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A PERIODIC NEWSLETTER

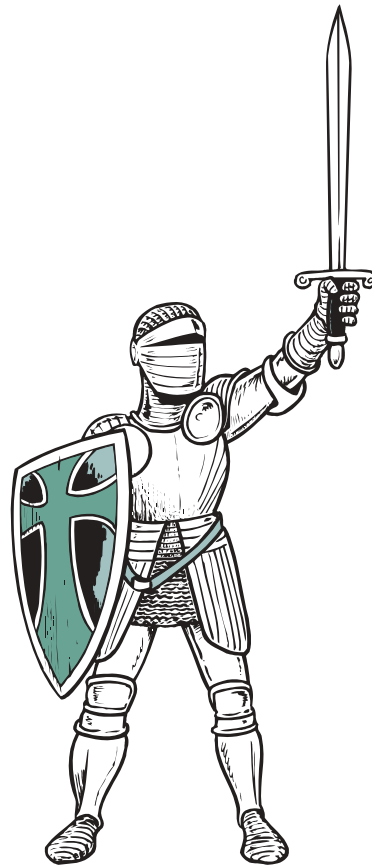
Summer 2003

Is Your Shield Full of Holes?

by Mark P. Santagata

Every year Connecticut entrepreneurs create thousands of business entities. Corporations, limited liability companies, and limited partnerships are formed with the intent, in part, of protecting the principals behind the entities from business related liability. Once these shields are in place, however, many business owners neglect their proper maintenance, or inadvertently operate them in a fashion that leaves the protection provided by the entity full of holes. When the validity of the protection provided by such a business entity is then tested in court, the result can place the personal assets of the business owner at risk. Lawyers call the process of attacking a business entity to reach personal assets "piercing the corporate veil." If piercing the veil is permitted by a court, it is as if the shield provided by the business entity does not exist, and the principals behind the entity can find their personal assets exposed to business creditors.

Connecticut courts use two analyses to determine whether a party seeking to enforce a judgment can have access to a principal's personal assets. Under the first analysis, known as the instrumentality test, a court examines the degree to which the individuals behind the business entity have control over the entity. Control is not merely a question of a majority interest in the business, but complete domination of the business so that the business entity exists as the alter ego of the individual exercising control. A court faced with the question of control will consider aspects of the business operation to determine if the entity is an independent,



viable business, or whether it is so dominated, financially or otherwise, by the principal that justice requires liability to be imposed on the real actor, the principal behind the shield. If this extreme level of control is found, the court can pierce the veil if it finds that the control was utilized to commit an unjust act that caused harm.

To minimize the risk that a court will pierce the veil under the instrumentality test, it is essential for business entities to have a separate and distinct existence from the principal behind the business. Financial accounts of the principal and the business should be separate, and the principal should not treat the two accounts interchangeably. The business should be adequately capitalized so as not to be financially dependent upon the principal. There should be an arm's length relationship between the individual running the business, and the business itself. Formalities associated with maintaining the entity, such as corporate meetings and filings with the Secretary of State, should be followed.

continued on next page

The second analysis under which a court can pierce the veil is known as the identity test. To break through a business entity using this test, the court must be satisfied that there was such a unity of interest between the business entity and its ownership that the independence of the entity had ceased or had never begun. If the court determines that the separate identity of the business entity is a fiction, then the court will not allow the underlying principal to escape direct liability.

Generally, the identity test is applied in situations where one business entity acts through another business entity to shield itself from liability. In such cases courts look at whether the two entities are actually run as a single business, examining such factors as the financial inter-relationships between the

companies, and the existence of common ownership, officers, directors and shareholders between the two. This theory is not reserved exclusively for interrelationships between businesses, however, and can also be applied where one or more individuals stand behind a business entity.

Piercing the corporate veil is not commonly permitted by the courts, but when it is allowed it defeats one of the primary advantages offered by business entities. To avoid situations where piercing the veil might be possible, business owners should be extremely careful about properly maintaining their business entities, and avoid actions which might ultimately result in the questioning of the independent existence of the entity. ☺

Liquidated Damages

by Judith Ellenthal

Typically, contracts for sale of residential real estate contain a liquidated damages clause. These clauses are intended to protect the Seller from a Buyer's default. Such a clause would be similar to the following:

If BUYER is in default hereunder, or, on or before the date of closing as set forth herein, indicates that BUYER is unable or unwilling to perform and SELLER stands ready to perform SELLER's obligations, SELLER's sole and exclusive remedy shall be the right to terminate this Agreement by written notice to BUYER or BUYER's attorney and retain the down payment as reasonable liquidated damages for BUYER's inability or unwillingness to perform.

