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# D I E D C I N I N G P I E R C I N G T H E C O R P O R A T E V E I L



*Many companies manage operational risk through the use of corporate subsidiaries. Yet in some circumstances, a parent company can be liable for a subsidiary's wrongdoing or contractual breach under a doctrine known as piercing the corporate veil. Counsel for corporate families must understand how courts apply this doctrine and should follow certain best practices to limit their clients' exposure to piercing claims.*

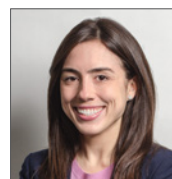


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A corporation and its shareholders are generally treated as separate legal entities. The corporation acts through its own agents and officers and enters into its own contracts. Only the corporation's assets, and not those of its shareholders, are available to pay any judgments against the corporation.

Many companies legitimately use the corporate structure to manage their operational risk by creating corporate subsidiaries to conduct their businesses, including contracting with customers and suppliers and incurring debt. This structure allows a parent company to shield itself from its subsidiary's liabilities and limit its exposure to the capital contribution it made to the subsidiary. However, plaintiffs asserting claims against a subsidiary often seek to disregard its corporate form and hold the parent company directly liable for the subsidiary's obligations. This type of claim is commonly referred to as "piercing the corporate veil."

This article explores the doctrine of piercing the corporate veil, including:

- The reasons plaintiffs seek to pierce the corporate veil.
- The primary doctrines courts apply to piercing claims.
- The standards of proof plaintiffs must meet to bring piercing claims.
- Best practices for parent companies to limit their liability exposure.

Although this article focuses on piercing claims in the parent-subsidiary context, the same principles can be applied to piercing claims against a corporation and its individual shareholders. This article does not address piercing in bankruptcy proceedings or other statutory schemes that may apply different standards to determine liability for piercing claims.

## PURPOSE OF PIERCING CLAIMS

The primary reason plaintiffs seek to pierce the corporate veil of a subsidiary is to reach the assets of the parent company. A company doing business through one or more subsidiaries can limit the amount that a potential plaintiff can recover in an action against a subsidiary by ensuring that, for example, each subsidiary holds only as many assets as are required for its operations and any statutory capitalization requirements. Because recovery against the subsidiary may be limited, a plaintiff may seek to pierce the corporate veil to reach the parent company's assets either:

- Before obtaining a judgment against the subsidiary to expand the potential pool of assets available to satisfy any successful claims against the subsidiary.
- After obtaining a judgment against the subsidiary when the judgment cannot be satisfied by the subsidiary's assets.

A plaintiff may also seek to pierce the corporate veil to obtain jurisdiction over a parent company that is not present in the US or does not do business within the US. Any decision by a court is likely unenforceable against a parent company if the court lacks personal jurisdiction over it. Therefore, a plaintiff may attempt to establish jurisdiction over the non-resident parent

company by arguing that the corporate form of the subsidiary should be disregarded so that the subsidiary's actions can be imputed to the parent company, which then establishes the court's personal jurisdiction over the parent (see *Box, Proving Personal Jurisdiction*).

Piercing claims may also be used as a threat to gain leverage in settlement negotiations with the subsidiary, not only to encourage settlement discussions but also to increase the potential settlement amount. Adding a piercing claim typically increases the burden and cost of defending the claim against the subsidiary for both the parent company and the subsidiary, particularly when the parent is a non-US company.

For example, because piercing claims are fact-specific, a plaintiff will likely have access during discovery to a broad range of documents and other information about the parent company, such as corporate documents, board minutes, and bank records. A plaintiff may also seek to depose officers, directors, or other senior employees of both the parent company and the subsidiary. The subsidiary may be more willing to settle the underlying claim to avoid subjecting the parent company to the additional burden and cost that would be involved.

