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The following issue is dedicated to the bright memory of the prominent representative of Georgian legal science, Professor Emeritus Guram Nachkebia

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Ana Kharaishvili *

Interrelation Between the Piercing the Corporate Veil and Limited Liability Principles in Corporate Law

The limited liability principle is one of the essential and, at the same time, most intensively discussed institutes of corporate law. The paper offers the analysis of this fundamental issue on a contextual level in system-comparative context and reveals its virtues and shortcomings in close connection with veil piercing doctrine. The liability and fate of the persons behind a juristic person, as an artificial formation created by natural persons (as a rule) on the basis of a fiction theory, has been and still is intensively discussed by legal systems of the antic world - Roman Law, Islamic Law and Italian Law of Medieval centuries on the one part and by almost every contemporary leading legal system on the other. Because of this very reason the paper provides the analysis of historical prerequisites, virtues and shortcomings, forms, preconditions, factors and challenges of practical use of these institutes in system-comparative context. All the foregoing will promote the correct practical application of characteristic for Georgian corporate law veil piercing, as an exc from limited liability rule.
Key words *- limited liability, piercing the veil, piercing, preconditions of piercing the veil, types of piercing, corporate veil, voluntary creditors, involuntary creditors.*

1. Introduction

The modern society is marked by the multiplicity and diversity of relations. Most of these relations aim at the attainment of certain result, however, quite often the initial, agreed goal of some relations fades later what, ultimately, does not lead to desirable for all the participants outcomes. In this very case the question of liability becomes particularly important - whether or not the person is responsible for the occurred consequences and to what extent. Therefore, the question of liability is one of the most complicated and multi-faceted topics for law - for the mechanism regulating the major part of the relations between the persons. In business relations this question, owing to its specificity, is moreover complicated and quite often even becomes a dilemma. In profit-oriented relations everything comes to figures, hence the parties to such relations try to explicitly identify all the possible consequences, which may occur in any direction of development of the relation. The persons make their investments and incorporate their companies in these extremely protected and guaranteed conditions. The principal instrument for the protection of the interests of the shareholders is the limitation of their responsibility through paid-in endowments.

Hence the paper aims at focusing on the purpose and essence of limited liability, as one of the fundamental principles of corporate law, reveal the mechanisms of operation of the piercing the veil doctrine as an exempted from the general rule standard. At the same time, it should be mentioned that the research also offers the overview of these two doctrines on principle level and their niche in law. Hence the piercing the veil doctrine will be analysed only in the light, that is necessary for its generalised theoretical study. Its detailed, practice-based analysis is beyond the goals and potential of this paper... The research is topical to the extent that unlike Anglo-American legal space, where the interrelation and balance between these two doctrines is fiercely debated, the Georgian legislator limits itself only to general stipulations, and neither the academic community favours the theoretical examination of this question.

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The research is mainly based on normative and comparative-law methods. The paper consists of 11 chapters and respective subchapters.

2. General Characteristic of the Principle of Limited Liability

Recent scholarship often emphasizes the divergence among European, American, and Japanese corporations in corporate governance, share ownership, capital markets, and business culture. But, notwithstanding the very real differences across jurisdictions along these dimensions, the underlying uniformity of the corporate form is at least as impressive. Business corporations have a fundamentally similar set of legal characteristics - and face a fundamentally similar set of legal problems - in all jurisdictions. Based on the foregoing the following basic legal characteristics of the business corporation can be listed, that are easily recognizable to anyone familiar with business affairs: legal personality, limited liability, transferable shares, delegated management under a board structure, and investor ownership. These characteristics respond to the economic exigencies of the large modern business enterprises and corporate law everywhere must, of necessity, provide for them. It follows that a principal function of corporate law is to provide business enterprises with a legal form that possesses these five core attributes. These are the provisions that comprise the legal core of corporate law that is shared by every jurisdiction.[1]

Limitation of liability is the basis of corporate law. Modern relations are marked by strict formation of the rights and obligations of the participants and outlining the scope of liability to the extent practicable. In any relation, and mainly in business relations, a party tries to clearly define its obligations from the very outset, as well as the scope of liability in the case of their violation nolens volens.

Relevant and important for the doctrine of limited liability is the discussion of the concepts of *entity shielding*[2] and *owner shielding*[3]. Without entity shielding a company cannot subsist as a separate juristic person. Entity shielding arises in three particular forms, namely "weak entity shielding", "strong entity shielding" and "complete entity shielding". Owing to the liability, intrinsic for a corporation, we deal with complete entity shielding. The latter protects company assets against non-company creditors, amongst them against the creditors of company owners. Hence, personal creditors of company shareholders and managers cannot have any claims against company assets, unless some relations were negotiated on behalf of the company. The concept of complete entity shielding is explicitly accepted by England, other European countries and all the states of North America, it is regarded as an unique principle qualifying company status and falls within the category of questions, which cannot be amended even by a series of agreements. Limited liability is the mirror image of entity shielding. In this context is may be called the owner (shareholder) shielding. This means that the creditors are not entitled to levy execution over personal assets of shareholders, directors and manages, apart from company assets. Like entity shielding, owner shielding may as well be strong and weak. In the latter case company creditors are able to gain access to personal assets of company shareholders in certain cases. In the case of strong owner shielding the creditors cannot claim satisfaction from their shareholders, directors or managers, apart from company assets.[4]

The concept of limited liability, as a policy question has become the basis of serious debates between the representative of the academic community. *Easterbrook* and *Fischel* support the limited liability doctrine based

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1. *Armour J., Haansmann H., Kraakman R.,* The Essential Elements of Corporate Law: What is Corporate Law? Harvard, *John M.,* Olin Center For Law, Economics, and Business, Discussion Paper №643, 7/2009, 2.
2. Entity Shielding.
3. Owner Shielding.
4. *Cabrelli D.,* The Case Against 'Outsider Reverse' Veil Piercing in Corporate law, University of Edinburgh, School of Law, Working Paper Series, №2010/03, 3-4.

on economic theory.[5] The other two, also renown scholars *Hansmann* and *Kraakman* oppose the argument of justifying the concept of *Easterbrook* and *Fischel* based on economic efficiency and propose the substitution of limited liability with *pro rata* liability for shareholders in tort creditor cases.[6]

The limited liability doctrine is the logical continuation of recognition of a corporation as an independent legal entity. Systemically the Civil Code of Georgia divides persons into two equally important types - natural persons and juristic persons. Falling within the status of a juridical person, in the meaning of Article 24 of the Code, a corporation acquires independence and separates itself from the persons who founded it; however, its purpose - to operate for the benefit of these persons, for them to profit - remains unchanged. Hence, if we presume that a corporation is founded as an independent (juristic) person and derives from other persons (both natural and juristic persons), limitation of company liability, as a person, solely to its assets, constitutes quite clear stipulation without any exemption.

