Disregarding the Corporate/LLC Veil:
The most litigated issue in corporate law

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1. Introduction

A 1991 study found that piercing the corporate veil was the most litigated issue in corporate law. Thompson, *Piercing the Corporate Veil: An Empirical Study,*76 Cornell L

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REV 1036 (1991).

Despite strong public policy favoring shareholder limited liability, creditors repeatedly try to collect corporate debts from corporate shareholders.

Generally, the law of the state of incorporation – not the state in which the shareholder or creditor resides – determines whether the corporate veil should be pierced. *Bartholomae Oil Corp. v. Booth*,146 Or 154, 28 P2d 1083 (1934); *Garetson-Hilton Lumber Co. v. Hinson*, 69 Or 605, 140 P 633 (1914). *But see* fn 2 in *Vuyksteke v. Broan*, 172 Or App 74, 17 P3d 1072 (2000)[2]. A state court does not have personal jurisdiction over a shareholder merely because the corporation did business in a foreign state. *Cannon Mfg. Co. v. Cudahy Packing Co.,* 267 US 333 (1925).

"The veil-piercing doctrine may be applied to LLCs under the same circumstances in which it is applied to corporations." *Saldaña v. Slingluff,* 2011 US Dist LEXIS 117509 (D Or 2011) (citing *BLD Products, LTC v. Tech. Plastics of Or.,* Case No. 05-556-KI, 2006 US Dist LEXIS 89874, 2006 WL 3628062 (D Or 2006). *See also Greenhunter Energy, Inc. v. W. Ecosystems Tech., Inc.,* 2014 WY 144, 337 P3d 454 (2014)*; Hector v. Mo-Dad Envtl. Serv., LLC,* 134 So3d 133 (La App 2014); *Kubican v. Tavern, LLC*, 232 W Va 268, 752 SE2d 299 (2013); *Westmeyer v. Flynn*, 382 Ill App3d 952, 889 NE2d 671 (2008)(applying Delaware law); *d'Elia v. Rice Development, Inc.*, 147 P3d 515 (Utah Ct App 2006).

2. *Amfac* test

Oregon has one of the better articulated tests for determining when the corporate form can be disregarded to impose liability on individual shareholders, a test first set out in *Amfac Foods, Inc. v. Int'l Systems & Controls Corp.*, 294 Or 94, 654 P2d 1092 (1982). As articulated in later decisions, the *Amfac* criteria are:

> There are three criteria for imposing liability on a shareholder:
>
> (1) The shareholder must have controlled the corporation.
>
> (2) The shareholder must have engaged in improper conduct in his exercise of control over the corporation; and

[2] By analogy, Oregon courts hold the law of the state of incorporation (rather than the law of the state where the action is brought) apply to issues related to whether a derivative action may be maintained. *Munson v. Valley Energy Inv. Fund, US, LP,* 264 Or App 679, 703, 333 P3d 1102 (2014); *Kollman v. Cell Tech Int'l, Inc.*, 250 Or App 163, 172, 279 P3d 324 (2012). *See also Roberts v. Triquint Semiconductor, Inc.,* 358 Or 413, 428, 364 P3d 328 (2015).

> (3) The shareholder's improper conduct must have caused plaintiff's inability to obtain an adequate remedy from the corporation. (footnotes omitted) *Rice v. Oriental Fireworks Co.*, 75 Or App 627, 633, 707 P2d 1250, 1255 (1985).

See also Acrymed, Inc. v. Convatec, 317 F Supp2d 1204, 1214 (D Or 2004).

Each of these three elements is discussed below.

3. Actual control

If a corporation or its shareholders have engaged in improper conduct (as discussed below), a creditor may be able to pierce the corporate form and impose liability for corporate debts onto those who had "actual control" over the improper conduct.

> The shareholder's alleged control over the corporation must not be only potential but must actually have been exercised in a manner either causing the plaintiff to enter the transaction with the corporation or causing the corporation's default on the transaction or a resulting obligation. Likewise, the shareholder's conduct must have been improper either in relation to the plaintiff's entering the transaction or in presenting or interfering with the corporation's performance or ability to perform its obligations toward the plaintiff. *Amfac Foods, supra*, 294 Or 94, 108-9, 654 P2d 1092 (1982).

The test for "actual control" has two prongs: the person sought to be held liable must have actual control over the improper conduct itself and actual control over the corporation as a whole. *Or Public Employees' Retirement Bd. v. Simat, Helliesen & Eichner,* 191 Or App 408, 83 P3d 350 (2004).

