

## The Corporate Veil - Separate Legal Entity

### ➤ Creation of a company

- A person lodges an application with ASIC under s117 and s118 directs ASIC to issue a certificate of registration.
- A company only becomes a separate legal entity after it has formally been incorporated by registration under the *Corporations Act* s119
- A company has the legal capacity and powers of an individual and the powers of a body corporate s124(1).

### ➤ In Saloman v Saloman & Co Ltd [1897] AC 22 the court found that the company's unsecured debts were to be paid out of the company's assets and Salomon had no liability to contribute personally. This was because the company had been registered properly with the consequence that the business was owned by the company, not Salmon even though he controlled it - meaning that the company is a company separate from its participants. Therefore business debts also belonged to the company and not Saloman.

### ➤ The separate legal entity principle has been a cornerstone of company law

### ➤ **Consequences of incorporation**

- Company's capacity to enter into contracts - In *Lee v Lee's Air Farming Ltd* it was held that Mr Lee, the owner and manager of his company Lee's Air Farming, could be, by a separate contract, an employee of the company. The company had the capacity to make a contract with Lee and the contract could not be impugned merely because Lee was also the manager of the company negotiating with himself.
- Company's capacity to own property- In *Macaura v Northern Assurance Co Ltd* once Macaura transferred land he owned to his company, it was held that he no longer had an insurable interest in the land, nor the timber that was growing on it. Owners of the company have no legal or equitable interest in the assets of the company.
- Company and corporate groups - multiple companies can be controlled by one company.
- Capacity of a company to commit torts

## ➤ Lifting the Corporate veil

- In exceptional circumstances courts may decide to lift the corporate veil and disregard the separate legal personality of the company. The usual result of lifting the corporate veil is that limited liability of owners will be lost. Lifting veil may also result in the owners or managers being held responsible for the actions of the company as if they were their personal actions; or lifting the veil may provide a remedy that would otherwise be denied, or to create an enforceable right.
- Legal issue: Should the corporate veil be lifted in the circumstances of a particular case? The following are situations where the veil has been lifted:
- Avoidance of legal obligations - In *Gilford Motor Co. Ltd v Horne* [1933] Ch 935, Horne left the Gilford Motor Company in order to set up his own business. When he left he agreed that he would not solicit any of his former employer's customers. As a way around this restriction he set up a company to run the new business. *It was held that Horne and Horne's new company were prevented by an injunction from soliciting the clients of his former employer. His company was also subject to the injunction as the judge went behind the veil of incorporation and ruled that the company and Horne were one and the same. The company was formed for an unlawful purpose.*
  - *Jones v Lipman*

Facts: Lipman entered into a contract to sell a house to Jones. Lipman later changed his mind and refused to complete the transaction. Lipman formed a limited company and conveyed the house to it, making the house now a property of the company instead of Lipman's.

Held: Jones succeeded in an action of specific performance against both Lipman and his company. It was held that Lipman should carry out the contract to sell the house to Jones. The limited company was not considered a separate legal entity because of Lipman's real purpose in using the company as a device or sham to avoid his contractual obligations.
- Fraud- In *Re Darby* [1911] 1 KB 95, Darby was an undischarged bankrupt with a previous conviction for fraud. He used a company to sell a license to work a quarry to a newly floated company (of which he was a promoter) at a substantial overvalue. The liquidator of the floated company claimed against Darby on the basis that Darby had breached his duty as promoter of the floated company. Darby claimed the profit on the sale of the license was made by his private company, not him. The court looked behind Darby's private company on the basis that the private company was set up as a sham to enable Darby to attempt

to evade his fiduciary duties to the company that he was promoting (Phillimore J at p 101).

- Use of the company as an agent- In *Re FG (Films) Ltd* [1953] 1 All ER 615 an American film company held 90% of shares in a British company. The British company was essentially without resources, having a share capital of £100, no place of business (save for a registered address) and no employees. When the British company sought to register a film under the Cinematographic Films Act 1938-1948 as the company that had made the film, the registration was rejected. Vaisey J stated that the English company did not have the resources to make the film and therefore its participation in the film making must have been as agent of the American company.

- *Group enterprises* - In *Smith, Stone & Knight Ltd v Birmingham Corporation* [1939] 4 All ER 116, Birmingham Corporation sought to compulsorily acquire property owned by Smith, Stone & Knight (SSK). The premises were used for a waste control business. That business was ostensibly conducted by the Birmingham Waste Co. Ltd whose name appeared on the premises, notepaper and invoices. The Birmingham Waste Co. Ltd was a wholly-owned subsidiary of SSK. SSK sought compensation for the disturbance of Birmingham Waste Co's business.

Held: The court agreed that SSK was entitled to compensation because Birmingham Waste Co. conducted its business as an 'agent' for SSK. In considering whether a subsidiary is carrying on its business as the parent company's business or as the subsidiary's own business, six questions were proposed:

1. Were profits of the business treated as profits of the parent?
2. Did the parent appoint persons to carry on the business?
3. Was the parent the 'head and brain' of the trading venture?
4. Did the parent govern the adventure?
5. Did the parent make profits via that direction?
6. Was the parent in effectual and constant control? (Atkinson J)

➤ **Australian courts are reluctant to lift the corporate veil**

- In *Walker v Wimbourne* (1976) 137 CLR 1, the issue was whether the funds of one company in a corporate group could be used to satisfy the debts of another member of the corporate group. The High Court held that each company in a corporate group is a separate legal entity and therefore the funds of one company cannot merely be shifted as if they are the property of another company in the same corporate group.

