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AN ANALYSIS OF THE DECISION IN *VTB CAPITAL PLC V NUTRITEK INTERNATIONAL CORP& ORS* [2013] UKSC 5 BY THE SUPREME COURT IN TERMS OF ITS IMPLICATIONS ON THE EVOLUTION OF THE PRINCIPLE OF PIERCING THE CORPORATE VEIL

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TABLE OF CONTENTS

TABLE OF CONTENTS ii

TABLE OF CASES iii

INTRODUCTION 1

I. A BRIEF HISTORY OF THE PRINCIPLE OF PIERCING THE CORPORATE VEIL UNTIL *VTB v NUTRITEK* CASE

A. In General 3

B. Agency Argument 4

C. Single Economic Unit Argument 5

D. Façade Argument 7

E. The *Adams v Cape* Case And Onwards 9

II. THE *VTB v Nutritek* CASE and ITS IMPLICATIONS ON THE PRINCIPLE 14

CONCLUSION 26

BIBLIOGRAPHY 27

TABLE OF CASES

- *Adams v Cape Industries plc* [1990] Ch 933
- *Adelson v Associated Newspapers Ltd* [2007] EWCH 3028
- *Albazero* [1977] AC 774
- *Alliance Bank JSC v Acquanta Corporation* [2011] EWCH 3281 (Corp)
- *Antonio Gramsci Shipping Corporation and Others v Stepanovs* [2011] EWHC 333
- *Atlas Maritime Co SA v Avalon Maritime Ltd* (The Coral Rose) [1991] All ER 769
- *Bank of Tokyo v Karoon* [1987] AC 45
- *Beckett Investment Management Group Ltd v Hall* [2007] EWCA Civ 613
- *Ben Ashem v Ali Shayif* [2009] 1 FLR 115
- *Creasey v Breachwood Motors Ltd* [1993] BCLC 480
- *Dadourian Group International Ltd v Simms* [2006] EWCH 2973
- *DHN Food Industries Ltd v Tower Hamlets LBC* [1976] 1 WLR 852 CA
- *Gilford Motor v Horne* [1933] Ch 935
- *J.H. Rayner (Mincing Lane) Ltd v Department of Trade and Industry and Others* [1989] Ch 72
- *Kensington International Ltd v Republic of Congo* [2005] EWCH 2684 (Comm) [2006] 2 BCLC 296
- *Lindsay v O'Loughnane* [2010] EWCH 529 (QB)
- *Littlewoods Mail Order Stores v Inland Revenue Commissioners* [1969] 1 WLR 1241
- *Ord & Anor v Belhaven Pubs* [1998] BCC 607

- *Pierelli Cable Holding NV v Inland Revenue Comm'rs* [2006] 1 WLR 400 (H.L.)
- *Prest v Petrodel Resources Ltd and Others* [2013] UKSC 34
- *Salomon v Salomon* [1897] AC 22
- *Scottish Cooperative Wholesale Society v Meyer* [1959] AC 324
- *Smith v Hughes* (1871) LR 6 QB 597
- *Smith, Stone & Knight v Birmingham Corporation* [1939] 4 ALL ER 116
- *Snook v London and West Riding Investment* [1967] 2 QB 786 [1962] 1 WLR 832
- *Stone & Rolls v Moore Stephens* [2009] UKHL 39
- *The Tjaskemolen (Now named "Visvliet")* [1997] 2 Lloyd's Rep. 465 (Q.B.)
- *Trebanog Working Men's Club and Institute Ltd v MacDonald* [1940] K.B. 576
- *Trustor AB v Smallbone* [2001] 2 BCLC 296
- *Tweedle v Atkinson* (1861) 1 B & S 393
- *VTB Capital Plc v Nutritek International Corp & Others* [2013] UKSC 5
- *Wallersteiner v Moir* [1974] 1 WLR 991
- *Woolfson v Stracthclyde Regional Council* [1978] UKHL 5
- *Yukong Line Ltd of Korea v Rendsburg Investmensts Corp of Liberia* [1998] 2 BCLC 485

INTRODUCTION

2013 has been very fertile for law professionals with regards to the "principle of piercing the corporate veil" due to two landmark judgements given by the Supreme Court. Both in the cases of *VTB Capital Plc v Nutritek International Corp & Others*[1] and *Prest v Petrodel Resources Ltd and Others,*[2] the Supreme Court has examined the principle and made determinations with regards to the scope of it.

As the evolution process of the doctrine proves, one of the most ambiguous and thus litigious subjects in English Company Law has been that the conditions and circumstances lead the courts to either decide upon disregarding the corporate personality of a registered company or not.[3] In other words, the issues and specifying the situations which necessitate "piercing the corporate veil" had not been easy to generalize. Although it is traditionally known that the courts do not allow companies which are used with intent to defraud or as a vehicle to evade existing obligations, both the cases of *VTB v Nutritek* and *Prest v Petrodel* have been given greater importance due to the fact that the judgements are given by the Supreme Court.

In the case of *VTB v Nutritek,* whose consequences constitute the subject of this article, the guidance given by the Supreme Court has significant implications on the evolution of the principle of "piercing the corporate veil" especially for determining what the principle is really not. Although the existence of the principle was not the subject to be decided upon in *VTB v Nutritek*, since it had been found unnecessary to do so in such a case where VTB can not succeed, the Supreme Court, by assuming the existence of the principle, overruled the decision given in *Antonio Gramsci Shipping*

[1] [2013] UKSC 5
[2] [2013] UKSC 34
[3] M.Moore: "A Temple built on faulty foundations:piercing the corporate veil and the legacy of *Salomon v Salomon*, The Journal of Business Law, March 2006, p.180

Corporation and Others v Stepanovs[4] - in which it is stated that the parent company controls the puppet company and may be sued because of breach of contract in circumstances where that puppet company has been used as a vehicle to conceal the true facts- and drew attention to its traditionally determined limits.

The judgement in *VTB v Nutritek* reflects and ratifies the rigid approach adopted since the unique case of *Salomon v Salomon*[5] in English Law[6]. Despite the fact that several attempts were made in order to extend the scope of the application of the principle as in the relatively new case of *Antonio Gramsci,* it can be said that the decision in *VTB v Nutritek* reshaped the future of the principle in line with the traditional perspective.