## PIERCING DOCTRINES

Courts typically make their decision to pierce the corporate veil by considering the structural relationship between the parent company and the subsidiary. To impute a subsidiary's actions and jurisdictional contacts to its parent company, a plaintiff must persuade the court that the parent company and the subsidiary are not truly separate companies.

To establish a piercing claim, a plaintiff must demonstrate that the subsidiary is either the parent company's:

- Alter ego (sometimes known as an "identity theory").
- Agent (sometimes known as an "instrumentality theory").

As courts have observed, "[t]he concept of piercing the corporate veil is equitable in nature" and there is "[n]o hard and fast rule." As a result, a court may apply either or both theories to pierce the corporate veil, so long as its ultimate inquiry focuses on the improper use of the corporate form. (*Patterson v. Hartford Healthcare Corp.*, 2018 WL 3117046, at \*4 (Conn. Super. Ct. June 5, 2018).)

## ALTER EGO THEORY

To reach a parent company using the alter ego theory, a plaintiff must prove that both:

- The parent company completely dominated and controlled the subsidiary, disregarding its separate identity.
- An injustice or other wrong to the plaintiff will likely result if the corporate veil is not pierced.

Some jurisdictions may also require the plaintiff to prove that the parent company used the corporate form to perpetrate a fraud on the plaintiff. For example, Delaware courts have required a showing of "fraud or similar injustice" to support piercing claims (see *Outokumpu Eng'g Enters., Inc. v. Kvaerner EnviroPower, Inc.*, 685 A.2d 724, 729 & n.2 (Del. Super. Ct. 1996);

# Piercing claims may be used as a threat to gain leverage in settlement negotiations with the subsidiary, not only to encourage settlement discussions but also to increase the potential settlement amount.



see also *In re Sunstates Corp. S'holder Litig.*, 788 A.2d 530, 534 (Del. Ch. 2001)).

Similarly, under Maryland law, courts generally refuse to disregard the corporate form except where it is “necessary to prevent fraud or enforce a paramount equity” (see *Antonio v. Sec. Servs. of Am., LLC*, 701 F. Supp. 2d 749, 759-60 (D. Md. 2010); *Iceland Telecom, Ltd. v. Info. Sys. & Networks Corp.*, 268 F. Supp. 2d 585, 589 (D. Md. 2003) (internal quotations omitted)).

## **Domination and Control by Parent Company**

The alter ego theory requires a plaintiff to prove that the parent company’s domination and control over the subsidiary was so extensive that the subsidiary was primarily conducting business for the parent company and ceased to exist as a separate legal entity. Courts generally focus on factors showing that the parent company ignored the subsidiary’s separate identity and operated the two companies as one entity controlled or directed by the parent company. For example, courts commonly examine the subsidiary’s:

### ■ **Corporate form and structure.** Courts may consider whether:

- the subsidiary’s corporate formalities are disregarded by the parent company;
- the subsidiary functions as a mere facade of the parent company;
- the parent company owns all of the subsidiary’s stock;
- the subsidiary is inadequately capitalized; or
- the subsidiary fails to pay dividends.

### ■ **Operational and contractual arrangements.** Courts may consider whether:

- the parent company and subsidiary share corporate officers and directors;
- the subsidiary shares offices, employees, bank accounts, and telephone numbers with the parent company;
- the parent company uses the subsidiary’s property as its own;

- the agreements and other arrangements (such as sharing administrative services, employees, or insurance coverage) between the parent company and the subsidiary are not arm’s-length transactions; or
- the subsidiary’s contracts contain cross-default provisions with contracts entered into by the parent company or any of its other subsidiaries.

### ■ **Financial arrangements with the parent company.** Courts may consider whether:

- the subsidiary makes undocumented “loans” to the parent company or extends credit to the parent company on other than market terms;
- the parent company pays the salaries of the subsidiary’s employees or makes all human resources decisions for the subsidiary;
- the parent company siphons money out of the subsidiary or accepts money intended for the subsidiary; or
- the subsidiary guarantees debts of the parent company or any of the parent company’s other subsidiaries.

