Routledge
Taylor & Francis Group

Journal of Corporate Law Studies

ISSN: (Print) (Online) Journal homepage: www.tandfonline.com/journals/rcls20

Separate legal personality – an explanation and a defence

Eva Micheler

To cite this article: Eva Micheler (17 Jul 2024): Separate legal personality – an explanation and a defence, Journal of Corporate Law Studies, DOI: 10.1080/14735970.2024.2365170

To link to this article: https://doi.org/10.1080/14735970.2024.2365170

JOURNAL OF CORPORATE LAW STUDIES
https://doi.org/10.1080/14735970.2024.2365170

Routledge
Taylor & Francis Group

Separate legal personality – an explanation and a defence

Eva Micheler

London School of Economics – Law School, London, UK

ABSTRACT

The article proposes a modern version of real entity theory to explain the principle of the separate legal personality of the company. This theoretical model relies on scholarship from the wider social sciences that demonstrates that organisations bring about behaviours that would not exist but for the organisational context. Organisations are real in their consequences. The principle of separate legal personality condones, supports, and protects the ability of organisations to act autonomously. The article further suggests that we do not need a principle of corporate 'disregard' but should continue on the path of developing context-specific rules addressing questions arising out of corporate abuses.

ARTICLE HISTORY Received 29 August 2023; Accepted 4 June 2024

KEYWORDS Corporate personality; veil piercing; concealment; evasion; real entity theory

1. Introduction

Some ten years ago company law performed a remarkable turn. Before the decision in *Prest v Petrodel*,[1] the doctrinal position was that there was an independent company law doctrine justifying the 'piercing of the corporate veil'. That doctrine was generally understood to lead to a 'disregard' of the company's separate legal personality (section 2).[2] Now the doctrine has been redefined and broken up into 'concealment' (where the term veil piercing is used as a label) and evasion (where an independent doctrine of veil

CONTACT Eva Micheler e.micheler@lse.ac.uk LSE Law School, Houghton Street, London WC2A 2AE, UK https://www.linkedin.com/in/eva-micheler-76a5285/

[1] *Prest v Petrodel* [2013] 2 AC 415.

[2] Alan Dignam and Peter B Oh, 'Disregarding the Salomon Principle: An Empirical Analysis, 1885–2014' (2019) 39 Oxford Journal of Legal Studies 16 (22) identified 213 cases as being concerned with the 'disregard' of the company's separate legal personality. Charles Mitchell, 'Lifting the Corporate Veil in the English Courts: An Empirical Study' (1999) 3 Company, Financial & Insolvency Law Review 15 (19) identified 290 such cases.

piercing is said to apply). The cases decided since *Prest*, suggest that evasion may not prove to have lasting impact. But either way neither concealment nor evasion now involves the 'disregard' of the company's separate legal personality (section 3).

This development has so far remained unexplained. To be sure this article does not criticise the outcome. It agrees, with all due respect, that the law has settled in the right place. It nevertheless suggests that there is something wrong. It argues that we did not see the veil piercing cases for what they were because we had an incomplete understanding of what separate legal personality means. Separate legal personality was introduced in the Joint Stock Companies Act 1844. How is it possible that it took 175 years to fully understand the separate legal personality of the company? For decades we applied and taught a doctrine, that we said was about 'disregarding' the separate legal personality of the company, only to realise that it, in fact, never was. Concepts matter. Uncertain concepts undermine the development of the law. Theories provide explanations that help us better understand the concepts that we use. It is useful to determine what we mean by separate legal personality and how it can be explained. Once this has happened, we can appreciate why there never was and never should be a doctrine suggesting that the company's separate legal personality is to be 'disregarded'.

This article suggests that veil piercing as a doctrine of 'corporate disregard' might have persisted because judicial reasoning continued to be informed by a conception of the company that reflects the English model of partnership law. The partnership approach may have continued also because it fits with nexus of contracts and agency theories, which, starting from the late 1970s, have informed academic analysis of UK company law and characterise separate legal personality as a fiction for contracts between participants (section 4).

The article argues that the principle of separate legal personality can be explained through a modern version of real entity theory. It relies on scholarship from sociology and psychology on groups and organisations and argues that organisations are social phenomena that are real in their consequences (section 5). This approach differs from a significant strand of company law literature that draws on the insights of law and economics. The purpose of this article is to advance a positive theoretical account within a sociological and psychological framework rather than to refute or persuade those who favour an economic account, although mention is made of the properties of the nexus of contracts model.

The article then draws a connection between real entity theory and separate legal personality (section 6). It suggests that the law finds organisations or firms and makes available the corporate form with a view to enabling them to better function independently and also with a view to imposing liability on

them.[3] We will also note that commercial ventures and their need for money and efficient management were at the heart of the foundations of the modern Companies Act and continue to occupy a central place in its evolution.

Using real entity theory, the company can be conceptualised as a legal mechanism allowing an organisation or a firm to act autonomously of its participants. It does more than providing a fictional nexus for contracting. This argument can be supported by reference to the history of modern company law. It can also be supported through an analysis of the characteristics of rules governing the formation and termination of modern companies. The liability of companies in tort, criminal and regulatory law supplies a further argument that companies do more than serve as a fictional nexus for contracting.

The article acknowledges that the current version of the Companies Act does not require companies to operate organisations or firms (section 7). Companies are available for all lawful purposes. In addition to the paradigmatic case of a company operating an organisation or a firm, companies are sometimes incorporated to do nothing but hold an asset or to remain dormant for the time being. The article argues, however, that this does not harm the conclusion that the corporate form has evolved for a paradigmatic purpose. It is logically possible for a legal tool to be shaped by a primary purpose, which can be identified in its characteristics, while being available for other use cases.

Section 8 comes back to abuses of the corporate form, which the veil piercing rules were originally said to address. In addition to the concealment principle, according to which judges look behind smoke screens to establish salient legal facts, legislation and case law have substantially evolved in recent decades. It is no longer possible to characterise, as Otto Kahn Freund famously did in the 1940s, the decision in *Salomon v Salomon* as 'calamitous'. The law has, with all due respect, settled in the right place. It recognises the company as a separate legal entity while addressing abuses through doctrines outside of company law rather than through a principle justifying its 'disregard'. Section 9 concludes.

2. Veil piercing as a doctrine of 'corporate disregard'

2.1. Introduction

Before 2013 the courts and academic scholarship accepted what was referred to as the doctrine of 'piercing the corporate veil'. At the time the doctrine was

[3]The article uses the term 'organisation', which is more common in the wider social sciences, interchangeably with the term 'firm', which is preferred in Economics and highlights the link between the corporate form and business.

understood to mean that, in certain circumstances, the legal personality of the company is 'disregarded' and 'a person who owns and controls a company is … identified with it in law by virtue of that ownership and control'.[4]

2.2. Sham, façade and other metaphors

Under this approach the company came to be referred to as a 'sham', 'façade', 'cloak' or 'alter ego' of the shareholders. In an article published in 1968 Murray Pickering identifies the following broad range of metaphors used to describe companies in this context: 'a mere nominee', 'a mere fraud', 'an agent', 'a trustee', 'mere device', 'a myth and a fiction', 'a pretended association', an 'unreal' procedure, 'a cloak', 'an artificial legal thing', 'a legal abstraction', 'mere machinery', 'a metaphysical conception', 'a sham or bogus', 'an abstract conception', a 'simulacrum', 'a cloak', a 'mere alter ego', an 'abstract being', a 'creature', 'a screen' and even a 'black sheep'.[5]

The most recent judicial statement of this approach can be found in *Adams v Cape*, where Slade LJ endorsed a dictum by Lord Keith of Kinkel who held in *Woolfson v Strathclude* that 'it is appropriate to pierce the corporate veil only where special circumstances exist that it [the company] is a mere façade concealing the true facts'.[6] Likewise, Lord Cooke, writing extra-judicially, observed that 'the "mere façade" exception was well-recognised'.[7]

2.3. The enigma of the doctrine

The veil piercing doctrine, while persistently appearing in case law and academic scholarship, had two fundamental flaws. Its boundaries were unclear, and it was rarely, if ever, applied.

