, debatable when applied to these facts. Rangoonwala could have known that following the transfer he would fail to make franchisee payments to PIP, ultimately

¹⁵⁵ See *id.* at 105.

¹⁵⁶ See UNIF. FRAUDULENT TRANSFER ACT § 1(7)(i)(D), 7A U.L.A. pt. 2, at 14 (1984).

¹⁵⁷ See *id.* § 4(a)(2)(i)–(ii).

resulting in his inability to pay the amounts owed, but, for nearly three years post-transfer Rangoonwala continued to make royalty payments. The fact that he continued to pay for so long would make it difficult for PIP to prove this second option. PIP, therefore, would not be able to show Rangoonwala's transfer to Kaswa was fraudulent.

PIP would, however, be able to prove Kaswa fraudulently transferred the franchise assets when it sold them upon learning of PIP's action against Rangoonwala. That transfer was made with actual intent to defraud a creditor. While PIP could not have avoided the transfer—because the buyer purchased the franchise assets for reasonably equivalent value—it would have been entitled to Kaswa's proceeds from the sale of the franchise assets. PIP's right to these proceeds would have proven useless, however, because Kaswa could only have been held liable for PIP's judgment against Rangoonwala if the court permitted PIP to reverse pierce and hold Kaswa liable for that judgment. Thus, even had PIP shown Kaswa's sale of the assets to be fraudulent conveyance, they would still not have been able to recover the value of the assets without reverse piercing. Accordingly, despite the court's assertion to the contrary, the doctrine of fraudulent conveyance did not in fact serve as an alternative remedy. Reverse piercing offered PIP its only chance at justice.

As the Lady X hypo and *Kaswa* illustrate, there are instances where fraudulent conveyance is unable to ensure just results, namely when an individual acquires assets via a corporation for the sole purpose of limiting personal liability. Even in those situations where a fraudulent conveyance action may successfully be asserted, like in *Kaswa*, the limited remedies the doctrine affords can cause undue hardships on plaintiffs while simultaneously benefitting the wrongdoing party. Furthermore, the statute of limitations, which could serve as a bar to recovery in fraudulent conveyance actions, would not preclude a judgment in a reverse piercing case. In reverse piercing, the wrong complained of—abusing the corporate form—is ongoing; it is the continued operation of the corporation that allows the defendant to elude liability.

2. Bypassing Normal Judgment Collection Procedures

While attaching shares is preferable to attaching assets—because the former only negatively implicates the liable shareholder—the realities of most alter ego corporations make attaching shares impracticable, if not impossible. Traditional attachment presents four potential problems in the reverse piercing context. First, many closely held alter ego corporations do not issue stock. Second, even when stock is issued, valuing these businesses is a difficult task. Third, even when valued, many closely held corporations place limitations on the alienability of the stock.¹⁵⁸ Finally, if the individual defendant is an equitable owner, she will not have any shares to attach. The *Lady X* hypothetical illustrates several of these shortcomings.

Shares in a corporation are considered part of an individual's assets. To satisfy one's judgment, a creditor can simply attach the judgment debtor's shares or rights to cash distributions.¹⁵⁹ Many closely held alter ego corporations, however, never issue stock.¹⁶⁰ In fact, limited liability companies ("LLCs") cannot issue stock at all—issuing instead membership interests.¹⁶¹ Furthermore, even when a closely held alter ego corporation does issue stocks, most do not pay dividends and avoid regular disbursements, opting instead to use the corporation's assets as a personal piggybank.¹⁶² The absence of distributions negates any chance of recovering moneys via successful attachment. The only option for the plaintiff after attachment would be to sell the shares; given the corporate abuse, even if successful this would not net much. Such a corporate structure thus deprives plaintiffs of "any means" of collecting on their judgments.¹⁶³

¹⁵⁸ A closely held alter ego corporation refers to a corporation that has already met the two elements required to prove alter ego. See *Maroun v. Wyreless Sys., Inc.*, 114 P.3d 974, 987 (Idaho 2005). Accordingly, it infers a lack of corporate formalities.

¹⁵⁹ *Litchfield Asset Mgmt. Corp. v. Howell*, 799 A.2d 298, 312 n.14 (Conn. App. Ct. 2002).

¹⁶⁰ See *Mix v. Plaza Redondo, Ltd.*, No. YC 023339, 2002 WL 34239685, at *4 (Cal. Super. Ct. Dec. 27, 2001).

¹⁶¹ Mark A. Sargent, *Are Limited Liability Company Interests Securities?*, 19 PEPP. L. REV. 1069, 1095 (1992).

