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INTERNALIZATION OF COSTS TO CORPORATE GROUPS: PART-WHOLE RELATIONSHIPS, HUMAN RIGHTS NORMS AND THE FUTILITY OF THE CORPORATE VEIL

*Dr. Kiarie Mwaura**

INTRODUCTION

Corporations conduct their business activities through a variety of business structures including, among others, wholly owned subsidiaries, partially owned subsidiaries, and affiliate corporations.¹ In the event that a parent corporation controls the subsidiary or affiliate corporations, it may easily influence them to pursue profits through activities that violate human rights. In such cases, the parent corporation may still avoid liability because entity law deems the two corporations to be separate entities. This obstacle of separate legal personality enables entities within a corporate group to enjoy the privileges of limited shareholder liability and, therefore, allows parent companies² to avoid accountability for human rights. This may arise, for instance, when a corporate group utilizes an undercapitalized foreign subsidiary to conduct risky business that poses a threat to human rights. When corporate structures are manipulated in this manner, tort and human rights victims³ end up bearing the cost of harmful

* Associate Dean, School of Law, University of Nairobi. The author wishes to thank the Human Rights Program at Harvard Law School for offering him a Visiting Fellowship, which made it possible to research and write up this article. Thanks are also due to staff at the Harvard's Human Rights Program, Edwin Abuya, David Capper, Brice Dickson, Tom Hadden and Andrew Keay for their informed comments and discussions. The usual caveat applies.

¹ See CYNTHIA WALLACE, *THE MULTINATIONAL ENTERPRISE AND LEGAL CONTROL: HOST STATES SOVEREIGNTY IN AN ERA OF ECONOMIC GLOBALIZATION* 102 (2nd ed. 2002). An affiliate corporation is a corporation that is associated with another. If a parent corporation has controlling interests in the affiliate, then the affiliate can be referred to as a subsidiary. If a parent corporation has no controlling or majority interests in the affiliate corporation, then it can be referred to as an associate. *Id.*

² See *id.* at 102, 171. The term parent corporation refers to a corporation that owns and controls other foreign affiliated corporations in two or more host states.

³ See *Vortex Fishing Sys., Inc. v Foss*, 38 P.3d 836, 841 (Mont. 2001). The violation of all human rights could form the basis of a claim under the tort of intentional infliction of emotional distress. In the United States, for example, the Montana Supreme Court has held that the standards that a plaintiff needs to satisfy in order to get damages for emotional distress under a human rights claim are much lower than those of tort. Under tort law, a plaintiff must suffer a substantial invasion of a legally protected interest, such that no reasonable person should be expected to endure it, in order to win damages. This standard is not applicable in human rights claims. It is also worthy of note that torts that have the required level of severity could also breach a variety of human rights, including the right not to be subjected to torture or cruel, inhuman or degrading treatment, the right to life, the right to liberty and security of the person etc. The rights whose violations lead to common tortious claims include, for example, freedom from torture (torture of protestors and workers), right to life (harassment of workers leading to death), environmental rights (nuisance arising from exposure to industrial toxics), liberty and security of the person, abolition of slavery and forced labour, freedom of movement (false imprisonment), right to work (economic torts arising from interference with trade or business) etc. Those which might not necessarily lead to obvious tortious claims (but which could still fall under the tort of intentional infliction of emotional distress) include, for example, right to organise and participate in collective bargaining, right to a fair trial, right to marry and form a family, right to political life, right to privacy, right to education, right to social security, right to non discrimination, right to equal pay, right to just and favourable remuneration. Research has shown that all categories of internationally recognized rights can be affected by corporate conduct. For more on

corporate activities, especially when they are left uncompensated. This amounts to externalization of business costs to victims and would, generally, be seen as an inefficient way of conducting business. However, some neo-classical economists argue, from a utilitarian standpoint, that victims stand to gain even when they are left uncompensated given that they eventually benefit from an increase in affordable goods and services that arise as a result of economic expansion.⁴ This view, however, is unjustifiable from a human rights standpoint because states have obligations, under international human rights law, to provide *ex ante* measures to prevent the occurrence of human rights violations in the first place⁵ as well as effective *ex post* measures to address violations when they occur.⁶ In view of this, it could be argued that regulations that incentivize corporations to disregard human rights cannot be socially efficient or human rights compliant. Cognizant of their duty under international human rights law, states that have withstood the worst of corporate misconduct are increasingly reforming their constitutions to impose human rights norms on corporations. In Africa, for instance, a growing number of countries, such as Kenya,⁷ Malawi⁸, Gambia,⁹ Ghana,¹⁰ South

this, see JOHN RUGGIE, BUSINESS & HUMAN RIGHTS RESOURCE CENTRE, PROTECT, RESPECT AND REMEDY: A FRAMEWORK FOR BUSINESS AND HUMAN RIGHTS, 14-15, <http://www.reports-and-materials.org/Ruggie-report-7-Apr-2008.pdf> (last visited 10 July 2011); JANET DINE, COMPANIES, INTERNATIONAL TRADE AND HUMAN RIGHTS 72 (2005).

⁴ Stephen Presser, *Thwarting the Killing of the Corporation: Limited Liability, Democracy, and Economics*, 87 NW. U. L. REV. 148, 178 (1992).

⁵ International Covenant on Civil and Political Rights, art. 2, Dec. 16, 1966, 999 U.N.T.S. 171 (requiring states to “take the necessary steps, in accordance with its constitutional processes and with the provisions of the present Covenant, to adopt such laws or other measures as may be necessary to give effect to the rights recognized in the present Covenant”).

⁶ *Id.* at art. 3 (a) (requiring states “[t]o ensure that any person whose rights or freedoms as herein recognized are violated shall have an effective remedy.”). See also International Covenant on Economic, Social and Cultural Rights, art. 2, Dec. 16, 1966, 993 U.N.T.S. 3; Basic Principles and Guidelines on the Right to a Remedy and Reparation for Victims of Gross Violations of International Human Rights Law and Serious Violations of International Humanitarian Law, G.A. Res. 60/147, art. 1(c), 3(a), U.N. Doc. A/Res/60/147 (Dec. 16, 2005), available at <http://www1.umn.edu/humanrts/instree/res2005-35.html> (last visited Dec. 7, 2010).

⁷ CONSTITUTION, art. 20 (1) (2010) (Kenya) (stating that the “Bill of Rights applies to all law and binds all state organs and all persons”).

⁸ Constitution of the Republic of Malawi (1995), ch. 4, art. 15(1) (providing that “[t]he human rights and freedoms enshrined in this Chapter shall be respected and upheld by the executive, legislature and judiciary and organs of the Government and its agencies and, where applicable to them, by all natural and legal persons in Malawi and shall be enforceable in the manner prescribed in this Chapter.”).

⁹ Constitution of the Republic of Gambia (1997), ch. 4, art. 17(1) (stating that “[t]he fundamental human rights and freedoms enshrined in this Chapter shall be respected and upheld by all organs of the Executive and its agencies, the Legislature, and, where applicable to them, by all natural and legal persons in The Gambia, and shall be enforceable by the Courts in accordance with this Constitution.”).

¹⁰ Constitution of the Republic of Ghana (1992), ch. 5, art. 12(1).

The Ghanaian Constitution stipulates:

The fundamental human rights and freedoms enshrined in this chapter shall be respected and upheld by the Executive, Legislature and Judiciary and all other organs of government and its agencies and, where applicable to them, by all natural and legal persons in Ghana, and shall be enforceable by the Courts as provided for in this Constitution.

Id.

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Africa,¹¹ have incorporated such human rights norms into their constitutional bill of rights. It is doubtful, however, whether these constitutional norms as well as other domestic measures could achieve their intended objectives given the reluctance of home states to extend extraterritorial liability to corporations within their territories as well as the failure of the norms to address the obstacle of separate legal personality within corporate groups.

The first objective of this Article is to assess the extent to which entity law undermines the protection of human rights by incentivizing corporations to disregard human rights concerns. The Article argues that the concept of separate legal personality within corporate groups encourages corporations to disregard human rights concerns and calls for its revision. It calls for the adoption of an enterprise liability approach for ascribing human rights and tortious liability within equity based corporate groups¹² so as to expose the entire corporate group to liability. Secondly, the Article examines whether the suggested enterprise liability approach could adequately deal with extraterritorial corporate human rights violations and argues for the adoption of an international convention that would oblige states to replace principles of entity law with those of enterprise law. It argues that the suggested enterprise principles should be constitutionally entrenched, where possible, in order to guard against their erosion. This holistic approach and the resultant risk of liability borne by the entire group could compel corporate boards to adopt policies that are geared towards avoiding human rights violations in the first place.

The first section considers the rationale for the doctrine of separate legal personality as well as the rationale for constitutional regulation of corporate conduct. The second part analyzes corporate and procedural constraints to human rights protection and relies on court decisions from the United Kingdom, Kenya, and United States, to show how far reaching the constraints are. The third part considers how domestic legal reform measures could overcome the constraints identified in the second part and the fourth part offers some conclusions.

I. THEORETICAL FRAMEWORK

A. The Rationale for the Doctrine of Separate Legal Personality

The ability of one corporation to hold shares in another creates a situation of majority and minority share-ownership. This often creates potential for abuse, as one group may, for instance, control the other and influence it to make decisions that have detrimental repercussions.¹³ In such cases, the group with majority share ownership may still avoid liability because entity law deems the two companies to be separate entities. This, sometimes, enables corporate groups to utilize corporate structures that allow them to avoid antitrust, monopoly, and tax regulations by, for instance, transferring profits from high tax jurisdictions to low tax

¹¹ S. AFR. CONST., 1996 (stating that “[a] provision of the Bill of Rights binds a natural or a juristic person if, and to the extent that, it is applicable, taking into account the nature of the right and the nature of any duty imposed by the right.”).

¹² See generally PETER T. MUCHLINSKI, *MULTINATIONAL ENTERPRISES AND THE LAW* 52-55, 317 (2nd ed., 2007). The paper focuses on equity based corporate groups as opposed to contractual forms of corporate groups. Whilst the former includes all corporations that are linked by shares, the latter are linked by contracts and could include, for example, corporations linked by distribution and production agreements as well as public private partnerships.

¹³ See generally *id.* at 45-79 (highlighting the different business structures that transnational corporations might adopt).

