A Review of Piercing the Veil Cases in Arkansas

I. What Does it Mean to “Pierce the Veil”

Piercing the veil is an equitable doctrine developed at common law, which under certain circumstances allows a court to order that the separate legal existence of a business entity be disregarded. Originally, the doctrine was designed to allow creditors and other claimants to recover against the shareholders of a corporation, despite the usual rule that shareholders have no personal liability for debts of the corporation. Early cases held that piercing was available only if “the privilege of transacting business had been illegally abused to the injury of a third party.” This evolved over time so that, in very general terms, the modern rule seems to be predicated on the notion that if certain owners of a business fail to respect the separate existence of that business, third parties (and sometimes even insiders) need not recognize the business either. The language of these opinions often asks whether the corporation was “a mere instrumentality of the principals,” or whether the corporation was no more than the “alter ego” of the person against whom recovery is sought. In recent years, this doctrine has been applied to other limited liability enterprises, so it is no longer accurate to speak solely in terms of piercing the “corporate” veil. The veil of limited liability can be pierced, when it is appropriate to do so, for entities such as the LLC as well.

Before turning to the specifics of when it might be appropriate to pierce the veil, some general observations may be helpful. First,

1. E.g., Rounds & Porter Lumber Co. v. Burns, 216 Ark. 288, 290, 225 S.W.2d 1, 2-3 (1949). For a more detailed consideration of the history of piercing in Arkansas, the opinion in Winchel v. Craig, 55 Ark. App. 373, 380-82, 934 S.W.2d 946, 950-51 (1996), traces the progression of the doctrine in Arkansas through 1996.


4. For example, in Anderson v. Stewart, 366 Ark. 203, 234 S.W.3d 295 (2006), the court expressly held that piercing could apply to LLCs.
although the vast majority of piercing cases (in Arkansas and elsewhere) still involve corporations, there are enough opinions dealing with other forms of enterprise, and those opinions are consistent enough, to be reasonably confident that the general principles of piercing apply to more than just the corporation. Second, there has never been a successful piercing case involving a publicly held enterprise; all of the piercing cases talk about closely held businesses, and usually a very small number of active owners (often a single owner) are being pursued. Third, the doctrine of piercing can also be used to collapse related corporations and disregard the separate existence of parent and subsidiaries or even sister corporations (this is sometimes called triangular piercing). Fourth, reverse piercing is also theoretically possible, where the separate existence of the corporation or other enterprise is to be disregarded in order to enable an owner’s creditors to recover against enterprise assets or even to allow insiders to disregard the entity’s existence in a legal proceeding. Only in the case of reverse piercing do you see attempts by insiders to disregard the entity’s separate existence; traditional piercing was generally limited to outsiders. Thus, a corporate shareholder or director cannot normally pierce the veil of his or her corporation in order to have the courts disregard its legal existence, unless the doctrine of reverse piercing is invoked. Presumably, the same limitations would apply to members or managers of an LLC, or partners in an LLP, limited partnership, or LLLP.

It is also worth emphasizing that piercing is not the only circumstance under which the owner of a limited liability business such as a corporation, LLC, LLP, limited partnership (as to limited partners) or LLLP might wind up being liable for a business debt. In addition to being liable if the veil of limited liability is disregarded, business owners are also liable for their promised contributions (provided that the promise to make the contribution is otherwise enforceable). Similarly, owners can be liable if they guarantee a debt of the business. Finally, owners are liable for their own conduct, and their status as owner in a limited liability business will not shield their personal assets from liability arising out of their own misconduct. For example, if they act as agents of the business and in the course of so acting, they commit a tort, they will be personally liable for any damage they inflict. The business may also be liable, for example under the doctrine of respondeat superior, but the fact that the individual actors are corporate shareholders or LLC members will not insulate them from responsibility for their own malfeasance. Alternatively, if

5. See Scott v. Central Arkansas Nursing Centers, Inc., 101 Ark. App. 424, 434, 278 S.W.3d 587, 595-96 (2008), noting that while shareholders are “not ordinarily liable for the acts of their corporation or LLC,” they “may be liable for their own acts or conduct.”

