

LLC's: How To Insure That They Protect You From Personal Liability

A. General Info

- It has long been recognized that a corporation is an entity distinct from its shareholders, even when it is owned by one person.
- Corporate shareholders and officers are generally insulated from personal liability for a corporations debts.
- This "shield" or "corporate veil" is one of the main benefits of creating a business entity.
- This "shield" is not absolute. The "shield" can be pierced.

B. Application to LLC's

- §183.0304 - Liability of LLC Members to Third Parties
 - "The debts, obligations and liabilities of a LLC shall whether arising from contract or tort, shall be solely the debts, obligations and liabilities of the LLC."
 - "A member or manager or a LLC is not personally liable for any debt, obligation or liability of the LLC **EXCEPT** that a member or manager may become personally liable by his or her acts or conduct other than as a member or manager."
 - Wisconsin appellate courts have not specifically addressed the issue of whether an LLC's veil can be pierced to impose personal liability.

C. Piercing the Corporate Veil or Disregarding the Corporate Fiction

- Limited liability will be disregarded and the corporate veil will be pierced when the business entity has no separate existence from the individual and if applying the corporate fiction would operate as a form of constructive fraud.
- Equitable remedy.
- Typical Situations:
 1. Member disguises personal assets as business entity's assets to induce a creditor to extend credit to or provide services or good to the entity assuming the entity has significant assets.
 2. Creditor or injured person attempt to hold the individual member personally liable for the entity because the entity was merely an alter ego of the individual.

- Must prove 3 prongs to prevail under the “alter ego doctrine” / “mere instrumentality” doctrine. *Consumer Co-Op of Walworth County v. Olsen*, 142 Wis.2d 465, 419 N.W.2d 211 (1988)

1. That the individual completely dominates the business practice such that the corporation has no separate mind, will, or existence of its own. Focus is on “control” not ownership.

Court looks at:

- a. The extent to which an entity follows the corporate formalities:
 - Held meetings
 - Maintained corporate records
 - Filed annual reports with the state
 - b. Siphoning of corporate funds by individuals
 - c. Non-payment of dividends
 - d. Co-mingling of corporate and personal funds
 - e. Non-functioning of other officers or directors
2. The individual used the control it had over the corporation to:
 - a. Commit fraud or wrong
 - b. To violate a statutory or other legal duty, or
 - c. To act dishonestly or unjustly

Key is to show that the control emanating from the corporate informality caused an injustice.

Factors to consider: Adequate capitalization

Was the corporation adequately capitalized when it was formed. Showing that a corporation was adequately capitalized at formation and then later became undercapitalized due to business losses will not suffice to pierce the corporate veil.

3. Creditor must show that it relied on a controlling shareholder’s financial misrepresentation — made to disguise undercapitalization – when creditor extended credit or good or services.

NOTE: It is not the presence or absence of any particular factor that is determinative. Rather, it is a combination of factors which, when taken together with an element of injustice or abuse of the corporate privilege, suggest that the corporate entity attacked had no separate mind, will or existence of its own and was therefore the mere instrumentality of tool of the shareholder. *Consumer Co-Op at 485.*

Drafted by:

Tristan R. Pettit, Esq.
Petrie & Stocking S.C.
111 E. Wisconsin Ave.
Suite 1500
Milwaukee, WI 53202
(414) 276-2850
Email: tpettit@petriestocking.com
Blog: www.LandlordTenantLawBlog.com