For more than 150 years in the United States and Continental Europe, and for more than 100 years in England, limited liability for shareholders has been the firmly established legal principle underlying corporation law. This fundamental policy emerged after large-scale political and economic struggle. It was intended to stimulate economic activity by encouraging widespread investment in corporate shares. Such investment would result from protecting investors against liability to corporate creditors and by limiting their risk to the loss of their investment in the corporation.[7]

"I analyse my words, when I say, that in my opinion, the limited liability corporation[8] is the greatest single invention of modern times... even electricity is less important as compared with limited liability company." - Such an attitude of *Nicholas Butler*[9] and this importance of limitation of liability of the shareholders can be overenthusiastic, however not only *Butler* thought so; his contemporary *Eliot*[10] also believed, that the limitation of liability was the most distinguished and the best attribute of corporation and the most efficient legal invention of the nineteenth century.[11]

However, the problem of limitation of liability, like almost every point of law, is not explicit. Recognition of the fact, that the limited liability doctrine is the core of corporate law does not mean that there are no reasonable arguments against it. Even when this doctrine was regarded as a discovery of the contemporary life *Dewing* admitted in his book,[12] that the limitation of liability was not the necessary attributes of a corporation and constituted just one of many legal features, attribution of which to modern corporation seemed desirable only for social reasonability.[13] Discussion of the shortcomings of limited liability, as qualifying principle of corporate law becomes ever more intensive in modern legal literature. Many authors demand the abolishment of this principle with more or less persistency, however the principle of piercing the veil doctrine as the means of piercing the corporate veil and exempted rule of limited liability, has many opponents too... Eventually, the limited liability doctrine is alive and feels well irrespective or well-reasoned criticism. Upon introduction of new forms[14] of

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5 *Easterbrook* and *Fischel* have many supports who express their opinion about the doctrine of limited liability with more or less pungency. E.g. one of the authors believes, that restriction of the rule of limited liability is killing the American corporation. *Presser S.B.,* Thwarting the Killing of the Corporation: Limited Liability, Democracy, And Economics, 87 Nw. U.L. Rev. 148, 1992, 2.

6 Ibid, 424.

7 *Blumberg P.I.,* Limited Liability and Corporate Groups,11 J. Corp. L. 573 1985-1986, 33.

8 Should mean the limitation of liability of a company, in general and not a specific organisational legal form.

9 Nicholas Murray Butler, President, Columbia University, 1911.

10 *Eliot Ch.W.,* President, Harvard University, 1869-1909.

11 *Meiners R.E., Mofsky J.S., Tollison R.D.,* Piercing The Veil of Limited Liability, 4 Del. J. Corp. L. 351 1978-1979, 351.

12 *Dewing A.S.,* The Financial Policy of Corporations, 5th ed., 1953.

13 *Meiners R.E., Mofsky J.S., Tollison R.D.,* Piercing The Veil of Limited Liability, 4 Del. J. Corp. L. 351 1978-1979, 357.

14 Unlike Georgian corporate-law reality, the legislator in the Unites States of America and the EU Member States tries to create better conditions for incorporation because of many reasons and precedent, what is naturally conditioned by the

doing business almost every new form shares the concept of limitation of liability as the principal reason of their existence. This flow and development of events demonstrate, that the legislators and the policymakers of this field still appreciate the concept of limitation of liability despite the appeal of the representatives of the academic community to social expenses of this doctrine.[15] We do believe, that of essential importance here is the outcome of a specific approach and what is preferential for a specific relation when weighing up the values. *Manne* and *Posner* explain in their works,[16] that the limitation of liability doctrine may result is certain undesirable consequence for involuntary creditors.[17] Unlike voluntary creditors, who have the contractual protection mechanisms, involuntary creditors do not enjoy the freedom of selection of creditors. However, *Posner* concludes, that limited liability is socially inefficient, unfavourable status of several tort creditors[18] is overweighed by reduced transaction expenses and enhancement of investments.[19]

3. Historical Predecessors of Limited Liability Doctrine

3.1. Limited Liability Principle in Ancient Roman Law

In Roman Law relatively advanced methods were developed to limit liability in contract or for wrongful acts. The most important of the techniques employed was the institute of the so-called *peculium*, which achieved wide usage by the middle of Republican times. The *peculium* consisted of assets entrusted to a slave by his master or to a son by his father. However the *paterfamilia* still remained the owner of the assets used for *peculium.* Furthermore, where the slave, or son, traded with his *peculium,* debts and liabilities incurred in such trading could only be enforced by third parties against the master or *paterfamilias* to the extent of the *peculium*, and not against all of the latter's property. Thus, any Roman seeking to invest in a business would trade through his slave or son and limit his liability by fixing the size of the *peculium*. Over time, a new special form of action - *actio de peculio et in rem verso* - was developed for the purpose of rendering the paterfamilias liable for actions of the family subordinate. The mentioned should be made of Byzantine *chreokoinonia,* which was the most popular mediaeval contract to pool capitals in sea ventures, where the liability was limited to invested assets. It is believed, that *chreokoinonia* was a sinew of mediaeval sea trade.[20]

3.2. Limited Liability Principle in Islamic Law

As regards Islamic Law, as set forth in the *Qurān* profits went with liability, meaning that only a person willing to bear a risk of loss was entitled to claim a profit. The first technique - the "licensed slave", which resembled the Roman *peculium,* implied the engagement of a slave in business relationship under the authorisation of the master. These relationships were rather diversified. The key point here was that only the slave was responsible for claims arising from the business. If the slave was unable to satisfy the claims from his earnings, he could be sold, with the proceeds used to settle claims. A second and more important means of achieving limited liability was the *qirād*, which is not mentioned in the *Qurān*. As drawn from the other sources *qirād* was created from a profit-sharing arrangement in which a merchant would take money from his colleague - the investor in order to work with it

interests of investments and economic circulation. It was the British LTD, which provoked the implementation of legal reform in relation to a limited liability company in Germany. See: Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen (MoMiG), 23.10.2008.

15 *Millon D.,* Piercing The Corporate Veil, Financial Responsibility and the Limits of Limited Liability, Washington & Lee Public Law and Legal Theory Research Paper Series, Working Paper № 03-13, 09-2003, 3.

16 *Manne H.G.,* Our Two Corporation Systems: Law and Economics, Virginia Law Reviews, Vol. 53, 1967, №2; *Posner R.A.,* The Rights of Creditors of Affiliated Corporations, 43 U. Chi. L. Rev. 499 1975-1976.