6. The current Restatement of Agency specifies that “[a]n employer is subject to liability for torts committed by employees while acting within the scope of their employment.” Rest (3rd) Agency § 2.04. “Employer” and “employee” are terms of art, designed to replace the old fashioned language of “master and servant” that was found in earlier restatements of the law.
they act as agents for the business and fail to fully disclose the existence and identity of the principal, they can be liable as agents for an unidentified principal under traditional agency law rules.\(^7\)

The remainder of this note will provide a little more detail about the current rules applicable to traditional piercing in the corporate context (whether to hold shareholders or related corporations liable), piercing the veil as to other forms of enterprise, and finally, the doctrine of reverse piercing in Arkansas.

II. Traditional Piercing of the Corporate Veil

As alluded to in the introductory section of this note, piercing the veil is a judicially-created and defined doctrine that allows courts to disregard statutorily authorized limited liability in business enterprises in order to allow persons who are ostensibly creditors of the business to access assets of owners or sometimes related entities. Originally developed and applied in the corporate context, the rule allowed courts to pierce the veil of limited liability traditionally available to corporate shareholders when the shareholders themselves failed to respect the enterprise as a distinct legal entity. The test for piercing in a corporate context has been formulated in a wide variety of ways, often asking whether the business is so controlled by its owners that it has become the mere alter ego or instrumentality of the owners. Of course those labels do not, in and of themselves, do much to help one understand when the “corporate facade” is likely to be disregarded by the courts.

Unfortunately, it has always been extremely difficult (some would say impossible) to articulate an accurate and predictive test for when the veil of limited liability will be pierced.\(^8\) We are left with the task of searching through cases to see how similar situations have been handled in the past, and this task is hampered by the facts that many of the written opinions offer only conclusory observations rather than a helpful recital of the actual facts.

Commentators have been very active in this area, attempting to analyze and dissect the existing case law. One of the most influential and frequently cited articles was published by Professor Robert Thompson in 1991, after an exhaustive review of more than 1600 reported piercing decisions.\(^9\) Professor Thompson listed the following factors as being

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7. See, e.g., Oliver v. Eureka Springs Sales Co., 222 Ark. 94, 95, 257 S.W.2d 367, 368 (1953), applying the doctrine but using the phrase “partially identified principal,” which was not the language of the earlier restatements rather than the current Restatement (3rd) of Agency. In Beech v. Crawford, Not Reported in S.W.3d, 1999 WL 1031310 (Ark. App. 1999), the Arkansas Court of Appeals applied these principles without referring to the restatement or its terminology. The court stated: “It is the agent’s duty to disclose his capacity as agent of a corporation if he is to escape personal liability for contracts made by him, and the agent bears the burden of proving that he was acting in his corporate, rather than individual, capacity.” Id., citing 19 C.J.S. Corporations § 540 (1990). Liability was imposed because there was no evidence showing that the agent told the third party “that he was contracting on behalf of the corporation.”


most frequently cited by the courts when they were deciding whether to pierce the corporate veil: lack of meaningful separation between the shareholders and their corporation, commingling of corporate and individual assets, inadequate (or grossly inadequate) capitalization of the corporation, failure to observe corporate formalities, shareholder domination and control of the corporation, and overlap of corporate personnel and management (when multiple corporations are involved).¹⁰

The author of an earlier treatise listed these eleven factors as being the most important in determining whether, in the context of subsidiary corporations, the parent had improperly dominated the subsidiary so as to justify piercing: (1) the parent corporation owned all or substantially all of the subsidiary’s stock; (2) the parent and subsidiary had common directors or officers; (3) the parent financed the operations of subsidiary; (4) the parent caused the subsidiary to have been incorporated; (5) the subsidiary was grossly inadequately capitalized; (6) the parent paid the salaries, expenses and losses of the subsidiary; (7) the subsidiary’s assets came solely from the parent, and the subsidiary conducted business only with the parent; (8) the parent’s records referred to the subsidiary as a department or division of the parent, and the parent’s records reflected the subsidiary’s business as its own; (9) the parent used the property of the subsidiary as its own; (10) the directors or executives of the subsidiary acted on behalf of the parent rather than independently in the interest of the subsidiary, and (11) corporate formalities for the subsidiary were not observed.¹¹ The author of that treatise also suggested that it was necessary to show some sort of impropriety in order to justify piercing, and listed these seven possibilities as bases for demonstrating such wrong-doing: (1) actual fraud; (2) violation of a statute; (3) stripping the subsidiary of its assets; (4) misrepresentation; (5) estoppel; (6) torts; or (7) other cases of wrong or injustice.¹²

