Introduction

A registered company is a body corporate (Companies Act 2006 (CA 2006), s. 16) and is a legal person separate from the shareholders. A company is therefore said to have ‘separate legal personality’ or ‘corporate personality’. This was recognized most famously in Salomon v A. Salomon & Co Ltd [1897] AC 22 (Salomon): ‘The company is at law a different person altogether from the subscribers to the memorandum: and … the company is not in law the agent of the subscribers or trustee for them’ (Lord Macnaghten).

The effect of corporate personality is to create a ‘veil of incorporation’ between the shareholders (and directors) and the company, preventing recourse to the shareholders for the debts of the company. This applies whether the shareholders are natural persons or corporate persons, so the veil is effective even in a corporate group, as recognized in The Albazer [1977] AC 774: ‘… each company in a group of companies … is a separate legal entity possessed of separate legal rights and liabilities’ (Roskill LJ). Accordingly parent companies are not liable for the debts of their subsidiaries (or vice versa).

The circumstances in which this veil of incorporation can be ‘lifted’ or ‘pierced’ (in other words, when corporate personality can be ignored for some purpose), whether by statute or by common law, are a matter of some discussion. For many years the key case was the decision of the Court of Appeal in Adams v Cape Industries plc [1990] Ch 433. That case is still important but it is now essential also to be aware of the recent Supreme Court decisions of VTB Capital plc v Nutritek International Corp [2013] UKSC 5 and Prest v Petrodel Resources Ltd [2013] UKSC 34. The latter, in particular, provided a detailed analysis of veil-piercing cases and policy.

Corporate personality and piercing (or lifting) the veil of incorporation tends to be a popular topic for exam questions, and can also connect with most other topics in company law.
In January 1999, Ben set up in business as a sole trader supplying cakes and desserts to local restaurants from leased premises. In January 2000, he formed Just Desserts Ltd and, in consideration of the transfer of the business and its assets, including the leased premises, to the company, he was issued with 10,000 £1 shares in Just Desserts Ltd. Ben was the sole shareholder and director. He signed a contract of employment with the company and drew a salary. In December 2004, Ben made a loan to the company of £25,000 to buy new equipment. The loan was secured by a floating charge over the company’s assets. In July 2006, Ben was injured in a gas explosion while at work and the building was badly damaged. Ben’s insurance policy on the building and contents was taken out in his name in January 1999.

In 2007, although the business was trading profitably, Ben decided that, in view of his injuries, he would retire and dissolve the company.

Advise Ben on the following:

(a) The validity of the one-man company
(b) His right to claim under his insurance policy for the fire damage to the property
(c) His claim against the company for compensation for his injuries
(d) His right to claim as a secured creditor in respect of his floating charge and for arrears of salary

This problem question requires you to apply a number of decisions made after *Salomon v A. Salomon & Co Ltd* [1897] AC 22 (*Salomon*) and subsequent decisions applying the principle of separate legal personality. This principle underpins the whole of company law and recognizes that the company is a legal person separate from its members and directors.
In respect of (a), one of the major aspects of importance of the *Salomon* decision was the implied recognition of the ‘one-man company’. At that time, company law required a minimum of seven subscribers to the memorandum of association in order to incorporate a company. The subscribers in this case were Mr and Mrs Salomon and their five children, but Mr Salomon’s wife and children held only a single share each and held their shares as nominees for Mr Salomon. Although the Court of Appeal (*Broderip v Salomon* [1895] 2 Ch 323) had taken the view that such an arrangement was an abuse of the companies legislation, the House of Lords did not accept that the status of the shareholders was relevant to the legality of the company. Since the statute ‘enacts nothing as to the extent or degree of interest which may be held by each of the seven or as to the proportion of interest or influence possessed by one or the majority over the others’ (Lord Halsbury), the court would not impose any such requirement and Mr Salomon’s company was valid. Accordingly the ‘one-man company’ was established *de facto* in English law long before the position was recognized in the *Companies (Single Member Private Limited Companies) Regulations 1992* which allowed the registration of the one-man private company (in *Companies Act 1985*, s. 1(3A)). Under the CA 2006, both private and public companies can be registered with one member (although a public company must have at least two directors: *Companies Act 2006* (CA 2006), s. 154(2)).

In this case, the company was registered after the coming into effect of the 1992 Regulations and the company is perfectly legally established. The only problem would be if Ben had formed his company to escape some existing legal liability or as part of a scheme to evade the rules of company law. In this case, the company could be regarded as a ‘mere façade’ and the veil of incorporation could be pierced: *Gilford Motor Co Ltd v Horne* [1933] Ch 935. This ground for piercing the veil of incorporation, provided there is clear impropriety in the use of the corporate structure, appears to have survived the Supreme Court’s recent analysis of piercing the veil in *Prest v Petrodel Resources Ltd* [2013] UKSC 34.

In respect of (b), in spite of the fact that Ben is the sole shareholder of the company, he has no legal or equitable title over the company’s property. This was established in *Macaura v Northern Assurance Company* [1925] AC 619 where Macaura tried unsuccessfully to claim under an insurance policy taken out in his own name to cover the destruction of property that had previously been transferred to a company that he had incorporated and in respect of which he held all the shares except for some held by nominees. Since the policy was taken out in Ben’s name prior to the incorporation of Just Desserts Ltd, any claim under the policy would fail on the grounds of the lack of Ben’s insurable interest. The only thing that could change the position would be if Ben had assigned the policy to the company along with the rest of the property. This does not appear to have happened. This shows the risks of incorporation when an individual is not fully aware of the consequences of the *Salomon* principle; although the principle operates to protect a shareholder’s assets from the company’s creditors it can also, on occasion, work against the shareholder, as here.

