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Piercing the Corporate Veil – Selected Issues in International Comparison

Abstract

The main purpose of the thesis is to give recommendation for possible application of the piercing doctrine in the Czech Republic. Secondary purposes are (i) analysis of effects caused by disregarding the principles of limited liability and separate legal personality because of piercing and (ii) detailed description of approaches to the piercing issue in selected legal systems (USA, UK and Germany).

The thesis starts with some terminological issues; it introduces the possible Czech equivalents of the notion "piercing the corporate veil" and explains that it can have slightly different meaning depending on the individual author. The differences stem especially from the questions whether piercing negates only the principle of limited liability or also the principle of separate personality; whether so called inner piercing (*Innenhaftung*) shall be part of the doctrine and whether the piercing doctrine shall be regarded as product of case-law only. Also some special forms of piercing (reverse piercing, lateral piercing and insider piercing) are introduced.

The third chapter analyses the relationship between the piercing doctrine and the principles of limited liability and separate legal personality. In particular it starts with advantages and disadvantages of the two principles for individual shareholders and the entire society. Subsequently, it analyses the impacts of the piercing doctrine on such advantages and disadvantages. In connection with the said analysis, the author distinguishes voluntary and involuntary creditors and draws conclusions regarding their protection by the piercing doctrine.

Chapters 4 – 7 cover the issue of piercing in three selected legal systems. First, the thesis deals with the situation in the USA. After brief overview of the historical development of the piercing jurisprudence, it starts with the so called three-factor piercing doctrine based on the work of F. J. Powell and it analyses in detail its three prongs (control, morally culpable conduct, casual relationship). Subsequently, so called single-factor piercing doctrines are examined - they are usually based on one of the prongs of the three-factor doctrine. The chapter also deals with theories based on the economic relations between the shareholder and company (especially the *theory of enterprise entity* introduced by A. Berle). In connection with individual doctrines, some empirical studies are mentioned (R. Thompson and his followers). The final section of the chapter deals with some substitutes for piercing: agency, fraudulent conveyance and equitable subordination.

Chapter 6 introduces the piercing the corporate veil doctrine in the United Kingdom. Again it starts with brief historical overview commencing by the decision *Salomon v. Salomon* (1897). Then it provides detail analysis of the dominant *mere façade* doctrine based on the *Adams v. Cape Industries plc* decision of 1990. Moreover other important doctrines are mentioned, in particular the single economic unit doctrine based on decision *DHN Food Distributors v. Tower Hamlets* and piercing doctrine based solely on the interest of justice argument. Finally the *genuine ultimate purpose rule* doctrine proposed by M. Moore is considered. The chapter also describes some alternatives to piercing: the statutory provisions on fraudulent trading a wrongful trading.

German approach to the piercing problematic is described in chapter 7. As usual, it contains brief historical overview. Apart the main doctrines, the chapter covers theoretical explanations of piercing formulated by German scholars (*Missbrauchlehre*, *Normzwecklehre*). After the general introduction, the chapter describes three main doctrines articulated by the

German courts. It starts with doctrine based on the German group law (*Konzernrecht*) and describes in detail its variants. Then it moves to the *existenzvernichtender Eingriff* doctrine, which was used until 2007. Finally, the chapter describes the current doctrine based on section 826 of the German civil code.

The aim of chapter 8 is to provide synthesis of the previous findings with due respect to possible piercing doctrine in the Czech Republic. It starts with considerations about the necessity and theoretical admissibility of piercing and deals with the interrelationship to the principle of legal certainty. It also suggests that application of the piercing doctrine shall be exceptional and ultimate mean to achieve justice and that the plaintiff shall be granted with some procedural privileges because of his limited access to internal company information.

The chapter then moves to factors the Czech doctrine shall use to determine permissibility of piercing – the possible main factors identified by the thesis are (i) control over the company, (ii) existence of single economic unit and (iii) factors derived from the interests of justice. The author concludes that the appropriate factor shall be derived from the interests of justice and formulates it as *extraordinarily morally culpable conduct* of the shareholder. However, such criterion is too vague with respect to the need of legal certainty. Therefore it shall be combined with some auxiliary criteria. In particular, the author suggests that the creditor, who seeks piercing, shall prove that he is unable to collect payment directly from the company. Secondly, there shall be causal relationship between the conduct of the shareholder and the loss of the creditor. Finally, the shareholder will usually exercise intensive control over the company. Should there be some doubts, the motive of the shareholder shall be considered. In its final section, the chapter deals with some legal consequences of piercing and the possible legal ground for piercing according Czech law.