

LIMITING YOUR PERSONAL LIABILITY

Although there are many advantages to forming an entity such as a corporation or limited liability company (LLC), one the most important advantage is that the owners, such as members or shareholders, of the entities are protected from personal liability, debts, or obligations of the business. Accordingly, it is important that members and shareholders must observe certain formalities with regard to both the internal operations and external appearances of the business. Failure to observe such formalities may make the shareholders or members vulnerable to the claims of creditors or potential plaintiffs who seek to "pierce the corporate veil". This can be done by claiming that the business, its shareholders or members are simply "alter egos" of one another thus making the individuals responsible for the debts, obligations or liabilities of the corporation or LLC.

The Supreme Court of Virginia has recognized that piercing the corporate veil is justified when the unity of interest and ownership is such that the separate personalities of the corporation and the individuals no longer exist. A review of case law reveals the following factors are reasons the courts will often find that the corporate entity is a mere agent of the shareholder and pierce the corporate veil:

- (a) if shareholders treat assets of the corporation as their own;
- (b) use corporate funds to pay private debts;
- (c) fail to keep separate corporate books;
- (d) fail to hold shareholders or directors meetings;
- (e) fail to issue stock; or
- (f) generally disregard corporate formalities.

The formalities that should be observed by both corporations and LLCs are relatively simple to put into practice. Internal operations can be described as the manner in which the corporation or LLC maintains its records, complies with necessary reporting requirements and conducts its financial affairs. The formalities of the external appearance generally refers to how the corporation or LLC holds itself out to the public.

In order to maximize the benefits under applicable law of operating a business as a corporation or LLC, there are a number of actions a corporation or LLC should take to protect its shareholders or members from potential liability. If you have questions on what actions to take to limit your personal liability or would like a more detailed explanation of corporate formalities please contact Sam Garbia at (703) 766-8081 or ssg@garbialaw.com.

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