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

By Nicholas 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 by 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]

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 piercing is to achieve an equitable result.[7] "Traditional piercing"[8] jurisprudence is well established and, despite some differences in formulation, universally followed by American courts.

The practice of reverse piercing the corporate veil is less well 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 to recover debts owed by a corporation's owner from the corporation itself or to allow a third-party creditor 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] Nonetheless, the approaches taken in states that have 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. Conflicting interests mandate that any allowance of reverse piercing delicately balance the needs of all involved parties to protect adequately all those involved.

This article 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 equal justice. Because of the competing interests reverse piercing implicates, this article 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 would be permitted a capital exemption prior to payment of the plaintiff's claim when that claim would liquidate the corporation. Finally, disputes amongst creditors should be dealt with using preexisting priority laws. Part I will discuss both traditional and outside reverse veil piercing. Part II will discuss the arguments for and against the various methods of outside reverse piercing through a case law analysis. Finally, Part III will advance 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.

I. Overview of Veil Piercing: Traditional and Reverse

Because reverse piercing is a variation of traditional veil piercing, Part I begins by detailing traditional veil 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 among the 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) that such domination was used to commit a fraud or wrong against the plaintiff.[21] Although some states purport to have three elements to allow a plaintiff to pierce the veil, the third being a causation or equitable results prong, the analysis is nearly identical.[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 must circumvent legitimate corporate purposes, so as to make the corporation a mere "alter ego."[26] States are split as to who may dominate a corporation, although 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 article only addresses reverse piercing in the context of a closely held corporation.

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 adherence to the corporation's separate existence would further a 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 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: inside[41] and outside—depending on the relationship of the party attempting to pierce the corporate veil.[42] The two types of reverse piercing implicate different interests and diverse policy concerns. To permit a comprehensive analysis, this article will only address outside reverse piercing.

i. Outside Reverse Piercing[43]

In an outside reverse piercing claim, the plaintiff, an "outside" third party, seeks to pierce the corporate veil to impose liability on the corporation 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 piercing[48] first arose in the landmark case[49] of *Kingston Dry Dock Co. v. Lake Champlain Transportation Co.*,[50] decided by Judge Learned Hand. In *Kingston Dry Dock*, 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 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 reverse piercing, holding that, 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] 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* furthered the acceptability of reverse piercing by holding the government's inability to satisfy legitimate tax debts provides a "sound basis" for reverse piercing of 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

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

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

Courts have taken two approaches to reverse piercing. This article will refer to the first 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 carry over the requirements of traditional veil piercing, this approach imposes additional requirements to better protect the diverse interests implicated by reverse piercing.

A hypothetical will be used, along with case law, to allow for an "apples to apples" comparison between various theories and remedies while highlighting their nuances. The hypothetical is as follows: Lady *X* (Lady) wants to form Corporation *X* (X Corp.), a wholesale health supplement distribution company. She needs $35,000 in startup funds. 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, each for $10,000. 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-Corp., and assumes the role of president. Lady does not receive any shares—those are instead split 50-50 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 the company, which does have several monthly retail customers. Lady purchases a new car and condominium in the corporation's name, although they are solely for her personal use. She also uses the corporation's revenue to pay all of her personal expenses. Despite her "arduous" labor 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 of X Corp. X Corp. has $3,000 in inventory, the condominium and car Lady purchased, two computers—worth $4,000—and $1,500 in a bank account.[72]

i. 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.[73] 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.[74] These cases 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.'"[75] The status as a separate entity granted to corporations was introduced to subserve the ends of justice, not subvert them.[76] 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."[77] As discussed previously, "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.[78] 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.[79] To avoid imposing this insurmountable bur-

den on plaintiffs, courts have adopted a lesser standard of control based on the same factors considered in traditional piercing cases.[80]

Certain factors relevant in analyzing traditional veil 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 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.[81]

To better understand the implications of the inverse method of reverse piercing, consider the doctrine 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 her 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,[82] because if Lady "was not deterred by the fact that [s]he did not hold all of the stock…why should h[er] creditors be?"[83]

ii. The "Equitable Results" Approach[84]

The Colorado Supreme Court directly confronted the often-cited downsides to reverse piercing[85] and acknowledged that when "inartfully performed," reverse piercing can negatively impact innocent third parties.[86] 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 corporate creditors alike. This effort swung the pendulum too far in the opposite direction; however, 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.[87] The Lady X hypothetical reaffirms that assertion, as this method would prevent JC from recovering. This section will first analyze the additional factor imposed by this method and then survey 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."[88] The court defined "equitable result[s]" to mean that neither innocent shareholders nor corporate creditors would be prejudiced by allowing reverse piercing.[89] This requires an analysis to assess the availability of other, less intrusive remedies, and discourages reverse piercing when such remedies are viable alternatives.[90] In *In re Phillips*, 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.[91] Similarly, reverse piercing did not injure innocent shareholders, as the individual defendant owned the corporation outright.[92] 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 *In re Phillips*, there have been just four reverse piercing cases in Colorado. These cases have failed to contribute objective methodology to the lip service *In re Phillips* paid to equitable results. The subsequent cases forgo the in-depth analysis necessary to obtain "equitable results," opting instead for a mechanical application of the elements.[93] The first case, *Stimpson v. Goldberg*,[94] misinterpreted the third prong of the reverse piercing test, finding the defendant's ability to move assets beyond the plaintiff's reach "manifestly inequitable and unfair" in satisfaction of the third prong.[95] Two years later, in *GRY Partners LLP v. Tabernash Meadows Water and Sanitation District*,[96] 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.[97] This holding begged the question of whether a capital investment would have prevented plaintiff from reverse piercing the corporation.