In a later decision, the Court of Appeals stated:

> A plaintiff seeking to hold a corporation's shareholder personally liable for a corporate debt must allege that the shareholder was in actual control of the corporation and that the plaintiff's inability to collect from the corporation is the result of the shareholder's improper conduct. *Amfac Foods v. Int'l Systems,* 294 Or. 94, 108, 654 P.2d 1092 (1982). The shareholder's conduct must have been improper either in relation to the plaintiff's entering the transaction in which the debt was incurred or in preventing or "interfering with the corporation's performance or ability to perform its obligations toward the plaintiff." *Handam v. Wilsonville Holiday Partners, LLC,* 221 Or App 493, 496, 190 P3d 480 (2008).

It bears repeating: All three prongs of the Amfac test must be present for a shareholder to be liable for corporate debts. "[N]either 'entire management' of a corporation nor ownership of substantially all of its stock constitute an adequate basis for disregarding the corporate entity." *Justin Kraft & Kraft Piano Servs., LLC v. Arden,*

2008 US Dist LEXIS 91001 (D Or 2008)(citing *Wakeman v. Paulson,* 257 Or 542, 480 P2d 434 (1971)).

> Shareholder control is necessary, but not alone sufficient to pierce the corporate veil. *Hambleton Bros. Lumber Co. v. Balkin Enterprises, Inc.,* 397 F3d 1217, 1228 (9th Cir 2005).

Simply owning 100% of the stock – without any improper conduct – alone is not enough to make the shareholder liable. *Levine v. Alpha Anesthesia, Inc.*, 145 Or App 549, 931 P2d 812.; *Miller Lumber Corp. v. Miller*, 225 Or 427, 357 P2d 503 (1961).

4. Improper conduct

Strong public policy favors the limited liability rights of shareholders, but courts will exercise their equitable powers and disregard the corporate form where fairness and justice so require. But this is an extraordinary power exercised only if there is clear evidence those who control the corporation have used the corporation to defeat justice by perpetuating fraud, improperly shielding themselves from contractual or tort responsibility or in other improper conduct.

Improper conduct can occur at formation, during operations or as creditors are beating on the door.

5. Gross undercapitalization

At one time, a corporation was required to raise a minimum amount of capital before it could begin doing business. *Statutory Minimum Capitalization Requirements*, 5 WILL L REV 331 (1969). This is no longer true in Oregon. But courts sometimes cite failure to contribute sufficient capital as one basis for piercing the corporate veil.

> It has been held that gross undercapitalization of the debtor corporation, by itself, may suffice to hold the shareholder liable to a creditor who is unable to collect against the corporation because it was inadequately capitalized. (citations omitted) *Amfac Foods, Inc. v. International Systems & Controls Corp.*, 294 Or 94, 109, 654 P2d 1092, 1102 (1982).

"The gross undercapitalization of a debtor corporation by itself could suffice to hold a shareholder liable to a creditor who is unable to collect against the corporation because of inadequate capitalization." *Stirling-Wanner v. Pocket Novels, Inc.*, 129 Or App 337, 341, 879 P2d 210 (1994).

The United States Supreme Court once stated:

> An obvious inadequacy of capital, measured by the nature and magnitude of the corporate undertaking, has frequently been an important factor in denying stockholders their defense of limited liability. *Anderson v. Abbott*, 321 US 349, 362, *rehearing denied*, 321 US 804 (1944).

In *Gardner v. First Escrow Corp.*,72 Or App 715, 696 P2d 1172 (Or 1985) involved an escrow company into which its shareholders initially contributed a mere $500, despite the fact that the corporation would be handling millions of dollars in transactions and despite the risk that the corporation's potential liabilities could be substantial. The court permitted plaintiff to recover against the shareholders and, in doing so, discussed inadequate capitalization, stating:

> Inadequate capitalization of a corporation is a form of improper conduct. Although there is no statutory minimum capitalization requirement in Oregon, a corporation must have sufficient capital to cover its reasonably anticipated liabilities, measured by the nature and magnitude of its undertaking, the risks attendant to the particular enterprise and normal operating costs associated with its business. Sufficiency of capital is measured at the time a corporation is formed and begins operations. (citations omitted) *Gardner v. First Escrow Corp.*, 72 Or App 715, 723, 696 P2d 1172, 1177-8 (1985).

See also Hambleton Bros. Lumber Co. v. Balkin Enterprises, Inc., 397 F3d 1217, 1229 (9th Cir 2005).