Evidence for the doctrine's lack of clarity can be found in the leading cases. Slade LJ, for example, wrote in *Adams v Cape* that there was 'rather sparse guidance as to the principles which should guide the court in determining whether or not the arrangements of a corporate group involve a façade'.[8] Lord Sumption concluded in *Prest v Petrodel* that '[r]eferences to "façade" or "sham" beg too many questions to provide a satisfactory answer'.[9] He wrote further that the doctrine 'is heavily burdened by authority, much of

[4]*Prest v Petrodel* [2013] 2 AC 415 at [16] (Lord Sumption); Sarah Worthington and Sinéad Agnew, *Sealy and Worthington's Text, Cases, & Materials in Company Law* (12th edn, OUP 2022) 35; Brenda Hannigan, *Company Law* (6th edn, 2021 OUP) para [3.14].
[5]Murray Pickering, 'The Company as A Separate Legal Entity' 31 (1968) MLR 481, 481–82. Perhaps the most creative of these was used by Templeman LJ in *Re Southard&Co Ltd* [1979] 1 WLR 1198 at 1208 (CA) who referred to a subsidiary company in precarious financial condition as the 'runt of the litter'.
[6]*Adams v Cape* [1990] Ch 433 (CA) at 539 (Slade LC).
[7]Lord Cooke, *A Real Thing, Turning Points of the Common Law, The Hamlyn Lectures* (Sweet & Maxwell 1997) 17.
[8]*Adams v Cape* [1990] Ch 433 (CA) at 543.
[9]*Prest v Petrodel* [2013] 2 AC 415 at [28] (Lord Sumption).

it characterised by incautious dicta and inadequate reasoning'.[10] Lord Neuberger wrote in *VTB v Nutritek* that the 'precise nature, basis and meaning of the principle are all somewhat obscure, as are the precise nature of circumstances in which the principle can apply'.[11] Lord Neuberger also observed that pejorative expressions such as sham, mask or cloak

> are often dangerous, as they risk assisting moral indignation to triumph over legal principle, and, while they may enable the court to arrive at a result which seems fair in the case in question, they can also risk causing confusion and uncertainty in the law.[12]

Academic commentators agreed with this assessment. The editors of Gower and Davies's 2012 edition characterised the law before the decision in *Prest* as 'haphazard'.[13] Professor Sarah Worthington and Dr Sinéad Agnew describe the veil piercing rules as expressed before *Prest* as 'exceptionally messy, and seemingly impossible to rationalise'.[14] Professor Alan Dignam and Professor Peter Oh observed that for over a century, UK courts have 'struggled to negotiate a coherent approach to the circumstances in which the *Salomon* principle … will be disregarded'.[15] They describe the law as 'confused'.[16] '[T]he principle and its limits are contested by both academic legal scholarship and the judiciary.'[17]

In addition to being unclear the doctrine also appears to have been rarely, if ever, applied. Lord Sumption observed that 'most of the statements of principle in the authorities are obiter, because the corporate veil was not pierced'.[18] Lord Neuberger wrote that 'there is not a single instance in this jurisdiction where the doctrine has been invoked properly and successfully'.[19] He also pointed out that the doctrine 'appears never to have been invoked successfully and appropriately in its 80 years of supposed existence'.[20] Robert Miles QC and Eleanor Holland argued that the concept of piercing the corporate veil 'has much exercised judges and commentators' but it 'is in fact an extremely rare specimen. It has arguably never been seen in the wild'.[21]

[10] ibid at [19] (Lord Sumption).
[11] *VTB v Nutritek* [2013] 2 AC 337.
[12] ibid at [124].
[13] Paul L Davies and Sarah Worthington, *Gower & Davies, Principles of Modern Company Law* (9th edn, Sweet & Maxwell 2012) 214; see also Marc Moore, 'A Temple Built on Faulty Foundations: Piercing the Corporate Veil and the Legacy of *Salomon v Salomon*' [2006] JBL 180.
[14] Worthington and Agnew (n 4) 35.
[15] Dignam and Oh (n 2) 16.
[16] ibid 18.
[17] Ibid 17.
[18] *Prest v Petrodel* [2013] 2 AC 415 at [27] (Lord Sumption).
[19] ibid at [64] (Lord Neuberger).
[20] ibid at [79] (Lord Neuberger).
[21] Robert Miles and Eleanor Holland, 'Piercing the Corporate Veil' in Edwin Simpson and Miranda Steward (eds), *Sham Transactions* (OUP 2013) 192, 206.

Despite these serious shortcomings the doctrine has nevertheless persisted. Lord Sumption remarked in *Prest v Petrodel* that 'the consensus that there are circumstances in which the court may pierce the corporate veil is impressive'.[22] Lord Neuberger observed that the doctrine 'has been generally assumed to exist in all common law jurisdictions'.[23] The number of cases associated with the doctrine is remarkable. Professor Alan Dignam and Professor Peter Oh identified and empirically analysed 213 veil piercing cases in 2019.[24] Charles Mitchell conducted a similar study in 1999, analysing 290 cases.[25]

Why did a doctrine that was all but impossible to define and had arguably never been applied persist so tenaciously? It will be suggested in section 4 that this happened because the judges may have inadvertently been reasoning on the basis of a partnership model of the company. It is also possible that the nexus of contracts model, which characterises companies as fictions facilitating contracting between participants and is currently the dominant theoretical approach, was a contributing factor. Before that we will analyse how veil piercing has been redefined.

3. Veil piercing redefined

3.1. Introduction

In 2013 the Supreme Court restated the veil piercing doctrine. Lord Sumption introduced a distinction between cases of 'concealment', where an independent veil piercing doctrine was not present,[26] and cases of 'evasion', where it was.[27] Later cases have cast doubt on whether 'evasion' will continue to exist. Moreover, we will see below that 'evasion' even if we accept its continued existence, does not involve the 'disregard' of the company's separate legal personality.

3.2. Concealment and evasion

In *Prest v Petrodel* Lord Sumption reasoned that in most veil piercing cases the term was used as a label. They should be referred to as instances of 'concealment'. Lord Sumption wrote,

> The concealment principle is legally banal and does not involve piercing the corporate veil at all. It is that the interposition of a company or perhaps

[22] *Prest v Petrodel* [2013] 2 AC 415 at [27] (Lord Sumption).
[23] ibid at [80] (Lord Neuberger).
[24] Dignam and Oh (n 2) 16 (22).
[25] Mitchell (n 2).
[26] For an earlier articulation of this point see Lord Cooke, *A Real Thing, Turning Points of the Common Law, The Hamlyn Lectures* (Sweet & Maxwell 1997) 13–15 and 17.
[27] *Prest v Petrodel* [2013] 2 AC 415.

> several companies so as to conceal the identity of the real actors will not deter the courts from identifying them, assuming that their identity is legally relevant. In these cases, the court is not disregarding the 'facade', but only looking behind it to discover the facts which the corporate structure is concealing.[28]

The company in these cases is treated in the same way as any natural person, 'say Mr Dalby's uncle',[29] (his spouse or partner) who is assisting someone to hide salient facts.

Lord Sumption then reduced 'veil piercing' as an independent doctrine of company law to what he referred to as cases of 'evasion'. Evasion is a situation where someone interposes a company to avoid an existing obligation. He identified two examples, *Guildford Motor v Horne* and *Jones v Lipmann*.[30] Both cases could have been decided on other grounds. But they were left standing as examples for 'veil piercing' as an independent doctrine of company law.

The effect of *Prest* is to significantly narrow the instances where veil piercing as a company law doctrine is held to apply. There was agreement across the bench that the circumstances where the veil will be pierced will be very rare.[31]

3.3. The retreat of evasion

On its own *Prest* already significantly reduces the scope of an independent veil piercing doctrine. The evasion principle, as defined in *Prest*, only applies in circumstances where someone interposed a company to avoid an obligation that they owed. It binds the company to a shareholder obligation. It is not available to do the reverse and impose a liability on a shareholder for an obligation owed by a company.[32]

Evasion, however, may not persist as a doctrine. Academic scholars have pointed out that the distinction between concealment, where the term 'veil piercing' operates as a label, and evasion, where Lord Sumption considered it to be an independent doctrine, lacks clarity.[33] Lord Sumption himself conceded that many cases will 'fall into both categories'.[34] Lady Hale wrote that

[28] *Prest v Petrodel* [2013] 2 AC 415 at [28] (Lord Sumption).
[29] ibid at [31] (Lord Sumption).
[30] See also *M v M* [2013] EWHC 2534 (Fam), which applied the evasion principle as stated in *Prest*.
[31] ibid at [103] (Lord Clarke) and at [98] (Lord Mance).
[32] *Hurstwood v Rossendale* [2021] 2 WLR 1125 at [72] (Lord Briggs and Lord Leggatt); Edwin C Mujih, 'Piercing the Corporate Veil: Where is the Reverse Gear?' 133 (2017) LQR 322.
[33] B Hannigan, 'Wedded to Salomon: Evasion, Concealment and Confusion on Piercing the Veil of the One-Man Company' [2013] 50 Irish Jurist 11; Peter Bailey, 'Lifting the Corporate Veil Becomes a Remedy of Last Resort after *Prest v Petrodel* in Supreme Court' (2013) 336 Company Law Newsletter 1; William Day, 'Skirting Around the Issue: The Corporate Veil after *Prest v Petrodel*' [2014] L.M.C.L.Q. 269; Mohamed F Khimji and Christopher C Nicholls, 'Corporate Veil Piercing and Allocation of Liability – Diagnosis and Prognosis' (2015) 30 Banking and Finance Law Review 211; Edwin C Mujih, 'Piercing the Corporate Veil as a Remedy of Last Resort after *Prest v Petrodel Resources Ltd*: Itching Towards Abolition?' (2016) 37 Company Lawyer 39.
[34] *Prest v Petrodel* [2013] 2 AC 415 at [28] (Lord Sumption).

she was not sure 'if it is possible to classify all of the cases in which the courts have been or should be prepared to disregard the separate legal personality of a company neatly into cases of either concealment or evasion'.[35]

Further, Lord Walker expressed doubts about the existence of veil piercing as an independent doctrine. His dicta have had substantial influence on the cases decided post *Prest*. He reasoned that the veil piercing doctrine did not exist as an independent rule. It was not a 'coherent principle or rule of law' but a label.[36] Lord Neuberger, while ultimately following Lord Sumption's distinction, was also 'strongly attracted by the argument' that the doctrine 'should be given its quietus'.[37]

In *Hurstwood Properties v Rossendale* Lord Briggs and Lord Leggatt shared Lord Walker's doubts as to whether veil piercing was a rule of law rather than a 'label used to describe the disparate occasions on which some rule of law produces apparent exceptions to the principle of the separate juristic personality of the corporate body'.[38] In *Gramsci v Recoletos* Beatson LJ discussed *Prest* and predicted that an independent veil piercing doctrine, having been regarded as unprincipled, would come to be seen as an anomaly incapable of further development.[39]