This article aims to critically analyze the implications of the decision given in *VTB v Nutritek* by the Supreme Court with regards to the evolution of the "principle of piercing the corporate veil". Although both the Companies Act 2006[7] and the Insolvency Act 1986[8] contain provisions which constitute exceptions to the separate corporate personality, the article focuses on common law exceptions. In doing so, firstly, the meaning given to the principle in English Law will be summarised and then the facts of the *VTB v Nutritek* case and the reasons behind the rejection of the claim regarding the veil piercing will be stated. After outlining both the history of the principle until *VTB v Nutritek* case and the approach which is adopted by the Supreme Court, the implications of the case on the evolution of the principle will be discussed. Eventually, the article will end with the conclusion reached.

[4] [2011] EWHC 333
[5] [1897] AC 22
[6] M.Moore: "A Temple built on faulty foundations:piercing the corporate veil and the legacy of *Salomon v Salomon*, The Journal of Business Law, March 2006, p.181
[7] s 399
[8] s 213, s 214, s 215, s 216

I. A BRIEF HISTORY OF THE PRINCIPLE OF PIERCING THE CORPORATE VEIL UNTIL *VTB v NUTRITEK* CASE

A. In General

The veil piercing doctrine in English Law has always been a concept that the courts have not been so much inclined to apply.[9] With the legacy of the unique case of *Salomon*, in which it is stated that "*the company is at law a different person altogether from the subscribers to the memorandum*"[10], even the existence of the doctrine has been criticised.[11] However, despite the fact that the House of Lords in *Salomon* authenticated the principle of separate corporate personality, the ability of the courts to ignore it is frequently asserted.[12]

Separate corporate personality signifies the judicial separation of the company's' personality from that of the shareholder's.[13] This well established law is also included in the Companies Act 2006.[14] On the other hand, the veil piercing doctrine stands on the opposite side of this law.

Piercing the corporate veil simply denotes "*disregarding the corporate personality*".[15] In some cases, the ignorance of the corporate personality might be for the benefit of the shareholders[16]. Whereas the cases in which as a result of disregarding the separate corporate personality, shareholders become responsible for the obligations of the company with all their personal assets and in accordance with this consequence

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[9] P.L.Davies and S. Worthington: *Gower and Davies Principles of Modern Company Law*,(9th edn), Sweet&Maxwell, London, (2012), p. 223
[10] Per Lord Macnaghten at p. 51
[11] B. Hannigan: *Company Law*, (3rd edn), Oxford University Press, Oxford, 2012, p. 45
[12] D. French, S.W. Mayson and C.L.Ryan: *Mayson, French & Ryan on Company Law*, (2011-2012 edn), Oxford University Press, Oxford, (2011), p. 121
[13] A. Dignam: *Hicks & Goo's Cases and Material on Company Law*, (7th edn), Oxford University Press, Oxford, (2011), p. 104
[14] s. 16
[15] *Prest v Petrodel Resources Ltd and Others* [2013] UKSC 34 at para 16 per Lord Sumption
[16] P.L.Davies and S. Worthington: *Gower and Davies Principles of Modern Company Law*,(9th edn), Sweet&Maxwell, London, (2012), p. 215. See, *Trebanog Working Men's Club and Institute Ltd v MacDonald* [1940] K.B. 576; *DHN Food Industries Ltd v Tower Hamlets LBC* [1976] 1 WLR 852 CA

there would not be limited liability for the shareholders anymore.[17] This outcome usually constitutes the aim behind the veil piercing.

It has not been possible to formulate a consistent principle accepted generally by the courts that is always applicable as a test in order to decide upon the circumstances where the separate corporate personality must be respected or where it must be disregarded.[18] However, in the course of a hundred years after *Salomon*, the courts have attempted several times to clarify the exceptions of the separate corporate personality. These attempts include "agency" exception in *Smith, Stone & Knight v Birmingham Corporation*[19] put forward by Atkinson J; "single economic unit" exception for group companies which was propounded by Lord Denning in *DHN Food Industries Ltd v Tower Hamlets LBC*[20] as well as the exceptions regarding fraud or mere façade or even in the interest of justice.[21]

B. Agency Argument

Defining the agency relationship between the shareholders and the company or in a group company context, parent as principal and subsidiary as agent, has been discussed to make it an exception to the separate corporate personality principle. This issue firstly put forward in *Salomon* by Williams J by expressing that the company was nothing but an agent of Mr. Salomon. However, the House of Lords eventually rejected the argument and held that a company never becomes an agent of the shareholders automatically even though the other shareholders are dummies but for Mr. Salomon.

[17] W.Pak and L. Bergkamp: "Piercing the Corporate Veil: Shareholder Liability for Corporate Torts", Maastricht Journal of European and Comparative Law, Vol:8, No:2, 2001, p. 180
[18] J.Birds and A.J.Boyle: *Boyle & Birds Company Law*, (8th edn), Jordans, Bristol, (2011), p. 62
[19] [1939] 4 ALL ER 116
[20] [1976] 1 WLR 852 CA
[21] P.L.Davies and S. Worthington: *Gower and Davies Principles of Modern Company Law,*(9th edn), Sweet&Maxwell, London, (2012), p. 217

The first attempt in English Law to set up comprehensive criteria for veil piercing doctrine in terms of the agency argument was in *Smith, Stone & Knight v Birmingham Corporation.*[22] In the case, Atkinson J established six factors of criteria in deciding upon agency relationships within the group companies. These were all about reaching the answer of the question "who was really carrying on the business" by determining the following

- *Were the profits treated as those of the parent company?*
- *Were the persons conducting the business appointed by the parent company?*
- *Was the parent company the head and brain of the trading venture?*
- *Did the parent company govern the adventure?*
- *Did the parent company make profit through its skill and direction?*
- *Was the parent company in effectual and constant control?*

By applying the criteria, the court ruled that the subsidiary was very closely controlled by the parent company and therefore the subsidiary was merely an agent of the parent company[23].For this reason,the parent company was found to be entitled to compensation for the compulsory purchase of its subsidiary's business.

