REMEMBERING THE CONCEPT OF THE CORPORATION

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REMEMBERING THE CONCEPT OF THE CORPORATION 1

INTRODUCTION 2
1 THE PROBLEM: THE MODERN CONCEPT OF THE CORPORATION 6
A A Corporation Need Not be Operated to Make Itself a Profit........ 8
(i) Classical concept of the corporation 8
(ii) Modern concept of the corporation 18
B A Corporation May be Operated to Fence-off Liabilities 33
(i) Classical concept of limited liability 33
(ii) Modern concept of limited liability 34
2 THE LEGAL PERSONALITY OF THE CORPORATION 42
A The Things of which the Concept of the Artificial Person is a Concept 42
B Not an Analogy from the Human Person 45
C Not a Concept of the Fictional Person 46
D A Concept that Contains a Fiction 47
(i) The other-worldly artificial person 48
(ii) The world-of-fact artificial person 49
(iii) The corporation 60
3 THE PROPOSED SOLUTION: REMEMBERING THE CLASSICAL CONCEPT OF THE CORPORATION 66
CONCLUSION 69

'a regulatory system has failed when one ends up having to nationalize half the banks in the country'

UK Shadow Chancellor, George Osborne[1]

'The present economic crises do not, I would argue, call for a "new capitalism," but they do demand a new understanding of older ideas'

Amartya Sen[2]

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[1] Hansard, House of Commons, 'Banking Bill', 13 October 2008, Column 702.
[2] 'Capitalism Beyond the Crisis' 26 March 2009, (2009) 56 New York Review of Books, http://www.nybooks.com/articles/22490 (accessed 14 April 2009).

INTRODUCTION

To those left standing in the wake of the subprime mortgage crisis, the failure of our current systems of financial regulation is obvious. The answers to the resultant questions are more opaque. How is it that the world's banks could have engaged in such risky lending practices? How do we explain the fact that the banks, and our financial system, were oblivious to the toxicity of their assets?

While it is clear that the credit crisis poses problems for systems of financial regulation, does the crisis pose particular problems for our current system of corporate law? In one sense, crises in the market are par of the course,[3] and are no indication of a deficiency in the way that the law conceives of the corporation. As Posner argues:[4]

> the specific doctrines of corporation law should not be expected, in general, to have a profound impact on the credit system or to alter the balance of advantage between debtor and creditor.

In another sense, '[t]he current financial crisis has complex origins', and it is difficult to attribute responsibility for the accumulation of 'systemic risk'.[5]

However, it is arguable that the way in which modern corporate law conceives of the corporation contributed to the accumulation of systemic risk in two ways. First, limited liability affects lending practices, and the toxicity of the assets that banks choose to acquire. Emerging empirical evidence suggests

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[3] See, eg, J Schumpeter *Capitalism, Socialism and Democracy*, New York, Harper Publishing, 1975 at 82.
[4] RA Posner 'The Rights of Creditors of Affiliated Corporations' (1975) 43 U Chicago L Rev 499 at 505.
[5] AM Spence 'Lessons from the Crisis', *Pimco*, Nov 2008, <http://www.pimco.com/LeftNav/Viewpoints/2008/Viewpoints+Lessons+from+the+Crisis+Spence+November+2008.htm>.

that the liability structure of a bank, including the limited liability structures within a corporate group of banks, affects the quality of the loans that the banks offer to the market as well as the price at which loans are offered.[6] The greater the banks' ability to avoid its liabilities, the more likely it is that the banks will pursue risky models of lending.

Secondly, and as this paper argues, our modern conception of limited liability affects the capacity of banks – and any emergent regulatory system – to measure the toxicity of assets. Prime Minister Gordon Brown has called upon the G20 summit to implement an early warning system 'so that international financial flows are properly monitored'.[7] However, as Michael Spence notes, there are doubts that we have the 'knowledge and capabilities' to acquire 'a complete picture of systemic risk'.[8] Undoubtedly, the creation of a more wholesome picture 'will require complex solutions'.[9] This paper proposes one of these solutions, which is to mend a fault-line on top of which relationships of credit are currently built.

Part One of this paper describes this fault-line, which has developed over the last 100 years. At the turn of the 20th century, corporate law in both the US and the UK abandoned the classical concept of the corporation in two ways. First, by way of judicial reform, the law accepted that a corporation need not be operated so as to make a profit for itself. The US and UK courts

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[6] A Purnanandam 'Originate-to-Distribute Model and the Sub-Prime Mortgage Crisis' (Draft), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1167786; V V Acharya 'A Theory of Systemic Risk and Design of Prudential Bank Regulation' http://ssrn.com/abstract=1334457.

[7] J Booth 'Gordon Brown: 'I called for global financial reform ten years ago'' *The Times*, Jan 26, 2009; see also 'UK PM Brown outlines agenda for G20 summit' *Forbes*, Feb 9, 2009 <http://www.forbes.com/feeds/afx/2009/02/09/afx6025257.html>.

[8] Spence (note 5).

[9] Spence (note 5).

conceded that a corporation may be incorporated, or may exist as a legal person, simply so that the corporation may make a profit, not for the corporation, but for its shareholders. This reform fractured the emerging 'skeleton of principle'[10] of corporate law. Part One outlines that, as a result, basic doctrines of the law concerning corporations (ie, federal regulation, securities regulation and the veil-piercing jurisprudence) are ungrounded in principle and modern corporate law remains internally inconsistent.

Part One then notes the second judicial reform that established modern corporate law. The courts of the US and UK permitted a corporation to be incorporated, or to exist as a legal person, simply so as to limit the liability of its shareholders. Under the classical concept of limited liability, corporate law fenced off[11] the assets of a business's investors from the claims of the business's creditors. A creditor could take recourse, not against Mr Salomon's assets, but only against the assets and profit stream of Salomon & Co's leather merchant business.[12] The toxicity of the creditors' assets depended upon the viability of the debtor's business.

In contrast, modern corporate law empowers shareholders to move the fence – and to partition off from the claims of creditors even the profit stream of a corporate group. Modern corporate law, unlike classical corporate law, vests debtors with the power to incorporate a corporation in order to house debts that the subsidiary owes or will owe. The debtor corporation need never exert any effort to generate a profit stream. It is irrelevant that the capital

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[10] *Mabo v Queensland (No 2)* (1992) 175 CLR 1 (HCA) at [29].

[11] Or 'partitioned' the assets; H Hansmann and R Kraakman 'Organizational Law as Asset Partitioning' (2000) 44 European Economic Rev 807; H Hansmann and R Kraakman 'The Essential Role of Organizational Law' (2000) 110 Yale L J 387.

[12] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

loaned to one corporation in the group was used to generate the profit stream of another member of the group.

It is on top of the fault-line of modern corporate law that this second fence was built and the modern concept of limited liability was premised. If a debtor is able to shift its debts to another member of its corporate group, or to distance itself from the profit stream(s) of the group, then a creditor is disabled from gauging whether or not the creditor may take recourse against a profit stream. In this way, the debtor is enabled to avoid its liabilities, and the creditor is disabled from measuring the toxicity and recoverability of its assets.

While Part One critiques the modern concept of the corporation, Part Two aims to justify the classical concept. Part Two argues that the classical (and the current stock market's) conception of the corporation should be preferred to the modern corporate lawyer's. This is because it is the classical conception that accords with a philosophical analysis of what it means to be an artificial person; and what it means for the law to vest legal personality in the corporation. To embark on the search for a principled concept of the corporation, the paper casts its net wider than the corporation, and asks the more basic question: who and what is a person? The name of 'person' is attached to an almost infinite variety of non-human things. The law personifies, *inter alia*, the government, the military, the State and the (almost oxymoronic) 'corporate person'. Part Two of the paper constructs a concept of artificial personality that explains the sense in which the law attributes the character of a person to the human being and a range of non-human things. To use this concept sensibly, the courts must treat a corporation as a thing that is of ultimate value, and that exists so as to benefit – *inter alia* but at the least – itself.

To restore the classical concept of the corporation, Part Three of the paper proposes a solution. It is argued that corporate law must afford creditors the same protection that securities law currently affords to investors. The listing rules of some of the world's leading stock exchanges conceive of the companies listed on their exchanges as only those persons that exist to benefit themselves. To ensure the integrity of the market, the listing rules prescribe that the companies whose securities are publicly traded are companies that pursue their own ends and act in their own interests, and are not corporations that exist merely to act in the interests of any other corporation. To ensure the integrity of all markets – public or private, debt or equity – the US and UK courts must also conceive of the corporation in the same way that the stock exchanges conceive of their listed corporations: as persons that exist to benefit themselves. Part Three adopts this conception in order to propose a principled test, by which the US and UK courts may pierce the corporate veil, and thereby remember and restore the classical conception of the corporation.

1 THE PROBLEM: THE MODERN CONCEPT OF THE CORPORATION

The corporation, in its form as a legal person as well as a corporation of investors, is almost 500 years old.[13] However, it is only in the last 100 years that the law has enabled a trading corporation to exist as a legal person, even if the corporation:

(i) is not operated so as to make itself a profit; and

(ii) exists, and is operated, only so as to limit the liability of the

[13] The Muscovy Corporation received a charter of incorporation from Queen Mary I in 1555, but may have also received a charter from King Edward VI in 1553; JA Williamson 'Review: The Muscovy Merchants of 1555' (1954) 69 The English Historical Rev 333.

corporation's shareholders.

These two changes in corporate law define the modern concept of the corporation, and distinguish it from the classical concept. The emergence of the modern concept of the corporation is not another consequence of the recent emergence of globalization and global trading. The multinational corporation is almost as old as the trading corporation.[14] Rather, and as this part outlines, the modern concept emerged as a result of two of the modern world's arguably most important judicial reforms of legal principle. They are arguably also two of the least legitimate of judicial reforms, as they were unarticulated and were mostly left unreasoned. The first shift of judicial attitudes prompted the courts in the US and UK to rule that a corporation's purchase of stock in another corporation is not ultra vires the parent corporation's powers even if the stock purchase resulted in, or was designed to ensure that, the subsidiary corporation acts in the interests only of the parent corporation; and not also of the subsidiary corporation itself. The second change of judicial attitudes caused the US and UK courts to conclude that the veil that separates the legal personality of two corporations ought not to be pierced simply because one corporation exists only to limit the liabilities of its parent corporation or other shareholders. This part concludes by noting that, as a result of these two judicial reforms, modern corporate law empowers shareholders to avoid, and not merely limit, liability.

[14] The Muscovy Corporation is reputed to have 'opened a rope house in Russia, where it employed English craftsmen to make cordage, only four years after the corporation's formation.' AM Carlos and S Nicholas "Giants of an Earlier Capitalism': The Chartered Trading Companies as Modern Multinationals' (1988) 62 The Business History Rev 398 at 399.

A A Corporation Need Not be Operated to Make Itself a Profit

(i) Classical concept of the corporation

Since the emergence of the trading corporation in the mid 16th century, the law has vested corporations with legal personality with the intention that each corporation be operated for the purpose of making itself a profit. In the US and UK, corporations have acquired, and continue to acquire, legal personality in one of two ways: by a special grant from the sovereign (either through a Royal Charter or by a private Act of Parliament) or, most recently, through a process of registration.[15] For a time, the only entities that acquired legal personality by way of a charter from the sovereign were those which proposed to undertake a venture that would not only make itself a profit,[16] but that would also further the political ambitions of the sovereign. The English monarchs chartered corporations 'as a tool in their overseas and financial policy',[17] while, in colonial USA, '[t]he Continental Congress chartered the Bank of North American in 1781, largely for the purpose of financing the Revolution.'[18]

(a) Legislatures

During the 19th century, however, 'the Victorians changed the point of

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[15] See G Todd 'Some Aspects of Joint Stock Companies, 1844-1900' (1932) 4 Economic History Rev 46 at 49.

[16] eg, WP Hackney and TG Benson 'Shareholder Liability for Inadequate Capital' (1981) 43 U Pittsburgh L Rev 837 at 856: 'early 19th century statutes chartering corporations did just that: they set forth detailed requirements as to the nature of the franchise granted – *the business to be undertaken*, and the required capital to be raised before such business could be commenced.'

[17] R Harris *Industrializing English Law: Entrepreneurship and Business Organization, 1720-1844* (Cambridge University Press) at 290.

[18] EM Dodd *American Business Corporations until 1860 with Special Reference to Massachusetts* (Harvard University Press Cambridge 1954) at 11.

companies.'[19] The legislatures of both the US States[20] and the UK[21] passed legislation that enabled the corporation to be incorporated, and have legal personality vested in it, upon a simple process of registration. The Acts made clear that the legislature intended each corporation incorporated through the process of registration to be operated for the purpose of making itself a profit. For example, section 25 of the Joint Stock Companies Act 1844 stated:

> 'That on the complete Registration of any Corporation … such Corporation and the … Shareholders … shall be and are hereby incorporated … for the Purpose of carrying on the Trade or Business for which the Corporation was formed'.

In 1855, the UK Parliament granted limited liability to the joint stock companies registered under the Act of 1844. During the debates on the Limited Liability Bill of 1855, the UK Parliament indicated that the only joint stock companies that should be granted limited liability under the Bill were the companies that were organized 'for the legitimate purpose of trade'.[22] Parliament did not intend a corporation to be granted legal personality, nor limited liability, simply so that the corporation could act to benefit only its shareholders – even the class of shareholders as a whole – by, for example, acting simply to increase the share price.[23] Nor did Parliament intend the corporation to be operated simply to benefit any other stakeholder, including

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[19] J Micklethwait and A Wooldridge *The Corporation: A Short History of a Revolutionary Idea* (Phoenix London 2003) at 5.
[20] Massachusetts passed a general incorporation statute by 1799, and perhaps even earlier; O Handlin and MF Handlin 'Origins of the American Business Corporation' (1945) 5 J of Economic History 1 at 4. Other states followed suit: New York Laws (1811) c67; 16 New York Const, Art VIII §1 (1846); Michigan Const, Art XV, §§1 and 2 (1850); Wisconsin Coast, Art XI §§1, 4 and 5 (1848); see KK Luce 'Trends in Modern Corporation Legislation' (1952) 50 Michigan L Rev 1291 at 1293.
[21] *Northern Central Rly Co v Walworth* 193 Pa 207, 44 A 253 (1899, SC Penn).
[22] DE Lilienthal 'The Regulation of Public Utility Holding Companies' (1929) 29 Columbia L Rev 404.
[23] Lord Monteagle described the 'bubble Companies', which the Act needed to 'guard against', as companies that were organised for the purpose of, eg, 'making a traffic in their shares'; HL Deb vol 139 c 2041 (9 August 1855).

employees.[24]

By the 1870s, the legislatures in both the US States[25] and the UK[26] amended the general incorporation statutes to provide for the incorporation of an entity 'for any lawful purpose'. At first glance, it seems that, by virtue of the amendment (which remains on the statute books of the UK[27] and many US States[28]), the UK and US legislatures no longer required a trading corporation to be incorporated and operated for the purpose of making itself a profit. However, it is argued that this amendment was not meant to affect the mercantile expectations imposed on each trading corporation. Rather, the amendment was aimed at liberalizing corporate law in two other ways.

First, the amendment ensured that, as a matter of law, and unlike the businesses incorporated under grants of royal charter or Acts of Parliament, the businesses that each registered trading corporation operated did not need to be a business that the sovereign or the legislature considered to be in the best interests of the public. In contrast, prior to the general incorporation statutes,

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[24] Lord Monteagle also described the 'bubble Companies' as companies that were organised for the purpose of paying 'staff … who would make a profit on the mere salaries they would receive'. HL Deb vol 139 c 2041 (9 August 1855).

[25] The first State statutes to specify that a corporation may be incorporated for 'any lawful purpose' were the following: New York Laws 1866 c838 at p1896; Laws 1875, c611 at p755; Illinois July 1, 1872, Laws 1871-72 p296; Massachusetts Act of April 14, 1874, c165; Maine February 3, 1876, c65, Laws 1876 p51.

[26] Joint Stock Companies Act 1862 (25 & 26 Vict c 89), s6.

[27] Companies Act 2006 (Eng) c 46, s7(2).