The fact that the distinction between evasion and concealment is hard to draw combined with the influence of Lord Walker's dictum on later cases has led to a situation where we can conclude that the evasion, as the much-diminished remnant of an independent veil piercing doctrine, may not have a future.[40] Either way, however, even if evasion continues to have traction we need to note that the two cases where it was said to apply do not involve a 'disregard' of the company's separate legal personality. In *Gilford* the company's existence was not challenged. The case concerned an injunction, which the company was subjected to, and this pre-supposes that the company exists.[41] In *Jones* a contract was enforced against the company, which also can only happen if its existence is recognised.[42]

Seen from this perspective the language of veil piercing reveals itself as misleading. Rather than being examples of a – previously large now much diminished – doctrine justifying the 'disregard' of the separate personality the cases turn out to all along have recognised the company as a separate legal entity.[43]

[35]ibid at [92] (Lady Hale).
[36]ibid at [106] (Lord Walker).
[37]ibid at [79] (Lord Neuberger); see also *Persad v Singh* [2017] BCC 799 at [17] (Lord Neuberger).
[38]*Hurstwood v Rossendale* [2021] 2 WLR 1125 at [71] (Lord Briggs and Lord Leggatt).
[39]*Gramsci Shipping v Recoletos* [2013] EWCA Civ 730 [2014] BusLR 239 at [66] and [60].
[40]Derek French, *Mayson, French & Ryan on Company Law* (37th edn, OUP 2021) 118.
[41]*Gilford Motor Co Ltd v Horne* [1933] Ch 935 at 937, 960, 961–62, and 965.
[42]*Jones v Lipman* [1962] 1 WLR 832 at 837.
[43]Christian Witting, 'Piercing the Corporate Veil' in William Day and Sarah Worthington (eds), *Challenging Private Law, Lord Sumption on the Supreme Court* (Hart 2020) 325.

3.4. Summary

The Supreme Court has redefined veil piercing into two categories: concealment and evasion. Under the concealment principle the company is treated in the same way as a natural person would be treated. In identical circumstances a company controlled by Dalby and Dalby's uncle face the same consequences. The term 'veil piercing' is merely used as a label. There is no corporate 'disregard'. The evasion principle also does not involve a 'disregard' of the company's separate legal personality. It applies, if it continues to have traction, to impose a liability on a company, the separate legal personality of which is fully recognised. Both concealment and evasion accept the company as a separate legal entity.

It would be possible to stop here and conclude that we have now and finally fully understood the veil piercing cases. This, however, would be a mistake. The persistent and prolonged uncertainty caused by the idea that the company's separate legal personality can and should be 'disregarded' reveals a conceptual misunderstanding in the doctrinal analysis of company law. We would benefit from understanding how it was possible for legal doctrine to persistently chase an elusive concept that undermines a foundational principle of company law. It will be argued in the next section that a particular understanding of the separate legal personality of the company could explain why we have misunderstood the cases in this area. We have adhered to an idea of the company that is shaped by its historical roots in English partnership law. It is also possible that the idea has been legitimised by the prevailing nexus of contracts explanation of the company, which conceives of companies as fictions. This understanding of the concept of separate legal personality may have affected our ability to see veil piercing for what it always was. We will further show that a modern version of real entity theory could be used to explain the principle of separate legal personality and can consequently help to finally lay to rest what all along was a barely workable approach.

4. Explaining the difficulty with recognising separate legal personality

We have concluded so far that the metaphors that were associated with veil piercing as a doctrine before the decision in *Prest* suggest that the company concerned and its shareholders are 'identical' and the separate legal personality of the company is 'disregarded'. In this view the company is not an actor in its own right. The real actors are shareholders who use the company as their 'cloak'. Murray Pickering articulates this when he writes about the company being 'simply a means by which the property and associated

rights of numerous individuals may be amalgamated and reconstituted for their more efficient and effective utilisation'.[44]

The idea that the company is a means through which shareholders aggregate their contributions characterises the company as akin to a partnership. It fits with the historical roots of company law, which evolved from a distinct model of partnership law.[45] In this model partnerships do not have separate legal personality.[46] These roots may have cast a shadow into the modern era. Derek French observes that anyone reading cases decided before the First World War will notice that judges in those days always treated the 'company' as a plural noun. The company was a 'they' rather than an 'it'.[47] 'Linguistically, the judges seemed to have been thinking of a company as an aggregate of its members.'[48] Law develops in a path dependent way. It is possible that the law continued to show the influence of these roots.

The idea that the company is an 'association' can also be found in contemporary academic scholarship. Derek French, for example, writes that the company is both a legal person and an association of its members.[49] The editors of *Gower* observe that there exists a powerful instinct to treat the company and its members as indistinguishable, especially when there is a single-controlling shareholder, whether an individual or a holding company.[50]

An English partnership model of the company also fits with the currently dominant nexus of contracts model, which conceives of the company as a fictional focus point for contracting between participants.[51] This characterisation of the company as a fiction through which the contributions of its participants are nothing more than aggregated can invite and legitimise arguments to ignore its separate legal personality and to, consequently, treat the company as an alter ego of its shareholder(s).

[44]Murray Pickering, 'The Company as a Separate Legal Entity' 31 (1968) MLR 481 (509); see also Sir Frederick Pollok's case note to *Salomon v Salomon* 13 (1897) LQR 6 (6–7).

[45]See e.g. Nathaniel Lindley and Samuel Dickinson, *A Treatise of the Law of Partnerships, Including Its Application to Companies* (4th edn, 1881).

[46]Other legal systems have models of partnership law that come closer to corporations. German Offene Handelsgesellschaften, for example, have separate legal personality and are registered (see also Henry Hansmann and Reinier Kraakman, 'The Essential Role of Organizational Law' 110 (3) (2000) The Yale Law Journal 387 and Mariana Pargendler, 'Regulatory Partitioning as a Key Function of Corporate Personality' in Elizabeth Pollman and Robert B Thompson (eds), *Research Handbook on Corporate Purpose and Personhood* (Elgar 2021) 263). In line with the argument advanced in this article partnership law can be characterised as an early organizational form, which continues to serve useful purposes but was and is ultimately unable to support the requirements of modern organizations. Indeed, in the UK the deed of settlement model came to be superseded by company law as we now know it.

[47]Derek French, *Mayson, French & Ryan on Company Law* (37th edn, Oxford University Press 2021) 138.

[48]ibid 138.

[49]ibid 5, see also 98, 128, 130, 135.

[50]Paul L Davies, Sarah Worthington, and Christopher Hare, *Gower Principles of Modern Company Law* (11th edn, Sweet & Maxwell 2021) para 7-001.

[51]Michael C Jensen and William H Meckling, 'Theory of the Firm: Managerial Behaviour, Agency Costs and Ownership Structure', 3 (4) (1976) Journal of Financial Economics 305; see also John Armour and others, *The Anatomy of Corporate Law* (3rd edn, Oxford University Press 2017) 5.

It is possible that veil piercing persisted as a doctrine of 'corporate disregard' because the urge to associate the company with its shareholders was so ingrained that we adopted an incomplete understanding of the concept of separate legal personality. This encouraged us to operate a principle of 'corporate disregard' that we knew did not work and that we also never applied. But we kept going faithful to the historic roots of company law and perhaps also reassured by the nexus of contracts model.

It would seem that it has been difficult to move the company out of the orbit of partnership law. Theory provides an explanation. Explanations can be useful to give context to legal concepts, assisting us to appreciate their boundaries. It will be argued below that it would be beneficial to consider real entity theory as an alternative model of the company. A modern version of real entity theory can supply an explanation for the principle of separate legal personality and help to better understand the concept of the separate legal personality of the company.

5. Real entity theory

5.1. Introduction

The well-known alternative to the partnership/nexus of contracts model is real entity theory. The origins of real entity theory are sometimes attributed to German jurist Otto von Gierke and the social theorist Walter von Rathenau.[52] In the UK Frederic Maitland was an eminent proponent of real entity theory.[53] In the early twentieth century real entity theory was arguably the dominant theoretical approach.[54] In its traditional form the model is unappealing because it is anthropomorphic.[55] It characterises the company as a human being where the directors act as the brain and workers operate as arms and legs. This way of describing the company dates back to a time

[52]Ron Harris, 'The Transplantation of the Legal Discourse on Corporate Personality Theories: From German Codification to British Political Pluralism and American Big Business' (2006) 63(4) Washington and Lee L Rev 1421 traces the theory's earlier origins; see generally Joshua Getzler, 'Law, History and the Social Sciences: Intellectual Traditions of Late Nineteenth- and Early Twentieth-Century Europe' in Andrew Lewis and Michael Lobban (eds), *Law and History: Current Legal Issues*, vol 6 (OUP 2004) 215.

[53]FW Maitland and Otto Gierke, *Political Theory of the Middle Age* (CUP 1900, reprinted in 1996, Thoemmes Press); see also Frederick Hallis, *Corporate Personality A Study in Jurisprudence* (OUP 1930) and Adolf Berle, 'The Theory of Enterprise Entity' (1947) 47 Columbia L Rev 343. Rathenau's work is cited in the seminal book dolf Berle and Gardiner Means, *The Modern Corporation and Private Property* (Legal Classics Library 1993) (see Martin Gelter, 'Taming or Protecting the Modern Corporation? Shareholder-Stakeholder Debates in a Comparative Light' (2010–2011) 7 NYU JL&Bus 641, 644); see also Ernst Freund, *The Legal Nature of Corporations* (University of Chicago Press 1897).

