EMPIRICAL STUDY

PIERCING THE MIST: BRINGING THE THOMPSON STUDY INTO THE 1990S

I. INTRODUCTION

Piercing the corporate veil is the single most litigated issue in all of corporate law.[1] However, little empirical research has examined when and under what circumstances courts pierce the corporate veil since Professor Robert Thompson's groundbreaking study in 1991, which considered cases decided prior to 1986.[2] As a result, we have analyzed the cases between 1986 and 1995 using a methodology modeled on Professor Thompson's to determine how courts approached cases involving piercing the corporate veil during this period.

One of the central aspects of the corporate form is that the corporation represents a legal entity that exists separately from its shareholders and owners.[3] Under this principle, the obligations of the corporation are not imputed to the owners, directors, or shareholders of the corporation, and shareholders' losses are capped at the amount of their investments.[4] Limited liability plays an important role in minimizing agency costs and facilitating efficient investment decisions.[5] However, courts have established the doctrine of "piercing the corporate veil," which allows a corporate creditor to disregard the corporate entity and thereby hold a corporation's shareholders and owners personally liable for the obligations of the corporation under certain circumstances.[6]

1. Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036, 1036 (1991) (comparing the number of cases retrieved in Westlaw with a search for "piercing the corporate veil" versus the number of cases resulting from searches to retrieve cases on the topics of "hostile takeovers" and "fiduciary duties"). We replicated the searches performed by Professor Thompson, and the results showed a similar ratio of cases in each category to that identified by Professor Thompson.

2. *Id*. at 1044.

3. United States v. Bestfoods, 524 U.S. 51, 61 (1998) (citing Burnet v. Clark, 287 U.S. 410, 415 (1932)).

4. Radaszewski v. Telecom Corp., 981 F.2d 305, 306 (8th Cir. 1992); *see also* MODEL BUS. CORP. ACT § 6.22(a) (1979).

5. FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 41–44 (1991) (enumerating six benefits of limited liability); *see also infra* Part II.

6. *Bestfoods*, 524 U.S. at 62.

Commentators criticize the manner in which courts apply the piercing doctrine as utilizing conclusory terms, rather than a formal framework, resulting in results-based reasoning.[7] Early criticism can be seen in a 1926 opinion by then-New York Court of Appeals Judge Benjamin Cardozo in which he stated that the doctrine of piercing the corporate veil is "enveloped in the mists of metaphor."[8] Commentators continue to lament the failure of courts to discuss the policy rationales behind the use of specific piercing factors when determining whether to pierce the corporate veil.[9] Further, when courts do state specific piercing factors, commentators argue that courts merely construct a "template"[10] of factors enumerated in prior cases, which they do not apply in a consistent, rational manner.[11]

Despite the rampant criticism of the manner in which courts apply the piercing factors to reach their decisions, commentators over the years have tended to agree that courts ultimately reach the correct decisions.[12] Early commentators, such as Elvin Latty[13] and Adolf Berle,[14] recognized that although courts used results-based reasoning, the decisions reached in piercing cases were generally correct. Modern commentators also recognize that courts are consistently able to wade through the mist of piercing factors they employ to reach the proper decision.[15]

This Empirical Study examines the piercing doctrine case law between 1986 and 1995 to analyze how courts have applied the piercing factors in different contexts. Part II of the Study explains the legal framework of limited liability and the piercing doctrine. Part III explains the methodology employed. Part IV analyzes the empirical results of the Study with a focus on the areas examined by

7. Stephen M. Bainbridge, *Abolishing Veil Piercing*, 26 J. CORP. L. 479, 513 (2001) ("Judicial opinions in this area tend to open with vague generalities and close with conclusory statements with little or no concrete analysis in between. There simply are no are no [sic] bright-line rules for deciding when courts will pierce the corporate veil.").

8. Berkey v. Third Ave. Ry., 155 N.E. 58, 61 (N.Y. 1926) (stating that courts should look to specific factors, rather than using conclusory terms, such as "alias" or "dummy").

9. Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. REV. 89, 109 (1985); Franklin A. Gevurtz, *Piercing: An Attempt to Lift the Veil of Confusion Surrounding the Doctrine of Piercing the Corporate Veil*, 76 OR. L. REV. 853, 853–54 (1997).

10. Gevurtz, *supra* note 9, at 856.

11. *See* Easterbrook & Fischel, *supra* note 9, at 109; Daniel Cummins, Comment, *Disregarding the Corporate Entity: Contract Claims*, 28 OHIO ST. L.J. 441, 448–50 (1967) (stating that the same factors are generally present in cases when shareholders seek to pierce the corporate veil).

12. *See* Adolf A. Berle, Jr., *The Theory of Enterprise Entity*, 47 COLUM. L. REV. 343, 345 (1947); Easterbrook & Fischel, *supra* note 9, at 89 (arguing that economic analysis explains piercing decisions); Elvin R. Latty, *The Corporate Entity as a Solvent of Legal Problems*, 34 MICH. L. REV. 597, 630 (1936).

13. Latty, *supra* note 12.

14. Berle, *supra* note 12.

15. Easterbrook & Fischel, *supra* note 9.

Professor Thompson and the theories advanced by commentators. Finally, Part V provides several conclusions regarding the application of the piercing doctrine in different contexts.

II. THE LAW AND THEORY OF LIMITED LIABILITY AND PIERCING THE CORPORATE VEIL

The doctrine of limited liability, which holds that shareholders and owners of a corporation are not liable for corporate obligations, represents one of the most fundamental aspects of the corporate form.[16] A corollary to limited liability is the legal doctrine that a corporation enjoys an existence as a separate entity distinct from its shareholders and owners.[17] While American courts have not always recognized the doctrine of limited liability,[18] it is currently widely accepted in American jurisdictions.[19]

Judge Frank Easterbrook and Daniel Fischel have identified six rationales that support the use of limited liability to insulate the personal assets of shareholders and owners from the claims of corporate creditors. First, limited liability decreases the costs associated with monitoring agents of the corporation.[20] Since principals will generally not face personal liability based on the actions of corporate agents, principals can expend fewer corporate resources monitoring agents, thereby reducing the costs of operating the corporation.[21]

Second, limited liability also reduces the need to monitor other shareholders.[22] Limited liability reduces the costs of operating the corporation by insulating shareholders' personal assets from claims that arise as a result of the actions of fellow shareholders.[23]

Third, limited liability also promotes the free alienability of securities, thereby creating an incentive for corporate managers to act efficiently.[24] Corporate managers recognize that buyout firms can freely target corporations that are not performing as well as they should, providing an incentive for directors and officers to manage the corporation efficiently to avoid corporate takeovers.[25]

Fourth, limited liability promotes rational market valuation of a

16. United States v. Bestfoods, 524 U.S. 51, 61 (1998); *see also* MODEL BUS. CORP. ACT § 6.22(a) (1979).

17. *Bestfoods*, 524 U.S. at 61 (citing Burnet v. Clark, 287 U.S. 410, 415 (1932)).