C. Single Economic Unit Argument

Another argument regarding veil piercing concerns the "single economic unit" theory created by Lord Denning in *DHN Food Industries Ltd v Tower Hamlets London*

[22] T.K.Cheng: "The Corporate Veil Doctrine Revisited: A Comparative Study of The English and The US Corporate Veil Doctrines", Boston College International and Comparative Law Review, Vol:34, Issue 2, (2011), p. 337

[23] J.Birds and A.J.Boyle: *Boyle & Birds Company Law,* (8th edn), Jordans, Bristol, (2011), p. 63. Also see: *J.H. Rayner (Mincing Lane) Ltd v Department of Trade and Industry and Others* [1989] Ch 72 in which it is stated by Kerr LJ: "*The facts of Smith, Stone and Knight were so unusual that they can not form any form of principle*". This case was also an example of strict adherence to the *Salomon*. (A. Dignam: *Hicks & Goo's Cases and Material on Company Law*, (7th edn), Oxford University Press, Oxford, (2011), p. 114)

Borough Council.[24] In the case, the Court of Appeal unanimously found the parent company entitled to compensation for the disturbance of business on the basis of the Land Compensation Act, although the owner of the land and business on it were owned by the subsidiary. The theory relies on the idea that, where the group companies are operated as a single unit for business purposes, the law should treat them as one.[25] Lord Denning expressed in *DHN* that:

> "*this group is virtually the same as a partnership in which all the three companies are partners and therefore they should not be treated differently. The three companies should, for present purposes, be treated as one and the parent company DHN should be treated as that one*".[26]

Two years after the *DHN*, the House of Lords clearly doubted the reasoning of Lord Denning, in *Woolfson v Stracthclyde Regional Council*.[27] The case was about the disturbance of business and loss of land under a compulsory purchase order and Mr. Woolfson, who was the majority shareholder but not the controller of the subsidiary, claimed for compensation since the land was owned by its subsidiary. The court found that Mr. Woolfson was not entitled to compensation and rejected his claim following the reasoning of the *DHN.* The reason was summarised by Lord Keith of Kinkel as:

> "*The grounds for the decision were that since DHN was in a position to control its subsidiaries in every respect, it was proper to pierce the*

[24] It should be noted that the phrase "single economic unit" have not been clearly referred by Lord Denning. The term was used by commentators and the courts. (T.K.Cheng: "The Corporate Veil Doctrine Revisited: A Comparative Study of The English and The US Corporate Veil Doctrines", Boston College International and Comparative Law Review, Vol:34, Issue 2, (2011), p. 339) See, *Pierelli Cable Holding NV v Inland Revenue Comm'rs*, [2006] 1 WLR 400 (H.L.)

[25] P.L.Davies and S. Worthington: *Gower and Davies Principles of Modern Company Law*,(9th edn), Sweet&Maxwell, London, (2012), p. 215

[26] Also see cases regarding corporate veil where Lord Denning took part: *Scottish Cooperative Wholesale Society v Meyer* [1959] AC 324; *Littlewoods Mail Order Stores v Inland Revenue Commissioners* [1969] 1 WLR 1241; *Wallersteiner v Moir* [1974] 1 WLR 991. Especially, the case *Littlewoods* in which Lord Denning warned against blind adherence to the *Salomon* draws attention. (T.K.Cheng: "The Corporate Veil Doctrine Revisited: A Comparative Study of The English and The US Corporate Veil Doctrines", Boston College International and Comparative Law Review, Vol:34, Issue 2, (2011), p. 338

[27] [1978] UKHL 5

corporate veil and treat the groups as a single economic entity for the purpose of awarding compensation for disturbance… I have some doubts whether in this respect the Court of Appeal properly applied the principle that it is appropriate to pierce the corporate veil only where special circumstances exist indicating that it is a mere façade concealing the true facts".

Starting with *Woolfson* which doubted the decision in *DHN*, the courts have started to reject the single economic unit theory and narrowed the application. The decision in *Bank of Tokyo v Karoon*[28] was prominent in this era. With the cutting explanation of Robert Goff LJ who stated that "*we are concerned not with economics but with law. The distinction between the two is, in law, fundamental and cannot here be bridged*", the Court of Appeal clearly dismissed the theory.[29]

D. Façade Argument

The most prominent exceptions to the principle in *Salomon* have been the decisions where "fraud, "mere façade" and "sham" are involved. In most of the cases concluded in favour of veil-piercing, the facts concerning instances where the company is being used by shareholders, is as a device to gain some benefits or to evade obligation.[30] In other words, despite the fact that there had been inconsistency and lack of a formulated approach towards the veil piercing doctrine, the courts have never been

[28] [1987] AC 45. In that case the CA has also reviewed the veil piercing doctrine on the diverse grounds such as fraud, agency and rejected all of them.(T.K.Cheng: "The Corporate Veil Doctrine Revisited: A Comparative Study of The English and The US Corporate Veil Doctrines", Boston College International and Comparative Law Review, Vol:34, Issue 2, (2011), p. 340

[29] Goff LJ was also took place in *DHN* case and signaled his approach toward the doctrine with that reasoning: "*.....this is a case in which one is entitled to look at the realities of the situation and to pierce the corporate veil. I wish to safeguard myself by saying that so far as this ground is concerned, I am relying on the facts of this particular case. I would not at his juncture accept that in every case where one has a group of companies one is entitled to pierce the veil, but in this case the two subsidiaries were both holly owned; further, they had no seperate business operations whatsoever.*"

[30] A. Dignam: *Hicks & Goo's Cases and Material on Company Law*, (7th edn), Oxford University Press, Oxford, (2011), p. 105

silent to the exploitation of the companies with the power derived from the *Salomon case* and have forged some limited exceptions to the separate corporate personality principle in order to curb extreme cases of abuse.[31]

In the *Salomon case* itself, the fraud assertion was propounded in order to make Mr. Salomon liable. It is clear from the reasoning of the decision that if there had been any fraud by Mr. Salomon regarding his company; the Court would have disregarded the corporate personality and held Mr. Salomon liable. Accordingly, it would not be wrong to say that the fraud or mere façade test was first applied in *Salomon*.