[54]Daniel Lipton, 'Corporate Capacity for Crime and Politics: Defining Corporate Personhood at the Turn of the Twentieth Century' (2010) 96 Virginia L Rev 1911 citing scholars around Berle and Means; for a modern discussion of the theory see David Gindis, 'From Fictions and Aggregates to Real Entities in the Theory of the Firm' (2009) 5 Journal of Institutional Economics 25 at 34; see also Ewan McGaughey, 'Ideals of the Corporation and the Nexus of Contract' (2015) 76(6) MLR 1057 at 1061.

[55]Jennifer Payne, 'Corporate Attribution and the Lessons of *Meridian*' in Paul S Davies and Justine Pia, *The Jurisprudence of Lord Hoffmann* (Bloomsbury 2015) 357 (361); Gindis (n 54) 25.

before the social sciences began to take an interest in organisations. It was based on intuitions.[56] Today we have scholarship that helps us to better understand human behaviour as well as organisations. That scholarship supports a modern version of real entity theory.

5.2. Organisations as real entities

Real entity theory posits that organisations or firms exist, to some extent, autonomously of their participants. To explain this perspective further it useful to begin with human behaviour.

5.2.1. Rational, natural and socially structured action

It has been empirically shown that human beings are capable of rational action but that they do not always base their actions on rational decision-making.[57] Much of human decision-making and behaviour is automated. Human beings adopt habits.[58] We also adapt behaviour to the social context. We, for example, dress, speak and behave differently in a private and in a professional capacity. When we interact with other people our behaviour is shaped by the habits and routines that are the consequence of previous interactions with these same individuals. When we act as members of an organisation our behaviour is affected by the policies and procedures adopted by that organisation. It is also affected by the informal understanding that we have become aware of in the course of interacting with other individuals working in the same social environment.[59]

When human beings work together, they establish routines. As the co-operation intensifies and increases in size these routines develop into processes and procedures. These affect everyone cooperating with an organisation, the person(s) who started the venture as well as those who work for it, supply it with resources or become its customers. An organisation emerges. As the size of this organisation increases some of these processes and procedures become formalised, and a culture emerges.[60] These affect how

[56]Eva Micheler, *Company Law – a Real Entity Theory* (OUP 2021) 20.
[57]Daniel Kahneman, *Thinking, Fast and Slow* (Penguin 2011) 21–38.
[58]See also Roger C Shank and Robert P Abelson, *Script, Plans, Goals and Understanding: An Inquiry into Human Knowledge Structures* (Hillsdale 1997), who argue that human action operates on the basis of pattern recognition. When new situations display similarities with previous experience, they trigger pre-existing scripts and lead to sequences of action borrowed from a well-known situation.
[59]Christian List and Philipp Pettit, *Group Agency: The Possibility, Design and Status of Corporate Agents* (OUP 2011); Susanna K Ripken, 'Corporations are People Too: A Multi-Dimensional Approach to the Corporate Personhood Puzzle' (2009) 15 Fordham Journal of Corporate and Financial Law 98, 131–33 and also Christian Witting, *Liability of Corporate Groups and Networks* (CUP 2018) 49.
[60]For an overview of the literature on corporate culture see Nien-he Hiseh, Benjamine Lange, David Rodin, and MLA Wolf-Bauwens, 'Getting Clear on Corporate Culture: Conceptualisation, Measurement and Operationalisation' (2018) 6 Journal of the British Academy 155; see also Andrew M Pettigrew, 'On Studying Organizational Cultures' (1979) 24(4) Administrative Science Quarterly 570; Mats Alvesson and Stefan Sveningsson, *Changing Organizational Culture: Cultural Change Work in Progress* (Routledge

individuals act.[61] Organisations bring about behaviour that would otherwise not exist.[62] Psychological experiments have shown that not only the behaviour, but also the perception of individuals is modified by the belief that they are acting as part of an organisation.[63]

5.2.2. Social structure

Together, the routines, process, procedures and culture that shape human action can be referred to as social structure. Organisations are the social structure which comes about when human beings work together. Social structure is persistent. New participants join, learn the behaviour, adopt it, and teach it to those who join after them. The routines adopted in an organisation are the result of experience-based learning processes. They are a source of conscious and tacit knowledge, which is socially held and helps organisations to succeed in the marketplace.[64] Because social structure shapes human behaviour we can conclude that organisations are real. They are real not in a tangible way but rather in their consequences.

The American philosopher, John R Searle distinguishes 'brute facts', such as people, houses, dogs or plants from 'social facts'.[65] The latter exist because there is a collective understanding that they exist. In this view organisations are like football teams. Their members act as part of a team. Non-members take part in this intention because they agree that the members

2008); Kim S Cameron and Robert E Quinn, *Diagnosing and Changing Organizational Culture: Based on a Competing Values Framework* (3rd edn, Jossey-Bass 2011); W Brook Tunstall, 'Cultural Transition at AT&T' (1983) 25(1) Sloan Management Review 15; Noel M Tichy, 'Managing Change Strategically: The Technical, Political and Cultural Keys' (1982) 11(2) Organizational Dynamics 59.

[61] For a foundational analysis of this point see Thorstein Veblen, 'The Limitations of Marginal Utility' (1909) 17 Journal of Political Economy 235 at 245; see also Andrew Van de Ven, 'The Institutional Theory of John R Commons: A Review and Commentary' (1993) 18 Academy of Management Review 129 and Herbert Simon, Administrative Behaviour: A Study of Decision-Making Processes in Administrative Organizations (4th edn, The Free Press 1997).

[62] Dianne Vaugham, *The Challenger Launch Decision* (University of Chicago Press 1996); see also David Welsh and others, 'The Slippery Slope: How Small Ethical Transgressions Pave the Way for Larger Future Transgressions' (2015) 100 Journal of Applied Psychology 114; Michel Ehrenhard and Timo Fiorito, 'Corporate Values of the 25 Largest European Banks: Exploring the Ambiguous Link with Corporate Scandal' (2018) Journal of Public Affairs 1, 4 and 7; see also Henrich Greve, Donald Palmer, and Jo-Ellen Pozner, 'Organizations Gone Wild: The Causes, Processes, and Consequences of Organizational Misconduct' (2010) 4(1) The Academy of Management Annals 53.

[63] Lynne G Zucker, 'The Role of Institutionalization in Cultural Persistence' (1977) 42 American Sociological Review 726; see also Yuval Feldman, *The Law of Good People* (CUP 2008) 105–124; Yuval Feldman, Adi Libson, and Gideon Parchomovsky, 'Corporate Law for Good People' (2021) 115 Northwestern University Law Review 1125.

[64] W Richard Scott, *Institutions and Organizations* (4th edn, Sage 2014) 36; Nicolai J Foss, 'Bounded Rationality and Tacit Knowledge in the Organizational Capabilities Approach an Assessment and a Re-evaluation' (2003) 12(2) Industrial and Corporate Change 185; for a foundational contribution see Edith Penrose, *The Theory of Growth of the Firm* (4th edn, OUP 1995); the importance of tacit knowledge has been recognised by legal scholars, see e.g. Brian Cheffins, 'Corporations' in Mark Tushnet and Peter Cane (eds) *The Oxford Handbook of Legal Studies* (OUP 2005) 485 at 497 and Edward B Rock and Michael L Wachter, 'Islands of Conscious Power: Law, Norms and the Self-Governing Corporation' (2001) University of Pennsylvania Law Review 1619.

[65] John R Searle, *The Construction of Social Reality* (Free Press 1995).

do not act as individuals but as members of an organisation. An organisation is something that, by consensus, is treated by everyone as a social unit.[66] Organisations are not associated with any particular brute fact. They are nevertheless real in their consequences.

5.2.3. Human agency

In addition to social structure, there exists human agency, which is capable of deviating from social structure. Human agency also modifies social structure over time. The interaction between social structure on the one hand and human agency on the other is complex.[67] There is a debate on the extent to which social structure limits human agency.[68] Some scholars put a strong emphasis on structure.[69] Others put more weight on individual agency. W Richard Scott observes that all, even innovative, action is affected by existing contexts and must adjust to it.[70] Conceiving of organisations as characterised by their processes, which affect human behaviour, should not be misunderstood as a reactionary normative agenda. Processes are a double-edged sword.[71] They also operate to facilitate change. The effect of organisational structure has been empirically proven to exist. Decisions made at the founding stage have been shown to 'imprint organisational characteristics that help determine an organization's future direction'.[72]

[66]Richard Adelstein, 'Firms as Social Actors' (2010) 6(3) Journal of Institutional Economics 329.

[67]Paul J DiMaggio and Walter W Powell, 'The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields' (1983) 48 American Sociological Review 147; Pursey PMAR Heugens and Michel W Lander, 'Structure! Agency! (And Other Quarrels): A Meta-Analysis of Institutional Theories of Organization' (2009) 52 Academy of Management Journal 61; Patricia H Thornton, William Ocasio, and Michael Lounsbury, *The Institutional Logistics Perspective: A New Approach to Culture, Structure, and Process* (OUP 2012); Thomas B Lawrence, Roy Suddaby and Bernard Leca (eds), *Institutional Work* (CUP 2009).