18. Phillip I. Blumberg, *Limited Liability and Corporate Groups*, 11 J. CORP. L. 573, 587–90 (1986) (citing early American cases that held shareholders liable for corporate obligations).

19. *Id.* at 591–95 (stating that limited liability was the rule in most American jurisdictions by the middle of the nineteenth century).

20. EASTERBROOK & FISCHEL, *supra* note 5, at 41.

21. *Id.*

22. *Id.* at 42.

23. *Id.*

24. *Id.* at 42–43.

25. *Id.* at 43.

firm's securities.[26] By basing the valuation of securities on available information about a corporation's current performance and future prospects without reference to the wealth of the firm's shareholders, a rational market price may be established for each corporate security.[27]

Fifth, limited liability allows individual investors to diversify their investment portfolios.[28] Since limited liability protects the personal assets of individual investors, investors are able to invest in a diverse array of companies to minimize the risk of loss.[29]

Sixth, related to this rationale, Easterbrook and Fischel argue that the most important function of limited liability is to enable investors to invest in any project with a positive net value, without the risk of jeopardizing their personal assets, thereby allowing firms to raise capital for worthy projects.[30]

However, even given the strong rationales in support of limited liability, courts have created the equitable doctrine of piercing the corporate veil to allow corporate creditors to hold owners and shareholders personally liable for corporate obligations under limited circumstances.[31] As discussed in Part I, courts have never enunciated a clear test for when they will pierce the corporate veil.[32] Rather, courts have relied heavily on the context in which the corporate actions took place, leading commentators to develop theories that are context-specific.

One of the theories that developed prior to Professor Thompson's study was that the traditional justifications of limited liability would lead courts to pierce the corporate veil more frequently in cases where the plaintiff was a tort creditor than where the plaintiff was a contract creditor.[33] This theory posits that

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26. *Id.*

27. *Id.*

28. *Id.* at 44; *see also* Henry G. Manne, *Our Two Corporation Systems: Law and Economics*, 53 VA. L. REV. 259, 262 (1967) (arguing that publicly held corporations with a large number of small-scale investors could not exist without limited liability); Stephen B. Presser, *Thwarting the Killing of the Corporation: Limited Liability, Democracy, and Economics*, 87 NW. U. L. REV. 148, 171 (1992) (observing that individual investors would refuse to invest in stocks if they faced widespread personal liability).

29. EASTERBROOK & FISCHEL, *supra* note 5, at 44. *But see* Presser, *supra* note 28, at 153–54 (questioning the assumption of Easterbrook and Fischel that limited liability was created to allow investors, rather than small firms, to diversify).

30. EASTERBROOK & FISCHEL, *supra* note 5, at 44. *But see* Presser, *supra* note 28, at 163 (arguing that limited liability is best understood as a legal doctrine intended to benefit small-scale investors, rather than large, publicly held corporations).

31. Kaycee Land & Livestock v. Flahive, 46 P.3d 323, 326 (Wyo. 2002) (noting that piercing the corporate veil is a judicially created doctrine that evolved through the common law without a statutory counterpart).

32. *See supra* Part I.

33. *See, e.g.*, Easterbrook & Fischel, *supra* note 9, at 112.

contract creditors, such as lenders, voluntarily enter into transactions with corporations knowing that the entity's owners are protected by limited liability; contract creditors, therefore, are able to negotiate for protection from limited liability in the form of a risk premium.[34] Tort creditors, however, do not voluntarily interact with the corporation and therefore do not enjoy the same opportunity to negotiate for a risk premium.[35] However, Professor Thompson's research indicated that courts pierced the corporate veil more often in contract cases than in tort cases.[36]

While this finding was contrary to the general theory advanced by Easterbrook and Fischel, Professor Thompson noted that many of the contract cases in which the court pierced the corporate veil involved fraud or misrepresentation by the corporation.[37] Easterbrook and Fischel accounted for this and argued that courts should allow a corporate creditor to pierce the corporate veil where the corporation and its agents acted fraudulently because the creditor was never able to negotiate for an adequate risk premium to compensate for the fraudulent activity of the corporation.[38] However, Professor Thompson's data also indicated that courts pierced more frequently in the contract setting than in the tort setting in cases where the court did not find misrepresentation.[39] Thus, Professor Thompson's findings directly contradicted the theory espoused by Easterbrook and Fischel.[40]

Even given Professor Thompson's finding of more frequent piercing in the contract setting, two modern commentators have criticized the use of limited liability in the tort setting.[41] Henry Hansmann and Reinier Kraakman posit that limited liability is antithetical to the modern American tort system.[42] They argue that, by allowing the doctrine of limited liability to shield the personal assets of corporate managers, managers are given an incentive to engage in risky activities, and the costs of these risky ventures are externalized to the public, rather than being absorbed by the corporation creating the risk.[43] While the arguments of Professors Hansmann and Kraakman have not been adopted by many other

34. *Id.*
35. *Id.*
36. Thompson, *supra* note 1, at 1058.
37. *Id.* at 1059.
38. Easterbrook & Fischel, *supra* note 9, at 112.
39. Thompson, *supra* note 1, at 1069.
40. *Id.*
41. Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879, 1880–81 (1991) (arguing that limited liability should be abrogated for involuntary tort creditors and replaced with a system that subjects shareholders to personal liability for corporate obligations that exceed the firm's assets in a pro rata manner).
42. *Id.*
43. *Id.*

commentators,[44] their critique of the use of limited liability in the tort context highlights the reasoning behind Easterbrook and Fischel's argument that courts should pierce more frequently in the tort setting than in the contract setting.