17 Mainly a creditor in tort cases is meant, a tort creditor.

18 Tort Creditor.

19 Ibid, 359.

20 See: *Hillman R.W.,* Limited Liability in Historical Perspective, 54 Wash. & Lee L. Rev. 615, 1997, 621.

without any liability to himself. The merchant had complete discretion on trading policy, but the investor could assert control over broader matters such as the nature of goods that the merchant could buy and sell and locations where the agent could travel. Profits were evenly divided between the merchant and the investor. As so described, the *qirād* presents an interesting twist on modern limited partnership,[21] in which it is the passive investor rather than the active manager enjoyed the benefits of limited liability.[22]

3.3. Limited Liability Principle in Italian Law of Mediaeval Centuries

In Mediaeval centuries the leading role with respect to limited liability was played by *commenda* of the eleventh century Italy, which has much in common with Islamic *qirād*. It is believed, that Italian *commenda* is the transformed version of *qirād* and derives from it. It was largely used in see commerce and had the characteristics of modern limited partnership. The passive partner would provide capital to active partner (the so-called travelling, managing partner) to finance an overseas commercial venture. The active, partner, who did not necessarily provide capital, was responsible for all aspects of management of the venture; and the passive partner enjoyed limited liability.[23] As a result of this type of liability of a passive partner and consequently, the development of entrepreneurship in this form the passive partners (investors) have managed to diversify their assets and make investments into different business, what, ultimately ended up with intensive development of the economy. However, it should as well be mentioned that *commenda* was mainly used in overseas commerce, whilst for *compagnia*, used for overland trade, limitation of liability was not characteristic; although insurance had more or less similar functions here, in the combination of these two mechanisms it is still believed, that limited liability associated with the *commenda* should be regarded as the exception rather than the rule for the time.[24]

4. Economic Benefit of Limited Liability Doctrine

4.1. General

A shareholder with limited liability is an anomalous animal. He has a title, without liability with regard to this property. Allowing his existence (of this type of a shareholder) is a material divergence from centuries-standing principle of property and agreement, on which principle the growth of trade and industry depended before the introduction of the concept of limited liability. What was the reason of this assumption and what were consequences thereof?[25] The Times of London wrote on 25 May, 1824, that nothing could be so unjust as for a few persons abounding in wealth to offer a portion of their excess for the information of a company, to play with that excess

21 For Georgian corporate law space - limited partnership.

22 See *Hillman R.W.,* Limited Liability in Historical Perspective, 54 Wash. & Lee L. Rev. 615, 1997, 621.

23 Limitation of the liability of a passive partner is apparent in "The Merchant of Venice" by Shakespeare, where the merchant Antonio clearly states that he has nothing to worry about his ship due to the limitation of his liability and lesser risk.

24 See: *Hillman R.W.,* Limited Liability in Historical Perspective, 54 Wash. & Lee L. Rev. 615, 1997, 625; For better understanding of historical development of limited liability principle see: *Watson A.,* Roman Slave Law, 1987; *Johnston D.,* The Development of Law in Classical and Early Medieval Europe: Limiting Liability: Roman Law and the Civil Law Tradition, 70 Chi-Kent L. Rev 1515, 1995; *Perrot D.L.,* Changes in Attitude to Limited Liability - The European Experience, in Limited Liability and the Corporation 81, 86, 1982; *Udovitch A. L.,* At the Origins of the Western *Commenda*: Islam, Israel, Byzantium?, 37 Spectrum 198, 201-02, 1962; *Hasanuzzaman S. W.*, Limited Liability of Shareholders: An Islamic Perspective, 28 Islamic Stud. 353, 1989; *Lieber A. E.,* Eastern Business Practices and Medieval European Commerce, 21 Econ. Hist. Rev 230, 1968; *Lopez R. S.,* Italian Leadership in the Medieval Business World, 8 J. Econ. Hist. 63, 1948.

25 *Hicks J.,* Limited Liability: the pros and cons, in *Orhnial T.* (ed.), Limited liability and the corporation, London, 1982, 11.

- to lend the importance of their whole name and credit to the society, and then should the funds prove insufficient to answer all demands, to retire into the security of their unhazarded fortune and leave the bait to be devoured by the poor deceived fish.[26] Despite intensive criticism of those times,[27] there naturally exists the rational explanation for the establishment of this principle (what resulted in its unconditional spread) and the leading role in this explanation is attributed to economical benefits and the analysis of this concept. Hence the subchapters to follow will offer the analysis of the factors, which conditioned the introduction of the principle of limitation of liability into corporate law in general:[28]

4.2. Incentives for Investments[29]

Limited liability principle provides for separation and dissociation of shareholder's assets from those of the company. There is a thick and non-transparent shielding - entity shielding - between the company and the shareholders. It is impossible to overcome and pierce through this shielding except for rare exemptions. It is the limited liability doctrine that promotes passive and inexperienced investors to make investments, gain profit though dividends, alienate shares in company management without direct intervention and jeopardizing their assets. Hence, limited liability plays the role of a "capital attraction instrument." It enables companies to mobilise large capital and maximise profit.[30]

4.3. Share[31] Transferability[32]

The most important feature of limited liability is that is accommodates transferable shares. Any extension of liability beyond the assets of the firm to the personal assets of the shareholders must, in order to be enforceable, impair transferability of shares. When numerous investors cooperate in large, long-lived investment projects, free transferability of shares makes this project more desirable for them than it would have been without this assumption. The link between the liability issue and transferability of shares can easily be seen through the imagination

[26] *Halpern P., Trebilcock M., Turnbull S.,* An Economic Analysis of Limited Liability In Corporation Law, The University of Toronto Law Journal, Vol. 30, №2, Spring 1980, 117-150, 117.

[27] However, 30 years later, in 1 July edition of The Economist the principle of limited liability was analysed in quite an opposite - positive manner.

[28] Apart from general reasons, listed below, determining limited liability, the corporate law of the United States of America is marked with one historical difference from the other legal systems, what is conditioned by its federal arrangement. It is a well-known fact, that corporate law is the law of the states, meaning that each states remained free to develop its own regulation in this field. Hence each was potentially in competition with the other states to create the optimal bodies of corporate law, to ensure the best environment for the operation of the enterprises and thus increase the number of incorporations. In sum, the specific history of corporate law in the United States has had a profound effect on the development of the doctrine of limited liability. The seeds were sown for a powerful economic engine that could give stability to investors by limiting their potential liability to the assets of the corporation. Hence the maintenance of this doctrine conditions the protection of the property of the shareholders. All other things being equal, one would expect that shareholders and corporate managers would be attracted to states with strong doctrines of limited liability. There is some evidence that this is the case Delaware, the most successful jurisdiction in terms of attracting incorporators, has a particularly strong doctrine of limited liability and stringent requirements for piercing the corporate veil. Not only are there substantive barriers to imposing liability on shareholders for the actions of the corporation, but there are also procedural barriers that make it a desirable jurisdiction for both corporate shareholders and managers - *Smith D.G.,* A Federalism-Based Rationale For Limited Liability, 60 Ala. L. Rev. 649, 2008-2009, 667-669.