(See, for example, *Iceland Telecom*, 268 F. Supp. 2d at 590-91; *Agai v. Diontech Consulting, Inc.*, 975 N.Y.S.2d 707, at \*2-3 (N.Y. Sup. Ct. 2013); *Sonora Diamond Corp. v. Super. Ct. Tuolumne Cty.*, 83 Cal. App. 4th 523, 538-39 (Cal. Ct. App. 5th Dist. 2000).) (For information on how courts analyze domination and control in the context of limited liability companies (LLCs), see *Box, Piercing of LLCs*.)

These factors are not exhaustive. The analysis is fact-specific, and courts have broad discretion in deciding what evidence supports an alter ego finding. Any one factor standing alone generally is insufficient to justify setting aside the corporate form. For example, a parent company’s ownership of all of its subsidiary’s outstanding stock is, by itself, insufficient to prove domination, even though it demonstrates that the parent company is the primary source of power and exercises control over the subsidiary. However, in certain cases, even one factor

## PIERCING OF LLCs

All 50 states have enacted statutes governing the creation of business entities in the form of LLCs. Some of these LLC statutes expressly authorize piercing claims against LLCs (for example, C.R.S. § 7-80-107). In other states, courts have applied common law piercing claims against corporations to LLCs (see, for example, *Stockdale v. Ellsworth*, 407 P.3d 571, 577-78 (Colo. 2017); *GreenHunter Energy, Inc. v. W. Ecosystems Tech., Inc.*, 337 P.3d 454, 462 (Wyo. 2014) (citing *Kaycee Land & Livestock v. Flahive*, 46 P.3d 323 (Wyo. 2002))).

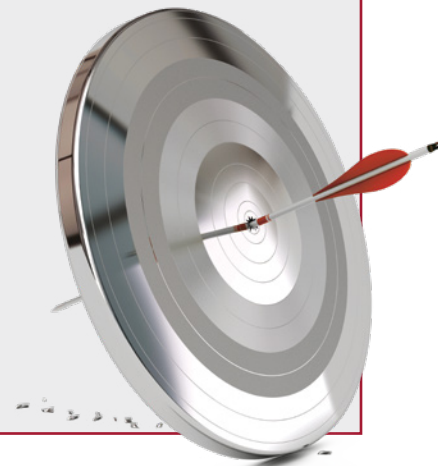
However, courts applying common law principles when conducting a piercing analysis generally place less emphasis on an LLC member's control and domination to reflect the practical differences between how LLCs and corporations are managed (for example, LLC members often directly manage an LLC). Most LLC statutes expressly protect members from personal liability for debts, liabilities, and obligations incurred solely by reason of being a member of the LLC. As a result, it can be more difficult for a plaintiff to assert piercing claims against subsidiaries that are LLCs than against those that are organized as corporations.

For example, in *D.R. Horton Inc. - New Jersey v. Dynastar Development, L.L.C.*, the plaintiff sought to pierce the corporate veil in a breach of contract claim against an LLC (2005 WL 1939778 (N.J. Super. Ct. Law Div. Aug. 10, 2005)). In refusing to hold the individual member and manager of the LLC personally liable for the breach, the court observed that the differing structure and purpose of LLCs suggested less weight should be placed on the observance of corporate formalities or a subsidiary's undercapitalization.

According to the court, the practical differences between managing an LLC and owning shares in a corporation meant that:

- The LLC member was more careful in distinguishing between his entities when entering formal contracts and refrained from engaging in informal correspondence.
- The LLC member did not intend to mislead the plaintiff about his position, even if he failed to correct any misimpressions about the roles of his different entities.
- The LLC form was not abused or used to perpetuate a fraud or injustice against the plaintiff, who had not relied on the existence of corporate formalities and was not directly harmed by the lesser degree of corporate formalities.
- It was rational economic behavior for the LLC member to share phone lines, staff, and business space among his various entities, given the lesser weight assigned to the domination and control factors in the LLC piercing context.
- It was reasonable for the LLC member to have misused stationery with the incorrect entity listed, as these types of minor errors are common among entrepreneurs and other LLC owners.