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ones.¹⁴ As a result of this, rules exist to regulate relationships within corporate groups in a variety of contexts including, tax law, criminal law, private international law, and corporate law.¹⁵

In the context of corporate law, the corporate veil separating a corporation from its individual or corporate shareholders allows the corporation to enjoy the privileges of limited liability.¹⁶ A parent corporation cannot, therefore, be held liable for acts of its subsidiary because the two companies are considered as two separate entities. It is, however, a common feature of most legal systems to, sometimes, look behind the corporate structure and classify a set of companies as one in order to attach liability for a culpable action.¹⁷ As will be seen in the next section, this may happen when a holding corporation is directly or indirectly in control of the subsidiary. However, the absence of precise corporate rules to determine when a court may disregard the separate personality rule within a corporate group creates loopholes that enable corporations to use strategic corporate structures in order to avoid liability. This offers incentives to corporate groups to invest in very risky ventures as well as to undercapitalize the subsidiaries operating in those areas so that the group can reduce its exposure to liability.¹⁸ By doing so, they externalize social costs to other non-shareholder actors, a fact that gives rise to inefficiency as the risk of loss does not pose a threat to any corporate actors (especially shareholders and managers).¹⁹

The negative effect of limited liability on tort and human rights victims differs significantly from its effects on contractual parties, such as creditors. Although the risk and potential loss is also transferred to creditors when they lend money to a corporation, they are often in a more favourable position than involuntary creditors because they enter into the contractual relationship voluntarily and with full knowledge of the risks involved. They, therefore, get the opportunity to insert protective clauses in the contracts and to, sometimes, charge high interest rates and risk premiums, hence reducing the negative consequences of limited liability. This allows for the internalization of the corporation's costs to the creditor and the contractual arrangement between the two can, be regarded as being economically efficient.²⁰

¹⁴ T. Hadden, *Regulating Corporate Groups: An International Perspective*, in *Corporate control and accountability: Changing Structures and the Dynamics of Regulation* (Joseph McCahery, Sol Picciotto & Colin Scott eds., 1993), 360.

¹⁵ For a detailed analysis of the different forms of regulations, see T. Hadden, *Liabilities in Corporate Groups: A Framework for Effective Regulation*, *Atti Del Convegno Sui Gruppi Organizzati dalla Rivista delle Società*, Novembre 1995 (Milano: Giuffrè, 1996), 1362-1378.

¹⁶ *Salomon v. Salomon*, [1897] A.C. 22 (H.L.) 51 (U.K.).

¹⁷ *Littlewoods Mail Order Stores Ltd. v. Inland Revenue Comm'rs*, [1969] 1 W.L.R. 1241, [1254] (U.K.). Reacting to the decision in *Salomon*, A.C. 22 (H.L.) at 51, which established the theory of legal separation of a corporate entity and its owners, Lord Denning MR observed: "The doctrine laid down in *Salomon v. Salomon & Co.* [1897] A.C. 22, has to be watched very carefully. It has often been supposed to cast a veil over the personality of a limited company through which the courts cannot see. But that is not true. The courts can and often do draw aside the veil. They can, and often do, pull off the mask. They look to see what really lies behind. The legislature has shown the way with group accounts and the rest. And the courts should follow suit."

¹⁸ See Henry Hansman & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879, 1882-83 (1991).

¹⁹ See John A. Siliciano, *Corporate Behavior and the Social Efficiency of Tort Law*, 85 MICH. L. REV. 1820, 1838-40 (1987).

²⁰ See David W. Leeborn, *Limited Liability, Tort Victims, and Creditors*, 91 COLUM. L. REV. 1565, 1584 (1991).

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As a result of this, lifting the corporate veil to protect voluntary creditors is thought to be improper, unless their decision to enter into a contractual relationship with the corporation has been influenced by misrepresentation or fraud.²¹ In contrast, tort and human rights victims are considered as deserving legal protection because they can neither monitor the activities of the corporation nor contract out to avoid potential risks.²² As a result, the shifting of social costs of the business to them is regarded as being an inefficient way of allocating resources.²³

Justifications for the concept of limited liability have also centered on the role it plays in enabling states to increase investments and, therefore, create wealth and enhance economic growth.²⁴ This is thought to be so because limited liability allows for investments to be made without risking loss beyond the amount invested²⁵ and, as a result, incentivizes corporations to be more entrepreneurial. Examples of benefits gained from entrepreneurship are thought to be payment of taxes and the provision of economic and social services, such as employment and transportation. It is also thought to play an important role in wealth creation by facilitating the operation of the capital markets where sellers and buyers exchange securities freely without the fear of incurring any personal liability for the conduct of the corporation.²⁶

Although limited liability is thought to play an important role in allowing investors to invest in risky projects that provide greater returns as well as to diversify their investments in a variety of corporations so as to minimize the risks that would arise from a single investment, its role in this respect appears to be exaggerated because corporate groups are not likely to cease investing in risky projects if they faced unlimited liability given that they could easily diversify their investments in order to reduce risks. Indeed, they might even diversify more and also make more efficient investment decisions so as to reduce the increased risk of loss.²⁷ Similarly, in the context of the role that limited liability plays in facilitating the operation of a liquid stock market, it is unlikely to have much effect on this because unlimited liability would only be exposed to corporate shareholders rather than individuals.²⁸

The extension of liability to dominant parent companies is, sometimes, objected to on the premise that corporate groups would shun high-risk business, which would then be conducted by corporations that are held directly by individuals who enjoy limited liability.²⁹ Easterbrook and Fischel are of the view that group liability would give competitive advantage to unaffiliated firms and, therefore, make corporate groups disintegrate into small firms. This, they argue, would make tort victims worse off because larger firms are more likely to have

²¹ See Richard A Posner, *The Rights of Creditors of Affiliated Corporations*, 43 U. CHI. L. REV. 499, 499-500 (1976).

²² See Leebron, *supra* note 20, at 1589-91.

²³ David Millon, *Piercing the Corporate veil, Financial Responsibility, and the Limits of Limited Liability*, 56 EMORY L. J. 1305, 1316-17 (2007).

²⁴ See Presser, *supra* note 4, at 163.

²⁵ See Edwin M Dodd, *The Evolution of Limited Liability in American Industry*, 61 HARV. L. REV. 1351, 1356 (1948).

²⁶ See *id.* at 1378-79.

²⁷ Richard A. Booth, *Limited Liability and the Efficient Allocation of Resources*, 89 NW. U. L. REV. 140, 148 (1994).

²⁸ Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability and the Corporation*, 52 U. CHI. L. R. 89, 111 (1985).

²⁹ See *id.*

more insurance for compensating victims.³⁰ However, this is not necessarily the case because, as Leebron points out, corporate groups are unlikely to shun such risky ventures if the cost of liability that they face could be offset by the profitability of conducting the business as a group.³¹

It is often the case that limited shareholder liability offers immense incentives to corporate groups to undercapitalize subsidiaries operating in high risk areas because their liability cannot be extended to others in the group.³² Although doing so might have very negative consequences for tort and human rights victims, some scholars of law and economics consider such transactions to be Kaldor-Hicks efficient because the net gains are seen to be greater than the net loss.³³ Some of the gains are considered to be the avoidance of agency costs that would arise from the monitoring of management by investors in the event that there was unlimited liability, a factor that is seen as having the potential of dissuading investors from investing in a corporation.³⁴ Having limited liability is also seen as a prudent way of avoiding agency costs that would arise if investors were to monitor other investors whose activities pose a risk to them.³⁵ Whilst there might be a stronger case for these arguments in the context of single entity corporations that are keen to attract human investors, the agency costs arising when one corporate entity monitors another are not necessarily undesirable because they can easily be offset by the extra returns that corporations get as a result of monitoring an investee corporation. Indeed, research has shown that corporate shareholders (institutional investors) are not necessarily averse to monitoring the management of investee corporations because they are increasingly recognizing the benefits to be derived from being a proactive corporate investor. For this reason, institutional investors in the United Kingdom, for example, have been playing a more proactive monitoring role since the early 1990s³⁶ and the government has keenly encouraged this practice by issuing a number of corporate governance policy documents which have clearly linked the monitoring of investee corporations with enhanced standards of corporate governance and profits.³⁷ It is noteworthy that before the

³⁰ *Id.*

³¹ See Leebron, *supra* note 20, at 1574, 1589.

³² See Hansman & Kraakman, *supra* note 18, at 1882-83.

³³ See generally John R. Hicks, *The Valuation of the Social Income*, 7 *ECONOMICA* 105, 111 (1940); See generally Nicholas Kaldor, *Welfare Propositions of Economics and Interpersonal Comparisons of Utility*, 49 *ECON. J.* 549, 550 (1939).

³⁴ See Easterbrook & Fischel, *supra* note 28, at 94.

³⁵ *Id.* at 95.

³⁶ JILL SOLOMON, *CORPORATE GOVERNANCE AND ACCOUNTABILITY* 118 (2007).

³⁷ See THE COMM. ON THE FIN. ASPECTS OF CORP. GOVERNANCE, THE REPORT OF THE COMMITTEE ON FINANCIAL ASPECTS OF CORPORATE GOVERNANCE 50 (1992) (U.K.) ("Given the weight of their votes, the way in which institutional shareholders use their power to influence the standards of corporate governance is of fundamental importance. Their readiness to do this turns on the degree to which they see it as their responsibility as owners, and in the interest of those whose money they are investing to bring about changes in companies when necessary, rather than selling their shares."); see THE CADBURY REPORT, THE REPORT OF THE COMMITTEE ON FINANCIAL ASPECTS OF CORPORATE GOVERNANCE 50 (1992). Other policy documents have encouraged institutional investors to play an active role in corporate governance. See generally HER MAJESTY'S TREASURY, MYNERS PRINCIPLES FOR INSTITUTIONAL INVESTMENT DECISION-MAKING: REVIEW OF PROGRESS (2004), available at http://www.hm-treasury.gov.uk/d/myners_principles_web.pdf; The Institutional Shareholders' Committee, The Responsibilities of Institutional Shareholders and Agents: Statement of Principles (Sept. 2005), <http://www.ivos.co.uk/institutionalshareholderscommittee/responsibilities.aspx>; DEREK HIGGS, REVIEW OF THE ROLE AND EFFECTIVENESS OF NON-EXECUTIVE DIRECTORS (2003), available at <http://www.dti.gov.uk/files/file23012.pdf>.

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introduction of the concept of limited shareholder liability in the United Kingdom in 1855, shareholders also played a very active role in governance of their investee corporations by attending meetings and debating corporate policies so as to improve standards of corporate governance, which ultimately lead to good returns.³⁸ They were, therefore, less concerned with the avoidance of agency costs.

Investors that are keen to avoid any monitoring costs might still be able to do so in an unlimited liability regime by implementing administrative policies that could help the entire enterprise avoid engaging in harmful activities in the first place. The agency costs for monitoring the management could also be reduced by having insurance cover for corporate conduct and having rules on proportional liability, where liability could be distributed on the basis of share ownership. The latter could reduce monitoring costs because shareholders are unlikely to be concerned with monitoring that they are not likely to be liable for.³⁹ The failure to reduce avoidable agency costs by utilizing any of the above mechanisms gives rise to inefficiency because it amounts to coercive transfer of costs to individuals.⁴⁰

As a result of the insufficiency of economic justifications for limited liability, Presser offers a historical justification for the concept and says that it was devised to “further economic progress and to maximise state wealth through encouraging investment.”⁴¹ He also observes that its key objective was to encourage individuals to invest in small firms and, because of this, it was a democratic tool aimed at assisting small investors, rather than wealthy ones. This was thought to be the case because only the very wealthy could invest in shares that came with unlimited liability.⁴² It was also felt that a majority of states in the United States could not have achieved the economic progress that they needed in the nineteenth century without the input of small investors.