Another issue regarding piercing the corporate veil is whether courts should pierce the corporate veil of a parent corporation to recover for the actions of a subsidiary. Phillip Blumberg challenges the application of limited liability in the parent-subsidiary context, arguing that the principal justification for limited liability—encouraging investors to provide capital for new business ventures—does not hold in this context.[45] In the parent-subsidiary context, the parent corporation is generally the sole shareholder, providing all of the capital investment for the subsidiary, and as such, Blumberg argues that limited liability serves no role in facilitating investment.[46] Blumberg argues that courts place too much emphasis on the rights of the corporation when they should focus on the duties of the corporation.[47] According to Blumberg, courts should look to the control, economic integration, administrative and financial interdependence, and use of a group persona to decide whether to hold corporate shareholders and owners liable, rather than applying a blanket of limited liability for parent corporations.[48]

Further, Professor Stephen Bainbridge argues that courts should apply enterprise liability in the parent-subsidiary context, instead of using a piercing theory.[49] Professor Bainbridge posits that enterprise liability analysis would allow courts to "acknowledge the important conceptual distinctions between holding an individual liable and holding a larger corporate enterprise liable."[50] Bainbridge argues that the main issue in the parent-subsidiary context is whether a parent has established a group of subsidiaries to externalize risks that the parent would otherwise be forced to absorb.[51] Thus, Professor Bainbridge would retain limited liability in the parent-subsidiary context, but he would allow corporate creditors of a subsidiary to collect against the parent corporation where the creditor could show that the parent formed the subsidiary solely to externalize risk.[52]

Finally, the law of piercing the corporate veil has largely

44. *See, e.g.*, JEFFREY D. BAUMAN, ELLIOTT J. WEISS, & ALAN R. PALMITER, CORPORATIONS: LAW AND POLICY: MATERIALS AND PROBLEMS 327 (5th ed. 2003).

45. Blumberg, *supra* note 18, at 574–75.

46. *Id.* at 624.

47. Phillip I. Blumberg, *The Corporate Entity in an Era of Multinational Corporations*, 15 DEL. J. CORP. L. 283, 328, 372 (1990).

48. *Id.* at 372.

49. Bainbridge, *supra* note 7, at 534 ("Analytical clarity would be furthered, however, by treating the allocation of liability within corporate groups as a variant of enterprise liability rather than as a species of veil piercing.").

50. *Id.*

51. *Id.*

52. *Id.*

evolved through the common law. While some statutes state that a shareholder may become liable for corporate obligations "by reason of his own acts or conduct," the statutes provide no guidance regarding how courts should apply the provisions.[53] The fact-specific inquiry in piercing cases does not lend itself to statutory codification, and commentators argue that codification of the piercing doctrine would enable corporate planners to structure transactions to avoid the reach of the statute in cases where the common law doctrine would hold the individuals personally liable.[54]

However, as Professor Thompson noted, the ad hoc judicial approach to piercing in no way diminishes the desire of corporate managers and lawyers to predict how courts will respond to piercing cases.[55] To that end, we seek to provide planners with more recent information on how courts decide whether to pierce the corporate veil.

III. METHODOLOGY

A. The Data Set

The cases used in this Study are a random sampling of cases reported in Westlaw from January 1, 1986 through December 31, 1995. Every case returned from a query on "pierc! /2 "corporate veil" was added in chronological order to a master list. From that list, every sixth case was analyzed. If the court did not return a decision on the piercing issue, the case was discarded. A total of 2901 cases were returned in the initial search, resulting in 483 cases analyzed. Of these 483 cases, 228 reached a decision on piercing the corporate veil.

Because our method was intended to mirror Professor Thompson's, we closely followed his methodology.[56] Thus, for each case analyzed, the following data was recorded: whether or not the veil was pierced, the year, the level of the court, the state, the number of shareholders in the corporation that was the object of the piercing, whether a person or an entity was behind the corporate veil, the identity of the party seeking the piercing, the substance of the claim, and whether or not the claim involved procedure.

For each case, we recorded instances of the more subjective factors that Professor Thompson noted courts used in their decisions of whether or not to pierce the corporate veil.[57] Although Professor

53. *See, e.g.*, MODEL BUS. CORP. ACT § 6.22(b) (1979).

54. *See* I. MAURICE WORMSER, DISREGARD OF THE CORPORATE FICTION AND ALLIED CORPORATION PROBLEMS 37–38 (1981) (arguing that it is impossible and preposterous to codify the piercing doctrine).

55. Thompson, *supra* note 1, at 1043.

56. *Id.* at 1044–45 (discussing the methodology).

57. *Id.*

Thompson's data-gathering form included eighty-five factors,[58] our data was funneled into only those eighteen categories for which Professor Thompson's study provided data: "instrumentality";[59] "alter ego";[60] "misrepresentation";[61] "agency";[62] "dummy";[63] "lack of substantive separation" and "intertwining";[64] "undercapitalization";[65] "informalities";[66] "domination and control";[67] and overlap in any of the following areas: officers, directors, owners, offices, business activities, employees, and management. Additionally, if the court noted the lack of any of these factors, this was recorded. In many cases, multiple factors were noted by the court as present or lacking, and this was recorded as well.

B. Methodology Questions

Even more so than Professor Thompson's study, this Study does not purport to create a record of every piercing case during the effective period.[68] Nor does it attempt to draw any conclusions about the numbers of cases in which piercing the corporate veil is litigated.

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58. *Id.* at 1044.

59. Unlike many of the other factors, this factor has no subset of characteristics for which opinions were analyzed. It was recorded only when the word was used specifically by the court. It is this conclusory nature of the "instrumentality" factor that has led to its criticism.

60. "Alter ego" and "dummy" were analyzed in the same manner as "instrumentality" and share many of its criticisms. *See supra* note 59.

61. "Misrepresentation" included misrepresentation as to the corporation's assets and financial condition, and misrepresentation as to the party responsible for payment. Professor Thompson notes that, while this activity is often referred to by the court as "fraud," many courts will find that the evidence supports a finding of "misrepresentation" where a common law claim of fraud could not be established. Thompson, *supra* note 1, at 1044 n.53.