[28] Alaska Stat §10.50.010; Del Code Ann tit §6; 805 ILCS §180/1-25; Ky Rev Stat §275.005; La Rev Stat Ann §12.1302; Mass Gen Laws, Ch 156C, §6(a); Me Rev Stat Ann, tit 31, §611; Miss Code Ann §79-29-108(1); Mo Rev Stat §347.035; NH Rev Stat Ann §304-C:7; NC Gen Stat §57C-1-03(3); Ohio Rev Code Ann §1705.02; Okla Stat tit 18, §2002; RULLCA §104(b); Va Code Ann §13.1-1008; Wash Rev Code §25.15.030; W Va Code §31B-1-112(a); cf: Model Business Corporation Act (2002) §3.01, which provides that '[e]very corporation incorporated under this Act has the purpose of engaging in any lawful *business*'.

the UK Parliament had indicated that:[29]

> [c]harters of incorporation are occasionally granted by the Crown to partnerships formed to carry on such undertakings as are considered deserving of encouragement on grounds of public policy.

In introducing the amendment, the legislatures thereby ensured that the only limitation that was placed on the business of each trading corporation was that the business was not otherwise in contravention of the law; eg, by creating a monopoly.[30] The amendment marked 'the abandonment of a pure public sphere notion of the business corporation.'[31]

Secondly, the amendment was also aimed at ensuring that the general incorporation statutes could vest legal personality, not only in trading corporations, but also in charitable or 'public' corporations. Non-profit (charitable or public) corporations predated the general incorporation statutes. For example, the oldest US corporation, Harvard College, is a public corporation.[32] Without the amendment, which allowed the incorporation by registration of associations 'for any lawful purpose', the statutes may not have enabled the incorporation, by way of registration, of non-profit enterprises.

It is a mistake, however, for the law to assume that, because the general incorporation statutes provide for the incorporation of charitable enterprises and non-profit corporations, a trading corporation may also be operated

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[29] Report on the Law of Partnership (1837) Parliamentary Papers #530.

[30] *Peabody v The Chicago Gas Trust Co* 130 Ill 268, 22 NE 798 (Ill SC, 1889) at 292, 298, 803, 805.

[31] R Harris *Industrializing English Law: Entrepreneurship and Business Organization, 1720-1844* (Cambridge University Press) at 284; see also TL Alborn *Conceiving Companies: Joint-Stock Politics in Victorian England* (Rouledge London 1998) at 4.

[32] PG Perrin 'Harvard College in the Seventeenth Century' (1936) 9 The New England Quarterly 530).

without any motive to make itself a profit. A trading corporation differs from the charitable or 'public' corporation in two ways. Most obviously, the non-profit corporation, but not the trading corporation, is operated so as to carry out the charitable or public functions for which the corporation was incorporated. For example, the terms of the Royal Charter under which the British Broadcasting Corporation ('BBC') was incorporated state that '[t]he BBC exists to serve the public interest.'[33] In particular, the BBC was incorporated so as to enable the BBC to, *inter alia*, 'promot[e] education and learning' and 'stimulat[e] creativity and cultural excellence'.[34] In contrast, a corporation that exists to serve the interests of its shareholders, or another corporation in a corporate group, does not further public or charitable ends, but simply the mercantile ends of someone other than itself. Thus, unless a corporation is incorporated and operated in order to further identifiable charitable or public purposes, the courts should classify the corporation, not as a non-profit corporation, but a trading corporation; and the courts should expect that corporation to further mercantile aims for itself.

(b) Courts

Until the turn of the 20th century, and the emergence of the corporate group, the courts in the US and the UK expected every corporation (other than charitable or public corporations) to operate to make a profit for itself. The courts expressed this expectation by circumscribing the power of the corporation to purchase and hold stock in other corporations. The courts limited the corporations' power to own shares in two ways. Both limitations

[33] Royal Charter for the Continuance of the British Broadcasting Corporation, Presented to Parliament October 2006, §3(1).
[34] BBC Royal Charter (note 33), §4.

reveal the fundamental expectation of the 19th century courts that the corporation be operated to make itself a profit.

(i) Refusal to imply a power to own shares

The US courts 'uniformly held',[35] and the UK courts less uniformly held,[36] that a corporation had no power to purchase or hold shares in another corporation, unless the legislature[37] or a Royal Charter had expressly or impliedly conferred that power on the corporation.[38] The courts refused to imply into a corporation's charter the power to own stock in another corporation. The courts' concern was that, if one corporation held stock in another corporation, the businesses of the two corporations could merge, and the corporations would cease to be distinct profit-making entities. The alignment of the corporations' profit streams concerned the courts for the following reason: a

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[35] F Freedland 'History of Holding Corporation Legislation in New York State: Some Doubts as to the 'New Jersey First' Tradition' (1955) 24 Fordham L Rev 370 at 370.

[36] *In re Barned's Banking Co* (1867) LR 3 Ch App 105 at 112; *In re European Society Arbitration Acts* (1878) 8 Ch D 679 (CA) at 704; cf: *In re Asiatic Banking Corporation* (1869) LR 4 Ch App 252 (CA) at 257.

[37] The State legislatures were reluctant to grant the power of stock ownership to corporations: F Freedland 'History of Holding Corporation Legislation in New York State: Some Doubts as to the 'New Jersey First Tradition' (1955) 24 Fordham L Rev 370 at 371. Though, the legislatures were comparably more willing to grant the power to railroad corporations: WR Compton 'Early History of Stock Ownership by Corporations' (1940) 9 George Washington L Rev 125 at 127; PI Blumberg 'Limited Liability and Corporate Groups' (1986) 11 J of Corporation Law 573 at 605.

[38] *Franklin Co v Lewiston Institution for Savings* 68 Me 43 (1877, SC Maine) at 46; *Booth v Robinson* 55 Md 419 (1880); *Nassau Bank v Jones* 95 NY 115 (1884); *Peabody v The Chicago Gas Trust Co* 130 Ill 268, 22 NE 798 (Ill SC, 1889) at 285-6, 801; *Davis v United States Electric Power & Light Co* 77 Md 35, 25 A 982 (1893); *Pauly v Coronado Beach Co* 56 F 428 (1893, Circuit Court, SD California) at 430; *Byrne v Schuyler Electric Manufacturing Co* 65 Conn 336, 31 A 833 (1895, SC Conn) at 350, 836; *Warren v Pim* 66 NJ Eq 353, 59 A 773 (1904, CA NJ) at 358-9, 775; *Hermitage Hotel Co v Dyer* 125 Tenn 302, 142 SW 1117 (1911, SC Tenn) at 306, 1118; 1A Fletcher Cyc Corp, §2825. The courts applied this restriction on their powers even to banking corporations: *First National Bank of Charlotte v National Exchange Bank of Baltimore* 92 US 122 (1875) at 128; *California National Bank v Kennedy* 167 US 362, 17 S Ct 831 (1897) at 367, 833; *Talmage v Pell* 7 NY 328 (1852 CA New York) at 343. The US courts also ruled, for a time, that a corporation's purchase of stock in another corporation was not only ultra vires the corporation's powers, but also contrary to public policy: *Louisville & Nashville Railroad Co v Kentucky* 61 US 677, 16 S Ct 714 (1896) at 698; see also *Robotham v The Prudential Insrance Co of America* 64 NJ Eq 673, 53 A 842 (1903, Ch NJ) at 697, 851-2.

corporation is not empowered to operate a business that falls outwith the terms of the objects provision in its constitution.[39]

(ii) Improper purpose for which power exercised

Furthermore, even if the objects clauses of the constitutions of two corporations were identical, and even if a corporation was expressly granted the power to own shares in another corporation, the US courts nonetheless considered it an improper exercise of the power if its exercise caused the parent corporation to control the business of the subsidiary corporation.[40] The courts' refusal to permit the power to own shares to be exercised in order to control another corporation did not preclude one corporation from acting as an agent to another corporation. It was recognized that it may be in the interests of one corporation to act in the interests of another corporation. Where the parent corporation did not prevent the subsidiary corporation from operating its own business, but merely established relationships of mutual exchange between the corporations, the courts did not characterize as improper the exercise of the

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[39] US: *Sumner v Marcy* 23 F Cas 384 (1847, Circuit Court D Maine) at 386;*Sumner v Marcy 23 F Cas 384* (1847, Circuit Court D Maine) at 344; *Franklin Co v Lewiston Institution for Savings* 68 Me 43 (1877, SC Maine) at 46; *Nassau Bank v Jones* 95 NY 115 (1884); *Bank of Commerce v Hart* 37 Neb 197, 55 NW 631 (1893 SC Neb); *Marbury v Kentucky Union Land Co* 62 F 335 (1894, 6th cir) at 342, 18; UK: *Joint Stock Discount Co v Brown* (1866) LR 3 Eq 139 (Eq) at 150-1; *In re European Society Arbitration Acts* (1878) 8 Ch D 679 (CA) at 704.

[40] *Sumner v Marcy* 23 F Cas 384 (1847, Circuit Court D Maine) at 386; *Pearson v Railroad Co* 62 NH 537 (1883, SC NH) at 548-9, 28; *Marbury v Kentucky Union Land Co* 62 F 335 (1894, 6th cir) at 17-18,342; *McCutcheon v Merz Capsule Co* 71 F 787 (1896, CA 6th cir); *Martin v Broadhead* 78 Ill App 105 (1898, CA Ill) at 107; *De la Vergne Refrigerating Machine Co v German Savings Institution* 175 US 40, 20 S Ct 20 (1899) at 48, 21; *Dunbar v The American Telephone and Telegraph Co* 224 Ill 9, 79 NE 423 (1906, SC Ill) at 24, 427; *Holt v California Development Co* 161 F 3 (1908, 9th cir) at 13-14, 29-30; *United Vacuum Sweeper Co v Groth* 210 Ill App 358 (1918, CA Ill); *Somners v Apalachicola Northern Railroad Co* 75 Fla 159, 78 So 25 (1918, SC Fla) at 219, 43; cf: *Green v People's Gas Light and Coke Corporation* 118 Misc 1, 192 NYS 232 (1922, SC NY) at 4-5, 235-6. The courts also held that the corporation's power to enter into contracts was exercised for an improper purpose if used not 'for the benefit and in the business of the corporation' but 'for the benefit or in the business of others'; *McLellan v File Works* 56 Mich 579, 23 NW 321 at 583, 322; *Humboldt Mining Co v American Manufacturing, Mining & Milling Co* 62 F 356 (1894, Circuit Court of Appeals, 6th Cir) at 362.

power to own shares in another corporation.[41]

The courts had reason to require that any power to purchase stock in another corporation not be exercised in order to control another corporation. Specifically, it may have been that the Special Act that granted a corporation the power of stock ownership expressed the legislative intention that the parent and subsidiary corporations each pursue for themselves their own line of business that is separate from the businesses of any other corporation.[42] For example, the charter of the Carroll Corporation empowered the corporation to acquire stock ownership in the following terms:[43]

> Said corporation may purchase real estate, mines and other property, and pay therefore in the stock of said corporation, and whenever said corporation shall become possessed of more than one mine, property or estate, said corporation may, if they so elect, make a distinct concern of each, and organize the same under a suitable designation.

More generally, however, the grant of incorporation to both the purchasing and subsidiary corporation entails an expectation that the incorporated entity be operated as a separate legal person that is 'entitled to retain its business and assets'[44]. In *Buckeye Marble & Freestone Co v Harvey*,[45] the Supreme Court of Tennessee reasoned that, to permit a corporation to exercise the power of

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[41] *Willoughby v The Chicago Junction Railways and Union Stockyards Co* 50 NJ Eq 656, 25 A 277 (1892, Ch NJ) at 690, 289-90; *St Paul Trust Co v Wampach Manufacturing Co* 50 Minn 93, 52 NW 274 (1892); *White v GW Marquardt & Sons* 105 Iowa 145, 74 NW 930 (1899); *Fourth National Bank of Nashville v Stallman* 132 Tenn 367, 178 SW 942 (1915); *Farmers' State Bank v Richter* 48 ND 1233, 189 NW 242 (1922); Note 'Power of a Corporation to Acquire Stock of Another Corporation' (1931) 31 Columbia L Rev 281 at 288-9.

[42] WR Compton 'Early History of Stock Ownership by Corporations' (1940) 9 George Washington L Rev 125 at 130.

[43] Laws of New Hampshire (1853), p1403; see WR Compton 'Early History of Stock Ownership by Corporations' (1940) 9 George Washington L Rev 125 at 130.

[44] *Creasey v Breachwood Motors Ltd* [1993] BCLC 480 (QB) at 492.

[45] 92 Tenn 115, 20 SW 427 (1892).

stock ownership in order to control the business of the other corporation, is to undermine the purpose for which the law incorporated the *parent* corporation:[46]

> The purpose and intent in granting a charter is, that the corporation shall carry on its business through its agents, and not through the agency of another corporation. The public policy of this State will not permit the control of one corporation by another.

In *Anglo-American Land, Mortgage & Agency Co v Lombard*,[47] the Eighth Circuit reasoned that the exercise of the power to own shares in order to control another corporation undermines the purpose for which the law granted legal personality to the *subsidiary* corporation:[48]

> Where it is not otherwise provided, the implication in a grant of corporate power and life is that the corporation … shall maintain an independent corporate existence, and not surrender the control of its affairs or the exercise of its powers to another corporation.

The US courts' concern that the corporation not exercise its power to hold shares in order to control the business of another corporation was grounded in a fundamental principle of corporate law. The fundamental principle expected each non-eleemosynary company to aim to make itself a profit. US and UK corporate law enacted this principle in two ways. First, the law limited the ways in which the directors could exercise their powers, so that each of the corporation's powers, which directors exercise, must be exercised in the interests of the corporation.[49] Secondly, the courts limited *all* powers of the

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[46] *Buckeye Marble & Freestone Co v Harvey* 92 Tenn 115, 20 SW 427 (Tenn SC 1892) at 118; see also *Berry v Yates* 24 Barb 199 (1857, SC NY).
[47] 132 F 721 (1904).
[48] *Anglo-American Land, Mortgage & Agency Co v Lombard* 132 F 721 (1904, 8th cir) at 735.
[49] Companies Act 2006 (Eng) c 46, s171(b); Alabama: Ala Code 1975 §§10-2B-8.30, 10-2B-8.42; Alaska: AS §§10.06.450(b), 10.06.468(b); Arizona: ARS §§10-830, 10-842, 10-3830, 10-3842; Arkansas: ACA §§ 4-27-830, 4-27-842, 23-18-321(a)(2)(c); Colorado: CRSA §7-108-401(1)(c);

corporation. The corporation had the power to act in order:

(i) to benefit another legal person or class of persons (eg, shareholders or employees) in order to benefit itself. For example, the UK courts held that the power to remunerate employees could be exercised only as required to benefit the company.[50] While the US courts held that the corporation's power was exercised for an improper purpose if used not 'for the benefit and in the business of the corporation' but 'for the benefit or in the business of others';[51] and

(ii) to benefit itself in a way that, derivatively, benefited other legal persons. For example, the company had the power to increase its profitability, and thus, the value of its share price and the value of the shareholders' shares.