Another court has said:

> `Inadequate capitalization' ... means capitalization very small in relation to the nature of the business of the corporation and the risks the business necessarily entails. Inadequate capitalization is measured at the time of formation of the corporation. A corporation that was adequately capitalized when formed but has suffered losses is not undercapitalized. Whether a corporation is undercapitalized ... presents a question of fact that turns on the nature of the business of the particular corporation. *Lichtenstein v. Consolidated Services Group, Inc.*, 978 F Supp 1 (D Me 1997).

5.1. Some states do not apply gross undercapitalization

While most states recognize gross undercapitalization as a basis for disregarding the corporate form, a few do not. For example, in one Washington case noted the court knew "of no rule of law requiring a corporate stockholder to commit additional funds to an already faltering corporation." (footnote omitted) *Truckweld Equipment Co. v. Olson*, 26 Wash App 638, 618 P2d 1017, 1022 (1980). Likewise, a Georgia court held:

> Appellant readily acknowledged that the holding company was not sufficiently capitalized to begin operations; however, undercapitalization of a corporation will justify piercing the corporate veil only when "coupled with evidence of an intent at the time of the

> capitalization to improperly avoid future debts of the corporation." Here, appellant offered a valid business reason for the manner in which the acquisition was financed and gave an unrebutted explanation of the investors' capitalization plans and the ultimate failure of that effort. Thus, there is no evidence of fraudulent intent at the time of capitalization. (citations omitted) *Marett v. Professional Insurance Careers, Inc.*, 201 Ga App 178, 181, 410 SE2d 373, 375 (1991).

See also Norhawk Investments, Inc. v. Subway Sandwich Shops, Inc., 61 Wash App 395, 399-400, 811 P2d 221, 223 (1991); *Kriegman v. Schultz (In re LLS Am., LLC)*, 520 BR 841 (ED Wash 2014); *Wehlage v. Empres Healthcare, Inc.,* 2011 US Dist LEXIS 125681(ND Cal 2011).

5.2. Funds considered as part of capitalization

By "capitalization," courts are referring to the consideration paid for a corporation's shares. Of course, this includes cash and other physical property paid for the stock. It may also including intangible assets, such as an employment contract with an experienced manager and potential contracts with customers. *Murphy Logging Co. v. United States*, 378 F2d 222 (9th Cir 1967).

Some courts consider shareholder loans in determining whether or not a corporation is undercapitalized. *Hartkopf v. Heinrich Ad. Berkemann*, 200 Ga App 355, 408 SE2d 450 (1991). "A shareholder loan is deemed a capital contribution if it is made to an initially undercapitalized corporation." *Houston's Inc. v. Hill*, 111 Or App 502, 506, 826 P2d 644, 646 (1992). *See also Stumbo v. Paul B. Hult Lumber Co.*, 251 Or 20, 444 P2d 564 (1968).

Other decisions exclude shareholder loans in determining inadequate capitalization. "Under Oregon law, a loan is not a capital investment because it does not increase the corporation's worth." *XDP, Inc. v. Watumull Props. Corp.,* 2004 US Dist LEXIS 12057 (D Or 2004)

While a loan by a shareholder may be considered part of the corporation's capitalization, a loan by a third party is not because such loans do not increase the worth of a corporation. *XDP, Inc. v. Watumull Props. Corp.,* 2004 US Dist LEXIS 12057 (D Or 2004); *Gardner v. First Escrow Corp.,* 72 Or App 715, 696 P2d 1172 (1985). Therefore, a "corporation is undercapitalized if the shareholders do not place at risk assets that are reasonably related to the corporation's anticipated business and

liabilities." *Klokke Corp. v. Classis Exposition, Inc.*, 139 Or App 399, 405-6, 912 P2d 929, 929 (1996).

Appropriate insurance may be considered in determining whether a corporation is inadequately capitalized. *Klokke Corp. v. Classis Exposition, Inc.*, 139 Or App 399, 405-6, n 7, 912 P2d 929, 929 (1996).

5.3. When measured?

In Oregon, inadequate capitalization is measured at a corporation's formation or at the beginning of its operations. *Vuyksteke v. Broan,* 172 Or App 74, 17 P3d 1072 (2000); *Stirling-Wanner v. Pocket Novels, Inc.*, 129 Or App 337, 879 P2d 210 (1994); *Gardner v. First Escrow Corp.*, 72 Or App 715, 696 P2d 1172 (1985)(also significant that the defendant corporation had a long history of inadequate capitalization).

Other courts have stated that inadequate capitalization can be measured at any point in a corporation's existence. *DeWitt Truck Brokers, Inc. v. W. Ray Flemming Fruit Co.*, 540 F2d 681 (4th Cir 1976).

