

Company and Partnership Law

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Introduction

The corporate Veil, understood as the barrier by which commercial companies have a legal personality different from that of its members and the limits to liability, is a fundamental pillar of economic development, so it must be respected and guaranteed. However, removing the corporate veil is dependent on various criterions and it's growingly debated that those criterion often hamper application of this principle. Considering the given quote of Lord Sumption in *Prest v Petrodel (2013)*, this assignment seeks to critically evaluate the principles in relation to the veil of incorporation. To what extent do you agree that the rules on lifting the corporate veil are too rigid?

Piercing the Corporate Veil

For lifting the corporate veil, there are two kinds of broad legal provisions statutory and judicial provisions, both rooted in the principles of separate personality, established in the *Salomon v Salomon (1896)* case. This case is an important antecedent in the construction of the corporate veil. However, it is already beginning to recognise that this veil can have certain disadvantages even for the shareholders themselves. In the case of the dismissal of the corporate veil, there are a large number of cases in which the veil can be lifted. The number of exceptions to Salomon's case is so great that it has been reduced to a shadow (Sealy and Worthington, 2013)

The guiding principle that supports the criterion that is applied, sometimes such as *Creasey v Breachwood (1993)* , in favour of the rejection of the veil and others not, is,

appears a clear injustice is avoided, although the line between the origins or not of the uprising is not well defined. The English judges have maintained the idea that the public interest can and should go beyond any legal norm that intends to break it, including the use of corporate forms (Bull, 2014).

The rigidity of rules on lifting the corporate veil

From the above case law analysis it is evident that the piercing of the corporate veil can only occur in very special cases, so that the piercing can occur should be proven, in a process of knowledge, an abuse of the corporate form and also that the abusive action causes harm or injury to any person or property make it impossible to exercise any right, especially credit, against society or those who control it (Alexander, 2016).

Lord Sumption in *Prest v Petrodel (2013)* argues that one of the major rigidity in the rules on removing the corporate veil is hypothetical nexus of company and society

When applying the theory of lifting the corporate veil it is to extend the liability of the external liability of the company to the shareholders who incurred the unfair practice, which can be the case that the company adapts to a situation of dissolution as in the corporation by reducing its net worth below fifty percent of the subscribed capital, therefore contrary to the position that the company does not lose its attributes. Lord Sumption believes that it may have more effects either direct or indirect, including the dissolution of the company or the nullity of the social contract (Tsang, 2014).

The English courts in many cases though has, lifted the veil of the legal personality to fight against the use of companies or social mechanisms in fraud of the rights of creditors. However, despite the courts' interpretation of these pieces of legislation, the protection of creditors remains fragmented and limited (Nicholas(2014). Clearly, the

legislator is keen to control with rigor the consequences that the consideration of man and his patrimony might have through the legal person. To overemphasise the personal risk, one risks emptying of its content the concept of company of capital.

This is how the legislator wanted to protect third parties who could contract with society on the basis of a false name. Section 108 (4) of the Companies Act 2006 provides that the officers or those who acted on behalf of the corporation may, if they have used a stamp or signed a commercial document on which the name of the corporation company does not appear in a legible manner, be declared indefinitely liable to the holder of the document for the amount of the debt (Lee, 2015):

This is a second-level responsibility since the leaders will only be sentenced if the company has not paid the debt itself; leaders are only asked to endorse it. The liability of the officer is engaged even if the third party has not been deceived by the error or omission (McArdleand Gareth 2013).

Section 332 of the Companies Act of 2006, on the other hand, gives power to the judge to impose personal liability for the debts of the company of any person whose liquidation of the company has shown that he has acted fraudulently. Creditors' rights or for any other fraudulent purpose, law also provides for criminal liability for any person who knowingly participated in the fraud (Bull, 2014):

The possibility of lifting the veil and thus reaching the natural persons beyond the legal person finds its limits in the actual text of the article. In the first place, the loss of the benefit of the limitation of liability for any person convicted of fraud can only be pronounced once the liquidation is ordered.

Lord Sumption in *Prest v Petrodel (2013)* appears to advocate that that section 332 be applicable at any time during the life of the company, provided that it appeared that the affairs of the company had been conducted in a deliberately fraudulent or unlawful manner. In fact, according to Lord Sumption, the usefulness of such a reform is not felt to be of paramount importance since section 332, in its current form, has a deterrent effect such that some directors would spontaneously propose to assume part of the debts to avoid a possible conviction (McArdle and Gareth, 2013)

The second restriction is the interpretation by the judges of the notion of fraud. Article 332 covers all cases where an activity has been conducted "with intent to defraud creditors or for any other fraudulent purpose". The conviction of the partners or directors of the company therefore depends on the assessment of a purely psychological concept: the intention to defraud (Okoli, 2014).