62. This factor noted descriptions by the court of an agency relationship between the shareholder and the corporation.

63. *See supra* note 60.

64. Although Professor Thompson recorded the existence of these factors separately, they were combined for our study, as the difference between the two as explained by Thompson is minimal. *See* Thompson, *supra* note 1, at 1045 n.55. These factors were noted where there was commingling of corporate and private funds, siphoning of funds, or treatment by the shareholder of corporate funds as personal.

65. "Undercapitalization" was noted both when it was present at the corporation's inception and in cases where the corporation became undercapitalized later.

66. "Informalities" was used to track cases where the court noted the lack of corporate formalities such as formal board meetings, record keeping, or payment of dividends.

67. "Domination and control" was noted where the shareholder personally paid or guaranteed corporate debts or owned all the stock of a corporation, where the court noted that the corporation had no independent action, or simply where the shareholder "dominated" the corporation.

68. *See* Thompson, *supra* note 1, at 1046 (noting that results based on reported cases may not be a representative sample of all cases considered, filed, or decided).

The data set for this Study is limited in many respects. It only includes cases reported in Westlaw. Thus, it does not include any cases that were settled or cases that were unreported. It may include decisions of both the trial and appellate courts for the same case. These variables may or may not result in a selection bias that prevents the data set from being representative of the totality of piercing disputes.

Nevertheless, because these limitations are the same as those faced by Professor Thompson, comparisons between his data and ours are meaningful.

IV. EMPIRICAL RESULTS

A. Frequency Distributions

1. Initial Comparisons

Initial observations made by Professor Thompson are also accurate for our data set. In none of the cases did the court pierce the veil of a public corporation.[69] Thus, courts' protection of the separateness of public corporations from their shareholders and the limited liability provided by the corporate scheme remains absolute.

For our data set, courts pierced the corporate veil in 35.53% of cases. This value is considerably lower than Professor Thompson's figure of 40.18%.[70]

TABLE ONE: OVERALL PIERCING RESULTS

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's Result (% Piercing)
#	228	81	151	35.53	40.18

Professor Thompson found no trend over time, noting that while the percentage of cases where the veil was pierced varied from year to year, the value had stayed relatively constant over several prior decades.[71] Thus, Thompson concluded that there was no trend toward increasingly allowing the veil piercing.[72]

The data for 1986–1995 indicates the opposite. The data from year to year varied greatly in some instances, in both the number of cases reported and the percentage of piercing. However, a trend is visible when the data is viewed over larger periods of time. Because our data set is limited to ten years, a decade-by-decade analysis is not relevant. Instead, an average for each of the previous three

69. Professor Thompson found that courts pierced in none of the nine cases in his data set involving public corporations. *Id.* at 1047 n.71.

70. *Id.* at 1048 tbl.1.

71. *Id.* at 1048–49.

72. *Id.* at 1048.

years was calculated, showing an increasing reluctance of courts to pierce the corporate veil.

TABLE TWO: YEAR

Category	Total Cases	Pierce	No Pierce	% Pierce	Average Piercing % for Previous Three Years
1986	17	7	10	41.18	n/a
1987	19	10	9	52.63	n/a
1988	24	10	14	41.67	0.45
1989	29	10	19	34.48	0.42
1990	25	6	19	24.00	0.33
1991	22	11	11	50.00	0.36
1992	20	7	13	35.00	0.36
1993	26	6	20	23.08	0.35
1994	27	9	18	33.33	0.30
1995	19	5	14	26.32	0.28

Professor Thompson found that state courts pierced in similar but slightly lower percentages than federal courts.[73] Our results were more pronounced. Thus, although Thompson stated that his findings contradicted suggestions that federal courts were more willing to pierce the corporate veil, our findings support the theory that federal courts pierce the veil more often than state courts.[74]

TABLE THREE: JURISDICTION

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's Results
Federal Courts	141	54	87	38.30	41.42
State Courts	87	27	60	31.03	39.34

Professor Thompson found that state trial, appellate, and supreme courts all pierced in relatively the same percentage of cases.[75] Our results showed reductions from Thompson's findings with regards to the willingness to pierce in the trial and supreme courts.

73. *Id.* at 1049 tbl.3.

74. See *id.* at 1049 n.78 for articles arguing that federal courts are more willing than state courts to pierce the corporate veil.

75. *Id.* at 1049, 1050 tbl.4.

TABLE FOUR: COURT LEVEL

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's Results
Trial	119	41	78	34.45	40.15
Intermediate	92	36	56	39.13	39.30
Supreme	17	4	13	23.53	42.09

Professor Thompson's data revealed no significant difference between individual and corporate plaintiffs.[76] Our data revealed similar results.

TABLE FIVE: INDIVIDUAL VS. CORPORATE PLAINTIFFS

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's results
Individual	102	33	69	32.35	37.70
Corporate	101	34	67	33.66	36.81

2. Differences Based on Whether the Defendant Is a Corporation or an Individual

In general, courts pierce the corporate veil to reach individual defendants more often than corporate defendants. From 1986–1995, courts pierced to reach an individual defendant 44.36% of the time, while only piercing in 23.75% of the cases where the defendant was a corporation. Professor Thompson also found this general observation to be true, although his specific percentages varied in significant areas.[77]

76. *Id.* at 1050 tbl.5.
77. *See id.* at 1055 tbl.7.

TABLE SIX: DEFENDANT IDENTITY

Identity of Shareholder	**Total Cases**	**Pierce**	**No Pierce**	**% Pierce**	**Professor Thompson's Results**
Individuals:					
One	47	19	28	40.43	49.64
Two or Three	51	25	26	49.02	46.22
Closely Held, but More than Three	19	8	11	42.11	34.98
Public Shareholders	1	0	1	0.00	0
Total Individuals	*133*	*59*	*74*	*44.36*	*43.13*
Corporate:					
Parent	47	8	39	17.02	36.79
Subsidiary	6	2	4	33.33	27.94
Sibling	22	8	14	36.36	41.53
Total Corp	*80*	*19*	*61*	*23.75*	*37.21*

3. Differences Based on the Number and Identity of the Shareholder

Professor Thompson concluded that the number of shareholders made a difference in the likelihood of veil piercing.[78] His results evidenced a correlation between an increase in the number of shareholders and a decrease in piercing.[79] Our data does not support this trend. We found a piercing rate of 40% for corporations with one shareholder; for corporations with two or three shareholders, the percentage rose to 49%, but for corporations with three or more shareholders, the percentage dropped to 42%.

