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Law Firm for Business

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Piercing the Corporate Veil – How to Avoid

Business owners can avoid the "piercing the corporate veil" by a creditor, or plaintiff in a lawsuit, and therefore avoid the adversary looking through to grab your personal assets for satisfaction of a liability:

1. *Form the Entity.* Form an entity to operate your business. (A corporation or LLC are equally protective. A partnership is not as protective).

2. *File State Annual Reports.* File the Secretary of State "annual report" each year in order to maintain active status of the business entity. File it on time, don't let it go dissolved by the state, for lapse of time after filing due date. If your entity goes dissolved by not filing the annual report, then you no longer have an entity. (It can be reinstated, but if a claimant files against you while there is no corp, then you are exposed personally)

3. *File Annual Tax Returns.*

4. *Avoid "Thin Capitalization".* Keep your business entity properly capitalized:

   a. Initially, and
   b. Continuously (to the extent possible on an ongoing basis).

   There is a concept of a "thinly capitalized entity", which claimants can say is not a real company because the business has no assets, no money, and no activity. Avoid the "thin capitalization" assertion, and keep some money in the company, and use it for an actual operating business.

   Current thinking is $1,000 to $2,500 capitalization required for the business (i.e. the amount that the founders invested into the business.)

5. *Observe Corporate Formalities*:
   a. Formation properly filed;
   b. Stock issuance properly documented, issued, and shares properly paid for (Keep copies of checks written to pay for shares. Keep stock records of ownership and issuance.);
   c. File State Annual Reports
   d. Prepare corporate minutes/resolutions at formation and for material changes & transactions. At least the initial minutes/resolutions are required.

6. *Separate Corporate Assets, Liabilities and Transactions*. Keep corporate assets/liabilities/transactions separated from personal, and from those of another entity. If you transfer to or from a personal account, or another business account, or if company pays personal expenses, then properly document in the company records the transactions, transfers and payments to or from those accounts, as loans, distributions or payroll checks.

7. *Sign Documents in Company Name Only.* Prepare and Sign company agreements, purchase contacts, vendor /supplier agreements, all services agreements, credit applications and all documents ….. Only in the full company name (not a dba). Never sign only in your personal name (always company name plus your name as officer).

   a. Fine to sign your personal name under the company name as officer (include your title), generally required.
   b. You may be required to provide a personal guarantee on a loan or a lease, which is a separate document or separate clause in a loan document, on which you will be required to sign our personal name. This is fine, if you can't negotiate it away. Not usually negotiable)

8. *Insurance.* Purchase proper insurance protection so that if a liability does occur, the insurance will cover much of it, and will not therefore emaciate the company's assets. And this will discourage a claimant from seeking your personal assets for satisfaction of claim, if company is uninsured.

9. *High Performance Standards.* Maintain high standards and levels of performance, competence, integrity, and due diligence on potential business associates, to avoid getting sued or into situations where liability might arise. Make good on your promises.

10. *Officers Authorized to Bind Company.* In corporate resolutions or minutes, authorize the officers to act for, and legally bind, the company, authorize only those officers or employees you want to act. This is a corporate record of no others permitted to bind the company.