One of the early cases after *Salomon*, which was successful for veil piercing on the basis of "fraud-mere façade" was *Gilford Motor v Horne*[32]. The facts of the case are as follows: Mr. Horne was under obligation not to solicit customers from his previous employer and in order to avoid that obligation he had established a company in his wife's name. The court ruled that the company was formed to cloak the facilities of Mr. Horne "as a mere cloak or sham[33]" to evade the existing obligation towards the Gilford Motor Co and thus felt justified in disregarding the separate corporate personality.[34] The words used by the Court of Appeal was given importance in the doctrine and used in *Jones v Lipman*[35] which was also a case in which the court pierced the corporate veil paying attention to the evasion of a pre-existing contractual obligation.

The power of the courts to pierce the corporate veil in the event of fraud-mere façade is also stated in *Woolfson* by Lord Keith in the House of Lords. As was stated

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[31] M.Moore: "A Temple built on faulty foundations:piercing the corporate veil and the legacy of Salomon v Salomon, The Journal of Business Law, March 2006, p.181

[32] [1933] Ch 935

[33] The word sham has been defined by Lord Diplock in the case of *Snook v London and West Riding Investment* [1967] 2 QB 786 as: "*Acts done or documents executed by the parties to the "sham" which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intended to create*."

[34] M.Moore: "A Temple built on faulty foundations:piercing the corporate veil and the legacy of Salomon v Salomon, The Journal of Business Law, March 2006, p.182-183

[35] [1962] 1 WLR 832

while discussing the effects of the case on agency exception, Lord Keith stated that "*it is appropriate to pierce the corporate veil where special circumstances exist indicating that it is a mere façade concealing the true facts*".[36] In the light of this expression, the evolution of the doctrine proceeded to another phase in which the decision in *Adams v Cape Industries plc*[37] made its mark.

E. The *Adams v Cape* Case and Onwards

Both the exceptions adopted by the courts stated above, which are agency-single economic unit-fraud or mere façade, have taken place and been discussed in the landmark decision of the Court of Appeal in *Adams v Cape*. The case was with regards to a liability issue within a group of companies. The aim of the claimant was to have the corporate personality of the parent company (Cape) disregarded, in order to make the parent company liable for its own obligations towards tort victims. Under this claim, the court had to decide whether judgements obtained in the USA against the parent company (Cape), which was an English registered company whose business was mining asbestos in South Africa and which was marketed all over the world, would be recognized and enforced by the English courts.[38]

The Court of Appeal, by reviewing the *Salomon case,* attempted to structure the rich but confusing body of case law regarding the circumstances which necessitate veil piercing in terms of group companies and brought some new and more restrictive approaches for veil piercing by holding that "*the court is not free to disregard the*

[36] It is suggested that "*although the dictum of Lord Keith is undeniably high authority, his Lordship did not explain what he meant by piercing the corporate veil or consider many previous cases, so the scope of the principle enunciated by his Lordship is not clear*".(D. French, S.W. Mayson and C.L.Ryan: *Mayson, French & Ryan on Company Law*, (2011-2012 edn), Oxford University Press, Oxford, (2011), p. 149.)
[37] [1990] Ch 933
[38] P.L.Davies and S. Worthington: *Gower and Davies Principles of Modern Company Law*,(9th edn), Sweet&Maxwell, London, (2012), p. 215

principles of Salomon v A. Salomon & Co Ltd merely because justice so requires."[39] In the case, the Court of Appeal rejected to pierce the corporate veil in order to expose the identity of the defendant as the controlling body behind a complex group structure by way of which potentially nocuous asbestos products were sold worldwide using low capitalised subsidiary companies.[40]

The single economic unit concept found no support in *Adams v Cape* independently on which the corporate veil might be pierced.[41] The court stated that there is not such a general principle that all the companies within a group context are to be regarded as one, and quite the contrary, the main principle is that "*each company in a group of companies is a separate legal entity possessed of separate rights and liabilities*".[42] However, it is also accepted that group companies may be treated as one unit at any rate for some purposes in the event that the wording of a specific statues or contracts may justify.[43]

In the history of veil piercing in English Law, the successful cases based on agency grounds have always been very limited.[44] The assertion based on agency failed in *Adams v Cape* too on the basis that the court found it not easy to presume any agency relationship between the company and the shareholders or between the parent company and the subsidiary in the absence of an express agreement.[45] It is also emphasised by Slade LJ that the parent company (Cape) did not have "day to day" control over the subsidiary in the USA, and so much so that, even the parent company carries on its

[39] J.Birds and A.J.Boyle: *Boyle & Birds Company Law*, (8th edn), Jordans, Bristol, (2011), p. 74
[40] M.Moore: "A Temple built on faulty foundations:piercing the corporate veil and the legacy of Salomon v Salomon, The Journal of Business Law, March 2006, p.181
[41] J.Birds and A.J.Boyle: *Boyle & Birds Company Law*, (8th edn), Jordans, Bristol, (2011), p.75
[42] at 532 citing Roskill LJ in the "*Albazero*" [1977] AC 774
[43] at 536
[44] M.Moore: "A Temple built on faulty foundations:piercing the corporate veil and the legacy of Salomon v Salomon, The Journal of Business Law, March 2006, p.183
[45] P.L.Davies and S. Worthington: *Gower and Davies Principles of Modern Company Law*,(9th edn), Sweet&Maxwell, London, (2012), p. 215

group company formed business as a single economic unit, it is not sufficient to generate an agency relationship between the parent and its subsidiaries.[46]

In *Adams v Cape*, the Court of Appeal accepted that there was one well-recognised exception to the rule prohibiting the veil piercing by way of referencing the *Jones v Lipman* case and the statement made by Lord Keith in *Woolfson*[47]. Having refused the mere façade assertion on the face of the facts and having stated that the Court was "*left with rather sparse guidance as to the principles which should guide the court in determining whether or not the arrangements of a corporate group involve a façade within the meaning of that word as used by the House of Lords in Woolfson…"*[48], the Court of Appeal emphasised that the "motive" with which a subsidiary was formed (or an existing used) is crucial.[49]