As a result of the role that the rule of limited shareholder liability plays in encouraging investment, Presser justifies its preservation even within corporate groups. This argument, however, overlooks the historical development of limited liability in the context of corporate groups. The concept of limited liability was devised long before corporations were allowed to own shares in other corporations. According to Blumberg, the very first corporations, which provided profitable public services, operated with unlimited liability in the United States until 1885 when limited liability was introduced to protect individuals who had invested in those corporations. During this time, however, corporations were not allowed to hold shares in other corporations. This remained the case until 1889 when New Jersey allowed corporations to hold shares in other corporations, hence creating, for the first time, the structures of holding companies or corporate groups. Despite the development of the concept of limited shareholder liability well before the emergence of corporate groups, the privileges of limited liability were extended to corporate groups when they emerged. They could therefore limit their liability the same way that individual investors could.⁴³ Similar developments were observed in the United Kingdom where the Limited Liability Act 1855 was introduced to protect indi-

³⁸ Len Sealy, *Perception and Policy in Company Law Reform*, in DAVID FELDMAN & FRANK MEISEL, *CORPORATE AND COMMERCIAL LAW: MODERN DEVELOPMENTS* 25 (1996).

³⁹ See Hansman & Kraakman, *supra* note 18, at 1906.

⁴⁰ JANET DINE, *THE GOVERNANCE OF CORPORATE GROUPS* 13 (2000).

⁴¹ See Presser, *supra* note 4, at 163.

⁴² *Id.*

⁴³ See generally PHILLIP I. BLUMBERG, *THE MULTINATIONAL CHALLENGE TO CORPORATION LAW: THE SEARCH FOR A NEW CORPORATE PERSONALITY* 3-19 (1993).

vidual investors rather than corporate ones. It can, therefore, be seen that corporate groups are still exploiting a concept that was not intended for their use to shield themselves from liability.

B. The Rationale for Constitutional Regulation of Corporate Conduct

As subjects of international law, states shoulder the responsibilities for protecting human rights. For this reason, they have a duty to prevent human rights violations by third parties (corporations). Where states fail to discharge this duty effectively, corporations operate without regard to international human rights standards in the course of their business and they often regard themselves as economic actors with no other motives apart from profit maximization. However, the growth of shareholder and consumer activism has led some to consider human rights concerns, especially when negative reputation threatens their profits. These measures have, however, been insufficient to contain corporate human rights abuses because corporations tend to ignore human rights concerns when there is no negative press or when they can creatively utilize corporate social responsibility mission statements and policy documents, as public relations tools, to disguise their human rights violations.⁴⁴ This remains the key problem afflicting the effectiveness of voluntary measures for regulating corporate conduct, including the UN Global Compact Principles and the OECD Guidelines for Multinational Corporations.⁴⁵

Despite the absence of a regulatory mechanism at the international level, states can, and sometimes do, impose human rights obligations on corporations which they must respect.⁴⁶ As such, it is not questionable whether corporations can bear human rights obligations. What remains controversial is whether they should be subject to constitutional scrutiny or private law; how states that are reluctant to regulate their corporations should be dealt with; and the extent to which they should respect and protect human rights violations given that states also have similar responsibilities.

A state seeking to prevent human rights violations by third parties has a variety of options open to it. It could, for example, choose to: ratify the International Covenant on Civil and Political Rights 1966 (ICCPR)⁴⁷ and accept responsibility for guaranteeing human rights within its jurisdiction (vertical effect);⁴⁸ subject the conduct of non state actors to a private

⁴⁴ See CHRISTIAN AID, *BEHIND THE MASK: THE REAL FACE OF CORPORATE SOCIAL RESPONSIBILITY* 3 (2004), available at <http://baierle.files.wordpress.com/2007/11/behind-mask.pdf>.

⁴⁵ See generally U.N. Global Compact, *The Ten Principles*, <http://www.unglobalcompact.org/AboutTheGC/TheTenPrinciples/index.html> (last visited 10/28/11); See generally Org. for Econ. Co-operation and Dev., *OECD Guidelines for Multinational Enterprises* (2008), <http://www.oecd.org/dataoecd/56/36/1922428.pdf>.

⁴⁶ See *Factories and Other Places of Work (Repealed) Act, 1951*, pmbl. (Kenya), available at http://www.kenyalaw.org/kenyalaw/klr_home/ (Search "Factories and Other Places of Work (Repealed) Act"; then follow "SEARCH" hyperlink).

⁴⁷ International Covenant on Civil and Political Rights, *supra* note 5, at art. 2 (requiring states "to take the necessary steps, in accordance with its constitutional processes and with the provisions of the present Covenant, to adopt such laws or other measures as may be necessary to give effect to the rights recognized in the present Covenant").

⁴⁸ According to the natural law theory, the social contract that was negotiated between the state and individuals gave the state the responsibility to protect individuals from the violation of human rights and individuals, in turn, pledged allegiance to the state. It is noteworthy that there were no powerful private entities at that time and, therefore, the natural law theorists, perhaps, did not consider private persons, such as corporations, as posing any threats to individual's rights. As a result of this, the first bills of rights to be drafted recognized only vertical application of human rights. See generally *THE DECLARATION OF INDEPENDENCE* (U.S. 1776); ENGLISH

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law that gives effect to a constitutional right (indirect horizontal effect);⁴⁹ or even subject the conduct of non state actors to direct constitutional scrutiny (direct horizontal effect).

The suitability of any of these options has been a cause of disagreement for scholars of constitutional law.⁵⁰ Although a detailed analysis of the options is beyond the scope of this Article, a brief account of the rationale for direct horizontality of constitutional law will explain why it could be the most appropriate method for regulating corporate conduct in the context of developing states (host states).

The campaign for direct horizontal effect, especially in Africa, has been triggered by the changing power dynamics between the private person and the state. An increase in corporate power as well as its corresponding negative impact on human rights has necessitated the need to protect the individual not only from the state, but also from the corporation.⁵¹ As a result, a number of host states have sought to constitutionalize corporate human rights obligations in order to have safeguards that would not only be difficult to weaken, but that would apply to all persons without exemptions. Private law obligations have been unable to guard against such exemptions as was the case in Kenya, between 1993 to 2003, when foreign corporations were exempted from the Factories Act of 1951 that safeguards labour rights.⁵²

Proponents of vertical effect regard the role of a bill of rights to be that of serving as a bulwark against states' intrusion into an individual's private life⁵³ and, as a result, regard private law as being sufficient to regulate corporate conduct. They also regard the constitution as the fundamental law that restricts, through judicial scrutiny, the legislative and administrative actions of the government rather than those of private persons who are considered free, equal, and autonomous.⁵⁴ In contrast, some natural law proponents argue that acts of non-state actors also deserve constitutional scrutiny because human rights norms are inalienable rights that are possessed by all persons and it does not matter, therefore, whether the threat to human rights emanates from the state or a third party. Consequently, failing to impose obliga-

BILL OF RIGHTS (U.K. 1689); DÉCLARATION DES DROITS DE L'HOMME ET DU CITOYEN [Declaration of the Rights of Man and of the Citizen] (Fr. 1789).

⁴⁹ See generally *RWDSU v. Dolphin Delivery Ltd.*, [1986] 2 S.C.R. 573 (Can.); Bundesverfassungsgerichts [BverfG] [Federal Constitutional Court] Jan. 15, 1958, 7 Entscheidungen des Bundesverfassungsgerichts [BVerwGE] 198, 1958 (Ger.). Following fear that, if identified, the claimants would be subjected to "lynch mob justice," the claimants applied successfully for an injunction to prevent publication of information about them. They had been convicted, both at the age of ten and a half, of the murder of a two-year-old child). *Venables v. News Group Newspapers Ltd.*, [2001] EWHC (QB) 32, [2001] 2 W.L.R. 1038 (Eng.).

⁵⁰ See Richard S. Kay, *The State Action Doctrine, the Public-Private Distinction, and the Independence of Constitutional Law*, 10 CONST. COMMENT. 329, 342-46, 351-353 (1993); Erwin Chemerinsky, *Rethinking State Action*, 80 NW. U. L. REV. 503 (1985); Stephen Gardbaum, *The "Horizontal Effect" of Constitutional Rights*, 102 MICH. L. REV. 387 (2003).

⁵¹ See *In re S. African Apartheid Litig.*, 346 F. Supp. 2d 538, 549 (S.D.N.Y. 2004) *aff'd in part, vacated in part, remanded sub nom. Khulumani v. Barclay Nat. Bank Ltd.*, 504 F.3d 254 (2d Cir. 2007) *aff'd sub nom. Am. Isuzu Motors, Inc. v. Ntsebeza*, 553 U.S. 1028 (2008).

⁵² See KENYA HUMAN RIGHTS COMMISSION, *MANUFACTURE OF POVERTY THE UNTOLD STORY OF EPZs IN KENYA* 47 (2004); Kiarie Mwaura, *Corporate Citizenship and Human Rights Reality and Prospects of the Proposed Constitutional Changes in Kenya*, in *CORPORATE CITIZENSHIP IN DEVELOPING COUNTRIES* 139, 155 (2006).

⁵³ Halton Cheadle & Dennis Davis, *The Application of the 1996 Constitution in the Private Sphere*, 13 S. AFR. J. ON HUM. RTS. 44, 45-46 (1997).

⁵⁴ See Chris Sprigman & Michael Osborne, *Du Plessis is Not Dead: South Africa's 1996 Constitution and the Application of the Bill of Rights to Private Disputes*, 15 S. AFR. J. ON HUM. RTS. 25, 42 (1999).

tions on non-state actors, who are sometimes more powerful than states,⁵⁵ is seen as a failure to protect human rights adequately. For the same reason, the differential treatment of human rights violations perpetrated by the state and those perpetrated by non-state actors is considered an insufficient approach for safeguarding rights.⁵⁶ It is also considered insufficient to make the state indirectly liable for failing to have in place regulations to prevent violations between private persons because the public expects their rights to be respected by all, including non-state actors.⁵⁷

Arguments have also been proffered against horizontality of constitutional law on the premise that it might cause a floodgate of trivial cases and, therefore, dilute constitutional safeguards against the state.⁵⁸ This is not entirely the case, however, because the supposed dilution has not been observed in countries, such as South Africa, that have had horizontality for more than ten years. It is also the case that horizontality is unlikely to trivialize constitutional safeguards because the language that is used in most constitutional provisions requires courts to only enforce rights against corporations where applicable.