The last of the *In re Phillips* progeny, *Shem, LLC v. Buhler*,[98] provides an answer to the question posed by *GRY Partners*.[99] Here, the plaintiff attempted to reverse pierce all of the corporations in which the individual defendant was involved, but succeeded only on those that the defendant wholly owned.[100] 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 X—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., although *Shem* seems to mandate that she cannot. The fact that she does not own any shares would prevent a finding of domination.[101] Assuming, *arguendo*, that she could be found to dominate the corporation, the question then turns on whether Brother and Friend's investments would serve as a bar to reverse piercing, a question unanswered in *GRY*. The court could respond to Brother's and Friend's capital investment in one of three ways: it could (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.[102]

Thus, the "equitable results" approach fails to achieve equity. 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 only the facts of each individual case will 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 for Supporting Courts' Rejection of Reverse Piercing

Rather than adopt either the inverse or equitable results method, many courts simply reject reverse piercing.[103] These courts cite several common objections. First, they say reverse piercing violates normal judgment collection procedures.[104] Second, courts point out the potential harm reverse piercing could bring to both innocent shareholders and corporate creditors.[105] 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.[106] Fourth, courts refuse to lessen the "domination" standard adopted in *FMC Finance Corp. v. Murphee*,[107] instead agreeing with Judge Hand that "outside reverse piercing is only appropriate in the rare case of a subsidiary dominating its parent."[108] Finally, several courts have expressed added disdain for reverse piercing when the plaintiff is a voluntary contract creditor as opposed to an involuntary tort creditor.[109]

Normal judgment collection procedures permit a judgment creditor to attach an individual defendant's stock in a corporation.[110] Reverse piercing, however, allows an individual to skip this step by levying directly against the corporation's assets.[111] 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.[112] 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.[113] These arguments, taken to the extreme, lead 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 credit.[114] While the equitable results approach takes account of these interests, this approach was discredited by a California court as creating requirements that "essentially eliminate the outside reverse piercing doctrine as a practical matter."[115]

Courts further contend that reverse piercing and its associated risks are unnecessary given the availability of alternative, more traditional, remedies.[116] The alternatives put forth include conversion, fraudulent conveyance, respondeat superior, and conventional agency law.[117] With such a wide gamut of remedies already available, courts insist there is no need to "invent" a new theory of liability.[118]

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.[119] Agreeing with Judge Hand, they argue that the nature of the parent-subsidiary 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.[120] 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.[121] Indeed, Judge Hand's labeling such an instance as this "extremely rare" seems correct.[122] If courts apply this standard, most, if not all, reverse piercing claims would be denied.[123]

Lastly, several courts that have considered reverse piercing also criticize a doctrine that would permit voluntary creditors of an individual, or corporation, to recover from another corporation.[124] At a minimum, courts suggest a distinction between voluntary and involuntary creditors given the distinct public policy issues each raises.[125] Judge Hand articulated this fear in *Kingston Dry Dock*, 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."[126] 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.[127]

III. The Need for Reverse Piercing: How a Hybrid Approach Can Protect the Interests of All Parties

When reverse piercing is "inartfully performed," its disadvantages—such as injuries to innocent shareholders and corporate creditors—easily outweigh the benefits, allowing a judgment creditor to recover.[128] 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.[129] Part III first provides a brief overview of oft-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.

A. The Inadequacy of Alternative Remedies

i. Fraudulent Conveyance

Courts often cite fraudulent conveyance law as an adequate alternative to reverse piercing. While this may suffice in many situations, there are instances where fraudulent conveyance law 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 law to the Lady *X* hypothetical brings this shortcoming to the forefront, as fraudulent conveyance law will prove useless to JC.[130] This section will discuss the scope and requirements of fraudulent transfer law, before applying it to the Lady *X* hypothetical. The remedy will then be applied to *Postal Instant Press* to show that, despite the court's assertion, fraudulent conveyance law is not an adequate alternative to reverse piercing.

Fraudulent conveyance law has remained largely unchanged[131] for five hundred years[132] 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 conditions[133] are met.[134] To aid in determining "actual intent," the relevant statute lists eleven "badges of fraud."[135] Fraudulent conveyance law has a statute of limitations of four years—as proposed in the Uniform Fraudulent Transfer Act—although many states have either increased or decreased this statutory period.[136]

If proven, fraudulent conveyance law affords a plaintiff limited remedies. The primary remedy is avoidance of the fraudulent transfer.[137] Some states also permit attachment or other provisional remedies against the asset transferred.[138] Additionally, a plaintiff is entitled to the value of the asset transferred when a fraudulent transferee subsequently transfers the asset.[139] This right, however, is lost when the transferee, without knowledge of the fraud, purchases the asset for fair consideration.[140]

Applied to the Lady *X* hypo, fraudulent conveyance law provides JC with little help. Under fraudulent conveyance doctrine, 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, not transferred to it. Even though Lady uses them for her personal use, they are 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 Uniform Fraudulent Transfer Act § 4(a) (1), requiring JC to show actual intent.[141] 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.[142]