In respect of (c), *Lee v Lee’s Air Farming Ltd* [1961] AC 12 established that a person could be the controlling shareholder, managing director, and also an employee under a contract of employment with their own company: ‘it is a logical consequence of the
decision in *Salomon's case* that one person may function in dual capacities' (Lord Morris). The court in that case allowed Mr Lee's wife to recover compensation for Mr Lee’s death as he had been an employee. However, in *Clark v Clark Construction Initiatives Ltd* [2008] EWCA Civ 1446 the court held that an alleged contract of employment could be ignored (i) where the company itself was a sham; (ii) where it was entered into for an ulterior purpose; and (iii) where the parties did not conduct their relationship in accordance with the contract—although the mere fact that an individual had a controlling shareholding did not, of itself, prevent a contract of employment arising but might raise doubts as to whether he was an employee. The court, therefore, held that the employment tribunal had reached a reasonable decision in rejecting Clark’s claim to be an employee. Subject to this, Ben should be able to claim as an employee for compensation.

In respect of (d), the separate personality of the company means that there is no reason why Ben cannot also be a creditor of the company and claim in the company’s liquidation. In *Salomon*, Mr Salomon had taken security over the company’s assets and this was held by the House of Lords to be valid, allowing him to recover in front of the unsecured creditors on the company’s insolvent liquidation. Ben's potential claims could be (i) as an employee in respect of any arrears of salary and unpaid holiday remuneration; (ii) as a secured creditor in respect of his loan to the company secured on a floating charge over the company’s assets; and (iii) as a shareholder for a return of capital once all the debts are paid off. In respect of the latter it is important to note that the shares in the company were allotted to him in respect of non-cash consideration. Since the company is a private company, there is no legal requirement for the business to be valued as would be the case for a public limited company under CA 2006, s. 593. The company is entitled to place whatever value it likes on the assets transferred to it in the absence of fraud: *Re Wragg Ltd* [1897] 1 Ch 796. In *Salomon*, the House of Lords was not concerned that the consideration paid by the company for Mr Salomon’s business (£39,000) was ‘extravagant’ and ‘represented the sanguine expectations of a fond owner rather than anything that can be called a businesslike or reasonable estimate value’. Accordingly, provided it was done honestly, there is no cause to question the consideration provided for the shares.

**Question 2**

Paradise Ltd imports furniture from India. Adam is the managing director and there are three other directors. In 1999, the board decided to set up a retail business and created a wholly owned subsidiary, Indus Ltd, for the purpose. The registered office of Indus Ltd is the same as that of Paradise Ltd, and Adam is the sole director of Indus Ltd.

The retail business was successful until late 2006 when other suppliers continued to supply the company only on Adam’s assurance that Paradise Ltd would give Indus Ltd financial support. By June 2006, Indus Ltd could not pay its debts as they fell due. It continued trading until February 2007 when it went into insolvent liquidation.

Advise the liquidator of Indus Ltd of any common law or statutory liability of Adam and Paradise Ltd and its directors for Indus Ltd’s debts.
This problem raises issues relating to the veil of incorporation and the judicial and statutory exceptions to the rule when the veil is lifted or pierced. Although the context of the question is the liquidation of a company within a small group, the question does not require a discussion of liquidation as such. The possibility of a business failing and going into insolvent liquidation is in many, if not most, cases the motivating factor for entrepreneurs to choose the form of a limited liability company limited by shares as a vehicle for their business. The context of the decision in Salomon was the failure of the company and whether the founder and principal shareholder was liable to indemnify the company's creditors. The question does, however, require you to apply sections of the Insolvency Act 1986 (IA 1986) relating to piercing the corporate veil.

Commentary

- The rule in Salomon and its application to a group of companies
- Judicial recognition of the separate identity of companies within a group
- Judicial exceptions to the rule
- Statutory piercing of the veil under the IA 1986 to make directors and other persons liable to contribute to the assets of a company in liquidation
- De facto and shadow directors

Answer plan

The decision in Salomon v A. Salomon & Co Ltd [1897] AC 22 (Salomon) is always cited as having established that a company is a separate legal person from its shareholders, allowing persons to carry on trading without exposing them to the risk of personal insolvency in the event of the failure of the business. In effect, the separate nature of the corporation from that of its members had been recognized as early as the seventeenth century and the decision in Foss v Harbottle (1843) 2 Hare 461 is an earlier example. In the context of a group of companies, the rule also means that the companies of a group are all separate legal entities and that there is no liability on a company within a group if one of the other group companies collapses into insolvent liquidation. A frequently quoted statement which illustrates the general rule was provided by Templeman LJ in Re Southard Ltd [1979] 1 WLR 1198 at 1208:

‘A parent company may spawn a number of subsidiary companies, all controlled directly or indirectly by the shareholders of the parent company. If one of the subsidiary companies, to change the metaphor, turns out to be the runt of the litter and
declines into insolvency to the dismay of its creditors, the parent company and other subsidiary companies may prosper to the joy of the shareholders without any liability for the debts of the insolvent subsidiary.’