¹⁶² See, e.g., *Goya Foods, Inc. v. Unanue*, 233 F.3d 38 (1st Cir. 2000) (holding that a closely held corporation was the alter ego of the judgment debtor because he used its assets as a personal piggybank).

¹⁶³ See *Litchfield*, 799 A.2d at 314.

While not easy, a failure to issue stock does not preclude attachment as courts have ways to evaluate the worth of a closely held corporation. Valuing a company is described as a “pseudoscience” or an “art form” because there are countless methods used to determine worth.¹⁶⁴ Regardless of the approach, factors of importance include property to be valued, the business history of the enterprise, the economic outlook of the industry, and the earning capacity of the company.¹⁶⁵ Once a valuation is determined, courts must then determine market value of the stock by establishing a proper ratio between valuation factors and the price per share that a reasonable buyer would be willing to pay.¹⁶⁶ The reality of alter ego corporations—with neglected formalities and commingled funds—only make these calculations more difficult. For instance, several factors, including dividends and expenses, would commonly be non-existent or vastly skewed because of the defendant’s misuse of the corporate form. While not impossible, accurately valuing a closely held alter ego corporation would be a protracted process with no great probability of an accurate outcome.

Even if a defendant’s alter ego corporation did issue stock and the corporation is accurately valued, attaching shares still may not be a viable option. In closely held corporations, there are often limitations on alienability. Stock ownership limitations can be imposed by a corporation’s chosen structure. For instance, if the alter ego corporation is an S corporation,

¹⁶⁴ Stanley J. Feldman, *Business Valuation 101: The Five Myths of Valuing a Private Business*, SCORE (May 10, 2011), www.score.org/article_business_valuation_101.html. The IRS recognizes three valuation approaches: the asset-based approach, the market approach, and the income approach—though all three need not be mutually exclusive. See I.R.S. BUS. VALUATION GUIDELINES § 4.48.4.2.3(2) (2006). There are, however, eight valuation methods routinely used by appraisers, investors, and business owners. See IRVING L. BLACKMAN, *VALUING YOUR PRIVATELY HELD BUSINESS: THE ART & SCIENCE OF ESTABLISHING YOUR COMPANY’S WORTH* 57 (rev. ed. 2005). For an overview of these valuation approaches see *id.* at 57–64.

¹⁶⁵ See I.R.S. BUS. VALUATION GUIDELINES §§ 4.48.4.2.2, 4.48.4.2.3. Other factors include the book value of the stock or interest and the financial condition of the business, the dividend-paying capacity, and the market price of stocks of corporations in a similar line of business. See *id.* § 4.48.4.2.3. Valuers also need to consider intangible property, including everything from patents and software to customer lists and forecasts. See *id.*

¹⁶⁶ See Annotation, *Valuation of Closely Held Stock for Federal Estate Tax Purposes Under § 2031(b) of Internal Revenue Code of 1954* (26 U.S.C.A. § 2031(b)), and *Implementing Regulations*, 22 A.L.R. FED. 31, § 4 (2008).

no other corporations or LLCs can be shareholders.¹⁶⁷ Similarly, most LLCs do not permit transfer of membership interests absent approval from other members.¹⁶⁸ Owners can place additional restrictions on alienability through the corporation's articles of organization and bylaws.¹⁶⁹ These restrictions can include qualifications and restrictions on the ownership of stock subject to a right to repurchase in the event of a violation.¹⁷⁰ Even if not an outright impediment, restrictions on alienability also lower the stock's marketability, and consequently the price.¹⁷¹ Alienability is crucial in a free market and restrictions on it could cause concern to a hypothetical buyer regarding the presence of a ready market for the corporation's stocks.¹⁷²

The Lady X hypothetical highlights several of the above-mentioned weaknesses of attaching stock in reverse piercing actions. A preliminary issue here is who actually owns the shares; Lady is only an equitable owner, and as such, she does not own X Corp. stock.¹⁷³ Lady also receives no cash distribution—be it dividends, profits, or salary—for her involvement. She instead pays personal expenses using corporate funds, which places the assets out of reach of attachment. If this matter were somehow addressed, courts would then have to attempt to value X Corp. This would involve pouring over accounts that may have been improperly maintained to determine the profitability of the corporation. Each expense would need to be scrutinized given the intermingling of funds and use of corporate assets for payment of personal expenses. Furthermore, there may or may not be restrictions on the alienability of X Corp.'s shares.