[29] Incentive for Investors.

[30] *Malik M.K.,* International Aspects of Corporate Law and Governance, University of Warwick, UK, partial fulfilment of the requirements of LLM for the session 2005-2006.

[31] Whereas the limitation of liability is characteristic for limited liability companies, joint-stock companies, and limited partnerships, a share for these purposes means the shareholders participation in capital and society in general.

[32] Share Transferability.

of such society, where the liability is extended to personal assets of the shareholders and where the shares are unconditionally alienable. In such and enterprise, in the eventuality of bankruptcy those partners, who have sufficient personal property for the satisfaction of creditors, would rather alienate their shares, than satisfy the interests of the creditors. The applicants for such shares would only be the pool of persons, whose property will be too minimal for the satisfaction of the creditors. Hence, when a creditor will try to gain access to personal property of the shareholders beyond the company assets, there will be the group of shareholders with such amount of assets, which will not be worth claiming. Hence, if a share is unconditionally alienable and liability extends only to the current owner, the extended liability will simply become inoperable. The simple answer to the question why opting for limited liability in this context is that freely transferable share results in *de facto* limited liability... However, it is possible to bring to effect the institute of extended (unlimited) liability trough the restriction of alienation of shares; meaning that, the company is capable of such various combinations of liability and free transferability of shares, as for unlimited liability not to become meaningless. The fact that the foregoing never happens in practice, has its explanation; specifically, extended liability results in additional costs because the circulation of assets will depend on personal property of the shareholders. This dependence makes equally important both for creditors and the shareholders to search for information about the shareholders and side-activities to control the actions of each other. Limited liability, which loosens the dependence of the company assets on shareholder's assets, is capable of reduction of the costs of transactions and search for information for all the parties and particularly in relationships, where there is a multitude of shareholders...[33] Hence, if shareholders cannot be held liable for the debts of the corporation, the wealth of individual shareholders is irrelevant in valuing those shares. As a result, each share of the corporation may be valued equally and all shares are fungible. Without limited liability, the value of shares in the corporation would not be determined by cash flows of the corporation, but rather would be dependent in part on the wealth of the shareholder that happens to hold the particular share. It is apparent that without limited liability, there would be a significant danger that organized markets could not function efficiently.[34] At the same time, this principle reduces the costs of determination of real value of the share in this light. Insofar as shares are equivalent in a company operating on the basis of the principle of limited liability, each of them has equal value what enables an investor to purchase them without searching for expensive information.[35]

4.4. Monitoring Costs[36]

It is presumed that limited liability also reduces the costs associated with shareholders' "need to monitor" the corporation. The less likely it is that shareholders will be responsible for the liabilities of the corporation, the less time and effort they must expend in ensuring that the corporation does not incur unwarranted liabilities. These cost reductions, in turn, encourage economic investment and the growth of organized markets. If limited liability were abandoned or eroded, the risk of shareholder freeriding[37] would dramatically increase. In a world in which shareholders were held responsible for the liabilities of the corporation, thereby necessitating greater monitoring of corporate activities, "only a fraction of the gains expected from effective monitoring [would] go to the monitor."

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33 *Woodward* S.E. Limited Liability in the Theory of the Firm, Journal of Institutional and Theoretical Economics, 141, 601-611, 1985, 601-602.

34 *Smith D.G.,* A Federalism-Based Rationale For Limited Liability, 60 Ala. L. Rev. 649, 2008-2009, 654.

35 *Sollars G.G.,* An Appraisal of Shareholder Proportional Liability, Journal of Business Ethics, Vol. 32, №4, Aug. 2001, 329-345.

36 Monitoring Costs.

37 "Freeriding" - literally this term means a person, who travels without tickets, contextually it refers to someone who relies on the efforts of others to benefit - *Levmore* S., Monitors and Freeriders in Commercial and Corporate Settings, 92 Yale L. J. 49, 1982, 49. In this case it means a shareholder who tries to reduce monitoring costs through monitoring activities carried out by the other shareholder without doing anything personally and carrying no expenses.

Accordingly, shareholders would have an incentive to freeride off of other shareholders' monitoring activities.[38]... shareholders would also be forced to incur the costs of "monitoring other shareholders." Because, in the absence of limited liability, the holdings of all shareholders are potentially available to satisfy any judgments against the corporation, shareholders would have an incentive to monitor the wealth of all the other shareholders to ensure that adequate funds will be available to satisfy any judgments. This might further add to monitoring costs.[39]

4.5. Facilitation of Diversification[40]

It is widely recognized that one of the virtues of limited liability is that it facilitates diversification. Without limited liability, shareholders would be unlikely to hold a wide array of stocks. Because their personal holdings would be put at risk with each corporate investment, shareholders would avoid exposing themselves to the additional risk of liability that would accompany investing in a wide range of corporations. Instead, they would seek to confine their investments to companies with which they were familiar or that were simply less costly to monitor. Critics argue that a rule of proportional liability would eliminate the need for limited liability to ensure diversification.[41]

4.6. Rejection of Risky, But at The Same Time Beneficial Projects[42]

In the absence of limited liability, corporate managers may reject projects that have a positive net present value because they are overly risk averse. According to *Easterbrook* and *Fischel*, avoiding such a problem is the real benefit of limited liability. Projects may not be undertaken solely because managers fear that the risk of potential shareholder liability for a particular project will outweigh the benefits. Under such circumstances, it is conceivable that projects may be rejected even though the benefits might otherwise outweigh the costs.[43]

5. Alternative Doctrines of Shareholders' Liability

5.1. Concept of Proportional Liability

The concept of proportional liability of a shareholder is regarded as one of the alternatives of the principle of limited liability. There are several mechanisms of its definition and operation. According to one of the versions proportional liability means personal liability of each shareholder for company debts and this liability is determined according to correlation of the share of the shareholder concerned with the other shares. Furthermore, this liability extends only to a victim of a tort, the same involuntary creditors.[44] *Sollars*[45] calls this modification the "*symmetry of gains and losses* (SGL)".[46] In his opinion, those, who have the chance to gain certain profit from the activities undertaken on their behalf, should also bear the potential losses associated with these activities. This concept is based on equity principle, it is equitable, when gains and losses associated with one and the same activity are