[68]Mats Alvesson and Stefan Sveningsson, *Changing Organizational Culture: Cultural Change Work in Progress* (Routledge 2008); Kim S Cameron and Robert E Quinn, *Diagnosing and Changing Organizational Culture: Based on a Competing Values Framework* (3rd edn, Jossey-Bass 2011); W Brook Tunstall, 'Cultural Transition at AT&T' (1983) 25 (1) Sloan Management Review 15; Noel M Tichy, 'Managing Change Strategically: The Technical, Political and Cultural Keys' (1982) 11 (2) Organizational Dynamics 59.

[69]Michael T Hannan and John Freeman, 'The Population Ecology of Organizations' (1977) 82(5) American Journal of Sociology 929.

[70]Scott (n 64) 262.

[71]ibid 273; see also Junlie Battilana and Thomas D'Aunno, 'Institutional Work and the Paradox of Embedded Agency' in Thomas B Lawrence, Roy Suddaby and Bernard Leca (eds), *Institutional Work* (CUP 2009) 31; V Lynn Meek, 'Organizational Culture: Origins and Weaknesses' (1988) 9(4) Organizations Studies 453 at 462–65; see also Anthony Giddens, *The Constitution of Society* (University of California Press 1984) 25–28 and 327 and Joanne Martin and Caren Siehl, 'Organizational Culture and Counterculture: An Uneasy Symbiosis' (1983) Organizational Dynamics 52.

[72]Warren P Boeker, 'The Development and Institutionalization of Subunit Power in Organizations' (1989) 34(3) Administrative Science Quarterly 388 at 408; see also Arthur L Stinchcombe, 'Social Structure and Organization' in James G March (ed), *Handbook of Organizations* (Rand McNally 1965) 142; see also Pettigrew (n 60) 570.

5.2.4. Size

Admittedly the significance of social structure increases with the size of an organisation. But even in a small organisation or firm habits and routines establish themselves and it takes deliberate effort and time to change these.

5.2.5. Beyond anthropomorphism

So far, we have argued that organisations can be characterised as real autonomous actors. They are more than the aggregation of the contributions from their participants. To be sure, this does not characterise them as human beings and so is not an anthropomorphic argument. Anthropomorphism is wrong because the metaphor only fits with an extreme structural model where there is no human agency. Organisations are characterised by the habits, routines, processes, procedures, and culture that human social interaction brings about. These are not biological but social phenomena which can be and are researched and understood by the methods available to the social sciences. In addition to the social structure shaping human action and thereby creating organisational action, there exists human agency, which is capable of deviating from social structure.

5.3. Summary

We have seen in this section that there is scholarship that supports the conclusion that organisations are autonomous entities that are real in their consequences, affecting brute facts through human beings displaying socially structured natural behaviour. If we accept the conclusions of this section, our next question for this article is: Can a real entity approach explain the principle of separate legal personality?

6. Establishing a link between real entity theory and separate legal personality

6.1. Introduction

This article argues that a link can be drawn between real entity theory and separate legal personality. It suggests that law finds organisations as a social phenomenon and makes an important contribution. It provides them with a mechanism that allows them to function better. This point can be substantiated by reference to the history of modern companies. It also can be supported by reference to the process through which companies are formed and terminated as well as through the rules imposing tortious and criminal liability as well as regulatory obligations on companies.

6.2. Historical context

Historically the provision of a legal form for organisations coincided with the period following the Enlightenment. From this time onwards individuals, organisations and the nation state became the primary categories of actors. W Richard Scott writes that the recognition of separate legal personality through law is not the cause for the rise of organisations but an 'indicator of the growing independence of these new corporate forms as they become recognized as legal persons in the eyes of the law'.[73] This does not undermine the point that there is also a causal effect the other way (top-down rather than bottom-up), with the availability of the corporate form operating as a co-constitutive ingredient for the rise of modern organisations and firms.[74]

We should also note that, while legal personality and the corporation existed before then, the Companies Act was first adopted to create a more suitable and better accountable tool for the large-scale commercial ventures of the Industrial Revolution, where the amount of finance required cannot easily be supplied through a partnership model or through debt financing. Business and its need for not only money but also for efficient management of both resources and a workforce was and continues to be at the heart of the corporate form.

The history of modern company law shows that the modern version of real entity theory set out above can explain separate legal personality. Between 1720 and 1844 the South Sea Bubble Act made incorporation very difficult.[75] In the UK this led to the emergence of deed of settlement companies.[76] These companies did not have separate legal personality but were legally constructed through partnership and trust law.[77] The investors

[73]Scott (n 64) 89.

[74]For contributions stressing the importance of the legal form for the development of the business firm see e.g. Simon Deakin, David Gindis, and Geoffrey M Hodgson, 'What is a Firm? A Reply to Jean-Philippe Robé' 17 (2021) Journal of Institutional Economics 861; Simon Deakin and others, 'Legal Institutionalism: Capitalism and the Constitutive Role of Law' (March 2015) Centre for Business Research, University of Cambridge Working Paper No 468 <www.jbs.cam.ac.uk/wp-content/uploads/2023/05/cbrwp468.pdf>; Eric Orts, *Business Persons, a Legal Theory of the Firm* (OUP 2013); Abraham A Singer, *The Form of the Firm* (OUP 2019); Simon Deakin, 'The Juridical Nature of the Firm' in *Sage Handbook of Corporate Governance* (2012) 113.

[75]The South Sea Bubble Act 1720, 6 Geo I, c 18.

[76]Nathaniel Lindley and Samuel Dickinson, *A Treatise on the Law of Partnership Including its Application to Companies* (4th edn, Westminster Hall 1878) 7.

[77]Michael Lobban, 'Joint Stock Companies' in William Cornish and others, *The Oxford History of the Laws of England*, vol XII, 1820–1914 Private Law (OUP 2010) 613; William Cornish and others, *Law and Society in England 1750–1950* (Hart 2019) 243–44; John Armour, 'Companies and Other Associations' in Andrew Burrows (ed), *English Private Law* (OUP 2013) [3.45]; Paul Davies, *Gower's Principles of Modern Company Law* (6th edn, Sweet & Maxwell 1997) 29–31; John Morley, 'The Common Law Corporation: The Power of the Trust in Anglo-American Business History' (2016) 116 Columbia L Rev 2145; Joshua Getzler and Mike Macnair, 'The Firm as an Entity before the Companies Act' (November 2006) University of Oxford Faculty of Law Legal Studies Research Paper Series, Working Paper No 47/2006; Joshua Getzler, 'Plural Ownership, Funds, and the Aggregation of Wills' (2009) 10 Theoretical Inquiries in Law 241; see also Paddy W Ireland, 'The Rise of the Limited Liability Company' (1984) 12 International Journal of Sociology of Law 239, 241.

transferred assets to trustees. Directors were appointed to manage the business. The investors received shares, with such rights to transfer the shares as the deed of settlement provided.[78] The principles of the law of partnerships, slightly modified, were thought to be applicable to these companies.[79] Deed of settlement companies were, however, cumbersome to operate. It was, for example, difficult for them to sue or be sued.[80] The Companies Act 1844 was therefore adopted and made available a more suitable and better accountable legal vehicle for the business ventures of that time.[81]

This historical background shows that separate legal personality can be described as helping organisations or firms to better function and to be responsible as subjects in the eyes of the law.[82] Professor Ronald Gilson argues that corporate law makes it possible for a corporation to become a 'real boy'.[83] It is suggested here that the point is better made in reverse. Corporate law makes it possible for real entities to become formal subjects of the law. It allows a social reality to become fully integrated into the legal system. Separate legal personality creates a formal legal unit which can operate independently from its members, directors, customers, suppliers and other stakeholders. This includes but is not limited to the ability for the company to make contracts or hold assets.

6.3. Formation

In addition to the historical roots of modern companies, the process through which companies are formed supports the argument that the corporate form is designed for the primary purpose of enabling an organisation or a firm to operate autonomously. This process consists of steps, the content and nature of which, can be explained by reference to a real entity approach.[84]

The formation process can be set in motion by one or more individual(s). There are also company formation agents, who set up hundreds of companies and operate their respective registered offices. In these instances, a company is set up before or irrespective of whether there is an intention for it to operate an organisation or a firm. However, irrespective of who sets up the company or for what purpose it is set up, those, who register a company need to give it a name that is distinct from the names of companies

[78]Lobban (n 77) 613; Cornish and others (n 77) 243–44; Armour (n 77) [3.45]; Andreas Televantos, *Capitalism Before Corporations: The Morality of Business Associations and the Roots of Commercial Equity and Law* (OUP 2020) 35–52.
[79]Ireland (n 77) 39.
[80]Davies (n 77) 31–32; Lobban (n 77) 618–19; Televantos (n 78) 43–51.
[81]Lobban (n 77) 617–23; Televantos (n 78) 43; Ireland (n 77) 241–42.
[82]See also Gindis (n 54) 25 at 39 and 41; see also David Gindis, 'Ernst Freund as the Precursor of the Rational Study of Corporate Law' (2020) 16(5) Journal of Institutional Economics 597.
[83]Ronald Gilson, 'From Corporate Law to Corporate Governance' in Jeffrey N Gordon and Wolf-Georg Ringe (eds), *The Oxford Handbook of Corporate Law and Governance* (OUP 2015) 7.
[84]CA 2006, s 9.

that have already been registered. They need to identify its registered office, a physical place to which documents can be sent, as well as an email address.[85] They need to appoint the first officers, who are to represent the company.[86] Companies are also publicly registered. Once the company has been registered a certificate of incorporation is issued as conclusive proof of its legal existence.[87]

The characteristics of the corporate formation process can be explained as having the purpose of enabling organisations to interact autonomously with third parties through a distinct name, a publicly identified agent, physical location, and email address. It is further possible to argue that the public register and the certificate of incorporation overcome the problem that an organisation does not have a brute physical existence. We have explained earlier that organisations are social facts. While it is right to say that organisations exist in reality, they are not permanently identified with any particular person or asset. Separate legal personality can be explained as a tool assisting an organisation or firm to autonomously engage in economic activity. Trusts and partnerships are also available for this purpose, but they do not serve it as well as companies do. Companies enable organisations to grow beyond the size to which a partnership or trust arrangement would be able to grow.