There are, however, a number of judicial and statutory exceptions to this fundamental rule which operate to lift (or pierce) the corporate veil between the company and its shareholder and directors—although it should be noted that Prest v Petrodel Resources Ltd [2013] UKSC 34 casts serious doubt on whether all these cases should be considered to be true examples of piercing the veil. An early example of the company’s separate personality being ignored is Re Darby, ex p Brougham [1911] 1 KB 95 where the High Court treated a company formed by two fraudsters as ‘merely an alias for themselves’.

During the twentieth century, there was some enthusiasm for lifting the veil, particularly in relation to corporate groups. This culminated in decisions like DHN Food Distributors Ltd v Tower Hamlets London Borough Council [1976] 1 WLR 852 where the Court of Appeal treated the three companies in a group as a single economic entity. This much criticized decision marks the high point in judicial piercing of the veil of incorporation, and reinforced the demands for some principles to be established so that litigants could predict when the court would, or would not, lift the corporate veil.

The Court of Appeal decision in Adams v Cape Industries plc [1990] Ch 433 rationalized the judicial exceptions to the rule in Salomon and demonstrated that the veil would not be lifted easily even within a corporate group, rejecting claims that the companies were a ‘single economic unit’ or that the American subsidiary was a facade or that the subsidiary was the agent of the parent. In rejecting the submissions, Slade LJ stated: ‘Neither in this class of case nor in any other class of case is it open to this court to disregard the principle of Salomon merely because it considers it just to do so.’ Although the Court of Appeal accepted that the veil could be lifted if the subsidiary was a mere facade concealing the true facts, it did not accept that this applied to the company, the group was entitled to organize its affairs to take advantage of the Salomon principle. While this limited ground for lifting the veil seems to have survived the Supreme Court decisions of VTB Capital plc v Nutritek International Corp [2013] UKSC 5 and Prest v Petrodel Resources Ltd [2013] UKSC 34, it is clear that (in the absence of significant further evidence) the veil would not be lifted/pierced in the case of Indus Ltd—there is no relevant impropriety in the creation or operation of the company.

As regards the promise made by Adam on behalf of Paradise Ltd assuring Indus Ltd’s creditors of Paradise Ltd’s financial support to Indus Ltd, this would not create any legal liability on Paradise Ltd. This type of statement is sometimes made in writing and is called a comfort letter. Such statements have been held to be insufficient to make a parent liable for its subsidiary’s debts: Kleinwort Benson Ltd v Malaysia Mining Corporation Bhd [1989] 1 WLR 379.

Applying these principles to the facts of the case, it would appear that neither Paradise Ltd nor its directors have any liability for Indus Ltd’s debts at common law.
Relevant statutory exceptions to the veil of incorporation in the Insolvency Act 1986 (IA 1986) must be examined to see whether they offer any solution. Under IA 1986, s. 212 there is the possibility of a liquidator obtaining a summary remedy against delinquent directors. This applies where, in the course of the winding up of a company, an officer or a person who is or has been concerned, or has taken part, in the promotion, formation, or management of the company has been guilty of any misfeasance or breach of any fiduciary or other duty in relation to the company. If this is established, the court may compel him to contribute such sum as the court thinks just to the company’s assets by way of compensation.

Section 213 of the IA 1986 creates the offence of fraudulent trading which provides that if, in the course of the winding up of a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or for any fraudulent purpose, the court may declare that persons who are knowingly parties to such conduct are liable to make such contribution to the company’s assets as the court thinks proper.

Wrongful trading is dealt with by IA 1986, s. 214. This operates where, in the course of the insolvent liquidation of a company, a person who was a director of the company at a time prior to the commencement of the winding up knew, or ought to have concluded, that there was no reasonable prospect that the company would avoid insolvent liquidation and yet continued to trade. The court may order such a person to make a contribution to the company’s assets as the court thinks proper: IA 1986, s. 214.

In respect of the summary remedy, when a company is insolvent or on the brink of insolvency, the interests of the creditors take over from the interests of the members in assessing a director’s duty to the company (see West Mercia Safetywear Ltd v Dodd [1988] BCLC 250 and CA 2006, s. 172(3)). Accordingly directors should ensure that the company’s property is not ‘dissipated or exploited for the benefit of the directors to the prejudice of the creditors’: Winkworth v Edward Baron Development Co Ltd [1987] 1 All ER 114. Continuing to trade and exposing the creditors to increased risk of loss could amount to a breach of directors’ duties and trigger an order under IA 1986, s. 212.

In respect of fraudulent trading, if it could be established that Adam continued to trade with suppliers in the knowledge that the company would be unable to pay for the goods or services when they fell due, this could constitute fraudulent trading. Paradise Ltd could also be liable for fraudulent trading with the necessary intention attributed to the company through the intention of Adam, the managing director of Paradise Ltd, by way of the identification theory: Tesco Supermarkets Ltd v Nattrass [1971] 2 All ER 127. In order for Paradise Ltd to be liable, it is necessary to establish that Adam, the sole director, is guilty of fraudulent trading: Re Augustus Barnett & Son Ltd [1986] BCLC 170. The problem would be establishing intent.

It would be more straightforward to bring a claim against Adam under wrongful trading, where it is not necessary to establish any intention to defraud. The section catches ‘honest but incompetent’ directors. Since liability arises not only in respect of de jure directors but also de facto and shadow directors, the liquidator could potentially bring claims against Paradise Ltd and its other directors. However, this requires, for shadow directorship, evidence that Adam was accustomed to act in accordance with instructions or directions from Paradise Ltd or its directors (IA 1986,
Question 3

‘Salomon is in the shadow. It is still alive but no longer occupies the centre of the corporate stage.’
(Schmittoff, C.M., ‘Salomon in the shadow’ [1976] JBL 305)

‘The veil of incorporation is as opaque and impassable as an iron curtain.’ (Samuels, A., ‘Lifting the veil’ [1964] JBL 218)

Which statement more accurately reflects the current law on lifting the veil of incorporation and why?