Even if deemed an insider, it is equally probable—and arguably more likely—that this badge of fraud will be found to be a valid investment in Lady's company—her first step down the road of entrepreneurship—not an illegal transfer. Her 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 threatened with a lawsuit. In that scenario, especially given Lady's retained use of the property to pay her expenses, 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, Inc. v. Kaswa Corp.*[143] shows that even in less "prototypical" reverse piercing cases, fraudulent conveyance alone can fall short of achieving equitable results.[144] In *Kaswa*, the defendant, Mr. Rangoonwala, purchased a Postal Instant Press (PIP) franchise from a third party.[145] PIP consented to the assignment and was a party to the agreement.[146] Following the purchase, Rangoonwala and a friend ran the franchise as general partners.[147] After several years of operating as partners, Rangoonwala created Kaswa Corp. for the sole purpose of operating the PIP franchise.[148] Thus, Kaswa, and not Rangoonwala, owned all the franchise assets.[149] Kaswa later merged with another company called The Print Works, but maintained the name Kaswa.[150] Upon being sued, Kaswa sold the assets to another company for fair value.[151] 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.[152] PIP attempted to add Kaswa as a judgment debtor under the theory of reverse piercing.[153] 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 fraudulent conveyance law.[154] An analysis, however, shows PIP would have likely been unable to recover using fraudulent conveyance law.

One way of showing fraudulent transfer would be to prove actual intent to hinder or defraud a creditor. There seems to be no problem 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 that 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 is that the transfer was to an insider as defined in the UFTA.[155] 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 that 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 (a) about to engage in a transaction with unreasonably small assets in relation to that transaction, or (b) that he intended to incur debts beyond his ability to pay. The first option is inapplicable here because 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 franchise payments to PIP, ultimately 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 Corp. 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 for reasonably equivalent value—it would have been entitled to Kaswa's accounts for the sale of the franchise assets. This argument, however, is moot 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, despite the court's assertion to the contrary, fraudulent conveyance law would not in fact serve as an alternative remedy for PIP. Reverse piercing offers PIP its only chance at justice.

As these examples illustrate, there are instances where fraudulent conveyance law 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 fraudulent conveyance law may be applicable, the limited remedies available can cause undue hardship on plaintiffs while potentially benefiting 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.

ii. 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 impractical, 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 the stock is valued, many closely held corporations place limitations on the alienability of the stock.[156] 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.[157] Many closely held alter ego corporations, however, never issue stock.[158] In fact, limited liability companies (LLCs) cannot issue stock at all—issuing instead membership interests.[159] Furthermore, even when a closely held alter ego corporation does issue stock, most do not pay dividends and avoid regular disbursements, opting instead to use the corporation's assets as a personal piggybank.[160] The absence of distributions negates any chance of recovering money 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.[161]

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.[162] 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.[163] Once a valuation is determined, courts must then determine the 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.[164] The reality of alter ego

corporations—with neglected formalities and commingled funds—only makes 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 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, no other corporations or LLCs can be shareholders.[165] Similarly, most LLCs do not permit transfer of membership interests absent approval from other members.[166] Owners can place additional restrictions on alienability through the Articles of Organization and the corporation's bylaws.[167] These restrictions can include qualifications and restrictions on the ownership of stock subject to a right to repurchase in the event of a violation.[168] Even if not an outright impediment, restrictions on alienability also lower the stock's marketability, and consequently the price.[169] 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 stock.[170]

The Lady *X* hypo 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.[171] 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 poring 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.

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.

iii. Agency and Respondeat Superior[172]

Agency generally "encompasses the legal consequences of consensual relationships."[173] 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."[174] 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.[175]

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* hypo, 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.

The facts of *Bennett v. Reynolds*[176] 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.[177] 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.[178] The individual defendant resided on property owned by the defendant corporation.[179] The individual defendant's conversion of the plaintiff's cattle also occurred on the corporation's land.[180] While the corporation itself did not raise cattle, the individual defendant did use the corporation's land for that purpose.[181] The individual defendant owned no part of the corporation—his daughters did— but defendant was the president and admitted that he "ma[d]e the decisions" and "r[a]n the ranch."[182] Plaintiff attempted to hold the corporation liable on a reverse piercing theory.[183] The court, however, held that because the individual defendant "used *corporate* authority over *corporate* employees, on *corporate* land, to convert cattle using *corporate* equipment," traditional agency principles were sufficient to hold the corporation liable for the conversion.[184]

Many times, however, the individual defendant's actions will not fall within the scope of corporate activity.[185] 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.[186]

iv. Conversion

Conversion is another oft-cited alternative to reverse piercing. The tort of conversion, however, has a very limited scope and is only effective in very specific factual situ-

ations, as is evidenced by its inapplicability to the Lady X hypothetical. This section will first discuss the elements of conversion, and 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 that other's right to control it that the actor may be required to pay the other the property's full value.[187] 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.[188] 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's taking it.