5.4. How much is enough?

The United States Supreme Court has indicated that the adequacy of the capitalization should be "measured by the nature and magnitude of the corporate undertaking." *Anderson v. Abbott*, 321 US 349, 362, *rehearing denied*, 321 US 804 (1944). In Oregon, adequate capitalization takes into account the assets placed at risk by the shareholders in relation to the corporation's anticipated business and liabilities. *Klokke Corp. v. Classis Exposition, Inc.*, 139 Or App 399, 405-6, 912 P2d 929, 929 (1996).

Some commentators have suggested a reasonable person standard while others have suggested a comparative analysis of corporations in the same industry. *Comment*, 14 BALT L REV 311 (1985).

In *Vuyksteke v. Broan*, 172 Or App 74, 17 P3d 1072 (2000), the Court of Appeals upheld the trial court's decision to pierce the corporate veil even though the defendant corporation had been capitalized with over $150,000; but this capital was contributed only after the corporation breached a contract – the conduct giving rise to the liability.

On the other hand, in *Hambleton Bros. Lumber Co. v. Balkin Enterprises, Inc.,* 397 F3d 1217 (9th Cir 2005), the court found that a capitalization of $2500 was alone insufficient to justify imposing the extraordinary remedy of piercing the corporate veil.

NOTE: Most cases finding an undercapitalization involve corporations initially capitalized with only a nominal sum. The corporation's $150,000 capitalization in *Vuyksteke* is at the outer edge of the capitalization cases.

The Oregon Court of Appeals has said:

> There can be no doubt that, as the trial court found, Classic was undercapitalized at its formation and continued to be undercapitalized until the Greyhound sale. A total capital of $1,000, which the shareholders may not even have paid, is completely inadequate to the magnitude and risks of the undertaking that Classic contemplated and to the normal operating costs associated with its intended business. That amount was not even an attempt to provide adequate capitalization; rather, it was the result of Classic's decision, for tax reasons, to have a merely nominal capitalization. In allowing tax considerations to control that decision, Classic exposed its shareholders to potentially unlimited liability for its normal business debts. *Klokke Corp. v. Classis Exposition, Inc.*, 139 Or App 399, 406, 912 P2d 929 (1996).

The mere fact that a corporation goes out of business and cannot pay its debts is not a sufficient basis to conclude that it was undercapitalized. *Aero Planning International, Inc. v. Air Associates, Inc.*, 94 Or App 143, 764 P2d 610 (1988).

5.5. Miscellaneous capitalization issues

In one case involving the purchase of a home from the homebuilder. After the sale, the homebuilder borrowed money from a bank and secured the loan by the purchaser's lot. At the time it borrowed these funds, the homebuilder was insolvent and unable to repay the loans. The Court of Appeals upheld the trial court's finding that this constituted improper conduct sufficient to pierce the corporation veil. *Gemignani v. Pete*, 187 Or App 584, 71 P3d 87 (2003).

Some authorities believe that a distinction should be drawn between inadequate capitalization cases involving contracts and cases involving torts. *See Amfac Foods, Inc. v. International Systems & Controls Corp*, 294 Or 94, 109, n 15, 654 P2d 1092, 1102 (1982); *Secon Service System, Inc. v. St. Joseph Bank and Trust*, 855 F2d 406, 413-4 (7th Cir 1988); Wuepper, *Piercing the Corporate Veil: A Comparison of Contract Versus Tort Claimants Under Oregon Law,* 78 OR L REV 347 (1999); Barber, *Piercing the Corporate Veil*, 17 WILL L REV 371 (1981); *Comment*, 14 BALT L REV 311 (1985).

6. Disappearing assets

Sometimes when a corporation is failing, the shareholders transfer corporate assets to themselves (or to another corporation owned by themselves) for little (or often no) consideration. Such transfers are improper. *Allen v. Meinig*, 109 Or App 341, 819 P2d 744 (1991); *Vermeer v. Dismantling Contractors, Inc.*, 90 Or 74, 751 P2d 796; *Salem Tent & Awning Co. v. Schmidt*, 79 Or App 475, 719 P2d 899 (1986).

The term "milking" is used to denote improper conduct which involves paying excessive dividends or diverting corporate assets to owners – it goes well beyond the payment of normal dividends and salaries. "Piercing a corporate veil based on "milking" of "excessive dividends" makes sense in cases of corporate manipulation where corporate assets are systematically and extensively removed from the corporation." *Hambleton Bros. Lumber Co. v. Balkin Enterprises, Inc.,* 397 F3d 1217, 1231 (9th Cir 2005).