Commentary

This question requires you to consider the current approach of the law to lifting the veil of incorporation, and evaluate whether it is now generally permissive (as suggested by the Schmittoff quote) or strict (as Samuels suggests). This requires consideration of the different grounds on which the veil may be lifted, focusing on the ‘mere facade concealing the true facts’, but also looking at other ways in which the veil might be lifted. You should also consider the attitude of the law more generally, taking particular account of recent decisions. You will need to reflect upon the changing law but your focus should be on assessing the current law rather than simply describing the historical development of the law.

Examiner’s tip

The quotes in this question are simply being used as a trigger for discussion so it is not necessary for you to have read the articles themselves before attempting the question. If you have read the articles don’t be tempted simply to describe the articles as that is not what the question asks you to do.
The quotes reflect the changing approaches of the law to lifting the veil of incorporation over the years. This essay will show that, despite the attempts of some judges (notably Lord Denning) to move the principle of separate corporate personality into the shadow, the current law is much more in line with Samuels’ quote than Schmittoff’s. This restrictive approach has been emphasized recently with the Supreme Court decisions in *VTB Capital plc v Nutritek International Corp* [2013] UKSC 5 and *Prest v Petrodel Resources Ltd* [2013] UKSC 34. Although distinctions can be drawn between ‘lifting’ and ‘piercing’ the veil (see, eg *Prest v Petrodel Resources Ltd*) and some academics have advocated the use of a range of different expressions (eg Ottolenghi, S., ‘From peeping behind the corporate veil, to ignoring it completely’ (1990) 53 MLR 338), this essay will use the term ‘lifting the veil’ generally.

**Lifting the veil by the courts**

The veil of incorporation is a metaphor for the separation of a company and its members which ensures that the members are not responsible for the company’s liabilities. Ever since the House of Lords in *Salomon v A. Saloman & Co Ltd* [1897] AC 22 (*Salomon*).
recognized the validity of Salomon’s ‘one-man company’, attempts have been made to lift this veil, whether to impose liability on those behind the veil or for some other purpose (eg attributing ‘enemy alien’ status in *Daimler Co Ltd v Continental Tyre and Rubber Co Ltd* [1916] 2 AC 307). The veil can be lifted by statute (*Dimbleby v National Union of Journalists* [1984] 1 WLR 427), but such provisions are uncommon and tend to impose additional liability on individuals rather than ignoring the company’s separate personality (eg liability for wrongful trading: *Insolvency Act 1986*, s. 214). Accordingly this essay will focus on when, if at all, the courts will lift the veil.

The trend of the courts is very much towards the Samuels statement. Suggestions that courts could lift the veil whenever justice required (eg *Re a Company* [1985] BCLC 333) were rejected in *Adams v Cape Industries plc* [1990] Ch 433 as was the argument that the veil could be lifted where a company and its members form a ‘single economic unit’ (*DHN Food Distributors v Tower Hamlets LBC* [1969] 1 WLR 852). *Woolfson v Strathclyde Regional Council*, 1978 SC (HL) 90 stated that the ‘only’ ground for lifting the veil is where the involvement of a company is a ‘mere facade concealing the true facts’ and this has been generally accepted (see *Adams v Cape Industries plc* and *Prest v Petrodel Resources Ltd*). This essay will first consider the ‘single economic unit’ and ‘mere facade’ grounds, and will then consider the use of agency or tort to avoid the veil by imposing liability directly on individual members or parent companies.

**Single economic unit**

The principle of separate corporate personality applies to corporate groups as it does to companies with human members (*The Albazero* [1977] AC 774; *Re Southard* [1979] 1 WLR 1198). However, in *Littlewoods Mail Order Stores Ltd v Inland Revenue Commissioners* [1969] 1 WLR 1241 and *DHN Food Distributors v Tower Hamlets LBC* [1976] 1 WLR 852 Lord Denning considered the economic reality of the situation—if a group was a ‘single economic unit’ in fact then it should be treated as such in law. Schmittoff’s quote dates from this period where courts were seen as more willing to lift the veil, pushing *Salomon* into the shadow. But in *Woolfson v Strathclyde Regional Council* the House of Lords doubted this approach and this was accepted in *Adams v Cape Industries plc* which held that the veil could be lifted on the basis of a ‘single economic unit’ only where this was the true construction of a statute, contract, or document. While this can allow veil-lifting on occasion (eg *Beckett Investment Management Group Ltd v Hall* [2007] ICR 1539), it is clearly very limited in scope. As far as this ground is concerned, the veil is indeed largely ‘opaque and impassable’.

**Mere facade concealing the true facts**

Although the courts have stated that the veil can only be lifted if the company is a ‘mere facade concealing the true facts’ *Adams v Cape Industries plc* recognized there was sparse guidance on what that means. It seems there must be some impropriety on the part of those using the company (although not necessarily when forming the company: *Ben Hashem v Ali Shayif* [2009] 1 FLR 115) and this impropriety must
be relevant—there must be a connection between the impropriety and the use of the corporate form: Trustor AB v Smallbone (No. 2) [2001] 1 WLR 1177. This was emphasized in Prest v Petrodel Resources Ltd.

