

# The consequences of salomon law company business partnership essay

[Law](#)



The principles separate legal personality and limited liability have raised questions because they are formulated on the basis of general reasons for not applying them, such as fraud, the company being a sham or façade, that the company is agent of the shareholder, that the companies are part of a single economic unit or even that the interests of justice require this result.

[1]Adams v Cape Industries[2]is an important decision of the Court of Appeal that addresses some of these issues, including the lifting of corporate veil and the legal status of subsidiary company. In the light of this case, this essay critically assesses the statement of Lord Goff in Bank of Tokyo v Karoon[3]to the effect that although economically they are one unit, a parent company and a subsidiary company are legally distinct and cannot be bridged. The consequences of Salomon v A Salomon & Co Ltd[4]is that as a separate legal entity, separate and distinct from its shareholders, the company must be treated like any other independent persons with rights and liabilities appropriate to itself. In legitimising the one-man company, Salomon also legitimises the group concept with each subsidiary company being a separate and distinct entity and not the agent of its parent company. [5]The parent company and the subsidiary are separate legal entities and each company is entitled to expect that the court will apply the principles of Salomon in the ordinary way and respect the identity of each company in the group.[6]The principles of separate legal personality and limited have made it very rare for the courts to pierce the corporate veil.[7]Adherence to a strict Salomon approach may not be appropriate in the modern business where much commercial activity is carried out in corporate groups in a way which could not have been envisaged in 1897. As a result, various alternative

approaches have been put forward, particularly for the law to allow to develop a mechanism whereby obligations and responsibilities could be attach to the group and not to the individual companies. In this way the law would reflect the economic reality which is that these companies trade as a group, raise capital as a group, and are considered by those dealing with them as a group. Thus, in *DHN Food Distributors Ltd v Tower Hamlets LBC*[8] Lord Denning supported for the development of a group enterprise law. However, in *Woolfsion v Strathclyde Regional Council*[9] the House of Lords rejected Lord Denning's view, doubting whether the Court of Appeal had applied the correct principle in *DHN*. Therefore, English courts have shown a strong determination not to embark on any development of a group enterprise law. The leading case is *Cape Industries*. It concerned the liability within a group of companies and the purpose of the claim was to circumvent the separate legal personality of the subsidiary towards involuntary tort victims. The issue was whether English court would recognise and enforce judgments obtained in the United States against Cape, an English company whose business was mining asbestos in South Africa and marketing it globally. This depended on whether Cape was present in the United States. The answer to that issue turned on whether Cape was present in the United States through its wholly owned subsidiaries or through another company that Cape has close relations with. Various arguments were put forward, one of them being the single economic unit argument. It was argued that where the group companies are operated as a single unit for business purposes, the court should disregard the legal distinction between them by treating them as one. However, Slade LJ, giving the leading judgment, stated that there was

no a general principle that all companies in a group of companies should be regarded as one. On the contrary, he stated that, the fundamental principle was that each company in a group company was a separate entity with its own legal rights and liabilities. Slade LJ went on to agree with the observations of Lord Goff in *Bank of Tokyo Ltd v Karoon*[10]who said that although economically a parent company and a subsidiary company are one, the legal distinction between the two was fundamental and could not be bridged. A number of authorities were referred to support the single economic unit argument, but the Court of Appeal distinguished them because they related to the construction of particular statutory or contractual provisions. However, the court sympathised with the claimants' submissions and agreed that to a layman, there is slender distinction between a case where a company trades itself in a foreign country and a case where it trades in a foreign country through its subsidiary, whose activities it has power to control. It also accepted that the wording of a particular statute or document may justify the court to construct it in such a way that the parent company and the subsidiary company may be treated as one economic unit at any rate for some purposes. Therefore, in aid of construction of a statute or a contract, the court may take into account the economic realities in relation to the companies concerned and that is the extent to which the single economic unit argument can succeed.[11]Thus, in constructing the application of an EU Regulation, the Court of Appeal held in *Samengo-Turner v J & H Marsh & McLennan*[12]treated a group companies as a single legal entity on the basis of their single economic interest. Similarly, in *Backett Investment Management Group Ltd v Hall*,[13]the Court of Appeal

constructed a clause in an employment contract in the context of a group of companies that formed a single economic entity, holding that it was not appropriate to be inhibited by considerations of corporate legal personality. In subsequent cases, the courts have been unwilling to go beyond Cape Industries. For example, pressed to regard a group of companies as a separate economic unit in *Re Polly Peck International plc (No. 3)*[14], Robert Walker J concluded that he could not accede to that submission for it would create a new exception to the Salomon principle unrecognised by the Court of Appeal in *Cape Industries*, something which was open to the court. Similarly, in *Ord v Belhaven Pubs Ltd*,[15]it was held that the courts will not allow a claimant with a claim against a subsidiary company to substitute the holding company or to the group subsidiaries as defendants to that claim simply because the group may be a single economic entity. The decision in *Cape Industries* demonstrates how strong is the principle of separate corporate personality and how the courts regard members of a group company as separate entities perhaps without exception. However, the decision raises issues of concerns relating to the position of creditors of a subsidiary company, the duties of the directors a subsidiary as well as the protection of minority interests.[16]Importantly, the decision failed to give adequate redress for the injuries of foreign victims of asbestos inhalation against an English holding company.[17]This may suggest that company law can technically enables a company wishing to operate outside the country to shield itself from liability against genuine claims for damages abroad by registering a foreign subsidiary. However, the principle separate personal liability and limited liability are so entrenched in English company law to

force the courts not to lift the corporate veil and hold a holding company shareholder liable for the actions of its subsidiary because of the desire to simply compensate injured claimants.[18] Nonetheless, a number of recent decisions in the House of Lords and the Court of Appeal have held that claims may be brought against a holding company in an English court. In *Lubbe v Cape plc*[19], the House of Lords held that the standard principles of negligence law apply in determining where a parent company owed a duty of care to a tort victim of a subsidiary.[20] In *Chandler v Cape plc*,[21] the Court of Appeal addressed the availability of damages in tort from a parent company for industrial injuries suffered by the claimant during employment by a subsidiary company. The court held that a parent company may owe a direct duty of care to a person injured by a subsidiary. This decision represents the first time that an injured employee of a subsidiary company has established that his employer's parent company owed him a duty of care. Although the Court of Appeal said that the case did not involve lifting the corporate veil, the outcome seems to have the effect because it imposes liability upon a parent company even though the parent company is legally separate from its subsidiary. In summary, *Cape Industries* is an importance decision on the principles of separate legal personality and limited liability, particularly in relation to group companies. It treats a parent company and a subsidiary company as legally distinct despite being one economic unit. However, the importance of the decision appears to have been limited by subsequent decisions, such as *Chandler* where the court imposed a direct duty on a parent company to a person injured by its subsidiary. The court did

not lift the corporate veil, but reached the same outcome through the application of the standard principles of negligence law.

## **BIBLIOGRAPHY**

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