The square peg of conversion would be inapplicable to the "circle" of facts implicated by the Lady *X* hypothetical. Prior to the battery, 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.[189] The defendant knowingly took the plaintiff's cattle and sold them off at an auction.[190] Even there, however, the tort of conversion was insufficient for plaintiff to recover. Conversion allowed the plaintiff to impose liability on 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.[191] Thus, absent a way to attach corporate assets, the plaintiff's judgment for conversion against the individual defendant would have been meaningless.[192]

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. *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."[193] As Section III.A illustrates, there are instances where, despite blatant misuse of the corporate form, justice dies on the doorstep of the court.[194] In the name of judicial convenience, courts have adopted overly simplistic standards that overlook the interests of involved parties, or have adopted strict requirements, if any at all, that again fail to do justice to each litigant. 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, courts can safeguard the interests of all parties at the expense of none.

i. Ownership Requirement v. "Domination"

Ownership as a prerequisite to reverse piercing is easily circumvented, facilitating the practice of "judgment-proofing."[195] 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.[196] 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.[197] This protection of innocent shareholders, while necessary, can be achieved by much less restrictive means.[198] In attempting to get around their own judicially imposed requirement, courts have stretched the ownership requirement beyond reason.[199]

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. 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 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.[200] 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.

ii. Innocent Shareholders

Small businesses are an integral part of the national economy[201] and investment is the engine that runs small

business.[202] 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.[203] It is not uncommon for these investors to require ownership interest or a board position, or both, as a prerequisite to their investment.[204] No remedy for reverse piercing that failed to take the interests of the investor into account would be beneficial to society. This section proposes guidelines to first determine 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* hypo.

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.[205] 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.[206] 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.[207]

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 needs to 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, when the enforcement of a judgment would liquidate the alter ego corporation. This would allow reimbursement to shareholders of their initial investment, provided the shareholder did not directly benefit from the dominator's abuse of the corporate form.

A capital exemption would allow any shareholder to receive a return on his initial investment amount prior to any disbursement to the plaintiff, ensuring that he or she 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. Yet, by potentially depriving a shareholder of revenue, dividends, and disbursements, it encourages shareholders to protect themselves by taking an active role in the oversight of the corporation in which they invest and bargaining for more power to protect such interests. To prevent fraud amongst family and close friends, there would be an exemption for those instances where the shareholder benefits directly from the fraud. A shareholder benefits directly when he or she receives some financial benefit because of the fraudulent arrangement.[208]

To illustrate the capital exemption theory, it will be applied to two versions of the Lady *X* hypothetical.[209] 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 was in and of itself 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.[210] Furthermore, X Corp. would still have more than enough value remaining[211] to cover both Friend and Brother's initial $5,000 investments and the loans from Banks One and Two and continue with business as usual.

Suppose, however, that the sale of the car and condo only totaled $125,000. That amount would be insufficient to satisfy JC's judgment—even after adding the remaining assets[212]—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 and Banks One and Two.

iii. Corporate Creditors

In rejecting reverse piercing, courts cite a voluntary judgment creditor's ability to protect itself as contributing to the doctrine's redundancy.[213] The rationale is that voluntary creditors, by definition, have chosen to deal with the individual defendant and thus have some ability to protect themselves.[214] 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 section will first discuss the various risks all creditors face and the means by 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.[215] Unsecured creditors[216] face a variety of risks, including those

of judgment creditors of the corporation itself and even some creditors of an individual shareholder.[217] 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.[218]

Unsecured corporate creditors also face risks should the corporation declare bankruptcy. Debts owed to unsecured creditors are secondary to those of secured creditors.[219] 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.[220] 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 described as the "federal analogue of veil-piercing."[221] This bankruptcy practice pools together the assets of multiple entities and permits creditors to recover their ratable share from the combined assets.[222]

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;[223] accordingly, their creditors should all be placed on an equal footing.

Assume that the 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.[224] Deducting that amount, 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 these 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 the other creditors—and had Bank One required additional collateral as security, it could have recovered the entire amount owed it by X Corp.

Conclusion

"Fraud is infinite."[225] 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."[226] The privilege of the corporate form need be used for "*legitimate* business purposes and must not be perverted."[227] 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."[228] 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, courts protect the interests of all involved parties. These factors, as detailed, are not so overbearing as to enfeeble this remedy, which is what has occurred with the "equitable results" approach. Instead, this analysis provides meaningful and objective measures by which a court can assess all the implications and cater to each one accordingly.

Endnotes

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 (1929)).
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 Chicago v. F.C. Trebein Co., 52 N.E. 834, 837 (Ohio 1898) (courts have confined "the 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.").
6. Gorsich v. Double B Trading Co., 893 P.2d 1357, 1362 (Colo. App. 1994).
7. In re Phillips, 139 P.3d 639, 644 (Colo. 2006).
8. "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.

9. *See* W. Fletcher, Cyclopedia of the Law of Private Corporations, §41.70, at 458–59 (1983 & Supp. 1989).

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 article 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.*, *id.*; In re Phillips, 139 P.3d at 645; Goya Foods, Inc. v. Unanue-Casal, 982 F. Supp. 103, 108 (D.P.R. 1997).

12. *See, e.g.*, Postal Instant Press, Inc. v. Kaswa Corp., 162 Cal. App. 4th 1510, 1513 (Cal. Ct. App. 2008) (refusing to adopt reverse piercing); Acree v. McMahan, 585 S.E.2d 873, 874 (Ga. 2003) (rejecting reverse piercing); Transamerica Cash Reserve v. Dixie Power and Water, 789 P.2d 24, 26 (Utah 1990) (refusing to apply reverse piercing to current case, without directly rejecting doctrine); McIntyre v. Nice, 2001 WL 1708832, at *6 (Me. Super. Ct. May 17, 2001) (noting that the court has never recognized reverse piercing and has stated the weight of authority is against the doctrine).