6.4. Termination

Like the formation the termination of a company requires the completion of a process, consisting normally of the winding up or liquidation of the company followed by its dissolution. During liquidation the company is represented by a liquidator or the Official Receiver, gives up its business, sells its assets, pays its debts and distributes any surplus amongst its members.[88] After that the dissolution process can start. If it appears that the realisable assets of the company are insufficient to cover the expense of its liquidation and the affairs of the company do not require any further investigation, the Official Receiver can apply for the company's dissolution but is required to give prior notice to the company's creditors.[89] The dissolution begins with an application to have the company removed from the register and is completed by it being struck off.[90]

[85]The requirement for an email address has been introduced by The Economic Crime and Corporate Transparency Act 2023 c 56, adding CA 2006, s 9(5)(aa).
[86]CA 2006, s 12; There is also a requirement for a statement of initial significant control (CA 2006, s 12A); If the company has a share capital a statement of capital and initial shareholdings needs to be added (CA 2006, s 10).
[87]CA 2006, s 15(4).
[88]Worthington and Agnew (n 4) 874–76.
[89]IA 1986, s 202.
[90]CA 2006, s 1003–1011 (voluntary strike off). The Registrar has the power to begin a dissolution process for companies, which are not carrying on business or are not in operation (CA 2006, s 1000), as well as

The process of winding up and dissolving a company needs to be completed before the separate legal personality of the company comes to an end. This applies even to illegal companies or those set up for fraudulent purposes. All companies exist until they are wound up and struck off the register.[91]

For our purposes we can observe that while it is said that fraud unravels everything,[92] it does not unravel the separate legal personality of the company. A contract and a trust induced by fraud can be rescinded by the innocent party to be considered as void ab initio. A company that has been set up or used for illegal or fraudulent purposes continues to exist.

The legal requirement for the completion of a winding up and dissolution process allows us to draw a link between companies and organisations or firms. If the company was simply a fictional nexus, it could be treated as non-existent, like a paradigmatic contract or a trust, certainly in cases of fraud or illegality. The legal requirement for winding up and dissolution gives the company as a legal tool a level of stability that goes beyond paradigmatic contract or trust law. This level of stability is valuable for organisations or firms. An organisation, once established, affects a number of actors, including but not limited to contractual parties. A winding-up process ensures that the relationships with these actors are brought to an end in an orderly manner. It ensures that the interests of all stakeholders are considered. While the process is applied to all companies no matter what their purpose it is essential for the paradigmatic case of a company operating an organisation.

Furthermore, a robust principle of separate legal personality is necessary to protect the integrity of the termination process of the company. A rule that resulted in the disregard of the company's separate legal personality would undermine the operation of the winding up and dissolution processes. Separate legal personality needs to be robust to enable these processes to run their course.

6.5. Accountability

Another link between real entity theory and separate legal personality is visible in the rules of corporate accountability. Professor Henry Hansmann and Professor Reinier Kraakman write that corporations facilitate asset partitioning.[93] They argue that the corporate form protects the funds of the corporation from

for companies whose liquidator is not acting or whose affairs have been fully wound up can be involuntarily struck off by the Registrar (CA 2006, s 1001).

[91] Examples of illegal companies are *In Re Senator Hanseatische Verwaltungsgesellschaft mbH* [1997] 1 WLR 515 (CA) (illegal lottery); *Re Equity and Provident Ltd* [2002] EWHC 186 (Ch), [2002] 2 BCLC 78 (worthless motor warranty plans); *Re PAG Management services Ltd* [2015] EWHC 2404 (CH) (illegal tax scheme); but see *PAG Asset Preservations* [2020] EWCA Civ 1017, [2020] BCC 979.

[92] *Prest v Petrodel* [2013] 2 AC 415 at [18] (Lord Sumption).

[93] Henry Hansmann and Reinier Kraakman, 'The Essential Role of Organizational Law' (2000) 110 (3) Yale Law Journal 387.

the creditors of its members and vice versa. This allows for efficient contracting but does not explain why the company is liable outside of contract law. There was a time when companies were not liable in either tort or crime.[94] If companies were just fictions or aggregates of their participants neither liability would be necessary. It would be sufficient to attach liability on the individual participants. Companies are, however, now liable both in tort and crime. Moreover, the modern approach of attributing criminal responsibility through a failure to prevent model demonstrates that the law accepts that corporations can act autonomously through their processes.[95]

The same applies to regulation. Professor Mariana Pargendler is right to observe that companies operate as nexi for regulation.[96] She does not explain, however, why we impose regulatory responsibility on companies to begin with. She gives the example of Alice, a shareholder in Apple Inc and points out that separate legal personality means that Apple Inc is not affected by Alice's regulatory or criminal misconduct. This, however, does not explain why Apple Inc has its own regulatory responsibility. If the company was nothing more than an aggregation of the contributions of its participants why do we not target regulation at its individual contributors commensurate to their respective level of involvement? Arguably this is too difficult to do.

We have seen above that there is empirical evidence that organisations give rise to conduct that would not occur but for their influence on human behaviour. They are more than the sum of the contributions of their participants. Organisations are a source of social norms that can bring about harmful conduct that individuals would not engage in but for the organisational context. It is therefore important to hold them legally accountable. Separate legal personality helps with organisational accountability. In addition to providing organisations with the ability to increase in size and complexity separate legal personality provides an anchor to which the law can connect and impose regulation as well as liability in both tort and crime.

[94]Tort: In *Director of Public Prosecutions v Kent and Sussex Contractors Ltd* [1944] KB 146 at 157 Mr Justice Hallett observed that 'at one point the existence, and later the extent and conditions of … [a body corporate's] … liability in tort was a matter of doubt … and it required a long series of decisions to clear up the position'; *Stevens v Midland Counties Railway Company and Lander* (1854) 10 Exchequer Reports (Welsby, Hurlstone, and Gordon) 352 at 356; 156 ER 480 at 482 (Anderson B): *Poulton v The London and South Western Railway Company* (1866–67) LRQB 534. Crime: Companies were initially held to be incapable of satisfying the mens rea requirement (*R v Cory Bros* [1927] 1 KB 810). This changed from the 1940s onwards (Law Commission, *Criminal Liability in Regulatory Contexts* (Law Com No 195, 2010) para 5.16; see also RB Cooke, 'A Real Thing: *Salomon v Salomon*' in *Hamlyn Lectures, Turning Points of the Common Law* (Sweet & Maxwell 1997) 23).

[95]Micheler (n 56) 93–97.

[96]Mariana Pargendler, 'Veil Peeking: The Corporation as a Nexus for Regulation' (2021) 169 University of Pennsylvania Law Review 717; for an earlier articulation of the concept of veil peeking see S Ottolenghi, 'From Peeping Behind the Corporate Veil, to Ignoring It Completely' 53 (1990) MLR 338.

6.6. Summary

In this section it has been argued that the principle of separate legal personality can be justified by reference to the characteristics associated with organisations or firms. The history of the company, the modern formation and termination process and the rules governing tortious, criminal as well as regulatory corporate liability enable us to use real entity theory as an explanation for the modern version of the principle of separate legal personality. It is possible to argue that the company has evolved as a legal tool enabling organisations or firms to operate autonomously of their participants. We now need to turn to our next question. Does the availability of the corporate form for other than organisational purposes undermine the conclusions drawn in the current section?

7. Non-organisational uses of the corporate form

Professor Susan Watson is critical of real entity theory. She points out that a company is brought about by incorporation rather than by the Companies Act recognising an existing organisation as having legal personality.[97] She further comments that an incorporated company that does not trade nevertheless has separate legal personality.[98] In her view companies exist 'separately from human beings as a type of fund consisting of rights'.[99]

This article acknowledges that companies can and are frequently set up and used to do nothing more but hold an asset. They are also set up and operated, sometimes in large numbers, by formation agents without any intention to operate an organisation or a firm. The law applies to such companies in the same way as it applies to companies set up with a view to operating an organisation or a firm.

However, the purpose of holding an asset or a fund does not explain separate legal personality, which would not be necessary if the purpose of the company was simply to hold an asset or a fund separately from human beings. Trust law already provides a mechanism to separate an asset or a fund from individual human beings. A trust is set up and operates without registration. Company law creates something that is designed to do more than hold an asset or a fund. The company has an outward facing independent legal existence and is outwardly accountable in tort, crime and as a subject of regulation.