4. Differences Based on the Identity of a Corporate Defendant

The likelihood of success for a plaintiff seeking to pierce the corporate veil and reach a corporate defendant has declined in a majority of cases since 1986. Professor Thompson found a 37% piercing rate for corporate defendants.[80] From 1986 to 1995, that rate plummeted to less than 24%. Although the difference is negligible in those cases seeking to reach a subsidiary or sibling corporation, these are a minority of cases. The vast majority of cases attempt to reach a parent corporation. Here the percentage of cases in which the veil was pierced was only 17%, less than half the percentage noted by Thompson.[81]

78. *Id.* at 1054.
79. *Id.* at 1054–55.
80. *Id.* at 1055 tbl.7.
81. Professor Thompson found that the veil was pierced in 36.79% of the cases attempting to reach a parent corporation. *Id.*

5. Differences Based on the Identity of the Plaintiff

Although the plaintiff's identity as an individual or corporation had little effect on piercing results, the nature of the plaintiff's relationship to the defendant did make a difference. Government plaintiffs were easily the most successful, piercing in over 54% of cases. The next most successful group of plaintiffs were creditors, piercing in 40% of their cases. Noncreditors were less successful, with a success rate of only 31%. Professor Thompson found no significant difference between the piercing rates of creditors and noncreditors, piercing at 42% and 40% respectively.[82] Similar to Thompson,[83] we found a very low rate of piercing when the plaintiff was either the corporation itself or a shareholder.

TABLE SEVEN: PLAINTIFF IDENTITY

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's Results
Creditor	45	18	27	40.00	42.32
Noncreditor	147	46	101	31.29	40.27
Government	24	13	11	54.17	57.80
Corporate	8	1	7	12.50	13.41
Shareholder	2	0	2	0.00	25.42

6. Differences Based on the Substantive Context in Which the Claim Arose

Arguably the most controversial of Professor Thompson's findings is that courts pierced more often in contract cases than in tort cases.[84] The conventional wisdom at the time of Professor Thompson's study was that the involuntary nature of tort cases would lead to a higher percentage of piercing when compared to contractual disputes in which the plaintiffs had voluntarily chosen to deal with the corporation.[85] Professor Thompson found that courts pierced the corporate veil in almost 42% of contract cases, but only in less than 31% of tort cases, a difference he found to be statistically significant.[86]

From 1986–1995, there was no substantial difference between the success rate for piercing in contract cases versus tort cases. However, unlike Professor Thompson's results, our results show a

82. *Id.* at 1057 tbl.8.

83. Professor Thompson found that courts pierced 13.41% of the time when the plaintiff was the corporation itself, and 25.42% when the plaintiff was a shareholder. *Id.*

84. *Id.* at 1058.

85. *See id.* at 1058 n.118 and accompanying text.

86. *Id.* at 1058 tbl.9, 1058 n.116 and accompanying text.

higher piercing rate for tort cases than contract cases. Courts pierced the veil in 31.11% of contract cases and 35.71% of tort cases. Interestingly, the ratio of contract to tort disputes has also remained relatively consistent. Pre-1986, the ratio was 3.45:1; from 1986–1995, it was 3.21:1.[87]

Our cases revealed no criminal piercing cases. This finding is probably not significant, as in Professor Thompson's pre-1986 study, there were only 15 criminal cases out of a total of 1600 cases.[88] The rate of piercing in statute-based cases was consistent with pre-1986 data.[89]

TABLE EIGHT: CONTEXT OF CLAIM

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's Results
Contract	90	28	62	31.11	41.98
Tort	28	10	18	35.71	30.97
Criminal	0	0	0	0.00	66.67
Statute	94	38	56	40.43	40.58

7. Differences Based on Procedure

Procedural cases are those where a plaintiff is attempting to pierce the corporate veil so as to establish proper jurisdiction or venue with respect to the defendant. These cases have received different treatment than contract and tort cases, both from courts and from scholars.[90] Of those who have not dismissed procedural cases outright from the study of piercing the corporate veil, some have argued that courts are more lenient in the procedural context.[91] Professor Thompson's pre-1986 data does not support this view; he found that courts pierced the veil in 39% of procedural cases.[92] Post-1986 cases had an even lower piercing rate, with courts piercing only 28.5% of the time.

87. Professor Thompson's data revealed 779 contract cases and 226 tort cases. Our study found 90 and 27 respectively, which becomes 540 and 162 when the sample rate is extrapolated. *Id.* at 1058 tbl.9.

88. *Id.*

89. *See id.*

90. *Id.* at 1059–60.

91. *See id*. at 1060 n.127 and accompanying text.

92. Thompson found that courts pierced in 59 of 153 procedural cases. *Id.* at 1060 tbl.10.

TABLE NINE: PROCEDURAL CASES

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's Results
Jurisdiction	12	4	8	33.33	36.88
Venue	2	0	2	0.00	58.33

8. Differences Based on Statutory Claims

Courts are asked increasingly to pierce the corporate veil in the statutory context. Pre-1986, less than 35% of piercing cases were statutory; from 1986–1995, over 41% of piercing cases were statutory cases.[93] However, the piercing rate for statutory cases has remained constant at just over 40%. Combined with the overall drop in piercing percentage for total cases, this means that a 1986–1995 statutory plaintiff was more successful than the average piercing plaintiff, while pre-1986, there was no discernable difference in success rates.[94]

Plaintiffs' success rates also vary widely depending on the particular statute they seek to enforce. For example, bankruptcy plaintiffs from 1986–1995 were successful in over 46% of piercing cases. This rate is consistent with the pre-1986 rate of 47%.[95] Even more successful are plaintiffs seeking to pierce under environmental statutes. They were successful 60% of the time from 1986–1995. This is a reduction from the pre-1986 rate of 83.33%, but is still above the average.[96] The most successful plaintiffs between 1986 and 1995 were those who sought to pierce under fraud statutes. They were successful 100% of the time. This figure is comparable to the pre-1986 figure of 81.82% due to the small sample size.[97]

Among the least successful plaintiffs pre-1986 were those seeking to enforce a workers compensation or tax statute, prevailing in only 12.82% and 30.83% of cases, respectively.[98] Between 1986 and 1995, the success rate for workers compensation plaintiffs stayed relatively low at 25%. However, tax plaintiffs saw their success rate increase greatly to 71.43% during this time. The success rate for ERISA plaintiffs also varied from pre-1986 rates, dropping from 100% to 40%.[99] That this decrease in success was also

93. Pre-1986 data showed that 522 cases out of 1583 were statutory. *Id.* at 1048 tbl.1, 1061. The 1986–1995 data extrapolates to 564 out of 1368.

