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DEMYSTIFICATION OF CORPORATE INDEPENDENCE THEORY IN COMPARATIVE LAW

Anifalaje Kehinde[1]

Abstract

The article examines the evolution of the common law theory of corporate personality and its accompanying benefits. By reference to empirical analysis, the paper explores the exceptions that have been made to the corporate independence theory by the legislature and the common law courts in comparative law. A succinct appraisal of those exceptions is made and it is concluded that the benchmark for ignoring the concept of corporate personality judging especially from the decisions of the courts has not followed any consistent pattern. The paper therefore argues for a need to have a more specific statutory guidelines to serve as reference points for the courts in appropriate cases when dealing with issues of lifting of the corporate veil especially between holding and subsidiary companies.

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1. Introduction

The concept of corporate personality is pre-eminent in company law. Under the classical theory of corporate existence, the corporation is regarded as a juristic person, endowed with life and capacity, and its affairs and separate identity is normally held sacrosanct and usually respected by the courts. A validating evidence of this principle in so far as non-commercial corporations are concerned could be traced to the statement of Sir Edward Coke in the early 17th Century in *Suttons Hospital case*[2] when he stated that a corporation was something invisible, immortal, existing in intendment and consideration of the law as a separate entity different from its members. Generally however, the corporation in the world of commerce is meant to serve as a device whereby, among its other purposes, one may do business with the risk of losing not all of one's possession but only that portion thereof which one has invested in the business in question. It is because of the various advantages of incorporation that numerous business people today prefer to trade by means of companies with limited liability rather than trading as a sole proprietor or in partnership with others.

The object of this paper is to examine the theory of corporate personality, its attendant benefits, and the statutory qualifications thereto in Nigeria, United Kingdom (U.K.), Brazil and the United States of America (USA). Thus, the paper will examine the relevant provisions of the Companies and Allied Matters Act (CAMA) 1990 (Nigeria), the Companies Act, 2006 (U.K.0, the New Brazilian Corporation Law, 1976 and the Delaware Corporation Law respectively. The paper will also examine notable exceptions which the common law courts have developed generally to delineate the legitimate use of the corporate form from the perspective of comparative law. The paper will conclude with a discussion of some aspects of the extant Nigerian corporate law that deserve more attention by the policymakers for purposes of reform.

2. Relevant Historical Antecedents

The development of the concept of corporate personality in the common law countries is traceable to public demands especially, the yearnings of business men to have their

2 77 E.R. 960

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unincorporated companies registered as incorporated companies with the object of acquiring the power to sue or be sued, as well as, limiting their liability in the event of trade loss. Initially, unincorporated companies could only strive to express their desires of having their liabilities limited by expressly contracting in every case that, liability should be limited to funds of the company – a solution only practicable where the contracts were of a formal type, such as for example, insurance transactions because, it was generally believed that a statement to this effect in the Deed of Settlement would be ineffective even if the creditor had notice of it.[3]

However, the Joint Stock Companies Act, 1844 (U.K.) introduced the incorporation of a company by registration but excluded the limited liability concept thereby preserving the personal liability of the members. The liability was to cease only three years after they had transferred their shares by registered transfer and creditors had to proceed first against the assets of the company by virtue of section 66 thereof. Also, the Companies Clauses Consolidation Act of 1845 merely solved the legal and not the commercial problems for it also denied members of a company freedom from personal liability and the economic slump of 1845-1848 drew poignant attention to the consequences of its absence.[4] A Royal Commission set up in 1854 containing representatives from England, Scotland and Ireland by a majority signed a Report, opposing the general extension of limited liability to Joint Stock Companies. Indeed, one of the protagonists of the limited liability concept on the Commission had vehemently argued that:

> *If there was a rule established by reason, authority and experience, it is that the interest of a community is best consulted by leaving to its members, as far as possible, the unrestricted and unfettered exercise of their own talents and industry and that restraint on limited liability offended against this golden rule.*[5]

Nevertheless, a Limited Liability Bill was passed into law in 1855. The Bill was however later repealed and incorporated in the Joint Stock Companies Act of 1856.

3 See L.C.B. Gower, 1979, *Principles of Modern Company Law,* (4th ed.) London, Stevens & Sons, p. 35
4 Ibid, p. 43.
5 See G.W. Bromwell Q.C. 1854, B.P.P. Vol. XXVII, p. 445.

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The 1856 Act allowed incorporation with limited liability to be obtained with a freedom almost amounting to licence. All that was required was for seven or more persons to sign and register a memorandum of association. The other requirements were in respect of the use of the word "limited" and provisions for registration and publicity. With this development, it was then made possible for business people to incorporate a company and at the same time have the liability of members limited to the amount contributed to the enterprise.

3. The Corporate Personality Evolution

The Companies Act 1862 (U.K.), gave power to seven or more persons to carry on business as a limited liability company because the limited liability Joint Stock Company was considered a necessary instrument of commercial progress. Thus, the privileges attaching to commercial corporations were granted to enable risky adventures to be embarked upon without the additional burden of personal liability of traders. However, the court in the celebrated case of *Salomon* v *Salomon*[6] considered it of great commercial importance as well, to encourage a trader or a group of small traders to utilise their capital in businesses conducted in the form of limited liability companies with little risk by making a distinction between the company and the men behind it. It was thus established in that case that, upon incorporation a company is generally considered to be a legal entity separate from its shareholders.

In *Salomon* v *Salomon*[7], the appellant, Aron Salomon had for some thirty years prior to 1892 carried on business as a leather merchant and hide factor and wholesale and export boot manufacturer under the style of A. Salomon & Co. A limited company was formed in 1892 to carry on the business, the subscribers to the memorandum of association being the appellant, his wife and daughter, and his four sons. The company purchased the business as a going concern for £39,000. The price was satisfied by £10,000 in debentures, conferring a charge over all the company's assets, $20,000 in fully-paid £1 shares and the balance in cash. Seven shares were subscribed in cash by the members and the result was that Salomon held 20,001 of the 20,007 shares issued

6 (1895 – 99) All E.R. 33
7 *Supra*

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and each of the remaining six shares was held by a member of his family apparently as a nominee for him. Salomon was thus the company's principal shareholder and its principal creditor. The company almost immediately ran into difficulties and only a year later, the then holder of the debentures appointed a receiver and the company went into liquidation. Its assets were sufficient to discharge the debentures but nothing was left for the unsecured creditors.

The trial court and the Court of Appeal held that the whole transaction was contrary to the true intent of the Companies Act and that the company was a mere sham and an "alias", agent, trustee, or nominee for Salomon who remained the real proprietor of the business. As such, the company was held entitled to be indemnified by the appellant to the amount of its trading debts. But the House of Lords in a unanimous decision reversed that decision of the Court of Appeal upon critical interpretation of the 1862 Companies Act and held that a company which had complied with the requirements relating to the incorporation of companies contained in the Companies Act was a legal entity separate and distinct from the individual members of the company with rights and liabilities appropriate to itself and that the motives of those who promoted the company were absolutely irrelevant in discussing what those rights and liabilities were.[8]

The court further stated that, it mattered not that all the shares in the company were held by one person, excepting one share each held by the persons who, as required by the Act, had subscribed their names to the memorandum of association to enable the company legally to be formed, nor did it matter that these persons were merely the nominees of the principal shareholder. According to the Court, the Act enacted nothing as to the extent or degree of interest which may be held by each of the seven shareholders, or as to the proportion of interest or influence possessed by one or the majority of the shareholders over the others and that one share was enough.

Consequently, the House of Lords held that the business belonged to the company and not to Salomon, and that the company was not the agent of the shareholders to

8 See Lord Halsbury, L.C. at p. 35

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carry on their business for them, nor was it the trustee for them of their property. The case thus established the distinct corporate personality of a company from that of its members thereby giving judicial force to the true intent and meaning of the Act which was to give a company legal existence with rights and liabilities of its own, whatever may have been the ideas or schemes of those who brought it into existence. The view has been expressed that it was not unlikely that a company constituted like that under *Salomon's case* was not in the contemplation of the legislature at the time when the Act authorising limited company was passed, but that the function of the court was to interpret the law and not to make it and that it must be remembered that no one need trust a limited liability company unless he so please, and that before he does so he can ascertain, if he so please, what is the capital of the company, and how it is held.[9] It has thus been established in the *Salomon's case* that once the company acts, it does so in its own name and right, and not as an agent or alias of its owners. The case has also established the fact that shareholders are not liable for the company's debts beyond their initial capital investment, and have no proprietary interest in the property of the company.