Critics of horizontality are also of the view that human rights obligations cannot apply to non-state actors because the language of most human rights provisions addresses states rather than individuals. Although provisions such as those providing safeguards against arrest, imprisonment, and extradition⁵⁹ are directed at the state, adopting a horizontal approach does not presuppose that human rights obligations should always apply to corporations, as courts are often given the discretion to determine when rights should be enforced directly against a corporation. The horizontal approach adopted in South Africa, for instance, allows horizontal application of human rights obligations but it does not mandate it.⁶⁰

Another argument proffered against horizontality is that it, undemocratically, allows judges to make political judgments about the rights of private persons. The legislature, rather than the judiciary, is seen as the most appropriate body to determine competing rights between individuals because it “possesses the democratic pedigree to make the uniquely political decisions that the process of balancing constitutional values as between private parties demands.”⁶¹ The balancing of rights between private persons is also criticized on the ground that constitutions do not provide a formula for this kind of balancing as they do with rights against the state.⁶² These standpoints, however, overlook the fact that judges are always making political decisions and that the balancing of rights against the state also involves the consideration of competing rights of two individuals, especially where one of them is suing the state for the failure to prevent the other from violating his rights. The standard applied against

⁵⁵ It has been argued that non-state actors pose a greater threat to human rights than states. See R. A. MacDonald, *Postscript and Prelude – The Jurisprudence of the Charter: Eight Theses*, 4 SUP. CT. L. REV. 321, 347 (1982).

⁵⁶ Brice Dickson, *The Horizontal Application of Human Rights Law*, in A HUMAN RIGHTS: AN AGENDA FOR THE 21ST CENTURY 59, 63 (Angela Hegarty & Siobhan Leonard eds., 1999).

⁵⁷ See *id.* at 65-67.

⁵⁸ See William P. Marshall, *Diluting Constitutional Rights: Rethinking “Rethinking State Action,”* 80 NW. U. L. R. 558, 569 (1985).

⁵⁹ Aharon Barak, *Constitutional Human Rights and Private Law*, in HUMAN RIGHTS IN PRIVATE LAW, 13, 17 (Daniel Friedmann & Daphne Barak-Erez eds., 2001).

⁶⁰ Constitution of the Republic of South Africa (1996), ch. 2, sec. 8(1). The Constitution states that the “Bill of Rights applies to all law, and binds the legislature, the executive, the judiciary and all organs of state.” *Id.*

⁶¹ Sprigman & Osborne, *supra* note 54, at 48.

⁶² See Barak, *supra* note 59, at 18.

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the state could also be applied against non-state actors and this would be democratic given that courts, as public authorities with human rights obligations, are increasingly making laws even in states that do not allow their laws to have direct horizontal effect.⁶³ The ultimate result under either a direct or an indirect system is that the individual is offered protection by the court, a fact that blurs the distinction between the two.⁶⁴ Commenting on the similarities between indirect and direct effect, Kumm observes:

A constitutional amendment explicitly establishing that constitutional rights have direct horizontal effect in Germany would neither impede the liberty of economic actors, nor would it provide additional protection for weaker economic parties. As a matter of substantive law and institutional division of labor, it would simply leave things as they are. With the comprehensive scope of constitutionally protected interests in Germany, private law in Germany is already applied constitutional law.⁶⁵

Apart from the similarities between the two, it is also notable that EU countries have some human rights obligations that are directly binding on corporations. Indeed, the European Court of Justice has held that the constitutional provisions contained in the Treaty of Rome on equal pay for men and women at work and non-discrimination on grounds of nationality apply to state and non-state actors.⁶⁶

Critics of horizontality often fail to see these similarities as well as the benefits that host states reap from horizontality, namely having more entrenched safeguards and having codified norms that constantly remind corporations of the human rights standards that they are expected to meet. Although the constitutionalization of corporate human rights norms has these advantages, it is clearly the case that almost all the countries that have adopted this approach have not gone far enough. As noted earlier, Article 12(1) of the Ghanaian Constitution, for example, stipulates that:

The fundamental human rights and freedoms enshrined in this Chapter shall be respected and upheld by the executive, legislature and judiciary and all other agencies and, where applicable to them, by all natural and legal persons in Ghana and shall be enforceable by the Courts as provided for in this Constitution.⁶⁷

Whilst the provision is commendable for extending human rights obligations to legal persons, it does not tackle the obstacle of the corporate veil within corporate groups. However, the adoption of similar constitutional clauses by a number of African countries clearly show that they have the political will to regulate corporate conduct and, with appropriate

⁶³ See Brice Dickson, *The Role of Judges in the Development of Constitutions*, 57 N. IR. LEGAL Q. 332 (2006).

⁶⁴ For example, the Supremacy Clause of the U.S. Constitution provides: "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. CONST. art. VI, cl. 2.

⁶⁵ Mattias Kumm, *Who's Afraid of the Total Constitution? Constitutional Rights as Principles and the Constitutionalization of Private Law*, 7 GER. L. J. 341, 359 (2006).

⁶⁶ See Case C 43/74, *Defrenne v. Sabena*, 1976 I.C.R. 547, 572.

⁶⁷ The Constitution of the Republic of Ghana (1992), ch. 5, art. 12(1).

international support, they could do it more appropriately by adopting constitutions norms that disregard the corporate veil within corporate groups. It is submitted that this is one area where states need, as the SRSB has observed, "effective guidance and support at the international level in order to achieve greater policy coherence."⁶⁸ Adopting a convention that embraces enterprise principles, for example, could help states to use it as a benchmark against which to measure their domestic policies.

II. STRUCTURAL AND PROCEDURAL CONSTRAINTS ON HUMAN RIGHTS PROTECTION

A. Entity Law

As mentioned in the above section, the general principles of corporate law on corporate groups focus on preserving the distinction between each individual corporation (entity law). Each individual corporation is regarded as having its own separate legal personality and, therefore, liability from the date of its incorporation.⁶⁹

As a result of the distinct corporate entity that companies enjoy, they have the right to organize their affairs in a manner that allows them to avoid group liability. This may involve, for instance, shifting resources between companies to ensure that the subsidiaries engaged in risky ventures are undercapitalized to minimize the risk of loss in the event of human rights or tortious liability. Courts have refused to lift the corporate veil in order to attach liability to companies that use a corporate structure in this manner, a fact that has been affirmed by Slade LJ in *Adams v. Cape Industries Plc.*⁷⁰

A similar judicial approach can be observed in Commonwealth African countries where the constitutional reforms mentioned earlier are taking place. The reason for this is mainly that their corporate laws are based on English law principles that they inherited from England at the time of their independence. Kenya's Companies Act, for instance, is based almost entirely on the 1948 English Companies Act. In addition, Kenya's Judicature Act⁷¹ permits the application of the common law and doctrines of equity in force in England as at 12 August, 1897. Whilst decisions of English courts given after the reception date are not of binding authority in the courts of the territory, they are entitled to the highest respect if the English law has not been subsequently modified. The English precedents on the veil lifting practice would therefore be applicable to Kenya and most other Commonwealth countries. A clear pointer to this is the case of *Mosi v. National Bank of Kenya Ltd* where Ringera J, whilst determining whether a holding corporation could be sued for a breach of contract by its subsidiary after the two merged their businesses, said:

A merger or amalgamation of business of a holding company (or a parent company in the language of some) with that of the subsidiary is a business decision with only administrative but not legal consequences as pertains to the legal status of the entities concerned.⁷²

⁶⁸ See Ruggie, *supra* note 3, at 13.

⁶⁹ British Companies Act, 2006, c. 46, § 16(3).

⁷⁰ *Adams v. Cape Industries Plc.*, [1990] Ch. 433, 544 (C.A.) (U.K.).

⁷¹ The Judicature Act, (2007) Cap. 8 § 3 (Kenya).

⁷² *Mosi v. National Bank of Kenya Ltd.*, (2001) # K.L.R. 333, 336 (Kenya).

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Whilst courts may, sometimes, pierce the corporate veil to impose liability on a parent corporation for the acts of its subsidiaries, it is not precisely clear when a court may do so and the absence of precise statutory rules in most jurisdictions does not help the situation. There is uncertainty, for instance, on whether a court is likely to be swayed by evidence of ownership of one corporation in another or the degree of control that it has on management affairs of the other. One might assume that a parent corporation having 98 percent controlling interest in a subsidiary would be regarded as being responsible for the acts of the subsidiary, but such a subsidiary was treated as an independent and separate entity in the case of *Kodak Ltd. v. Clark*.⁷³

The main grounds that courts have used to justify the lifting of the corporate veil within corporate groups include instances where a corporate structure has been used to perpetrate fraud, where the group of companies is considered to be one economic entity and where there is an agency relationship.

Firstly, courts will lift the corporate veil when a corporation is formed for the purposes of perpetrating a fraud. This ground can be utilized to attribute the liability of the subsidiary to the holding corporation as well as to the culpable individuals. For example, in the Kenyan case of *Caneland Ltd. v. Dolphin Holdings Ltd.*,⁷⁴ Mbaluto J enforced a judgment against a wholly owned subsidiary of the defendant so as not to allow “a debtor to hide behind the cloak of corporate identity to avoid meeting its legal obligations.”⁷⁵

However, the scope within which this ground can be utilized is limited by the criteria used by the courts to determine what amounts to fraud. Whilst shifting around risky business activities to undercapitalized subsidiaries might appear to some to be fraudulent, doing so has been regarded as a legitimate way of conducting business.⁷⁶

Secondly, courts may regard a group of companies that are under the dominant control of one as constituting a single economic unit.⁷⁷ For this to happen, the holding corporation must have substantial or absolute control of the affairs of the subsidiary. Case law in this area is, however, not precise as to the exact degree of control that is required to meet the veil lifting threshold. The fact that a holding corporation appointed all directors of a subsidiary and determined the subsidiary’s corporate policy was sufficient to lift the corporate veil and treat the two companies as one in *Holdsworth & Co v. Caddies*.⁷⁸ Similarly, the control of a subsidiary’s corporate policy, even where the holding corporation did not wholly own the subsidiary, served as a sufficient basis for lifting the corporate veil in *Scottish Co-op Wholesale Society v. Meyer*.⁷⁹

Later cases, however, show that courts have become reluctant to dislodge the corporate veil on the basis of control of subsidiary’s policy alone and they have required further proof to the effect that the subsidiary was a façade⁸⁰ or that it did not have any corporate

⁷³ *Kodak Ltd. v. Clark*, [1903] 1 K.B. 505 (U.K.).

⁷⁴ *Caneland Ltd. v. Dolphin Holdings Ltd.*, 1 E.A.L.R. 29 (C.C.K.) (1999) (Kenya).

⁷⁵ *Id.* at 32.

⁷⁶ See *Adams*, [1990] Ch. at 544.

⁷⁷ This may happen, for example, when a group of companies is reorganized with the motive of avoiding liability. See *Ord v. Belhaven Pubs Ltd.*, 2 B.C.L.C. 447 (C.A.) (1998), *rev’g Creasey v. Breachwood Motors*, (1992) B.C.C. 639 (U.K.).

⁷⁸ *Holdsworth & Co. v. Caddies*, (1955) 1 W.L.R. 352 (H.L.) (U.K.).

⁷⁹ *Scottish Co-op Wholesale Soc’y v. Meyer*, [1959] A.C. 324 (H.L.) (Scot.).