(2005 WL 1939778, at \*37-38.)



may be enough if sufficient evidence of domination and control is present.

### Injustice or Other Wrongs to Plaintiff

Once control and domination has been established, the plaintiff must then show that the parent company's control resulted in a wrong to the plaintiff. A showing of fraud usually satisfies this requirement, but is not a necessary element in all jurisdictions. For example, in California, Ohio, North Dakota, and South Dakota, a plaintiff can satisfy the injustice element through a showing of inequity, injustice, or an overall element of unfairness.

For example, in *Wyatt v. Wyatt*, a divorce action, the evidence supported the court's finding to pierce the corporate veil of the husband's three corporations for purposes of dividing the marital property. The court held that the husband illegally abused the corporate form to his wife's detriment, and therefore pierced the corporate veil to prevent an injustice. (545 S.W.3d 796, 801 (Ct. App. Ark. 2018).)

Courts have not always provided clear guidance on what constitutes an inequity, injustice, or unfairness sufficient to justify disregarding the corporate form. Although a showing of fraud is not always required, the injustice or other wrongs that courts rely on in disregarding the corporate form often appear similar to fraud (see *Flushing Plaza Assoc. No. 2 v. Albert*, 102 A.D.3d 737, 738-39 (N.Y. App. Div. 2d Dep't 2013) (finding that piercing was appropriate where the trial court had found, among other things, that the parent company stripped the subsidiary of its assets, rendering it judgment-proof)).

### AGENCY THEORY

Under the agency theory, a plaintiff seeks to prove that the subsidiary was acting as an agent of the parent company. The parent company's liability for the subsidiary's actions is based on the concept that a principal is liable for actions taken by its agent within the scope of the agent's authority. To prevail on an agency theory, a plaintiff must typically establish that the parent company:

- Authorized the subsidiary (the alleged agent) to act on its behalf, and the subsidiary agreed to act as the parent company's agent.
- Exercised total control over the subsidiary.

In some circumstances, a plaintiff may also need to establish a close connection between the plaintiff's claims and the purported agency.

A parent company's ownership of the subsidiary's stock and common management between the parent company and subsidiary generally are insufficient to establish an agency relationship (see, for example, *Scott v. NG U.S. 1, Inc.*, 881 N.E.2d 1125, 1131-34 & n.14 (Mass. 2008) (citing *My Bread Baking Co. v. Cumberland Farms, Inc.*, 233 N.E.2d 748, 751-52 (Mass. 1968))). Courts usually do not find an agency relationship absent evidence that the parent company both authorized the subsidiary to act on its behalf and exercised extraordinary control over the subsidiary.

### Authority to Act as Agent

A subsidiary's authority to act for its parent company can be either actual or apparent.

Actual authority exists when a parent company's words, conduct, or other actions manifest an intent to grant authority to a subsidiary to act on the parent company's behalf. Actual authority can be either express or implied by reasonable inferences from the express authority granted by the parent company. For example, an express grant of authority to perform a particular act on behalf of the parent company also includes an implied authority to take the necessary steps to complete the act. In either case, actual authority exists when the subsidiary (as the agent) can infer that the parent company consented to its performance of a particular act (see *In re Parmalat Sec. Litig.*, 594 F. Supp. 2d 444, 451-52 (S.D.N.Y. 2009)).

By contrast, apparent authority exists when a parent company's words, conduct, or other actions give a third party the impression that a subsidiary has authority to act on the parent company's behalf, and the third party accepts and relies on this impression. Apparent authority cannot be based solely on the subsidiary's actions.