Connecticut: CGSA §§33-756(a)(3), 33-765(a)(3), 33-1104(a)(3), 33-1111(a)(3); Florida: FSA §§607.0830(1)(c), 617.0830(1)(c); Hawaii: HRS §§414-221(a)(3), 414-233(a)(3), 414D-149(a)(3), cf §414D-155(a)(3); Indiana: IC §§23-1-35-1(1)(a)(3), 23-17-13-1(a)(3), 27-1-7-12.5(a)(3), 28-13-11-1(3), 30-1-830(1)(b), 30-1-842(1)(c), 30-3-80(1)(c), 30-3-85(1)(c); Iowa: ICA §§490.830(1)(b), 490.842 (1)(c), 504.831(1)(b), 504.843(1)(c); Maine: 13-B MRSA §717(1)(c), 13-C MRSA §§831(1)(b), 843(1)(c), cf 13-B MRSA §720(1)(c); Maryland: MD Code Corporations and Associations §2-405.1; Massachusetts: MGLA 156B §65, MGLA 156D §§8.30(a)(3), 8.42(a)(3), MGLA 180 §6C; Michigan: MCLA § 450.1541a(1)(c); Minnesota: MSA §§302A.251(1), 302A.361, 317A.251(1), 383B.905(2); Mississippi: Miss Code Ann §§79-4-8.30(a)(2), 79-4-8.42(a)(2); Montana: MT ST §§35-1-418(1)(c), 35-1-443(1)(c); 35-2-416(1)(c), cf §35-2-441(1)(c); Nebraska: NE ST §§21-1986, 21-2095(1)(c), 21-2099(1)(c), cf §21-1992(a)(3); New Hampshire: NH Rev Stat §§293-A:8.30(a)(3); 293-A:8.42(a)(3); New Jersey: NJSA §14A:6-1(2); North Carolina: NCGSA §§55-8-30(a)(3), 55-8-42(a)(3); North Dakota: NDCC §§10-19.1-50, 10-19.1-60, 10-33-45, 10-33-56; Oregon: ORS §§60.357, 60.377; Pennsylvania: 15 Pa CSA §§512, 1712, 5712; Rhode Island: Gen Laws 1956 §§7-1.2-801(b)(3), 7-6-22(b)(3); South Dakota: SDCL §§47-1A-830, 47-1A-842(3); Tennessee: TCA §§48-18-301(a)(3), 48-58-301(a)(3), 48-58-403(a)(3); Utah: UCA 1953 §16-10a-840; Vermont: 11A VSA §8.30(a)(3); Virginia: Va Code Ann §13.1-690; Washington: RCWA §§23B.08.300(1)(c), 23B.08.420(1)(c), 24.06.153(1)(c); West Virginia: W Va Code §§31D-8-830(a), 31D-8-842(a)(3), 31E-8-830(a)(2), 31E-8-842(a)(3).

[50] Eg, *Hutton v West Cork Rly Co* (1883) 23 Ch D 654; *Dafen Tinplate Co Ltd v Llanelly Steel Co Ltd* [1920] 2 Ch 124 (Ch); *Sidebottom v Kershaw, Leese and Co Ltd* [1920] 1 Ch 154 (CA) at 164; *McLellan v File Works* 56 Mich 579, 23 NW 321, 583, 322; *Humboldt Mining Co v American Manufacturing, Mining & Milling Co* 62 F 356 (1894, Circuit Court of Appeals, 6th Cir) at 362.

[51] *McLellan v File Works* 56 Mich 579, 23 NW 321, 583, 322; *Humboldt Mining Co v American Manufacturing, Mining & Milling Co* 62 F 356 (1894, Circuit Court of Appeals, 6th Cir) at 362.

However, the company did not have the power to act for the purpose, not of benefitting itself, but simply of benefitting another legal person or class of persons; eg, its shareholders.

(ii) Modern concept of the corporation

(a) The reform

Around the turn of the 20th century, the US courts abandoned the common law line of reasoning that considered it improper for one corporation to exercise the power of stock ownership to control another corporation. The modern courts now hold that the power of stock ownership may be exercised to control a subsidiary corporation;[52] and thereby to ensure that one corporation acts, not to make itself a profit, but to assist the other corporation in making a profit.[53] The US and UK courts cease to picture the company as an incorporated *business* – like Salomon & Co – and now imagine the company as an incorporated *trust*.

This change of attitude affected a judicial reform of corporate law that changed the modern world. Prior to the turn of the 20th century, the holding corporation device was 'far from unknown either to industry or the courts'.[54] However, the holding corporation inundated the commercial landscape as soon

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[52] *Rogers v Nashville C & St L Rly Co* 91 F 299 (1898, CA 6th cir) at 312, 23-4; *Northern Central Rly Co v Walworth* 193 Pa 207, 44 A 253 (1899, SC Penn) at 214-6, 255-6; *Bigelow v Calumet & Hecla Mining Co* 167 F 721 (1908, CA 6th cir) at 723-4, 4-5; *State v Atlantic City and Shore Railroad Co* 77 NJL 465, 72 A 111 (1909, CA NJ) at 470-1, 114; *Henry L Doherty & Co v Rice* 186 F 204 (1910, CC ND) at 212, 15-16; *Citizens Lumber Co v Elias* 199 NC 103, 154 SE 54 (1930, SC NC) at 107-8, 56-7; 1A Fletcher Cyc Corp, §95.

[53] *Ellerman v The Chicago Junction Railways and Union Stockyards Co* 49 NJ Eq 217, 23 A 287 (1891, Ch NJ) at 240, 295.

[54] Comment 'Federal Regulation of Holding Companies: The Public Utility Act of 1936' (1936) 45 Yale L J 468 at 470.

as the law permitted a corporation to exercise, without limit, its power to own stock. As a result of New Jersey's statutory grant of corporate power to own stock in the late 1890's, '1336 corporations, with an aggregate authorized capital of over two billion dollars, [had] formed in New Jersey during the first seven months of 1899.'[55] By 1929, 'sixteen holding corporation groups controlled 92% of the power produced by private companies in the United States.'[56] By 1995, 'the ten largest companies on the Fortune 500 owned an average of 62 subsidiaries each.'[57]

Nonetheless, despite the importance of the change in judicial attitudes, the reform remained unarticulated.[58] The courts did not identify the extent to which their decision conflicted with existing authority, nor offer reasons as to why the courts ought no longer to invigilate the purposes for which the power of stock ownership was exercised.

It is commonly assumed that the holding corporation emerged as a result of legislative reform. The variation in judicial attitude roughly coincided with the amendment to the general incorporation statutes of most US States. The amendment expressly empowered corporations to purchase and hold the stock

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[55] EM Dodd 'Statutory Developments in Business Corporation Law, 1886-1936' (1936) 50 Harvard L Rev 27 at 34; see also *Liggett Co v Lee* 288 US 517 (1933) at 562-3.

[56] Comment 'Federal Regulation of Holding Companies: The Public Utility Act of 1936' (1936) 45 Yale L J 468 at 470-1; see also DE Lilienthal 'The Regulation of Public Utility Holding Companies' (1929) 29 Columbia L Rev 404 at 404.

[57] EJ Gouvin 'Resolving the Subsidiary Director's Dilemma' (1996) 47 Hastings L J 287 at 287.

[58] Cf PI Blumberg 'Limited Liability and Corporate Groups' (1986) 11 J of Corporation Law 573, who argues that the modern law's mistake was not the law's impulsive decision to remove the limits to the legislative power to hold stock, but the law's decision unthinkingly to grant limited liability to corporate shareholders. However, it is argued that the grant of limited liability was a consequence of the law's grant to corporations of the power to own stock. Though, the emergence in the early 1900s of the modern corporate group did prompt historians to review 'the unmixed blessing' of limited liability: HA Shannon 'The Limited Companies of 1866-1833' (1933) 4 Economic History Rev 290 at 307.

of other corporations.[59] For example, section 51 of the New Jersey Corporation Act, as revised in 1896, provided that:

> any corporation may purchase, hold, sell, assign, transfer, mortgage, pledge or otherwise dispose of the shares of the capital stock of, or any bonds, securities or evidences of indebtedness created by any other corporation or corporations of this or any other state, and while owner of such stock may exercise all the rights, powers and privileges of ownership, including the right to vote thereon.

The current State statutes continue to include this legislative grant of corporate power.[60]

However, there are two problems with the assumption that the legislature's express grant to corporations of a power of stock ownership motivated or rationalized the judicial reform. First, the amendment did not

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[59] New York was the first State to introduce the amendment to the general incorporation statutes; F Freedland 'History of Holding Corporation Legislation in New York State: Some Doubts as to the 'New Jersey First Tradition' (1955) 24 Fordham L Rev 370; EQ Keasbey 'New Jersey and the Great Corporations' (1899-1900) 13 Harvard L Rev 198 at 207. New Jersey (NJ Laws 1888, c259 at p385; NJ Laws 1888, c259 at p445; NJ Laws 1889, c265, § 4 at p414; NJ Laws 1893, c171, §1 at p301), and then the other States followed suit.

[60] Most jurisdictions adopt the Revised Model Business Corporation Act (1984) § 3.02(6), which provides that a corporation has the power: 'to purchase, receive, subscribe for, or otherwise acquire; own, hold, vote, use, sell, mortgage, lend, pledge, or otherwise dispose of; and deal in and with shares or other interests in, or obligations of, any other entity'; Ala Code § 10-2B-3.02(6); Alaska Stat § 10.06.010(7); Ariz Rev Stat Ann § 10-302(6); Ark Stat Ann § 4-27-302(6); Colo Rev Stat § 7-103-102(f); Conn Gen Stat § 33-647; Fla Stat § 607.0302(6); Ga Code Ann § 14-2-302(6); Haw Rev Stat § 414-42(6); Idaho Code § 30–1–304; 805 ILCS 5/3.10(g); Ind Code § 23-1-22-2(6); Iowa Code § 490.302(6); Ky Rev Stat Ann § 271B.3-020(1)(f); Me Rev Stat Ann tit 13-C, § 302(6); Miss Code Ann § 79-4-3.02(6); Mont Code Ann § 35-1-115(6); Neb Rev Stat § 21-2025(6); NH Rev Stat Ann § 293-A:3.02(6); NC Gen Stat § 55-3-02(a)(6); Or Rev Stat § 60.077(2)(f); SC Code Ann § 33-3-102(6); Tenn Code Ann § 48-13-102(6); Utah Code § 16-10a-302(6); Vt Stat Ann tit 11A, § 3.02(6); Va Code Ann § 13.1-627(A)(6); Wash Rev Code § 23B.03.020(2)(f); W Va Code § 31D-3-302; Wis Stat § 180.0302(6); Wyo Stat § 17-16-302(a)(vi). Other jurisdictions adopt the Model Business Corporation Act (1969) § 4(g); Md Corps & Ass'ns Code Ann § 2-103(9); Mass Gen L ch 156B, § 9(g); MCL § 450.1261(h); Minn Stat § 302A.161 subd (6); Mo Rev Stat § 351.385(6); Nev Rev Stat § 78.070(2); NJ Rev Stat § 14A:3-1(f); NM Stat Ann § 53-11-4(G); NY Bus Corp Law § 202(a)(6); ND Cent Code § 10-19.1-26(6); Okla Stat tit 18, § 1017; RI Gen Laws § 7-1.2-302; Tex Bus Corp Act Ann art 2.02(A)(7); 6A Fletcher Cyc Corp, §2832.

include the 'clear and unambiguous' language, to express a statutory policy, that is needed to displace the common law rule that required the corporation's power to acquire shares not to be exercised for the improper purpose of acquiring control of another corporation.[61] Some courts interpreted these statutes as 'declarations of public policy'[62] that a corporation should be permitted, not only to purchase shares in another corporation, but also to control that other corporation. However, as a Note in the Columbia Law Review noted:[63]

> [t]hat these decisions are more the result of a different attitude on the part of the courts toward large corporations, than of the statutes themselves, is shown by the absence of express permission to buy stock for control in almost all of the statutes.

Only one statute revealed a policy that a corporation should be empowered to control another corporation.[64] Currently, only the statute of Ohio expressly indicates that the power of stock ownership may be exercised in order to control another corporation.[65] Other statutes implied a policy that no corporation be controlled by any other corporation. For example, §180.11 of the Wisconsin statute permitted a corporation to purchase shares in another corporation only where, *inter alia*: 'the assent of the holders of three fourths of the capital stock of both the corporation proposing to take such stock *and the*

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[61] *Kappers v Cast Stone Construction Co* 184 Wis 627, 200 NW 376 (1924, SC Wis) at 633, 378.
[62] Note 'Power of a Corporation to Acquire Stock of Another Corporation' (1931) 31 Columbia L Rev 281 at 289.
[63] Note 'Power of a Corporation to Acquire Stock of Another Corporation' (1931) 31 Columbia L Rev 281 at 289.
[64] NY Stock Corporation Law (McKinney Supp 1930) §18 (the purchasing corporation may elect its own directors to the board of the other corporation.)
[65] Ohio Rev Code Ann § 1701.13(F): '[i]n carrying out the purposes stated in its articles and subject to limitations prescribed by law or in its articles, a corporation may: … (3) Form or acquire the control of other corporations, domestic or foreign, whether nonprofit or for profit… .'

corporation in which it is proposed to be taken.'[66] As the Court of Chancery of New Jersey noted:[67]

> Section 51 [of the Corporation Act, as revised in 1896] may have been declaratory and its sole effect may have been to remove certain, perhaps vague, doubts as to the inherent capacity or incapacity of corporations to acquire and hold shares of stock of other corporations, even when such acquisition is made strictly in pursuance of the corporate objects.

Thus, while the amendments confirmed the power of corporations to acquire stock in other corporations, they did not state that the power was also to be exercised without any legal limit. The amendments did not make clear that the conferred power was exercisable even for the purpose, which the courts had hitherto considered improper, of controlling another corporation.

There is a second problem with the assumption that the legislative grant of corporate power justified the courts' decision not to supervise the manner of the power's exercise. Prior to 1900, the courts were attentive to the powers of both parent and subsidiary corporation. The courts qualified the parent's power to own stock in the subsidiary so that the power did not undermine the purpose for which the law granted legal personality, and all other corporate powers, to either the parent or the subsidiary corporation.[68] In contrast, because the modern courts give a limitless interpretation to the parent's power to own stock, the courts are necessarily oblivious to the subsidiary's power to operate its own business. While §3.02(6) of the Model Business Corporation Act (2002) empowers the corporation to hold stock in another corporation,

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[66] Emphasis added. See *Kappers v Cast Stone Construction Co* 184 Wis 627, 200 NW 376 (1924, SC Wis).
[67] *Robotham v The Prudential Insrance Co of America* 64 NJ Eq 673, 53 A 842 (1903, Ch NJ) at 695, 851.
[68] See notes 46 and 48.

§3.02(10) empowers the other corporation 'to conduct *its* business'.[69] As a matter of logic, the corporation's powers under §3.02 are necessarily limited – at least by reference to the other powers that the general incorporation statutes vest in corporations. While modern courts articulate corporate law principles, and apply those principles to the corporation at the bar table, the courts do not contemplate the extent to which their decisions render those principles inapplicable to any other corporation. The result is that modern courts, by refusing to impose a limit to the corporate power to own stock, empower one corporation to appropriate from the corporation in which it owns stock the power 'to conduct its [own] business'.[70]

(b) Doctrinal inconsistency

The reform of judicial attitudes concerning the corporate power to hold shares fractured the structure of principle of corporate law. Modern corporate law now vests legal personality in the corporation, not so that it may generate its own profit stream, but simply so that it may act as a 'unit… in a line of production.'[71] In this way, the law enables shareholders to segregate a profit stream from the legal person of the corporation, and then combine independent profit streams within the non-legal entity of the corporate group. The ease with which the assets of a corporation may be manipulated amongst

[69] See note 60 (emphasis added).
[70] Model Business Corporation Act (2002) §3.02(6).
[71] WO Douglas and CM Shanks 'Insulation from Liability Through Subsidiary Corporations' (1929) 39 Yale L J 193 at 197; E Dillavou 'Desirable Legal Changes in Holding Corporation Legislation' (1930-1934) 7 American L School Rev 857 at 857; Comment 'Federal Regulation of Holding Companies: The Public Utility Act of 1936' (1936) 45 Yale L J 468 at 473-4; JM Landers 'A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy' (1975) 42 U Chicago L Rev 589 at 589-90.

members of a corporate group was promptly noted.[72] And the holding corporation was quickly used as a mechanism by which the corporate group avoided liabilities.[73] Problematically, different parts of the law responded to the emergence of the holding corporation with contradictory reforms. The result is that modern corporate law remains unanchored in principle and internally inconsistent.

