

Topic 2- Corporate Personality and Limited liability

Corporate Personality

- A company is a separate legal entity, with all the powers of an individual and comes into existence upon registration: **S112, 119, 124**
- Separate legal personality of a company comes from **Salomon's case**
- A company can contract with its employee even where the director (acting as an agent of the company) and the employee are the same person: **Lee**

Piercing the Veil

- A corporation is distinct from its members, being a separate legal entity and therefore members' property cannot be used to satisfy the debts of the corporation: **Salomon**
- However, query when there is 1) Fraud, 2) Agency, 3) Direct Duty of Care 4) Statutory provisions that may require the "corporate veil" to be lifted
- There are no unifying principles, courts reason by analogy: **Briggs v James Hardie**
- The veil is lifted in **special/ egregious circumstances** indicating the company is a **mere façade: James Hardie**
- The court is not free to disregard the principle of **Salomon** merely because it considers justice so requires: **Adams v Cape**

Piercing the Veil – Fraud

- **Test:** Was the sole/ dominant purpose of incorporation the evasion of pre-existing legal obligations?
 - **Gilford Motor:** Corporation incorporated purely to escape restrictive covenant over activities. New company was a "mere cloak or sham" used to breach contractual obligations
 - **Jones v Lipman:** Prior to completion on sale of land contract, D sold land to his own company (sole shareholder/ director), thus breaching contract with P.
- **NB:** Sham is difficult to make out in court given the inherent nature of the argument (weak legal basis and what evidence to adduce)

Piercing the Veil- Agency

- The mere fact one shareholder is dominant does not make the corporation his/ her agent (Agent = corporation; Principal = Director)
- **TEST: Smith Stone Knight (SSK) 6 point test for determining if subsidiary and therefore can we access the parent (Atkinson J)**, approved in **Pioneer Concrete**
 - Facts: X (holding company) sought compensation for Y (subsidiary) loss; all 5 directors of Y were directors of X; Y's profits transferred directly to X
 - 1) Were Y's profits treated as profits of X (parent)
 - 2) Were the persons conducting Y appointed by X?
 - 3) Was X the head and brain of the trading venture?
 - 4) Did X govern the adventure, decide what should be done and what capital should be earmarked upon?
 - 5) Did X make the profits by its skill and direction?
 - **6) Was X in effectual and constant control?**
 - P, A, B, G, S, C
 - Profits, Appointed by, Brain, Governed (Ventures), Skill of X, Control
- **NB:** CJ Rogers in **Briggs:** We don't like it in Australia because effectively every subsidiary would be pierced by the corporate veil and therefore limited liability would no longer be useful.
- **HD:** Finally, House of Lords also rejected the agency argument in **Salomon**.

Piercing the Veil- Corporate Groups

- PF, each member company is a separate legal entity with its own rights, privileges, duties and liabilities separate from those of other group members: **Industrial Equity**
- In the absence of contract creating additional rights, creditors of company Y can only look to Y for payment of the debt – cannot use the holding company: **Industrial Equity**
- They must not take into account profits of other members: **Industrial Equity**
- **NB:** Arguably this position insulates parents’ risk – allowing them to make decisions without being affected
- UK jurisprudence of **DHN** had the veil lifted and owner could claim compensation across corporate group because 1) wholly owned 2) no separate business operations 3) Owners were disturbed in possession and enjoyment (DHN closed all together because of disturbance to one subsidiary) - very liberal approach and not followed in Australia/ went against body of law at this point
 - Tension between commercial reality + **Salomon principles**
- Rogers CJ/ Court called on the parliament to address the distinction between common law practices and commercial practice. Reform would mean certainty for creditors and protects lazy creditors but also destroys golden rule of **Salomon’s: Qintex Finance**
- Finally, the golden rule of **Salomon’s** was echoed in **Pioneer Concrete** (NSWSC)
- **Takeaway:** Cross corporation guarantees should be demanded in these situations instead of relying on bad reform that destroys separate personality principle

Piercing the Veil- Direct duty of care

- Employees of subsidiaries may be awarded damages against the holding company if it can be found that the parent owed them a duty of care: **CSR Ltd v Wren**
 - Here, S had the **operating manuals of P, code of conduct** indicating that is “how the S would do things”, which allowed them to pierce the veil DHN style
- These situations lead to an overall consideration by Rogers J regarding the argument for piercing the veil in a corporate group where tort liability is concerned, the court may need to be more ready to lift the veil in favour of those claimants: **Briggs v James Hardie**
 - NB: It is not authority (procedural case), as soon as JH were brought to proceedings, they settled indicating a PF case. There are also no **unifying principles** in this area of the law.

Piercing the Veil- Insolvent Trading

- A Parent or director may be held liable for subsidiaries that trade whilst insolvent (**S588V, S588G**)
- Insolvency: if and only if person is able to pay all debts as and when due/ payable, using the Cash flow test: **S95A(1)**
 - A person who is NOT SOLVENT is therefore insolvent
- Breach as a company: Breaching **S588V** involves
 - A,B) P incurring further debts for S when insolvent, which includes declaration of dividend, buying back shares, reducing share capital etc
 - C) There were reasonable grounds for suspecting P is insolvent or would become insolvent
 - D) Either P or P’s directors were aware that there are such grounds for suspecting OR having regard to the nature and extent of P’s control over S’ affairs, it is **reasonable** to expect that
 - A) holding company in P’s position would be aware
 - B) One or more of such a holding company’s directors would be aware
 - E) Post 2001
- Breach as a director: Breaching **S588G**
 - 1) S588G applies when there is a “director” and company which is insolvent/ becomes so because of debt, at the time reasonable grounds for suspecting insolvency and post act (A,B,C,D) – **more commonly used in problem questions**

- 2) By failing to prevent the company from incurring the debt, the person contravenes this section if
 - a) there are such grounds for so suspecting
 - b) a reasonable person in a like position in a company in the company's circumstances would be so aware
- 3) Person commits an offence if as a director, the company is "insolvent", the person suspected and they failed to prevent it (**dishonest**)
- Breach as a consultant: If they are properly appointed or de facto, this is particularly so if their appointment is unconstrained: **Grimaldi v Chameleon Mining**

What is a director?

- **De Jure director:** director appointed S9(a)(i)
- **Director under another name** S9(a)(ii)
- **De facto director:** person who acts in position of director: S9b(i)
- **Shadow director:** persons according to whose instructions or wishes the directors of a company are accustomed to act for: S9b(ii)
 - In **Standard Chartered**, the court found that there needs to be a 1) willingness to control 2) Actuality of control over financial management given in this case the S **willingly listened**
 - Not enough to be just be dominant shareholder (plenty of those situations which don't need to be caught)