There are a number of piercing cases in Arkansas. Most of them have involved situations where a third party sought to pierce the veil of a corporation to reach assets of either individuals or distinct corporate entities, generally on the theory that as a result of the shareholder’s control over the corporations or the manner of operating the businesses in question, the shareholders or related corporations should also be held responsible. Arkansas courts typically state that they are “quite liberal” in protecting the limited liability of corporate shareholders, but commentators do not always agree with this assessment.¹³

10. Id. Two good, albeit older, articles with a listing of factors in other kinds of piercing cases (i.e., not necessarily involving parent-subsidiaries) are Cathy S. Krendl & James R. Krendl, Piercing the Corporate Veil: Focusing the Inquiry, 55 DENV. U. L. REV. 1, 16-17 (1978); and David H. Barber, Piercing the Corporate Veil, 17 WILLAMETTE L. REV. 371, 374-75 (1980).

11. Frederick J. Powell, Parent and Subsidiary Corporations § 6 (1931).


13. For example, one study found that in 1990 Arkansas courts pierced the veil in nearly 40% of the reported cases (or in 9 of the 23 reported cases where piercing was sought). Robert B. Thompson, Piercing the Corporate Veil: An Empirical Study, 76 CORNELL L. REV. 1036, 1039 (1991). A more recent study placed the percent at over 56%. Peter Oh, Veil Piercing, 89 TEX. L. REV. 81, 115 (2010). Another commentator concluded that while Arkansas generally follows traditional rules governing piercing, the rules are applied so that the veil of limited liability has actually been pierced more easily here and that “it is particularly dangerous to fail to adhere to corporate formalities in Arkansas.” Stephen B. Presser, Piercing the Corporate Veil, § 2:4. Arkansas.
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Early Arkansas cases suggested that piercing should only occur if “the privilege of transacting business was illegally abused to the injury of a third party.”\textsuperscript{14} Gradually, Arkansas courts began to use other language to describe piercing factors.

Perhaps the most liberal example of piercing to date can be found in a 1981 opinion from the Arkansas Court of Appeals, \textit{Humphries v. Bray}.\textsuperscript{15} In that case, the Court of Appeals pierced the veil of limited liability to hold a sole shareholder liable under the Arkansas Workers Compensation Act, apparently without any evidence of illegality or wrongdoing on the part of the sole shareholder. Technically, that Act applies only to businesses with five or more employees and the corporation in question had fewer employees. However, the sole shareholder also owned and operated two sole proprietorships, and if the businesses were considered together, there were more than five employees. The court found that none of the three businesses had more than two employees and that separate records were maintained for each of the three businesses; in its opinion it cited no evidence of any intent to circumvent application of the Workers Compensation Act. The court did note that one bookkeeper kept accounts for all three businesses, that it was sometimes difficult to distinguish between the businesses, that the businesses were all in the same building with a single sign, that the businesses had a shared listing in the phone book, that some funds were moved between businesses to meet payroll, and that employee W-2 forms did not always use the correct business names.\textsuperscript{16} Although the court in \textit{Humphries} cited language to the effect that piercing should be applied based on the circumstances of each case “when the facts warrant its application to prevent an injustice,” it offered no explanation of how piercing the veil would in fact “prevent an injustice.” Instead, the court merely offered its conclusion that “application [of the doctrine] in the instant case was warranted.”\textsuperscript{17}

One commentator has suggested that the result in \textit{Humphries} “may be to allow piercing the veil simply on the basis of a failure to adhere to corporate formalities, and without any evidence whatsoever on the part of the sole shareholder of an intent to perpetrate an injustice, wrongful act, or fraud.”\textsuperscript{18} This would be consistent with statements made in cases like \textit{Woodyard v. Ark. Diversified Ins. Co.},\textsuperscript{19} where the court stated that the veil of corporate liability could be pierced and the corporate form ignored “where fairness demands it.”\textsuperscript{20}