(i) State law

In 1913, and at the behest of its recent Governor, Woodrow Wilson, New Jersey passed the Seven Sisters Acts of 1913.[74] The Acts were passed to tighten its corporate law, introduce anti-trust measures and restore its soiled reputation as the 'Mother of Trusts'.[75] The corporations that had incorporated in New Jersey[76] re-incorporated in Delaware.[77] By the time the Seven Sisters Acts were repealed in 1917, 'Delaware, and then a number of other states began to offer incorporation on terms of increasing liberality.' [78] The States' 'race to the bottom'[79] of corporate regulation, which Delaware has ever since led, had

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[72] E Dillavou 'Desirable Legal Changes in Holding Corporation Legislation' (1930-1934) 7 American L School Rev 857 at 860; JP Chamberlain 'Regulation of Public Utility Holding Companies' (1931) 17 American Bar Association J 365 at 365.
[73] M Breckenridge 'Tax Escape by Manipulations of Holding Corporation' (1930) 9 North Carolina L Rev 189; Note 'Legislation Extending Control over Public Utility-Affiliate Contracts' (1931-1932) 45 Harv L Rev 729at 729; K Field 'Some Uses of Holding Corporations' (1932) 8 J of Land & Public Utility Economics 175; K Field 'Use of Subsidiary Corporations in Segregating Risk' (1933) 9 J of Land & Public Utility Economics 150.
[74] NJ Laws 1913 cc13-19.
[75] HN Butler 'Smith v Van Gorkom, Jurisdictional Competition, and the Role of Random Mutations in the Evolution of Corporate Law' (2006) 45 Washburn L J 267 at 269-70; WL Cary 'Federalism and Corporate Law: Reflections upon Delaware' (1974) 83 Yale L J 663 at 664; HN Butler 'Nineteenth-Century Jurisdictional Competition in the Granting of Corporate Privileges' (1985) 14 J of Legal Studies 129 at 163.
[76] See note 55.
[77] See note 75.
[78] JW Hurst *The Legitimacy of the Business Corporation in the Law of the United States 1780-1970* (University Press of Virginia Charlottesville) at 69-70.
[79] *Liggett Co v Lee* 288 US 517 (1933) at 558-9.

begun.

The US States have cultivated a range of corporate laws that aim to encourage corporations to incorporate under their State laws.[80] In so doing, the States further erode the fundamental principle that a corporation is operated in order to make itself a profit. Of especial importance is the States' restatement of the law of directors duties, and their application to corporate groups and holding companies.

State corporate law no longer insists that the directors' duty to act in the best interests of the corporations is a duty that is owed simply to the corporation.[81] In *Dodge v Ford Motor Co*,[82] the Supreme Court of Michigan held that:[83]

> [a] business corporation is organized and carried on primarily for the profit of its stockholders. The powers of the directors are to be employed to that end.

The modern courts now understand the directors' duty to act in the interests of the corporation as a duty to act in the interests of 'the corporation and its shareholders'.[84] When applied in the context of corporate groups, this reasoning is apt to confuse. If a director owes a duty to act in the best interests

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[80] Eg, WL Cary 'Federalism and Corporate Law: Reflections upon Delaware' (1974) 83 Yale L J 663.
[81] Cf *Unocal Corp v Mesa Petroleum Co* 493 A 2d 946 (SC Del 1985) at 958; *Paramount Communications Inc v Time Inc* 571 A 2d 1140 (Del 1989) at 1154; *Credit Lyonnais Bank Nederland NV v Pathe Communications Corp* 1991 Del Ch LEXIS 215 (Del 1991) at [108]; *First American Corp v Al-Nahyan* 17 F Supp 2d 10 (DDC 1998)
[82] 204 Mich 459, 170 NW 668 (1919).
[83] *Dodge v Ford Motor Co* 204 Mich 459, 170 NW 668 (1919, SC Mich) at 507, 684.
[84] *Aronson v Lewis* 473 A 2d 805 (Del 1984) at 811; *Guth v Loft* 5 A 2d 503 (Del 1939) at 510; Smith v Van Gorkom 488 A 2d 858 (Del 1985) at 872; see also Companies Act 2006 (Eng) c 46, s172: 'A director of a corporation must act in the way he considers … would be most likely to promote the success of the corporation for the benefit of its members as a whole'.

of the corporation and its shareholders, must the director act in the interests of the corporation (for whom he is a fiduciary) or the parent corporation, which holds stock in the corporation? Arguably, State law hit rock bottom in the *Anadarko* case, when the Supreme Court of Delaware concluded that:[85]

> in a parent and wholly-owned subsidiary context, the directors of the subsidiary are obligated only to manage the affairs of the subsidiary in the best interests of the parent and its shareholders.

To compensate, some US courts impose on the parent corporation a fiduciary duty to act in the interests of the subsidiary corporation.[86] The UK courts impose on the parent an 'obligation to conduct what are in a sense its own affairs as to deal fairly with its subsidiary.'[87] Thus, as a result of the law's uncertain commitment to the principle that a corporation must be operated in its own interests, and in order to make a profit for itself, directors are left 'in an untenable position'.[88]

(ii) Federal securities law

As the States liberalized the regulations to which corporations were made

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[85] *Anadarko Petroleum Corp v Panhandle Eastern Corp* 545 A 2d 1171 at 1174 (1988, Del) at 1174. For the UK courts' approach to directors' duties in the context of corporate groups, see *Charterbridge Corp Ltd v Lloyds Bank* [1970] 1 Ch 62; *Bristol and West Building Society v Mothew* [1998] Ch 1 (CA); *Extrasure Travel Insurances Ltd v Scattergood* [2002] EWHC 3093; [2003] 1 BCLC 598 (Ch).

[86] *Southern Pac Co v Bogert* 250 US 483 (1919) at 487-88, 492; *Gottesman v General Motors Corp* 279 F Supp 361 (SDNY 1967); *Getty Oil v Skelly Oil Co* 267 A 2d 883 (Del 1970) at 886; *Banco de Desarrollo Agropecuario SA v Gibbs* 709 F Supp 1302 (SDNY 1989) at 1306. Cf *Sinclair* Oil Corp v Levien 280 A 2d 717 (Del 1971) at 720.

[87] *Scottish Co-operative Wholesale Society Ltd v Meyer* [1959] AC 324 (HL) at 343. A breach of this obligation may entitle a minority shareholder to relief under the unfair prejudice remedy of s994 of the Companies Act 2006; *Nicholas v Soundcraft Electronics Ltd* [1993] BCLC 360 (CA).

[88] EJ Gouvin 'Resolving the Subsidiary Director's Dilemma' (1996) 47 Hastings L J 287 at 293; ED Enriquez 'Honor Thy Shareholder at All Costs? Towards a Better Understanding of the Fiduciary Duties of Directors of Wholly-Owned Subsidiaries' (2003) 32 Southwestern U L Rev 97; SJ Padfield 'In Search of a Higher Standard: Rethinking Fiduciary Duties of Directors of Wholly-Owned Subsidiaries' (2004) 10 Fordham J Corporate & Financial L 79.

subject, the burden of supervising corporate activities fell on the securities regulators.[89] As State laws raced to develop laws that interfered least with corporate management, the securities regulators opted to run their own race, outside (and in addition to) the framework of corporate law. Securities regulation quickly imposed requirements on corporations that State corporate law was unwilling to enforce. For example, it was the listing requirements of the New York Stock Exchange ('the NYSE') that first compelled corporations listed on the Exchange to make available to shareholders annual reports.[90]

The listing rules of the NYSE, like many other of the world's leading stock exchanges, also imposed the following precondition to listing. For a corporation to list its securities on its exchange, the corporation must be an entity that is operated in order to make itself a profit. Currently, the NYSE requires that a corporation 'must meet one of the … financial standards'.[91] If a corporation is an 'affiliated corporation', it must have 'at least 12 months of operating history' before it can list on the exchange. That is, the corporation must satisfy the classical concept of the corporation, and operate to make itself a profit, for at least 12 months before its securities are tradable on the exchange.[92]

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[89] JW Hurst *The Legitimacy of the Business Corporation in the Law of the United States 1780-1970* (University Press of Virginia Charlottesville) at 70-1.

[90] JW Hurst *The Legitimacy of the Business Corporation in the Law of the United States 1780-1970* (University Press of Virginia Charlottesville) at 91: 'the most effective pressure began with the late-nineteenth-century expansion of the listing requirements of the New York Stock Exchange. The Exchange moved from the first request for some reports from listed companies in 1866 to a strong suggestion for the filing of annual reports in 1895, to a requirement of annual earnings reports and submission of balance sheets in 1900, to a 1909 requirement that listed companies distribute annual financial reports to their stockholders, and then to an active threat of delisting to enforce requirements of annual reports in 1932 and to enforce a minimum of informative detail in 1933.'

[91] Listed Corporation Manual, §102.01C.

[92] See also rule 2(4) of Criteria for Listing Examination of Stock, Tokyo Stock Exchange: 'The applicant must be able to ensure independence from its parent corporation, etc.'

The UK's Financial Services Authority imposes a more stringent requirement on companies that apply for admission of its securities on a regulated market. The new applicant must demonstrate, not only that it has a track record of profitability, but also that it:[93]

(i) 'controls the majority of its assets' and

(ii) 'will be carrying on an independent business as its main activity.'[94]

Thus, even though State corporate law no longer requires corporations to be operated in order to make themselves a profit, and no longer requires directors of a corporation in a corporate group to act in the interests of the corporation, securities regulation continues to expect that each corporation listed on regulated markets will be operated to make itself a profit. To ensure the integrity of the markets,[95] securities regulation retains the classical concept of the corporation.

(iii) Veil-piercing jurisprudence

Absent a classical (or stock broker's) concept of the corporation, modern courts lack the tools needed to describe the boundaries of legal personality. The US and UK courts 'pierce the veil'[96] that separates the legal personality of the

[93] Listing Rules, r6.1.4R.
[94] Listing Rules, r6.1.4R(3).
[95] Eg, LR 6.1.6 of the Financial Services Authority's Listing Rules explains that: 'LR 6.1.4R is intended to enable prospective investors to make a reasonable assessment of what the future prospects of the applicant's business might be.'
[96] The term was first penned by Maurice Wormser: M Wormser 'Piercing the veil of corporate entity' (1912) 12 Colum L Rev 496. The German courts use the epithet of 'Durchgriffshaftung'; C Alting 'Piercing the Corporate Veil in American and German Law - Liability of Individuals and Entities: A Comparative View' (1994) 2 Tulsane J Comparative & International L 187 at 190.

corporation and its shareholders[97] in order to hold a shareholder liable for the liabilities of the corporation. The US and UK courts use a range of labels to describe the nature of the relationship between a corporation and its shareholders that warrants the piercing of the corporate veil. The courts in both jurisdictions have expressed an intention to pierce the veil whenever the maintenance of separate legal personalities 'would work fraud or injustice.'[98] The US courts, though not the UK courts,[99] are also willing to pierce the corporate veil if the incorporated entity is 'a mere agency or instrumentality'[100] or 'alter ego'[101] of its shareholders.

How does the recognition of legal personality 'work fraud or injustice'? When does a corporation act as 'a mere agent' or 'alter ego' of another legal person? To identify the meaning of the different metaphors, the US and UK courts apply a similar – and equally indeterminate – catalogue of factors.[102]

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[97] On the principle of separate legal personality, see, eg, Revised Model Business Corp Act §§6.22, 2.02(b)(2)(v) (1994); Del Code Ann tit 8, §102(b)(6) (1992); *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL).

[98] US: *Taylor v Standard Gas & Electric Co* 306 US 307, 59 S Ct 543 (1939) 322, 550; *NLRB v Deena Artware Inc* 361 US 398 (1960); *US v Milwaukee Refrigerator Transit Co* 142 F 247 at 248 (CCED Wis 1905); UK: *Woolfson v Strathclyde Regional Council* [1978] SC (HL) 90 (HL) 96; *Creasey v Breachwood Motors Ltd* [1993] BCLC 480 (QB) at 492; see also TL Alborn *Conceiving Companies: Joint-Stock Politics in Victorian England* (Rouledge London 1998) 62, 1885.

[99] *Adams v Cape Industries Plc* [1990] 1 Ch 433 (CA); cf *Littlewoods Mail Order Stores Ltd v IRC* [1969] 1 WLR 1241 (CA) at 1254; *Wallersteinr v Moir* [1974] 1 WLR 991 (CA) at 1013. In these two cases, Denning LJ was willing to pierce the veil when the corporation was a 'puppet' of another legal person.

[100] *Chicago, Milwaukee & St Paul Rly Co v Minneapolis Civic and Commerce Association* 247 US 490, 38 S Ct 553 (1918) 493-4, 554; TL Alborn *Conceiving Companies: Joint-Stock Politics in Victorian England* (Rouledge London 1998) 62, 1885.

[101] *Burnet v Clark* 287 US 410, 53 S Ct 207 (1932) 415, 208.

[102] US: *Lowell Staats Mining Co Inc v Pioneer Uravan Inc* 878 F 2d 1259 (10th cir 1989) at 1262-3; *US v Jon-T Chems Inc* 768 F 2d 686 (5th cir 1985) at 691-2; *Nelson v International Paint Co Inc* 734 F 2d 1084 (5th cir 1984) at 1093; *Miles v American Tel* 703 F 2d 193 (5th cir 1983) at 195-6; *DeWitt Truck Brokers Inc v W Ray Flemming Fruit Co* 540 F 2d 681 (4th cir 1976) at 685-7l; *Steven v Roscoe Turner Aeronautical Corp* 324 F 2d 157 (7th cir 1963) at 161; *Panamerica Mineral Servs Inc v KLS Enviro Resources Inc* 916 P 2d 986 (Wyo 1996) at 990; *Zaist v Olson* 154 Conn 563, 277 A 2d 552 (1967); UK: *Adams v Cape Industries Plc* [1990] 1 Ch 433 (CA) 530-1. For an alternate description of the catalogue, see WO Douglas and CM Shanks 'Insulation from Liability Through Subsidiary Corporations' (1929) 39 Yale L J 193, 196-7;

Even though precedent's determination of the facts of a case is not binding, the common law courts nonetheless rely on a uniform, but unreasoned, catalogue to make consistent their answers to a question that concerns legal concepts.

There are two problems with the approach of the courts. First, the courts confuse a relationship of agency with a non-relationship of alter-ego.[103] A non-relationship of alter-ego justifies the piercing of the veil, and the attribution to the shareholder of the corporation's personal *liabilities*. In contrast, a relationship of agency justifies only the characterization of the actor as the principal's agent and the attribution to the principal of the agent's *actions*.

The second problem is that these conclusory labels and the assorted catalogue of factors do not identify a reason as to why any particular factor, or any particular relationship between a corporation and its shareholders, justifies the law treating the corporation's personal liabilities as the shareholder's personal liabilities.[104] The courts do not identify a reason for piercing the veil, but merely reach, in each case, one of two conclusions: first, 'a normative

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Note 'Piercing the Corporate Veil: The Alter Ego Doctrine Under Federal Common Law' (1982) 95 Harvard L Rev 853, 854; PI Blumberg 'The Transformation of Modern Corporation Law: The Law of Corporate Groups' (2005) 37 Connecticut L Rev 605, 612; JM Landers 'A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy' (1975) 42 U Chicago L Rev 589, 598.

[103] Eg, *Platt v Bradner* (1924) 131 Wash 573, 230 Pac 633; *Oriental Inv Co v Barclay* (1901) 25 Tex Civ App 543, 64 S W 80; *Re Muncie Pulp Co* (1905) 139 Fed 546, 71 CCA 530; *Mobil Oil Corp v Linear Films Inc* 718 F Supp 260 (1989 D Del) at 271; *Brewarrana v Commissioner of Highways* (1973) 4 SASR 476 at 480; *Wallersteinr v Moir* [1974] 1 WLR 991 (CA) at 1013: 'I am quite clear that they were just the puppets of Dr Wallersteiner. … He was the principal behind them.' RW Hamilton 'The Corporate Entity' (1971) 49 Texas L Rev 979 at 983.