In order to ensure the maximum protection of creditors, the judges first gave to the concept of fraud a very broad content: "There is a presumption of fraud if a company pursues its activity and contracts damages, whereas its Directors know that there is a good chance that they can never be honoured. Then, returning to a more restrictive attitude, they considered that the one who invoked fraud must prove "a dishonesty implying, according to the criteria of loyalty in force between traders, a real moral blame" (Schall, 2016)

Although several decisions were challenged and criticised on this subject, some criteria finally emerged from the case law and allowed to delimit certain parameters of application of the lifting of the corporate veil. On the one hand, it is almost exclusively

against companies with a single shareholder or very restricted shareholding that the courts have allowed the lifting of the corporate veil.

Lord Sumption in making the distinction between creating a legal situation in which the author of the edict is no longer bound by an obligation and merely concealing the situation in which he is still bound by that obligation, the Court of Appeal in *Prest v Petrodel* establish the uniqueness of the action to break through corporate veil. However, the distinction is not quite convincing, suggesting that the contribution of the judgment is elsewhere, in its unifying force (Schall, 2014).

Generally, the English courts look at what intention presided over the formation of the company and sanction any fraudulent maneuvers by lifting the veil of the legal person. In the absence of a definition of the notion of fraud, it is difficult to predict with certainty in what circumstances the courts will go beyond the legal facet. It seems that improper conduct, even if it is not characterised by maneuvers, is a source of responsibility for the person who originated it.

The court proposes in *Prest* (2013) to put the judges in the correct legal process based on the *concealment principle*, the fact for the real author of the facts litigious [to interpose] one or more companies in order to conceal his identity. In this situation classically, the judge is not bound by the qualification created artificially by the author of the editing.

The *Court in Prest v Petrode* (2013) therefore condemns the practice of the Courts of circumventing rigorous legal reasoning by invoking *piercing the corporate veil*

On a residual basis, if the facts do not characterise any other lawsuit, *piercing the corporate veil* is possible subject to proving the *evasion*, that is to say the element of

fraudulent intention constituting this action. Therefore, if ultimately the Court does not sanction the assembly before it, it means that the facts or means invoked are lacunary and not the right.

Since the Court only "clears" a pre-existing principle, it must minimise the connection between the principles of *escape* and *concealment*. In other words, the previous case law would have been in agreement with *Perst* if the rule had at that time been properly articulated. This company is by nature biased and its result artificial. The crux of the distinction between the two principles identified would be the existence of a head of responsibility independent of the involvement of society. The use of a company to pass social funds diverted for own account *Trustor AB v Smallbone (2001)* that to engage in commercial activity in violation of a non-competition clause *Gilford v Horne (1935)* appear to betray the master's conscience of the case to be bound by an obligation - which he has the intention of ignoring. However, the first is simply a case of *concealment* while the second is a case of evasion.

Under the doctrine of corporate veil, Invoking *escape* will not be easy in practice: the risk of censorship seems substantial and the judge will probably prefer to place himself in the field of *concealment* which is not without reminding of fictively, but the time when it was assimilated to nonexistence.

It seems that *Prest* effectively answers this need when it requires that an *evasion* by the author of the montage is demonstrated. Thus, the judge can "*pierce the statutory veil*" when the author, who is under a legal obligation manages to escape by interposing a company which he has control. The action results solely in the deprivation, for the

company or the person who controls it, of the advantage that would otherwise be withdrawn from the legal personality distinct from the company (Lee, 2015)

The concept of raising the corporate veil remains a great mystery for lawyers, who have had great difficulty, some seeing a formidable breach to attack the shareholders as soon as damage is caused to the co-contractors of a company. However, in many cases, the lifting of the corporate veil is not the appropriate remedy (Tsang, 2014)

The notions about the corporate veil reached a certain degree of maturity following *Prest*. However, the fact remains that the lifting of the corporate veil is initially an exception to the legal personality independent of companies. The lifting of the corporate veil must therefore continue to be an exceptional measure. On the other hand, it seems to us that too precise a definition of the limits of its use is not the most appropriate solution either.

While remaining an exceptional measure, justifiable to use because of certain criteria of equity that ultimately depend on each individual case, this now codified notion allows greater flexibility and a better remedy against the resourceful people certainly, but lacking good faith and honesty (Lee, 2015).

Conclusion

It can be concluded in confirmation to Lord that the rules on lifting the corporate veil are too rigid. While corporate veil principle is a fundamental concept but its application has always been debated in relation to lifting this veil due to legal technicalities. Lord Sumption, in the *Prest* case offers lot of rationale that it's not simple to explore the hard and fast principles for removing the corporate veil due to its over signified status as a doctrine beyond label. Though, these rules on lifting the corporate veil certainly

important to keep the equilibrium between business organisation and individuals and Lord Sumption approach to completely override them from creditors protection over shareholders is also not fully valid.

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