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  \item \textsuperscript{14} Rounds & Porter Lumber Co. v. Burns, 216 Ark. 288, 290, 225 S.W.2d 1, 2-3 (1949); Neal v. Oliver, 246 Ark. 377, 391, 438 S.W.2d 313, 320 (1969) (describing piercing as a method of avoiding “putting fiction above right and justice”); Banks v. Jones, 239 Ark. 396, 399, 390 S.W.2d 108, 110 (1965) (refusing to pierce because of lack of evidence to support a finding of illegal abuse of the corporate form to the injury of the appellant); Winchel v. Craig, 55 Ark. App. 373, 380-82, 934 S.W.2d 946, 950-51 (1996) (tracing the progression of piercing law in Arkansas through 1996).
  \item \textsuperscript{15} 271 Ark. 962, 611 S.W.2d 791 (Ark. App. 1981). \textit{Humphries} has been an influential case on Arkansas law with regard to piercing. See, e.g., Epps v. Stewart Information Services Corp., 327 F.3d 642, 649 (8th Cir. 2003).
  \item \textsuperscript{16} \textit{Humphries}, 271 Ark. at 965, 611 S.W.2d at 793.
  \item \textsuperscript{17} \textit{Humphries}, 271 Ark. at 966, 611 S.W.2d at 793.
  \item \textsuperscript{18} \textit{Stephen B. Presser, Piercing the Corporate Veil, § 2:4. Arkansas}.
  \item \textsuperscript{19} 268 Ark. 94, 594 S.W.2d 13 (1980).
  \item \textsuperscript{20} \textit{Woodyard}, 268 Ark. at 99, 594 S.W.2d at 17 (1980).
\end{itemize}
More recently, the Arkansas Supreme Court stated in *Arkansas Bank & Trust Co. v. Douglass*, that fraud or illegal acts need not be alleged; mere allegation of wrongdoing should be enough to pierce. The court in *Douglass* ignored the corporate form of a subsidiary on the grounds that it was a “mere tool” of the parent corporation, after concluding that there was sufficient evidence that the subsidiary had been established to do indirectly what the parent company could not do directly under statute.

On the other hand, there are recent piercing cases in Arkansas that suggest that fraud, illegality, or injustice is an element of piercing in Arkansas. Perhaps the leading Arkansas case suggesting that fraud or illegality is necessary in order to support an order of piercing is *Anderson v. Stewart*. Citing two earlier opinions, the Arkansas Supreme Court noted that “[i]n special circumstances, the court will disregard the corporate facade when the corporate form has been illegally abused to the injury of a third party.” The *Anderson* court then cited a legal treatise listing the following five common grounds for disregarding the corporate existence, all of which include some sort of fraud or other wrongdoing: 1) the corporate form is used to evade the payment of income taxes; 2) it is used to hinder, delay, and defraud creditors; 3) it is used to evade a contract or tort obligation; 4) it is used to evade the obligations of a federal or state statute; or 5) it is used to perpetrate fraud and injustice generally. The *Anderson* court also bluntly claimed that “Arkansas cases in which the corporate veil has been pierced have generally involved some fraud or deception.”

One of the cases cited in *Anderson, EnviroClean, Inc. v. Arkansas Pollution Control and Ecology Comm’n*, ordered piercing on the grounds that there was abuse of the corporate facade in order to circumvent regulatory limitations on the transfer of certain facilities. While it did not specifically hold that fraud was required, it did cite the same language that was relied upon in *Anderson*, to the effect that “in special circumstances the court will disregard the corporate facade when the form has been illegally abused.”

Some opinions from the Arkansas Court of Appeals have apparently embraced the notion that fraud or illegality should be re-

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22. *Douglass*, 318 Ark. at 470, 885 S.W.2d at 870.
23. 366 Ark. 203, 234 S.W.3d 295 (2006). Technically, *Anderson* involved piercing the veil for a limited liability company. However, the court relied exclusively on corporate law, did not distinguish between corporations and LLCs, and in fact (inaccurately) referred to the LLC as a corporation and its members as “shareholders.”
required in order to pierce the veil. In a very recent opinion the court refused to award piercing where there “were no allegations, much less evidence, of fraud or other abuse of the corporate form.”

30 Similarly, in *Rhodes v. Veith*, the Arkansas Court of Appeals reversed an award of piercing on the basis that the trial court had found no fraud, illegality or overreaching. The finding that there was no “illegal abuse” of the corporate form also lead the court to decline to support piercing in *Dalrymple v. Dalrymple*.

On the other hand, other opinions tend to cite both the rules that piercing should be available when it is equitable as well as stating at least a preference for a finding of fraud or wrongdoing. In one fairly recent court of appeals decision not designated for publication, the court first acknowledged that the Arkansas Supreme Court “has stated that it is a nearly universal rule that a corporation and its stockholders are separate and distinct entities, and the court will only disregard the corporate facade when the corporate form has been illegally abused to the injury of a third party.” The court then paid homage to the more liberal position, stating that “[t]he conditions under which the corporate entity may be disregarded or looked upon as the alter ego of the principal stockholder vary according to the circumstances of each case. The doctrine of piercing the corporate veil is applied when the facts warrant its application to prevent an injustice.”

