Bail Agents Professional Liability Insurance
PIERCING THE CORPORATE VEIL

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Some Bail Agents feel they do not need professional liability insurance (also known as Errors and Omissions, or E&O) because their firm is incorporated. They reason that—in the event of a lawsuit—their personal assets would be safeguarded behind a corporate "shield".

Unfortunately, the protections that an incorporated status can provide aren't as ironclad as one may believe. Depending on the circumstances behind the legal actions being taken, the finances of individual shareholders may still be at risk.

Rockwood Programs has asked one of the country's most prestigious law firms—Wilson, Elser, Moskowitz, Edelman & Dicker LLP—to conduct some research in to the matter. Their findings, provided under a memorandum entitled **"PIERCING THE CORPORATE VEIL"**, is provided below.

Please let the following serve as a basic overview on the topic of piercing the corporate veil. As per your instructions, we have focused our analysis on how California, Texas and Florida courts approach veil piercing. As you will see, one of the elements that courts may consider when assessing whether to pierce a corporation's veil and attach a principal's assets is whether the corporation is undercapitalized. In the context of your inquiry regarding bail agents merely closing up shop and opening elsewhere under a new name if they are the subject of an adverse judgment and uninsured, a court could look to the lack of insurance as evidence of undercapitalization and consider the undercapitalization, along with other elements, in deciding whether the corporate veil should be pierced.

We have located case law in Texas which addresses insurance in the context of undercapitalization. We also located cases in Missouri and Alaska that address this issue. Because an analysis of whether a specific corporate veil should be pierced is necessarily fact specific, and because undercapitalization is only one of the elements that courts consider when determining whether a veil should be pierced, it is not surprising that there is limited case law involving lack of insurance and undercapitalization.

Based on the research we have conducted, it is safe to say that if a bail agent is uninsured, is on the receiving end of an adverse judgment and decides to close down the business only to reopen as another, it is possible that the principal may be held personally liable for the judgment and his/her personal assets attached for purposes of satisfying the judgment.

Please let us know if you require a more detailed analysis of any of the following.

I. ELEMENTS

Under California and Florida law, the general requirements for piercing the corporate veil are essentially the same. A plaintiff is required to prove both that the corporation is a mere instrumentality or "alter ego" of the defendant and that the defendant engaged in improper conduct. Texas is slightly distinguishable. While it also recognizes the "alter ego" theory, it also abides by the "illegal purpose" theory and the "sham to perpetrate a fraud" theory.

a. California

According to Mid-Century Ins. Co. v. Gardner, 9 Cal. App. 4th 1205, 1212 (Cal. App. 3d Dist. 1992), under California law, "[t]here is no litmus test to determine when the corporate veil will be pierced; rather, the result will depend on the circumstances of each particular case. (citing H. A. S. Loan Service, Inc. v. McColgan, 21 Cal.2d 518, 523 (1943)). However, there are two general requirements, "'(1) that there be such unity of interest and ownership that the separate personalities of the corporation and the individual no longer exist and (2) that, if the acts are treated as those of the corporation alone, an inequitable result will follow.'" *Id.* at 1212 (quoting Mesler v. Bragg Management Co., 39 Cal.3d 290, 300 (1985)).

The factors to consider when assessing said requirements include:

> Commingling of funds and other assets, failure to segregate funds of the separate

entities, and the unauthorized diversion of corporate funds or assets to other than corporate; the treatment by an individual of the assets of the corporation as his own; the failure to obtain authority to issue stock or to subscribe to or issue the; the holding out by an individual that he is personally liable for the debts of the corporation; the failure to maintain minutes or adequate corporate records, and the confusion of the records of the separate entities ; the identical equitable ownership in the two entities; the identification of the equitable owners thereof with the domination and control of the two entities; identification of the directors and officers of the two entities in the responsible supervision and management; sole ownership of all of the stock in a corporation by one individual or the members of a family; the use of the same office or business location; the employment of the same employees and/or attorney; the failure to adequately capitalize a corporation; **the total absence of corporate assets and undercapitalization**; the use of a corporation as a mere shell, instrumentality or conduit for a single venture or the business of an individual or another corporation; the concealment and misrepresentation of the identity of the responsible ownership, management and financial interest, or concealment of personal business activities; the disregard of legal formalities and the failure to maintain arm's length relationships among related entities; the use of the corporate entity to procure labor, services or merchandise for another person or entity; the diversion of assets from a corporation by or to a stockholder or other person or entity, to the detriment of creditors, or the manipulation of assets and liabilities between entities so as to concentrate the assets in one and the liabilities in another; the contracting with another with intent to avoid performance by use of a corporate entity as a shield against personal liability, or the use of a corporation as a subterfuge of illegal transactions; and the formation and use of a corporation to transfer to it the existing liability of another person or entity.

[Associated Vendors, Inc. v. Oakland Meat Co., 210 Cal. App. 2d 825, 838-840 (Cal. App. 1st Dist. 1962) (citations omitted).]