¹⁶⁷ *S Corporation vs. C Corporation: A Comparison*, BIZFILINGS, <http://www.bizfilings.com/learn/s-corporation-vs-c-corporation.aspx> (last visited Feb. 11, 2012).

¹⁶⁸ *LLC vs. S Corp: Which Business Type Is Right for Me?*, BIZFILINGS, <http://www.bizfilings.com/learn/llc-vs-s-corp.aspx> (last visited Feb. 11, 2012).

¹⁶⁹ Edward D. Tarlow, *Creative Succession Planning for Managing and Owning the Family Business*, FINDLAW, <http://library.findlaw.com/1999/Aug/1/126127.html> (last visited Feb. 11, 2012).

¹⁷⁰ *See id.*

¹⁷¹ *Cook v. Comm'r*, 349 F.3d 850, 856 (5th Cir. 2003).

¹⁷² *See Estate of Jung v. Comm'r*, 101 T.C. 412, 434 (1993); *see also Trust Servs. of Am., Inc. v. United States*, 885 F.2d 561, 569 (9th Cir. 1989) (holding resale restrictions may require discount to accurately value the stock).

¹⁷³ For a discussion on the need for imposing liability on equitable owners, *see infra* Part III.B.1.

Accordingly, even when courts are able to move past issues of valuation and alienability, they may run into additional problems as traditional judgment collection procedures are incapable of penalizing an equitable owner who uses a corporation to judgment proof herself.

3. Agency¹⁷⁴

Agency generally “encompasses the legal consequences of consensual relationships.”¹⁷⁵ A principal, by manifesting consent for another, the agent, to work subject to the principal’s right of control, gives the agent the “power to affect the principal’s legal relations through the agent’s acts and on the principal’s behalf.”¹⁷⁶ In a reverse piercing context, this would require the individual debtor to have been acting as an agent of the alter ego corporation when she committed the wrong so liability could be imputed to the corporation. While individual state laws vary slightly, this requires a plaintiff to show that (1) the individual was authorized by another to act for or in place of another person or corporation and (2) the act leading to the claim occurred within the scope of authority.¹⁷⁷

While agency principles can impute liability in specific instances, once the use of the corporate form to shelter personal assets is acknowledged, the limitations of agency principles of liability become clear. An individual debtor is essentially judgment proof provided the original cause of action falls outside the corporation’s scope. Thus, in the Lady X hypothetical, despite Lady’s personal insolvency, JC would be unable to attach the corporation’s assets because JC’s tort claim arose from conduct falling outside Lady’s scope of employment with X Corp.

¹⁷⁴ Courts often cite both agency and respondeat superior as alternative remedies. However, respondeat superior is merely a specific type of agency, employer liability. See RESTATEMENT (THIRD) OF AGENCY Intro. (“The common law of agency in the United States encompasses the principle of respondeat superior . . .”). Accordingly, all references to agency should be read to include respondeat superior.

¹⁷⁵ *Id.*

¹⁷⁶ *Id.*

¹⁷⁷ See *Bennett v. Reynolds*, 242 S.W.3d 866, 896 (Tex. App. 2007), *rev’d in part on other grounds*, 315 S.W.3d 867 (Tex. 2010).

The the underlying conflict in *Bennett v. Reynolds*¹⁷⁸ proved conducive to remedy via agency principles. There, the Supreme Court of Texas rejected an attempt to reverse pierce the corporate veil, choosing instead to impute liability to the corporation by applying agency principles.¹⁷⁹ Plaintiff had a longstanding feud with the individual defendant, and after discovering Defendant auctioned off thirteen of his cattle, Plaintiff sued both the individual Defendant and Defendant's corporation for conversion.¹⁸⁰ The individual Defendant resided on property owned by the Defendant corporation.¹⁸¹ The individual Defendant's conversion of Plaintiff's cattle also occurred on the corporation's land.¹⁸² While the corporation itself did not raise cattle, the individual Defendant did use the corporation's land for that purpose.¹⁸³ The individual Defendant owned no part of the corporation—his daughters did—but the defendant was the president and he admitted that he “[made] the decisions” and “[ran the] ranch.”¹⁸⁴ Plaintiff attempted to hold the corporation liable on a reverse piercing theory.¹⁸⁵ The court, however, held that because the individual defendant used *corporate* authority over “*corpora[te]* employees, using *corpora[te]* materials and equipment,” traditional agency principles were sufficient to hold the corporation liable for the conversion.¹⁸⁶

Many times, however, an individual defendant's actions will not fall within the scope of corporate activity.¹⁸⁷ Limiting liability to situations involving an agency relationship assumes that the corporate form can only be misused by the acts of its agents—ignoring the possibility that the corporate form itself could be used to procure a wrong by using it as a shelter for personal assets.¹⁸⁸

¹⁷⁸ *Id.*

¹⁷⁹ See *Bennett v. Reynolds*, 315 S.W.3d 867, 884–85 (Tex. 2010)

¹⁸⁰ *Bennett*, 242 S.W.3d at 874–75.