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

14. *C.f.* In re Phillips, 129 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, 647 N.Y.S.2d 904, 908–10 (N.Y. Sup. Ct. 1995) (holding that New York only requires a showing that a corporation is the alter ego of the individual, and failure to disregard corporate entity would procure a fraud to plaintiff), *with* Towe Antique Ford Found. v. I.R.S., 999 F.2d 1387, 1390 (9th Cir. 1993) (holding that 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).

16. *See* Black's Law Dictionary (9th ed. 2009).

17. Anderson v. Abbott, 321 U.S. 349, 362 (1944).

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

19. *Id.*

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*, 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*, 647 N.Y.S.2d at 908–09. *See also* Sea-Land Servs., Inc. v. Pepper Source, 941 F.2d 519, 520 (7th Cir. 1991) (holding that in Illinois, there are two requirements 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.* (quoting Van Dorn Co. v. Future Chem. & Oil Corp., 753 F.2d 565, 569–70 (7th Cir. 1985))).

22. *See, e.g.*, In re Phillips, 139 P.3d 639, 646 (Colo. 2006) (stating that Colorado law requires that the insider and corporation be alter egos, that justice requires recognizing the substance of the relationship over the form because adherence to the corporate form would sanction a fraud, and that an inequitable result be achieved by piercing).

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

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

27. *See supra* text accompanying note 20.

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 alter ego. 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 any reverse piercing action against a publicly traded company would necessarily implicate innocent shareholders and should accordingly fail. All subsequent references to a corporation are to a closely held corporation, unless explicitly stated otherwise.

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 "arm's length," whether corporations are treated as independent profit centers, the 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 his or its own. *See id.* For additional factors courts have relied on, *see also* Associated Vendors, Inc. v. Oakland Meat Co., 26 Cal. Rptr. 806, 813–15 (Cal. Dist. Ct. App. 1963). *See also* Robert's Hawaii Sch. Bus, Inc. v. Laupahoehoe Transp. Co., Inc., 982 P.2d 853, 870–72 (Haw. 1999).

31. *See generally* Meshel v. Ohev Sholom Talmud Torah, 869 A.2d 343 (D.C. Cir. 2005); Fantazia Int'l Corp. v. CPL Furs NY, Inc., 67 N.Y.S.2d 28 (N.Y. App. Div. 2009).

32. *See* State v. Easton, 647 N.Y.S.2d 904, 908 (N.Y. Sup. Ct. 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, Inc. v. Catawba Dev. Corp., 689 S.E.2d 143, 147 (N.C. Ct. App. 2009).

37. Walk-In Med. Ctrs., Inc. v. Breuer Capital Corp., 778 F. Supp. 1116, 1123 (D. Colo. 1993) (citing Ward v. Cooper, 685 P.2d 1382, 1383 (Colo. App. 1984)).

38. *Shamrock*, 159 F. Supp. at 696 (internal quotation marks omitted).

39. *See* In re Phillips, 139 P.3d 639, 644 (Colo. 2006).

40. *See* State v. Easton, 647 N.Y.S.2d 904, 909 (N.Y. Sup. Ct. 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 of 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. W. Nat'l Mutual Ins. Co., 302 N.W.2d 350, 353 (Minn. 1981), which allowed a corporate insider to pierce the veil so that she could "stack" (redeem multiple insurance policies) six insurance policies, instead of receiving

the benefits of only one policy—the ability to "stack" was only available to the corporation itself. 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.*, 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 claim 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. In re 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….'" (quoting Schenley Distillers Corp. v. United States, 326 U.S. 432, 437 (1946))). For a more comprehensive analysis of inside reverse piercing, see Crespi, *supra* note 3, at 38–55.