However, "[t]he courts have cautioned against relying too heavily in isolation on the factors of inadequate capitalization or concentration of ownership and control." Mid-Century Ins. Co. v. Gardner, 9 Cal. App. 4th 1205, 1213 (Cal. App. 3d Dist. 1992).

b. Florida

Under Florida law, "in order to pierce the corporate veil, a plaintiff is required to prove both that the corporation is a mere instrumentality or alter ego of the defendant and that the defendant engaged in 'improper conduct.'" Priskie v. Missry, 958 So.2d 613, 615 (Fla. Dist. Ct. App. 4th Dist. 2007) (citing Seminole Boatyard, Inc. v. Christoph, 715 So. 2d 987, 990 (Fla. 4th DCA 1998)).

c. Texas

Under Texas law, the theories for piercing the corporate veil were originally set forth in Castleberry v. Branscum, 721 S.W.2d 270, 271 (Tex. 1986) as at least eight different theories; however, the Fifth Circuit combined the theories and identified three theoretical "strands." 11-165 Dorsaneo, Texas Litigation Guide § 165.01 (citing Gibraltar Sav. v. LDBrinkman Corp., 860 F.2d 1275, 1288-1289 (5th Cir. 1989)).

The strands include:

1. The **"alter ego theory,"** available when there is a true unity of identity between the corporation and another person or entity.

2. The **"illegal purpose"** doctrine includes: using the corporate fiction to evade obligations, monopolize, circumvent statutes, or justify wrongs. Here, the court focuses on the relationship between the corporation, its owners, and state laws. Gibraltar Sav. v. LDBrinkman Corp., 860 F.2d 1275, 1288 (5th Cir. 1988), cert. denied, 490 U.S. 1091 (1989).

3. The **"sham to perpetrate a fraud"** theory. Under this analysis, the concept of **inadequate capitalization** is especially important for tort claimants, and for some contract creditors, as a basis for disregarding the corporate fiction. Gibraltar Sav. v. LDBrinkman Corp., 860 F.2d 1275, 1289 (5th Cir. 1988), cert. denied, 490 **U.S.** 1091 (1989).

[11-165 Dorsaneo, Texas Litigation Guide § 165.0.]

II. UNDERCAPITALIZATION

California includes undercapitalization of corporate assets as a factor to consider when making the veil piercing determination. Texas specifically includes undercapitalization under one of its theories for establishing corporate liability. Specifically in Ramirez v. Hariri, 165 S.W.3d 912, 915 (Tex. App. Dallas 2005), the court noted the existence of liability insurance to refute the supposition that the corporation was undercapitalized. However, the court ultimately decided that though undercapitalization was a factor to consider, it could not by itself justify piercing the corporate veil.

a. Alaska

L.D.G., Inc. v. Brown, 211 P.3d 1110, 1126 (Alaska 2009)

Viewing the evidence in the light most favorable to Brown, reasonable inferences can be drawn that are sufficient to create a jury question under either veil-piercing theory. A reasonable fact-finder could infer that Gjovig (1) was the sole shareholder and officer of L.D.G.; (2) did not honor the formalities of L.D.G's corporate form, but paid employees out of his own pocket and apparently under the table; n49 (3) commingled personal and corporate funds, not only by using personal funds to pay employees but also by apparently taking corporate money for personal use without accounting for it; n50 (4) undercapitalized L.D.G., as demonstrated by his payment of employees out of his own pocket, his evident failure to obtain insurance to cover adverse judgments, and his taking corporate money for personal use without accounting for it; (5) manipulated the actual business in and out of the corporate form to both avoid tax laws and make sure that potential claimants against the bar operations would be unable to obtain a satisfiable judgment; n52 and (6) hid behind L.D.G.'s corporate form to try to avoid liability for his employees' dram shop violations.

b. Missouri

Haynes v. Edgerson, 240 S.W.3d 189, 197 (Mo. Ct. App. 2007)

Mr. Haynes moved to amend his petition to add Mr. Edgerson as a party on the theory that the corporate veil should be pierced. Mr. Haynes submits that the control of the corporation was used to perpetuate a violation of a legal duty because the corporation was undercapitalized in that it did not have sufficient insurance to cover liability. Mr. Edgerson and the Agency counter that they had sufficient insurance but that Mr. Haynes did not file his claim soon enough to meet the requirements of his insurance policy, which required the claim in this case to be filed by June 27, 2003.

Three elements are required in order to pierce the corporate veil. First, the defendant must have control and domination of the corporate entity; second, defendant must have used that control to commit fraud or violate a legal duty; third, the control and breach of duty must be the proximate cause of the injury. Mobius Mgmt. Sys., Inc. v. West Physician Search, L.L.C., 175 S.W.3d 186, 188-89. (Mo. App. E.D. 2005). The fraud or violation of a legal duty can be met by showing that the company is undercapitalized. Id. at 189. Such undercapitalization is circumstantial evidence of an improper or reckless disregard for the rights of others. Id. at 189. Inadequate capitalization is generally measured at the time of incorporation. Real Estate Investors Four, Inc. v. Am. Design Group Inc., 46 S.W.3d 51, 58 (Mo. App. E.D. 2001).

The company had no assets beyond office furniture and had insurance coverage good for only one year, and this was essentially the state the Agency was in when it was incorporated. Mr. Edgerson completed and signed the paperwork, mostly in the form of the applications for the first and second policy, and he contacted and informed Mr. Haynes about the coverage in the insurance. Mr. Edgerson admitted in his deposition that he had complete control over the corporation. Finally, because Mr. Edgerson was in control of the corporation and caused the injury to Mr. Haynes through this control, the third element is met.