¹⁸¹ *Id.* at 871.

¹⁸² *Id.* at 872.

¹⁸³ See *id.* at 869–70.

¹⁸⁴ See *id.* at 898.

¹⁸⁵ See *id.* at 875–76.

¹⁸⁶ *Id.* at 897 (emphasis added).

¹⁸⁷ See, e.g., *Goya Foods, Inc. v. Unanue*, 233 F.3d 38 (1st Cir. 2000); *Fischer Inv. Capital, Inc. v. Catawba Dev. Corp.*, 689 S.E.2d 143 (N.C. Ct. App. 2009); *C.F. Trust, Inc. v. First Flight Ltd. P'ship*, 111 F. Supp. 2d 734 (E.D. Va. 2001).

¹⁸⁸ See *Fischer*, 689 S.E.2d at 151–52.

4. Conversion

Conversion is another often-cited alternative to reverse piercing. The tort of conversion, however, has a very limited scope and is only effective in very specific factual situations, as will be evidenced by its inapplicability to the Lady X hypothetical. This Subsection will first discuss the elements of conversion, then apply it to the hypothetical before finally applying the doctrine to a recent case to highlight the remedy's limited scope.

Conversion is an intentional exercise of dominion or control over another's property that so seriously interferes with their right to control it that the actor may be required to pay the other the property's full value.¹⁸⁹ There are several factors considered in determining the severity of an exercise of dominion, including the duration and the intent to assert a right inconsistent with the other's right of control.¹⁹⁰ The initial requirement, however, for any action in conversion is that the plaintiff had a legal right to the converted property prior to the defendant taking it.

The square peg of conversion would be inapplicable to the "circle" of facts implicated by the Lady X hypothetical. Prior to the tort, JC had no legal rights in any of the assets belonging to X Corp. and, thus, would not be able to claim conversion. Furthermore, the judgment obtained against Lady would not be sufficient to vest JC with any legal rights in the assets of X Corp.

In the *Bennett* case, the plaintiff's primary cause of action was for conversion.¹⁹¹ The defendant knowingly took the plaintiff's cattle and sold them at an auction.¹⁹² Even there, however, the tort of conversion was insufficient for Plaintiff to recover. Conversion allowed the plaintiff to impose liability against the defendant as an individual. The defendant, however, was insolvent because his alter ego corporation owned all his assets, including the farm he lived on.¹⁹³ Thus, absent a

¹⁸⁹ RESTATEMENT (SECOND) OF TORTS § 222A(1) (1965).

¹⁹⁰ See *id.* § 222A(2). Other factors considered are the actor's good faith, the extent and duration of the resulting interference, the harm done to the chattel, and the inconvenience and expense caused to the other. See *id.*

¹⁹¹ *Bennett v. Reynolds*, 242 S.W.3d 866, 896 (Tex. App. 2007).

¹⁹² See *id.*

¹⁹³ See *id.* at 871-72, 896.

way to attach corporate assets, the plaintiff's judgment for conversion against the individual defendant would have been meaningless.¹⁹⁴

Conversion seems ill suited to deal with the problem of "judgment proofing" by use of the corporate form to hide assets. While cases like *Bennett* and *Postal Instant Press* could provide a basis for conversion, most reverse piercing cases involve corporations sheltering the defendant's personal assets, as opposed to assets belonging to the plaintiff. Furthermore, *Bennett* and *Postal Instant Press* highlight the futility in permitting a judgment against an insolvent defendant. Even if successful, 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.

B. Reverse Piercing: A New Approach

It is the task of the court "to do justice to each litigant."¹⁹⁵ As Section A of Part III illustrates, there are instances where, despite blatant misuse of the corporate form, justice dies on the doorstep of the court.¹⁹⁶ In the name of judicial convenience, courts have adopted overly simplistic standards that overlook the interests of involved parties, or strict requirements, if any at all, that again fail to do justice to each litigant. Courts can safeguard the interests of all parties at the expense of none by (1) requiring plaintiff to show the inadequacy of other remedies, (2) permitting recovery against equitable owners, (3) permitting a capital exemption for innocent shareholders, and (4) applying preexisting creditor-priority laws.