For example, *Indagro, S.A. v. Nilva* involved an alleged personal guarantee in connection with a settlement agreement between former joint venture partners. The plaintiff argued that the guarantee was a valid agreement based on representations by two individuals the plaintiff believed were acting as the defendant's agent. Specifically, the plaintiff argued that these agents had apparent authority to bind the defendant to the guarantee because it had sent the two agents to the arbitration and settlement conference on its behalf.

In rejecting the plaintiff's argument, the court found that the plaintiff failed to provide admissible evidence that the defendant had consented to allow or knowingly permitted its agents to represent it personally in the arbitration, and therefore lacked the authority to offer a personal guarantee on the defendant's behalf. (2016 WL 3574330, at \*8 (D.N.J. June 30, 2016), *aff'd*, 733 F. App'x 50 (3d Cir. 2018); see also

*ER Holdings, LLC v. 122 W.P.R. Corp.*, 887 N.Y.S.2d 138, 139-40 (N.Y. App. Div. 2d Dep't 2009).)

### Total Control

In addition to authority, to succeed under the agency theory, a plaintiff must prove the subsidiary acted under the parent company's control. However, the ordinary level of control that a parent company would exercise, either as a majority shareholder or through common management (assuming proper compliance with corporate formalities), is insufficient by itself to satisfy the control element of the agency theory (see *My Bread Baking Co.*, 233 N.E.2d at 753).

Instead, a plaintiff must show the parent company either:

- Actively participated in exercising control over the subsidiary.
- Affirmatively directed the subsidiary to act in a certain way with respect to the plaintiff.
- Influenced or otherwise directed the outcome of the subsidiary's decision-making regarding the substance of the action.

For example, the court in *In re Parmalat* found that evidence of the following was sufficient to raise a material issue of fact on the existence of an agency relationship between an accounting firm and its member firms (its subsidiaries):

- Its subsidiaries agreed to be bound by resolutions of the parent company.
- The parent company had authority over its subsidiaries' professional practices.
- The parent company had control over its subsidiaries' acceptance and rejection of client engagements.
- The parent company influenced and directed the outcome of the subsidiary's decision-making concerning its engagement with the plaintiff.
- The parent company exercised control over which employees of the subsidiary performed work on the engagement with the plaintiff.

(594 F. Supp. 2d at 452.)

### PIERCING STANDARDS FOR JURISDICTION AND LIABILITY

In general, the burden of proof for piercing claims is demanding given the presumption that the parent company and its subsidiary are separate legal entities. As discussed above, both the alter ego and agency theories require a plaintiff to prove some level of domination and control by a parent company beyond that ordinarily exercised over a subsidiary.

However, the required burden of proof and a court's likelihood of piercing the corporate veil may vary depending on whether the determination is being made for jurisdictional or liability purposes.

In most cases, a parent company's sole contact with a forum state is its ownership of the stock of a subsidiary located in the state or doing business in the state. Stock ownership, however, rarely is sufficient by itself to establish personal jurisdiction over a non-resident parent company (for a discussion of how to prove

## PROVING PERSONAL JURISDICTION

Personal jurisdiction is a court's power to adjudicate the rights and obligations of particular persons, corporations, or other legal entities within its jurisdictional reach. By contrast, subject matter jurisdiction concerns a court's power to adjudicate particular types of causes of actions and disputes.

Personal jurisdiction is based on the facts and circumstances of each case. For corporations that are neither incorporated nor domiciled in the forum jurisdiction (which is often the case when a parent company defends against a piercing claim), personal jurisdiction is fact-specific and not always easy to establish. Notably, the mere fact that a subsidiary company does business within a state does not confer jurisdiction over its non-resident parent company, even where the parent is the sole owner of the subsidiary (*Hernandez-Denizac v. Kia Motors Corp.*, 257 F. Supp. 3d 216, 221 (D.P.R. 2017)).