⁸⁰ *Woolfson v. Strathclyde Regional Council*, (1978) S.L.T. 159 (H.L.) (Scot.). According to Marc Moore, companies that are set up with the intention of shielding a person from formal responsibility should also be

independence from the parent corporation.⁸¹ Indeed, the proof of a strong economic link between groups of companies in *Bank of Tokyo v. Karoon* could not persuade the English Court of Appeal to treat a group of companies as one.⁸²

Similarly, the English Court of Appeal in 1990 concluded that the sole proof of control of a subsidiary by a holding corporation was insufficient to justify the dislodging of the corporate veil in *Adams v. Cape Industries*.⁸³ The court declined to dislodge the corporate veil in this case despite the proof of Cape's control of the general corporate policy of the subsidiary, including the subsidiary's expenditure and financial policy. The court treated the subsidiary as an independent entity on the basis that it was not totally dependent on Cape, as it ran its own business by, for instance, entering into independent contracts and employing its own staff. The Court of Appeal was of the opinion that only absolute control that made a subsidiary lack corporate independence would have justified the lifting of the corporate veil.

The rationale for failing to treat a group of companies as one economic entity in order to do justice to tort and human rights victims should be contrasted with the approach that accounting and tax regulations often adopt to deal with corporate groups. Such regulations often ignore the separate personality rule within corporate groups and require them to prepare consolidated accounts for the entire group.⁸⁴

Although establishing that a holding corporation was in control of the subsidiary may sometimes not be a sufficient basis for courts to lift the veil as we have seen, courts have utilized a third ground to lift the corporate veil when an agency relationship between two companies can be established. In such circumstances, the principal is regarded as being responsible for the actions of the agent. However, the corporate veil is less likely to be lifted in cases where the agent and the principal would be regarded as distinct entities, unless one corporation is seen as an aider and abettor of the other's actions.⁸⁵ The failure on the part of the alleged principal corporation to interfere with the management of the subsidiary is sufficient for a court to deny the existence of an agency relationship regardless of the amount of shares that one corporation holds in another.⁸⁶

In order for a court to find an agency relationship between two entities, it is not necessary for a formal contract to exist between the two,⁸⁷ as the relationship may be express or implied. The existence of an agency relationship may, for instance, be proved by establish-

treated as a mask or façade. See Marc Moore, *A Temple Built on Faulty Foundations: Piercing the Corporate Veil and the Legacy of Salomon v. Salomon*, 2006 J. Bus. L. 180, 198.

⁸¹ See *Adams*, [1990] Ch. 433.

⁸² [1987] A.C. 45, 64 (C.A.).

⁸³ [1990] Ch. 433.

⁸⁴ See Kenya Companies Act, (1962) Cap. 486 § 151; See also British Companies Act, 2006, c. 46, § 1162. To determine the existence of a holding-subsidiary relationship, the British Companies Act 2006 (Section 1162) considers the relationship to exist if the parent company "(a) holds a majority of the voting rights in the undertaking, or (b) it is a member of the undertaking and has the right to appoint or remove a majority of its board of directors, or (c) it has the right to exercise a dominant influence over the undertaking— (i) by virtue of provisions contained in the undertaking's articles, or (ii) by virtue of a control contract." Tax legislation has also been used in this regard to prevent corporate structures from being used as instruments for tax avoidance. See, e.g., *Firestone Tyre & Rubber Co. v. Lewellin*, (1957) 1 W.L.R. 464 (H.L.) (U.K.).

⁸⁵ See *Bowoto v. Chevron Texaco Corp.*, 312 F. Supp. 2d 1229 (N.D. Cal. 2004).

⁸⁶ In *Kodak v. Clarke*, the court held that there was no agency relationship between two companies on the basis that the holding company never bothered with the management of the subsidiary despite the fact that it had 98 percent shareholding in the subsidiary. *Kodak v. Clarke*, (1902) 2 K.B. 89 (U.K.).

⁸⁷ *Doe v. Unocal Corp.*, 395 F.3d 932, 974 (9th Cir. 2005).

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ing that the principal has authorized the agent “to enter into contracts on behalf of the corporation without submitting them to the corporation for approval.”⁸⁸ Other indicators of the existence of an agency relationship have included: daily meetings between the executives of two entities that were geared towards executing the actions that led to the harm; and situations where employees of one entity requested the employees of the other entity to do certain specific acts.⁸⁹

For instance, in the U.S. case of *Bowoto v. Chevron Texaco*, Judge Illston observed that Chevron ought to be held liable for the acts of its Nigerian subsidiary, Chevron Nigeria Ltd (CNL), for deaths and injuries caused to persons who were protesting against CNL’s activities in Nigeria. The evidence of communication between the two companies and the common officers between the two companies persuaded the court to find an agency relationship between the two. According to Illston:

[Chevron] exercised more than the usual degree of direction and control which a parent exercises over its subsidiary. The agency relationship alleged by plaintiffs is directly related to the plaintiffs’ cause of action, in that plaintiffs allege that defendants were significantly involved in security matters and benefited directly from CNL’s oil production, which was made possible or at least protected by the military’s wrongful use of force to quell unrest among Nigerians.⁹⁰

Liability could also attach to a holding corporation where it is established that the corporation had control over the conduct that gave rise to the injury and, therefore, owed a duty of care to the plaintiffs. In *Lubbe v. Cape Plc*,⁹¹ the Court of Appeal used a fault based approach to opine that a holding corporation could be liable for tortious acts of its subsidiary if it was established that the holding corporation controlled the operations of the subsidiary. According to the court, the question of control could be satisfied by establishing that the directors and other senior personnel of the holding corporation were responsible for the decisions that led to the injury. The control test in this case focused on the control that the parent corporation had over the conduct that gave rise to the injury, rather than absolute control of the subsidiary by the parent corporation as was the case in *Adams v. Cape Industries*.

Courts in the United Kingdom have been divided on the question of the existence of an extra discretionary ground for lifting the corporate veil for the sake of doing justice. Whilst Cumming-Bruce LJ in 1985 was of the opinion that the courts could use their power to lift the corporate veil to achieve justice,⁹² Slade LJ in 1990 opined that it is not open to the court to disregard the corporate veil on this ground.⁹³ Although some courts in the United States have

⁸⁸ F & K. Jabbour v. Custodian of Israeli Absentee Property, (1954) 1 W.L.R. 139, 146 (Q.B.) (U.K.).

⁸⁹ The fact that Unocal employees requested the military to construct helipads for the convenience of corporate executives was held to be an indication of an agency relationship. *Doe v. Unocal Corp.*, 395 F.3d 932, 973 (9th Cir. 2005).

⁹⁰ Judge Illston also observed that an agency relationship could even be created by ratification where the purported agent acts outside his authority, but the principal later on expressly or impliedly adopts the act of the agent. According to Illston, CNL could impliedly be treated as an agent of Chevron on the basis that Chevron covered up CNL’s misdeeds. See *Bowoto v. Chevron Texaco Corp.*, 312 F. Supp. 2d 1229, 1246 (N.D. Cal. 2004).

⁹¹ *Lubbe v. Cape Plc.*, (2000) 1 W.L.R. 1545 (H.L.) (U.K.).

⁹² *In re a Company*, (1985) 1 B.C.C. 99421 (C.A.) (U.K.).

⁹³ *Adams*, [1990] Ch. at 536.

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lifted the corporate veil under this ground in order to attach liability to a parent corporation that undercapitalizes its subsidiaries,⁹⁴ some have been less willing to do so and have maintained that undercapitalization alone cannot trigger veil piercing without more proof of fraudulent use of the subsidiary.⁹⁵ The latter position appears to be the one favored in the United Kingdom.⁹⁶

B. Forum non Conveniens

In the event that a tort or human rights victim sues a subsidiary corporation in a foreign jurisdiction where the parent corporation has a seat, he has to establish that the foreign court has jurisdiction to hear the case. The task of proving this becomes difficult if the litigant cannot persuade the court to lift the veil between the parent and the subsidiary corporation so that a link to the foreign forum could be established. Courts have affirmed that a mere relationship between a parent and a subsidiary corporation is insufficient to establish jurisdiction in a forum.⁹⁷

Even where the litigant is able to persuade the court to lift the corporate veil, the court has to be satisfied that there is no other more appropriate forum to hear the case. The case might therefore still be dismissed under the forum non conveniens grounds, which entails considering all the factors connecting a suit to available jurisdictions so as to ensure that it is heard in the jurisdiction that has the most connections to it.⁹⁸

Under the forum non conveniens doctrine, the inability to guarantee justice in the alternative forum is not a factor that appears to deter courts from sending suits to those forums. For example, in *Dow Chem Co v. Alfaro*⁹⁹ the absence of a jury trial and the setting of a maximum compensation of \$1080, for injuries arising from the use of chemical pesticides in Costa Rica were considered to be insufficient grounds for hearing the case in the United States. Other factors that courts in the United States have rendered as insufficient pointers to take jurisdiction include: unavailability of legal aid or contingency fee arrangement,¹⁰⁰ inadequate compensation,¹⁰¹ lack of punitive damages,¹⁰² lack of damages for non economic harm,¹⁰³ lack of class action proceedings,¹⁰⁴ and trial delays.¹⁰⁵

The problems posed by the concept of forum non conveniens are also a common feature of the English law, as courts would also stay proceedings before them if they consider

⁹⁴ See 1 WILLIAM MEADE FLETCHER ET AL., *FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS* § 41.30 (perm. ed., rev. vol. 2006); see *Minton v. Cavaney*, 364 P.2d 473 (Cal. 1961).

⁹⁵ *United States v. Healthwin-Midtown Convalescent Hosp. & Rehab. Ctr. Inc.*, 511 F. Supp. 416 (C.D. Cal. 1981), *aff'd*, 685 F.2d 448 (9th Cir. 1982); see *Walker v. Signal Cos Inc.*, 149 Cal. Rpt. 119 (Cal. Ct. App. 1978).

⁹⁶ See comments by Slade LJ, in *Adams*, [1990] Ch. at 544.

⁹⁷ *Doe v. Unocal Corp.*, 248 F.3d 915, 925 (9th Cir. 2001).

⁹⁸ See *Spiliada Mar. Corp. v. Cansulex Ltd.*, (1987) A.C. 460 (H.L.) (U.K.).

⁹⁹ *Dow Chemical Co. v. Alfaro*, 786 S.W.2d 674 (Tex. 1990).

¹⁰⁰ *Magnin v. Teledyne Cont'l Motors*, 91 F.3d 1424, 1430 (11th Cir. 1996).

¹⁰¹ *Delgado v. Shell Oil Co.*, 890 F.Supp 1324, 1357-58 (SD Tex. 1995), *aff'd*, 231 F.3d 165 (5th Cir. 2000).

¹⁰² See *Macedo v. Boeing Co.*, 693 F.2d 683, 686 (7th Cir. 1982).

¹⁰³ *Delgado*, 890 F. Supp. At 1329.

