Title:
X.2 - Piercing the corporate veil

Content:

No. X.2 - Piercing the corporate veil

(a) The separate legal personality of a corporation ("corporate veil") may be disregarded in exceptional cases in order to hold a shareholder liable for the corporation's debts.

(b) Exceptional cases are cases of:

i) clear under-capitalization,

ii) mingling of corporate and financial spheres, especially in case of total control of the parent company over the business and financial affairs of its subsidiary, or

iii) fraud.

Commentary:

1 The Principle reflects situations in which the idea of the nature of corporations which constitute entities that are separate and distinct from its members, who are liable only to the extent that they have contributed to the company's capital, must be disregarded due to the application of the Principle of good faith.

2 In all three scenarios listed in the Principle, the concept of the corporation as a separate legal entity is misused by its founders or initiators. In these cases, the corporation is a mere "façade", used by its founders to shield themselves from claims raised against them by their creditors by hiding behind the corporate entity which they have established but which does not possess any assets necessary to satisfy the claims of these creditors.

3 It must be noted that the Principle is an exception to the basic rule that corporations as separate legal entities are acknowledged. The application of the Principle therefore requires a very strict test, i.e. clear evidence of under-capitalization, mingling of spheres or fraud, so as to ensure that the Principle remains the exception.