[38] *Smith D.G.,* A Federalism-Based Rationale For Limited Liability, 60 Ala. L. Rev. 649, 2008-2009, 654.
[39] Ibid, 655.
[40] Facilitation of Diversification.
[41] Ibid, 655.
[42] Corporate managers may reject projects that have a positive net present value because they are overly risk averse.
[43] Ibid.
[44] However, the idea of application of proportional, i.e. *pro rata* liability, even with respect to involuntary creditors, was fiercely criticised. It was presumed, that in this case problematic is the question of identification of involuntary creditors, identification of shareholders, determination of costs, etc. For details see: *Coffey M.P.*, In Defense of Limited Liability - A Replay To Hansmann and Kraakman, 1Geo. Mason L. Rev. 59, 1994.
[45] *Sollars G.G.,* Assistant professor in the Management Department of Fairleigh Dickinson University's College of Business Administration In Teaneck, New Jersey, Ph. D. from the Darden School of the University of Virginia.
[46] Symmetry of Gains and Losses (SGL).

equally borne by a shareholder. If a person does not want to bear the risk of potential loss, he may protect himself through refusing potential gain.[47] Classical and historical model of the principle of proportional liability operated in California State for a rather long period of time, in 1849-1931. It comes, that at the beginning of the twentieth century this principle was still topical against the background of the development of economic relationships and was still operable in one of the successful states in the light of doing business.

5.2. Double liability concept

For three quarters of a century - between, roughly, the Civil War and the Great Depression -shareholders in American banks were responsible not only for their investments, but also for a portion of the bank's debts after insolvency.[48] If a bank failed, the receiver[49] would determine the extent of the insolvency and then assess shareholders for an amount up to and including the par value of their stock. This system of "double liability"[50] was actively and vigorously enforced throughout the period of its existence, generating an enormous volume of litigation, including nearly fifty decisions by the United States Supreme Court and hundreds more in the state courts and lower federal courts.[51] After adopting the National Banking Act by the Congress the legislator provided, that "each shareholder shall be liable to the amount of the par value of the shares held by him, in addition to the amount invested in such shares" (according to one author, the par value of a share of most of the banks amounted to 100 USD). Apart from the protection of the interests of the creditors, the principle of double liability also protected stockholders and bank director from the engagement in hazardous operations... Senator Sherman explained that in addition to providing security for creditors, the double liability provision "tends to prevent the stockholders and directors of a bank from engaging in hazardous operations.[52]... Although this type of liability existed for quite a long period of time for banks, nowadays it is already a past and forgotten approach. Its elimination was conditioned by several factors, amongst them: ultimately, it was presumed, that it failed to protect the interests of the creditors; failed to maintain public confidence in the banking system; as a result, the growth of the number of insolvent shareholders, who no more participated in the management of failed banks, failure of the banking system for the past years and the discovery of the deposit insurance system as the better alternative for the attainment of specific goals conditioned the elimination of the principle of double liability.[53] However, some scholars still believe, that American Banking policy picked up the wrong course when eliminated double liability and introduced deposit insurance instead of it.[54]

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47 *Sollars G.G.,* An Appraisal of Shareholder Proportional Liability, Journal of Business Ethics, Vol. 32, № 4, Aug. 2001, 334.

48 Although a bank is a somewhat different and special entity in corporate law, the corporate-law liability of banks will also be shortly discussed as it is important to analyse all the forms of corporate-law liability and its historical types in this part of the paper.

49 Here a creditor should be meant in the broad sense of the word - the one, who is entitled to receive something from the bank, as from the debtor.

50 Double Liability.

51 *Macey J.R., Miller G.P.,* Double Liability of Bank Shareholders: History an Implications, Yale Law School Faculty Scholarship Series, 1-1-1992, 31.

52 Senator's opinion was later proved by empirical researches. *Grossman R.S.,* Fear and greed: The Evolution of Double Liability in American Banking, 1865-1930, Explorations in Economic History 44, 59-80, 2007, 62

53 For details about double liability principle and the reasons that conditioned its elimination see: *Marquis R.W., Smith F.P.,* Double Liability for Bank Stock., The American Economic Review Vol. 27, №3, Sep., 1937, 490-502; *Grossman R.S.,* Fear and greed: The evolution of double liability in American banking, 1865-1930, Explorations in Economic History 44, 59-80, 2007; *Macey J.R., Miller G.P.,* Double Liability of Bank Shareholders: History an Implications, Yale Law School Faculty Scholarship Series, 1-1-1992; *Grossman R. S.,* Double Liability and Bank Risk Taking, Journal of Money, Credit and Banking, Vol. 33, №2, Part 1, May 2001, 143-159.

54 In their opinion (meaning *Jonathan Macey* and *Jeffrey Miller*) the concept of double liability is the best method to give incentive to managers to minimise hazardous activities to balance the problem of ethical hazard. *Blumberg P.I.,* Blumberg on Corporate Groups, 2nd ed. Vol. 3, 122-60.

6. General Overview of the of Piercing Liability Doctrine

"*Piercing* seems to happen freakishly. Like lightning, it is rare, severe, and unprincipled. There is a consensus that the whole area of limited liability, and conversely of piercing the corporate veil, is among the most confusing in corporate law."[55] It is believed, that predictability and consistency[56] is one the main goals of modern jurisprudence. These twin principles, which stem bask from the period of *Magma Carta,*[57] underlay the doctrine of *stare decisis*[58] case-law. Predictability and consistency in judicial judgments are important for obvious reasons. They promote public confidence in the law; foster certainty; enhance stability in the law; create efficiency; promote unbiased, meritorious decisions; and encourage judicial restraint. However, predictability and consistency are particularly important in the context of business law, an in this realm they encourages citizens to conduct business, leading to a more viable economy. Inversely, unpredictability and inconsistency discourage business by generating a lack of reliance. These integral twin principles do not exist in the piercing doctrine. Instead, as stated earlier, the piercing doctrine operates in a factually intensive vacuum that is wholly removed from traditional notions of *stare decisis*. The most of the current piercing formulations provide an extraordinary degree of discretion to the judiciary, thus stepping away from the above mentioned principles. Consequently, a number of scholars work on a variety of mechanisms to alleviate the predictability and consistency problem.[59]