It would appear from the above language that if the Buyer defaults, the Seller can keep the down payment, which is usually 10% of the purchase price, as the entire amount of compensation for the Seller's loss. Here the parties are working out a settlement in advance to avoid delay and litigation. The effect of the language would seem to be clear, but it is not.

A recent Connecticut Superior Court held that where the default by the Buyers was not willful and the Seller suffered no damage, then the Buyers were entitled to the return of their down payment, notwithstanding the liquidated damages clause in the contract. The Buyers' breach was not considered willful due to their reliance on the real estate broker's representation. This case follows other Connecticut cases holding that even where there was a valid liquidated



damages clause, it was not to be enforced when the non-breaching party suffered no damage. The reasoning is that if the damage contemplated by the parties never occurs, then the intent of the parties is not served nor is justice served by the enforcement of the liquidating damages clause.

A more recent Connecticut Appellate Court decision held that a liquidated damages clause would be enforced, if the Seller was unwilling to perform even for personal reasons. In this case, the court held the language of the liquidated damages clause was clear and not ambiguous. The difference in this case from the other cases were the words in liquidated damages clause, "for whatever reason." The liquidated damages clause was enforceable due to the inclusion of that phrase and the Seller was entitled to retain the down payment.

What does this mean to a Seller or a Buyer? The first thing to do is to make sure when the contract is negotiated that the language in the liquidated damages clause is clear and unambiguous and it expresses your intent. If you are the Buyer, be careful of phrases such as "for whatever reason." As well as negotiating the language of a liquidated damages clause in the contract of sale, you can also negotiate it out of the contract and leave the issue of a breach of the contract to

the common law remedies.

In the event of a breach, the Seller has to mitigate his damages. The Seller cannot recover for damages which could reasonably have been avoided. He should take all reasonable steps to continue to actively market the house for sale and not increase his damages.

The validity of a liquidated damages clause depends on the circumstances of the case and the specific language of the clause in the contract, as well as case law. If you cannot negotiate a settlement among the parties, then a court of law's interpretation would prevail. ☺

Mechanic's

Liens by David J. Coviello

Fail to pay your contractor and you may find yourself at the receiving end of a mechanic's lien. The lien is a device that can be used by contractors to protect their interests in the event of non-payment. The mechanic's lien is a creature of statutory law. As such, specific attention must be paid to the statutory framework to establish and preserve any rights pursuant to such a lien. This article provides an overview of the time limitations and procedures for filing a mechanic's lien and instituting an action to foreclose it.

Pursuant to the Connecticut General Statute §49-34, a mechanic's lien is not valid, unless the person performing the services or furnishing the materials, records the lien with the town clerk within ninety days of completing the work. In addition, and within the same time, or prior to the recording of the mechanic's lien but not later than thirty days after recording the lien, a copy of the lien must be served upon the owner of the building or land.

The mechanic's lien must describe the premises, the amount claimed for the lien, the name or names of the person against whom the lien is being filed and the date of the commencement of the performance of services or furnishing of materials. The lien must be subscribed and sworn to by the lienor. That is, the lienor must sign the document before a notary public and swear by written affirmation to the truth of the matters asserted within the lien.

Service of the mechanic's lien upon the owner of the building or land must be made by any indifferent person, state marshal or other proper officer. If the owner resides in the same town in which the building is being constructed or renovated, the mechanic's lien must be served by leaving it with the owner at his or her usual place of abode. If the owner does not reside in the same town, but has a known agent in the town, the lien may be served upon that agent. Otherwise, it may be served by registered or certified mail to

the owner's residence. If the owner of the building or land is an entity other than an individual, the statutory agent for service of process for the entity must be served.

In the event that the lienor is a subcontractor, as opposed to a general contractor, the statute requires that the lienor also file a notice of intent with the general contractor. This requirement must be satisfied only if the general contractor filed an affidavit on the land records, within fifteen days after commencing construction, that identifies the name, address, and description of the land that is the subject of the construction. As a practical matter, because of problems associated with the proper indexing of such a notice, it makes sense to file the notice regardless of whether or not an affidavit was discovered in the land records. Service of the notice must be made in accordance with the same guidelines governing the service of the lien.