[104] WO Douglas and CM Shanks 'Insulation from Liability Through Subsidiary Corporations' (1929) 39 Yale L J 193 at 195; RW Hamilton 'The Corporate Entity' (1971) 49 Texas L Rev 979 at 979, 981; WJ Rands 'Domination of a Subsidiary by a Parent' (1998) 32 Indiana L Rev 421 at 422; WP Hackney and TG Benson 'Shareholder Liability for Inadequate Capital' (1981) 43 U Pittsburgh L Rev 837 at 845-5.

conclusion that piercing is or is not appropriate',[105] or secondly, a tautologous conclusion that the circumstances in which the courts pierce the veil 'vary according to the circumstances in each case.'[106]

The result is that the boundaries to the corporation's legal personality are arbitrarily drawn. Empirical studies reveal that the US courts decide 'hundreds, if not thousands, of irreconcilable cases in each year',[107] while a study in 2004 showed that 'Republican appointees accept … claims [to pierce the corporate veil] at a significantly lower rate than Democratic appointees: 27% as opposed to 41%.'[108] An empirical study of the UK courts' decisions discloses that the courts are almost four times as likely to pierce the veil when the party requesting the piercing is the government as when the party is an employee of the corporation.[109] Perplexingly, the Industrial Tribunal and Employment Appeal Tribunal are more than twice as likely to pierce the veil as the Land, VAT, Transport and Trademarks Tribunals.[110] In sum, the area of law 'smacks of palm-tree justice'.[111]

Some corporate lawyers suggest that corporate law will never understand, or set, the boundaries to the corporation's personality. For

[105] JM Landers 'A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy' (1975) 42 U Chicago L Rev 589 at 620.
[106] *Automotriz del Golfo de California SA de CV v Resnick* 47 Cal 2d 792, 306 P 2d 1 (1957) at 796, 4.
[107] PI Blumberg 'The Transformation of Modern Corporation Law: The Law of Corporate Groups' (2005) 37 Connecticut L Rev 605 at 611-2; RB Thompson 'Piercing the Corporate Veil: An Empirical Study' (1991) 76 Cornell L Rev 1036 at 1037. Empirical studies of Australian caselaw report the same absence of judicial consensus: IM Ramsay 'Allocating Liability in Corporate Groups: An Australian Perspective' (1999) 13 Connecticut J International L 329 at 345.
[108] CR Sunstein, D Schkade and LM Ellman 'Ideological Voting on Federal Courts of Appeals: A Preliminary Investigation' (2004) 90 Virginina L Rev 301, 321.
[109] C Mitchell 'Lifting the Corporate Veil in the English Courts: An Empirical Study' (1999) 3 Company Financial and Insolvency Law Review 15 at 25.
[110] Mitchell (note 109).
[111] LCB Gower and others *Gower's Principles of Modern Company Law*, (Stevens & Sons London 1979 4th ed) at 138.

example, Davies reasons that:[112]

> Much effort has been expended by corporation lawyers in trying to explain these instances [in which the separate legal personality of the corporation should be ignored]. It is suggested that no single explanation for these cases will be found and that in any event corporation lawyers are not well equipped to provide the explanation or explanations.

While securities regulation protects the integrity of the investment markets by opting to run its own race, and conceive of the corporation as an entity that generates its own profit stream, the veil-piercing jurisprudence fell out of the race. The caselaw abandoned the search for a concept of the corporation that will enable courts to delineate the boundaries of corporate personality by reference to principle; and not a catalogue of indeterminate factors.

It is argued that the courts are unable to identify a principle by which the courts may sensibly pierce the corporate veil because the courts no longer conceive of the corporation as an entity that is operated to generate its own profit stream. Under the classical concept of the corporation, an 'alter-ego' may sensibly be defined as a corporation that acts, not to generate a profit for itself, but *only* to generate a profit for another legal person. Thus, Corporation A controls Corporation B if (and only if) B does not act in B's own interests, and in an attempt to generate a profit stream for B, but acts *only* to further the interests of A, and to generate a profit for A.

In this way, the act of an alter-ego – which justifies the piercing of the veil – differs from the act of an agent – which justifies only the characterization of the actor as the principal's agent. The agent acts in the interests of another

[112] PL Davies *Introduction to Corporation Law* (Oxford University Press Oxford 2002) at 37-8.

person in order to act in its own interests. In contrast, the alter-ego acts in the interests of another person without concern for whether (and without the intention of ensuring that) the act furthers her own interests, and its own independent business. Thus, as a result of the judicial reform, which abandoned the classical concept of the corporation as an entity that is operated to make itself a profit, modern corporate law lost sight of the only principle by which the boundaries of legal personality are sensibly delineated.

B A Corporation May be Operated to Fence-off Liabilities

Upon its abandonment of the classical concept of the corporation, modern corporate law lacked the tools by which to define the boundaries of the corporation's legal personality. While securities regulation retained the classical concept of the corporation in order to protect the integrity of the securities' markets, the courts persevered with an agenda of judicial reform.

(i) Classical concept of limited liability

Limited liability is the principle that separates the assets and liabilities of the corporation from the assets and liabilities of its shareholders. The principle thereby precludes, for example, a shareholder claiming that the assets of the corporation are his own assets.[113] The principle also precludes the corporation's creditors from taking recourse against the assets of the corporation's

[113] Eg, *Macaura v Northern Assurance Co Ltd* [1925] AC 619 (PC).

shareholders.[114] Under the classical concept of the corporation, the courts held that:[115]

> a corporation may be organized for the very purpose of avoiding personal liability provided the corporation really exists and *is doing business* as permitted by law.

However, as the modern courts abandoned the principle that a corporation is a legal person that operates to generate for itself a profit stream, the courts also modified their understanding of the concept of limited liability.

(ii) Modern concept of limited liability

Under the classical concept of the corporation, the courts held that shareholders may incorporate a business for no reason other than to ensure that the shareholders obtain the protection of limited liability. The courts considered it inappropriate to pierce the corporate veil of a corporation that, like Salomon & Co, operated its own business simply because the incorporators were desirous of limiting their own liability.

Under the modern concept, the US and UK courts consider it inappropriate to pierce the corporate veil of a corporation that, unlike Salomon & Co, was never intended to operate to make itself a profit. The courts are

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[114] See Ulpian's maxim: 'Si quid univeritate debetur singuli non debetur; nec quod debet universitas singule debent', which Blumberg translates as 'Where anything is owing to a corporation, it is not due to the individual members of the same, nor do the latter owe what the entire association does.' PI Blumberg 'The Transformation of Modern Corporation Law: The Law of Corporate Groups' (2005) 37 Connecticut L Rev 605 at 578; see also note 11.

[115] *Trenga Realty v Tiseo* 117 AD 2d 951, 499 NYS 2d 262 (1896, SC NY) at 951, 264 (emphasis added); see also *Bartle v Homeowners Coop Inc* 309 NY 103, 127 NE2d 832 (1955) at 833: 'The law permits the incorporation *of a business* for the very purpose of escaping personal liability'; *Texas Indus Inc v Dupuy & Dupuy Dev Inc* 227 So 2d 265 (La App 1969) at 269: 'The general rule is that an individual may incorporate *his business* for the sole purpose of escaping individual liability for the corporate debts.' 1A Fletcher Cyc Corp, §93.

currently prone to reason that 'a corporation may be organized for the very purpose of avoiding personal liability'[116] regardless of whether the corporation also conducts any business for itself.[117] For example, in *Anderson v Abbott*,[118] the US Supreme Court reasoned in the following way:[119]

> Normally the corporation is an insulator from liability on claims of creditors. The fact that incorporation was desired in order to obtain limited liability does not defeat that purpose. Elenkrieg v. Siebrecht, 238 N.Y. 254, 144 N.E. 519… .

This observation is at discord with the House of Lords' decision in *Salomon v Salomon & Co*,[120] for the following reason. In the *Salomon* case, the Lords decided that the veil ought not to be pierced when '[t]he very object of the creation of the corporation … [was to ensure that] the liability of the members for the debts incurred by the corporation shall be limited.'[121] Yet, the Lords reached this decision with respect to a corporation that had a business to conduct for itself.

In contrast, while the Supreme Court, like the House of Lords, noted that shareholders may make use of the corporate device in order to limit their liability, the Court did not also note the condition that the incorporated entity that insulates liability also be an incorporated business. The Court's reform of the classical concept of limited liability, which insisted that the corporate device resemble Salomon & Co, was unarticulated. It is noteworthy that the *Elenkrieg* case,[122] to which the Court referred, is no precedent for the Court's modern

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[116] *Trenga Realty v Tiseo* 117 AD 2d 951, 499 NYS 2d 262 (1896, SC NY) at 951, 264 (emphasis added).
[117] Eg, *Zubik v Zubik* 384 F 2d 267 (3d cir 1967) cert denied 390 US 988, 88 S Ct 1183 (1968) at 273.
[118] 321 US 349, 64 S Ct 531 (1944).
[119] *Anderson v Abbott* 321 US 349, 64 S Ct 531 (1944) at 361-2, 537-8.
[120] [1897] AC 22 (HL).
[121] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 44.
[122] 238 NY 254, 144 NE 519 (1924 CA NY).

concept of limited liability. In the *Elenkrieg* case, the court articulated the classical concept of limited liability:[123]

> Many a man incorporates his business or his property and is the dominant and controlling feature of the corporation. He may do so for the very purpose of escaping personal liability, and he may do so as a cover if in fact the corporation really exists – is doing business as permitted by the laws of this state or the state of its incorporation; in other words, is a person recognized by the law.

The modern concept, unlike the House of Lords' in the *Salomon* case, envisages that a corporation need not be an incorporated business, but may simply be an incorporated bundle of assets or liabilities.[124] For example, in a number of cases, the US courts reason that the law not only 'allows businesses to incorporate to limit liability', but also allows businesses to 'isolate liabilities among separate entities'.[125] Across the Atlantic,[126] and in the case of *Adams v Cape Industries plc*,[127] the Court of Appeal similarly reasoned that the formation of a corporation for the purpose of shifting an incorporator's future liabilities 'onto another member of the group'[128] is not 'an unlawful purpose',[129] which

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[123] *Elenkrieg v Siebrecht* 238 NY 254, 144 NE 519 at 261-2, 521.

[124] Eg, Hayek argued that 'it is necessary in the interest of the efficient use of resources that the corporation be regarded primarily as an aggregate of material assets.' FA Hayek 'The Corporation in a Democratic Society: in Whose Interest Ought It and Will It Be Run?' in MB Anshen and L George (eds) *Management and Corporations 1985* (New York McGraw-Hill Book Company Inc 1960) at 103.

[125] *Florez v Holly Corp* 154 Fed Appx 707 (2005 10th cir) at 708; *Frank v US West Inc* 3 F 3d 1357 (10th Cir 1993) at 1362; *Glover v Heart of America Management Co* 38 F Supp 2d 881 (1999 D Kan) at 890; *Dunn v Tutera Group* 181 FRD 653 (1998 D Kan) at 659; *Burnet v Intercon Security Ltd* 1998 US Dist LEXIS 3648 (1998 D Ill) 11; *Walker v Toolpushers Supply Co* 955 F Supp 1377 (1997 D Wyo) 1381; *Catanzaro v Suprevalu* 1994 US Dist LEXIS 19991 (1994 D Miss) at 9; *Jemez Agency Inc v Cigna Corp* 866 F Supp 1340 (1994 D New Mex) at 1343; *Gilmore v List & Clark Constrution Co* 862 F Supp 294 (1994 D Kan) at 298; *Cascade Energy and Metals Corp v Banks* 896 F 2d 1557 (1990 10th cir); *Yoder v Honeywell Inc* 104 F 3d 1215 (1997 10th cir) at 1220; *Boughton v Cotter Corp* 65 F 3d 823 (1995 10th cir) at 836; *Skidmore v Canada Life Assurance Co* 907 F 2d 1026 (1990 10th cir) at 1027.

[126] And also across the Pacific: *Donnelly v Edelston* (1994) 13 ACSR 196 at 205.

[127] [1990] 1 Ch 433.

[128] *Adams v Cape Industries Plc* [1990] 1 Ch 433 (CA) at 544.

[129] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 56.

justifies a piercing of the corporate veil. In so amending their concept of the corporation, the US and UK courts also radically reformed their concept of the corporate group, and the principles of separate legal personality and limited liability.

(a) The modern corporation in a corporate group

Under the modern concept of the corporation, each corporation in the corporate group is no more than a duly registered and incorporated entity. A corporation is not necessarily a discrete profit-making entity. Separate legal personality, in this corporate group context, means that the shareholders' assets and liabilities – but not their businesses – are separate from the assets and liabilities of the corporation. For example, in *Adams v Cape Industries Plc*, '[e]ach corporate member of the Cape group had its own well-defined commercial function designed to serve the over-all commercial purpose of mining and marketing asbestos.'[130] More than one corporation may be engaged in a single profit-making enterprise, which aims to make a profit for only one corporation.

Limited liability, under the modern concept, means that the companies in a corporate group may choose 'to ensure that the legal liability … in respect of particular future activities of the group … will fall on another member of the group'.[131] To take advantage of limited liability, a parent corporation may turn another member of the group into 'the runt of the litter'.[132] A corporation in a corporate group may exist simply to house the liabilities of other members of

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[130] *Adams v Cape Industries Plc* [1990] 1 Ch 433 (CA) at 482-3.
[131] *Adams v Cape Industries Plc* [1990] 1 Ch 433 (CA) at 544. See also *Harrods Ltd v Dow Jones & Co Inc* [2003] EWHC 1162, [2003] All ER (D) 327 (May) (QB) at [25]; *Cannon Manufacturing Co v Cudahy Packing Co* 267 US 333, 45 S Ct 250 (1925) at 335, 251; *Zubik v Zubik* 384 F 2d 267 (3rd Cir 1967), cert denied 390 US 988 (1968) at 273.
[132] *Re Southard & Co Ltd* [1979] 1 WLR 1198 (CA) at 1208.

the group.

For example, in *Ord v Belhaven Pubs Ltd*,[133] the plaintiffs sued the defendant corporation for damage that they allegedly sustained as a result of the defendant's negligent misrepresentations, and which arose out of the plaintiff's purchase of a lease in 1989. In 1992, the assets and liabilities of the defendant corporation, which was a member of a corporate group, were shifted among other members of the group 'as part of what appears to be a normal attempt to rationalize the group's operating structure'.[134] Upon a review of the group accounts, an accountant gave evidence that:[135]

> [t]here is … every indication that the group treated its subsidiary companies as though they were divisions of one large corporation rather than as individual legal entities.

A result of the group's restructuring, 'instead of having a surplus of assets over liabilities, the [defendant corporation's] position had been reversed',[136] so that the defendant corporation no longer had any assets out of which a judgment-debt could be satisfied.[137] Nonetheless, the Court of Appeal refused to pierce the corporate veil of the defendant corporation on the ground that:[138]

> [i]t was just the ordinary trading of a group of companies under circumstances where, as was said in *Adams v Cape Industries plc* [1990] BCLC 479 at 520, [1990] Ch 433 at 544, the corporation is in law entitled to organise the group's affairs in the manner that it does, and to expect that the court should apply the principles of *Salomon v A Salomon & Co Ltd* in the ordinary way.

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133 [1998] 2 BCLC 447 (CA).
134 *Ord v Belhaven Pubs Ltd* [1998] 2 BCLC 447 at 451.
135 *Ord v Belhaven Pubs Ltd* [1998] 2 BCLC 447 at 452.
136 *Ord v Belhaven Pubs Ltd* [1998] 2 BCLC 447 at 453.
137 *Ord v Belhaven Pubs Ltd* [1998] 2 BCLC 447 at 450.
138 *Ord v Belhaven Pubs Ltd* [1998] 2 BCLC 447 at 458.

In the *Adams* case, the Court of Appeal reasoned that '[w]hether or not this is desirable, the right to use a corporate structure in this manner is inherent in our corporate law.'[139]

The Court of Appeal, like the US Supreme Court, did not note the ways in which 'the right to use a corporate structure in this manner' – ie, to use an incorporated legal person as if it was an unincorporated trust that existed to be of benefit only to shareholders – was once incompatible with corporate law. Nor did the Courts note the ways in which 'the right to use a corporate structure in this manner' conceived of the corporation as an entity that exists only to be of benefit to its shareholders and not to be of benefit to itself; ie, conceived of the company as a trust. In articulating a modern concept of the corporation, the US and UK courts failed to articulate the nature of the change in judicial expectations as to the way in which companies conduct business within a corporate group.

(b) The classical corporation in a corporate group

Under the classical concept, each corporation in the corporate group was a discrete profit-making centre. Separate legal personality, in the corporate group context, meant that the shareholders' assets and liabilities – but also their businesses – were separated from the assets, liabilities and business of the corporation. In *Gas Lighting Improvement Co Ltd v IRC*,[140] Lord Sumner made clear that:[141]

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[139] *Adams v Cape Industries Plc* [1990] 1 Ch 433 (CA) at 544.
[140] [1923] AC 723 (HL).
[141] *Gas Lighting Improvement Co Ltd v IRC* [1923] 1 AC 723 (HL) at 741.