> "Milking" has been defined as: "To deprive or defraud (a person, etc.) (from, of money, etc.), esp. by taking regular amounts over a period of time; to exploit, turn into a source of (freq. illicit) profit, advantage, information, etc.; to extract all possible advantage from." *Hambleton Bros. Lumber Co. v. Balkin Enterprises, Inc.,* 397 F3d 1217, 1230 n 11 (9th Cir 2005)(quoting IX Oxford English Dictionary 772 (2d ed 2001)).

Milking is another for of "improper conduct" which can for the basis for disregarding the corporate form.

> Shareholders have been held liable for a corporation's debts because they have milked a corporation by the payment of excessive dividends, by the sale of products to the shareholders at a reduced price, or by exacting unreasonable management charges. *Amfac, supra*, 294 Or 94, 109, 654 P2d 1092 (1982).

In *Oregon Public Employees' Retirement Bd. v. Simat, Helliesen & Eichner;* 191 Or App 408, 83 P3d 350 (2004), the court upheld a trial court finding that by transferring $1 million to themselves, controlling shareholders had "milked" the corporation because the reduction in operating capital had reduced the chances the corporation could attract additional investors and, without these additional investors, the corporation failed.

7. Commingling & confusion

"In some number of cases, shareholders have been held liable for corporate debts because of misrepresentations by the shareholder to the creditor, confusion or commingling of assets, or because the respective enterprises were not held out to the

public as separate enterprises." *Amfac Foods, supra*, 294 Or 94, 110, 654 P2d 1092, 1102 (1982).

If a corporation and its shareholder fail to act as if there is a difference between corporate property and shareholder property, courts are inclined to do the same. One court noted: "if the officer has demonstrated disregard of the corporate form, treating the corporation essentially as a conduit for personal business affairs, the court may likewise disregard the corporate entity to avoid injustice." *Weeks v. Kerr*, 486 NE2d 10, 12 (Ind App 1985).

An isolated act of commingling is not enough; there need be substantial confusion. *Aero Planning International, Inc. v. Air Associates, Inc.*, 94 Or App 143, 764 P2d 610 (1988).

> There must be such a commingling of property rights or interests as to render it apparent that they are intended to function as one, and, further, to regard them as separate would aid the consummation of a fraud or wrong upon others. *Norhawk Investments, Inc. v. Subway Sandwich Shops, Inc.*, 61 Wash App 395, 401, 811 P2d 221, 224 (1991).

See also BDL Products, LTC v. Technical Plastics of Oregon, LLC, 2006 WL 3628062 (D Or); *Salem Tent & Awning Co. v. Schmidt*, 79 Or App 475, 482, 719 P2d 899, 903 (1986).

8. Corporate formalities

While failure to observe corporate formalities (minutes, director & shareholder meetings, etc.) is often mentioned as one of the wrongs committed by a corporation which has engaged in multiple wrongs, such a failure does not appear to be reason alone for piercing the corporate veil.

> Although it would have been more orderly and businesslike, if the directors of the corporation had evidenced the understandings between the different stockholders by formal resolutions, rather than to proceed in the informal manner which they chose, nevertheless in such an instance as this, wherein all the stock of the corporation is owned by a few, and all or most of the stockholders are actively engaged in the enterprise of the corporation, it is often the practice to transact ordinary business without formal resolutions. *Roles v. Roles Shingle Co.*, 147 Or 365, 371, 31 P2d 180, 182 (1934).

See, also McMunn v. ML&H Lumber, Inc., 247 Or 319, 429 P2d 798 (1967); *Uni-Com Northwest, Ltd. v. Argus Publishing Co.*, 47 Wash App 787, 737 P2d 304, *rev den*, 108 Wash 2d 1032 (1987).

Particularly in close corporations, courts seldom rely on this ground alone. "As to

closely held corporations, in particular, action taken informally can be valid even though corporate formalities are not followed." *White v. Thatcher Financial Group, Inc.,* 940 P 2d 1034, 1037 (Colo App 1996).

> [A] failure of shareholders in a closely held corporation to strictly observe corporate formalities is not relevant to our decision of whether to pierce the corporate veil of a close corporation absent evidence indicative of and amounting to a true disregard of the corporate entity. *Consumer's Co-op of Walworth County*, 142 Wis 2d 165, 419 NW2d 211, 220 (1988).

The one corporate formality to which courts do attach particular attention, however, is the keeping of separate financial books and records. If shareholder and corporate assets are commingled, corporate creditors may be able to look to shareholder assets for repayment.