If, instead of focusing on the general discussion of whether fraud or illegality is necessary, attention is turned to the actual factors that are discussed in the cases, it does appear that the three most common grounds for piercing in Arkansas are significant failure to observe formalities, substantial undercapitalization of the corporation, and/or evidence that respecting the corporate form would allow the parties to evade the requirements of law. Not all of these factors need to be present, and in most cases only one or two of these are mentioned or appear to have been a factor in the decision.

Failure to observe formalities is mentioned in a number of cases as being essential in finding that the corporate veil should be disregarded. Unreported decisions are supposed to be those that break no new ground, and perhaps it is simply that the issue appears so well settled that the courts of appeal believe that they are saying nothing new. However, some of the clearest explanations of the importance of observing corporate formalities can be found in recent opinions not designated for publication. In *Rush-Bradley v. Van Ore*, the court (after reciting precedent to the effect that fraud or illegality should be present in order to pierce the veil), focused on the fact that the shareholder “failed to scrupulously follow corporate formalities. “There were no minutes of annual shareholder meetings, and (despite the fact that the burden of proof in piercing cases is normally on the

34. *Id.*, citations to the same supreme court case omitted.
claimant, the court also relied on the fact that the shareholder “failed to introduce any financial records” proving the separate corporate existence. The court was also concerned with the omission of the word “Incorporated” from the corporation’s signs and letterhead. The corporation in that case had converted property belonging to the claimant, but the court ordered that the veil be pierced so as to permit recovery against the shareholder as well.

The Eighth Circuit Court of Appeals, applying Arkansas law in a 1988 opinion, also found that failure to observe formalities and respect the corporate accounts as assets to be used for corporate purposes alone could result in piercing.36

In addition, when the corporate formalities are observed, Arkansas courts appear reluctant to pierce the veil. In one 2010 opinion from the Arkansas Court of Appeals, the court relied on proper filing of tax returns, separate payroll records and reports, separate payments to employees, and separate workers’ compensation plans in declining to combine related corporations even though they were both owned and operated by the same person, with the same employees.37 In an earlier case,38 the court focused on evidence that the failure to observe some formalities did not justify piercing when there was evidence that “the corporation adhered to corporate formalities by keeping its own financial records and bank accounts, by filing separate tax returns, and by recording the loans made.”39 One year earlier, the court had upheld a trial court’s refusal to pierce the veil, relying on the facts that there was “no evidence that appellees failed to hold corporate meetings or otherwise disregarded the corporate form” or that the corporate account was ever used for non-business purposes.40

A second factor that appears to play a critical role in multiple reported cases is significant undercapitalization of the corporation at issue. For example in Winchel v. Craig,41 a jury verdict ordering piercing of the veil was sustained on the basis that there was substantial evidence that the shareholders took no steps to provide for the contingent liability for personal injuries, and that the shareholders terminated the business and started a new one rather than making sufficient provision for such liability.42 The court also commented on the corporation’s failure to provide insurance to cover such obligations.43 Failure

41. 55 Ark. App. 373, 934 S.W.2d 946 (1996).
42. Winchel, 55 Ark. App. at 379, 934 S.W.2d at 949.
43. Winchel, 55 Ark. App. at 381, 934 S.W.2d at 950.
to adequately fund corporate operations was also the primary concern that led a bankruptcy court to pierce the veil in an earlier opinion.\(^{44}\) The factors that indicated undercapitalization in the bankruptcy case included the fact that the corporation never turned a profit, had a negative net worth, the other shareholder-owned companies turned a profit on this corporation’s under-priced goods, and no interest was paid on accounts between the companies.\(^ {45}\)

The third factor that appears to be commonly relied upon as a justification for piercing in Arkansas is a finding that failure to pierce would allow the corporation, often the parent of a subsidiary corporation, to avoid application of a statutory or regulatory requirement. Although the court emphasized that there was no fraud or illegality, use of a corporate subsidiary to allow the parent to accomplish “indirectly what they could not do directly” was found to be sufficient grounds for piercing in *Arkansas Bank & Trust Co. v. Douglass*.\(^ {46}\) Similarly, the court in *EnviroClean, Inc. v. Arkansas Pollution Control and Ecology Com’n*,\(^ {47}\) ordered piercing on the grounds that there was abuse of the corporate facade in order to circumvent regulatory limitations on the transfer of certain facilities. *Woodyard v. Ark. Diversified Ins. Co.*\(^ {48}\) also permitted piercing in order to prevent a parent from avoiding application of statutes that would otherwise have applied to it. Interestingly, some of these opinions appear to suggest that this amounts to wrongdoing or illegality and some (like *Douglass*) simply say that this kind of “unfairness” is enough.

