Piercing the Corporate Veil: Theoretical Analysis and Empirical Evidence

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Corporate limited liability and its flip side, piercing the corporate veil, are both devices for allocating the risk of insolvency between firm owners and creditors. In this article, we make the claim that since the doctrine of corporate limited liability externalizes costs from the owners of the firm to its creditors, it is not normatively justifiable vis-à-vis creditors who were unable to charge a premium for the concomitant risk. In the theoretical part, we scan various types of owner-creditor pairs with the objective of defining the optimal risk allocation device to fit their relationship. In the empirical part, we analyze all the legal cases litigated in the Israeli courts between 2011 and 2016 where plaintiffs sought to pierce the corporate veil. We show that except in the most obvious cases (those involving fraud or overreaching), the courts frequently err in applying the theory and hence the law of piercing remains, as Judge Cardozo once remarked, "enveloped in the mists of metaphor." We conclude by offering a list of recommendations.