Clearly the motivation of the individual is important. Where the corporate form has been used deliberately to evade an existing liability this has resulted in the veil being lifted (eg Jones v Lipman [1962] 1 WLR 832; Gilford v Horne [1933] Ch 935), as did the use of a company to hide misappropriated money (Trustor AB v Smallbone (No. 2) [2001] 1 WLR 1177) or abuse the companies legislation (Re Bugle Press [1961] Ch 270), although the Supreme Court decisions in VTB Capital plc v Nutritek International Corp and Prest v Petrodel Resources Ltd raise doubt as to whether all these are true examples of veil-lifting. What is clear is that merely using separate personality to push liability onto another member of a group is not impropriety (‘the right to use a corporate structure in this manner is inherent in our corporate law’: Adams v Cape Industries plc). Ord v Belhaven Pubs Ltd [1998] 2 BCLC 447, rejecting Creasey v Breachwood Motors Ltd [1993] BCLC 480, showed that even transferring assets from a company after a potential liability had arisen would not justify lifting the veil where this was not done with the purpose of evading that liability (the transfer was part of a group reorganization of assets). Similarly restrictively, VTB Capital plc v Nutritek International Corp denied that the veil could be lifted simply to impose liability on a person behind a ‘dishonorable’ transaction, and in Prest v Petrodel Resources Ltd an individual’s impropriety in matrimonial proceedings was not considered relevant in lifting the veil.

It follows that while the courts remain willing to lift the veil on this ground, the principle is applied restrictively and so the current law is closer to the statement of Samuels than Schmittoff.

**Agency**

If a company is the agent of its shareholder(s) then liability for the company’s debts will fall on the shareholder, by-passing the corporate veil (although not disturbing the separate personality of the company). The House of Lords in Salomon rejected the idea that the company was acting as Salomon’s agent; the fact that a company has a single member or is a wholly-owned subsidiary is not enough to make it the agent of its member or parent company. In the past courts have found an agency relationship between a subsidiary company and its parent company (eg Smith, Stone & Knight v Birmingham Corp [1939] 4 All ER 116) but Adams v Cape Industries plc made clear that agency cannot be presumed from the closeness of operations between a parent company and its subsidiary (see also Yukong Line Ltd of Korea v Rendsburg Investments Corp of Liberia (No. 2) [1998] 1 WLR 294). The current law shows that it is very unlikely that an agency relationship will be found on the facts, leaving the veil intact.

**Tort**

If a member (or director) has personally committed a tort then personal (or joint) liability could follow. However, the courts have generally been reluctant to impose tortious
liability on those behind the corporate veil, recognizing the potential for damage to the principle of separate personality (Williams v Natural Life Health Foods Ltd [1998] 1 BCLC 689). One area of tort liability of current interest is the responsibility of parent companies for activities of their subsidiaries. Chandler v Cape Industries plc [2012] 1 WLR 3111 held that while responsibility does not arise by mere fact of the corporate relationship, on the facts the parent company had assumed a direct duty of care to the subsidiary’s employees. While strictly outside the realms of lifting the veil, it shows there is some scope for avoiding the application of the Salomon principle.

**Conclusion**

To conclude it can be seen that the high-point of veil-lifting recognized in Schmittoff’s quote is long gone. Despite occasional indications of more Denning-esque views (eg in Ratiu v Conway and ors [2005] EWCA Civ 1302) recent decisions show a clear reluctance to depart from the principle of separate corporate personality and lift the veil except where there is abuse of the corporate form. This is so regardless of the seriousness or moral force of the claimant’s position. Largely in line with Samuels’ quote, the current law starts from the assumption that the veil is indeed an ‘iron curtain’; contrary to Schmittoff’s statement Salomon is very much ‘centre stage’.

**Question 4**

Write a case note on Prest v Petrodel Resources Ltd [2013] UKSC 34 focusing on the company law issues raised in the case.

**Commentary**

Writing a case note (or case comment) is a question technique that you might need to be able to deal with in exams, alongside more conventional essay and problem questions. It is a way of ensuring that you focus on a case—usually a particularly important case or an interesting recent decision on an important topic. Preparing your own case notes is also a useful revision and study technique to deepen your knowledge and develop your case analysis.

**Prest v Petrodel Resources Ltd [2013] UKSC 34** is the most recent and authoritative judicial statement on the law of lifting (or piercing) the veil of incorporation, and is a case that will repay careful consideration. The case considers whether companies owned and controlled by Mr Prest could be ordered to transfer properties owned by the companies to Mrs Prest as part of a divorce settlement. In this case Mrs Prest’s claim could not be met by the transfer of Mr Prest’s shares in the company (as might seem an obvious solution) because both Mr Prest and the company were resident abroad, making enforcement impossible.
Examiner’s tip

Focus on the case but don’t look at it in isolation—link it to other cases and consider how a case has developed the law or might influence the law in the future.