Obviously, the preceding cases emphasize and talk about piercing in the corporate context. The reasons for using this as the starting point are that: (1) as incomplete as it is, the Arkansas law on piercing in the corporate context is far more complete than for any other form of business; and (2) when piercing has been awarded to hold owners of other kinds of business liable, the same essential rules have been followed.

**III. Piercing the Veil of Limited Liability for other Entities**

There are only a handful of cases dealing with piercing of unincorporated entities in Arkansas, and they all appear to be focused on LLCs.

The first reported decision in Arkansas to grant piercing in the context of an LLC was *Anderson v. Stewart*,\(^ {49}\) and it would be easy to overlook this case when researching because the court keeps referring to piercing of the “corporate” veil to hold the “shareholders”...
liable. Technically, in the context of an attempt to pierce the veil of limited liability of an LLC, there is no corporation and there are no shareholders. Despite these errors in terminology, however, the analysis of the court is basically sound. As stated by the court, the issue was “whether the trial court erred in applying the doctrine of ‘piercing the corporate veil’ and holding shareholders in a limited liability company individually liable.” The court determined that the trial court’s decision to pierce “the corporate veil” to hold the individual defendants liable was not clearly erroneous because the owners did not properly maintain business records as required by the Check Casher’s Act, withdrew assets in a manner designed to see that there were insufficient assets, and arranged for the same individuals to carry on the business even after closing of the LLC. These are precisely the same kinds of issues that would lead to piercing in the corporate context—failure to observe required formalities, and evading regulatory requirements.

A more recent opinion confirms that piercing of the veil for an LLC is possible in Arkansas, but offers no explanation of the circumstances under which it is appropriate. In Marx Real Estate Investments, LLC v. Coloso, the court mentions almost in passing that the LLC’s “corporate veil” was pierced so that its owners would be “personally liable.”

There are other cases that suggest the Arkansas courts are willing to consider piercing of the veil for an LLC, such as Sherry Holdings, LLC v. Hefley, in which the basis for declining to pierce the veil of the LLC was that evidence that a single member owned the business was insufficient grounds, just as there would be insufficient grounds to pierce a corporation’s veil solely on the grounds that it had a single shareholder. In K.C. Properties of N.W. Arkansas, Inc. v. Lowell Inv. Partners, LLC, the court provides a long discussion of piercing in the corporate context before concluding that the facts then before it did not justify piercing the veil of the LLC. This was a rather stringent interpretation of the piercing doctrine since the owners of the LLC had apparently admitted in discovery that a number of formalities had been completely ignored, including failure to properly admit members, draft an operating agreement, keep books and records, maintain assets, pay for its own debts, or receive contributions.

This general approach of borrowing from corporate law in order to determine when it is appropriate to pierce the veil for unincorporated entities continues today. The underlying rationale is that LLCs are designed to be similar to corporations in many respects, and therefore the principles of corporate law should apply to LLCs in similar cases. However, the specific circumstances under which piercing of the veil is appropriate for LLCs is not as clear as it is for corporations.

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50. Arkansas courts seem remarkably consistent in speaking about the doctrine of piercing the “corporate veil” to go after an LLC’s “shareholders.” For instance, in K.C. Properties of N.W. Arkansas, Inc. v. Lowell Inv. Partners, LLC, 373 Ark. 14, 280 S.W.3d 1 (2008), the court repeatedly used this terminology in declining to pierce the veil. The same language appears in the most recent LLC piercing case as of the date these materials were prepared, Marx Real Estate Investments, LLC v. Coloso, 2011 Ark. App. 426 __ S.W.3d __, 2011 WL 2368343 (June 15, 2011) (saying only that [t]he court pierced MREI’s corporate veil to hold [its owners] ... personally liable.


57. K.C. Properties, 373 Ark. at 33, 280 S.W.3d at 16.
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rated entities is consistent with opinions on the subject from other jurisdictions. One commentator has bluntly concluded that “[c]ase law suggests that corporate law piercing principles will be applied to LLCs and there is no reason to believe that LLPs will be treated differently.”