The company, irrespective of what its purpose is, is further organised by law through the Companies Act and its constitution. This is true even for a one person company such as in *Lee v Lee Air Farming*.[100] It had a shareholder,

[97]Susan Mary Watson, 'The Corporate Legal Person' [2019] Journal of Corporate Law Studies 137 (162).
[98]ibid.
[99]Ibid.
[100][1961] AC 12 (PC).

a director and an employee. These roles were occupied by the same person but that did not undermine their respective independent legal significance. The Companies Act 2006, moreover, provides special organisational procedures for a situation where the sole member of a company is also one of its directors and enters into a contract with the company.[101]

The fact that the corporate form is available not just for organisational but for all lawful purposes (CA 2006, s 7(2)) does not undermine the insight that the corporate form can be explained by reference to the paradigmatic case of a company running an organisation or firm. It is logically possible to accept that a legal tool has evolved for a primary object, which explains its specifications, while nevertheless being put to other uses.

In everyday life, too, an object can be designed for a primary use case while serving other applications that do not explain its features. A mundane example of this would be a chair, whose proportions and dimensions reflect some standardised measurements of the human body in a sitting position. Chairs are nevertheless used for a range of purposes, none of which explain its properties. They store clothes in bedrooms (to be worn again or to be cleaned). People use chairs to store books and papers, more or less temporarily. Chairs serve as substitutes for ladders. For all these use cases chairs are helpful, but the properties of a chair cannot be explained by these purposes. If we were to design something for these additional use cases the object would look very different. Old-fashioned mute servants are better for the temporary storage of clothes in a bedroom. Shelves and filing cabinets are more suitable for storing books and papers. Ladders are optimised for the reaching of higher levels.

There are furthermore good policy reasons to design the corporate form with autonomous organisational action in mind while at the same time making it available for all legal purposes.

Limiting the availability of the corporate form to the purpose of running an organisation or a firm would not necessarily prevent abuses. Before the Companies Act 1844, the corporate form was only available ad hoc for individual projects through either a Royal Charter or a Private Act of Parliament. The authority approving incorporation on an ad hoc basis could ensure that the corporate form was available only for projects that were, in their policy judgement, suitable for the corporate form. We should note that this selective availability of the corporate form did not eliminate fraud. The South Sea Bubble happened while the ad hoc concession system was still in place.

Moreover, no harm is done by companies being set up to remain dormant or for the purpose of doing nothing but holding an asset. Concealment and evasion adequately address abuses in this context while leaving the companies separate legal personality in tact. It can also be beneficial to allow a

[101]CA 2006, s 231.

single individual to set up and control a company with a view to operating a micro-business. Questions have been raised about whether limited liability should be available to small businesses.[102] There are, nevertheless, good policy reasons to make the corporate form available for micro businesses. They can operate to support organisations, acting as their incubators and allowing a micro enterprise to grow into a larger business. The law, moreover, has adopted statutory means to identify and rectify abuses of the corporate form. These will be examined in the next section.

8. Abuses of the corporate form

8.1. Introduction

The robust availability of the corporate form has attracted substantial academic criticism. Kahn-Freund famously observed in the 1940s that the decision in *Salomon v Salomon* was 'calamitous'.[103] Professor Alan Dignam and Professor Peter Oh comment that the *Salomon* principle has always attracted controversy because of 'its potential to cause injustice by favouring shareholders over creditors, even involuntary creditors such as tort victims'.[104] On the critical side, scholars have instead tackled the dysfunctional academic and judicial analysis within this area, and urged root and branch reform in the interests of justice and fairness.[105] The editors of Gower's most recent edition also stress that *Salomon* has continued to be controversial and that the heated politics of the issue persist.[106]

We have seen in section 3 that the concealment as well as the evasion principle established in *Prest* accept the principle of separate legal personality but nevertheless address abuses of the corporate form. It will be shown in this section that since Kahn-Freund's assessment, the law has developed a number of further tools addressing abuses of the corporate form. On balance these have begun to create an adequate safety net for those affected by such abuses.

8.2. Illicit corporate controllers

In this subsection we will argue that the rules on fraudulent and wrongful trading, directors' disqualification, and phoenix companies appropriately

[102]Davies, Worthington and Hare (n 50) [7-005].
[103]Otto Kahn-Freund, 'Some Reflections on Company Law Reform' (1944) 7 MLR 54, 54.
[104]Dignam and Oh (n 2) 16 (17).
[105]ibid 17.
[106]Davies, Worthington and Hare (n 50) 7-004 (controversial), 7-007 (heated politics); see also Marc Moore, 'A Temple Built on Faulty Foundations: Piercing the Corporate Veil and the Legacy of *Salomon v Salomon*' [2006] JBL 180.

address situations where one or more individuals deploy companies for illicit goals without regard to the company's creditors.

The rules on fraudulent and wrongful trading impose personal liability on corporate controllers, directors and shadow directors, who either act fraudulently (IA 1986, s 213) or who continue to trade beyond the point at which they ought to have concluded that the company is not going to avoid insolvent liquidation (IA 1986, s 214).

Fraudulent trading occurs, for example, when a director obtains or helps to obtain credit or further credit when he or she knew that there was no good reason for thinking that funds would become available to pay the debt when it became due shortly thereafter.[107] In addition to the liability arising under IA 1986, s 213, any person who knowingly is a party to carrying on a business with the intent to defraud creditors commits a criminal offence under CA 2006, s 458.[108]

The wrongful trading rules introduce personal liability for controllers, unless they can show that they have taken every step beyond the point where they ought to have concluded that the company was not going to avoid insolvent liquidation with a view to minimising the potential loss for creditors.[109] Examples of wrongful trading include a situation where a director continues with a project guided by 'willfully blind optimism' holding an objectively unfounded view that 'something might turn up'.[110]

The fraudulent and wrongful trading rules are supported by the Company Directors Disqualification Act 1986, which enables the Secretary of State to apply for the disqualification of individuals, whose conduct has shown that they are unfit to be concerned in the management of a company. Examples of unfitness include the failure keep proper accounting records, and the failure to pay PAYE and crown debts.[111] Since 2015 it has been possible for compensation orders to be made in disqualification proceedings.[112]

Personal liability is also imposed on directors and shadow directors of companies which have gone into insolvent liquidation if they become involved with the management of a company with the same or a similar name within five years from the beginning of the liquidation of the insolvent company.[113] This is designed to address the problem of phoenix companies, where the same individuals set up

[107] *R v Grantham (Paul Reginald)* [1984] QB 675.
[108] *R v Hollier (Jayson Wayne)* [2013] EWCA Crim 2041.
[109] IA 1986, s 214 (3); *Grant v Ralls* [2016] EWHC 243 (Ch) [2016] Bus. L.R. 555; Harry Rajak, 'The Complex Story of Wrongful Trading' [2017] Company Law Newsletter 392.
[110] *Roberts v Frohlich* [2011] EWHC 257 (Ch) [2011] 2 BCLC 625; see also *Re Produce Marketing Consortium (No 2)* [1989] BCLC 520 (Ch).
[111] *In Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch 164.
[112] Company Directors Disqualification Act 1986, s 15; *Re Noble Vintners* [2019] EWHC 2806 (Ch) [2020] BCC198.
[113] IA 1986, s 215 and 216.

one failing company after the next, continuing the same apparently unviable business. This addresses a form of abuse of separate legal personality without undermining the independent existence of the company concerned.

The combination of the fraudulent and wrongful trading rules with the directors' disqualification regime and the rules on phoenix companies constitutes a targeted mechanism addressing abuses of the corporate form. We no longer need an independent company law doctrine justifying 'corporate disregard' to hold illicit controllers accountable. The modern law accepts that businesses sometimes fail. Separate legal personality together with limited liability means that creditors have to accept this ordinary business risk. The risk to creditors is, however, increases in the vicinity of insolvency. At this point the corporate form is abused by a controller causing the company to take on debt that they either knew or should have known was not going to be repaid. At this point limited liability is no longer available to them, and the courts can order directors and shadow directors to make contributions that they think fit. Separate legal personality, however, continues to exist until the company is struck off the register.

8.3. Corporate groups

Corporate groups are an example where the corporate form is sometimes said to be abused.[114] They were made possible not only by the corporate form, but more specifically by the law permitting companies to act as shareholders and as directors of other companies. There was a time when holding shares in other companies was considered to be ultra vires, but the law changed in the nineteenth century.[115] Corporate directors are currently permitted, but only if the company also has another director who is a natural person.[116]

From the perspective of real entity theory, we can observe that there are organisational reasons explaining the use of a corporate group structure. Incorporating sub-units of a group independently makes it possible for these to be run in relative autonomy from other sub-units. Groups also sometimes emerge through acquisitions of pre-existing companies, where each of these now sub-units has a distinct history that continues to shape its business and thus justifies its operation as a separate legal entity. The separate legal personality of sub-units facilitates a management structure where a parent company is responsible for strategy and for overseeing the performance of the respective subunits.[117] With separate legal personality subunits are also

[114]See recently Jonathan Hardman, 'Fixing the Misalignment of the Concession of Corporate Legal Personality' (2023) 43 Legal Studies 443.
[115]Christian A Witting, *Liability of Corporate Groups and Networks* (CUP 2018) 65–66.
[116]CA 2006, s 155; The Government has proposed further restrictions on corporate directorships <www.gov.uk/government/publications/economic-crime-and-corporate-transparency-bill-2022-factsheets/fact-sheet-identity-verification-and-authorised-corporate-service-providers>.
[117]Christian A Witting, *Liability of Corporate Groups and Networks* (CUP 2018) 37.

better able to source independent debt and equity finance.[118] In an international context separate legal personality facilitates compliance with the different regulatory regimes operating in different countries.[119]

There is nevertheless a dark side to group structures, for they can result in vulnerable individuals being exposed to risks emanating from large international businesses without adequate individual redress.[120] It will be argued in this subsection, that the law has developed a range of tools addressing corporate abuse through group structures and that on balance further intervention should be carried out in the specific context rather than through a general rule of corporate 'disregard'.