94. Pre-1986, the success rates for statutory and average plaintiffs were 40.58% and 40.18% respectively, compared with 40.43% and 35.53% for success rates from 1986–1995. *See id.* at 1048 tbl.1, 1058 tbl.9.

95. *Id.* at 1062 n.135.

96. *Id.*

97. Pre-1986, the veil was pierced in 9 of 11 cases, and from 1986–1995, the veil was pierced in 2 of 2 cases. *Id.*

98. *Id.*

99. Thompson found that courts pierced in 2 of 2 ERISA cases. *Id.*

accompanied by a large increase in the number of ERISA claimants seeking to pierce the veil may account for the difference.[100] The other group of plaintiffs whose success rate was lower than that of pre-1986 plaintiffs was those plaintiffs filing discrimination claims.[101]

By combining statutory piercing results with the occurrence of traditional piercing factors, Professor Thompson concluded that the importance of such factors as undercapitalization, informalities, and misrepresentation was lower in statutory cases than in contract cases.[102] From 1986–1995, undercapitalization was noted in almost 37% of statutory cases where the courts pierced the corporate veil. Courts piercing the veil in contract cases found undercapitalization to be a factor in almost 43% of cases. Unlike pre-1986 courts, which found informalities and misrepresentation in twice as many contract cases as statutory cases, there was no similar discrepancy in the number of contract cases and statutory cases in which the courts found misrepresentation and informalities from 1986–1995.[103]

TABLE TEN: STATUTORY CLAIMS

Category	Total Cases	Pierce	No Pierce	% Pierce	Professor Thompson's Results Pierce / No Pierce / Rate
Bankruptcy	28	13	15	46.43	16 / 18 / 47.06%
ERISA	20	8	12	40.00	2 / 0 / 100%
Environment	5	3	2	60.00	5 / 1 / 83.33%
Workers Comp.	4	1	3	25.00	5 / 34 / 12.82%
Tax	7	5	2	71.43	6 / 15 / 30.83%
Discrimination	4	0	4	0.00	5 / 2/ 71.43%
Fraud	2	2	0	100.00	9 / 2 / 81.82%
Patent	4	1	3	25.00	14 / 5 / 73.68%
Real Property	4	1	3	25.00	3 / 12 / 20.00%

100. Before 1986, ERISA claims made up 0.38% of all statutory claims (2 of 522) and only 0.13% of all piercing cases (2 of 1583). *Id.* From 1986 to 1995, ERISA claims comprised 21.28% of all statutory claims (20 of 94) and 8.77% of all piercing cases (20 of 228).

101. While pre-1986 discrimination plaintiffs enjoyed a 71.43% success rate (5 of 7), none of the four plaintiffs from the 1986–1995 data set were successful. *See id*.

102. *Id.* at 1062.

103. From 1986 to 1995, courts found "informalities" in 35.71% of contract cases and 36.84% of statutory cases. They also found "misrepresentation" in 25% of contract cases and 26.32% of statutory cases. Thompson's data shows that pre-1986 courts found "informalities" in 20.49% of contract cases and 11.16% of statutory cases, and "misrepresentation" in 29.97% of contract cases and 17.41% of statutory cases. *Id.* at 1062 n.137.

B. Reasons Given by the Courts

Courts continue to use a laundry list of factors in determining whether or not to pierce the corporate veil. As some critics of piercing jurisprudence have noted, some of the factors are conclusory while others do not correlate with a particular result.[104] The "indeterminacy of veil-piercing law" reflected in Professor Thompson's study is not refuted by the results culled from our data set.[105]

1. Initial Comparisons

Not surprisingly, two of the three factors most often associated with a piercing result were the two most often criticized as being conclusory: "instrumentality" (100%) and "alter ego" (97.5%).[106] These factors also had the highest piercing correlation in pre-1986 cases.[107] The only other factor whose mention correlated 100% with a piercing result was "misrepresentation."

Factors less associated with a piercing result were "intertwining" (89.36%), "undercapitalization" (89.19%), "agency" (87.5%), "dummy" (80%), "informalities" (79.41), and "domination and control" (75%). Of these factors, "undercapitalization," "informalities," and "domination and control" had substantially increased success over pre-1986 cases, while "dummy" and "agency" were less successful.[108]

Overlap between the shareholder and corporation was of less importance to courts, as courts pierced in only 53.6% of cases involving overlap. This is similar to the overall importance of overlap in pre-1986 cases, which resulted in piercing in 56.53% of cases.[109] Among the various forms of overlap, courts pierced most often where there was overlap of owners (78.95%), business activity (66.67%), and directors (53.13%). Courts pierced in exactly half of the cases where they found overlap of employees and offices. Less important were officers (45%) and management (33.33%). The largest variations in piercing rate among factors as compared to pre-1986 cases were: management, with a 31.79% decrease in

104. *See, e.g.*, Latty, *supra* note 12, at 625; Cummins, *supra* note 11, at 441.

105. Thompson, *supra* note 1, at 1063.

106. *Id.*; *see also* Robert Hamilton, *The Corporate Entity*, 49 TEX. L. REV. 979, 979 (1971).

107. Thompson found that courts pierced in 97.33% of cases where "instrumentality" was a factor and in 95.58% of cases where "alter ego" was a factor. *Id.* at 1063 tbl.11.