¹⁰⁴ See *Aguinda v. Texaco, Inc.*, 945 F. Supp., 625, 627 (S.D.N.Y. 1996).

¹⁰⁵ *Banco Latino v. Lopez*, 18 F. Supp. 2d 1327 (S.D. Fla. 1998).

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that the courts of another country, which is not a signatory to the Brussels Convention,¹⁰⁶ are more appropriate to hear the case. However, courts will not stay such proceedings if the defendant is domiciled in a Contracting State that is a signatory to the Convention. Instead, the courts would have jurisdiction to hear the case if the defendant is domiciled in their jurisdiction. This is because Article 53 of the Brussels Convention allows companies to be sued where they are domiciled and a corporation is considered to be domiciled in a jurisdiction if it has its seat there.¹⁰⁷

Although the traditional practice in the United Kingdom has been to reject the application of the Brussels Convention's domicile principle in cases where there is a choice between a forum in a Brussels Convention country and a non-Brussels Convention country,¹⁰⁸ the ECJ has taken a different approach, in *Owusu v. Jackson*, and applied the principle in a case where only one of the defendants was domiciled in a Contracting state. This was despite the fact that a majority of the defendants were domiciled in Jamaica, a factor that could have pointed to Jamaica as the most appropriate forum under the forum non conveniens doctrine. The ECJ ruled that the principles of forum non conveniens do not apply when a defendant is domiciled in a contracting state and because Jackson was so domiciled in this case, the case ought to have been heard in England.

Although the approach taken by the ECJ in this case has been criticized for not allowing domestic forums to apply their own rules in cases that do not affect the interests of the European Community,¹⁰⁹ the ECJ approach, which could eliminate the forum non conveniens doctrine if it is widely followed, is laudable as it is likely to do justice to tort and human rights victims who are unable to get justice from host states. The elimination of the forum non conveniens doctrine alone is, however, insufficient because entity law could still constrain victims who are unable to meet the threshold for veil lifting between a parent corporation and a foreign subsidiary, which is required for the case to be heard in the forum of the parent corporation. As discussed below, one way of overcoming this constraint is to replace principles of entity law with those of enterprise law.

III. OVERCOMING THE CONSTRAINTS

The absence of precise statutory rules on the veil lifting practice makes it difficult to ascertain the degree of control that is necessary to trigger the piercing of the veil. Given the reluctance of courts to probe too deeply into the question of control within corporate struc-

¹⁰⁶ The main objectives of the Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters 1968 are to increase economic efficiency and promote a single EU Market by harmonizing the rules on jurisdiction and preventing forum shopping and parallel litigation. See 1968 Brussels Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters pmbl., Sept. 27, 1968, available at [http://eur-lex.europa.eu/LexUriServ.do?uri=LEX:41968A0927\(01\):EN:HTML](http://eur-lex.europa.eu/LexUriServ.do?uri=LEX:41968A0927(01):EN:HTML).

¹⁰⁷ To determine whether a corporation has a seat in a jurisdiction in the United Kingdom, for instance, the Civil Jurisdiction and Judgments Act 1982, section 42 (3), which incorporated the Convention, allows courts to consider a number of factors including: "whether a corporation is incorporated in the UK or formed under the law of the UK; whether it has its registered office or some office address in the UK; or whether its central management and control is exercised in the UK." Civil Jurisdiction and Judgments Act 1982, c.27, § 42(3), (U.K.).

¹⁰⁸ In such cases, it has been held that the forum non conveniens doctrine applies. See *In re Harrods Ltd.*, [1992] 72 (C.A.) 124(d), 127(f)(U.K.).

¹⁰⁹ Trevor C. Hartley, *The European Union and the Systematic Dismantling of the Common Law of Conflict of Laws*, 54 INT'L. & COMP. L.Q. 813, 820 (2005).

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tures,¹¹⁰ a parent corporation can easily maintain strategic control of its subsidiaries and, at the same time, avoid liability by delegating management matters that are likely to be seen as making a subsidiary dependent on the parent corporation.¹¹¹ The ease with which companies can conceal their effective control over another makes reliance on the control test an ineffective approach to determine liability within a group of companies.

States seeking to fulfill their international human rights obligations with respect to averting and redressing corporate human rights violations within corporate groups can do so by adopting legislative rules that are centered on identifying the real economic identity of the business. One way of doing this is adopting enterprise principles, an approach to which we now turn.

A. Utilization of Enterprise Principles

The procedural barriers encountered by plaintiffs suing either foreign subsidiaries or parent corporations can be largely attributed to entity law, which allows one economically intertwined group companies to have separate legal identities.¹¹² Rather than focusing on separate legal identities, laws seeking to regulate corporate groups should adopt a single business enterprise approach that considers the economic unity of the entire group. This approach has been more acceptable in the United States, where it has been applied upon proof of an intertwined economic relationship between corporate entities. Factors that courts in the United States have taken into account to prove an intertwined relationship between entities within a group have included: control,¹¹³ economic integration,¹¹⁴ financial interdependence,¹¹⁵ administrative interdependence, overlapping employment structure,¹¹⁶ and common group persona,¹¹⁷ among others.¹¹⁸ The consideration of these factors allows for a much more liberal

¹¹⁰ Empirical studies have found that courts in the U.S., England, and Australia are more likely to lift the corporate veil to expose individual shareholders than corporate shareholders in a corporate group. Courts are also less willing to lift the veil in tort cases than other cases. See Robert B. Thompson, *Piercing the Veil Within Corporate Groups: Corporate Shareholders as Mere Investors*, 13 CONN. J. INT'L L. 379, 379-82 (2009); Charles Mitchell, *Lifting the Corporate Veil in the English Courts: An Empirical Study*, 3 COMP. FIN. & INSOLV. L. REV., 15, 22 (1999).

¹¹¹ Jamie Cassels, *Outlaws: Multinational Corporations and Catastrophic Law*, 31 CUMB. L. REV. 311, 326 (2001).

¹¹² For more on this, See Phillip Blumberg, *Asserting Human Rights Against Multinational Corporations Under United States Law: Conceptual and Procedural Problems*, 50 AM. J. COMP. L., 493, 498 (2002).

¹¹³ The term control is interpreted widely to encompass the influence and dominance of one corporation over another.

¹¹⁴ Examples of this might include the use of group insurance, group purchasing, group warehousing, group marketing, etc.

¹¹⁵ Such as intragroup financing.

¹¹⁶ This might include intra group exchange of employees, joint employee training programs, and group insurance.

¹¹⁷ See BLUMBERG, *supra* note 43, at 94 ("In this area of integrated operations, the constituent companies of the group utilize the same group trade name, trademarks, logo, and in some cases even color schemes and style of uniforms around the world.").

¹¹⁸ Grayson v. R.B. Ammon, 778 So.2d 1 (La. Ct. App. 2000). The case spelled out the following eighteen factors that might be taken into account to determine whether a group of companies constitutes one economic enterprise:

corporations with identity or substantial identity of ownership, that is, ownership of sufficient stock to give actual working control; common directors or officers; unified

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approach to veil lifting than that of the United Kingdom, where enterprise principles have only been utilized to require corporate groups to prepare consolidated group accounts.¹¹⁹ This is also the trend followed in other Commonwealth countries, such as Australia¹²⁰ and Kenya.¹²¹ Apart from helping to identify the true economic reach of a group for taxation purposes, enterprise principles also help to define the relationships within a group of companies for the purposes of competition law. Entities within a group of companies are, for example, considered to form one economic entity when considering whether agreements between them distort competition within the EU common market.¹²² Similar principles could also be utilized to extend tortious and human rights liability to the entire group so as to minimize corporate effect on human rights. Doing so would not only give effect to the original purpose of limited liability, which entailed the protection of human rather than corporate shareholders,¹²³ but would also raise standards of corporate conduct by making it risky for a parent corporation to ignore the activities of its subsidiaries that pose a threat to human rights. It would also ensure that victims of corporate abuse are not left uncompensated.¹²⁴

administrative control of corporations whose business functions are similar or supplementary; directors and officers of one corporation act independently in the interest of that corporation; corporation financing another corporation; inadequate capitalization; corporation causing the incorporation of another affiliated corporation; corporation paying the salaries and other expenses or losses of another corporation; receiving no business other than that given to it by its affiliated corporations; corporation using the property of another corporation as its own; noncompliance with corporate formalities; common employees; services rendered by the employees of one corporation on behalf of another corporation; common offices; centralized accounting; undocumented transfers of funds between corporations; unclear allocation of profits and losses between corporations; and excessive fragmentation of a single enterprise into separate corporations.

Id.

¹¹⁹ Companies Act 2006, c. 46, § 399(2), (U.K.) available at http://www.legislation.gov.uk/ukpga/2006/46/pdfs/ukpga_20060046_en.pdf. Britain's City Code on Takeover and Mergers also follows these principles to impose obligations on any person or body acting in concert with others to breach regulations. The definition of the term "acting in concert" under the code is wide enough to cover all entities that might be complicit in breach of regulations. Unless the contrary is established, a parent company, its subsidiaries, and its associates and companies of which such associates are associated are considered to be acting in concert. In such situations, ownership or control of twenty percent or more of the equity share capital is considered to be acting in concert where there is an agreement or understanding (whether formal or informal) actively to cooperate through the acquisition by any of them of shares in the company so as to obtain or consolidate control of that company. See The Takeover Code, 2011, § C(1), (U.K.) available at <http://www.thetakeoverpanel.org.uk/wp-content/uploads/2008/11/code.pdf>; see British Companies Act, 2006, c. 46, § 399.

¹²⁰ See Australian Corporations Act 2001, § 323.

¹²¹ See Kenya Companies Act, (1962) Cap. 486 § 151.

¹²² Treaty Establishing the European Communities, art. 81 (prohibiting agreements between undertakings that are intent on restricting or distorting competition within the common market, does not extend to agreements entered into by undertakings that are part of companies); see Case T-102/92, *VIHO Eur. v. BV Comm'n*, 1995 E.C.R. II-00017 upheld by Case-C-73/95, *Viho Eur. BV v. Comm'n*, 1996 E.C.R. I-05457; *Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 777 (1984).

¹²³ See BLUMBERG, *supra* note 43, at 58.

¹²⁴ This was the case in claims arising from the Bhopal gas leak. See Tamar Lewin, *Carbide is Sued in U.S. by India in Gas Disaster*, N.Y. TIMES, Apr. 9, 1985, at A1.

As a result of the difficulties that might arise in identifying corporate entities that should be treated as one economic entity,¹²⁵ there is a strong case for applying strict¹²⁶ or automatic¹²⁷ liability to parent companies for acts of their wholly owned subsidiaries while, at the same time, giving them a chance to rebut the presumption that the subsidiaries are wholly owned. It is preferable to base the presumption of liability on the question of ownership of a subsidiary rather than its control¹²⁸ because the latter approach might enable a corporation to avoid liability by strategically delegating management matters that are likely to be seen as making a subsidiary dependent on the parent corporation. Pro rata unlimited liability, however, could be applied where there is partial ownership of subsidiaries so that every holding corporation within the group shares the costs of liability on a proportional basis.