9. Violations of statute

A violation of a statute is another basis upon which courts have pierced the corporate veil.

> In a number of cases involving regulations, courts have enjoined conduct of parent corporations which, in order to evade federal or state regulation, were doing business by means of wholly-owned subsidiaries. (citations omitted) *Amfac Foods, Inc. v. International Systems & Controls Corp.*, 294 Or 94, 110, 654 P2d 1092, 1102 (1982).

For example, in *United States v. Reading Co.*, 253 US 26 (1920), the court enjoined a parent railroad company from conducting mining operations through a subsidiary. At the time, railroads were themselves legally prohibited from engaging in mining operations.

On the other hand, organizing a corporation merely to obtain a tax advantage is not improper conduct sufficient to set aside the corporate form. *El Salto, S.A. v. PSG Co.*, 444 F2d 477 (9th Cir 1971).

A discussion of the liability of parent corporations for their subsidiaries' acts under particular statutes is contained in 99 HARV L REV 986 (1986)(illegal disposal of hazardous wastes) and 35 U FLA L REV 701 (1983)(workers' compensation).

An interesting issue is whether or not a corporation may recover under an insurance policy when damages are caused by an illegal act by one of its shareholders. In an action by a corporation against its fire insurance carrier for a fire intentionally set by a 50% shareholder, the Court of Appeals held that "a corporation will not be

precluded from recovery simply because the arsonist owned fifty percent of its stock. Without evidence that the other shareholders acquiesced in the arsonist's conduct, the corporation is innocent of wrongdoing and should be allowed to recover for its loss." *Minnesota Bond Ltd. v. St. Paul Mercury Insurance Co.*, 72 Or App 187, 695 P2d 579, *reversed on other grounds*, 300 Or 85, 706 P2d 942 (1985).

10. Licensing & administrative cases

Closely related to this issue are licensing cases where the licensing authority looks through the corporate entity at a shareholder or at a predecessor corporation to determine whether to issue or revoke a license. For example, in *Palm Gardens, Inc. v. Oregon Liquor Control Commission*, 15 Or App 20, 514 P2d 888 (1974), the OLCC was permitted to look through the corporate form at past liquor violations of the principal shareholder. *See also A.J. Rose & Son, Inc. v. Board of Funeral Directors and Embalmers*, 31 Or App 537, 570 P2d 1008 (1977).

In a 2007 Oregon Supreme Court case, the Court reversed the Court of Appeals and held an affiliated corporation liable for the debts of a failed insurance company where the two corporations were under common control and had filed untimely and inaccurate reports to the Department of Consumer and Business Services ("DCBS") stating:

> Although we agree with the general statement by the Court of Appeals that one company's failure to file timely and accurate forms or to make required deposits ordinarily would not constitute the kind of improper conduct required to pierce the corporate veil, the facts in this case lead us to conclude that CCCC and SNIC, and the individuals who controlled both of those companies, took those actions to evade government regulation and deceive DCBS. *State ex rel Neidig v. Superior National Insurance Co.,* 343 Or 434, 462,173 P3d 123 (2007).

Under the Oregon tax code (ORS 317.705), parent and subsidiary corporations can treated as "unitary business" for tax purposes if among other things there is centralized management or a common executive force between the corporations. In *Rent-A-Center, Inc. v. Dep't of Revenue* (Or Tax May 12, 2014), the tax court found that having two executives of the parent serve on the subsidiary's board of directors, granting stock options to the CEO of the subsidiary in the parents stock and that the promotion of the subsidiary's CEO to become CEO of the parent was

insufficient to make the two corporations a “unitary business.”

11. Proximate cause

Injury alone is not enough to disregard the corporation. If injury alone were sufficient, the corporate form would provide little protection to shareholders because creditors of insolvent corporations are nearly always injured. To be held liable on a theory of corporate disregard, there must be some link between a shareholder's misconduct and the creditor's harm. Proximate cause is the third element of the *Amfac* test.

> Given improper conduct by the shareholder exercising control over the corporation, the plaintiff must also demonstrate a relationship between the misconduct and the plaintiff's injury. If a shareholder's improper conduct causes no injury to a corporate creditor, there is no basis for a recovery from the shareholder. Consistent with the general policy of shareholder immunity, a shareholder's improper conduct does not give a hunting license to a corporate creditor to redress a general wrong. Surprisingly, this requirement has received little express attention in many of the appellate court opinions. (footnote omitted) *Amfac Foods, Inc. v. International Systems & Controls Corp.*, 294 Or 94, 111, 654 P2d 1092, 1103 (1982).