> [b]etween the investor, who participates as a shareholder, and the undertaking carried on, the law interposes another person, real though artificial, the corporation itself, and the business carried on is the business of that corporation, and the capital employed is its capital and not in either case the business or the capital of the shareholders.

Limited liability, in the corporate group context, meant that:[142]

> [i]f one of the subsidiary companies … turns out to be the runt of the litter and declines into insolvency to the dismay of its creditors, the parent corporation and the other subsidiary companies may prosper to the joy of the shareholders without any liability for the debts of the insolvent subsidiary.

Limited liability did not mean that a parent corporation, or other subsidiary companies, may shift assets or liabilities onto a subsidiary corporation. A corporation could shift its assets and liabilities onto another member of the group only if the corporation also transferred its business to the other corporation. This is for two reasons. First, the parent corporation had no power to use the ownership of stock in the subsidiary to control the subsidiary's business operations and to prevent the subsidiary from operating its own business. Secondly, other subsidiary companies had no power to employ their assets or liabilities in order to operate another corporation's business. Thus, the operating corporation of a corporate group had no power to control the activities of a liability-holding corporation, and to shift liabilities onto it, unless the liability-holding corporation accepted the transfer of liabilities in furtherance of its own profit-making operations. And, the asset-holding corporation of a corporate group had no power to use its assets simply in order to further the profit-making activities of another corporation.

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142 *Re Southard & Co Ltd* [1979] 1 WLR 1198 (CA) at 1208.

This part of the paper has argued that the decision of the Court of Appeal in the *Adams* case, and the decision of the US Supreme Court in *Anderson v Abbott*, were not decisions that merely applied a pre-existing body of corporate law doctrine. They were decisions that reformed the principles of separate legal personality and limited liability. Under the classical concept, the corporation was an entity that aimed to make itself a profit. Under the classical concept of limited liability, a shareholder was empowered to fence off his personal assets from the claims of the corporation's creditors. However, the creditor was entitled to have her debts paid out of the corporation's profit stream. The creditors were guaranteed that, even if the entity was incorporated simply so as to enable the shareholder to build a fence around her assets, the entity nonetheless was striving to generate an income out of which debts could be paid.

Under the first reform of the classical concept, the corporation is no longer an entity that necessarily aims to make a profit for its shareholders. And under the second reform of the classical concept, the corporation may be an entity that aims to do nothing but fence-off the liabilities of its shareholders. The modern concept of limited liability empowers the shareholder to move the fence and avoid liability. As the courts will not pierce the corporate veil whenever a corporation exists simply so as to limit the liabilities, not of the corporation's *business* but of the corporation's *shareholders*, the shareholder may ensure that no creditor gains access even to the corporation's profit stream. As the courts no longer expect a corporation to generate its own profit stream, shareholders may ensure, first, that no corporation in a corporate group that generates a profit holds any assets, and secondly, that no corporation that holds

any assets generates a profit stream. In this circumstance, the shareholder risks none of its assets. Its liability is not limited; it is avoided.

This part of the paper tested the utility of the modern concept of the corporation as a doctrine of corporate law. The next part of the paper argues that corporate law should restore the classical conception of the corporation. The part argues that the law fails to understand what it means for a corporation to be a legal person until it remembers the classical conception of the corporation and expects each corporation to make itself a profit. The part then outlines the way in which the rules concerning the piercing of the veil should be reformed and the way in which the classical concept may be restored.

2 THE LEGAL PERSONALITY OF THE CORPORATION

Must the corporation aim to make itself a profit? Must a legal person treat itself as a thing of ultimate value or may it exist simply to be of instrumental value to other legal persons by, for example, fencing off their liabilities? What does it mean for the law to personify some thing? To investigate these questions, this paper asks a more fundamental set of questions: to which kinds of things does the concept of personality sensibly apply? Why do we personify companies and States but not plants or animals? And, most relevantly, why does the law personify the corporation but not the trust? To answer these questions, this part of the paper constructs a concept of the person that applies, in different ways, to human beings and non-human things.

A The Things of which the Concept of the Artificial Person is a Concept

'Person' is not synonymous with 'human'. While the human is a being, the

person is, as Locke describes, 'a forensic term'.[143] As a word, 'person' has more aspects than 'human', because it is used to refer to more beings. We use it to refer to ourselves and our humanity. Yeats described that which 'makes a person be thinking of the four last ends, death and judgment, heaven and hell.'[144] The other kinds of 'person' are varied. Hobbes identified the 'fictional person', and noted that:[145]

> as *persona* in Latin signifies the *disguise* or *outward appearance* of a man, counterfeited on the stage … a *person* is the same that an *actor* is, both on the stage and in common conversation; … and he that acteth another is said to bear his person… .

Hobbes noted that it is not only 'people of flesh and blood' who are personified:[146]

> There are few things that are incapable of being represented by fiction. Inanimate things (as a church, an hospital, a bridge) may be personated by a rector, master, or overseer.

Hobbes was prepared to personify 'a temple, a bridge, or … anything whatsoever that needs money for its upkeep.'[147]

The persona of the fictional character is a creation of human imagination. Harold Pinter explains that:[148]

> [i]t's a strange moment, the moment of creating characters who up to that moment have had no existence. … The author's

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143 J Locke *An Essay Concerning Human Understanding* (5th Fontana Library London 1964) Ch XXVII at 220.
144 WB Yeats and L Gregory *The Unicorn from the Stars* (Macmillan Co New York 1908) Act III, 100.
145 T Hobbes *Leviathan* (Hackett Indianapolis 1994) Ch XVI at [3].
146 Hobbes (n 145) Ch XVI at [9].
147 T Hobbes and CT Wood, TSK Scott-Craig and B Gert (tr) *Man and Citizen* (Humanities Press New York 1972) Ch XV at [4].
148 H Pinter 'Art, Truth & Politics' (Nobel Lecture 7 December 2005).

> position is an odd one. In a sense he is not welcomed by the characters. The characters resist him, they are not easy to live with, they are impossible to define. You certainly can't dictate to them. To a certain extent you play a never-ending game with them, cat and mouse, blind man's bluff, hide and seek. But finally you find that you have people of flesh and blood on your hands, people with will and an individual sensibility of their own, made out of component parts you are unable to change, manipulate or distort.

Then, there is the 'spirit person', who is composed of neither flesh and blood, nor things inanimate. Virginia Woolf's imagination personified a woman's experience as the 'Angel in the House':[149]

> You who come of a younger and happier generation may not have heard of her – you may not know what I mean by the Angel in the House. … She excelled in the difficult arts of family life. She sacrificed herself daily. If there was chicken, she took the leg; if there was a draught she sat in it – in short she was so constituted that she never had a mind or a wish of her own, but preferred to sympathize always with the minds and wishes of others.

Perplexingly, the persona of the spirit, like the fictional person, is not only a product of, but is also distinct from, the human who imagines her. Woolf 'turned upon' her Angel, and 'caught her by the throat', because: 'Had I not killed her she would have killed me. She would have plucked the heart out of my writing.'[150]

One 'of the most noteworthy feats of the legal imagination' is that the law extends 'for good and sufficient reasons … the conception of personality

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[149] V Woolf 'Professions for Women' in (eds) *The Death of the Moth and Other Essays* (Penguin Books Middlesex 1961) at 202.
[150] Woolf (note 149) at 203.

beyond the class of human beings'[151] and distinct legal persons. The law personifies, *inter alia*, the government, the military and the (almost oxymoronic) 'corporate person'. In incorporating a corporation, the relevant statutes create an 'artificial person'[152] and the law has its own 'strange moment … of creating characters'.[153]

What does it mean to be a distinct and independent person? The name of 'person' is attached to an almost infinite variety of non-human things. Is there any one concept that explains the sense in which the character of a person is attributed to the human being, the acted part, Pinter's people, Hobbes' hospital, Woolf's Angel and the law's corporation?

B Not an Analogy from the Human Person

To identify the non-human things that we sensibly personify, it is not enough to apply by way of analogy a concept of the human person. Many concepts of the person aim to identify the distinctive properties of the human being.[154] For example, Strawson explained that:[155]

> [w]hat I mean by the concept of a person is the concept of a type of entity such that *both* predicates ascribing states of consciousness *and* predicates ascribing corporeal characteristics, a physical situation & c are equally applicable to a single individual of that single type.

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[151] PJ Fitzgerald *Salmond on Jurisprudence* (12th edn Sweet & Maxwell London 1966) at 305.
[152] *Colonial Building and Investment Association v AG of Quebec* (1883) 9 App Cas 157 (PC) at 166; see also *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 30.
[153] Pinter (note 148).
[154] Eg, AJ Ayer 'The Concept of a Person' in (eds) *The Concept of a Person* (Macmillan Press London 1963); HG Frankfurt 'Freedom of the Will and the Concept of a Person' (1971) 68 J of Philosophy 5 at 6-7; DC Dennett 'Conditions of Personhood' in (eds) *Brainstorms: Philosophical Essays on Mind and Psychology* (Harvester Press Sussex 1981).
[155] PF Strawson 'Persons' in (eds) *Individuals: An Essay in Descriptive Metaphysics* (University Paperbacks London 1959) at 101-2.

The focus on the distinctive properties of the human person is meant to explain why it is that humans are a unique species and are thereby distinguishable from, for example, animals and robots.

It is a mistake, however, to take these peculiarly human characteristics to be 'the relevant base for the classification of persons' generally, and the relevant criterion that adjudges 'whether corporations, Venusians, mongolian idiots, and fetuses are persons'.[156] Even if the human person is sensibly taken to be the focal case of the person, there is no reason why the characteristics that are peculiar to human persons are the characteristics on which an analogy from the focal human person to the artificial person is sensibly based. The human's corporeal characteristics do not extend, by way of analogy, to corporeal things like a hospital, nor to incorporeal things, like the State and the corporation. The concept of the person must not only select a feature of the human person that is uniquely human, but must also explain why it is that that characteristic makes her the focal case of the person and makes non-human things, like the corporation, a non-focal case of person.

C Not a Concept of the Fictional Person

The concept of the non-human, artificial person is distinguishable from the concept of the fictional person. The fictional person is only one type of artificial person. It is the personified thing from another world. The author of a character (or the author's audience) treats the character as a person who acts in the world of fact, even though the character acts only in the world of fiction.

[156] AO Rorty 'A Literary Postscript: Characters, Persons, Selves, Individuals' in AO Rorty (eds) *The Identities of Persons* (University of California Press Berkeley 1976) at 322; see also PA French 'The Corporation as Moral Person' (1979) 16 American Philosophical Quarterly 207.

For example, Pinter treats his characters as if they are beings who act autonomously in the same world that he does:[157]

> In the play that became *The Homecoming* I saw a man enter a stark room and ask his question of a younger man sitting on an ugly sofa reading a racing paper. I somehow suspected that A was a father and that B was his son, but I had no proof. This was however confirmed a short time later when B (later to become Lenny) says to A (later to become Max), 'Dad, do you mind if I change the subject?...'

The things that belong to this world of fact, albeit incorporeally, are not beings that are treated as persons in the same fictitious sense.[158] When we personify corporations or other artificial persons of the incorporeal kind, we treat the corporation, hospital or other incorporeal thing as a person who has a corporeal body that is capable of action, even though it does not. The proposition that the fictional thing is a person is fictitious in a different way from the proposition that the incorporeal thing is a person. However, both the fictional and incorporeal persons are varieties of the same concept of the artificial person. As the rest of this paper argues, this is because we natural persons, as author, audience or thinker, reach the conclusion that the character and the incorporeal are persons for the same fictitious reason; ie, for the reason that the things are beings of ultimate value.

D A Concept that Contains a Fiction

A concept of the person is a concept of a being that is of ultimate value. The natural, human person is the being whose existence is value in and of itself. The value of the human's being does not derive from her contribution to the well-

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[157] Pinter (n 148).
[158] Eg, HLA Hart 'Definition and Theory in Jurisprudence' in (eds) *Essays in Jurisprudence and Philosophy* (Clarendon Press Oxford 1983) at 58.

being of any other thing, but is accepted without justification, or simply upon reflection.[159]

(i) The other-worldly artificial person

In contrast, the things that we personify as artificial persons are not things whose existence is of ultimate value. The existence of the fictional character or a spirit person is not ultimately valuable because neither of their value is non-derivative on the value of something else; namely, the value that the artificial person contributes to the human person who reads the book or believes in a spirit. And the value of the hospital or the corporation is not ultimately valuable because their value is merely instrumental. 'Corporations, as artifacts, are not ends in themselves.'[160] Nonetheless, a concept of the person that contains a fiction is a concept of the things that we treat as if it is of ultimate value.

The concept of the artificial person is a rational fiction, and not an imaginative or intuitive flight of a philosopher's fancy, if there is a reason for which we imaginatively treat non-human things as beings of ultimate value. We natural persons personify a thing as an artificial person for the reason that the thing's personification as a person, and as an end, is a means to the end of human well-being. That is, we make a decision to treat a thing as a person for the reason that this treatment of the thing as an end enables the thing to be intrinsically valuable, or used as an instrument, to our own ends. This concept of the artificial person is a concept of the things:

(i) whose existence is not of ultimate value;

[159] Eg, CM Korsgaard 'The Authority of Reflection' in *The Sources of Normativity* (Cambridge University Press Cambridge 1996) at 91; *Airedale NHS Trust v Bland* [1993] AC 789 (HL) at 826.
[160] RT De George 'Collective and Corporate Responsibility' (1987) 21 Noûs 448 at 449-50.

(ii) who are fictitiously treated as beings whose existence is of ultimate value; and

(iii) who are fictitiously treated as beings whose existence is of ultimate value so that the thing may be of intrinsic or instrumental value to human persons.

The artificial persons that act in another world are generally personified so as to be of intrinsic value to the human person. Other-worldly persons are intrinsically valuable to world-of-fact human persons, for the reason that '[t]he other world is this world too'.[161] A reader's interactions with a fictional character, and a believer's interactions with a spirit person, contribute to the well-being of a human's life. Cervantes explained that Don Quixote was of intrinsic value: 'For me alone Don Quixote was born and I for him.'[162] Other-worldly persons may also be of instrumental value. In *Time Regained*, Proust's narrator explains how it is that the personification of a fictional character is instrumentally valuable:[163]

> my book being merely a sort of magnifying glass like those which the optician at Combray used to offer his customers – it would be my book, but with its help I would furnish them with the means of reading what lay inside themselves.

(ii) The world-of-fact artificial person

The artificial persons that act in this world through the corporeal bodies of human persons are generally personified so as to be only of instrumental value,

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[161] T Tranströmer and R Fulton (tr) 'How the Late Autumn Night Novel Begins' in *New Collected Poems* (Bloodaxe Newcastle upon Tyne 1997) at 119.
[162] M de Cervantes Saavedra and JM Cohen (tr) *The Adventures of Don Quixote* (Penguin Books Hardmonsworth 1950) vol 2, Ch LXXIV at 940.
[163] M Proust and A Major and T Kilmartin (tr) 'Time Regained' in *In Search of Lost Time* (Everyman's Library London 2001) vol 4 at 606-7.

and not intrinsic value, to the human person. For example, inanimate things are personified so that their maintenance may be procured and so that they may be of consequential value to those attending a service in a church, being treated in a hospital or crossing a bridge.

(a) A bearer of rights

A basic way in which we treat the inanimate or incorporeal things of this world as beings that are of ultimate value is to treat the thing as an entity that is capable of bearing rights. Raz explains that:[164]

> [a]n individual is capable of having rights if and only if either his well-being is of ultimate value or he is an 'artificial person' (e.g. a corporation).

Raz explains why it is that an individual whose well-being is of ultimate value is an individual who 'is capable of having rights'.[165] To have a right is to have an 'aspect of … well-being' that grounds and defines that right. An aspect of the person's well-being is a reason, in and of itself, for holding others to be under a duty. This aspect of a person's well-being is 'the interest which figures essentially in the justification of the statement that the right exists' and the interest on which the 'right is based'.[166] This is because, 'to the extent that there are no conflicting considerations of greater weight',[167] rights:[168]

> are the grounds of duties in the sense that one way of justifying holding a person to be subject to a duty is that this serves the interest on which another's right is based.