Presser, a critic of the enterprise liability approach, argues that this approach could lead to unnecessary governmental supervision of corporations that would, in turn, make them less effective in providing checks on abuse of power by the government.¹²⁹ Instead of adopting enterprise principles, Presser makes a case for insurance coverage of risky businesses activities and statutory rules on adequate capital on the premise that enterprise principles would lead to a transfer of “wealth to a few lucky plaintiffs and trial lawyers,” rather than discouraging corporate misconduct.¹³⁰

Presser’s first argument, overlooks the fact that the wealth and influence of corporations in the era of globalization gives them the incentives to be as unaccountable as governments. The suggested statutory rules on capital might also not work efficiently because such rules could hurt corporations engaging in lawful business that cannot raise the minimum threshold of capital. Besides, the impossibility of predicting the cost of harm that a corporation could incur would makes the task of setting a minimum threshold difficult. The argument on insurance coverage is not without its flaws either because an insurance cover cannot serve as an absolute alternative to group liability in the event that a corporation purchases inadequate insurance, has difficulties obtaining insurance coverage¹³¹ or where insurance for a certain type of risk, such as complete bankruptcy¹³² or “highest possible expected liabil-

¹²⁵ Some categories of corporate groups could evade regulation as a result of such difficulties. For more on this, see Muchlinski, *supra* note 12, at 322; Dine, *supra* note 40, at 64.

¹²⁶ According to Richard Meeran, the TNC should be regarded:

as a conglomeration of units of a single entity, each unit performing a specific function, the function of the parent company being to provide expertise, technology, supervision and finance. In so far as injuries result from negligence in respect of any of the parent company functions, then the parent should be liable.

Richard Meeran, *The Unveiling of Transnational Corporations: A Direct Approach*, reprinted in *HUMAN RIGHTS AND THE RESPONSIBILITY OF TRANSNATIONAL CORPORATIONS* 161, 170 (Michael K. Addo ed., 1999).

¹²⁷ The concept of absolute enterprise liability has been utilised in India for injury arising from the conduct of ultra-hazardous industrial processes. *Mehta v. Union of India*, 1988 A.I.R.1115.

¹²⁸ For more on this presumption, see D. Milman, *Groups of Companies: The Path Towards Discrete Regulation*, in *REGULATING ENTERPRISE: LAW AND BUSINESS ORGANIZATIONS IN THE UK* 232 (David Milman ed., 1999).

¹²⁹ Stephen Presser, *The Bopalusa Explosion, “Single Business Enterprise,” “Alter Ego,” and other Errors: Academics, Economics, Democracy, and Shareholder Limited Liability: Back Towards a Unitary “Abuse” Theory of Piercing the Corporate Veil*, 100 Nw. U. L. REV. 405, 434 (2006).

¹³⁰ *Id.*

¹³¹ Corporations that are new to a risky business might experience this problem. See Easterbrook & Fischel, *supra* note 28, at 115.

¹³² *Id.* at 102.

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ity”¹³³ is unavailable in the market. It is submitted that the exposure of the entire corporate group to human rights and tortious liability could compel parent corporations to take adequate precautions to guard against violation of human rights in the first place, a factor that would be somewhat irrelevant in a scenario where an insurance cover suffices. Consequently, whilst introducing legislative measures that expose the entire group to liability could help states to prevent the occurrence of human rights violations in the first place, the same cannot be said of insurance measures that provide only *ex post* redress and which could actually incentivize corporations to engage in more risky business activities. Such measures would not meet international human rights standards, as they would only offer compensation to tort and human rights victims without removing the incentives to ignore human rights concerns.

Although the adoption of enterprise principles in one jurisdiction could go a long way towards reigning in corporate groups operating within that jurisdiction, the problem of reaching holding companies operating outside the jurisdiction would still remain because of a possible conflict of laws between two or more jurisdictions and, perhaps, the failure of foreign courts to recognize and enforce a judgment that underpins enterprise rather than entity principles. The next section considers whether an international approach would be required to resolve this problem.

B. Is there a Case for an International Approach?

As mentioned earlier, proponents of a domestic approach to corporate regulation regard the state as having the primary duty to protect against human rights violations by third parties. As will be seen, however, relying on the state alone is an insufficient way of safeguarding human rights because most states are reluctant to address extraterritorial human rights abuses that are perpetrated by corporations operating within their territory. For the domestic approach to work, both home states and host states would need to adopt legal reforms that make parent holding companies operating within their territories liable for acts of their foreign subsidiaries. Whilst host states have, in the past, shown willingness to do so by, for instance, adopting a single business enterprise approach,¹³⁴ the same cannot be said of home states, which remain the key beneficiaries of transnational trade.

Some scholars of international human rights law are of the view that home states have responsibility for extraterritorial corporate violation of human rights by foreign subsidiaries. McCorquodale and Simons,¹³⁵ for example, argue that the failure on the part of the home states to regulate foreign subsidiaries amounts to a breach of their international law obligations, which require states to not only guarantee protection to individuals within their territory, but also to others that are subject to their jurisdiction¹³⁶ and not necessarily within

¹³³ *Id.* at 116.

¹³⁴ See, e.g., Argentine Foreign Investment 21.382, Sep. 8, 1993, available at <http://www.cnv.gov.ar/LeyesReg/Leyes/ing/LEY21382.htm> (making foreign affiliates of companies domiciled in Argentina liable for the obligations of their Argentine subsidiaries).

¹³⁵ Robert McCorquodale & Penelope Simons, *Responsibility Beyond Borders: State Responsibility for Extraterritorial Violations by Corporations of International Human Rights Law*, 70 MOD. L. REV. 598, 602 (2007).

¹³⁶ “The High Contracting Parties shall secure to everyone within their jurisdiction the rights and freedoms defined in Section I of this Convention.” The European Convention on Human Rights and its Five Protocols art. 1 Nov. 4, 1950 available at <http://www.hri.org/docs/ECHR50.html>. “The State Parties to this Convention undertake to respect the rights and freedoms recognized herein and to ensure to all persons subject to their

the territory.¹³⁷ They argue that the constructive knowledge that states have about human rights violations by subsidiaries in foreign territories could trigger an obligation under international law requiring states to compel parent corporations, within their territories, to regulate their foreign subsidiaries.¹³⁸ Secondly, they contend that states have shown willingness to respect this duty and have, therefore, started to pierce the corporate veil in order to extend the liability of foreign subsidiaries to the parent corporations.¹³⁹ Thirdly, they are also of the view that the home states' responsibility under international human rights law could be triggered when a state authorizes a corporation to exercise a public duty, where it acts on behalf of the state or where the state is complicit in the corporate violation of human rights.¹⁴⁰

The first argument appears to imply that a foreign subsidiary would generally be deemed to be within the jurisdiction of the home state. This would only be the case if international law treats parent companies and their subsidiaries as one economic entity. However, this is not the case at the moment because international law and courts utilize entity principles to define the relationships between subsidiaries and parent companies¹⁴¹ given that there is an absence of internationally accepted standards favouring an enterprise approach to corporate regulation.¹⁴² In view of this, it would be the host state that would be deemed to have international law obligations to protect individuals within its jurisdiction. In the event that there was a general acceptance of enterprise principles at the international level, then it would be possible to extend the liability of a foreign subsidiary to the holding corporation and then to the home state for having constructive knowledge of foreign human rights violations.

The second argument implies that there is a general willingness on the part of home states' courts to pierce the corporate veil and hold parent corporations to account for extraterritorial activities. This is, however, not entirely the case. Although there have been a few occasions where domestic courts have pierced the corporate veil to extend liability to a parent holding corporation,¹⁴³ veil lifting within corporate groups, as discussed earlier, remains a very slim exception rather than a general rule. Indeed, home states appear to be more concerned with maintaining competitive business legal environments, which exonerate their corporations from liability, rather than protecting human rights in foreign territories. Home states are, therefore, more likely to defend their legal separation from the activities of foreign subsidiaries rather than accept the extension of liability to tax-paying parent corporations within their territories.

The reluctance of home states to take responsibility for extraterritorial liability can clearly be seen in the fiercely competitive investment policies of EU countries, which have made it difficult for the countries to agree on the need to have uniform regulations on corporate group liability. EU member states, for instance, opposed an attempt in 1985 to introduce

jurisdiction the free and full exercise of those rights and freedoms." American Convention on Human Rights art. 1 Nov. 22, 1969 available at http://www.hrcr.org/docs/American_Convention/oashr.html.

¹³⁷ In *Saldano v. Argentina*, a distinction between territory and jurisdiction and the possibility of holding a state liable for acts of its agent outside the territory has been made by the Inter American Commission on Human . *Saldano v. Argentina*, Inter-Am. Comm'n H.R., Report No. 38/99, OEA/Ser.L.V/II.95, doc. 7 rev. ¶ (1999)

¹³⁸ *McCorquodale & Simons*, *supra* note 135, at 616-17.

¹³⁹ *Id.* at 617.

¹⁴⁰ *Id.* at 606.

¹⁴¹ Case Concerning the Barcelona Traction, Light and Power Co. (Belg. v. Spain), 1970 I.C.J. 3 (Feb. 5).

¹⁴² See WALLACE, *supra* note 1, at 656-57.

¹⁴³ *Id.*; see, e.g., *Connelly v. RTZ Corp.*, [1998] A.C. 854 (H.L.) (appeal taken from Eng.); *Lubbe et al. v. Cape Plc.*, [2000] 4 All E.R. 268 (H.L.) (appeal taken from Eng.).

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uniform EU regulations on corporate group liability arguing that they would undermine the privileges of limited liability and create extra administrative, auditing, and legal costs.¹⁴⁴ This has somewhat frustrated some of the objectives of the EU, namely the development of harmonious economic activities¹⁴⁵ and equal treatment of companies within the bloc.¹⁴⁶

It is also worthy of note that one of the key reasons why the British Company Law Review Steering Group recently shied away from making recommendations for attributing liability to United Kingdom holding companies for acts of their foreign subsidiaries was the fact that this was going to make the United Kingdom a less competitive legal environment for business.¹⁴⁷ Similar sentiments can be discerned in academic debates as well where, for instance, Presser, makes a case against the adoption of the single business enterprise doctrine in the United States on the premise that the doctrine would disadvantage the country's industries by making them less competitive than their counterparts in Europe and Asia.¹⁴⁸ Moreover, some host states have, in the past, been put under immense pressure to shun the single business enterprise approach within their territories so as not to expose foreign holding companies to liability. A good illustration of this point is the stance taken by home states to oppose fiercely the Argentine Foreign Investment Law of 1973, which made foreign affiliates of companies domiciled in Argentina liable for the obligations of their Argentine subsidiaries. The fierce opposition eventually led to the ouster of the government that had introduced the single business enterprise doctrine, an approach that was eventually abandoned when the new government restored the entity approach through the Argentine Foreign Investment Law of 1976.¹⁴⁹ It can, therefore, clearly be seen that home states do not have any general willingness to abandon the entity approach to the regulation of corporate groups.

