HANSU REAL ESTATE COMPANY TAX | IP 20 YIL YEARS

PIERCING THE CORPORATE VEIL

1. Introduction

Before explaining the concept of piercing the corporate veil, it is necessary to mention the concept of persons in law. In the legal order, persons are divided into real and legal persons. The term that legally defines the period from one's mother's womb to death, provided that the person is born and alive, is called a real person. In the case of legal personality, it may be that people come together to fulfill their commercial and social goals and use their goods for this purpose. Legal persons are entities coming to life in that way, emerging independently of people.

The general rule in Turkish Commercial Law and Enforcement and Bankruptcy Law is that the legal entity itself is responsible for the business and transactions of the legal person, independent of the partners. In the case of company debt, the partners' assets cannot be attached. The fact that the shareholders have limited responsibilities to the company and are not responsible for third party receivables, creates a veil between shareholders and third party creditors. This situation causes detriment to the creditors as a result of the shareholders' violation of the principle of honesty. For this reason, the concept of piercing the corporate veil emerges.

The concept of piercing the corporate veil is frequently applied by the courts, although it is not regulated in legislation. As in the decision of the Supreme Court 19th Civil Department dated 24.03.2015, based on 2014/7187, numbered 2015/4144, it is an execution that has developed and accepted through case law.

II. Circumstances When the Corporate Veil Can Be Pierced

In the event of the existence of certain conditions, the veil between the legal entity and the shareholders is lifted and the law prevents the malicious shareholder from taking unfair advantage of the legal entity of the company and taking refuge behind the legal entity in order to get rid of the debt. These cases are as follows:

1. Deficiency of Equity

If the company's capital is insufficient as a result of the failure to take measures to protect the interests of the creditors and to sustain the business life of the company, deficiency of equity occurs. In case of deficiency of equity, the corporate veil can be pierced and the shareholders can be held liable.

Third-party creditors who are unable to collect their receivables due to the existence of a causal connection between the shareholder and the company and the insufficient assets of the company may demand the company debt to be covered by its shareholder. The reasonable causal connection in question refers to situations in which the creditor is able to hold a person (shareholder or separate legal entity) liable if the creditor cannot collect their receivables due to the wrongful act of such person who drained the company assets.

2. Piercing the Corporate Veil in Companies with a Controlling Shareholder

There is a parent-subsidiary relationship between the companies that have two different legal entities, but one of which is affiliated to the other. The parent company is the decision-maker, and the legal independence of the subsidiary company is not taken into consideration. For this reason, when the corporate veil is pierced, the parent company may be held liable for the debts of the subsidiary.

3. Intermingling of the Assets of the Company and the Shareholders

Company assets and shareholders' assets are separate from each other. The shareholder's responsibility is limited to the amount of capital committed to the company. Even though there is no harm in using the company assets within the principle of good faith and without harming the interests of the company and the creditors, if the company assets are used to the detriment of creditors against good faith, the corporate veil may be pierced and the shareholders may be held liable.

III. Types of Piercing the Corporate Veil

1. Piercing the Corporate Veil Directly

The above-mentioned explanations are related to piercing the corporate veil directly which is the most typical example of piercing the corporate veil. It means the extension of the scope of liability of legal entity to cover shareholders; in other words, a debt of the legal entity is paid from the assets of the shareholders.

2. Reverse Piercing the Corporate Veil

If a debt of a shareholder is not paid, his/her share in the company can be seized and it will then be possible to sell the seized share. In case of paying the debt of the shareholder from the assets of the company, reverse piercing the corporate veil occurs and the debt of the shareholder is paid from the assets of the legal entity.

3. Cross Piercing the Corporate Veil

It is a method usually applied for group companies; first, the liability of the parent company is extended because of the debt of a subsidiary company of a group company. Then, the debt owed by the subsidiary partnership is paid from the assets of another subsidiary company by extending the liability of the subsidiary company of the parent company.

IV. Conclusion

The partners or other companies that drain the company's assets in violation of the principle of honesty are jointly responsible for the detriment caused to their creditors. In this case, if a third party creditor is unable to collect his/her receivables, he/she can hold the shareholder or the parent company liable. If the court finds that the assets of the principal debtor company have been drained by the partner or parent company, it will rule on the collection of the assets from these individuals.

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