The Court of Appeal in *Adams v Cape* was also emphatic and found it legitimate to use corporate structure "where it is set up legitimately to manage risks".[50] The statement of Slade J is remarkable:

> "*....we do not accept as a matter of law that the court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use corporate structure in this way is inherent in our corporate law*".[51]

[46] at 549
[47] at 539
[48] at 543
[49] J.Birds and A.J.Boyle: *Boyle & Birds Company Law*, (8th edn), Jordans, Bristol, (2011), p. 76
[50] B. Hannigan: *Company Law*, (3rd edn), Oxford University Press, Oxford, 2012, p. 52
[51] at 520

The *Adams v Cape* case rather narrowed the application of the principle of piercing the corporate veil and was regarded as a disambiguation of the principle established in *Salomon*.[52] The court maintained respect for the corporate form, as stated in *Salomon,* without causing a deprivation of capacity to prevent abuses of the corporate structure for future courts.[53] The guidelines set up in *Adams v Cape* have been consistently followed in later cases and the courts have refrained from decisions in favour of veil piercing unless "mere façade" was shown in corporate structure.[54]

Adams v Cape is seen as the leading case; however, it has not been that much of a desperate situation for veil piercing plaintiffs after *Adams v Cape*, despite its widespread effects.[55] There have been attempts both to widen it, as well as to narrow it. For instance, the *Creasey v Breachwood Motors Ltd* case[56] which did not follow the ruling in *Adams v Cape* and ended up in favour of veil piercing but was ultimately overruled in *Ord & Anor v Belhaven Pubs*[57].

In addition, since 2007, there have been some indications in terms of desisting from the rigid approach adopted in *Adams v Cape*.[58] For instance, *in Beckett Investment Management Group Ltd v Hall*[59] the Court of Appeal clearly ratified Lord Denning's veil piercing judgement in *Littlewoods* in which his Lordship stated that "*the answer is I think, the law today has regard to the realities of big business. it takes the group as being one concern under one supreme control*" and treated parent and the subsidiary

[52] A. Dignam: *Hicks & Goo's Cases and Material on Company Law*, (7th edn), Oxford University Press, Oxford, (2011), p. 121
[53] M.Moore: "A Temple built on faulty foundations:piercing the corporate veil and the legacy of *Salomon v Salomon*, The Journal of Business Law, March 2006, p.184
[54] J.Birds and A.J.Boyle: *Boyle & Birds Company Law*, (8th edn), Jordans, Bristol, (2011), p. 77
[55] T.K.Cheng: "The Corporate Veil Doctrine Revisited: A Comparative Study of The English and The US Corporate Veil Doctrines", Boston College International and Comparative Law Review, Vol:34, Issue 2, (2011), p. 340
[56] [1993] BCLC 480. See also "*The Tjaskemolen*" (Now named "Visvliet") [1997] 2 Lloyd's Rep. 465 (Q.B.) which referenced the *Creasey v Breachwood Motors Ltd.*
[57] [1998] BCC 607. See also *Trustor AB v Smallbone* [2001] 2 BCLC 296
[58] A. Dignam: *Hicks & Goo's Cases and Material on Company Law*, (7th edn), Oxford University Press, Oxford, (2011), p. 127
[59] [2007] EWCA Civ 613

companies as one. Likewise, in *Adelson v Associated Newspapers Ltd*[60] the single economic unit theory was suggested as a solution[61]. In this era, *Stone & Rolls v Moore Stephens*[62] also drew attention. The majority of the House of Lords in *Stone & Rolls* disregarded the separate corporate personality and imputed the shareholders' fraudulent purposes to the company.

The brief history above shows us that the veil piercing doctrine plays a small role in English Law, once the facts of the case moves outside the area of specific contracts or statutes.[63] Accordingly, since there are substantial overrules of the decisions in the history of the doctrine; the inconsistency among the judgements becomes unavoidable. However, if any case comes before the highest court, the impact of the reasoning and approach taken by it becomes all-important. This effect can also be seen in the decision of *VTB v Nutritek* by the Supreme Court which overruled the relatively new case of *Antonio Gramsci*. The court in *Antonio Gramsci* decided in favour of veil piercing by imposing direct contractual liability in order to allow a third party to claim on breach of contract against not only the puppet company but also against others behind it. As will be discussed below, the decision of the Supreme Court contains substantial determinations especially on the basis of an extensive interpretation of the doctrine.

[60] [2007] EWCH 3028
[61] A. Dignam: *Hicks & Goo's Cases and Material on Company Law*, (7th edn), Oxford University Press, Oxford, (2011), p. 127
[62] [2009] UKHL 39
[63] P.L.Davies and S. Worthington: *Gower and Davies Principles of Modern Company Law*,(9th edn), Sweet&Maxwell, London, (2012), p. 223. Also see, *Atlas Maritime Co SA v Avalon Maritime Ltd (The Coral Rose* [1991] All ER 769

II. THE *VTB Capital Plc v Nutritek International Corp & Others* CASE and ITS IMPLICATIONS ON THE PRINCIPLE

In 2007, an English incorporated bank, VTB Capital Plc (VTB) entered into agreements with a Russian Company Russagroprom LLC (RAP). The agreements were regarding a loan and VTB loaned US$225.050.000 to RAP, to enable RAP to buy six Russian dairy companies and three associated companies from Nutritek International Corp (Nutritek). Having paid three interest payments, in 2008, RAP defaulted on the Facility Agreement and was unable to pay the loan anymore. VTB cashed the securities in and could only recover $40.000.000. So, VTB firstly claimed that it was induced into entering into agreements through misrepresentations made by Nutritek and then by asserting that Mr. Konstantin Malofeev was the ultimate owner and controller of the Nutritek, Marshall Capital Holdings (Marcap BVI) and Marshall Capital LLC (Marcap Moscow), sought to amend its pleaded case to contend that RAP's corporate veil should be pierced- with the effect that Mr. Malofeev, Marcap BVI and Marcap Moscow would be treated as jointly and severally liable with RAP for breaches of, and/or otherwise subject to remedies to enforce, two of the agreements.[64]

The mainstay which VTB relied on was the decision of Burton J in *Antonio Gramsci* which concerned the claim due to alleged siphoning of funds by executives of a company by way of establishing façade companies specifically to be used as vehicles to carry out the alleged fraud.[65] It was ruled in *Antonio Gramsci* that the controlling parties using a puppet company as a device to defraud may be sued under breach of contract. Therefore, what VTB was trying to seek was personification of the controlling body within a corporation in order to make that body liable as if it was a party to the contract as allowed in *Antonio Gramsci*.