In view of the third argument which suggests that home states could incur liability for authorizing a corporation to exercise a public duty, this is certainly a possibility but one that would have limited benefits in protecting human rights in host states. First, the option is limited to situations where a corporation engages in activities that have a public element and would, therefore, not reach corporations violating human rights in the course of their commercial activities. Secondly, the operation of the separate personality rule within corporate groups would still be constraining whilst seeking to extend the liability of a subsidiary in a foreign territory to the parent holding corporation (in the home state) and then to the home state itself,

¹⁴⁴ See Amended Proposal for a Council Directive Complementing the Statute for a European Company with Regard to the Involvement of Employees in the European Community, 1991 O.J. (C138) 8; Amendments to the Rules of Procedure of the Court of Justice of the European Communities of 15 May 1991, 1991 O.J. (L 176) 1; LUCIE A. CARSWELL & XAVIER DE SARRAU, *LAW AND BUSINESS IN THE EUROPEAN COMMUNITY*, § 4-27 (1993).

¹⁴⁵ Treaty of Rome art. 2, Mar. 25, 1957, available at <http://www.hri.org/docs/Rome57/Part1.html>.

¹⁴⁶ Treaty of Rome art. 54(3)(g), Mar. 25, 1957, available at <http://www.hri.org/docs/Rome57/Part3Title03.html>; Sandra K. Miller, *Piercing the Corporate Veil Among Affiliated Companies in the European Community and in the U.S.: A Comparative Analysis of U.S., German, and U.K. Veilpiercing Approaches*, 36 AM. BUS. L.J. 73 (1998).

¹⁴⁷ The Final Report published on July 26, 2001 and the new Companies Act of 2006 that was based on that report do not contain any rule on human rights or tortious liability of corporate groups. For more on the reluctance of the steering group to address the question of corporate groups, see COMPANY LAW REVIEW STEERING GROUP, (2001), available at <http://www.dti.gov.uk/files/file23279.pdf>; P.T. Mulchinski, *Holding Multinationals to Account: Recent developments in English Litigation and the Company Law Review*, 23 COMPANY LAWYER 176 (2002).

¹⁴⁸ See *supra* text accompanying notes 128, 129.

¹⁴⁹ See BLUMBERG, *supra* note 43, at 189. For more examples of the manipulation of developing countries by home states, the World Bank, and International Monetary Fund (IMF), see DINE, *supra* note 40, at 74-75.

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especially where the harm is caused directly by a subsidiary that has some independence from the parent corporation acting under the instruction of the state. Due to the constraints of entity law, there would still be a need to lift the corporate veil in order to attribute the liability of the subsidiary to the parent corporation, a task that would entail satisfying one of the onerous grounds for lifting the veil.

Although it is the case that states can be, and have been, held liable for acts of their agents in foreign territories,¹⁵⁰ this logic would only apply to a parent-subsidiary relationship under the very few instances when it is possible to lift the corporate veil under entity law. This remains a major obstacle to human rights protection which has neither been addressed adequately by scholars of international human rights law nor by the Special Representative of the UN Secretary General on the issue of human rights and transnational corporations and other business enterprises (SRSG).¹⁵¹ Although one of his reports urges states to address constraints on human rights protection, such as forum non conveniens, in order to extend liability to corporations in their territories, it does not go far enough in recognizing that a state's duty to protect is broader and requires states to ensure that their corporate laws, especially the principle of separate legal personality, do not incentivize corporations to violate human rights.¹⁵² It also fails to recognize this obstacle whilst addressing challenges faced by victims that are seeking redress from a parent corporation in a home country. The report only recognizes the following obstacles: prohibitive costs (absence of legal aid), lack of standing for non citizens, claims barred by statutes of limitation, dismissal of cases on forum non conveniens grounds.¹⁵³ Although the obstacle of forum non conveniens might appear to be connected with that of the corporate veil, they are nevertheless different and addressing one would not necessarily resolve the problems created by the other. The appropriateness of a forum, for example, only becomes an issue if it is possible to lift the veil in the first place. It is because of this reason that sufficient attention needs to be given to states' duty to deal with the obstacle of the corporate veil if corporate groups are to be regulated effectively.

Given that most home states are likely to oppose the extension of liability either to themselves or to their tax paying parent corporations, as the above examples clearly shows, there is a need for some form of international compliance mechanisms that would persuade states to comply. One such mechanism would be an international convention obliging states to replace principles of entity law with those of enterprise law, an approach that would allow for the consideration of the economic reality of the entire corporate group whilst apportioning human rights and tortious liability.¹⁵⁴ In order to deal effectively with the extraterritorial nature of corporate human rights violations, the proposed convention could take the format of the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions which requires signatory states to criminalize the bribery of a foreign

¹⁵⁰ *Lopez Burgos v. Uruguay*, Human Rights Committee, Communication No. R 12/52, U.N. Doc. Supp. No. 40 (A/36/40)(1981); *see Montero v. Uruguay*, Human Rights Committee, Communication No. 106/1981, U.N. Doc. Sup. No. 40 (A/38/40) (1983).

¹⁵¹ *See Ruggie*, *supra* note 3, at 3, 5.

¹⁵² *See id.* at 5, 10. The report mentions in passing that a "parent company is generally not liable for wrongs committed by a subsidiary," but it does not mention the extent to which this problem affects human rights violation and what the solutions to it are. *Id.*

¹⁵³ *See id.* at 23.

¹⁵⁴ Covering all aspects of torts and human rights violations could help avoid problems that might arise when some claims under the law of tort are not recognised as human rights violations and vice versa.

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public official with a view to obtaining or retaining business¹⁵⁵ and to establish jurisdiction for extraterritorial bribery offences when they are committed in whole or in part in the jurisdiction of the signatory state.¹⁵⁶ The proposed convention could have far more wide ranging consequences than the OECD Convention and its uniform application could address the reluctance of individual states to adopt enterprise principles in their home countries for the fear of losing corporate investments to corporate liability havens.

Although it would not matter where a corporation is sued, under the proposed convention, as the entire corporate enterprise would be liable whenever it might have a presence, corporations would need to be vigilant in order to apply for striking out of subsequent claims that might be based on the same facts before a court that got seized of the matter first.

Whilst some home states and the business community are, undoubtedly, likely to resist, the adoption of the proposed convention for economic reasons, the UN needs to adopt it in order to set standards for states on how to stamp out extraterritorial corporate human rights violations. Apart from serving as a platform from which to exert pressure on individual states to comply, a convention that embraces the notion of reciprocity could bring about progressive compliance in non-compliant states. It could also serve as an authority that courts could use to justify the application of enterprise principles whenever they are determining tortious or human rights liability within corporate groups and, in turn, allow the constant use of such an approach to permeate progressively into most domestic legal systems. By adopting such a convention, the UN would be fulfilling one of its key duties which entails, in the words of SRSg, “setting expectations and aspirations” for states.¹⁵⁷ Despite the use of such promising words, the SRSg appears, on the whole, to favour a domestic rather than an international approach to corporate regulation.¹⁵⁸ One factor that could have prompted him to favour this approach is the concern that the business community and the states that are fearful of losing part of their sovereignty as a result of an international convention¹⁵⁹ might reject his recommendations as they did with the UN Norms on Transnational Corporations. There are a number of examples, however, which clearly show that states are not always averse to complying with clear international norms even when such norms face domestic objections. Such examples include, for example, the banning of commercial hunting of whales in Japan so as to comply with the terms of the International Whaling Commission, the reform of the Clean Air Act in the United States as a result of a WTO ruling, and the arrest of Slobodan Milosevic in Yugoslavia following extradition demands by a UN War Crimes Tribunal.¹⁶⁰ These examples, among others, are clear pointers to the utility of international institutions and norms in shaping domestic policies and laws. Besides, non-compliance by some states is an insufficient justification for rejecting a convention approach given that there are many other effective

¹⁵⁵ Organisation for Economic Co-operation and Development, Convention on combating Bribery of Foreign Public Officials in International Business Transaction, Nov. 21, 1997, available at <http://www.oecd.org/dataoecd/4/18/38028044.pdf>.

¹⁵⁶ *Id.* at art. 4(1).

¹⁵⁷ See Ruggie, *supra* note 3, at 28.

¹⁵⁸ See *id.* The reports indicates that “[t]he United Nations is not a centralized command-and-control system that can impose its will on the world – indeed it has no ‘will’ apart from that which Member States endow it. But it can and must lead intellectually and by setting.” *Id.*

¹⁵⁹ States are often reluctant to transfer their sovereignty to international bodies in the absence of clear benefits. See Daniel Drezner, *On the Balance Between International Law and Democratic Sovereignty*, 2 CHI. J. INT’L L. 321, 322 (2001).

¹⁶⁰ *Id.*

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conventions that have not been endorsed by all states. Examples of such treaties include the Rome Statute of the International Criminal Court and the Maastricht Treaty (aspect of the European Monetary Union) which have not been embraced by the United States and United Kingdom respectively.

The failure on the part of the SRSB to embrace an international approach to solve a transnational problem will only serve to postpone the problem of getting states to accept responsibility for regulating corporate groups and, generally, delay the search for a solution.

CONCLUSIONS

The strategic utilization of corporate structures has played a key role in undermining the protection of human rights, especially in host states. The ease with which corporate groups utilize the privileges of limited liability to escape tortious and human rights liability gives them immense incentives to utilize structures that reduce their exposure to liability. Given states' responsibility, under international human rights law, to prevent the occurrence of human rights violations in the first place, they have an obligation to adopt legislative measures that would stop the misuse of corporate structures. Whilst states that have reformed their constitutions in order to extend human rights norms to corporations are to be commended for taking this approach, they need to go a step further by utilizing enterprise principles to extend tortious and human rights liability to the entire network of corporate groups, which were not the intended beneficiaries of the privileges of limited liability when they were first devised. This would make it possible for parent and subsidiary corporations to be regarded as one economic entity for the purpose of tortious and human rights claims. However, given that home states are likely to resist such an approach for economic reasons, they need to be obliged to comply progressively through the mechanism of an international convention. Such a convention could create a state-wide uniform approach towards regulation of corporate groups and, in turn, render it difficult for corporations to escape liability in jurisdictions that might opt to retain entity principles in the absence of compulsion.

In order for this approach to be effective, legislative reforms, especially in host states, need to be constitutionally entrenched in order to guard against their erosion and also serve as a constant reminder of the onerous obligations that corporate groups have towards human rights. Widely drafted principles of enterprise law should be able to prevent the avoidance of liability by allowing courts to presume liability of holding corporations for the ownership of subsidiaries. This approach would not only serve as a disincentive for corporations to hide behind the corporate veil in order to violate human rights, but it would also ensure that victims of corporate abuse are not left uncompensated. Without such reforms, the principles of entity law as well as those of *forum non conveniens* will continue to undermine human rights protection by shifting the costs of business to tort and human rights victims.