Thus, once the memorandum of association is duly signed and registered, the subscribers *ipso facto* become a body corporate capable forthwith of exercising all the functions of an incorporated company. Members of a company are not generally in their personal capacity, entitled to the benefits nor would they be liable for the responsibilities or the obligations of the company. Indeed, Lord Macnaghten eloquently observed in *Salomon's case* that:

> *The company is at law a different person altogether from the subscribers to the memorandum, and, though it may be that after incorporation the business is precisely the same as it was before, the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustees for them. Nor are the subscribers as members liable, in any shape or form, except to the extent and in the manner*

9 See Lord Herschell at p. 45.

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> *provided by the Act. That is, I think the declared intention of the enactment.*[10]

In Nigeria, the position of the House of Lords in the *Salomon's case* has been given statutory expression in section 37 of the Companies and Allied Matters Act (CAMA) 1990 wherein it is provided that:

> *As from the date of incorporation mentioned in the certificate of incorporation, the subscribers of the memorandum together with such other persons as may, from time to time become members of the company, shall be a body corporate by the name contained in the memorandum, capable forthwith of exercising all the functions of an incorporated company including power to hold land, and having perpetual succession and a common seal, but with such liability on the part of the members to contribute to the assets of the company in the event of its being wound up as is mentioned in this Act.*

Therefore, once a company has complied with all the requirements of the CAMA in respect of registration and of matters precedent and incidental to it and has been duly registered by the relevant authority, the company *ex hypothesi* becomes a duly formed legal *persona* with corporate attributes and capable of incurring legal liabilities.

4. Fundamental Significance of the Corporate Personality Theory

The theory of corporate personality is the cornerstone of company law because all the relevant legal rules have been woven around it. Indeed, corporation has become the nucleus of industrial activity as it facilitates corporate investments needed for development both in the developed and developing countries of the world because of the attendant significant attributes associated therewith. The most fundamental of these attributes from which all others spring from is the fact that the legal theory of corporation establishes the doctrine of separate personality of the company. An

10 See Lord Macnaghten at p. 48.

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incorporated company is, in law, a separate and distinct entity from its shareholders and directors. In *New Resources International Ltd & Anor* v *Oranusi,*[11] the court stated that once a company is incorporated under the relevant laws, it becomes a separate person from the individuals who are its members. It has capacity to enjoy legal rights and is subjected to legal duties which do not coincide with that of its members.

Similarly in *Chartered Brains Ltd & Anor* v *Intercity Bank Plc,*[12] it was held that an incorporated company is a different legal entity from its management and that it has s separate and distinct life and existence. In *Aso Motel Kaduna Ltd* v *Deyemo*[13] it was held that the fact of the appellant's incorporation entailed that it was a company and, being a company, it had a distinct legal personality and distinct identity from its shareholders, subscribers and promoters. As such, it was not an agent of its shareholders and therefore could not be an agency of the Federal Government even if all its shares were wholly owned by that government. Thus, the corporation is a legal entity distinct from its members and is capable of enjoying rights and of being subject to duties which are not the same as those enjoyed or borne by its members.

Furthermore, flowing from the afore-mentioned juristic personality of a corporation is the intertwined concept of limited liability. The concept of limited liability affords great opportunity to business men to embark on risky adventures without the additional burden of their personal liability as the corporate structure generally protects shareholders from liability to company's creditors. Members have no individual liability to the company's creditors for debts owing by the company. As such, the liability of shareholders for the company's debts is limited to the amount they have paid or have agreed to pay to the company for its shares. Thus, creditors who have claims against the company may only proceed against the company's assets and cannot proceed against the personal or separate assets of the members as a general rule. Consequently, the most a member in the company can lose is the amount paid for the shares themselves and thus the value of individual investment.[14]

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11 (2011) 2 NWLR (Pt. 1230) 102

12 (2009) 15 NWLR (Pt. 1165) 445; See also *Vibelko Nigeria Ltd & Anor* v *NDIC* (2006) 12 NWLR (Pt. 994) 280; *A.I.B. Ltd* v *Lee & Tee Industries Ltd* (2003) 7 NWLR (Pt. 819) 366. .

13 2006) 7 NWLR (Pt. 978) 87

14 See P. L. Davies (Ed), 2003, *Gower and Davies' Principles of Modern Company Law,* 7th ed., London,

Indeed, in *Salomon* v *Salomon*[15] the House of Lords held that the company had no right of indemnity against Salomon, the major shareholder in the company. Also, in *The King* v *Portus; ex parte Federated Clerks Union of Australia*[16] it was stated that the company is a distinct person from its shareholders; the shareholders are not liable to creditors for the debts of the company. The shareholders do not own the property of the company. Thus, the doctrine of limited liability serves to attract and encourage corporate investment, much needed to facilitate development in any given society and is also believed to be the springboard to raise managerial standards in a corporate organisation.[17] It ought to be noted however, that, limited liability acts merely as a default provision. It can be "contracted around", provided creditors have the opportunity and the bargaining power to do so.[18]

Also, in recognition of the separate and distinct entity of an incorporated association, the law vests in it a legal personality which can sue or be sued in its own corporate name.[19] Thus, in *Oakes* v *Turquand and Harding*[20] it was held that the direct remedy of a creditor is solely against the incorporated company. The creditor had no dealing with an individual shareholder, and that if he was driven to bring an action to enforce any right he might have acquired, he must sue the company and not any of the members of whom it is composed. Similarly, in *Foss* v *Harbottle,*[21] it was held that where a wrong is dome to a company, the proper plaintiff is the company and not its individual members, for as long as the company is in existence, it is bound by the decisions of the majority in general meeting, who may well ratify or confirm the very act of which those individuals are complaining. Also, in *Commercial Bank Credit Lyonnais (Nig) Ltd* v *Okoli & Ors,*[22] it was held that a body corporate is a juristic person that has legal

Sweet & Maxwell, p. 176. See also N. Hawke, 2000, *Corporate Liability,* London, Sweet and Maxwell, p. 108.

15 *Supra*

16 (1949) 79 CLR 42.

17 See Amin George Forji, 2007, "The Veil Doctrine in Company Law". Available at http://www.llrx.com/features/veildoctrine.htm (Last Accessed, May 15 2014)

18 See generally, P.L. Davies, 2002, *An Introduction to Company Law, England, Clarendon, Ch. 4.*

19 See *Salomon* v *Salomon* (Supra); *Okatta* v *The Registered Trustees of the Onitsha Sports Club* (2008) 13 NWLR (Pt. 1105) 632.

20 (1867) L. R. 2 H. L. 325

21 (1843) 2 Ha. 460

22 (2009) 5 NWLR (Pt. 1135) 446. See also, Laban-Kowa v Alkali (1999) 9 NWLR (Pt. 620) 601; Ibrahim

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personality to sue or be sued.

Furthermore, incorporation enables the property of the company to be clearly distinguished from that of its members. As such, a company may own property in its own right. Although there is the general assumption that the shareholders own the company as a matter of fact, shareholders are not in law, part owners of the undertaking as the undertaking is different from the totality of the shareholding.

Therefore, a shareholder has no direct proprietary rights in the company's property beyond his shares. In *Macaura* v *Northern Assurance Company Ltd*[23] Macaura, a major shareholder had taken out policies relating to the company's timber in his own name and the same was later destroyed by fire. It was held that the policies were unenforceable by Macaura on the ground that a shareholder had no insurable interest in the company's property. Moreover, the fact that incorporation makes it possible for the company's capital to be separated from the assets of its members necessarily gives adequate protection to corporate credits even where members are secured creditors.

It ensures that the capital of the company would not be used to meet the liability of individual members to their creditors. In essence, the creditors need not bother about the financial strength of the shareholders since the company has a separate and identifiable capital for satisfaction of their credit. In *Georgewill* v *Ekine*[24], it was held that the property of the company is quite different from that of the members and that members could not treat the company's property as if it was their personal property. Also in *The King v Portus; ex parte Federated Clerks Union of Australia*[25]the court stated that the shareholders are not liable to creditors for the debts of the company. The shareholders do not own the property of the company.

Another significance of incorporation is the increased facility it gives the company for borrowing money. Once incorporated, a company can raise money on debentures, and

v N.U.B. Ltd (2004) 10 NWLR (Pt. 885) 537.

23 *(1925) A.C. 619*

24 (1998) 8 NWLR (pt. 562) 454, C.A.

25 *(1949) 79 CLR 42*

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any member of a company acting in good faith is as much entitled to take and hold the company's debentures as any outside creditor.[26] Also, incorporation facilitates the transfer of the members' interests as shares constitute items of property which are freely transferable in the absence of express provision to the contrary in the articles of association of the company or any other law. It is however important to state that in Nigeria, restriction has been placed on transfer of shares for a private company limited by shares by virtue of section 22 of CAMA.