Amfac cites two examples where the absence of a causal link prevented a creditor from recovering from shareholders: *Wakeman v. Paulson*, 257 Or 542, 480 P2d 434 (1971) and *Schlecht v. Equitable Builders, Inc.*, 272 Or 92, 535 P2d 86 (1975). In both cases, the court refused to hold a shareholder liable when the a creditor introduced insufficient evidence that the shareholder's misconduct was linked to the creditor's right to payment.

Since *Amfac*, at least five Oregon decisions have analyzed the proximate cause prong of this piercing test.

In *Gardner v. First Escrow Corp.*, 72 Or App 715, 696 P2d 1172 (1985), plaintiffs were induced to use the corporation's escrow services through the fraud of one of its shareholders. The corporation was inadequately capitalized. After a transaction resulted in plaintiffs' loss, the corporation was unable to satisfy the judgment.

> There was evidence from which the jury could have found that Daniels' and Reierson's control was exercised in a manner "either causing plaintiff to enter the transaction with the corporation or causing the corporation's default on the transaction or the resulting obligation.” Daniels negotiated the escrow services for office space agreement with Praggastis. Laeger, Praggastis' agent, was responsible for having the escrow transferred from Nevada to First Escrow. First Escrow and its shareholders had a financial interest in

> acting as escrow agent, because providing such services for Praggastis was in lieu of rent. A jury could have found that plaintiffs would not have agreed to have First Escrow close the exchange had they been aware of the relationship between First Escrow and Praggastis. Plaintiffs recovered a judgment against First Escrow. Because it has no assets, it has been unable to satisfy that judgment. A jury could have found that First Escrow's lack of assets was directly attributable to the failure of Daniels and Reierson to provide adequate capital for the corporation. (citations omitted) *Gardner v. First Escrow Corp.*, 72 Or App 715, 724, 696 P2d 1172 (1985).

In *Oregon Public Employees' Retirement Bd. v. Simat, Helliesen & Eichner;* 191 Or App 408, 83 P3d 350 (2004), the Court of Appeals upheld a trial court's finding of causation between the act of the shareholders' in transferring $1 million to themselves (thus reducing operating capital and the probability of attracting outside investors) and the collapse of the corporation.

The analysis in two cases is much briefer. In each, the court merely concluded that the improper conduct - primarily inadequate capitalization and milking - caused the plaintiff to have an inadequate remedy against the corporation. *Rice v. Oriental Fireworks Co.*, 75 Or App 627, 707 P2d 1250 (1985); *Salem Tent & Awning Co. v. Schmidt*, 79 Or App 475, 719 P2d 899 (1986). *See also Federal Savings and Loan Insurance Corp. v. Umpqua Savings and Loan Association*, 97 Or App 250, 776 P2d 24 (1989)(party's failure to allege inability to collect debt defeats claim).

In *J.C. Compton Co. v. Brewster,* 185 Or App 382, 59 P3d 1288 (2002), *other issues reconsidered and affirmed,* 187 Or. App. 709 (2003), the court upheld jury findings that there had been improper conduct, but no damages resulting from that conduct.

In addition, a federal trial court granted summary judgment on a piercing claim because there was no evidence in the record that the corporation was unable to pay the debt. *Summit Props., Inc. v. New Tech. Elec. Contrs., Inc.,* 2004 US Dist LEXIS 13053 (D Or 2004). *See also Agristor Credit Corp. v. Schmidlin,* 601 F Supp 1307 (D Or 1985).

12. Recovery may be limited to sum milked

In cases involving inadequate capitalization or milking, a shareholder's liability to a corporate creditor may be limited to no more than the amount milked

by the shareholder or to an amount no more than the difference between adequate capitalization and the amount actually contributed.

> The rule contained in the text, 294 Or at 108-09, although easily stated, may not be easily applied. The damages which flow from, say, improper capitalization or milking, may or may not be limited to the amount of the shortage of capital or amount milked from the corporation. In some cases the causal relationship will be clear. In others, the causal relationship will be less clear, but still sufficient to create a question for the trier of fact. For example, if the sole effect of a shareholder milking $200,000 from a corporation is to reduce the amount available for creditors, the shareholder's liability to corporate creditors would be limited to $200,000. (citations omitted) *Amfac Foods, Inc. v. International Systems & Controls Corp.*, 294 Or 94, 111, n 18, 654 P2d 1092, 1103 (1982).

Although *Gardner*, *Rice*, and *Salem Tent* each involved allegations of inadequate capitalization, none of these cases address the issue of whether a creditor could recovery an amount in excess of the initial adequate capitalization.