¹⁹⁴ In this case, the court applied agency principals because Defendant's business involved cattle raising. *See id.* at 896. However, had Defendant been involved in a different line of business, the only means by which Plaintiff could have satisfied his judgment would have been through reverse piercing of the corporate veil.

¹⁹⁵ *Desist v. United States*, 394 U.S. 244, 259 (1969).

¹⁹⁶ *See infra* Part III.A.

1. Ownership Requirement Versus "Domination"

Ownership as a prerequisite to reverse piercing is easily circumvented, facilitating the practice of "judgment-proofing."¹⁹⁷ One would be able to shirk responsibility merely by including alternate shareholders in the corporate charter; indeed, that is exactly what many judgment debtors have done.¹⁹⁸ The sole protection afforded by requiring ownership is that it ensures no innocent shareholders will be adversely affected by a decision to reverse pierce. The protection of innocent shareholders, while vital, does not necessitate that their mere existence should preclude a plaintiff from reverse piercing. In many closely held corporations—often the subject of reverse piercing—these other shareholders are family and friends who receive no compensation and are not even able to explain their responsibilities within the corporation.¹⁹⁹ This protection of innocent shareholders, while necessary, can be achieved by much less restrictive means.²⁰⁰ In attempting to get around their own judicially imposed requirement, courts have stretched the ownership requirement beyond reason.²⁰¹

To prevent inequity, all courts should apply a "domination" standard. The disallowance of reverse piercing for a lack of legal ownership is a denial of justice because of a mere technicality. Additionally, mandating ownership simply permits those who wish to escape liability to do so by having other shareholders. Such a standard would not lower the threshold to permit piercing. A plaintiff would still need to show that the individual exercised control over a corporation to such an extent that the corporation is but a mere alter ego or instrumentality. The only

¹⁹⁷ Judgment-proofing occurs when a creditor is unable to satisfy an actual or potential judgment for money damages because the debtor has no property, does not own enough property within the court's jurisdiction to satisfy the judgment, or claims the benefit of statutorily exempt property. BLACK'S LAW DICTIONARY 921 (9th ed. 2009).

¹⁹⁸ See, e.g., *Shem, LLC v. Buhler*, No. 06 CV 687, 2008 WL 4532827 ¶ 13 (D. Colo. June 27, 2008) (denying Plaintiff's reverse piercing claim because individual defendant was "not the sole owner").

¹⁹⁹ See *id.*

²⁰⁰ For a suggested approach to protecting innocent shareholders see *infra* Part III.

²⁰¹ See *Riddle v. Leuschner*, 335 P.2d 107, 111 (Cal. 1959) (holding ownership requirement satisfied as to individual defendant who owned one share and did not participate in business, but not as to other individual defendant who owned no shares but served as the manager of corporation and made all business decisions).

difference would be that a corporation could then be reverse pierced because of the actions of both legal *and* equitable owners. This standard is currently used by many courts and prevents injustice because it is malleable to the truth of a particular situation, rather than emphasizing legal form over function.²⁰² By applying a “domination” standard that permits reverse piercing because of the actions of an equitable owner, courts would no longer have to resort to nominal ownership and, more importantly, judgment debtors could not immunize themselves with the stroke of a pen on a stock certificate. Applied to the Lady X hypothetical, such a standard would allow JC to reverse pierce X Corp. for the judgment against Lady despite her lack of legal ownership in the corporation.

2. Innocent Shareholders

Small businesses are an integral part of the national economy²⁰³ and investment is the engine that runs small business.²⁰⁴ Those looking to start up a business or to capitalize their small business often rely on investments from friends, family, venture capitalists, angel investors, and the like.²⁰⁵ It is not uncommon for these investors to require an ownership interest, a board position, or both as a prerequisite to their investments.²⁰⁶ No remedy for reverse piercing that failed to take the interests of the investor into account would be beneficial to society. This Subsection proposes guidelines to first determine

²⁰² See, e.g., *Sheffield Servs. Co. v. Trowbridge*, 211 P.3d 714, 720 (Colo. App. 2009) (requiring ownership “would open the door to fraud”); *State v. Easton*, 169 Misc. 2d 282, 289, 647 N.Y.S.2d 904, 909 (Sup. Ct. Albany Cnty. 1995).

²⁰³ Small businesses represent over ninety-nine percent of the nation’s employers and over fifty percent of its private sector employment. See OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMINISTRATION, *Small Business Profile: United States* (2009), available at www.sba.gov/advo/research/profiles/09us.pdf.

