**CORPORATIONS CAN PROVIDE LIMITED LIABILITY**

**BY: WILLIAM G. MORRIS, ESQ.**

Corporations with limited liability for shareholders were not favored in 18th-century England or the early United States. There was substantial concern for creditors and a belief that providing limited liability for shareholders of a corporation was somewhat unethical. As the 19th century evolved, experiments with limited liability in some states resulted in businesses moving to the states allowing shareholder protection. Over time, public policy recognized creditors could protect themselves if they understood they had to rely on the assets of the corporation to satisfy a debt and not the shareholders. The concurrent belief that allowing limited liability for shareholders would spur investment and economic growth helped make the concept of limited or no liability for shareholders of the corporation for corporate debts and liabilities the norm.

The result of this process is that shareholders in modern corporations are insulated from liability for corporate debts. The corporation is a separate legal entity from its owners and those dealing with the corporation must look to the corporation alone for payment. This same protection from liability applies to other limited liability entities such as limited liability companies. Personal assets of a shareholder or business owner are protected from claims of business creditors.

There are exceptions to protection from liability afforded by a corporation or other entity. A shareholder is liable if the shareholder physically injures someone by the shareholder’s own action. A shareholder can also be liable when the shareholder personally guarantees a corporate loan or other debt. And, the government can hold certain shareholder responsible for failure of the corporation to pay tax obligations.

Since states were originally reluctant to make corporate owners insulated from liability for corporate debt, it should not be surprising that when a corporation is used to defraud or injure, the protection can be lost. When an injured person attempts to go behind the corporate shell and hold a shareholder responsible, the process is known as piercing the corporate veil.

When an injured person can establish that a corporation was created or utilized to commit a fraud or cause harm to another for something different than a breach of contract or normal business, the injured person may be able to pierce the corporate veil against a shareholder or even an officer. But, public policy in Florida makes it difficult to get past the liability protection since that protection is the primary reason for incorporating in the first place. Those dealing with the corporation are supposed to understand the corporation is a separate legal entity and is the party responsible for its debts.

Although Florida court decisions confirm that equity will not allow a corporation to be used for improper conduct, the improper conduct has to be pretty bad to hold shareholders liable for a corporate obligation.

Florida cases set out three criteria to pierce the corporate veil. First, the shareholder must be in such control and domination that the corporation does not really have independent existence. Control of the corporation by a single shareholder, all by itself, is never going to be enough because the reason for incorporation is to protect the shareholder from liability. If the shareholder could be so easily reached, we would be back in the 18th century mindset that creditors must be protected and not limiting the liability of shareholders in a corporation. Second, the shareholder must abuse the corporate shell to try and avoid liability for some fraudulent or improper purpose. Third, the improper purpose or use harmed the plaintiff.

Control and domination of the corporation by a shareholder when used as a basis for piercing the corporate veil is often restated as the alter ego test. The alter ego test is the most frequently litigated issue. If the plaintiff cannot establish dominion and control, there is little hope of reaching the shareholder’s pocket.

The manner in which the shareholder conducts corporate businesses is often the shareholder’s downfall in trying to avoid liability. When the corporation bank accounts are used as personal bank accounts of the shareholder, the test can be met. How is that done? It can be established if the plaintiff can prove the corporation accounts pay the shareholder’s grocery bill, credit card, car payment and meals and that such expenses have no relationship to corporate business. Failure to hold corporate meetings, have corporate bylaws and maintain records of corporate activity are also evidence of alter ego status for the corporation.

Many plaintiffs think that if they can just prove the corporate shell is a sham, they will win and the shareholder will have to pay a judgment that could otherwise be only against the corporation. That is not the case, even though many Florida trial judges have agreed with plaintiffs in those cases. Florida’s Supreme Court confirmed something more is needed in the seminal case of *Dania Jai-alai Palace, Inc. v. Sykes*.

In the Sykes case, Sykes was a customer at Dania Jai-alai suing for injuries after she was crushed between 2 cars in the parking lot. She sued the corporation operating valet parking at the lot because the injuries were caused by its agent driving a car. She also sued Dania Jai-alai arguing that Dania owned the corporation operating the parking valet. Because Dania had complete ownership and control of the corporation operating valet parking, Sykes argue the corporation was the alter ego of Dania and Dania was liable for damages.

Florida’s Supreme Court explained that liability under the alter ego theory is not based on that alone. The corporation must have been used to commit some wrongful act which equity would not allow to go unpunished. In the case of injury to Sykes caused by negligent operation of a motor vehicle by a parking valet, no such wrongdoing existed and Dania was not liable.

Piercing the corporate veil in Florida can be done, but it is very difficult. Bad business practices alone are not going to be enough wrongdoing to open the door. In most cases, investors relying on the structure of the limited liability entity to protect them from judgments find that reliance well-placed.

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