Also, incorporation gives perpetual succession to the company. A corporation, as a juristic person in law, cannot be incapacitated by illness, mental or physical. Unlike a natural person whose legal existence terminates at death, a corporation has not (or need not have) an allotted span of life. It is immortal as long as the law creating it allows its existence and it is only subject to demise in accordance with the law.[27] As such, a change in membership or death of a member does not affect the existence of the company. Also, it has been argued that the application of the corporate personality principle by the courts has made it less intractable to solve basic legal issues relating to the companies' activities such as its legal competence, scope of its capacity, as well as rights and liabilities of the joint stock body.[28]
Conversely, incorporation entails a lot of formalities and is necessarily attended with some expense and with a loss of privacy.

It should be noted however, that, some of the incidents of corporate personality may not be available to shareholders of American companies. In *Re Rieger, Kapper & Altmark*[29] for example, it was held that on the bankruptcy of a firm, the property of a company it formed to manufacture goods which the firm sells could be pursued for satisfaction of its creditor. Similarly, with regards to the property of the company viz-a-viz the interest of the shareholders of a company, it was held in *Riggs* v *Commercial Mutual Insurance Co*[30] that a shareholder has an insurable interest in the assets of his

26 See Lord Macnaghten in *Salomon's case* at p. 48
27 See Commercial Bank (Credit Lyonnais(Nig.) Ltd v Okoli & Ors (2009) 5 NWLR (Pt. 1135) 446; New Resources International Ltd & Anor v Oranusi (Supra)
28 See Akanki, O, "The Relevance of Corporate Personality Principle", (1977-1980), 11 *Nigerian Law Journal*, p. 14
29 (1907) 157 Fed. 609
30 125 N.Y. 7

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company. Also, whereas the separate identity of parent and subsidiary companies is recognised under Anglo-Nigerian laws, it is ignored under the American law. As such, a loan to a subsidiary is treated as an equity investment by the parent making it and it is payable only after outside creditors of the subsidiary have been paid in full.

This approach is dubbed the "Deep Rock Doctrine." In *Taylor v Standard Gas Co*[31] for instance, it was held that insiders who become creditors of a company are subordinated to other creditors when the company goes insolvent. However, this will happen only where it is equitable to so do. In *Anderson* v *Abbott*[32] a group of companies had been formed to take over the legitimate business of another for better management; without violating any rule of law or policy and without allegations of fraud, the shareholders of the parent company were still compelled, on failure of one of the companies which had insufficient capital for the scope of its activities, to contribute more money than they had agreed or owed to the company to satisfy other creditors. It has been rightly argued that the American "Deep Rock Doctrine" has the disadvantage of making decentralisation of large business organisation by way of holding and subsidiary companies less attractive and may stultify the rule that allows amalgamation and take over for efficient management.[33]

5.0. Governmental Policy Developments

It is trite that the consequence of recognising the separate personality of a company is to draw the veil of incorporation over the company and no one is entitled to go behind the veil. Consequently, officers and members of an incorporated company are covered by the company's veil of incorporation and that veil cannot be lifted, as a matter of course, for the purpose of attaching legal responsibility or liability to its officers who are carrying on the usual business of the company.[34] It is however incontrovertible that no matter how beneficial legal concepts might be, they are apt to conflict with some of the diverse human activities and interests. And where no such conflict exists, concepts

31 306 U.S. 307 (1939); 149 F. 2d. 996

32 321 U.S., 349 (1944)

33 See Akanki, O. (n. 26)., 32.

34 See e.g. Agbonmagbe Bank v G.B. Ollivant (1961) 1 All NLR 116; Ogbodu v Quality Finance Ltd (2003) 6 NWLR (Pt. 815) 147; Yusuf v Adewuyi Brothers (1991) 7 NWLR (Pt. 201) 39.

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could be used to achieve aims they are not and should not be designed to serve. Thus, whilst the concept of corporate personality has been applied by the courts to serve its important purposes, it has been used by some unscrupulous elements as a device to defeat some important values in the law.

onsequently, governments across jurisdictions have risen to the challenge through the legislature as well as the courts to readily ignore the separate identity of a corporation when it is believed that such a corporation is merely a facade, a mask or sham used by members or directors to avoid recognition in the eye of equity whilst carrying out fraudulent or illegal activities. In appropriate cases therefore, the legislature through necessary statutory intervention and the courts in the exercise of their equitable jurisdiction would, "lift or pierce the corporate veil", or "crack open the corporate shell" where the corporate structure is being used for activities that are too flagrantly opposed to justice, convenience or the interests of revenue. In *Atlas Marine Co. SA v Avalon Maritime Ltd (No 1)*[35], Staughton LJ stated that:

> *To pierce the corporate veil is an expression that I would reserve for treating the rights and liabilities or activities of a company as the rights or liabilities or activities of its shareholders. To lift the corporate veil or look behind it, therefore should mean to have regard to the shareholding in a company for some legal purpose.*

Thus, in cases where the principle of corporate personality is ignored as well as the limited liability of the shareholders, it is said that the "veil of incorporation" is lifted to see who really are the brains and hands controlling the company so as to make them personally responsible for the acts of the company.[36] In doing this, the law either goes behind the corporate personality to the individual members, or, in the case of a group of associated companies, it ignores the separate personality of each company in favour of the economic entity constituted by such group. The doctrine of 'lifting the veil' however varies from one country to the other. In the United States of America, the doctrine of "lifting the veil" is generally referred to as "piercing the corporate

35 (1991) 4 All ER 769.
36 See also Young J. in Pioneer Concrete Services Ltd v Yelnah Pty Ltd (1986) 5 NSWLR 254 .

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veil".

5.1. Statutory Qualifications of Corporate Theory

In Nigeria, the Companies and Allied Matters Act (CAMA) 1990 contains a number of provisions relating to the lifting of the corporate veil which are geared towards ensuring that creditors are protected against the machinations of unscrupulous persons who may want to use the corporate structure to perpetrate fraud or other illegal activities. The first of such statutory qualifications of the corporate personality theory would be found in section 93 of the CAMA which provides to the effect that if a company carries on business without having at least two members and does so for more than six months, every director or officer of the company during the time that it so carries on business after those six months and who knows that it is carrying on business with only one or no member shall be liable jointly and severally with the company for the debts of the company contracted during that period.

This provision is geared towards the protection of the interest of the creditor who transacts business with a company at such a time that the latter is in breach of section 18 of the CAMA. Nevertheless, the directors or officers can only be liable under the section only if they have knowledge of the fact that there has been a reduction in the number of members and their liability is only in respect of debts contracted after the expiration of six months. It should also be noted that the said officers may escape being made liable under the section by transferring shares to a nominee in order to have the statutory minimum membership. They are also empowered under section 408 of CAMA to petition for winding up of the company on the ground that it cannot pay its debts exceeding N2, 000.00. It ought to be noted however, that, while the statutory minimum number of members for every company in Nigeria is two as required by section 18 of the CAMA, in England, by section 123 of the Companies Act 2006, it is possible for a single person to incorporate a company.

Another statutory qualification to the corporate personality theory would be found in section 506 of CAMA, which is similar to section 213 of the Insolvency Act 1986 (U.K.), to protect creditors in any situation where the corporate structure is used for

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fraudulent trading. Thus, the courts are empowered to lift the corporate veil if, during the course of the winding up of a company, it appears that any business of the company has been carried out in a reckless manner or with intent to defraud creditors of the company. The court, on the application of the official receiver, or the liquidator or any creditor or contributory of the company, may, if it thinks proper so to do, declare that any persons who were knowingly parties to the carrying on the business in the manner aforesaid shall be personally responsible without any limitation of liability for all or any of the debts or other liabilities of the company as the court may direct. In the U. K. however, such an application may only be brought by the liquidator. In contrast to the provisions of section 93 of the CAMA, wherein liability of those found culpable is limited to debts incurred by the company, the provisions of section 506 of CAMA and section 213 of the 1986 Insolvency Act (U.K.) cover all liabilities of the company.

Furthermore, the phrase, "any persons" may make a shareholder liable if it is proved to the satisfaction of the court that he participated in the management decision which are intended to, or likely to defraud the creditors of the company. It has been rightly argued that these sections represent a potent weapon in the hands of creditors which could be used to check the activities of over-sanguine directors.[37] However, these sections have their limitation in the sense that they can only be invoked only when the company is being wound up and the applicant must discharge the burden of proving fraud. In *Re Patrick Lyon Ltd*[38] for example, the court stated that the applicant has to show "actual dishonesty involving, according to current notions of fair trading among commercial men, real moral blame." Since this standard was difficult to attain in most instances, a new provision has been introduced in section 214 of the Insolvency Act 1986 (U.K.) to deal with what is known as "wrongful trading".