IV. “Reverse Piercing”

Traditionally, piercing involved attempts to hold shareholders personally liable for corporate debts, even though the corporate form was supposed to offer owners protection against personal liability. As noted in the preceding materials, there are cases that have applied these rules to hold owners of other limited liability but unincorporated entities (most notably members of LLCs) personally liable. In some cases, however, the effort shifted from going after the owner of the limited liability entity, and instead has focused on holding the corporate entity liable for the personal debts of its shareholders, generally based upon a showing that the corporate entity was really the alter ego of the individual owner(s). There are only a very few reverse piercing cases applying Arkansas law.

Speaking in general terms, reverse piercing cases tend to arise in one of two different situations. “The most common reverse pierce cases involve ‘insider’ reverse piercing claims. Such claims involve a dominant shareholder or other controlling insider who ‘attempts to have the corporate entity disregarded to avail the insider of corporate claims against third parties or to bring corporate assets under the shelter of protection from third party claims that are available only for assets owned by the insider.’ Other reverse piercing cases, however, involve ‘outsider’ reverse piercing claims where third party claimants or judgment creditors with claims against a corporate insider attempt to disregard the corporate entity to reach the assets of the corporation to satisfy those claims.”

It appears that most courts dealing with a “reverse piercing” claim tend to apply the traditional veil-piercing analysis, which requires abuse or failure to respect the corporate form in a manner that results in fraud, injustice or inequity in order to order piercing of the veil. Courts are often very concerned about the rights of innocent shareholders, and may be especially reluctant to order reverse piercing if their rights might be compromised.

Perhaps not surprisingly, there are very few reported decisions in Arkansas that seem to involve claims of reverse piercing at all. In 1974, the Arkansas Supreme Court (without actually confirming that the issue before it involved a claim for reverse piercing by insiders) refused to allow shareholders to disregard the corporate existence of an entity that they had formed and in which they each owned 50%. “A corporation is an entity separate from its stockholders. The fact these stockholders each held fifty percent of the stock in the Corporation does not make it tantamount to a partnership. The corporate existence cannot be so lightly regarded by its stockholders.”


The only “express” reference to reverse piercing in a reported case from an Arkansas state court appears in a 1999 opinion from the Arkansas Court of Appeals.61 That case involved an attempt by an outsider to recover against the assets of a corporation on the basis of alleged wrongdoing by the corporate shareholder. The court specifically acknowledged that this was an attempt to obtain “a reverse piercing of the corporate veil.”62 In denying the request, the court recited the general principle that “[i]t is a nearly universal rule that a corporation and its stockholders are separate and distinct entities, even though a stockholder may own the majority of the stock.”63 Instead the court suggested that the corporate “facade” might be disregarded only in special circumstances where “corporate form has been illegally abused to the injury of a third party.”64 Based on its conclusion that there was no evidence that the corporate form had been “illegally abused,” the court declined to reverse pierce.

In Nursing Home Consultants, Inc. v. Quantum Health Servs., Inc.,65 a federal circuit court (applying Arkansas law) observed that “the ‘reverse piercing’ doctrine ... is itself controversial in that it allows corporations to be held liable for the acts of their shareholders...”66

These cases make it appear that reverse piercing could be available in appropriate circumstances, for both businesses that are organized as corporations and potentially any other unincorporated business offering its owners limited liability as well.

**Conclusions**

Piercing the veil is a doctrine that continues to arise under Arkansas law, and there have been a number of cases dealing with the issue. All too often, however, the courts provide insufficient guidance as to the precise type of behavior that will put owners of limited liability businesses at risk of losing their protection against personal liability. In advising business clients, it would seem important to warn them that they need to respect the separate existence of their business, and observe the formalities associated with having a business that is distinct from them. In addition, they should be advised that the privileges of conducting business through a limited liability entity should not be used to improperly avoid statutory or regulatory requirements, or to perpetrate a fraud or injustice on third parties. Because there is so little law on point, however, it is impossible to offer precise warnings about operational choices that are problematic. On the other hand, when seeking to fully advance the rights of claimants against limited liability entities, the doctrine of piercing (or, in appropriate cases reverse piercing) should not be forgotten.

62. Thomsen Family Trust, 66 Ark. App. at 300, 989 S.W.2d at 937.
63. *Id.*
64. *Id.*, citation omitted.