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[164] J Raz *The Morality of Freedom* (Clarendon Press Oxford 1986) 166.
[165] Raz (n 164) 166.
[166] Raz (n 164) 169.
[167] Raz (n 164) 172.
[168] Raz (n 164) 183.

Thus, it is because the human is a person whose 'well-being is of ultimate value'[169] that the human is the focal case of the person whose well-being is a sufficient reason to impose duties on others and who is capable of holding a right.

However, things other than the human are capable of having rights. We understand States and corporations to be right-holders. Raz is less fulsome in his explanation of the reasons for which an artificial person is capable of possessing rights. He does note that:[170]

> [w]hatever explains and accounts for the existence of such persons, who can act, be subject to duties, etc. also accounts for their capacity to have rights. Whether certain groups, such as families or nations, are artificial or natural persons is important for determining the conditions under which they may have rights.

It is not enough – in order sensibly to conceive of a thing as a person – that the artificial person be a thing of such value to humans that we ought (ie, have a reason) to promote their well-being. This is because we natural persons may owe duties to promote the well-being of a thing without that thing having any right to have its well-being promoted. In this case, the duty is owed to someone other than the thing who is the subject of the duty. Raz gives an example:[171]

> I have a duty to water certain plants because I promised their owners to look after them while they are away on holiday. My gardener has a duty to look after my garden because his contract of employment says so. … In all these cases the people who have duties to act in certain ways have them because it benefits plants. Yet in none of them is it true that the plants have a right to the benefits. The reason is that in all these cases the benefit is to be

[169] Raz (n 164) 166.
[170] Raz (n 164) 176.
[171] Raz (n 164) 177.

> conferred on a thing whose existence and prosperity are not of ultimate value.

The trust is like the plant. The trustee has a duty to promote the well-being of a trust (ie, the trust property) without the trust having any right that it be protected; and without the trust being personified.

Artificial persons are not *all* of the things whose well-being natural persons have a duty to protect. Human persons (and other artificial persons) have a duty to protect and promote a non-human thing in two different kinds of circumstances. The first is where the non-human thing – eg, the plant or the trust – is not a person. In this case, the thing's contribution to the human's well-being is a reason to ground a duty on persons to protect the thing. Yet, there is no reason to vest a right in the thing that it be protected. It is enough simply to vest a right in the beneficiaries (ie, the owner of the plant or the beneficiaries of the trust) that the thing's well-being be protected.

The second kind of circumstance in which human persons have a duty to promote a non-human thing is where the non-human thing – eg, the State or the corporation – is personified. In this case, the thing's contribution to the human's well-being is a reason to treat the thing as an entity that is of ultimate value. The thing is treated as an entity whose well-being grounds rights, which vest in the thing, and which are reasons for grounding duties on other persons. Artificial persons are capable of possessing rights that are grounds for imposing duties on other (natural or artificial) persons.

Even if it makes sense to treat an artificial person as a thing that is capable of bearing rights, are all the non-human things that we treat as rights-

bearers necessarily artificial persons? For example, is there a sense in which the law may treat a partnership as a rights-bearer[172] but nonetheless deny the partnership's legal personality?[173]

It is argued that if a thing is treated as a rights-bearer, it is necessarily vested with a degree of personality. This is for the following reason. To treat some thing as an entity that is capable of bearing rights is to assume that the value of the thing to its own self (ie, the presumed ultimate value of the thing), is the reason for which a duty is imposed on another being to protect or promote the thing's well-being. If a duty is imposed on another being to protect the thing's well-being by reason of the value of the thing to another being (other than itself), then the duty is not imposed by reason of the thing's *right* to be protected, but by reason of the value of having the thing protected. When the law treats a partnership as a bearer of its own rights, which are separate from its partner's rights, the law asserts the separate personality of the partnership.[174] This does not mean that all rights-bearers are bearers of all facets of personality. To conceive of a thing as a rights-bearer is only one way in which we imagine the thing to be ultimately valuable. For example, personality entails that the person is capable, not only of bearing rights, but also of bearing responsibility. Nonetheless, to the extent that we treat a thing as a rights-bearer, we uphold, to some degree, the fiction of the thing's personality.

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[172] eg, s302(b) of the Uniform Partnership Act 1997 (National Conference of Commissioners on Uniform State Laws, US) purports to deal 'with the right of the partnership to recover partnership property transferred by a partner without authority'; comment 3, 40.
[173] eg, *Sadler v Whiteman* [1910] 1 KB 868 at 889.
[174] eg, s 101(10) of the Uniform Partnership Act 1997 (National Conference of Commissioners on Uniform State Laws, US) defines '[p]erson' to mean 'an individual, corporation, … partnership … or any other legal or commercial entity.' See also The Law Commission and The Scottish Law Commission *Partnership Law* (2003) at [2.5] 6, [4.7] 32 and [4.29] 37.

If a difference between the things that are artificial persons and the things that are non-persons is that artificial persons are rights-bearers while non-persons are merely the subject of duties but are not capable of bearing rights, the following question arises: why is a hospital or a State – but not a plant – an artificial person, which should be treated as capable of bearing rights? Why does the law personify the corporation, but not the trust? In what circumstances is it of instrumental value to humans to impose duties on persons to protect and promote a thing:

(i) for the reason that the thing is of ultimate value and a bearer of its own rights; and not

(ii) for the simpler reason of the thing's contribution to the human's well-being?

That is, how is the value of a personified thing to be distinguished from the value of a non-personified thing?

(b) Of irreducible value

As this paper has already noted, we natural persons personify inanimate and corporeal things as well as incorporeal and corporate things. The value of an inanimate, corporeal thing is easily observable. The church exists to provide a place of worship, and the bridge is built to enable land or water to be crossed. The value of an incorporeal, corporate body is to pursue the 'common purpose' of a plurality of individual persons. Dicey is oft-cited for his explanation of the nature of corporate personality in terms of the fact (and not the 'pestilential'[175] legal fiction) of the corporate body's 'common purpose':[176]

[175] J Bentham *The Works of Jeremy Bentham* (Tait Edinburgh 1859) vol 1 at 235.

> When a body of twenty or two thousand or two hundred thousand men bind themselves together to act in a particular way for some common purpose, they create a body which by no fiction of law but by the very nature of things, differs from the individuals of whom it is composed.

The question that Dicey left unanswered was: 'why should such a fact be thought to have any bearing at all upon the problem of personality?'[177] Salmond concluded that the fact was irrelevant:[178]

> Ten men do not become in fact one person, because they associate themselves together for one end, any more than two horses become one animal when they draw the same cart.

The difference between a group of persons, whom are sensibly personified as a corporate person, and the horses drawing a cart is that our imaginative conception of a corporate person serves a function and thereby has meaning, but our conception of a two-horsed person does not. We need not conceive of a two-horsed person in order to enable the horses to draw the cart. We need not personify a non-human thing, if:

(i) the thing is of (instrumental or intrinsic) value only to ascertainable individual persons or class(es) of persons; and so

(ii) its value is adequately protected if rights are vested only in those individual persons, or classes of persons, to whom the thing is valuable.

First, the value of a non-personified thing or group of things, like two

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[176] AV Dicey 'The Combination Laws as Illustrating the Relation between Law and Opinion in England During the Nineteenth Century' (1904) 17 Harvard L Rev 511 at 513; see also AW Machen 'Corporate Personality' (1910) 24 Harvard L Rev 347 at 360.
[177] J Dewey 'The Historic Background of Corporate Legal Personality' (1926) 35 Yale L J 655 at 673.
[178] J Salmond *Jurisprudence* (7th edn Sweet & Maxwell Ltd London 1924) at 342.

horses, a plant or a trust, is reducible to – and explicable in terms of – the value that the thing has for individual persons, or a class of persons. For example, the value of the trust is wholly reducible to the value that the trust has for its beneficiaries. A consequence is that, for a trust to be valid and enforceable, the trust's beneficiaries must be ascertainable. While the trustees need not 'have before them, or be able to get, a complete list of all possible objects … the trust is valid if it can be said with certainty that any given individual is or is not a member of the class.'[179]

Secondly, as the thing's value is reducible to individual persons or a class of persons, there is no need to characterize the thing as a rights-bearer, and a person, in order to protect the value of the thing. The law need not conceive of the trust as a person, and vest rights in the trust, in order to enable the trust property to be held on trust and managed profitably for its beneficiaries. It is enough that the law vests a right only in the trust's beneficiaries that the trustee acts in their interests.

Yet, some things must be personified, and characterized as rights-bearers, in order to enable them to be of value and to serve their function. We need to conceive of a thing or a group of persons as a person in order to enable the thing (or the group) to serve its function, if:

(i) the (instrumental or intrinsic) value of the thing is not reducible to the value that the thing has for individual persons, or class(es) of persons; and so

(ii) the value of the thing is not adequately protected if rights are vested only in the individual persons, or classes of persons, whom

[179] *McPhail v Doulton* [1971] AC 424 (HL) at 456.

> the thing benefits, and not in the thing itself. Instead, the value of the thing is protected only if the thing is personified and characterized as a rights-bearer and thus, is vested with the right to have its value protected and promoted.

First, the value of a personified thing, like a hospital, is irreducible to – and not explicable in terms of – the value that the thing has for any one discrete and ultimately valuable person, or any class of such persons. Instead, the thing is valuable for the reason that it enables a classless group of persons to achieve valuable ends. The thing is valuable for a classless group of persons in that it is of value to a range of human persons who are so variable that they cannot be described in terms of any common attribute or set of attributes, and who do not form any discrete class or set of classes. For example, the value of a hospital cannot be explained in terms of the value that the hospital has for any class of persons. The only attribute that is common to the persons who derive value from a hospital – ie, its patients – is the fact that they used, and needed to use, the hospital for its value.[180]

Secondly, to enable a thing to be of instrumental value to a classless group of human persons, the thing must be treated as a being of ultimate value, and a rights-bearer. As the personified thing is of value to a classless group of people, there is no class of persons in whom there is a reason to vest the right to have the thing's value protected. Even if the right to have the thing's value protected was vested in the class of persons who are most likely to benefit

[180] A hospital may exist to serve a particular class of patients. For example, the hospital may admit only those patients who can afford to pay its fees, or who belong to a particular religion. In this circumstance, the hospital limits to a class of persons the persons whom it is prepared to be of use. Yet, the hospital does not qualify the range of persons for whom the hospital is valuable *qua* a hospital, but simply the range of persons who may utilize the hospital's value.

from the protection and promotion of the thing's well-being, the value of the thing would not adequately be protected. For example, the value of a hospital, as a place in which the sick are treated, is not protected if the right to have a hospital maintained is vested, not in the hospital itself, but in the class of persons who are most likely to benefit from the hospital's maintenance; eg, those who suffer from an existing medical condition. In this circumstance, the hospital would not be maintained as a place in which the unexpectedly ill, injured or diseased are able to be treated. Instead, the value of these kinds of things is protected only if the things are personified and characterized as rights-bearer and thus, vested with the right to have their value protected and promoted. Thus, we treat inanimate and incorporeal things as being of ultimate value in this way for the reason of enabling the things to be of instrumental value to a classless body of human persons. Similarly, the law treats inanimate and incorporeal things as legal persons so that the things may be of instrumental value to a variable and classless body of human persons.

An example of a thing that serves a function only upon personification, and the law's conceptualization of it as a rights-bearer, is the State. Hugo Grotius defined the State, which 'constitute[s] a sole person in the eyes of international law',[181] as a 'body of free men, united together in order to enjoy common rights and advantages.'[182] Pufendorf also conceived of the State in terms of the unity of its instrumental value, when he defined the State as:[183]

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[181] Montevideo Convention on Rights and Duties of States (signed 26 December 1933, entered into force 26 December 1934) 165 LNTS 19(Montevideo Convention), Art 2.

[182] H Grotius and AC Campbell (tr) *The Rights of War and Peace: Including the Law of Nature and of Nations* (Hyperion Press Westport 1979) at [XIV] 25.

[183] S Pufendorf *De Iure Naturae et Gentium Libri Octo* Bk VII, Ch 2, §13, para 672 translated in J Crawford *The Creation of States in International Law* (2nd Clarendon Press Oxford 2006) at 6; Montevideo Convention, Art 10.

> a compound moral person, whose will, intertwined and united by the pacts of a number of men, is considered the will of all, so that it is able to make use of the strength and faculties of the individual members for the common peace and security.

If a State is to protect the peace we must conceive of the State, and not the collection of the State's nationals, as the bearer of the right to the State's protection and promotion. It is the well-being of the State that grounds the duty on all other persons not to make the State 'the object of military occupation nor of other measures of force'.[184] This is because the State, as an instrument of 'common peace and security',[185] is valuable to a classless group of persons. The range of persons who benefit from peace and security in a State cannot be described in terms of any common attribute and do not form any discrete class or set of classes. A state of peace and security is valuable to persons more variable than, for example, the State's nationals and residents. For example, in outlining the US's changed military strategy, President Barack Obama explained that the persons who stand to benefit from a state of peace and security in the States of Afghanistan and Pakistan are variable. The beneficiaries of peace in Afghanistan and Pakistan are describable, not in terms of any common attribute, but in terms only of other corporate persons:[186]

> [T]ogether with the United Nations, we will forge a new Contact Group for Afghanistan and Pakistan that brings together all who should have a stake in the security of the region – our NATO allies and other partners, but also the Central Asian states, the Gulf nations and Iran; Russia, India and China. None of these

[184] Montevideo Convention art 11.

[185] S Pufendorf *De Iure Naturae et Gentium Libri Octo* Bk VII, Ch 2, §13, para 672 translated in J Crawford *The Creation of States in International Law* (2nd Clarendon Press Oxford 2006) at 6; Montevideo Convention, Art 10.

[186] B Obama 'Remarks by the President on a New Strategy for Afghanistan and Pakistan' 27 March 2009 http://www.america.gov/st/texttrans-english/2009/March/20090327121221xjsnommis0.1558496.html&distid=ucs (accessed 7 April 2009)

> nations benefit from a base for al Qaeda terrorists, and a region that descends into chaos. All have a stake in the promise of lasting peace and security and development.

(iii) The corporation

The difference between the classical and modern concepts of the corporation inheres in the extent to which each concept requires every incorporated corporation to resemble a legal person. The classical concept of the corporation required each corporation to treat itself as a thing of ultimate value, and to aim to make a profit for itself. In so doing, the courts did not deny the instrumental value of the company. But the courts limited the ways in which the company could be of instrumental value.[187]

In contrast, the modern concept of the corporation permits a corporation not to treat itself as a thing of ultimate value, but simply to be of instrumental value to a class of shareholders. The courts permit a corporation to resemble a trust. As Part One of this paper explored, the modern US and UK courts permit a corporation to be of instrumental value to an ascertainable class of beneficiaries; namely, its shareholders. The corporation has a power (and the directors have a duty) to act in the interests of the class of shareholders, even if the action is not in the interests of the corporation itself. And when a corporation acts, not to benefit itself but only to benefit its shareholders, the courts refuse to pierce the veil and expand the boundaries of corporate legal personality beyond the legal form of the incorporated entity. However, a problem with this concept of the corporation is that it misdescribes the corporation's legal personality in two ways.

[187] See text at pages 16-18.

(a) A bearer of rights

First, the modern concept fails to treat a corporation as a thing that is of ultimate value. This is because the modern concept mistakes the role of the fictitious proposition in the concept of legal personality. This paper argued that the law reaches the conclusion that a non-human thing is a person on the fictitious assumption that the thing is a being of ultimate value. To treat a corporation as a thing of ultimate value is to treat the thing – and to require other persons to treat the thing – as an ends in itself. To consider a corporation to be a legal person is to understand it to be a thing who acts in its own interests and to protect its own well-being.

Yet, the modern concept treats the corporation as if it were a plant or a trust. The concept reduces the directors' duty to act in the interests of the corporation to a duty that is of the same type as the gardener's duty to water a person's plants or the trustee's duty to manage a trust fund. The gardener's duty is grounded in the intrinsic value to her employer of healthy plants, and her employer's right that the plants well-being be protected and promoted. The trustee's duty is grounded in the beneficiaries' right that the trust fund be well-managed. The modern concept similarly grounds the directors' duty in the instrumental value to the class of shareholders of a useful corporation. The modern concept fails to recognize the corporation's own right that its well-being be protected as the exclusive source of the directors' duty to act in the interests of the corporation. In this way, the modern concept of the corporation fails to treat the corporation, and fails to require other legal persons to treat the corporation, as a rights-bearer, a thing of ultimate value, and an end in itself.