[64] [2013] UKSC 5 at para 114
[65] Also see the judgement of Burton J in *Alliance Bank JSC v Acquanta Corporation* [2011] EWCH 3281 (Corp)

Firstly, Mr. Justice Arnold in the High Court of Justice in Chancery Division refused to follow *Antonio Gramsci* and said that *Antonio Gramsci* was rather a decision to ignore privity of contract instead of piercing the corporate veil.[66] Having stressed on the characteristics of the principle of piercing the corporate veil, he stated that:

> "*.....where a claim of wrongdoing is made against the person controlling the company, it is ... inappropriate to permit the corporate veil to be lifted to enable the claimant to pursue a contractual claim against that person.*"[67]

Upon the appeal, the Court of Appeal held that the principle of piercing the corporate veil was alive but nevertheless the case before it was not one that could be applied, by stating that,

> *".....we accept that the court can, in an appropriate case, "pierce a company's corporate veil" and, in doing so, substantially identify the company with those in control of it, no authority has been cited to us, apart from Burton J's decisions in Gramsci and Alliance, that supports the proposition that, once the veil is pierced, the court either does or can (or that it is arguable that it does or can) proceed in consequence to a holding either that the puppet company was a party to the puppeteer's contract, or vice versa."*[68]

The point that the Court of Appeal emphasised was the principle of privity of contract. It can be seen in the expression of Lord Lloyd:

> "*Not only do we not regard the common law as recognising the principle for which VTB contends, we are also not persuaded that it would be a*

[66] [2011] EWHC 3107 (Ch) at para 101
[67] [2011] EWHC 3107 (Ch) at para 99 See *Yukong Line Ltd of Korea v Rendsburg Investmensts Corp of Liberia* [1998] 2 BCLC 485; *Ben Ashem v Ali Shayif* [2009] 1 FLR 115;*Dadourian Group International Ltd v Simms* [2006] EWCH 2973; *Lindsay v O'Loughnane* [2010] EWCH 529 (QB)
[68] [2012] EWCA Civ 808 at para 91

principled development of the law for us to recognise it by our decision in this appeal. Any such development would not be a modest development of existing principle. It would, in substance, amount to the adoption by the courts of a jurisdiction to subject parties to contractual obligations under a contract to which neither they, nor the only undisputed parties to the contract, had ever agreed or intended that they should be subject."[69]

Although the court clarified the conditions -which are in regard to the façade to conceal the true facts- to decide in favour of veil piercing, it stated that the principle does not amount to allow claims deriving from breach of contract against a non contracting party even if the non-contracting party is the controller of the contracting party.

The statement of Lord Lloyds shows the importance given to the privity of contract principle. With the decision of the Court of Appeal, it was clarified that the veil piercing doctrine could not be a remedy to make company owners, shareholders or directors party to a contract which the controlled party entered into. This issue also constituted the rejection point of veil piercing in the Supreme Court which upheld the decision of the Court of Appeal.

The Supreme Court, in short, found that VTB's case constitutes extension to the circumstances where traditionally the English Courts had pierced the corporate veil.[70] According to the court, the extension derived from the principle of privity of contract and also contrary to authority as well as to the principle.[71] The court stated that the extension would mean holding the person controlling the company liable as though he had been a co-contracting party, despite the fact that neither he nor any of the

[69] at para 95
[70] [2013] UKSC 5 at para 131
[71] at para 145

contracting parties wanted him to be.[72] Additionally, since the alleged misrepresentation gives birth to tort liability, the Supreme Court expressed that VTB may claim to be compensated due to the alleged fraudulent statements of Mr. Malofeev on the basis of tort liability instead of seeking redress from Mr. Malofeev by way of relying on the veil piercing argument.[73]

The judgement in terms of veil piercing started with consideration of whether there was such a principle where in some circumstances the court should pierce the corporate veil and continued with the reasons why VTB could not succeed in this case. The point which triggered the court to adopt this systematic was the arguments of the defendant in which it was suggested firstly that, there is no such principle and the court in fact can not pierce the corporate veil regardless of whatever has been said concerning veil piercing in previous cases despite the fact that those cases may often be justified on alternative basis; and secondly even though the court can, in principle, pierce the corporate veil, this case is not the case to do so due to the fact that the arguments of VTB represents an illegitimate and unprincipled extension of the circumstances in which the veil can be pierced.[74]

Primarily, Lord Neuberger, who gave the judgement and then unanimously agreed, considered the background of the concept of veil piercing starting from the terms being used to express disregarding the separate corporate personality and obiter made by Lord Keith in *Woolfson* about which his Lordship said that the House of Lords was "*prepared to assume that the power existed"*.[75] Lord Neuberger continued with an explanation of the value given to the circumstances where façade appears by also criticising the expressions as "sham", "mask", "true facts", "cloak", "device", "puppet",

[72] at para 132
[73] at para 146
[74] at para 117
[75] at para 121

and drew attention to the possible confusion and uncertainty that those can cause in the law.[76]

Having seen the argument of the defendant regarding the existence of the doctrine "*worthy of serious consideration*", his Lordship also acknowledged the claimants statement that "*it may be right for the law to permit the veil to be pierced in certain circumstances in order to defeat justice*"[77] via referring to *Adams v Cape* in which the existence of the principle was upheld; *Kensington International Ltd v Republic of Congo*[78] where his Lordship found it difficult to explain the basis of the decision apart from piercing the corporate veil, as well as all the leading textbooks which accept the existence of the principle.[79]