42. *See* In re Phillips, 139 P.3d at 644–45.
43. Outsider reverse piercing is also referred to as "reverse alter ego." *See* Acree v. McMahan, 585 S.E.2d 873, 874 (Ga. 2003).
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 and Triangular Piercing of the Corporate Veil*, 223 N.Y.L.J 1 (2000). This is also referred to as triangular piercing because liability moves up, from one affiliate to the dominant individual, 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 (Cal. Ct. App. 2008) ("Perhaps the oldest reverse piercing case is *Kingston*….").
50. Kingston Dry Dock Co. v. Lake Champlain Transp. Co., 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." The first mention of the term "reverse pierce" came 45 years later in a Georgia case. *See* Kingston Dev. Co. v. Kenerly, 208 S.E.2d 118, 122 (Ga. Ct. App. 1974).
51. *Kingston Dry Dock*, 31 F.2d at 266.
52. *See id.*
53. *See id.*
54. *See id.*
55. *Id.* at 267.
56. *Id.*
57. W. G. Platts, Inc. v. Platts, 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.
65. *Id.* at 696 (emphasis added). Following *Shamrock*, reverse piercing claims became more frequent, albeit with mixed success. *See, e.g.*, Divco-Wayne Sales Financial Corp. v. Martin Motor Vehicle Sales, Inc., 195 N.E.2d 287 (Ill. 1963) (denying an outside reverse piercing claim); Olympic Capital Corp v. Newman, 276 F. Supp. 646 (C.D. Cal. 1967) (rejecting outside reverse piercing); Central 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* by 429 U.S. 338 (1977)).
67. *See id.* at 939.
68. Valley Finance, Inc. v. United States, 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. Accordingly, unless "inside" is specifically included, "reverse piercing" refers to outside reverse piercing.
71. Reverse piercing does necessitate some slight alterations to the traditional veil piercing methodology. *See infra* Part II(A)(i).
72. All subsequent applications of the "Lady *X* Hypothetical" will assume that the domination and fraud/injustice requirement have been satisfied to highlight the impact that subsequent conditions, or the lack thereof, have on the interests of shareholders, corporate creditors, and the judgment creditor.
73. While not exhaustive, states that have adopted the inverse method of piercing include New York, Connecticut, Nevada, Oregon, Virginia, Iowa Idaho, Wisconsin, Illinois, Texas, and Kentucky. *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. Partnership, 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 VA law precluded the remedy, but only because plaintiff failed to show corporation was in fact an alter ego of individual debtor)); Litchfield Asset Management Corp. v. Howell, 799 A.2d 298, 312 (Conn. App. Ct. 2002); Minich v. Gem State Developers, Inc., 591 P.2d 1078 (Idaho 1979) *rev'd in part on other grounds*; Crum v. Krol, 425 N.E.2d 1081 (Ill. 1981); Central Nat'l Bank & Trust Company of Des Moines v. Wagener, 183 N.W.2d 678 (Iowa 1971); Nutrition Rich Products v. Nutritional Resources, No. 99-CI-00483, 2003 WL 1339309 (Ky. App. Feb. 21, 2003); State v. Easton, 169 Misc. 2d 282, 647 N.Y.S.2d 904 (Sup. Ct. 1995); LFC Marketing Group, Inc. v. Loomis, 8 P.3d 841 (Nev. 2000); Amfac Foods v. Int'l Systems, 654 P.2d 1092 (Or. 1982); American Petroleum Exchange, Inc. v. Lord, 399 S.W.2d 213 (Tex. App.1966)); Olen v. Phelps, 546 N.W.2d 176 (Wis. 1996).
74. *See* Postal Instant Press v. Kaswa Corp., 162 Cal. App. 4th 1510, 1522 (Cal. Ct. App. 2008).
75. *Litchfield Asset Management Corp.*, 799 A.2d, at 312.
76. Shamrock Oil & Gas, Co. v. Ethridge, 159 F. Supp 693, 697 (D. Colo. 1958).
77. See *infra* Part II (A)(ii) for an alternative view on how to deal with domination in a reverse piercing context.
78. *See supra* notes 24–29 and accompanying text.
79. *See* FMC Finance 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.").
80. *See id.*
81. *See* Pac. Dev., Inc. v. United States, 1979 WL 1283, at *2 (D.D.C. Jan. 3, 1979).
82. Because Bank One secured its loan under Article 9, it would have priority over Lady's claim even under this approach.
83. Sea-Land Servs., Inc. v. Pepper Source, 941 F.2d 519, 521–22 (7th Cir. 1991).
84. This article 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 this method of reverse piercing from the inverse method.
85. For a detailed discussion of the criticisms of reverse piercing see *infra* Part II.B.