The section was introduced to deal with situations where negligence rather than fraud is combined with a misuse of corporate personality and limited liability. In this instance, there is no need to prove dishonesty. However, while section 213 covers anyone involved in the carrying on of the business, thus qualifying the limitation of

37 See L.C.B. Gower, (n. 2), p. 115.
38 (1933) Ch. 786 at 790-791.

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liability of members, section 214 is aimed specifically at directors. Section 214 states:

> (1) . . . if in the course of the winding up of a company it appears that subsection 2 of this section applies in relation to a person who is or has been a director of the company, the court, on the application of the liquidator, may declare that, that person is to be liable to make such contribution if any to the company's assets as the court thinks proper.
>
> (2) The subsection applies in relation to a person if –
>
> (a) the company has gone into insolvent liquidation;
>
> (b) at some time before the commencement of the winding up of the company,
>
> that person knew or ought to have concluded that there was no reasonable
>
> prospect that the company would avoid going into insolvent liquidation; and
>
> (c) that person was a director of the company at that time.

Thus, if a director continues to trade at a time that he knew or ought to have known that there was no reasonable prospect of avoiding liquidation, he will risk having to contribute to the debts of the company. Thus, in *Re Produce Marketing Corporation Ltd (No 2)*[39] the company had already drifted into insolvency over a period of seven years. There was no suggestion of wrongdoing on the part of the two directors involved but, they did not put the company into liquidation in time. They were held liable to contribute £75,000 to the debts of the company.

Furthermore, while section 213 and 214 of the Insolvency Act (U.K.) create a civil liability for fraudulent trading, section 993 of the Companies Act (U.K.) makes fraudulent trading a criminal offence punishable on conviction *inter alia* to imprisonment for a term not exceeding ten years or a fine (or both), for every person

39 (1989) 5 B.C.C. 569

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who is knowingly a party to the carrying on of the business of a company with intent to defraud creditors of the company or creditors of any other person, or for any fraudulent purpose. And, in contrast to the provisions of section 213 and 214 of the Insolvency Act which are applicable only when the company is in liquidation, the provisions of section 993 of the Companies Act applies whether or not the company has been, or is in the course of being wound up.[40] Although it is only the provisions of sections 213 and 214 of the Insolvency Act that operate to lift the corporate veil, section 993 of the Companies Act is a major reform of the law that the Nigerian policy makers may want to adopt in addition to the civil liability of section 506 of CAMA.

Another instance where the corporate veil would be lifted would be found in section 631(4) of CAMA which creates a criminal liability in cases where there has been a mis-description of a company and other associated irregular acts with the company's name or seal in transaction with third parties. By this section, it is an offence punishable on conviction to a fine of N500.00 for any officer of a company or any person on its behalf to use or authorise the use of any seal purporting to be the seal of the company whereon its name is not so engraved as stipulated by the Act, or to issue or authorise the issue of any business letter of the company or any notice, or other official publication of the company or to sign or authorise to be signed on behalf of the company any bill of exchange, promissory note, endorsement, cheque or order for money or goods wherein its name is not mentioned in the manner required by the Act; or to issue or authorise to be issued any bill or parcels, invoice, receipt, or letter of credit of the company wherein its name is not mentioned in the manner required by the Act.

In addition to payment of the fine, such a person shall be personally liable to the holder of any such bill of exchange, promissory note, cheque, or order for money or goods, for the amount thereof, unless it is duly paid by the company. The object of the provisions of this section no doubt, is to give adequate warning to those dealing with limited liability companies of the possible risks they face. It is also geared towards facilitating the exercise of due care by every officer of the company so as to avoid

40 See section 993(2) Companies Act, 2006 (U.K.).

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being held personally liable while professing to be acting for and on behalf of the company. For instance, in *Penrose* v *Martyr*[41] the officer of the company was held liable for accepting a bill of exchange on which the word "limited" was omitted from the name of the company.

A similar provision is contained in section 45 of the Companies Act (U.K.) wherein it is provided that it is an offence for an officer of a company, or a person acting on behalf of a company to use, or authorise the use of, a seal purporting to be seal of the company on which its name is not engraved.

Another statutory qualification of the concept of corporate personality would be found in section 290 of the CAMA. Although a director of an incorporated company cannot be held liable for the loan granted in favour of the company unless he is a surety or guarantor of the loan, section 290 of the CAMA however provides that where a company receives money by way of loan for a specific purpose and with intent to defraud, fail to apply the money for the purpose for which it was received, every director or officer of the company shall be personally liable to the person from whom the money was received.

The statutory exception will to a large extent check the excesses of companies which are only in the business of defrauding unsuspecting business partners, including creditors. Thus, in *Public Finance Securities Ltd* v *Jefia*[42] the respondent vide the undefended list procedure sued the applicants for the recovery of the sum of ₦3, 593,851.00 (Three million, five hundred and ninety-three thousand, eight hundred and fifty-one naira) with interest. According to the respondent, he had made several deposit payments totalling that amount with the 1st appellant based on the assurance and warranty of the 2nd appellant; that upon maturity, the respondent would be paid. The appellants never made good their promise to pay the respondent at the appropriate time, hence the institution of the suit by the respondent. The trial court found the appellants liable jointly and severally to pay to the respondent the sum with interest.

41 (1855) E.B.& E 499
42 (1998) 3 NWLR (Pt. 543) 602, C.A.

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The appellants' appeal to the Court of Appeal was dismissed on the application of section 290 of CAMA to the case.[43]

Similarly, in *Alade* v *Alic (Nig) Ltd & Anor*[44] the Supreme Court applied the provisions of section 290 of the CAMA to lift the veil of incorporation of the 1st respondent company on finding that the substantial amount of the loan obtained from a bank for purposes of trading activities between the company and the appellant pursuant to a partnership agreement was used in settling the company's prior indebtedness to the bank. A similar provision to section 290 of CAMA would be found in Article 158 of the Law N0 6.404 of the New Brazilian Corporation Law of 1976 which provides to the effect that while an officer shall not be personally liable for commitments undertaken on behalf of the company and by virtue of normal administrative acts, he shall however answer in civil courts for losses caused when he acts with negligence or fraud within his attributions or powers or in violation of law of corporate by-laws. Also, in the U.S.A., section 102(b)(6) of the Delaware Corporation Law for example, provides that the certificate of incorporation may contain a provision imposing personal liability for the debts of the corporation on its stockholders or members to a specified extent and upon specified conditions; otherwise the stockholders or members of a corporation shall not be personally liable for the payment of the corporation's debts except as they may be liable by reason of their own conduct or acts.

Another instance where the concept of corporate personality may be disregarded is in the preparation of financial statement of holding and subsidiary companies. By section 336 of CAMA, section 399 of the Companies Act 2006 (U.K.), and Article 275 of the New Brazilian Corporation Law No 6.404 of 1976, the directors of the holding company is required in the preparation of individual accounts for that year to also, prepare group financial statements which deal with the state of affairs and profit and loss of the company and the subsidiaries. This provision is of great importance to creditors because the group financial statement gives them a total picture of the

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43 See also section 3(3)(b)(ii) of the Failed Banks Act of 1994 which empowers the Tribunal in the exercise of its powers under the Act to, lift the corporate veil of a body corporate where it is necessary for the purpose of revealing its members who may be liable jointly or severally for the debt owed by the corporate body to a failed bank.

44 (2010) 19 NWLR (Pt. 1226) 111

financial standing of the whole group and they are better informed for purposes of subsequent transactions and the prospects of recovering the debt due from any of these companies.

5.2. Judicial Intervention .

The courts have also persistently upheld the legal theory of the corporation by holding in several cases that shareholders are not in the eye of the law, joint owners of the business of the company and that the company is distinct and separate from the shareholders with full capacity for its rights and duties. Nevertheless, there have been exceptional instances where the courts have ignored the doctrine of the corporate personality and have been constrained to lift the veil of incorporation. Generally, where it is found that the company has been formed basically for fraud or improper conduct for example, the court would, despite the limited liability rule, disregard the corporate entity of a company to make the members, officers or directors as the case may be personally liable for the acts of the company. In *United States v Milwankee Refrigerator* Co[45] the court stated that :

> *A corporation will be looked upon as a legal entity as a general rule . . . but when the notion of legal entity is used to defeat public convenience, justify wrong, protect fraud or defend crime, the law will regard the corporation as an association of persons.*

Thus, the court would neither allow the corporate theory to be used as an instrument to perpetrate fraud nor as a device to evade a contractual or other legal obligation. Where there is a fraud or a deliberate breach of trust, the courts would lift the corporate veil to achieve justice. In *Standard Chartered Bank v Pakistan National Shipping Corporation*[46] it was established that reliance upon fraudulent representation was in itself sufficient, irrespective of other matters, to lift the veil. In *Alade* v *Alic (Nig) Ltd & Anor*[47] the appellant had entered into a partnership agreement with the 1st respondent, a registered company, for trading purposes. The 2nd respondent was the managing

45 145 F. 1007, 1012 (C.C.E.D. Wis. 1906.)
46 (2003) A.C. 959
47 (Supra)

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director and virtual owner of the 1st respondent. Based on the agreement, the appellant raised a loan for use in the trading to be carried out by the respondent from a bank, the International Bank for West Africa.