Once the mechanic's lien has been properly served and recorded, the Connecticut law provides that the lien shall not continue in force for a longer period than one year after the date of the recording of the lien on the land records. Therefore, an action to foreclose a mechanic's lien must commence within one year after the lien was recorded to preserve the lienor's rights under the lien. This statute also requires that a lis pendens be recorded on the land records within one year from the date of recording. A lis pendens is a document recorded on the land records that warns all persons that any interest acquired in the property during the pendency of the foreclosure action is subject to its outcome.

In sum, because the failure to satisfy the statutory requirements may prove fatal to any rights a contractor may have under the statute, it is advisable that you contact an attorney soon after non-payment so that your rights to recover owed monies will be protected and preserved. ☺

Personal Notes

Edward F. Nemchek has become a member of the Board of Directors of Babe Ruth Baseball of Stamford, Inc.

Paul T. Tusch was re-elected as President of the Volunteer Center of Southwest Fairfield County and also appointed Vice Chairman of the Connecticut Bar Association Family Law Section. Paul recently lectured at the CBA Annual Meeting in New Haven. This year's topic was an Annual Survey of Recent Developments in Connecticut Family Law. Paul also organized and moderated the CBA Family Law Section's annual Continuing Legal Education program held in New Britain and entitled: "The Bulletproof Financial Affidavit."

Sherwood R. Spelke spoke at a First Time Home Buyer's Seminar sponsored by First County Bank. Sherwood was nominated for a second term as co-chairman of the Real Estate Committee of the Regional Bar Association and

continues to serve as a member of the Board of Directors of the Stamford Museum and Nature Center.

Mark P. Santagata has been appointed to the Kids In Crisis Strategic Planning Committee and the Planned Giving Committee. Mark was also elected to the Board of the Regional Bar Association.

In June, **Ronald E. Kowalski, II** served as a Special Master (Tax Appeals) for the Stamford Superior Court. Recently, Ron also moderated and presented at a program sponsored by the Easton Senior Center, titled "Understanding the Revaluation" and participated in a Government/Politics panel at Fairfield University, conducted by the University's Career Planning Center.

On May 29, 2003, **Mark P. Santagata, Edward F. Nemchek, Judith Ellenthal**

and Sherwood R. Spelke conducted a seminar for the Regional Bar Association on Litigation Issues Arising out of Real Estate Transactions.

The Fairfield County Alumnae Seminar announces plans for its 24th annual seminar. This year's presentation, "Food as a Force in the Kitchen and Around the World." examines food from its connection with our lives and history to its environmental and global economic issues. The Alumnae seminar, an annual colloquium on a topic of current interest and special importance to women, is presented as a public service by a committee of alumnae from the original Seven Sisters Colleges. The committee includes Smith alumna **Alice A. Fitzpatrick**. The seminar is given to the Public and will be held Wednesday, October 22, 2003 from 9:00 am to 1:30 pm at the Italian Center in Stamford. For more info, please contact Attorney Fitzpatrick at (203) 327-2000.

CACACE, TUSCH & SANTAGATA is a full service general practice law firm dedicated to providing its clients with quality legal work. The firm occupies the second and third floors of the office building located at 777 Summer Street, Stamford, Connecticut, and has an office at 124 West Putnam Avenue, Greenwich, Connecticut. Our attorneys' areas of practice include:

ZONING AND LAND USE PLANNING ❖ REAL ESTATE TRANSACTIONS ❖ CIVIL LITIGATION
ADMINISTRATIVE HEARINGS AND APPEALS ❖ VALUATION OF PROPERTY ❖ FAMILY LAW ❖ LANDLORD/TENANT LAW
ESTATE PLANNING AND PROBATE ❖ ELDER LAW ❖ BUSINESS AND CORPORATE LAW ❖ CRIMINAL LAW

Case by Case is intended to provide a periodic discussion of developments and issues of interest to our clients and friends. If readers have questions concerning the matters discussed herein, they should direct them to Edward F. Nemchek, the attorney responsible for the newsletter's content at: CACACE, TUSCH & SANTAGATA by telephone at (203) 327-2000 or by e-mail at ENEMCHEK@LAWCTS.COM.

N.B. The information contained in this newsletter is informational and not intended to be legal advice and may not be reproduced in any form without consent. Requests for consent should be directed to Paul T. Tusch, Esq., Cacace, Tusch & Santagata, P.O. Box 15859, 777 Summer Street, Stamford, Connecticut 06901-0859.



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IN THIS ISSUE...

<i>Is Your Shield Full of Holes?</i>	P. 1
<i>Liquidated Damages</i>	P. 2
<i>Mechanics' Liens</i>	P. 3
<i>Personal Notes</i>	P. 4