The leading argument in the criticism of limited liability doctrine is unfair position of involuntary, tort creditors, in contrast to voluntary, contractual creditors, which have certain protective mechanisms at their disposal and are in the position to determine the terms and conditions of the contract. A creditor is very restricted in tort relations. Actually, he "involuntarily" got involved into these relations and he is blocked by insuperable shielding of the corporation as a separate entity when he tries to find a fair escape from these relations... It is believed, that historically doctrine was meant to protect the shareholders from corporate contract liability and claims brought by voluntary creditors. The rule that was efficient for contract creditors was, it appears, simply adopted for both, without much concern about the possibility of distinguishing between the two. Hence several authors[60] support the elimination of limited liability in the case of corporate torts[61]... Hence corporate and tort law created a certain exemption from limited liability of a shareholder and then developed this exemption into the veil-piercing doctrine. However, irrespective of the use of this doctrine in tort cases, its unconditional application in mass and large-scale torts (like, environment) is devoid of any logic. It is largely disputed whether who bears the burden in this case. Striking a balance between a tort victim (creditor) and shareholders requires specific analysis and assessment of potential of diversification, risk and transaction costs.[62]

The commentators are unanimous that the main purpose of veil-piercing doctrine is the reinstatement of equity. However, the notion of equity is one of the most problematic and hard-to-defined concepts of law. Hence the enforcement of piercing by judiciary to this end and under this motivation will always give rise to disputes

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55 *Easterbrook F.H., Fischel D.R.,* Limited Liability and the Corporation, 52 U. Chi. L. Rev.,1985, 89.

56 Predictability and Consistency.

57 The doctrine was then transformed to the United States.

58 Stare decisis - "keep to the determined decision and maintain the calm" - the doctrine according to which the courts are required to abide by the case-law of the supreme court.

59 See *Marcantel J.A.,* Because Judges are not Angels Either: Limiting Judicial Discretion By Introducing Objectivity Into Piercing Doctrine, Kansas Law Review, Vol.59, №2, 2011, 12-15.

60 *Hansmann H., Kraakman R.,* The End of History Corporate Law, 89 Geo. L.J., 439, 2001, 466-67.

61 *Kahan D.R.,* Shareholder Liability for Corporate Torts: A Historical Perspective, The Georgetown Law Journal, Vol. 97:1085, 1087.

62 See *Alexander J.C.,* Unlimited Shareholder Liability Through a Procedural Lens, 106 Harv. L. Rev. 387, 1992, 3. We will not further concentrate on the aspects of competition of corporate and tort law at federal and state levels as these issues is not relevant for Georgian corporate law.

and difference of opinions. It is far easier to develop such a doctrine in Anglo-American case-law, to interpret it on a case-by-case basis and even to change the direction according to the circumstances of the case, but the foregoing seems more or less complicated for the legal system of continental law owing to its specific nature…. In one of the cases[63] the English court explained that the court will use its powers to pierce the corporate veil if it is necessary to achieve justice irrespective of the legal efficacy of the corporate structure under consideration. Also, it is asserted in the judgment, that in the exercise of a discretion in relation to injunctive relief 'the eye of equity' can, I think, look behind the corporate veil in order to do justice.[64]

These days, veil piercing is allowed and imposed only under exceptional circumstances in English courts. However, until the late 1970s, the courts demonstrated considerable willingness to pierce the veil when justice so required. In this context most notable is the single economic unit theory, propounded by Lord Denning,[65] which allows a court to treat a corporate parent and its wholly owned subsidiaries as a single entity, a theory that would be considered expansive even under U.S. law.

7. Types of Veil Piercing

7.1. According to Subjects

According to subjects, there are two main types of piercing: the first is one in which the separate corporate personality is disregarded and the shareholders are held liable for the corporation's debts. Such cases may be called shareholder liability cases. There are the other types of corporate veil cases in which separate corporate personality is disregarded without the imposition of shareholder liability. In these cases, as a general rule, the court ignores a subsidiary as a separate legal entity, does not recognise it as a separate legal entity to allow a court to exercise jurisdiction over the corporate parent. Such cases in judicial practice are called the cases of a separate legal entity. It is worth mentioning, that while the bulk of the corporate veil cases in the United States have been shareholder liability cases, shareholder liability is rarely imposed in the English cases.[66]

7.2. According to Forms

In addition to the above gradation the literature[67] is aware of different classification of piercing. Specifically, according to form, there are the following cases of piercing: 1) tort versus contract cases, 2) horizontal versus vertical piercing cases, 3) reverse piercing cases and 4) triangular piercing cases. Piercing in tort and contract cases concerns the liability arising from contract relations between a company and a creditor on the one hand, and on the other the liability, arising from inflicting damage; Horizontal piercing involves a plaintiff's attempt to pierce the veil of one subsidiary to reach the assets of another subsidiary. For example, a corporation A, a parent corporation, owns shares in three subsidiary corporations, B, C, and D. A horizontal piercing claim would involve a plaintiff attempting to pierce the veil of B to attack the assets of C. Hence, the plaintiff attempts to simultaneously attack two corporations of equal power. Consequently, this type of piercing is called horizontal piercing. As regards ver-

[63] In re a Company.

[64] Atlas-Maritime Co. v. Avalon Maritime Ltd., - *Cheng T.K.,* The Corporate Veil Doctrine Revisited: A Comparative Study of the English and the U.S. Corporate Veil Doctrines, Boston College International and Comparative Law Review, Vol. 34, Issue 2, Art. 2, 5-1-2011, 354.

[65] Single Economic Unit Theory.

[66] See *Cheng T.K.,* The Corporate Veil Doctrine Revisited: A Comparative Study of the English and the U.S. Corporate Veil Doctrines, Boston College International and Comparative Law Review, Vol. 34, Issue 2, Art. 2, 5-1-2011.

[67] The further types and forms of piercing the veil are discussed according to *Marcantel's* work: *Marcantel J.A.,* Because Judges Are Not Angels Either: Limiting Judicial Discretion By Introducing Objectivity Into Piercing Doctrine, Kansas Law Review, Vol. 59, № 2, 2011.

tical piercing, it occurs when a plaintiff attempts to pierce through the corporate shield of a subsidiary to reach the assets of a parent. Unlike the previous case the plaintiff is now attempting to pierce an inferior corporate entity - a subsidiary - in an attempt to reach the assets of a superior corporate entity - the parent. This type of piercing is called vertical one; Reverse piercing cases[68] can occur both in cases of shareholder's liability and cases of separate corporate entity discussed above. In the common corporate context where there is a single corporate entity and a number of shareholders, a reverse pierce would be an attempt by the plaintiff to pierce through the shareholder to reach the corporation, the assets of the corporation. In the cases of separate corporate entity, in the context of a multicorporate structure, a reverse pierce would occur where a plaintiff attempts to pierce a parent to reach a subsidiary, the assets of a subsidiary. Triangular piercing cases are the most complicated of the piercing structures. They can arise from tort or contract cases, have elements of horizontal and vertical structures, and involve reverse piercing. Ultimately, Triangular piercing cases exist where a plaintiff attempts to pierce a parent corporation to reach a shareholder of the parent, in an attempt to reach an otherwise unrelated corporation of which the shareholder owns an interest. Thus, imagine a parent company, A, is solely owned by a shareholder, B. Furthermore, imagine that B owns shares in an unrelated corporation, C. Now imagine that while the plaintiff has only dealt with A and B, the plaintiff has had no direct relationship with C. Nevertheless, both A and B are insolvent. Thus, the plaintiff seeks to pierce A to reach B to reach C. This, of course, forms a triangle, giving rise to the name.