²⁰⁴ Credit also plays a critical role in the capitalization of small businesses. For a discussion of the importance of corporate creditors see *infra* Part III.

²⁰⁵ See OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMINISTRATION, *Small Business Research Summary* (2008), available at <http://archive.sba.gov/advo/research/rs331.pdf>; *Startup Financing*, ENTREPENUER <http://www.entrepreneur.com/money/howtguide/article52718.html> (last visited Feb. 11, 2012).

²⁰⁶ See Robert C. Illig, *Minority Investor Protections as Default Norms: Using Price To Illuminate the Deal in Close Corporations*, 56 AM. U. L. REV. 275, 325 (2006); see also *Angel Investors*, SMALL BUS. NOTES, <http://www.smallbusinessnotes.com/financing/angelinvestors.html> (last visited Feb. 11, 2012).

the innocence of a shareholder and then provides safeguards for truly innocent shareholders. Finally, the proposal will be illustrated by application to the Lady X hypothetical.

Investors who negotiate for power within a corporation are in a position to insulate the corporation from reverse piercing claims through adherence to corporate formalities and adequate oversight.²⁰⁷ All stockholders in a closely held corporation, have fiduciary duties of the "utmost good faith and loyalty," requiring them to act in the best interests of the corporation.²⁰⁸ These stockholders can use the power they have to ensure that the activities that give rise to a finding of domination do not transpire either through traditional corporate means or, if necessary, by judicial intervention.²⁰⁹

Despite a member's potential breach of this fiduciary duty leading to a reverse piercing claim, permitting a shareholder's loss of capital in these instances could have negative effects on investment in small companies. Given the importance of such investments and the reality that not all investors with power will utilize it, any exercise in reverse piercing need take adequate measures to protect shareholders. The best way to protect the interests of both the shareholders and plaintiffs would be to permit a capital exemption for innocent shareholders when the enforcement of a judgment would liquidate the alter ego corporation. This would allow reimbursement to shareholders of their initial investment.

To prevent fraud amongst family and close friends, the first step is to determine whether a shareholder is innocent. A shareholder would be innocent if they did not benefit directly from the fraud. A shareholder benefits directly when they

²⁰⁷ See Illig, *supra* note 206 (explaining that all investors are in a position to negotiate for power, though some investors accept lower purchase prices in exchange for limited power).

²⁰⁸ Wilkes v. Springside Nursing Home, Inc., 353 N.E.2d 657, 661 (Mass. 1976) (quoting Cardullo v. Landau, 105 N.E.2d 843, 845 (Mass. 1952) (internal quotation marks omitted)).

²⁰⁹ See *id.* at 663; see also Smith v. Atl. Props., Inc., 422 N.E.2d 798, 803 n.9 (Mass. 1981) ("The majority may not exercise their corporate powers in a manner which is clearly intended to be and is in fact inimical to the corporate interest . . .") (quoting J.A.C. Hetherington, *The Minority's Duty of Loyalty in Close Corporations*, 1972 DUKE L.J. 921, 946 (internal quotation marks omitted)).

receive some financial benefit because of the fraudulent arrangement.²¹⁰ Courts in their power could look to additional factors to determine a shareholder's innocence.

Once a shareholder is deemed innocent, they 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. The capital exemption would only be triggered when a plaintiff's claim would drain the corporation of all its assets. While permitting some recovery, the capital exemption, by potentially depriving a shareholder of revenue, dividends, and disbursements, encourages shareholders to protect themselves by taking active roles in the oversight of the corporations in which they invest in and by bargaining for more power to protect such interests.

To illustrate the capital exemption theory, it will be applied to two versions of the Lady X hypothetical.²¹¹ X Corp. only has \$1,500 in liquid assets—only one one-hundredth of the judgment owed to JC. Thus, JC would have to attach assets belonging to X Corp. in order to satisfy his \$150,000 judgment. JC could attach both the car and the condominium belonging to X Corp. If these two assets totaled \$170,000, JC would be able to satisfy his judgment and X Corp. would still have all of its inventory and equipment, plus \$20,000 resulting from the sale of the assets. As the purchase of these assets, were in and of themselves an abuse of the corporate form, their sale would not adversely affect X Corp., as would the sale of inventory or company equipment, which are necessary to its continued operation.²¹² Furthermore, X Corp. would still have more than enough value remaining²¹³ to

²¹⁰ For example, suppose a boyfriend "invests" \$10,000 in his live-in girlfriend's corporation. The girlfriend has no money of her own, but uses her corporation to pay all their expenses. If a plaintiff attempted to reverse pierce the girlfriend's corporation, the boyfriend would not be eligible for the capital exemption as he prospered from the misuse of the corporation.