Case facts

Introduction

Why is case significant

Case facts

Judgments of lower courts

Supreme Court judgment

Comment

Important elements of the decision

Conclusion

Prest v Petrodel Resources Ltd [2013] UKSC 34 gave the Supreme Court a second chance in only a few months (the first being VTB Capital plc v Nutritek International Corp [2013] UKSC 5) to update and clarify the law on lifting the veil of incorporation. Prior to these cases the most recent authoritative guidance was that of Adams v Cape Industries plc [1990] Ch 433 (Court of Appeal) and before that Woolfson v Strathclyde Regional Council 1978 SC (HL) 90. Since lifting (or, as the Supreme Court prefers, ‘piercing’) the veil means ignoring the separate personality of a company and its members (as established in Salomon v A. Salomon & Co Ltd [1897] AC 22) and thus potentially undermining the ‘unyielding rock’ of company law (Templeman, Lord, ‘Forty years on’ (1990) 11 Co Law 10), this issue is of great importance.

The case concerned proceedings for ancillary relief following the divorce of Yasmin Prest from her oil-tycoon husband, Michael Prest, in which Mr Prest was found to be the effective sole owner and controller of several companies holding properties in the UK. Mr Prest had not been co-operative—his conduct of the proceedings was ‘characterised by persistent obstruction, obfuscation and deceit, and a contumelious refusal to comply with rules of court and specific orders’ (Lord Sumption).

At first instance (YP v MP and Petrodel Resources Ltd [2011] EWHC 2956) Moylan J, in part satisfaction of a lump sum award to Mrs Prest, ordered Mr Prest to procure the transfer of properties held in the name of two companies and ordered the companies to execute documents as necessary. Although the judge concluded that he was not able to pierce the veil under general principles (as the impropriety of Mr Prest did not relate to the use of the companies), Moylan J interpreted the Matrimonial Causes
Act 1973 (MCA 1973), s. 24 widely by construing ‘property’ to include property over which an individual exercises control.

In the Court of Appeal (Petrodel Resources Ltd v Prest [2012] EWCA Civ 1395) the majority (Rimer and Patten LJ) found in favour of the appellant companies, rejecting both any suggestion that the veil could be lifted and Moylan J’s interpretation of the MCA 1973. The majority criticized the generous approach of the family courts to piercing the veil and decreed that this practice ‘must now cease’ (Patten LJ). However the minority (Thorpe LJ) favoured the looser approach to lifting the veil in family cases, describing the alternative as offering ‘an open road and a fast car to the money maker’.

The Supreme Court judgment

The Supreme Court reversed the Court of Appeal decision, with the seven Justices unanimously finding in favour of Mrs Prest, but not by lifting the veil of incorporation, nor by restoring Moylan J’s interpretation of the MCA 1973. Instead the court reassessed the facts and concluded that Mr Prest had provided the purchase money for the properties, giving rise to a presumption (that was not rebutted) that the properties were held by the companies on resulting trust for Mr Prest. Nonetheless the Supreme Court offered some useful (albeit strictly obiter) discussion of veil-piercing.

The main judgment was given by Lord Sumption (whose reasons were expressly accepted, in the main, by Lords Neuberger, Mance, Clarke, and Walker). Lord Sumption recognized that the principle of separate corporate personality is in some sense a fiction, but is one that amounts to ‘the whole foundation of English company and insolvency law’. Although a foundational principle should presumably not be easily disturbed, the Supreme Court accepted a limited jurisdiction to pierce the veil, allied to the broader principle that absolute legal principles can be overturned in the event of fraud. Lord Sumption indicated that ‘piercing the veil’ happens only where separate personality is disregarded. He separated authorities into ‘evasion’ cases—where the corporate form was being used improperly—and ‘concealment’ cases—where regard was simply had to facts behind the veil; only the first category were properly examples of veil-piercing.

The veil should, therefore, be pierced only where necessary ‘to prevent the abuse of corporate legal personality’, such abuse being using the company to evade the law or to frustrate its enforcement, and ‘only for the purpose of depriving the company or its controller of the advantage they would otherwise have obtained’ (Lord Sumption). This should be a remedy of ‘last resort’, following the approach taken by Munby J in Ben Hashem v Al Shayif [2009] 1 FLR 115, to be used only ‘when all other more conventional remedies have proved to be of no assistance’ (Lord Clarke).

Comment

The Supreme Court’s judgment provides some welcome clarity. First, the explicit acknowledgement that a veil-piercing jurisdiction exists is helpful after doubts were sown by Lord Neuberger in VTB Capital plc v Nutrikef International Corp. It is also now
clear that family law cannot take an independent approach to this issue, contrary to dicta in cases such as *Nicholas v Nicholas* [1984] FLR 285.

Lord Sumption’s distinction between ‘concealment’ and ‘evasion’ may help in assessing the different ways in which a court approaches the veil of incorporation and in reducing the cases where it is thought necessary to lift or pierce it. Nonetheless, as Lord Sumption recognized, many cases combine both elements, while Lady Hale doubted whether all cases could be classified in this way. There is obviously scope for confusion as Lords Sumption and Neuberger disagreed on whether to class some cases (eg *Gilford Motor Co Ltd v Horne* [1933] Ch 935) as evasion or concealment. This is an area that may need further consideration in later cases. Furthermore, not all judges fully accepted a strict limitation on the principle to ‘evasion’ cases, eg Lord Mance felt it would be ‘dangerous’ to foreclose all possible future situations in which the principle might arise.

The connecting of veil-piercing with the principle that statute should not be used as an engine of fraud shows clearly that veil-piercing relies on the corporate form being used for some deliberately dishonest purpose. This is in line with the approach of the Court of Appeal in *Adams v Cape Industries plc*. The impropriety must thus be relevant impropriety—bad behaviour in itself does not justify piercing the veil. What matters is an improper purpose in the use of the company, although there need not have been an improper purpose in creating the company (*Ben Hashem v Al Shayif*). Furthermore, although it was acknowledged that Mr Prest had himself ignored the corporate veil and misapplied corporate assets (the group was described as his ‘money box which he uses at will’ (Moylan J)), such behaviour does not allow a court to disregard the corporate veil in the same way.