8. Main Factors of Piercing the Veil

In one of the cases[69] the California Court of Appeals offered the exhaustive list of preconditions for referral to piercing the veil: 1. 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 uses; 2. the treatment by an individual of the assets of the corporation as his own; 3. the failure to obtain authority to issue stock or to subscribe to or issue the same; 4. the failure to maintain minutes or adequate corporate records, and the confusion of the records of the separate entities; 5. sole ownership of all of the stock in a corporation by one individual or the members of a family; 6. the use of the same office or business location; 7. the employment of the same employees and/or attorney; 8. the failure to adequately capitalize a corporation; 9. the total absence of corporate assets, and undercapitalization; 10. he use of a corporation as a mere shell, instrumentality or conduit for a single venture or the business of an individual or another corporation; 11. the concealment and misrepresentation of the identity of the responsible ownership, management and financial interest, or concealment of personal business activities; 12. the disregard of legal formalities and the failure to maintain arm's length relationships among related entities; 13. the use of the corporate entity to procure labour, services or merchandise for another person or entity; 14. 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; 15. 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; 16. the formation and use of a corporation to transfer to it the existing liability of another person or entity; 17. the holding out by an individual that he is personally liable for the debts of the corporation; 18. the identical equitable ownership in the two entities; 19. identification of the directors and officers of the two entities in the responsible supervision and management; 20. the identification of the equitable owners of the two entities with the domination and control of the two entities.[70]

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[68] Reverse piercing is also called as voluntary piercing, because in most cases a shareholder instigates this type of liability himself. *Cheng T.K.,* The Corporate Veil Doctrine Revisited: A Comparative Study of the English and the U.S. Corporate Veil Doctrines, Boston College International and Comparative Law Review, Vol. 34, Issue 2, Art. 2, 5-1-2011, 371.

[69] *Assoc. Vendors, Inc. v. Oakland Meat Co.*, 26 Cal. Rptr. 806, 813-815 (Ct. App. 1962).

[70] There are numerous piercing the veil tests in American and English judicial practice (judicial practice identifies some 85 potential factors, which are categorised according to several groups. *Millon D.,* The Still-Elusive Quest to Make Sense of

9. Criticism of Veil-Piercing

Three prominent theories exist for elimination of the doctrine: the Bainbridge Proposal, the Mandatory Insurance Proposal, and the Mandatory Capitalization Proposal… Professor *Bainbridge* has been an outspoken critic of the piercing doctrine[71] and has explicitly advocated its abolition for two reasons: first, he posits that the doctrine is unprincipled and uncontrollable and second, he argues the doctrine has predictability costs without serving any policy goals. As to the first reason, the author argues that veil piercing lacks any objective criteria and are mostly composed of a variety of factors that a court, retrospectively, will review to determine whether piercing is appropriate in a case concerned. This obviously leads to uncertainty and unpredictability from a corporate planning perspective. The problem becomes particularly exacerbating when courts seize on one aspect of the factors test and consider it dispositive, even when that aspect, standing alone, is simply a common virtue of even legitimate corporations. As to the second reason, Professor Bainbridge argues that this unpredictability has social costs without any social benefit.[72] As regards mandatory insurance approach, the concept behind it, that a corporation, as a matter of legislative requirements, should always carry "sufficient insurance, aiming at the protection of creditors' interests"… However, this approach was also heavily criticised as a factor obstructing the incorporation of a corporation, because a new corporation may fail to secure adequate insurance.[73] It seems, that those corporations who do nothing wrong and unlawful would pay enhanced premiums for insurance they do not need to pay as a result of those who game the system by engaging in risky conduct. From a public policy perspective, this result is undesirable.[74] The mandatory capitalization, or the same mandatory minimal capital doctrine is one of important and disputed aspects of corporate law, and in this context is the means of satisfaction of creditors' claim in the event of liability… However, this concept is also widely criticizes, as a regulation creating a barrier to incorporation.

10. Perspective of Application of Piercing the Veil Doctrine in Georgian Corporate law

In our opinion, granting such wide discretion to the court in Georgian corporate law and respectively in business environment to pierce the corporate veil - as to the provision created by the heavy hand of the legislation, characteristic for the countries of Continental Europe - is not justified, even under the pretext of equity. As already mentioned, one of the leading motives of application of veil piercing doctrine in tort-based relations in

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Veil-Piercing, Texas Law Review See Also, Vol. 89:15, 2009, 16); however, owing to specific features of Anglo-American legal system, they are not exhaustive. Almost in every case judges try to develop the perfect test of piercing the veil. Worth mentioning is the first attempt of the English judge, *Atkinson* to determine the 6 criteria of piercing the veil in one of the cases (*Smith, Stone & Knight Ltd. v. Birmingham*, 1939, 4 ALL E.R. 116(K.B.) at 121 Eng); Also interesting is *Frederic Powerll's* three tests of piercing in parent-subsidiary relationships (see *Powell F.J.*, Parent and Subsidiary Corporations, 1931). The list of piercing the veil criteria cannot be exhaustive also due to the fact, that when making a decision about piercing the veil the American courts (unlike the English courts) take account of the trends and factors of general policy with regard to specific fields of law (e.g. labour and tax law). Hence the thorough study of the case-law may provide for a very large list, consisting of many items, but this paper aims at focusing on the interrelationship between limited liability and piercing the veil doctrines, hence the paper does not discuss in details *alter egos, instrumentality* and other theories, providing for piercing the veil, with their benefits and shortcomings. The above listed criteria of California Appeals Court more or less concern every thesis, that is relevant in the case of piercing the veil, hence this time we limited our research only to general review because, at in the case concerned we need them with regard to the discussion of the attributes of a legal entity.

[71] See *Bainbridze's* works on this issue: *Bainbridge S.M.,* Abolishing Veil Piercing, 26 J. Corp. L. 479 (2001); *Bainbridge S.M.,* Abolishing LLC Veil Piercing, University of Illinois Law Review, Vol. 2005 №1.