86. In re Phillips, 139 P.3d 639, 645 (Colo. 2006) (en banc).
87. As the subsequent application will reveal, JC would be unable to recover from Lady X under this method.
88. *See Phillips*, 139 P.3d at 641. The requirement that an equitable result be achieved also exists in traditional veil piercing cases. Previously, however, this requirement was routinely incorporated into the second prong requiring a showing of fraud or injustice.
89. *See id.* at 646.
90. *See id.* at 647.
91. *See id.* at 646.
92. *See* In re Phillips, 139 P.3d at 646.
93. The most recent case, Carreras v. Lemon, No. 07-cv-00739-MSK-KMT, 2008 WL 3895527, at *2 (D. Colo. Aug. 22, 2008) dismisses a plaintiff's claim for reverse piercing for failure to provide any factual basis, as to any of the three elements, to entitle plaintiff to relief.
94. No. 2004CV1563, 2006 WL 3949633 (Colo. Dist. Ct. Nov. 8, 2006).
95. *Id.* at *10.
96. No. 2006CV220, 2008 WL 5597587 (Colo. Dist. Ct. June 12, 2008).
97. *Id.* at *8.
98. No. 06 CV 687, 2008 WL 4532827 (Colo. Dist. Ct. June 27, 2008), *aff'd*, No. 08CA2138, 2009 WL 2810330 (Colo. App. Sept. 3, 2009).
99. *See id.* at *2–6.
100. *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 the plaintiff's interest in reverse piercing. *Id.*
101. 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.*
102. *See id.*
103. States that have expressly rejected reverse piercing include Georgia, Utah, and California. *See* Postal Instant Press v. Kaswa Corp., 77 Cal. Rptr. 3d 96, 102 (Cal. 2008); Acree v. McMahan, 585 S.E.2d 873, 874 (Ga. 2003); Transamerica Cash Reserve Inc. v. Dixie Power & Water, 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*, 789 P.2d 24); *see also* Floyd v. IRS, 151 F.3d 1295, 1298–1300 (10th Cir. 1998) (rejecting reverse piercing under Kansas law).
104. *See e.g.*, *Cascade Energy & Metals Corp.*, 896 F.2d at 1577. For a rejection of the arguments against veil piercing, see *infra* Part 3A.
105. *See, e.g.*, *Cascade*, 896 F.2d at 1577.
106. *See Floyd*, 151 F.3d at 1300.
107. 632 F.2d 413, 422 n.8 (5th Cir. 1980).
108. *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).
109. *See id.*
110. *See, e.g.*, *Cascade*, 896 F.2d at 1577.
111. *See id.*
112. *See id.*
113. *See id.*
114. *See* Acree v. McMahan, 585 S.E.2d 873, 874–75 (Ga. 2003).
115. *See* Postal Instant Press, Inc. v. Kaswa Corp., 77 Cal. Rptr. 3d 96, 106 (Cal. Ct. App. 2008).
116. *See, e.g.*, Floyd v. IRS, 151 F.3d 1295, 1300 (10th Cir. 1998).
117. *See, e.g.*, *id.*
118. *See id.*
119. *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)).
120. *See Kingston Dry Dock*, 31 F.2d at 267.
121. *See Floyd*, 151 F.3d at 1299.
122. *Kingston Dry Dock*, 31 F.2d at 267.
123. *See* Crespi, *supra* note 3, at 68.
124. *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 transaction, such as a breach of contract case, than in a nonconsensual transaction….").
125. *See id.*; *see also* Edwards v. Monogram Indus, 730 F.2d 977, 980–84 (5th Cir. 1984) (discussing the differences between tort and contract cases in the veil piercing context); Frank H. Easterbrook and Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. Chi. L. Rev. 89, 112 (1985) (discussing the economic reasons for making a tort/contract distinction when piercing the corporate veil).
126. *Kingston Dry Dock*, 31 F.2d at 267.
127. *See* Postal Instant Press v. Kaswa Corp., 77 Cal. Rptr. 3d 96, 105 (Cal. Ct. App. 2008); *see also Cascade*, 896 F.2d at 1577.
128. In re Phillips, 139 P.3d 639, 645 (Colo. 2006).
129. C.F. Trust, Inc. v. First Flight Ltd. P'ship, 140 F. Supp. 2d 628, 642 (E.D. Va. 2001).
130. For a description of the elements giving rise to fraudulent conveyance, *see infra* note 133 and accompanying text. *See also* Unif. Fradulent Transfer Act. § 4(a) (1984).
131. *See* BFP v. Resolution Trust Corp., 511 U.S. 531, 540–41 (1994).
132. The prototypical, and most oft-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. 76 Eng. Rep. 809, 811–14 (1601). 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.
133. The other conditions require that the debtor either (a) "was engaged or was about to engage in a business or transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction;" or (b) "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." U.F.T.A. §§ 4(a)(2)(i) & (ii) (1984).
134. U.F.T.A. § 4 (a) (1984). The UFTA has been adopted in 43 states and the District of Columbia.
135. *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 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 after a substantial debt was incurred; (11) the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor." U.F.T.A. § 4(b) (1984). These badges of fraud are not presumptions of fraud, but merely relevant evidence. *See id.* at § 4, Comment 5.

136. *See, e.g.* Fla. Stat. Ann. § 56.29(6)(a) (2005) (creating a one-year statute of limitations when a judgment has already been obtained); N.Y. C.P.L.R. § 213 (2004) (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. Regardless of the time frame, 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. Ct. 1995) (citing Fish v. East, 114 F.2d 177 (10th Cir. 1940)).

137. *See* U.F.T.A. § 7(a)(1) (1984). *See also id.* at Comment 2.

138. *See* U.F.T.A. § 7 Comment 2 (1984). 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 (1985).

139. U.F.T.A. § 8(b) (1984). The plaintiff is also entitled to any depreciation in value of the asset while in the possession of the fraudulent transferee. *See id.* at § 8(c).

140. *See* U.F.T.A. § 8(a).

141. JC must show there was a transfer to an insider made with "actual intent to hinder, delay, or defraud any creditor of the debtor." U.F.T.A. § 4(a)(1) (1984).

142. 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.

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

144. The facts of *Kaswa* also presented issues of harm to an innocent shareholder and a voluntary/involuntary distinction. While these factors should be considered in any reverse piercing effort, they are omitted from discussion in this section, which focuses solely on the adequacy of fraudulent conveyance law as a substitute remedy for reverse piercing. For a discussion of the voluntary/involuntary creditor distinction and the impact of innocent shareholders, see *infra* Part III(B)(i) and Part III(B)(ii), respectively.

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

146. *See id.*

147. *See id.*

148. *See id.* at 98–99.

149. *See id.*

150. *See id.* at 99.

151. *See id.*

152. *See id.* at 98–99.

153. *See id.* at 100, 101–02.

154. *See id.* at 105.

155. *See* U.F.T.A. § 1(7)(i)(D) (1984).

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

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

158. *See* Mix v. Plaza Redondo, Ltd., No. YC023339, 2002 WL 34239685 at *4 (Cal. Super. Ct. February 15, 2002).

159. Mark A. Sargent, *Are Limited Liability Company Interests Securities?*, 19 Pepp. L. Rev. 1069, 1095 (1992).

160. *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).

161. *See Litchfield Asset Mgmt. Corp,* 799 A.2d at 314.

