

Looking Beyond *Salomon v. Salomon*

Alexander Gay, Department of Justice¹

The last few weeks has seen a great deal of judicial activity on the corporate responsibility front. The Ontario courts issued a ruling in a long legal battle between Ecuadorian villagers that are looking to collect on a foreign judgment against a related Canadian company for environmental damages in Ecuador: *Yaiquaje v Chevron Corporation*, 2017 ONSC 604 (CanLII). We also saw the issuance of a decision by the British Columbia courts where Guatemalan miners allege that a Canadian mining company is responsible in tort law for the actions of a subsidiary operating in Guatemala that had security guards shoot at miners: *Garcia v. Tahoe Resources Inc.*, 2017 BCCA 39 (CanLII). While I do not wish to pronounce myself on the merits of each one of these cases, what I do know is that the law as it stands in common law jurisdictions is struggling to deal with a new corporate reality, namely a reality where related companies that form part of a larger group of companies are allowed to act in concert, yet continue to enjoy distinct legal personality that shelter them from collective responsibility. The principles of limited liability found in *Salomon v. Salomon* do not lend themselves to assigning legal responsibility in this new corporate shell game. While the law has been able to ignore the shortcomings of *Salomon v. Salomon* principles and rely on various other legal measures to address corporate responsibility between related companies – namely the piercing of corporate veils or the attribution of liability under tort law – the courts have to find a better way to hold related companies that act in concert responsible for wrongdoings.

The corporation is a by-product of a society that needed legal vehicles to facilitate capital accumulation and feed the industrial machine in England. The jurists that created this legal construct sought to create a divide between the shareholders and the officers/directors of the corporation, where shareholders could invest capital without incurring liability. If the corporation failed or posed an act for which it could be found responsible, its legal personality gave creditors access to only the assets of the corporation and nothing more. Capital could assume risk this way. Over time, the corporation evolved into a group of companies sharing a common goal, acting in concert and related in some manner or another. Companies became the shareholders of other companies and complex corporate structures developed. An unintended consequence of allowing a corporation to own the shares of another corporation is that the divide between shareholders and officers/directors becomes blurred. These same companies that form part of the group of companies all face some form of control through inter-corporate stock ownership, the concentration of voting rights and management/shareholders agreements that allow them to act in concert.

¹ The views expressed by the author are not those of his employer the Department of Justice.

The common law offers a half-baked solution to this corporate reality, namely the piercing of corporate veils or the attribution of liability when a parent company involves itself in tortious acts posed by a subsidiary. In the case of the former, the veil of company A may be pierced and the company may be considered as part of company B if, for example, it can be shown that there was fraud. There are a number of other circumstances that allow for the piercing of corporate veils. However, veil piercing fails to take into consideration the entire group of companies that act in concert and that benefit from each other in some fashion. As for tort law, the common law requires that a plaintiff show that: (a) the businesses of the parent and subsidiary are in a relevant respect the same; (b) the parent has, or ought to have, superior knowledge on some relevant aspect of health and safety in the particular industry; (c) the subsidiary's system of work is unsafe as the parent company knew, or ought to have known; and (d) the parent knew or ought to have foreseen that the subsidiary or its employees would rely on its using that superior knowledge for the employees' protection. For the purposes of (d) the law does not require a plaintiff to show that the parent is in the practice of intervening in the health and safety policies of the subsidiary. The court may find that element (d) is established where the evidence shows that the parent has a practice of intervening in the trading operations of the subsidiary, for example production and funding issues: *Caparo Industries Plc v Dickman* [1990] 2 AC 605. While these legal measures offer some reprieve from the rigidity of *Salomon v. Salomon*, they are but half-measures and largely unresponsive to the corporate reality.

As we look back in history, we have seen moments of legal lucidity where the common law has sought to take a broader approach to corporate accountability. Lord Denning in *DHN Food Distributors Ltd (In Liquidation) v. Tower Hamlets London Borough Council*, Court of Appeal, (1976) 32 P & C.R. 240 held that corporate reality as between related companies acting in concert had to take priority over the legal formalism that confronts us under *Salomon v. Salomon*. The case of *DHN* involved a compulsory purchase order of land by a Borough Council. The issue was whether amounts were payable by the Borough Council to three related companies for the disturbance of displacing them. The three companies were located on the same premises, owned by the same shareholders and shared the same directorship. One company held land, the other operated the business and the third owned the vehicles used for the business. All three companies operated in concert towards a common going concern. The inter-relatedness between these three companies was plain and obvious. The argument advanced by the Borough Council was that the company that held the lands was not entitled to disturbance as it did not hold an ownership interest in the business that had been displaced. The other two companies were also not entitled to compensation because they held no interest in the lands. Lord Denning in his decision held that while these companies each enjoyed a distinct legal personality under *Salomon v. Salomon*, it could not be relied upon to defeat a claim by a series of companies that act as a whole and that are bound hand and foot to the actions of the others. Rather, the reality was that they should all be treated as one entity. In reaching his conclusion, Lord Denning did not engage in the exercise of veil piercing, rather he accepted the relationship between these companies for what it was. The approach adopted by Lord Denning was, however, short-lived. A number of subsequent decisions from the House of Lords reverted to legal formalism. One of the landmark cases

was *Adams v Cape Industries plc* [1990] Ch 433 where it was said that, as a matter of law, the court is not entitled to lift the corporate veil as against a defendant company which is the member of a corporate group 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. The same legal formalism continues to pervade recent decisions from Canadian courts.

The civil law legal system appears to be taking a more comprehensive and robust approach when assessing corporate behaviour. For instance, within the law of international commercial arbitration or European competition law, the courts have developed different legal tests for assessing corporate responsibility. Within the context of European competition law, the courts have applied the “decisive influence” test – if a corporation has a decisive influence and has exercised that influence, it assumes responsibility for the actions of a related company. Economic and legal links are examined in making that assessment: Case T-132/07, *Fuji Electric System Co. Ltd. v. Commission*, 12 July 2011. The case law in the EU creates a presumption in favour of decisive influence where a company owns a substantial interest in the shares of a subsidiary. The onus then reverts to the party opposing the presumption to show that the ownership interest was not used to influence: *Akzo Nobel v Commission* [2009] ECRI-8237; Case-90/09 P - *Quimica and Others v. Commission*, 20 January 2011. In cases where the presumption is sustained, the parent is jointly and severally liable for all liabilities relating to the subsidiary. The EU competition law offers a fresh approach to corporate responsibility, beyond the piercing of corporate veils and beyond the difficult exercise of attributing responsibility between companies under tort law. In the Canadian context, similar concepts have been conceived. The federal government recently introduced a debarment regime for deciding whether a related company should be debarred from participating in a federal procurement for an offence committed by a related company. Under this legal test, which determines if a company is entitled to do business with the Canadian government, a company will be held responsible for the actions of a related company if “*it directed, influenced, authorized, assented to, acquiesced in or participated in the commission of the offense of the related company*”. Turning a blind eye to the corporate actions of a related company does not absolve a company of responsibility under this legal test. Separate legal personalities may be maintained, but collective responsibility is also infused, holding the group of companies responsible for wrongdoings if the legal test is met.

We need to take stock of where we are on the law of corporate responsibility and assess how it can progress so that it may be responsive to our social needs. We need not look far to find approaches and solutions to the legal formalism that ails us.