The courts have most recently started to use tort law to construct liability of parent companies, who involve themselves operationally in the management of the subsidiary's business. In these instances, the parent company is characterised as a tortfeasor in its own right.[121] This is a relatively new development, which, for the time being, concerns questions of jurisdiction rather than substantive tort law. It is nevertheless a noteworthy attempt to undermine the ability of corporate groups to impose risk on vulnerable individuals.

The legislature has added further tools.[122] Company Law textbooks sometimes refer to *Daimler v Continental Tyre* to point out that an English incorporated company can be characterised as an enemy company under the Trading with the Enemy Act 1939.[123] Legislation has moved on since that Act. Modern sanctions regimes address corporate group structures in a more targeted and deliberate manner. The most recent sanctions against Russia, for example, apply to companies which are owned and controlled directly or indirectly by a sanctioned individual. Control is defined as the holding (directly or indirectly) of more than 50% of the shares or the voting rights or as holding the right to (directly or indirectly) appoint or remove the majority of the directors.[124] This approach is superior to the approach available through a doctrine of corporate 'disregard' residing within company law. It better addresses the circumstances associated with a particular conflict and its supporting political regimes.

[118]ibid 47–48.
[119]Thom Wetzler, 'In Two Minds: The Governance of Ring-Fenced Banks' [2019] Journal of Corporate Law Studies 197.
[120]Davies, Worthington and Hare (n 50) (11th edn, Sweet & Maxwell 2021) 7-005; Hardman (n 114) 454–56.
[121]The most recent case is *Okpabi v Royal Dutch Shell* [2021] UKSC 3 [2021] WLR 1294.
[122]For a recent contribution discussing further legislation in this context see Mariana Pargendler, 'The Fallacy of Complete Corporate Separateness'(2024) 14 Harvard Business Law Review Online 1, at 11–13.
[123]Worthington and Agnew (n 4) 58–60.
[124]Russia (Sanctions) (EU Exit) Regulations 2019/855, reg 7; further guidance is contained in OFSI's General Guidance on UK Financial Sanctions (August 2022) <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1169348/Financial_Sanctions_General_Guidance.pdf> 17.

There are further statutory provisions protecting the public purse from situations where underfunded companies fail to pay national insurance and tax contributions. The Social Security Administration Act 1992 imposes personal liability on the officers of a company whose fraud or neglect is responsible for the company's failure to pay national insurance contributions.[125] Under the Finance Act 2009, senior accounting officers, who need to be appointed by certain large companies, are responsible for a fine if they do not ensure that the company establishes and maintains appropriate tax accounting arrangements.[126]

Pension, consumer and competition laws also now contain provisions that have adapted to the fact that group structures have become prolific and can negatively affect interests that deserve protection. Workplace pensions are, for example, protected in the insolvency of a corporate group. The Pension Act 2004 enables the Pension Regulator to require other companies within a group to provide reasonable financial support for an under-funded or insufficiently resourced occupational pension scheme managed by a service company within the group.[127] More generally, the UK Government has recently said that it will adopt the UNCITRAL Model Law on Enterprise Group Insolvency.[128] Product liability rules protect consumers by imposing liability on importers and producers irrespective of whether the injured person has a contractual relationship with them.[129] In the area of consumer law, the Court of Appeal has held that a non-trading holding company could be a trader for the purposes of the Unfair Trading Regulations 2008.[130] Competition law uses the concept of an 'undertaking', which is 'any entity engaged in economic activity, regardless of its legal status' and which includes 'an economic unit which may consist of more than one legal or natural person, such as a group of companies'.[131]

Modern legislation further uses a failure to prevent model to allocate responsibility for conduct that is associated with corporate groups as well as alongside supply chains. This technique acknowledges the legal

[125]Social Security Administration Act 1992 (1992 c 5), s 121C; *O'Rorke v Revenue and Customs Commissioners* [2013] UKUT 499 (TCC), [2013] BTC 2096.
[126]Finance Act 2009 (2009 c 10), Sch 46 para [1] and [4].
[127]*Re Nortel GmbH (in administration) and other companies; Re Lehman Brothers International (Europe) (in administration) and other companies (Nos 1 and 2)* [2013] UKSC 52, [2013] 2 BCLC 135; see also *Granada UK v The Pension Regulator* [2019] EWCA Civ 1032, [2020] ICR 747.
[128]<www.gov.uk/government/consultations/implementation-of-two-uncitral-model-laws-on-insolvency/outcome/implementation-of-two-uncitral-model-laws-on-insolvency-summary-of-consultation-responses-and-government-response>; for a critical analysis of the Model Law see Irit Mevorach, 'Is the Future Bright for Enterprise Groups in Insolvency? – Analysis of UNCITRAL's New Recommendations on the Domestic Aspects' in Paul Omar (ed), *International Insolvency Law: Reforms and Challenges* (Routledge 2013).
[129]Consumer Protection Act 1987 (1987 c 43) Part 1, which imposes a strict liability regime. The Act operates alongside the law of negligence (*Donoghue v Stevenson* [1932] AC 562).
[130]*R v Scottish and Southern Energy Plc* [2012] EWCA Crim 539, [2012] CTLC 1.
[131]*Toshiba Carrier UK Ltd v KME Yorkshire Ltd* [2012] EWCA Civ 1190 at [38].

boundaries of separate legal personality while imposing obligations on companies to prevent wrong-doing by anyone acting for their benefit. Control needs to be exercised over subsidiaries but also suppliers or agents. In the UK, the Bribery Act 2010 imposes criminal liability for the failure to prevent the payment of bribes by another person irrespective of whether the other person is a subsidiary, agent or supplier.[132] The most recent relevant addition to the statute book is the criminal offence of failure to prevent fraud.[133]

In the EU the Corporate Sustainability Due Diligence Directive will create a regime that requires certain companies to take on responsibility for human rights abuses and environmental harm in their global supply chains. The Directive will also affect UK companies which operate in the supply chains of those companies to which the Directive is going to apply.[134]

Addressing the problems associated with corporate groups is currently done through specific legislation addressing particular contexts. There is wisdom in this. The interests protected by the different areas are diverse and the respective legal rules follow their own structure and logic. It is better to regulate groups in a way that is embedded in the respective specific legislation. This is not to say that the law has reached a state where we can conclude that all or even most problems associated with groups are solved.[135] From the perspective of academic scholarship, it does mean, however, that we should not attempt to chase an elusive principle of corporate 'disregard' but rather look beyond company law to assess whether corporate groups and the problems associated with them have been adequately addressed.

9. Summary

It has been argued in this article that the courts have recently rejected the existence of a principle of corporate 'disregard'. This happened after several decades of case law and academic scholarship attempting to pin down a company law doctrine justifying the 'disregard' of the company's separate legal personality. *Prest v Petrodel* recharacterised the doctrine into instances of 'concealment', where rules outside of company law operate to remove smoke screens and judges are taking decisions on the true facts, and 'evasion', where a company is used to avoid an existing obligation. *Hurstwood v Rossendale* and *Gramsci Shipping v Recoletos* have since cast doubt on whether the evasion principle will have traction. Neither principle, however, involves the 'disregard' of the company's separate legal personality.

[132]Bribery Act 2010, s 7(2).
[133]Economic Crime and Corporate Transparency Act 2023 (c 56) s 199.
[134]The current draft text of the Corporate Sustainability Due Diligence Directive includes the amendments adopted by the European Parliament on 15 March 2024 <https://data.consilium.europa.eu/doc/document/ST-6145-2024-INIT/en/pdf>.
[135]Hardman (n 114) 454–56.

The article argues that the difficulties the courts and academic scholarship have experienced in fully appreciating the implications of separate legal personality can be explained by roots of UK company law in English partnership law. The current dominant academic model, the nexus of contracts approach, conceptualises the company as a fictional nexus for the aggregation of contributions by its participants and may have contributed.

The article proposes a modern version of real entity theory that explains companies not in anthropomorphic terms but as vessels for organisations to act autonomously. This model relies on theoretical and empirical scholarship from the wider social sciences that demonstrates that organisations are real in their consequences. The robust principle of separate legal personality condones, supports, and protects the ability of organisations to act autonomously. Real entity theory supplies a theoretical as well as empirical justification for a robust principle of separate legal personality by the courts.

The article acknowledges that companies can be used for non-organisational purposes. This does, however, not undermine the observation that they have evolved for the paradigmatic purpose of enabling an organisation to better act autonomously. It is logically possible for a legal tool to evolve to display features that suit a core purpose while being available more generally.

The article concludes that, since Otto Kahn-Freund famously characterised the decision in *Salomon v Salomon* as 'calamitous', a substantial amount of case law as well as legislation has emerged that largely addresses abuses of the corporate form. We do not need a principle justifying the 'disregard' of the separate legal personality of the company.

Disclosure statement

No potential conflict of interest was reported by the author(s).

ORCID

Eva Micheler http://orcid.org/0000-0002-7922-2436

Notes on contributor

Eva Micheler is a professor at the LSE Law School and a co-investigator at the LSE Systemic Risk Centre. She writes on corporate law and on the law of securities and digital assets. Her most recent book is entitled 'Company Law – A Real Entity Theory'.