If the law conceives of the corporation as a thing that may exist only so as to be of instrumental value to a class of persons, then the law denies the separate legal personality of the corporation. The law cannot keep out of its sights its understanding of the corporation as a thing of ultimate value. Nor, however, can it 'drop out of the final reckoning'[188] its understanding of the corporation as a thing that is of instrumental value to a classless group of people.

(b) Of irreducible value

The second way in which the modern concept of the corporation misdescribes the corporation's legal personality is that the concept fails to recognize the ways in which a corporation, when treated as a legal person, is of instrumental value to a classless group of persons. The function of the non-eleemosynary corporation is to use its pool of capital in order to make a profit.[189] The Court of Exchequer in Equity reasoned, in *Bligh v Brent*:[190]

> The property is money – the subscriptions of individual corporators. In order to make that profitable, it is entrusted to a corporation who have an unlimited power of converting part of it into land, part into goods, and of changing and disposing of each from time to time; and the purpose of all this is the obtaining a clear surplus profit from the use and disposal of this capital… .

A profitable corporation is, of course, of use to its shareholders. Any

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[188] LL Fuller 'Legal Fictions' (Pt 3) (1930) 25 Illinois L Rev 877 at 895.

[189] The function of the eleemosynary corporation is to use its pool of capital in order to further its public or charitable aims. The eleemosynary corporation differs from the non-eleemosynary corporation that is operated without any motive to make itself a profit in that the eleemosynary corporation, in pursuing its public or charitable ends, acts as a legal person and is of value to a classless group of people, while the not-for-profit non-eleemosynary corporation does not act as a legal person and is of benefit only to a class of persons.

[190] (1836) 2 Y & C Ex 268, 160 ER 397; see also Hayek (note 124) at 115.

surplus profit is distributable to shareholders in the form of dividends. Yet, a profitable corporation is of use also to a classless range of other legal persons. When a corporation acts in order to benefit itself and to increase its profitability, the corporation thereby benefits a range of other legal persons. For example, if a corporation decides to reinvest its surplus profit by expanding its business, the corporation's share price may rise, the corporation may employ new staff and the corporation may open a new branch in a remote community. In this way, the corporation benefits the corporation's shareholders and employees and the members of the remote community.

When a single pool of capital is used in order to make a profit for a single person, a classless group of people stand to benefit. Shareholders are one class of persons who stand in line. But the remaining beneficiaries are so variable that they cannot be described in terms of any common attribute or set of attributes. The economic crisis of 2008 exemplifies the variability of persons who benefit from a corporation that operates to make itself a profit. In response to the crisis, the UK Government (amongst others) announced itself 'ready to buy preference shares in the … banks' that elected to be part-nationalized.[191] When Mervyn King, the Governor of the Bank of England, appeared before the House of Commons Treasury Select Committee, he defended the decision to recapitalize the banks, and argued that the Government will 'get money down the road which will more than justify the initial sums put up.'[192] The Governor understood that, as shareholder in a recapitalized bank, the bank might ultimately be in a position to distribute a

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[191] Hansard, HC Deb, 8 October 2008, Col 278.

[192] 'Government's UKFI corporation to manage investments in high-street banks', The Times, 4 November 2008: http://business.timesonline.co.uk/tol/business/industry_sectors/banking_and_finance/article5075536.ece (accessed 12 April 2009).

dividend to it and the Government might thereby profit. Yet, the Government did not purchase preference shares in the bank as an investment decision. As Mervyn King explained to the Treasury Select Committee, the bank recapitalization 'was not done in the interests of the banks. It was done to protect the rest of the economy from the banks.'[193] The banks were recapitalized so as to protect the economy – ie, the classless group of people for whom a profitable bank is instrumentally valuable – from the consequences of unprofitable banks. There was a critical distinction to be drawn between the importance of acting in the interests of the banks, and thereby acting in the interests of a classless group of people, and the unimportance of acting in the interests of the classes of employees and shareholders. As Joseph Stiglitz noted, there was:[194]

> a critical distinction [to be drawn] between saving the banks and saving the bankers and shareholders. We could have saved the banks but let the bankers and shareholders go.

Thus, to the extent that the modern concept conceives of the corporation as a legal person that exists to be of instrumental value to the class of shareholders, the concept underestimates the range of persons for whom a corporation is of instrumental value and the irreducibility of the corporation's value.

It is argued that, in contrast to the modern concept, the classical concept of the corporation understood the way in which a non-human, corporate thing is sensibly personified. This is because the classical concept required each

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193 'Government's UKFI corporation to manage investments in high-street banks', The Times, 4 November 2008: http://business.timesonline.co.uk/tol/business/industry_sectors/banking_and_finance/article5075536.ece (accessed 12 April 2009).

194 Joseph E Stiglitz 'A Bank Bailout That Works' 4 March 2009, *The Nation* http://www.thenation.com/doc/20090323/stiglitz?rel=hp_currently (accessed 14 April 2009).

corporation to treat itself as a thing of ultimate value so that it may thereby be of instrumental value to a classless group of people. The first part of this paper explored one way in which the classical concept expected each corporation to act to make a profit for itself. The courts permitted a corporation to be of instrumental value to a range of other legal persons. However, the courts limited the ways in which a corporation may be of instrumental value in two ways. First, the corporation had the power to act to benefit another legal person, but only if, in so acting, the corporation aimed to benefit itself. Secondly, the corporation also had the power to be of benefit to another legal person if the person's gain was derived from, and reflected in, the corporation's own gain. However, no corporation had the power to own stock in another corporation simply so as to be able to use the subsidiary corporation for its own ends. As the law fictitiously treats the corporation like every human person, and understands it to be of ultimate value, no person has a 'right to use a corporate structure'.[195] No person has a 'right to use' any other person. Nozick explains that to use another person is to deny that person's separate personality:[196]

> There are only individual people, different individual people, with their own individual lives. Using one of these people for the benefit of others, uses him and benefits the others. … To use a person in this way does not sufficiently respect and take account of the fact that he is a separate person, that his is the only life he has.

If the law conceives – or permits others to conceive – of the corporation as a thing that may exist only so as to be of instrumental value to other persons

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[195] *Adams v Cape Industries Plc* [1990] 1 Ch 433 (CA) at 544.
[196] R Nozick *Anarchy, State, and Utopia* (Basil Blackwell Oxford 1974) at 33.

(including other corporations), then the law denies the separate legal personality of the corporation.

3 THE PROPOSED SOLUTION: REMEMBERING THE CLASSICAL CONCEPT OF THE CORPORATION

To conceive of a corporation as a separate legal person, the law must expect each corporation to treat itself as a thing of ultimate value. What if a corporation refuses to treat itself as an ends in itself? Restoring the classical concept, it is proposed that an 'alter-ego' may sensibly be defined as a corporation that acts, not to generate a profit for itself, but *only* to generate a profit for another legal person. An alter-ego is a corporation that fails to treat itself as a thing of ultimate value and an end in itself. An alter-ego is a legal person who fails to act in fulfillment of its personhood, and fails to act: [197]

> for one's own sake and on one's own account [but] *merely* for the benefit of and as instrument of another person (as a slave does).

Thus, Corporation *A* is the alter-ego of Corporation *B* if (and only if) *A* does not act in *A*'s own interests, and in an attempt to generate a profit stream for *A*, but acts *only* to further the interests of *B*, and to generate a profit for *B*.[198]

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[197] T Aquinas *Commentary on the Sentences of Peter* Lombard at distinction 44, question I, article 3.

[198] For proposals based on a similar principle of corporate profitability, see *Henderson v Rounds & Porter Lumber Co* 99 F Supp 376 (1951) at 381, where the Court held that 'the court should … place responsibility on the defendant' where:

> the defendant dominated and manipulated the affairs of [another corporation] *for its own interest*, rather than the best interest of the [other corporation] as a separate corporate entity… .

See also the decision of the trial judge Alton J, which the Court of Appeal overruled in Ord, and in which she held (*Ord v Belhaven Pubs Ltd* [1998] 2 BCLC 447 at 454): 'that the court would be justified in lifting the veil and treating Holdings … as liable for this contingent debt' on the ground that: 'the directors of the [subsidiary corporation] … acted solely in the interests of the group and at the behest of Holdings'. For academic support see RW Hamilton 'The Corporate Entity' (1971) 49 Texas L Rev

Corporation *A* is the alter-ego of Corporation *B* if (and only if) *A* is not operated in *A*'s own interests, but is managed on trust for *B*.

What if a corporation is part operating corporation and part alter-ego; part Salomon & Co and part-trust? Must the profit making purpose of the corporation be the sole purpose that the corporation pursues, or merely the dominant or critical purpose? May the corporation pursue other incidental purposes? And how is the dominance of a purpose measured? What if the corporation is a mere shelf corporation, and is yet to resemble either Salomon & Co or a trust?

To apply the test, the courts need not classify the entirety of the corporation's legal personality. To identify the boundaries to a corporation's personality, and pierce the corporate veil, the courts do not divest the parent corporation of its stock in the subsidiary corporation.[199] Nor do the courts revoke the charter of the corporation that acts as an alter-ego.[200] To pierce the corporate veil is merely to attribute a particular asset or liability of one incorporated entity to another legal person. Thus, to pierce the veil, the courts need examine only the particular acts of a corporation that ground the relevant asset or liability.

In particular, the proposal is that the courts should pierce the corporate

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979 at 1003; JM Landers 'A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy' (1975) 42 U Chicago L Rev 589; WJ Rands 'Domination of a Subsidiary by a Parent' (1998) 32 Indiana L Rev 421 at 456.

[199] Cf *US v Reading Co* 253 US 26 (1923).

[200] For example, the Pennsylvania Legislature revoked in 1872 the charter of the South Improvement Corporation, which 'was the vehicle through which the Standard Oil interests created their notorious system of rebates', after the Corporation's 'method of suppressing competition aroused the ire of the public'; JC Bonbright and GC Means *The Holding Company: Its Public Significance and its Regulation* (McGraw-Hill Book Co Inc New York 1932) at 61.

veil, and attribute an asset or liability of a corporation (*A*) to one of its shareholders or another member of the corporate group (*B*), whenever:

(i) corporation *A* acquired the asset or liability as a result of performing an act;

(ii) corporation *A* performed the act with the intention of generating a profit for corporation *B*;[201] and

(iii) corporation *A* performed the act without any intention of 'carrying on [the corporation's own] independent business'[202] and generating a profit for *A*.[203]

If the corporation fails to use, for example, loaned capital to generate its own profit stream, but uses the capital to generate only the profit stream of another legal person, the creditor may take recourse against that other legal person. If a corporation fails to use the services of an employee to generate its own profit stream, but uses the services to generate only the profit stream of another legal person, the employee may take recourse against that other legal person. For the purposes of identifying the extent of a corporation's liability to its voluntary and involuntary creditors, the boundaries of the corporation's legal personality expand to include the legal person in whose interests the corporation's assets or liabilities were managed. Whenever a corporation is operated as a trust for another legal person, the legal personality of the corporation expands to include the trust's beneficiaries.

In this way, corporate law affords creditors the same protection that is afforded to investors by ensuring that each corporation – whether or not its

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[201] Or pursuing the charitable ends of corporation *B*, if *B* is a charitable corporation.
[202] r6.1.4R(3) of Listing Rules.
[203] Or pursuing its own charitable ends, if *A* is a charitable corporation.

securities are listed on a regulated exchange – is required to attempt to generate for itself a profit stream. Creditors, like the investing public,[204] may assume that a corporation to whom it loans its capital will use the capital to generate its own profit stream. Creditors may 'make a reasonable assessment of' a corporation's 'future prospects'.[205] The assessment that the creditor is empowered to make is only as reasonable, and is as risky, as any potential investor's assessment. The creditor is in no way assured that the corporation's business will not 'f[a]ll upon evil days',[206] as Salomon & Co's business did, and fall into insolvency. A creditor cannot take recourse out of the assets of another member of a corporate group whenever the debtor corporation 'turns out to be the runt of the litter' of the group.[207] The creditor is simply assured that the corporation will use the asset that the creditor advances to it in order to attempt to generate a profit, out of which the asset may be repaid.

CONCLUSION

This paper outlined the two judicial reforms by which the US and UK courts abandoned the 'older ideas'[208] of the classic concept of the corporation. The first reform removed the law's expectation that each corporation be operated in order to generate itself a profit. The second reform entitled shareholders to form a corporation simply so as to fence-off the shareholders' liabilities from the shareholders' assets and profit-stream. Taken together, there is cause to wonder whether the reforms have eroded the structures that facilitate the return of credit in free markets. While the principle of limited liability may

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204 See text at pages 26-28.
205 Financial Services Authority's Listing Rules LR 6.1.6; see text at note 95.
206 *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 49.
207 *Re Southard & Co Ltd* [1979] 1 WLR 1198 (CA) at 1208.
208 'Capitalism Beyond the Crisis' 26 March 2009, (2009) 56 New York Review of Books, http://www.nybooks.com/articles/22490 (accessed 14 April 2009).

successfully have ensured that 'the demand for credit' is high,[209] the courts' modern application of the principle may also have played a role in ensuring that the availability of credit is low. As an economist noted during the Great Depression:[210]

> Experience shows that financial policies are really tested and false theories exploded in periods of general business depression.

Ever since the courts of the US and UK abandoned the classic concept of the corporation, and preferred the modern concept, corporate law has struggled to account for doctrinal inconsistencies. To remedy these, this paper proposed a principled test that courts should use in order to identify the circumstances in which the corporate veil is justifiably pierced, and in order to restore the classic concept of the corporation.

Part Two of this paper set about outlining why it is that, if the corporation is to be treated as a legal person and vested with its own legal rights, the law must treat the corporation as an end in itself; ie, the courts must prefer the classic concept of the corporation. The 'person' is one of two things. First, the person is a human. If not, the person is a fiction. Pinter's people, Hobbes' hospital, the State and the law's corporations are persons in the latter sense. Plants, robots, molecules and trusts, on the other hand, are not persons in either sense. Fictional characters, inanimate objects and incorporeal entities are personified when they are treated as beings that are of ultimate value. This treatment is fictitious. That is, Pinter, Hobbes, international law and corporate

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[209] RA Posner 'The Rights of Creditors of Affiliated Corporations' (1975) 43 U Chicago L Rev 499 at 503.

[210] K Field 'Use of Subsidiary Corporations in Segregating Risk' (1933) 9 J of Land & Public Utility Economics 150 at 150.

law are aware that their understanding of these non-human things as beings of ultimate value is false.

Pinter is not accountable to the strictures of rationality. He is free to personify as he pleases, as Cervantes did. Philosophers and lawyers, on the other hand, give reasons and aim not to reason arbitrarily or tautologically. The imaginative personification of things is rational to the extent that there is a reason for which we treat the thing as being of ultimate value. It makes no sense to treat a plant as a thing of ultimate value. A plant, a trust or two horses drawing a cart need not be treated as a thing of ultimate value in order for any of them to be of intrinsic value or instrumental value to human persons. But for a hospital to be of instrumental value *qua* a hospital, it must be of value to a classless body of sick persons. It is the irreducibility to identifiable and finite human persons of a thing's intrinsic or instrumental value that rationalizes our fictitious treatment of it as an ultimately valuable person. This means, then, that the law must treat each corporation, and must expect every legal person to treat each corporation, as if the corporation is a thing of ultimate value. Until corporate law restores the classic conception of the corporation, the law will continue to misunderstand what it means for a corporation to be a separate legal person. To understand what it means for a corporation to be a legal person, and to circumvent the fault-line of modern corporate law, the law must re-examine and return to the older idea of both capitalism and corporate law: 'the profit motive'.[211]

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[211] 'Capitalism Beyond the Crisis' 26 March 2009, (2009) 56 New York Review of Books, http://www.nybooks.com/articles/22490 (accessed 14 April 2009).