To establish personal jurisdiction over a non-resident defendant corporation, a plaintiff generally must demonstrate that:

- The defendant is subject to general or specific jurisdiction under the state's long-arm statute.
- The court's exercise of either general or specific jurisdiction over the defendant meets certain minimum due process standards of fairness.

### LONG-ARM STATUTES

Each state has its own statute (known as a long-arm statute) or court rules to authorize the exercise of personal jurisdiction over non-resident defendant companies that have sufficient contacts with the forum state. These statutes may apply to actions brought in state or federal court.

Long-arm statutes vary from state to state but generally allow courts to exercise:

- General personal jurisdiction over a non-resident defendant that has sufficiently continuous and systematic contacts with the forum state as to render the defendant "at home" in that state.
- Specific personal jurisdiction where the suit arises from:
  - the defendant's actions within the forum state (for example, a breach of contract case arising out of a business transaction completed within the forum state); or

- the plaintiff's injury within the forum state (for example, in-state injuries caused by a defective product manufactured by the defendant outside the forum state).

Some long-arm statutes also permit claims to be brought for injuries occurring outside the state under certain circumstances. Companies must carefully examine the long-arm statute of the particular forum state, because some permit suits against non-resident defendants on more liberal terms than others.

### General Jurisdiction

In contrast to specific jurisdiction (see below *Specific Jurisdiction*), a court's exercise of general, or all-purpose, jurisdiction over a defendant extends to any cause of action that falls within the court's subject matter jurisdiction.

As noted above, general jurisdiction over a defendant corporation exists where the defendant's affiliations with the forum state are so continuous and systematic as to render the defendant "at home" in that state, such as when the corporation either:

- Is incorporated in the forum state.
- Has its principal place of business in the forum state.

(*Daimler AG v. Bauman*, 571 U.S. 117, 137 (2014) (describing these as paradigmatic bases for general personal jurisdiction).)

While the Supreme Court in *Daimler* contemplated the possibility of an exceptional case where a defendant corporation's operations in a state other than its place of incorporation or principal place of business could be so substantial as to render the corporation "at home" in that state (*Daimler*, 571 U.S. at 761 n.19), it offered no guidance on what factors might render a case exceptional.



Search [Supreme Court: Presence of Subsidiary in Forum State Insufficient for General Jurisdiction Over Foreign Parent Corporation](#) for more on the *Daimler* decision.

Lower courts have not yet defined what an exceptional case entails, but have offered some instruction on factors that are insufficient to create an exceptional case (see, for example, *Brown v. Lockheed Martin Corp.*, 814 F.3d 619, 629-30

personal jurisdiction, see *Box*, *Proving Personal Jurisdiction*). As a result, a plaintiff wishing to bring the parent company into a suit against the subsidiary often attempts to pierce the corporate veil to establish personal jurisdiction over the parent company.

When examining piercing claims for jurisdictional purposes, a court is not determining the ultimate liability (if any) of the parent company. Instead, the court determines only whether the parent company, which is not otherwise subject to personal jurisdiction of the court, can be compelled to participate in

the action. Accordingly, most courts are inclined to apply a less stringent analysis when considering a piercing claim for jurisdictional purposes.

For example, some jurisdictions do not require evidence of fraud to establish personal jurisdiction over a non-resident parent company, even if fraud is later required to hold the parent company liable for its subsidiary's conduct (see *Int'l Equity Invs., Inc. v. Opportunity Equity Partners, Ltd.*, 475 F. Supp. 2d 456, 459 (S.D.N.Y. 2007) (citing *Marine Midland Bank, N.A. v.*

(2d Cir. 2016) (finding a case was not exceptional where a defendant had operated its business in the forum state for decades, ran operations from numerous leased facilities in the state, employed state residents as employees, and enjoyed substantial revenue from the state, but was incorporated and had its principal place of business elsewhere); *Martinez v. Aero Caribbean*, 764 F.3d 1062, 1070 (9th Cir. 2014) (finding a case was not exceptional where a defendant's significant contracts and marketing activities in the state were "minor compared to its other worldwide contacts").