Klokke Corp. v. Classis Exposition, Inc., 139 Or App 399, 912 P2d 929 (1996), involved undercapitalization and milking. After noting that damages flowing from cases may involve "significant factual issues," the court upheld the decision of the trial court to limit damages against one shareholder to the sum improperly transferred to that shareholder alone, not the total amount milked by all shareholders.

To be held liable on a theory of corporate disregard, there must be some link between a shareholder's misconduct and the creditor's harm. Proximate cause is the third element of the *Amfac* test.

> Given improper conduct by the shareholder exercising control over the corporation, the plaintiff must also demonstrate a relationship between the misconduct and the plaintiff's injury. If a shareholder's improper conduct causes no injury to a corporate creditor, there is no basis for a recovery from the shareholder. Consistent with the general policy of shareholder immunity, a shareholder's improper conduct does not give a hunting license to a corporate creditor to redress a general wrong. Surprisingly, this requirement has received little express attention in many of the appellate court opinions. *Amfac Foods, supra*, 294 Or 94, 111, 654 P2d 1092 (1982).

In *Oregon Public Employees' Retirement Bd. v. Simat, Helliesen & Eichner;* 191 Or App 408, 83 P3d 350 (2004), the court found causation between the shareholders' act of transferring $1 million to themselves (thus reducing operating capital and the probability of attracting outside investors) and the collapse of the corporation. *See, also Gardner v. First Escrow Corp.*, 72 Or App 715, 696 P2d 1172 (1985).

In *J.C. Compton Co. v. Brewster,* 185 Or App 382, 59 P3d 1288 (2002), *affirmed,* 187 Or App 709 (2003), the court upheld jury findings that there had been improper conduct – but held that no damages resulted from that conduct.

13. Related theories

Other theories exist to allow creditors to obtain relief after a corporation fails and goes out of business.

If corporate assets have been transferred to insiders (or entities controlled by insiders), the transfer may constitute a fraudulent conveyance under ORS 95.200 *et seq; Allen v. Meinig,* 109 Or App 341, 819 P2d 744 (1991).

Sometimes when the assets of an insolvent corporation are acquired by another corporation, the acquiring corporation can become liable at least for the value of the assets acquired – maybe more. There are 4 generally accepted exceptions to the general rule that a corporation purchasing all of the assets of another corporation acquires only these assets and not the liabilities:

> To this general rule there are four well recognized exceptions, under which the purchasing corporation becomes liable for the debts and liabilities of the selling corporation. (1) Where the purchaser expressly or impliedly agrees to assume such debts; (2) where the transaction amounts to a consolidation or merger of the corporations; (3) where the purchasing corporation is merely a continuation of the selling corporation; and (4) where the transaction is entered into fraudulently in order to escape liability for such debts. *Erickson v. Grande Ronde Lumber Co.*, 162 Or 556, 568, 92 P2d 170, 174, 94 P2d 139 (1939).

See, also Tyree Oil, Inc. v. BOLI, 168 Or App 278, 7 P3d 571 (2000); *Western Helicopter Services, Inc. v. Rogerson Aircraft Corp.*, 728 F Supp 1506 (D Or 1990).

Distributions made to shareholders while the corporation is insolvent are void. *Enron Corp. v. Bear, Stearns Int'l Limited,* 323 BR 857 (SD NY 2005).; *Field v. Haupert,* 58 Or App 117, 647 P2d 952 (1982). Directors can be liable to the corporation for declaring illegal distributions. ORS 60.367(1); *Rapid Displays Inc. v. Gorder*, 155 Fed Appx 962, 2005 WL 3271355 (9th Cir 2005).

ORS 60.367 does ***not*** create an action at law by creditors against directors or shareholders for illegal distributions. *Wakeman v. Paulson*, 264 Or 524, 506 P2d 683 (1973). However, creditors may be able to impose liability upon "bad faith" shareholders and negligent directors through a bankruptcy trustee, a receiver or some other

proceeding in equity. *Id.; In re Sheffield Steel Corp.,* 320 BR 405 (NE OK 2004); *Rosebud Corp. v. Boggio*, 39 Colo App 84, 561 P2d 367 (1977).

If a dissolved corporation's assets are distributed to shareholders before payment of corporation's debts, creditors may seek satisfaction from shareholders to the extent of the distributed assets. ORS 60.645(2); *Lonsdale v. Chesterfield*, 99 Wash 2d 353, 662 P2d 385 (1983); *Fountain v. Burke*, 160 Ga App 262, 287 SE2d 39 (1982).