²¹¹ This Section will only discuss the ramifications for X Corp.'s two shareholders, friend, and brother; for a discussion on issues concerning X Corp. creditors see *infra* Part III.B.3.

²¹² Arguably, the sale of these assets could actually benefit the corporation because Lady has been using corporate funds to pay for her personal expenses, including those related to these personal items belonging to the corporation.

²¹³ X Corp. would still have \$3,000 in inventory, two computers worth \$4,000, and \$21,500 in cash—including the \$1,500 previously in the bank and the proceeds from the sale.

cover both Friend and Brother's initial \$5,000 investments, to cover the loans from Banks One and Two, and to continue with business as usual.

Suppose, however, sale of the car and condo only totaled \$125,000 in sales. That amount would be insufficient to satisfy JC's judgment—even after adding the remaining assets²¹⁴—thus requiring him to attach other assets belonging to the corporation. Following sale of the assets, JC would not receive the entire \$133,500. Friend and Brother would first be entitled to a return of their initial \$5,000 investments. JC may try to argue that Friend and Brother benefitted from the fraud because of their relationship to Lady, but that would require a showing of some financial gain as a result of the abuse of the corporate form, not present on these facts. Absent such a showing, JC would not be able to prevent Friend and Brother from recovering their initial investments. The remaining \$123,500 would be divided amongst JC, Bank One, and Bank Two.

3. Corporate Creditors

In rejecting reverse piercing, courts cite a voluntary judgment creditor's ability to protect itself as contributing to the doctrine's redundancy.²¹⁵ The rationale is that voluntary creditors, by definition, have chosen to deal with the individual defendant and thus have some ability to protect themselves.²¹⁶ Thus, they argue that a distinction should be made between tort and contract judgment creditors. While this rationale is valid, such logic ignores the fact that *all* voluntary creditors have that ability to protect themselves, be it a creditor of the individual or of the corporation. Because not all creditors sufficiently insulate themselves in the event of a breach, there are well-established laws governing the rights of such creditors, and it is these laws that should govern in reverse piercing cases. This Subsection first discusses the various risks all creditors face and the means

²¹⁴ The only remaining assets are the inventory, the bank account, and the two computers, which, when combined, only amount to \$8,500.

²¹⁵ See, e.g., *Cascade Energy & Metals Corp. v. Banks*, 896 F.2d 1557, 1577 (10th Cir. 1990) (“[T]he analysis of corporate veil issues is different in a consensual transaction . . . than in a nonconsensual transaction . . .”).

²¹⁶ See *id.*

in which such creditors can protect their interests. It will then look to pre-existing creditor and bankruptcy laws and apply those laws to the Lady X hypothetical.

Much is made of the chilling effect that would ensue were a corporate creditor to be superseded by a judgment creditor, yet, this is exactly what already happens.²¹⁷ Unsecured creditors²¹⁸ face a variety of risks, including those of judgment creditors of the corporation itself and even some creditors of an individual shareholder.²¹⁹ In spite of that ever-present risk, creditors continue to lend to small businesses. Accordingly, considering that loans to closely held corporations are made despite the nearly infinite grounds upon which a corporation could face its own action, it cannot then be said that the risk of judgment against a corporation, stemming from an action against an individual, would deter loans to closely held corporations. Furthermore, unsecured creditors already face some risks from reverse piercing by the IRS, as the doctrine has widespread acceptance in federal tax cases.²²⁰

Unsecured corporate creditors also face risks should the corporation declare bankruptcy. Debts owed to unsecured creditors are secondary to those of secured creditors.²²¹ It is only after all secured debts are settled that unsecured creditors are entitled to the corporation's remaining assets on a pro rata basis.²²² In most instances, the remaining unsecured creditors do not receive full payment from the debtor's estate. Furthermore, bankruptcy law exposes a creditor to the exact same risks as reverse piercing—a corporation being held liable for the actions of an individual shareholder—through a process known as substantive consolidation. Substantive consolidation has been

²¹⁷ See U.C.C. § 9-317(a)(2) (2010).

²¹⁸ Unsecured creditors are those creditors who have not taken out a lien or other security interest in a debtor's assets as collateral in the event of a breach. See BLACK'S LAW DICTIONARY 425 (9th ed. 2009). Transactions involving security agreements are governed by U.C.C. Article 9. See generally U.C.C. § 9-101 (2011).