Meanwhile, the 1st respondent was already a customer of the said bank and was indebted to the bank but, the 2nd respondent who carried out the transaction on behalf of the 1st respondent did not disclose this fact to the appellant. When the loan was credited into the account of the 1st respondent for purposes of trading on produce, the bank used the sum to off-set the indebtedness of the 1st respondent. The 2nd respondent kept the appellant in the dark of all the transactions of the 1st respondent and refused to render accounts of its trading activities under the partnership. Based on this, the appellant instituted an action at the High Court to claim a certain sum of money as damages suffered as a result of the 1st respondent's breach of partnership agreement, and which breach was masterminded, procured and instigated by the 2nd respondent as agent of the 1st respondent in fraud of the appellant. The court held that the conduct of the 2nd respondent amounted to fraud which justifies the lifting of the veil of incorporation of the 1st respondent in order to see the fraud perpetrated by the 1st respondent on the appellant.

In the instant case, the Supreme Court stated that the court would not allow a party to use his company as a cover to dupe, cheat or defraud an innocent citizen who entered into lawful contract with the company, only to be confronted with the defence of the company's legal entity as distinct from its directors.[48] In *Gilford Motor Co* v *Horne,*[49] the defendant, a former employee of the plaintiffs, had covenanted not to solicit its customers. He however attempted to evade this obligation by forming a company which undertook the soliciting. An injunction was granted against both him and the company notwithstanding that the company was not a party to the covenant. The company was described as "a device, a stratagem" and a mere cloak or sham. Also, in *Jones* v *Lipman*[50]the defendant attempted to avoid completing the sale of his house to the plaintiff by conveying it to a company formed for the purpose. The plaintiff

48 See *per* Muntaka-Coomassie J.S.C. at p. 142, paras C-E.
49 (1993) Ch. 935
50 (1962) 1 W.L.R. 832

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applied to the court for an order of specific performance against the defendant and the company. The court ordered a specific performance of the agreement between the defendant and the plaintiff on the ground that the company was nothing but a device and a sham, a mask which he holds before his face in an attempt to avoid recognition by the eye of equity. The cases of *Gilford Motor Co* v *Horne* and *Jones v Lipman* clearly show the readiness of the court to lift the veil of incorporation in order to compel the defendants to honour their obligations in the interest of justice.

Also, in the U.S. case of *Walkovszky* v *Carlton*[51] the Court of Appeal of New York held that the law permits the incorporation of a business for the very purpose of enabling its proprietor to escape personal liability but, manifestly, the privilege is not without its limits. Broadly speaking, the courts will disregard the corporate form, or, to use accepted terminology, "pierce the corporate veil" whenever necessary "to prevent fraud or to achieve equity." It must be noted however, that while the court would readily lift the veil of incorporation in order to prevent the owners from perpetrating a fraud, they would not do so in order to assist them from escaping its consequences. Thus, in *R v Arthur,*[52] a director who was charged with fraudulent conversion of company property claimed that he had acted with the consent of his co-director with whom he had shared the spoils, and that the two of them and their wives were the only members. In convicting him, the court held that this was no defence as the company was a separate legal entity. Also, it has been held in *Chimwo* v *Owhonda & Ors,*[53]that allegation of crime lifts the veil of corporate or voluntary associations and opens up the body to judicial enquiry upon good and substantial facts placed before a court of competent jurisdiction.

Also, where a corporate structure has been used by a defendant to avoid such rights of relief as third parties already possess against him, the veil of incorporation would be lifted. In *Re a Company*[54] wherein the corporate veil was lifted, the Court of Appeal stated that the court would use its power to pierce the corporate veil if it is necessary

51 (1966) 18 N.Y 2d. 414
52 (1967) Crim. L. R. 298.
53 (2008) 3 NWLR (Pt. 1074) 341
54 (1985) BCLC 333

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to achieve justice irrespective of the legal efficacy of the corporate structure under consideration. In the case, it was held that the evidence established that the defendant had created a network of English and foreign companies and trusts through which he could dispose of his English assets and, when the insolvency of the plaintiffs was imminent and after the alleged fraud had been committed, he had used this network to dispose of his assets. The court stated that in these circumstances, the corporate veil could be pierced in order to achieve justice.

Furthermore, it has been established in *Woolfson v Strathclyde Regional Council*[55] that the veil can be lifted where special circumstances exist indicating that the company is a mere facade concealing the true facts.

Moreover, the corporate veil will be lifted where it is necessary for purposes of determining the actual residence of a registered company. This usually arises where it is suspected for instance, that a company is owned or controlled by alien enemy or similar persons. The test here is to determine the place of its central management and control. In such a case, the residence of its controlling members may be treated as the residence of the company. For example, in *Daimler Company* v *Continental Tyre and Rubber Company*[56] the court demonstrated its readiness to lift the corporate veil while construing the meaning of Trading with the Enemy Act 1914, a statute unrelated to company law, so as to fulfil the purpose of the legislation regardless of the existence of the corporate form. In the instant case, a company was incorporated in England with the object of selling tyres manufactured in Germany by a German company.

In the English company, the majority of the shares were held by Germans and the directors of the company were Germans resident in Germany. The circumstances revealed that the English company was controlled by the Germans. In the course of the 1st World War, the English company filed a suit to recover a trade debt. It was held that the company had become an enemy company as it was controlled by residents in an enemy country and as such, the suit filed by it was incompetent and it was therefore

55 (1978) SC (HL) 90
56 (1916) 2 A.C. 307

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dismissed. The court further remarked that it would be against public policy to allow alien enemies to trade behind a corporate facade. The court disregarded the company's British identity by virtue of registration and instead focussed attention on the control of the company's assets and identity of the controlling members.

One other area where the lifting of the corporate veil has been of great importance is in the treatment of holding and subsidiary companies. By section 338 of the CAMA, a body corporate is to be regarded as the subsidiary of another, that is, the holding company, if the holding company is a member of it and controls the composition of its board of directors in the sense that it has power to appoint or remove a majority of the board or, if it holds more than half of its "equity share capital," that is, the issued shares. In the U.K. however, section 1159 of the Companies Act 2006 provides inter alia that a company is a 'subsidiary' of another company, its 'holding company', if that other company either holds a majority of the voting rights in it, or is a member of it and has the right to appoint or remove a majority of its board of directors; or is a member of it and controls alone, pursuant to an agreement with other members, a majority of the voting rights in it; or if it is a subsidiary of a company that is itself a subsidiary of that other company.

Generally, where a business is carried on through a group of companies, the fundamental principle of corporate personality equally applies to each of the companies. In effect, individual subsidiaries within a conglomerate will be treated as separate entities and the parent company cannot be made liable for the subsidiaries' debts on insolvency. As such, all companies in a group of companies are separate legal entities possessed of separate legal rights and liabilities and are not the agents of their controlling shareholders.

In *The* Albazero[57] where a cargo of crude oil was transported by Concord Petroleum Corporation, a wholly-owned subsidiary of Occidental Petroleum Corporation, the English Court of Appeal reaffirmed that each company in a group of companies is a separate legal entity possessed of separate legal rights and liabilities. Thus, a parent

57 (1977) A.C. 774 at p. 807. Per Roskill LJ

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company is allowed under this arrangement to conduct its more risky or liability-prone activities through its subsidiary companies.[58] Furthermore, the holding company can create subsidiaries with inadequate capitalisation and secure loans to the subsidiaries with fixed charges over their assets, despite the fact that this is "not necessarily the most honest way of trading."[59] Nevertheless, the courts, just like in the case of a single corporation, would where necessary, lift the veil of incorporation in order to get at the economic entity constituted by such group of associated companies. Thus, if a subsidiary company is found to be acting as an agent for its holding company, based on the agency principle, the latter may be bound by the same rights and liabilities of its subsidiary.

In *Smith, Stone & Knight Ltd* v *Birmingham Corporation,*[60] the holding company bought a partnership firm and registered it as a company to carry on business as its subsidiary, but never assigned the business to be transacted to the newly-formed company. The parent company had complete control over the operation of the other company. A parcel of land owned by the subsidiary was however compulsorily acquired by the defendant and the holding company claimed compensation for the disturbance of the business of its subsidiary. The court held that from the facts of the case, the subsidiary acted as the agent of the holding company which should be regarded as being in occupation of the premises. The court further remarked that the separate legal personalities of two entities were not conclusive of the matter but rather the determining factor remains whether there is effective, total and constant control of the subsidiary by the holding company. Furthermore, the court laid down six tests to serve as guiding principles for the courts in determining whether the veil should be lifted in a holding and subsidiary relationship.