Despite the fact that there has been an opportunity to make clear what the principle really is or whether the doctrine really exists given the obscurity of the concept as explained above, the Supreme Court decided not to go deeper and found it unnecessary to do so in such a case. The reason behind that was stated by Lord Neuberger as:

> "*In my view, it is unnecessary and inappropriate to resolve the issue whether we should decide that, unless any statute relied on in the particular case expressly or impliedly provides otherwise, the court can not pierce the veil of incorporation. It is unnecessary because the second argument raised on behalf of Mr. Malofeev, to which I shall shortly turn, persuades me that VTB can not succeed on this issue. It is inappropriate because this is an interlocutory appeal, and it would therefore be wrong*

[76] at para 124
[77] at para 127
[78] [2005] EWCH 2684 (Comm), [2006] 2 BCLC 296
[79] at para 127

(absent special circumstances) to decide an issue of such general importance if it is unnecessary to do so."[80]

The fact that can be inferred from this statement is that, the Supreme Court left the ambiguity still ambiguous and refrained from making declaratory statements with respect to the existence of the principle, since it found that, assuming that the principle exists given the circumstances where the veil piercing is traditionally held in English Law, this case constitutes an extension.[81]

The key point here is that the Supreme Court has assumed the existence of the doctrine and defined what constitutes the extension in light of traditionally held veil piercing cases. The extension in the eyes of the court was the attempt to hold a controlling body behind a company, which entered into a contract, directly liable as a co-contractor from a breach of contract.

One of the basic principles of common law is that, "*a contract could not effectively confer rights or impose duties on those who are not parties to it*"[82] which is termed as "privity of contract". The Supreme Court stressing on this basic principle, decided that Mr. Malofeev and the other defendants who are not a signatory to a contract which is breached can not be liable from it even though the contracting company had allegedly been used for fraudulent purposes.[83] Lord Neuberger stated that such an extension "*receives no support from any case*" save for the decision in *Antonio Gramsci* and none of the judgements that VTB relied on was "*on analysis, of assistance to its case*.[84]

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[80] at para 130
[81] at para 132
[82] R. Goode and E. McKendrick: *Goode on Commercial Law*, (4th edn), Penguin Boks, London, (2010), p. 113 Also see, *Tweedle v Atkinson* (1861) 1 B & S 393
[83] at para 132
[84] at para 133

Based on the cases which were relied on by VTB, the court examined the well known cases such as *Gilford Motor v Horne* and *Jones v Lipman*, and found that "*the decisions can not have been based on piercing the corporate veil*" on the grounds that there was nothing that company has been involved in.[85]

Antonio Gramsci case, which was the only decision that the Supreme Court found supportive to the arguments of VTB, was about a fraudulent manoeuvre within the charterparty contracts. The ruling was regarded as quite contrast with the aim behind the ruling of *Salomon* and the principle of "privity of contract"[86], and in fact, has raised the debate on the scope of the principle which had already been very uncertain. Lord Neuberger as the reason for overruling the *Antonio Gramsci*, stated that:

> "*I think the reasoning in the case involved a misrepresentation of the decisions in Gilford and Jones. It seems to me that the conclusion in Gramsci was driven by an understandable desire to ensure that an individual who appears to have been the moving spirit behind a dishonourable (or worse) transaction, action, or receipt should not be able to avoid liability by relying on the fact that the transaction, action or receipt was effected through the medium (but not agency) of a company But that is not on any view enough to justify piercing the corporate veil for the purpose of holding the individual liable for the transaction, action, or receipt especially where the action is entering into a contract*".[87]

According to the court, there was an "*overwhelming case*" against the proposal of VTB to decide upon extension of the principle. Although the Supreme Court assumed the existence of the principle and decided on the basis of the assumption, the

[85] at para 134 and 135
[86] B. Hannigan: *Company Law*, (3rd edn), Oxford University Press, Oxford, 2012, p. 46
[87] at para 147

court stressed the principle established in *Salomon* and stated that "*strong justification would be required before the court would be prepared to extend it*".[88]

The point of Lord Neuberger is that, he found the claim to hold Mr. Malofeev severally and jointly liable with the contracting party RAP contrasting with the decision and reasoning of *Salomon* via emphasising the existence of agency law within the context of running a company as a natural result.[89] As His Lordship stated by citing the unique case *Smith v Hughes*[90] in which the importance is given to the objective interpretation of the contracting party's action:

> "*In any event, it would be wrong to hold that Mr. Malofeev should be treated as if he was a party to an agreement, in circumstances where (i) at the time the agreement was entered into, none of the actual parties to the agreement intended to contract with him, and he did not intend to contract with them and (ii) thereafter, Mr. Malofeev never conducted himself as if or led any other party to believe, he was liable under the agreement. That is the right approach seems to me to follow from one of the most fundamental principles on which contractual liabilities and rights are based, namely what an objective reasonable observer would believe was the effect of what the parties to the contract, or alleged contract, communicated to each other by words and actions, as assessed in their context*".

Another aspect that the Supreme Court touched upon while refusing the proposal to extend the scope of the principle was in regard to the existence of another remedy which is available for the claimant in order to be compensated. The court found it more difficult to justify the extension where the claimant did not really need to seek

[88] at para 137
[89] at para 136
[90] (1871) LR 6 QB 597

indemnity from Mr. Malofeev. The reason behind this was the existence of the remedy for VTB in tort. As the claimant asserted that it was induced to enter into agreements through misrepresentation made by Nutritek and this allegation could easily be enough to sue Mr. Malofeev for damages within the scope of tort liability, the court did not see any necessity for extension.[91]

Lord Neuberger also rejected the argument that the contracting party RAP was being used as "*a façade to conceal true facts*". As he said:

> *In my view, if the corporate veil is to be pierced, "the true facts" must mean that, in reality, it is the person behind the company, which is the relevant actor or recipient (as the case may be). Here, on VTB's case, "the true facts" relate to the control, trading performance, and value of the Dairy Companies (if one considers the specific allegations against Mr. Malofeev), or to the genuineness of the nature of the underlying arrangement (which involves a transfer of assets between companies in common ownership). Neither of these features can be said to involve RAP being used as a "façade to conceal true facts*".[92]

The expression that the claimant used "*abusing the corporate structure*" is also regarded as nothing that can be added to the debate.[93] The court, without giving any meaning to the phrase, found the argument an illegitimate extension of the situations where the corporate veil can be pierced.