²¹⁹ See *United States v. Scherping*, 187 F.3d 796, 803 (8th Cir. 1999); see also Timothy E. Graulich, *Substantive Consolidation—A Post-Modern Trend*, 14 AM. BANKR. INST. L. REV. 527, 538 n.50 (2006) (citing Douglas G. Baird, *Substantive Consolidation Today*, 47 B.C. L. REV. 5, 11 (2005)).

²²⁰ See, e.g., *Scherping*, 187 F.3d at 803 (“[R]everse piercing is a well-established theory in the federal tax realm.”)

²²¹ See U.C.C. § 9-317(a); see also 11 U.S.C. § 546(b)(1) (2006).

²²² 11 U.S.C.A. § 726(b) (West 2011).

described as the "federal analogue of veil-piercing."²²³ This bankruptcy practice pools together the assets of multiple entities and permits creditors to recover their ratable share from the combined assets.²²⁴

The risks reverse piercing poses to corporate creditors are not unique to that remedy. All voluntary creditors, be they of the individual or the corporation, have the opportunity to protect themselves from other creditors. If an individual's creditor is able to reverse pierce, it necessarily means the corporate form is being used to procure a fraud. To permit recovery to those creditors dealing with the corporation who fail to protect themselves over those who work with a fraudulent individual is unjust. An alter ego corporation is one that has been dominated to the extent that the corporation and the individual are essentially one entity;²²⁵ accordingly, their creditors should all be placed on equal footing.

Assume sale of all X Corp.'s assets, including the car and condominium, nets \$100,000. X Corp. cannot cover all of its outstanding debts, which total \$170,000. Bank One, which took a secured interest in X Corp.'s inventory would automatically receive the proceeds from the sale of the inventory—\$3,000—bringing the amount it is owed down to \$7,000.²²⁶ Deducting \$3,000 and Brother's and Friend's capital exemptions, X Corp. is left with \$87,000 to cover \$167,000 in debt. The court would distribute the remaining funds pro rata among the three creditors. This would result in JC receiving \$78,143 towards his claim, Bank One receiving an additional \$3,647, and Bank Two receiving \$5,210. Applying preexisting creditor priority laws ensures each creditor some return on the amount owed to it. These laws do not disturb the expectations of creditors because they are the very laws that govern all transactions entered into by creditors. Those creditors, like Bank One, who take measures to protect their interests are rewarded; Bank One received 66.5% of its original loan back compared to the approximately 52% received by other creditors—and had Bank One required additional collateral as security, it could have recovered up to the entire amount owed by X Corp.

²²³ See Graulich, *supra* note 219.

²²⁴ *Id.* at 528.

²²⁵ See *Gorsich v. Double B Trading Co.*, 893 P.2d 1357, 1362 (Colo. App. 1994).

²²⁶ For simplicity, inclusion of additional factors, like interest, is omitted.

CONCLUSION

“Fraud is infinite.”²²⁷ The law cannot rely solely on traditional remedies or it will find itself “perpetually eluded by new schemes” contrived by “the fertility of man’s invention.”²²⁸ The privilege of the corporate form need be used for “*legitimate* business purposes and must not be perverted.”²²⁹ By failing to permit reverse piercing, courts bless this perversion and deprive plaintiffs of a needed remedy, while simultaneously rewarding wrongdoers who shield their assets through corporate misuse. Traditional remedies are unable to combat the types of fraud that give rise to reverse piercing claims, and failure to adopt new remedies will lead to justice being “eluded by new schemes.”²³⁰ Courts, however, can protect the interests of all involved parties by permitting reverse piercing when (1) traditional remedies are inadequate (2) against both legal and equitable owners (3) with a capital investment exception for innocent shareholders, and (4) relying on preexisting creditor priority rules. These factors are not so overbearing as to enfeeble this remedy as occurred with the “equitable results” approach. Instead, this reverse piercing analysis provides meaningful and objective measures by which a court can assess the implications the doctrine would have on all parties and cater to each accordingly.

²²⁷ *Letter from Lord Hardwicke to Lord Kaimes* (June 30, 1759), quoted in 1 JOSEPH STORY, COMMENTARIES ON EQUITY JURISPRUDENCE AS ADMINISTERED IN ENGLAND AND AMERICA 262 n.1 (14th ed. 1918) [hereinafter *Lord Hardwicke Letter*].

²²⁸ *Id.*

²²⁹ *Postal Instant Press, Inc. v. Kaswa Corp.*, 77 Cal. Rptr. 3d 96, 102 (Ct. App. 2008) (emphasis added).

²³⁰ *Lord Hardwicke Letter*, *supra* note 227.