The tests are whether the profits of the subsidiary are treated as the profits of the parent company; whether the persons conducting the business of the subsidiary are appointed by the parent company; whether the parent company was the head and brain

58 See *The U.K. 'S Approach to the Lifting of the Corporate Veil.* Available at http://www.lawteacher.net/company-law/essays/the-uks-approach-law-essays.php. (Last Accessed, 20 May 2014)

59 See per Staughton, LJ in *Atlas Maritime C. S.A.* v *Avalon Maritime Ltd, (No 1)* (1991) 4 All E.R. 769.

60 (1934) All E.R. 116

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of the venture; whether the parent company govern the adventure, decide what should be done and what capital the venture should have; whether the company makes a profit through the parent company's skill and direction and whether the company was given effectual and constant control. Where all these questions are answered in the affirmative, the court would infer agency relationship between the subsidiary and the holding company in order to lift the veil of incorporation.

In *Re F.G. (Films) Ltd*[61] an American company, seeking to gain the advantages afforded to British-made films caused a company to be incorporated in England. The company had no place of business other than a registered office and no staff other than three directors, one of whom was the President of the American company. The capital was only 100 pounds, of which the President held 90 pounds. A film was produced, nominally by the English company, but with all the finance and facilities provided by the American. The court in the circumstance held that in so far as the English company had acted at all, it had done so as agent of the American company which was the true maker of the film.

Moreover, the courts have in some situations applied the trust concept to lift the veil of incorporation. Thus, in *Littlewoods Stores* v *I.R.C.*[62] the holding company, Littlewoods, had purchased a capital asset and vested it in a property holding company which was its wholly-owned subsidiary. It sought to obtain a tax advantage by relying on the fact that the subsidiary was a separate legal entity, but the court held that the subsidiary company and the holding company were one and the same. Lord Denning M. R. sounded a note of warning in the case when he declared that:

> *The doctrine laid down in Salomon's case has to be watched very carefully. It has often been supposed to cast a veil over the personality of a limited company through which the courts cannot see. But, that is not true. The courts can, and often do pull off the mask. They look to see what really lies behind. The*

61 (1953) 1 W.L.R. 483
62 (1969) 1 W.L.R. 1241

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legislature has shown the way with group accounts and the rest. And the courts should follow suit.

Furthermore, the court will disregard the corporate veil so as to treat a group of companies as a single unit where it is established that the corporate entity is used for tax evasion or to circumvent tax obligation. Thus, in *Firestone Tyre and Rubber Coy* v *Llewellin*[63] an American tyre manufacturing parent company had a wholly-owned English subsidiary company. All the directors of the subsidiary company resided in England with the exception of one who was also the President of the American company. The American company contracted with European distributors that any order they placed with it would be satisfied by its English subsidiary. However, the distributor sent their order for tyres directly to the subsidiary which met them without an approval from the American company. The subsidiary deducted its manufacturing expenses and a small commission from the proceeds of the sale of the tyres and sent the balance to the holding company.

The court held that although the English subsidiary was a separate legal entity which was selling its own goods, nevertheless, the sales were the means whereby the American parent company carried on its European business so that it was trading in the United Kingdom through the agency of the subsidiary and thus, the American company was subject to English company taxation on the deal.

Moreover, where the conglomerates are considered to be a single economic entity, the court may lift the corporate veil. In *D.H.N. Ltd* v *Tower Hamlets,*[64] Lord Denning MR. had argued on the theory of the "single economic unit" wherein the court examined the overall business operation as an economic unit, rather than strict legal form in holding that a group of companies was in reality a single economic entity and should be treated as one. In the instant case, the parent company sued the defendant claiming compensation for the disturbance of its business and that of its subsidiary within the same group of companies, when the land vested in yet another subsidiary was compulsorily acquired. The court held that the three companies should for the

63 (1957) 1 W.L.R. 464
64 (1976) 1 W.L.R. 852

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purpose, be treated as one, and that the parent company, D.H.N. should be treated as that one. However, in *Woolfson* v *Strathclyde Regional Council,*[65] it was established that the element of control is a central issue in determining whether the corporate veil should or should not be lifted. In the instant case, there was the question as to whether a group of companies could be regarded as a single entity for legal purposes; that is whether a subsidiary and parent company could be regarded as a single entity in order to enable them to claim compensation for disturbance on a compulsory purchase.

The House of Lords ruled that Woolfson and its subsidiaries were not a single economic unit due to operational practices. The House of Lords specifically disapproved of Lord Denning's views expressed in *DHN Food Distributors Ltd* on group of companies and doubted whether the Court of Appeal properly applied the principle that it is appropriate to pierce the corporate veil only where special circumstances exist indicating a mere facade concealing the true facts.[66] Consequently, it was held that on the facts of the case, there was no basis on which the corporate veil could be pierced as there were no grounds for treating the company structure as a mere facade.

Also, in the exercise of its mareva jurisdiction, the court does lift the veil of incorporation in order to prevent a defendant from taking any action which is designed to ensure that subsequent orders of the court were rendered less effective than would otherwise be the case. Thus, in the exercise of its mareva jurisdiction to freeze assets pending the outcome of litigation, the court should not limit its consideration to funds which a defendant has a legal right if there is any reasonable ground to believe that moneys could be made available to him from other sources.

In *Atlas Maritime C. S.A.* v *Avalon Maritime Ltd (No 1)*[67] the court held that where a defendant company, which was subject to a mareva injunction sought the release of moneys from the frozen fund to meet its legal expenses, but whose circumstances suggested a close financial involvement with the parent company, the court was entitled

65 (1978) SC (HL) 90 HL (Sc).

66 See also *Adams v Cape Industries plc* (1990) BCLC 479 wherein the "single economic unit" theory was also rejected by the Court of Appeal.

67 (1991) 4 All ER 769.

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to lift the corporate veil and decline to grant the release sought, if it were satisfied that the parent company would make the necessary funds available so as not to impede the defendant company from resisting the claim against it. There is no doubt that if the decision of the court in the instant case were otherwise, the subsequent orders of the court made in favour of the plaintiff was likely to have been rendered less effective because the plaintiff might not have been able to recover the full cost awarded.

In recent times however, the English courts have exhibited great reluctance at ignoring the corporate veil especially while dealing with a group of companies. For example, in *Adams v Cape Industries Plc*[68], it was established that the corporate veil should not be pierced just because a group of companies operated as a single economic entity unless the wording of a particular statute or document justifies, because the general principle is that "each company in a group of companies . . . is a separate legal entity possessed of separate rights and liabilities." Furthermore, in that case, the circumstances under which the courts could lift the veil of incorporation were significantly narrowed down to three by the Court of Appeal. The first of those circumstances is stated to be that if the court is interpreting a statute or document wherein there is some lack of clarity which would allow the court to treat a group as a single entity. Secondly, where special circumstances exist indicating that the corporate structure is a "mere facade concealing the true facts". Thirdly, where there is an agency relationship, express or implied.

In the instant case, until 1979, Cape, an English company, mined and marketed asbestos. Its worldwide marketing subsidiary was another English company named Capasco. It also had a U.S. marketing subsidiary incorporated in Illinois, named NAAC. In 1974, some 462 people sued Cape, Capasco, NAAC and others in Texas, for personal injuries arising from the installation of asbestos in a factory. Cape protested at the time that the Texas court had no jurisdiction over it but in the end it settled the action. In 1978, NAAC was closed down by Cape and other subsidiaries were formed with the express purpose of reorganising the business in the USA to minimise Cape's presence there for taxation and other liability issues. Between 1978 and 1979, a further 206

68 (1990) BCLC 479

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similar actions were commenced and default judgements were entered against Cape and Capasco (who again denied they were subject to the jurisdiction of the court but this time did not settle). In 1979, Cape sold its asbestos mining and marketing business and therefore had no assets in the USA.

The claimants thus sought to enforce the judgements in England where Cape had most of its assets. The issue that arose was whether Cape was present in the US jurisdiction by virtue of its US subsidiaries. The only way that could be the case in the court's view was if it lifted the veil of incorporation, either treating the Cape group as one single entity, or finding the subsidiaries were a mere facade or that the subsidiaries were agents for Cape. On the argument that the Cape group should be treated as one, the court held that "save in cases which turn on the wording of particular statutes or contracts, the court is not free to disregard the principle of *Salomon v Salomon & Co Ltd*(1897) A.C. 22 merely because it considers that justice so requires." According to the court, the law, for better or worse, recognises the creation of subsidiary companies, which though in one sense the creatures of their parent companies, will nevertheless under the general law fall to be treated as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities.