### Specific Jurisdiction

Specific jurisdiction refers to a court's exercise of jurisdiction over a defendant where the suit arises out of, or is related to, the defendant's contacts with the forum state (*Walden v. Fiore*, 571 U.S. 277, 283-84 (2014)).

To establish specific jurisdiction over a non-resident defendant corporation, a plaintiff must show only a minimum level of contacts between the defendant, the forum, and the litigation, rather than the continuous and systematic contacts required for general jurisdiction. Absent a connection between the defendant's contacts in the forum state and the facts of the underlying controversy, no specific jurisdiction can exist, regardless of the extent of a defendant's unconnected activities in the state (*Squibb Co. v. Superior Court*, 137 S. Ct. 1773, 1781 (2017)).

In the jurisdictional context, the piercing analysis is often duplicated. For example, some states authorize the exercise of specific jurisdiction over non-resident organizations that transact business through a resident alter ego subsidiary corporation for claims arising out of the subsidiary's business transactions. In these cases, a court must undertake a preliminary analysis to determine if a resident corporate subsidiary is an alter ego of a non-resident parent company to decide whether the parent is subject to jurisdiction. (*AKH Co. v. Universal Underwriters Ins. Co.*, 2018 WL 4111717, at \*6 (D. Kan. Aug. 29, 2018) (describing Kansas law).) This preliminary analysis focuses on the same factors as the typical alter ego analysis described above (see above *Alter Ego Theory*).

### DUE PROCESS

If the requirements of a long-arm statute are satisfied, a court must next consider whether the exercise of personal

jurisdiction over a non-resident defendant comports with due process (a test of fairness rooted in the US Constitution). A state's exercise of personal jurisdiction over a non-resident defendant generally satisfies due process only if the following three elements are satisfied:

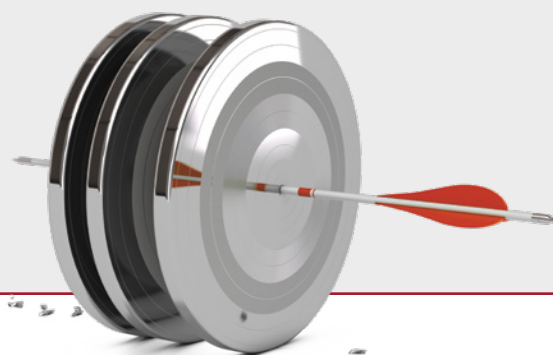
- The defendant has minimum contacts with the forum state (this analysis typically duplicates the minimum contacts analysis required for the exercise of specific jurisdiction).
- The defendant "purposefully availed" itself of the privilege of conducting activities in the forum state.
- The court's exercise of jurisdiction over the non-resident defendant is fair and reasonable.

When a suit involves activities that fall squarely within the provisions of a state's long-arm statute, due process is usually satisfied. When the nature of the defendant's contacts with the state are disputed or when the activities at issue do not fall squarely within the terms of the state's long-arm statute, the court must conduct a comprehensive due process analysis of the non-resident defendant's contacts with the forum state.

As with other claims, in the piercing context, these factors include whether:

- The claim directly arises out of, or relates to, the defendant's forum state activities.
- The defendant's in-state contacts represent a purposeful availment of the privilege of conducting activities in the forum state.
- The exercise of jurisdiction is reasonable.

(*Hernandez-Denizac*, 257 F. Supp. 3d at 221.) Some courts will also consider the interest of the forum state in providing a forum for its residents and the convenience of the parties (see, for example, *McCall Law Firm, PLLC v. Crystal Queen, Inc.*, 2017 WL 5652389, at \*5 (E.D. Ark. Mar. 3, 2017)).