162. Stanley J. Feldman, *Business Valuation 101: The Five Myths of Valuing a Private Business*, Score, www.score.org/article_business-valuation-101.html (last visited May 10, 2012). 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* IRS Business 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, 57 Rev. Ed. (2005). For an overview of these valuation approaches, *see id.* at 57–64.

163. *See* IRS 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. Valuators also need to consider intangible property, including everything from patents and software to customer lists and forecasts. *See id.*

164. *See* 22 A.L.R. Fed. 31 § 4.

165. *S Corporation vs. C Corporation: A Comparison,* Bizfilings, http://www.bizfilings.com/learn/s-corporation-vs-c-corporation.aspx (last visited May 10, 2012).

166. *LLC vs. S Corp: Which Business Type is Right for Me?*, Bizfilings, http://www.bizfilings.com/learn/llc-vs-s-corp.aspx (last visited May 10, 2012).

167. Edward D. Tarlow, *Creative Succession Planning for Managing and Owning the Family Business*, FindLaw, library.findlaw.com/1999/Aug/1/126127.html (last visited May 10, 2012).

168. *See id.*

169. Cook v. Commisioner of I.R.S., 349 F.3d 850, 856 (5th Cir. 2003).

170. *See* Estate of Jung v. Comm'r, 101 T.C. 412, 434 (1993); *See also* Trust Services 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).

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

172. Because respondeat superior is merely a specific type of agency, employer liability, this section will only refer to agency. *See* Restatement (Third) of Agency Intro ("The common law of agency in the United States encompasses the principle of respondeat superior…").

173. *Id.*

174. *Id.*

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

176. *Id.*

177. *See id.*

178. *Id.* at 869–71.

179. *Id.* at 871.

180. *Id.*

181. *See id.* at 869–70.

182. *See id.* at 898.

183. *See id.*

184. *Id.* at 885 (emphasis added).

185. *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. 2009); C.F. Trust, Inc. v. First Flight Ltd. P'ship (E.D. Va. 2001).

186. *See Fischer Inv. Capital, Inc.*, 689 S.E.2d at 151–52.

187. Restatement (Second) of Torts § 222(A)(1).

188. *See id.* at (A)(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.

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

190. *See id.*

191. *See id.* at 871–72, 896.

192. In this case, the court applied agency principles because defendant's business involved the raising of cattle. *See id.* at 896. Had defendant been involved in a different line of business, however, the only means by which plaintiff could have satisfied his judgment would have been through reverse piercing the corporate veil.

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

194. *See supra*, Part III.A.

195. 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).

196. *See, e.g.*, Shem, LLC v. Buhler, No. 06 CV 687, 2008 WL 4532827 (Colo. Dist. Ct. June 27, 2008) (denying plaintiff's reverse piercing claim because the individual defendant "[was] not the sole owner").

197. *See id.*

198. For a suggested approach to protecting innocent shareholders, *see infra*, Part III(B)(ii).

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

200. *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 County 1995).

201. Small businesses represent over ninety-nine percent of the nation's employers and over fifty percent of its private sector employment. *See* U.S. Small Business Administration, Office of Advocacy, Small Business Profile (Oct., 2009), *available at* www.sba.gov/advo/research/profiles/09us.pdf.

202. 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(B)(iii).

203. *See* U.S. Small Business Administration, Office of Advocacy, *Small Business Research Summary* (Sept., 2008), *available at* http://archive.sba.gov/advo/research/rs331.pdf; Entrepreneur, *Startup Financing*, http://www.entrepreneur.com/money/howtoguide/article52718.html (last visited July 4, 2011).

204. *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 Business Notes, http://www.smallbusinessnotes.com/financing/angelinvestors.html (last visited Jul. 10, 2011).

205. *See* Illig, *supra* note 204 (explaining all investors are in a position to negotiate for power, though some investors accept lower purchase prices in exchange for limited power).

206. Wilkes v. Springside Nursing Home, Inc., 353 N.E.2d 657, 661 (Mass. 1976) *quoting* Cardullo v. Landau, 105 N.E.2d 843 (Mass. 1952).

207. *See id.* at 663. *See also* Smith v. Atlantic Props., Inc., 422 N.E.2d 798, 803 fn.9 (Mass. Appeals Ct. 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 (1972).

208. 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.

209. This section will only discuss the ramifications for X Corp.'s two shareholders, Friend and Brother; for a discussion of issues concerning X Corp.'s creditors, see *infra* Part III(B)(iii).

210. 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.

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

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

213. *See, e.g.*, Cascade Energy & Metals Corp. v. Banks, 896 F.2d 1557, 1577 (10th Cir. 1990) ("The analysis of corporate veil issues is different in a consensual transaction…than in a nonconsensual transaction…").

214. *See id.*

215. *See* UCC 9-317(a)(2).

216. Unsecured creditors are those creditors who have not taken out a lien (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 UCC Article 9. *See generally* U.C.C. § 9-101 (2011).

217. *See* United States v. Scherping, 187 F.3d 796, 803 (8th Cir. 1999); *see also* Timothy E. Graulich, Thesis, *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).

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

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

220. 11 U.S.C.A. § 726(b) (West 2011).

221. *See* Graulich, *supra* note 217.

222. *Id.* at 527.

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

224. For simplicity, additional factors such as interest are omitted.

225. 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").

226. *Id.*

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

228. Lord Hardwicke Letter, *supra* note 225.

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