**Conclusion**

Arguably *Prest v Petrodel Resources Ltd* made few changes to company law. After all, in essence it confirms the existence of a principle that was not generally in serious doubt and, to a significant extent, confirms earlier case law on when it should apply.

However, the case emphasizes the principle’s status as a ‘last resort’—where no other legal principle can aid the claimant. It also provides further guidance on the limited circumstances in which veil-piercing may be permitted. It might, therefore, be expected that the number of cases seeking to pierce the veil will reduce still further and claims evoking the principle will be more carefully formulated. Any future attempt to expand veil-piercing beyond ‘evasion’ cases will have little support; even Lord Mance (who, along with Lady Hale, declined to limit the principle) observed ‘no-one should … be encouraged to think that any further exception … will be easy to establish, if any exists at all’.

Despite Mrs Prest’s success on the facts, *Prest v Petrodel Resources Ltd* does not give a spouse in Mrs Prest’s position much comfort from company law. Only if the company is being used in order to evade liability or frustrate enforcement will the veil be pierced, and only impropriety in that sense is relevant to the court’s determination. This conclusion is undoubtedly positive from the sense of legal and commercial clarity but may be unappealing to a layperson who would, like Mr Prest himself, view the company and controller as one and the same. The use of trusts gives hope to the non-controlling spouse in these cases, but one must wonder if this re-opens uncertainty as to the ownership of ‘corporate’ assets that the case had otherwise sought to close.
Question 5

Analyse the way in which the law has evolved to enable corporate bodies to be held liable for tortious and criminal offences requiring the establishment of intent or privity with particular regard to corporate manslaughter.

Commentary

This question requires you to examine the development of the identification theory for the purpose of establishing tortious and criminal liability, recognizing the limitations of the common law approach as regards the successful prosecution of companies for manslaughter. The solution to this is the creation of a statutory offence of corporate manslaughter and the scope of the legislation in moving from the doctrine of attribution to the gross negligence test.

Answer plan

- Explanation of the ‘identification theory’ and its application to tort and criminal offences
- Limitations on the application of the theory to cases of corporate manslaughter, particularly in the case of large companies
- Explanation and analysis of the scope of the statutory offence of corporate manslaughter

Suggested answer

Very early on, English law solved the problem of making a company liable in tort and crime in cases where it is necessary to establish criminal or tortious intention. The courts developed the identification theory, or alter ego doctrine, which attributes the requisite intention or knowledge of a person, or persons, controlling the company to the company, making the company tortiously or criminally liable.

In respect of tortious liability, in Lennard’s Carrying Co Ltd v Asiatic Petroleum Co Ltd [1915] AC 705, the appellant shipowners were sued for damages for the loss of cargo caused by a ship running aground due to its being unseaworthy because of defective boilers. The House of Lords ruled that the necessary fault or privity to establish liability could be identified in respect of the company where the fault or privity existed in the mind of a person who was ‘the directing mind and will’ of the company. Criminal liability of companies for crimes requiring a mental element was established in 1944 when companies were convicted of intent to deceive (DPP v Kent and Sussex Contractors Ltd [1944] KB 146) and conspiracy to defraud (R v ICR Haulage Ltd [1944] KB 551) with the court imputing the knowledge and intention of the company’s ‘human agents’ to the company. In HL Bolton (Engineering) Ltd v TJ Graham & Sons Ltd [1957] 1 QB 159, Denning LJ stated, ‘Some of the people in the company are … nothing more than hands
to do the work ... Others are directors and managers who represent the directing mind and will of the company, and control what it does. The state of mind of these managers is the state of mind of the company and is treated by the law as such.' In *Stone & Rolls Ltd v Moore Stephens* [2009] UKHL 39 where a one-man company had been set up solely as a vehicle for defrauding banks, the House of Lords held that the company was primarily, rather than vicariously, liable for the frauds perpetrated by the sole member/director.

The limits of the identification theory were demonstrated in *Tesco Supermarkets Ltd v Nattrass* [1971] 2 All ER 127 where a branch manager was held not to be identified with the company, allowing the company to avoid liability for misleading pricing under the Trade Descriptions Act 1968, showing that the bigger and more complex the company, the easier it will be for liability to be avoided. In *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 AC 500, Lord Hoffman considered the attribution of liability to companies in some detail. He emphasized that whose thoughts and/or acts should be attributed to the company will depend upon the rule of law that is being applied and so the ‘directing mind and will’ formulation is not the only test for attribution. Despite *Meridian Global Funds Management Asia Ltd v Securities Commission* it is clear that the ‘directing mind and will’ rule still applies in most cases (e.g. *A-G’s Reference (No. 2 of 1999)* [2000] QB 796), as was apparent in *R v St Regis Paper Company Ltd* [2012] 1 Cr App R 14 where the Court of Appeal applied the principle and rejected any alternative special rule of attribution. The Law Commission has recently (July 2013) suggested that its next programme of law reform could include a full consideration of corporate liability (following consultation on liability in regulatory contexts in 2010) including consideration of whether liability should move away from the identification model.