[72] *Marcantel J.A.,* Because Judges Are Not Angels Either: Limiting Judicial Discretion By Introducing Objectivity Into Piercing Doctrine, Kansas Law Review, Vol. 59, № 2, 2011, 16.

[73] *Wix G.W.,* Piercing the Corporate Veil: Should Michigan Consider Statutory Solutions? 79 U. Det. Mercy L. Rev. 637, 9.

[74] *Marcantel J.A.,* Because Judges Are Not Angels Either: Limiting Judicial Discretion By Introducing Objectivity Into Piercing Doctrine, Kansas Law Review, Vol. 59, № 2, 2011, 19.

Anglo-American legal system is the restitution of justice; it should be mentioned that perception of justice is particularly intensified in such cases as a tort creditor is an involuntary creditor and has not gone through the phase of negotiation of contract terms and conditions with the company. Hence, piercing the veil in tort cases *prima facie* seems more equitable. However, we believe, that this should not be acceptable for Georgian reality. Despite the grave condition of a victim of tort, this should not become the factor conditioning and influencing the piercing of corporate veil in a specific case. Here the starting point is the principle of principles, characteristic for corporate law - the status of a corporation, a separate person, a separate legal entity. A creditor, be it a contract or tort creditor, enters into relationship (either voluntarily or involuntarily) with a specific entity, who has all the characteristics of an entity. And the motivation that is was created by specific persons (founders) can in no way become the factor influencing piercing the veil, even in the case of a tort victim. But in cases when actually there is no person, with the attributes of a legal entity, one should not speak about any kind of veil-piercing - as the existence of a legal entity is itself doubtful. Closer scrutiny of the above list of the factors of piercing the veil will demonstrate, that almost every point explicitly speaks for the absence of some important attribute of a separate formation, legal entity. e.g. separate assets, record-keeping, management, personnel. Hence, if in a specific case a company fails to meet these criteria, there does not exist a corporate veil, as an object of piercing, as there is no *de facto* corporation and the society is misled. I.e. the function of the court is to establish on a case-by-case basis, whether it is dealing with a skeleton, devoid of content. If it is proved, that this is the case, it means that the company has never acquired the status of limited liability as it is not a company in fact and nothing is to be pierced… The fact, that limited liability stems from and is actually conditioned by the status of a legal entity is also proved by the situation, that piercing the veil is applied only in cases, when the existence of a company as a separate person becomes doubtful. It is quite natural - if the existence of a legal entity (with all its characteristics) is not doubtful, it is apparent for everyone, that the company is an independent person and irrespective of whether or not it is financially successfully, it is clear from the very outset, that no other person, even its founder (or a person, who joined it later), be it a natural or juristic person entity, is not liable for their liabilities. It should be mentioned, that the status of a corporation as a separate and independent person was first admitted in the renown case from judicial practice of Great Britain - *Salomon v. Salomon*.[75] Lord Summers interpreted this precedent in one of the cases[76] in the light of liability: "Between the investor, who participates as a shareholder, and the undertaking carried on, the law interposes another person, real though artificial, the company itself, and the business carried on is the business of that company, and the capital employed is its capital and not in either case the business or the capital of the shareholders. Assuming, of course, that the company is duly formed and is not a sham…the idea that it is mere machinery for affecting the purposes of the shareholders is a layman's fallacy. It is a figure of speech, which cannot alter the legal aspect of the facts." The law can say, "Treat your subsidiary like an independent, profit-making enterprise, and we will give you limited liability. That is what we ask of other corporations, and we ask it of you, too."[77]

11. Conclusion

The Law of Georgia on Entrepreneurs provides for a general rule, that a special partner of a limited partnership, a shareholder of a limited liability company, a joint-stock company and a cooperative are not liable to creditors for company debts.[78] As regards piercing the corporate veil doctrine, the Law offers its most general and prima facie passive definition. A limited partner of a limited partnership, partners of a limited liability company, a joint-stock company and a cooperative are personally liable to company creditors in the event they abuse the legal forms of limitation of liability.[79] The scope and depth of development of the doctrine within Anglo-American legal system

[75] *Salomon v. Salomon & Co. Ltd* AC 22, 1897.
[76] *Gas Lighting Improvement Co Ltd v IRC* AC 723, 1923.
[77] *Rands W.J.,* Domination of a Subsidiary By A Parent, Indiana Law Review, Vol. 32:421, 1999, 456.
[78] Law of Georgia on Entrepreneurs, 28 October, 1994 3.4.
[79] Ibid, 3,6.

in this light was clearly demonstrated above. Limited liability doctrine and the concept of piercing the veil in connection with the former have taken a very remarkable rout of development in this legal system. Worth mentioning are the variations of approaches to these two controversial doctrines from the end of the nineteenth century until present days, or to be more precise, to piercing the veil as the exemption rule of limitation of liability. Initially, the limitation of the shareholders's liability to their endowments to the corporation was considered as a magnificent achievement of legal intercourse; later the development of relationships and social environment brought the interests of a creditor to the forefront; the accumulated judicial practice conditioned the actualization of the question of combination of the absolute nature of limited liability - insuperable to a certain extent restriction for creditors, with fair legal and economic intercourse. Hence the courts started to intensively pierce the corporate veil, what conditioned considerable development of this doctrine both in court-rooms and academic works. As regards the present days, they are apparently marked with toughening of the criteria of overcoming corporate form and exceptional care in application of the piercing of the veil doctrine.

Such development of legal forms of doing business was inconceivable for Georgia, as a former Soviet country due to historical reasons. After gaining independence, the Law of Georgia on Entrepreneurs, adopted in 1994, introduced limited liability as the milestone of corporate law from the very outset; it also provided for the provision about piercing the corporate veil (3.6), but with general and ambiguous stipulation. This general stipulation should better refer to cases when a creditor requests piercing the corporate veil of a company to access personal assets of the shareholders. As regards the other type of piercing the veil, characterised with greater number of disputes and case-law in legal systems, meaning parent-subsidiary relationship, Georgian Law says nothing about it. However, the practice gradually becomes aware of the cases of transferring assets from a company to a subsidiary without liabilities; this particularly concerns the construction business. Hence although the promotion of launching the economic activity and simplification of statutory requirements with this regard (meaning the elimination of statutory minimal authorised capital, optional nature of most rules of law, etc.) is of particular importance for Georgia as a newly-democratic country, again to ensure the fair economic environment, provision of creditors with such protective mechanisms, that are prescribed by the economic and legal systems of leading countries, should also be topical.

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