108. Correlation of "undercapitalization' increased from 73.33% to 89.19%, "informalities" from 66.89% to 79.41%, and "domination and control" from 56.99% to 75%, while "agency" decreased from 92.31% to 87.5% and "dummy" from 89.74% to 80%. *Id.* The drop in success for "agency" and "dummy" may be a result of the small sample size, as courts pierced in 7 of 8 cases where "agency" was a factor and 4 of 5 where "dummy" was a factor.

109. *Id.*

importance; owners, with a 29% increase; employees, with a 19.23% decrease; and business activity, with a 14.73% decrease.

TABLE ELEVEN: PRESENT FACTORS

Category	Cases Where Factor Present	Pierce	No Pierce	% Pierced	Professor Thompson's Results Pierce / No Pierce / Rate
Instrumentality	13	13	0	100.00	73 / 2 / 97.33%
Misrepresentation	21	21	0	100.00	70 / 8 / 89.74%
Alter ego	40	39	1	97.50	173 / 8 / 95.58%
Intertwining	47	42	5	89.36	174 / 30 / 85.29%[110]
Undercapitalization	37	33	4	89.19	88 / 32 / 73.33%
Agency	8	7	1	87.50	48 / 4 / 92.13
Dummy	5	4	1	80.00	159 / 10 / 94.08
Informalities	34	27	7	79.41	101 / 50 / 66.89%
Domination & Control	44	33	11	75.00	314 / 237 / 56.99%
Overlap:					
Owners	19	15	4	78.95	87 / 87 / 50.00%
Business Activity	6	4	2	66.67	35 / 8 / 81.40%
Directors	32	17	15	53.13	66 / 86 / 43.42%
Employees	8	4	4	50.00	36 / 16 / 69.23%
Office	14	7	7	50.00	40 / 28 / 58.82%
Officers	40	18	22	45.00	49 / 52 / 48.51
Management	6	2	4	33.33	28 / 15 / 65.12%
Total Overlap	125	67	58	53.60	459 / 343 / 56.53%

2. Absent Factors

Many courts also noted the absence of certain factors in their decisions. As in Thompson's study of pre-1986 cases, "misrepresentation" was the factor whose absence was most often noted by courts.[111] Courts noting the absence of "misrepresentation" refused to pierce in 94.44% of those cases. The second most

110. These figures combine Professor Thompson's figures for "intertwining" and "lack of substantive separation." *See id.*

111. *Id.* While pre-1986 courts noted the absence of "misrepresentation" in almost one-quarter of all piercing cases, from 1986–1995 that figure jumped to over 31%. *Id.* at 1064–65.

frequently noted absent factor was that of "alter ego," mentioned in almost one-quarter of all cases. However, this factor proved to be more predictive than "misrepresentation," with courts refusing to pierce in 100% of cases where they specifically found that "alter ego" was not present.

TABLE TWELVE: ABSENT FACTORS

Absent Factor Mentioned	**Total Cases Where Factor Not Present**	**Pierce**	**No Pierce**	**% Refuse to Pierce**	**Professor Thompson's Results Pierce / No Pierce / Rate**
Alter ego	57	0	57	100.00	1 / 165 / 99.40%
Intertwining	35	1	34	97.14	1 / 99 / 99.00%[112]
Undercapitalization	26	1	25	96.15	3 / 48 / 94.12%
Informalities	20	1	19	95.00	4 / 71 / 94.67%
Instrumentality	19	1	18	94.74	0 / 59 / 100%
Misrepresentation	72	4	68	94.44	30 / 361 / 92.33%
Domination & Control	27	2	25	92.59	2 / 124 / 98.41%
Dummy	12	1	11	91.67	0 / 64 / 100%
Agency	3	1	2	66.67	1 / 53 / 98.15%

3. Undercapitalization

Courts pierced the veil in 89.19% of all cases where "undercapitalization" existed. Of the 28 contract cases which pierced the veil, "undercapitalization" was present in 12 (42.87%); of the 10 tort cases in which the court pierced the veil, "undercapitalization" was present in 4 (40%). A piercing result was more likely in tort cases in which "undercapitalization" was present (100%) than in contract cases (80%).

Of the 38 statutory cases where the court pierced the corporate veil, undercapitalization was a factor in 14 (36.84%). In total, undercapitalization was mentioned in 15.96% of all statutory cases, with courts piercing in 93.33% of the statutory cases where

112. These figures combine Professor Thompson's figures for "intertwining" and "lack of substantive separation." *See id.* at 1063 tbl.11.

undercapitalization was found.

In cases where the court pierced the corporate veil, undercapitalization was a factor in 40% of cases where the defendant was the sole shareholder, 53.85% of cases where the corporation had two or three shareholders, and 25% of cases where the court pierced the veil of a close corporation. "Undercapitalization" was much more prevalent in cases where the court pierced to reach a sibling corporation (50%) rather than a parent or subsidiary (9.09%).

TABLE THIRTEEN: UNDERCAPITALIZATION

Number of Shareholders	**Number of Cases When Court Pierced**	**Number of Piercing Cases Citing Undercap**	**Percentage of Piercing Cases that Cited Undercap**	**Professor Thompson's Results for Percentage of Piercing Cases that Cited Undercap**
One	20	8	40.00	14.60
Two or Three	26	14	53.85	24.55
Close	8	2	25.00	11.96
Parent/Sub	11	1	9.09	11.11
Sibling	8	4	50.00	10.53

"Undercapitalization" and "fraud" were both present in only 8 of the 228 total cases (3.51%).[113] "Misrepresentation" was present in 21.62% of all cases where "undercapitalization" was present, and in 24.24% of cases where "undercapitalization" was present and the court pierced.

4. Informalities

Courts pierced the corporate veil in 79.41% of all cases where the court found that "informalities" existed.[114] This is an increase from pre-1986 cases, where the rate was just under 67%.[115] When compared with other factors, informalities appear to be less important than all but one.

When cases are separated by context, "informalities" appear equally important in contract (35.71%) and statutory cases (37.84%), but less important in tort cases (20%). For cases where courts found informalities, the veil was pierced in 66.67% of contract cases, 100% of tort cases, and 87.5% of statutory cases.[116] The lack of uniformity

113. All cases in which "undercapitalization" and "misrepresentation" were present were piercing cases, comprising 10.09% of all piercing cases.

