Piercing the Corporate Veil: Understanding the Limits of LLC Protection

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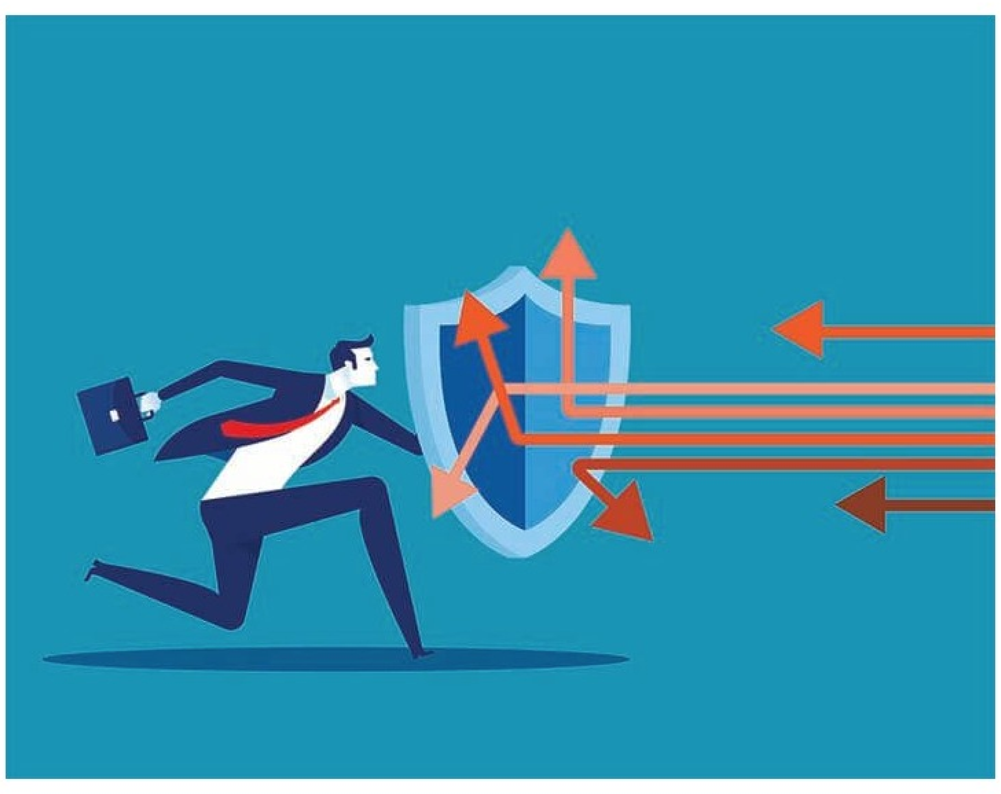
One of the most important reasons to form a limited liability corporation (LLC) is to protect yourself from personal liability for the business's debts. But that protection can disappear if you fail to separate your personal finances from those of the business. That's why simply setting up an LLC isn't a foolproof method for protecting yourself. If you don't manage your LLC properly, a person or business can come after your personal assets. This is called piercing the corporate veil.



When Creditors Can Pursue Personal Assets

There are two key situations that make it possible for a creditor to pierce the corporate veil and come after your personal assets:

1. Lack of real separation between the LLC and yourself. When you set up an LLC, it's important that you run it like a real business. The following situations place you at risk and fail to keep legal separation between you and your LLC:

- Using the LLC's bank account to pay your personal bills
- Depositing checks made out to the LLC into your personal bank account
- Failing to keep minutes and business records for the LLC
- Not creating bylaws for your LLC
- Setting up your LLC with insufficient capital

If you don't make it clear that the LLC and you are legally separate entities, you are in danger of losing the corporate veil, so be sure to observe corporate formalities.

2. Fraud or wrongful actions. If you do anything under the guise of your LLC that plays fast and loose with the law, you can jeopardize the corporate veil. Examples of such actions include:

- Taking out loans you know you can't repay
- Defrauding people or businesses
- Breaking the law

A court will have little respect for the corporate veil if your LLC disregards the law. If your LLC commits fraud, you could personally be in hot water.

How Courts View LLCs and True Separation

The corporate veil is only pierced if a court makes a determination that it should be. The court must determine that there is there no true separation between the members and the LLC and that some kind of fraud has taken place. In most situations, the court requires there to have been "serious misconduct."

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Once that determination is made, the court then allows a creditor to access the member's home, personal bank account, investments, and other assets to pay off any judgments that are entered against the LLC. All of the member's personally owned assets are then up for grabs.

When Personal Creditors Come After Your Business

Another situation to be aware of is when personal creditors access your LLC assets to satisfy your personal debts. For example, if Marco owns Cool Sunglasses LLC, which he runs as a business, but he personally goes into bankruptcy, his creditors can access his ownership interest in the LLC.

There are three ways this can happen:

- The court can order the LLC to pay the creditor any money that is due to the member from the LLC.
- The court can allow the creditor to foreclose on the LLC member's ownership portion of the LLC.
- The court can order that the LLC be dissolved.

An LLC provides important protection from personal liability, but you have to be careful to maintain a separation between your personal financial life and the LLC. By ensuring that your LLC is always acting in accordance with the law, you can ensure that you keep those protections in place.

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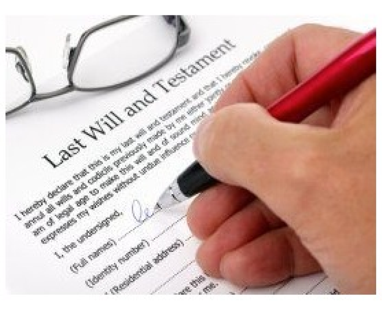

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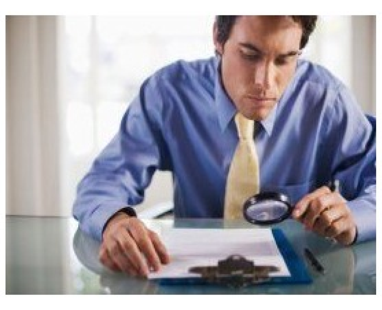

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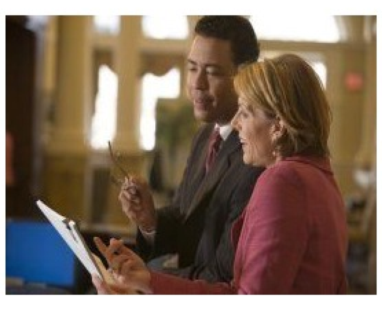

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