The court also quoted with approval the words of Lord Keith in *Woolfson v Strathclyde Regional Council* where he stated that it is appropriate to pierce the corporate veil only "where special circumstances exist indicating that it is a mere facade concealing the true facts" and held that although Cape's motive in restructuring its US business through its various subsidiaries was to try to minimise its presence in the USA for tax and other liabilities, there was nothing illegal as such. The court stated that:

> *Whether or not such a course deserves moral approval, there was nothing illegal as such in Cape arranging its affairs (whether by the use of subsidiaries or otherwise) so as to attract the minimum publicity to its involvement in the sale of Cape asbestos in the United States of America . . . we do not accept as a matter of law that the court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group*

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merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use a corporate structure in this manner is inherent in our corporate law.

On the agency argument, it was held that the veil of incorporation could in essence be pierced when there was an express agency agreement, for example, between the parent and the subsidiary company. In the absence of such an agreement, no agency relationship could be presumed. Although the US company was found to have rendered certain services to Cape Industries Plc and even acted as its agent in relation to some specific transactions, it was held not sufficient to constitute a general agency agreement. The subsidiaries were independent businesses free from the day-to-day control of the parent with no general power to bind the parent. Accordingly, the court held that Cape was not present in the USA through its subsidiaries.

In *Samengo-Turner v J & H Marsh & McLennan (Services) Ltd,*[69] the first circumstance laid down in *Adams v Cape Industries Plc* to treat a group of companies as a single legal entity on the basis of their single economic interest in interpreting the application of EU Regulation was applied by the court. Also, in *Viho Europe BV v Commission of the European Communities*[70].it was held that a company and its subsidiaries were to be regarded as a single economic entity for the purposes of art. 85(1) of the EEC Treaty.

However, apart from providing the three circumstances under which a veil of incorporation may be lifted, the decision in *Adams v Cape Industries plc* has further established, contrary to the previous established judicial stance that, the court will not lift the veil of incorporation simply because it is thought to be necessary in the

69 (2007) 2 C.L.C. 104.
70 (1996) Case C- 73/95 P

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interest of justice.[71] In *Creasey v Breachwood,*[72]an employee had a claim for unfair dismissal against a company. After the claim arose, all assets of the company had been transferred to another company owned by the same individuals and the first company had been dissolved. The second company was joined as a party to the action. It was held that the court had power to lift the veil of incorporation to achieve justice where its exercise is necessary for that purpose. However, in *Ord v Belhaven Pubs Ltd,*[73] the decision of the court in *Creasey's case* was overruled and the decision of the Court of Appeal in *Adam's case* in this respect was affirmed.

The court further reiterated the principle that the separate legal personalities of the companies could not be disregarded on the basis that they were effectively a single economic unit. According to the court, the veil can only be pierced only if there has been some impropriety linked to the use of the corporate structure to conceal some wrongdoing. In the instant case, Ord and Belhaven Pubs Ltd were engaged in a legal action about a lease. During the course of the action the group structure of which Belhaven Pubs Ltd was a part was reorganised because of a financial crisis within the group. As a result of the reorganisation, Belhaven Pubs Ltd had no assets or liabilities and would therefore have nothing with which to pay any judgement against it. As the litigation regarding the lease was still continuing Ord applied to have the parent company of Belhaven Pubs Ltd substituted. The Court of Appeal held that holding company as a shareholder enjoys limited liability and it is not liable for the debts of the subsidiary companies whose shares it owns.

The court further held that the reorganisation of the group was legitimate and not merely a facade to conceal the true facts. The assets were found to have been transferred at full value and the motive appeared to be the group's financial crisis rather than any other ulterior motive. The court further stated that before the veil could be lifted, the court must be satisfied that a defendant acted pursuant to some improper or fraudulent motive creating or utilising a corporate facade as a sham or device to

71 See also *Hashem v Shayif & Anor.* (2008) EWHC 2380 (Fam.)
72 (1992) B.C.C. 658
73 (1998) 2 BCLC 447

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achieve something which it could not otherwise lawfully do.[74]

Also, in *Trustor AB v Smallbone*[75] during Smallbone's period as Trustor's managing director various sums of money had been transferred in breach of fiduciary duty from Trustor to another company owned and controlled by Smallbone. Trustor applied to the court to pierce the corporate veil so as to treat receipt by the second company as receipt by Smallbone on the grounds that the company had been a sham created to facilitate the transfer of the money in breach of duty. It was argued that the company had been involved in the improper acts and that the interest of justice demanded such a result. It was held that the court is entitled to pierce the corporate veil and recognise the receipt of the company as that of the individuals in control of it if the company was used as a device or facade to conceal the true facts thereby avoiding or concealing any liability of those individuals. The court however stated that for the veil to be lifted there had to be a link between the impropriety and the facade and that there is no general power to lift the veil in the interests of justice.

Similarly, in the US, the court will not pierce the corporate veil just because the interest of the case demands so. Thus, in *Perpetual Real Estate Services Inc. v Michaelson Properties Inc*[76]it was held that no piercing could take place merely to prevent "unfairness" or "injustice", where a corporation in a real estate building partnership could not pay its share of a law suit bill. Generally however, theories, such as, "alter ego" or "instrumentality rule" based upon "unity of interest and ownership", "wrongful conduct" and "proximate cause" have attempted to create a piercing standard. For example, in *Gentry* v *Plan Corporation of Houston*[77] the court stated that:

> *A subsidiary corporation will not be regarded as the alter ego of its parent merely because of stock ownership, a duplication of some or all of the directors or officers, or an exercise of the control that stock ownership gives to stockholders. On the other*

74 *Ibid* at p. 453
75 (2001) 1 W.L.R. 1177
76 974 F. 2d. 545 (4th Cir. 1992)
77 528, S.W. 2d. 571 at 573

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> *hand, where management and operations are assimilated to the extent that the subsidiary is simply a name or conduit through which the parent conducts its business, the corporate fiction may be disregarded to prevent fraud or injustice.*

It has however been argued that these theories have failed to articulate a real-world approach which courts could directly apply to their cases and have thus been driven to apply the "totality of circumstances" to analyse all given factors in any particular case.[78] Thus, in *Kinney Shoe Corp. v Polan,*[79] a corporation was undercapitalised and was only used to shield a shareholder's other company from debts, the veil was pierced because its enforcement would not have matched the purpose of limited liability.

Also, in recent times, there has been a growing concern about ameliorating the harsh effect of limited liability on tort victims and employees, otherwise called 'involuntary creditors', who are unable to contract around limited liability. Thus, in deserving circumstances, a duty of care in negligence may be deemed to be owed directly across the veil of incorporation. It has been established in *Connelly v RTZ Corp Plc*[80], at least in theory, and depending on the amount of control exerted over the subsidiary, that a parent company could owe a duty of care to the workers of the subsidiary. In the instant case, Mr Connelly has been a uranium miner working in Namibia for a subsidiary of RTZ. He subsequently developed cancer and attempted to sue the parent company in London alleging that RTZ had played a part in the health and safety procedures employed by the subsidiary and that RTZ owed a duty of care to him. RTZ applied to have the action struck out in London arguing that Connelly should sue the subsidiary in Namibia.

The majority of the House of Lords found that the matter could not be heard in Namibia because of the complexity of the case and the cost and that London was the appropriate forum. When the case was subsequently heard at the High Court and the tortuous issue was tried, RTZ argued that the subsidiary was Connelly's employer and

78 *Piercing the Corporate Veil* Available at http://en.wikipedia.org/wik/Piercing-the-corporate-veil (Last accessed 20 May 2014)

79 939 F. 2d. 209 (4th Cir.1991)

80 (1998) A.C. 854

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therefore, any duty of care was owed by the Namibian subsidiary. RTZ also argued that the claim was time barred under the Limitation Act 1980. The court refused to strike out the action on the duty of care point finding that it was arguable that the parent company had responsibility for health and safety at the mine and this would have been such as to create a duty of care to Connelly. It was however held that the claim was time barred under the Limitation Act as Connelly could have brought the case in 1989 but chose not to.

Similarly, in *Lubbe* v *Cape Industries Plc,*[81] about 3,000 employees and nearby residents of Cape Industry's wholly-owned asbestos-mining subsidiary in South Africa claimed damages from the parent company in London for death and personal injury caused by exposure to asbestos at or near the mining operation in South Africa. The House of Lords again found that South Africa was the more appropriate place to sue but that the lack of legal representation and the expert evidence required to substantiate the claim in South Africa would amount to a denial of justice. It was therefore held that the action could proceed against the parent in London. The case went back to the High Court for trial and in January 2002 Cape settled the action for £21 million.