114. Courts pierced in 27 of 34 cases.

115. Courts pierced in 101 of 151 cases.

116. Courts pierced in 10 of 15 contract cases, 2 of 2 tort cases, and 14 of 16

across contexts is similar to that of pre-1986 cases, where courts pierced in 61% of contract cases, 53% of tort cases, and 40% of statutory cases.[117] Only in 5 of 27 cases (18.51%) in which the court found "informalities" did the court also find "misrepresentation." Thus, any correlation between the existence of "misrepresentation" and "informalities" in piercing cases has declined since Professor Thompson's study.[118]

5. Contract Versus Tort

Professor Thompson noted the relatively low number of tort cases among piercing cases.[119] In cases decided between 1986 and 1995, tort cases accounted for only 11.84% of all piercing cases, down slightly from 14.28%.[120]

When cases where "misrepresentation" was a factor are removed from the analysis, the piercing rates understandably are reduced. However, even in non-"misrepresentation" cases, courts continue to pierce more in tort cases (28%) than in contract (25.3%).[121]

TABLE FOURTEEN: LACK OF MISREPRESENTATION

Category	Total Cases Where Misrepresentation Was Not a Factor	Pierce	No Pierce	% Pierced
Contract	83	21	62	25.30
Tort	25	7	18	28

Less than half of the tort cases involved a corporate defendant, down from the 72.68% of corporate defendants in pre-1986 cases.[122] However, corporate defendants were far more successful than their individual counterparts against tort plaintiffs, as courts reached only 16.66% of corporations as opposed to 57.14% of individuals.[123]

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statutory cases.

117. Thompson, *supra* note 1, at 1068.

118. Professor Thompson found a connection in 24 of 101 cases (23.76%). *Id.*

119. Professor Thompson found that only 226 of 1583 cases were tort cases (14.28%). *Id.*

120. In this Study, only 27 of 228 cases were tort cases.

121. For contracts cases, courts pierced in 28 of 90 cases (31.11%). Of those 90 cases, "misrepresentation" was a factor in 7, all of them piercing cases. For torts, courts pierced in 10 of 28 total cases. Of those 28 cases, "misrepresentation" was a factor in 3, all of them piercing cases.

122. Corporations were defendants in 12 of 26 tort cases from 1986–1995. Corporations were the defendants in 149 of 205 pre-1986 tort cases. Thompson, *supra* note 1, at 1069 n.171.

123. Of the 12 cases in which corporations were the defendants, courts pierced in just 2. Courts pierced in 8 of 14 tort cases where the defendant was an individual shareholder.

V. CONCLUSION

Limited liability furthers many important policy goals of a capitalist system. Limited liability enables individuals to invest in corporate ventures they deem to be worthwhile, thereby providing financing for firms. However, the protection of limited liability is not absolute. Under certain circumstances, courts will utilize the equitable piercing doctrine to disregard the corporate entity and hold the corporation's owners personally liable for corporate obligations. Commentators have historically criticized the ad hoc reasoning employed by courts in piercing cases. The empirical analysis in this Study provides insight into the way courts analyze piercing cases.

First, the data showed that courts refused to pierce the veil when the corporate defendant is a public corporation. The fact that none of the defendants in the 228 cases we examined were public corporations shows that plaintiffs recognize that the rationales supporting limited liability are too strong to be overcome when the corporation's securities are traded on public markets. This finding supports the argument of Easterbrook and Fischel that two of the chief rationales supporting limited liability are the ability of individual investors to diversify their portfolios and the facilitation of rational pricing of corporate securities based on the current performance and future prospects of a corporation. As a general rule, there is no market for the shares of closely held corporations. Thus, there is no risk that piercing in the close corporation context will affect the ability of markets to act rationally in pricing corporate securities or hinder individual investors from investing in multiple corporations to diversify and minimize the risk of loss.

The data also showed that between 1986 and 1995, courts pierced more frequently in the tort setting than in the contract setting. The finding held for cases involving misrepresentation, as well as cases where the court did not find misrepresentation. This finding is contrary to Professor Thompson's results, and it supports the argument of many commentators that courts should pierce the veil more frequently in tort cases than in contract cases. The ability of contract creditors, who voluntarily interact with the corporation, to negotiate for a risk premium ex ante should lead courts to pierce more frequently when the plaintiff is a tort creditor whose only remedy is an ex post recovery from the corporation and its owners. However, the distinction vanishes when a corporate defendant engages in misrepresentation. A plaintiff cannot negotiate for a risk premium sufficient to compensate for misrepresentation on the part of the corporate defendant, so courts should disregard the context and pierce the corporate veil when defendants engage in misrepresentation. The findings support the conclusion that misrepresentation warrants disregarding the corporate veil, as the court pierced in over 94% of the cases where they found

misrepresentation. While much of the discussion of piercing is context-specific, the fact that courts pierced almost universally when they found misrepresentation suggests that courts are focused more on the conduct of the defendant than on the context.

Finally, our findings show that plaintiffs brought their claims in federal court much more frequently between 1986 and 1995 than pre-1986. While only 40% of the cases Professor Thompson examined were litigated in federal court, over 60% of the cases we examined were decided by federal courts. This is likely due to the fact that Congress has codified significant areas of the common law of torts. The fact that cases are being litigated in the federal system is very significant in light of the fact that our analysis shows that federal courts are almost 10% more likely to pierce the corporate veil than state courts. This finding is of practical significance to parties litigating piercing cases.

Given the fact that piercing the corporate veil is the most litigated issue in corporate law, it is very surprising that there has been so little empirical research examining how courts approach piercing cases. Our results show that courts have altered their approach to piercing cases since Professor Thompson's study, examining cases prior to 1986. Our findings regarding how courts approach cases in the contract context versus the tort context directly contradict the findings of Professor Thompson. Further, the increased frequency of cases being litigated in the federal system, combined with the increased frequency of piercing results in federal courts, is very significant for parties involved in piercing cases. The ultimate end of this Study is to provide commentators and practitioners with additional data on how courts approach piercing cases, and we hope that our findings prove useful.

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