Since there is a statutory penalty of life imprisonment, companies cannot be guilty of murder but *R v HM Coroners for East Kent, ex p Spooner* (1987) 3 BCC 636, DC established that a company could be guilty of manslaughter. Since this necessitated the identification of the company with an individual guilty of the crime, the prosecution of P&O Ferries failed when the guilt of the managers could not be established. The judge rejected prosecution arguments that the knowledge and intentions of the individual managers should be aggregated to establish the criminal intention of the company: *R v P&O Ferries (Dover) Ltd* (1991) 93 Cr App Rep 72.

The first conviction for corporate manslaughter arose from the deaths of four teenagers on a canoeing trip at sea against a one-man company operating an activity centre. The managing director’s failure to heed previous warnings of potential danger by the company’s instructors was attributed to the company and both were convicted of manslaughter: *R v Kite and OLL Ltd* [1996] 2 Cr App Rep (S) 295. The fact that it was easier to prosecute small companies was criticized in *Re Attorney-General’s Reference (No. 2 of 1999)* [2000] QB 796.

Public pressure to reform the law on corporate manslaughter finally resulted in the Corporate Manslaughter and Corporate Homicide Act 2007 (CMCHA 2007) which came into force on 6 April 2008 and created a statutory offence of corporate manslaughter (corporate culpable homicide in Scotland).

The offence builds on gross negligence manslaughter and is concerned with the way in which an organization’s activities were managed or organized and whether an adequate
standard of care was applied to the fatal activity. The offence is committed where an organization owes a duty to take reasonable care for a person’s safety and the way in which activities of the organization are managed or organized by senior management amounts to a gross breach of this duty causing death of a person or persons. A substantial part of the failing must have occurred at senior management level, ie those making significant decisions about the organization or substantial parts of it, including those carrying out HQ functions as well as those in senior operational management roles. The identification of senior management will depend on the nature and scale of the organization’s activities. Apart from directors and similar senior management positions, roles likely to be considered include regional managers in national organizations and managers of different operational divisions.

The organization concerned must owe a ‘relevant duty of care’ to the victim in respect of systems of work and equipment used by employees; the condition of worksites and other premises occupied by an organization; and products or services supplied to customers. These duties are set out in CMCHA 2007, s. 2 and include: employers’ and occupiers’ duties, duties connected to supplying goods and services, commercial activities, construction and maintenance work, using or keeping plant, vehicles, etc, and duties relating to holding a person in custody. The duty of care will apply to persons working or performing services for the organization and could include subcontractors and persons supplying services other than employees. It is for the judge to decide whether a relevant duty of care is owed: CMCHA 2007, s. 2(5). Common law rules preventing a duty of care being owed by one person to another through joint engagement in unlawful conduct or because of voluntarily acceptance of risks are to be disregarded: CMCHA 2007, s. 2(6).

The CMCHA 2007 sets out a number of exemptions covering deaths connected with certain public and government functions. The management of these functions involves wider questions of public policy and is already subject to other forms of accountability. Areas in which exemptions apply include military operations, policing, emergency response, child protection work, and probation.

Organizations convicted of the offence can receive: (a) an unlimited fine; (b) a publicity order requiring them to publicize the conviction and details of the offence; or (c) on the application of the prosecution after consultation with the appropriate regulatory authority or authorities, a remedial order requiring them to address the cause of the fatal injury. Failure to comply can lead to prosecution and an unlimited fine on conviction.

In England and Wales and in Northern Ireland the consent of the Director of Public Prosecutions is needed before a case can be taken to court. In Scotland all prosecutions are initiated by the Procurator Fiscal. Subject to this, in England and Wales and in Northern Ireland individuals can bring a private prosecution for the new offence, but it is no longer possible to bring proceedings for common law gross negligence manslaughter against an organization to which the 2007 Act applies: CMCHA 2007, s. 20. In Scotland, the common law continues in force and the Procurator Fiscal will determine the appropriate charge according to individual circumstances.

Instead of identifying the individual guilty of the breach of care, the CMCHA 2007 identifies the senior management as those having a significant role in the decision making, management, or organization of the whole or a substantial part of the
organization’s activities (CMCHA 2007, s. 1(4)(c)) and avoids the problem with larger organizations where the complexity of the structure might otherwise lead to evasion of liability. In addition, the standard of gross negligence is an objective one whose breach falls below what can reasonably be expected of the organization in the circumstances: CMCHA 2007, s. 1(4)(b).

In conclusion, the new offence should have far-reaching implications for a larger group of organizations, including government departments previously covered by Crown privilege and senior individuals within those organizations.

Further reading

Ferran, E., ‘Corporate attribution and the directing mind and will’ (2011) 127 LQR 239
Field, S., and Jones, L., ‘Death in the workplace: who pays the price?’ (2011) 32 Co Law 166
Griffin, S., ‘Holding companies and subsidiaries—the corporate veil’ (1991) 12 Co Law 16
Kahn-Freund, O., ‘Some reflections on company law reform’ (1944) 7 MLR 54
Linklater, L., ‘“Piercing the corporate veil”—the never ending story?’ (2006) 27 Co Law 65
Moore, M., ‘A temple built on faulty foundations’ [2006] JBL 180
Ottolenghi, S., ‘From peeping behind the corporate veil, to ignoring it completely’ (1990) 53 MLR 338
Samuels, A., ‘Lifting the veil’ [1964] JBL 218
Schmitthoff, C. M., ‘Salomon in the shadow’ [1976] JBL 305
Sullivan, G. R., ‘The attribution of culpability to limited companies’ [1996] CLR 515