Also, in *Chandler v Cape Plc,*[82] it was held that tort victims and employees, who did not contract with a company or have very unequal bargaining power, are exempted from the rules of limited liability. In the case, the claimant who was an employee of Cape Plc's wholly–owned subsidiary, which had gone insolvent successfully brought an action in tort against Cape Plc for causing him an asbestos disease, asbestosis. The court emphasised that piercing the corporate veil was not necessary and held that there would be direct liability in tort for the parent company if it had interfered in the operations of the subsidiary in any way, such as over trading issues.

Similarly, in the United States' case of *Minton v Cavaney,*[83] the plaintiff's daughter drowned in the public swimming pool owned by the defendant. The court held that

81 (2000) 1 WLR 1545
82 (2011) EWHC 951
83 56 Cal. 2d. 576 (1961)

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parent companies or shareholders would be treated as personally liable "when they provide inadequate capitalisation and actively participate in the conduct of corporate affairs." Also, in *Sindell v Abbott Laboratories*[84] the California Supreme Court holds drug manufacturers liable to injured victims according to their portion of market share.

By and large, it would be observed that even though attempts have been made in a few cases to provide some judicial guidelines on when to lift the corporate veil, the exercise of the courts' discretionary power to lift the corporate veil has not followed any consistent pattern as the decisions of the courts have varied from one case to the other. In *Briggs v James Hardie & Co Pty*[85] the court had remarked that:

> *There is no common, unifying principle, which underlies the occasional decision of the courts to pierce the corporate veil. Although an ad hoc explanation may be offered by a court which so decides, there is no principled approach to be derived from the authorities.*[86]

Nevertheless, a review of the judicial decisions would reveal that the courts generally lean in favour of upholding the corporate personality principle enunciated in *Salomon's case.* In peculiar situations however, such as where it is established that the corporate structure is being blatantly used as a cloak for fraud or some other improper conduct the courts are more readily disposed to finding that a company is an alias of its members. Furthermore, although it would be observed also from a review of the cases that the erstwhile view that the veil of incorporation could be lifted simply because the "justice of the case" demands no longer holds sway among the judiciary, it would still appear from general judicial reasoning that the courts do employ "equitable discretion" guided by general principles such as mala fides to test whether the corporate veil has been used as a mere device for some improper conduct.[87]

In a situation where only one person is in control of the affairs of the company, the

84 607P 2d. 924 (Cal), 449 US 912 (1980)
85 (1989) 16 NSWLR 549
86 Ibid
87 See Capuano, A, "The Realist's Guide to Piercing the Corporate Veil", *Australian Journal of Corporate Law*, (2009) 23(1) 56-94.

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greater the impropriety of such a person, the greater the likelihood of the veil being lifted to his detriment and less the likelihood of its being lifted for his advantage. However, in the case of holding and subsidiary companies, the likelihood of the veil being lifted would depend mostly on the degree and extent of control exercised by the holding company over the subsidiary as well as the financial independence of the subsidiaries.[88] Generally however, for tax and accounting purposes, a group of companies will more likely be treated as a single economic entity whereas for general civil liability, the rule laid down in *Adams v Cape Industries Plc* would most likely prevail. It has also been argued that the courts will mostly lift the corporate veil in small privately-held businesses than in big public corporations that trade on stock exchange because of the large number of shareholders in such corporations as well as the limited resources and time at the courts' disposal to handle these.[89]

6. Proposal for Rapid Progress and Stability

In spite of the comparative advantage of incorporation over other forms of business organisations, the decision in *Salomon's case* has established the fact that it is to all intents and purposes possible for just one man to incorporate a company. In Nigeria, although section 18 of the CAMA has provided in theory that there must be at least two subscribers to the memorandum of association, what obtains in practice is the apparent conflict between the legislative intent and legislative result. It is common knowledge that most companies in Nigeria are owned and managed solely by an individual, while the members of his family are registered as the shareholders.[90]

In some other situations, the second person is brought in at a fee or otherwise nominally to satisfy the statutory minimum requirement and has little or no control over the affairs of the company. In this wise, it is desirable that the law should be amended so as to permit single member limited liability companies as we have in other countries such as in the U.K.in order to reflect the prevailing socio-economic reality. In the

88 See L.C.B. Gower, (n. 2) 137.
89 See "The UK'S Approach to the Lifting of the Corporate Veil" Available at http://www.lawteacher.net/company-law/essays/the-uks-approach-law-essays.php (Last Accessed 18 May 2014)
90 See also the view of *per* Muntaka-Coomassie, JSC in *Alade* v *Alic (Nig) Ltd & Anor* (Supra) at p. 142.

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alternative, it may be necessary to require that each subscriber to the memorandum of association, especially where there are only two subscribers, has a certain percentage of the issued share capital of the company that would give a substantial interest in the company so that the possibility of having a *de-facto* one-man business will be eradicated. This will also curb the tendencies of some businessmen using other subscriber to the memorandum as a front in order to obtain the statutory minimum requirement.

Another area that needs to be looked into for purposes of reform is the position of a creditor who has given an unsecured loan to a company which eventually fails and is wound up. This is one of the reasons why the decision in *Salomon's case* has been variously criticised as calamitous[91] and shocking.[92] In the case, Salomon, who was to all intents and purposes the owner of the company was held entitled to repayment of his money before the unsecured creditors were paid simply because he made himself the preferred creditor of the company. In this wise, it is necessary and desirable in the interest of justice that the ordinary trade creditors of a trading company be given preferential claim on the assets of a company in liquidation in respect of debts incurred within a certain limited time before winding up. As the law stands in Nigeria, whenever there is a winding up order, debenture holders generally step in and sweep off every available assets of the company.

Also, it is desirable to have a provision similar to section 214 of the Insolvency Act (U.K.) to deal with "wrongful trading" so as to make those found culpable liable for the debts or other liabilities of the company, since the duty of discharging the burden of proving fraud as required in section 506 of CAMA is almost unattainable in most cases

Furthermore, it has been discovered that the theory of corporate personality may, in the case of holding and subsidiary companies, produce inequitable results in some situations. For example, the case of *Adams v Cape Industries Plc* has established that the veil of incorporation would not be lifted unless there is *inter alia* an express

91 See e.g. Khan-Freund, "Some Reflections on Company Law Reform", (1944) 7 M.L.R. 54

92 See e.g. L.C.B. Gower, (n. 2) p. 99.

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agency agreement between the holding company and the subsidiary. Thus, a creditor who is unable to prove such express agency relationship would have to prove an implied agency, which in most cases, is a uphill task since there is generally no judicial yardstick to determine whether the company acted as an agent. In this circumstance, the hapless creditor is barred from obtaining any remedy unless he could bring his case within any of the other recognised exceptions.

Also, the definition of "subsidiary" in section 338 of CAMA needs to be amended. By that section, a body corporate is to be regarded as the subsidiary of another, that is, the holding company, if the holding company is either a member of it and controls the composition of its board of directors or if it holds more than half of its "equity share capital" that is, the issued shares. The first part of this definition relating to control is too generalised as it does not distinguish between legal control and actual control. Also majority shareholding may not vest the control of the company in majority shareholders as the minority shareholders may in fact carry more votes. In this wise, it is important to note that although section 116 of CAMA forbids a company from authorising the issue of shares which carry more than one vote in respect of each share or which do not carry any right to vote, section 143 thereof however makes provision for instances where preference shares may carry the rights to more than one vote per share on a poll. It is therefore more expedient to take a cue from the definition given to subsidiary companies in the provisions of section 1159 of the English Companies Act to the effect that a company is a "subsidiary" of another company, its "holding company", if that other company *inter alia* holds a majority of the voting rights in it or is a member of it and controls alone pursuant to an agreement with other members, a majority of the voting rights in it.

Furthermore, it is not uncommon for a holding company to have total control over the trading activities of its subsidiary and even be trading most profitably through it without any legal responsibility to pay any of the unpaid debts of its subsidiaries. In this wise, there is a need for statutory intervention to prevent holding companies from forcing an insolvent subsidiary company into liquidation if it can be proved that the group as an entity is still solvent.

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7. Conclusion

Whilst one is not unmindful of the relative merits of the common law for its enormous capacity to grow in the hands of percipient judges, it is however desirable that the legislature goes further to provide clear guidelines on when it would be legally expedient to lift the corporate veil especially when dealing with cases relating to group corporate structures for enhancement of certainty. The corporate personality edifice which has served as an excellent social institution to the abiding credit of municipal and international trade would maintain its pride of place in commerce, in industry and as an instrument of social cohesion if the legislature and the courts do not rest on their oars in persistently attuning the relevant legal rules to maintain the necessary equilibrium between the interest of the economy and that of justice.

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