Although the case was mostly about a jurisdiction, *forum non-conveniens,* issue, the decision and reasoning touched upon the important aspects of naturally obscure veil piercing doctrine in English Law. The Supreme Court, for the first time, had the chance to evaluate the principle and despite the fact that no clarifying approach was adopted

[91] at para 146
[92] at para 142
[93] at para 143

since it was found to be unnecessary in such a case, demonstrated that the principle of separate corporate personality is still sound.

Given the history of the principle of piercing the corporate veil, inconsistent decisions in terms of the scope of it are not unknown. However, after *Antonio Gramsci,* the application of the principle, which had not been so clear fundamentally, stepped into another phase. This phase was opened to make the controller(s) of the company directly liable from the contracts which the controlled company entered into. The decision in *Antonio Gramsci* basically contrasted with not only the spirit of the principle of separate corporate personality, but also with the principle of privity of contract. Eventually and unsurprisingly, the Supreme Court, by considering whether the person behind the contracting company treated it as if it were a co-contractor, overruled the *Antonio Gramsci* and closed the door to any claim which may aim to hold the controller of the company directly liable from contracts of that company. In other words, no doubt remained after *VTB v Nutritek* that the veil piercing doctrine can not be a remedy to make any of the shareholders party to a contract which the company entered into.

Apart from overruling the *Antonio Gramsci* case and rotating the assumed principle to its traditional base again, the Supreme Court left many questions ambiguous with respect to both the meaning of the principle of piercing the corporate veil and circumstances in which the principle can be invoked. The reason for that was the court's assumption on the existence of the veil piercing principle due to the over-extensive nature of the claim of the claimant under the facts of the case. Therefore it can be said that, although the court did not take the opportunity to explain the principle, in order to explain the reasons of the extensive nature of the claim, it determined what the principle is really not, by rejecting to hold the controller of the company liable from breach of contract.

It must also be noted that, while the judgement in the Supreme Court did not provide that much guidance in terms of the principle, the decision of the Court of Appeal in the case was more explanatory in terms of the veil piercing. For instance, upon the submission of the defendant regarding the existence of the principle, the court disagreed with the opinion that "*there is no such principle as piercing the veil*" [94] and by citing Lord Keith's statement in *Woolfson* which stated that, "*we do not consider that it is open to this court to question the veil piercing principle*".[95]

Even though the precise nature of the principle has not been made that much of a subject of discussion in the Supreme Court, by comparison with the decision of the Court of Appeal, the obiter of Lord Neuberger in the Supreme Court was of great value as the reasoning of overruling the *Antonio Gramsci.* His Lordship remarked that piercing the veil is a last resort remedy which should be invoked when there is no other remedy available. This point of view can be inferred from the explanation of his Lordship regarding the unnecessary nature of the proposed extension. According to Lord Neuberger, the extension was more difficult to justify due to the fact that the remedy in tort was available for VTB.

Another point that needs to be stated is the perception of Lord Neuberger with respect to the basis of the well-known veil piercing cases *Jones v Lipman* and *Gilford Motor Co v Horne.* His Lordship indicated that those cases could be explained in other basis but veil piercing. The reason for his Lordship's argument was the company's non-involvement to any "concealment of true facts". Having taken into account the meaning his Lordship has given to the phrase "true facts" in his judgement and not describing the acts of the defendants as evasion, agreeing with that perception is not easy. The reason

[94] at para 48
[95] at para 49

for not agreeing with that argument is the evasive characteristics of the defendant's actions in order to get free from pre-existing contractual obligations in those two cases.

As explained by Lord Sumption in *Prest v Petrodel* which is the latest and leading case by reason of the decision given regarding both the existence and scope of the principle of piercing the corporate veil:

> "*it is that the court may disregard the corporate veil if there is a legal right against the person in control of it which exists independently of the company's involvement, and a company is interposed so that the separate legal personality of the company will defeat the right or frustrate its enforcement*".[96]

The *Prest v Petrodel* is a landmark case in which the Supreme Court, five months after the *VTB v Nutritek* ratified the existence of the principle and determined the scope of it. Having surveyed the authorities on the concept, the court held that on very limited occasions the veil piercing doctrine can be invoked. It would never be wrong to say that, the Supreme Court, by stressing the evasive actions, lead the scope of the doctrine to the clearest point. As the court put it:

> "*….there is a limited principle of English Law which applies when a person is under an existing legal obligation or liability or subject to an existing legal restriction which he deliberately evades or whose enforcement he deliberately frustrates by interposing a company under his control. The court may then pierce the corporate veil for the purpose, and only for the purpose, of depriving the company or its controller of the advantage that they would otherwise have obtained by the company's separate legal personality*".[97]

[96] at para 28
[97] at para 35.

CONCLUSION

In this article, by way of briefly touching on the history of the veil piercing doctrine, the first Supreme Court decision containing examinations regarding the doctrine has been analyzed. Although the case was mostly about a jurisdiction issue and so much so that the veil piercing argument has been put forward to create a jurisdiction by the claimant; with the challenge of the defendant regarding the existence of the principle of piercing the corporate veil, the Supreme Court, even though in limited basis, made mention of the principle and instead of stating what the principle is, stated what the principle is not.

Due to the fact that the court found no solid base for the claimant to pierce the corporate veil, it denied determining whether the principle exists. From this aspect, it can be said that the court did not take the opportunity to disambiguate the naturally ambiguous principle. On the other hand, the determinations made, by assuming the existence of the principle, are of high value.

With the decision, the court ratified the separate corporate personality principle established in *Salomon* and stressed on the privity of contract. The most important conclusion that can be inferred from the decision is that, even though the principle exists, its limits can not go as far as holding the controlling body of a company directly liable from the contracts of the company controlled. In other words, the concept of making a person behind jointly and severally liable with the company itself is found incoherent with the rationale behind the principles of separate corporate personality as well as privity of contract.

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