*Miller*, 664 F.2d 899, 904 (2d Cir. 1981)). Even in jurisdictions where fraud is not required to hold the parent company liable, courts may still apply a less onerous standard for jurisdictional purposes than the standard required for liability purposes (see *D. Klein & Son, Inc. v. Good Decision, Inc.*, 147 F. App'x. 195, 196 (2d Cir. 2005); see also *In re Platinum & Palladium Antitrust Litig.*, 2017 WL 1169626, at \*46 n.21 (S.D.N.Y. Mar. 28, 2017) (acknowledging that the Second Circuit has not yet addressed "whether the same standard that governs the alter ego analysis for liability purposes controls for jurisdictional purpose[s]").

When analyzing piercing for liability purposes, courts generally require plaintiffs to prove all elements under either the alter ego or agency theory. For example, under the alter ego theory, a plaintiff must prove both the parent company's exercise of control and domination over the subsidiary as well as a connection between the plaintiff's injury and the parent company's domination.

# A well-capitalized and insured subsidiary substantially weakens the possibility that a plaintiff will suffer an injustice if the corporate veil is not pierced. This is because the plaintiff can collect the full amount of a judgment from the subsidiary without needing to reach the parent company's assets.

## BEST PRACTICES

There are many steps a parent company can take to minimize the risk of piercing claims. In particular, a parent company should:

- **Observe corporate formalities and structures.** A well-capitalized and insured subsidiary substantially weakens the possibility that a plaintiff will suffer an injustice if the corporate veil is not pierced. This is because the plaintiff can collect the full amount of a judgment from the subsidiary without needing to reach the parent company's assets. Therefore, a parent company should:
  - properly capitalize and insure the subsidiary;
  - document the reasons for the subsidiary's capital structure and the level of capital used;
  - comply with corporate formalities, including properly issuing all stock certificates; and
  - properly file the subsidiary's articles of incorporation.
- **Ensure the subsidiary operates independently.** Control of a subsidiary's major transactions through stock ownership and board control and an overlap of directors, officers, or other staff are not determinative of a piercing claim. However, too much control by a parent company over the day-to-day business decisions of its subsidiary has led courts to refuse to dismiss the parent company as a defendant (see, for example, *In re Parmalat*, 594 F. Supp. 2d at 455). A parent company should avoid structuring its relationship with a subsidiary in ways that permit the parent company to exercise final decision-making power or other undue influence on the routine business operations of the subsidiary. Additionally, a parent company should:
  - create a separate and independent bank account for the subsidiary;
  - maintain separate books and records for the subsidiary;
  - keep a balance between debt and equity that is appropriate for the type of business the subsidiary operates;
  - have the subsidiary hire its own employees, paid from the subsidiary's own funds, and preclude the parent company from hiring and firing the subsidiary's employees;
  - create an independent board of directors for the subsidiary to conduct board meetings separately from the parent company;

- maintain separate offices and telephone numbers for the subsidiary;
  - file separate tax returns from the subsidiary; and
  - avoid references to the subsidiary as a "division" or "department" of the parent company or similar terms.
- **Maintain arm's-length transactions.** For example, a parent company should:
- ensure all financial transactions with the subsidiary are on an arm's-length basis, including any loan to or from the parent company; and
  - fully document all transfers of money or other property between the parent company and subsidiary.

Additionally, a non-US parent company should carefully structure its relationship with a US subsidiary to avoid creating minimum contacts between the non-US parent company and a forum state. This can help shield the non-US parent company from being subject to personal jurisdiction in that forum, which, in turn, can reduce the risk that the parent company will need to respond to burdensome discovery requests. (For more on personal jurisdiction, see *Box, Proving Personal Jurisdiction*.)



Search [Protecting Foreign Parent Corporations from Personal Jurisdiction in the US](#) for information on what foreign parent companies can do to limit their exposure to litigation in the US.

Search [Protecting Foreign Corporations from US Discovery](#) for information on how courts may order foreign companies to produce documents in US litigation through their US affiliates and practical tips to help foreign companies reduce their involvement in US discovery.

