

Piercing the Veil of Business Incorporation: An Overview of what Warrants It

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Abstract

From the age long decision of House of Lords in the case in *Salomon v. Salomon & Co Ltd* (1897) AC 22 (HL), it became established that a corporation is a different entity from the owners, shareholders or directors. A corporation has a life of its own and characteristics of perpetual succession in the event of the death or retirements of the owners or the directors that were appointed through the memorandum and articles of association. Upon the incorporation of a company, it acquires capacity of artificial person as such it can own property, become a party to a contract, act in a tortuous manner and become tortuously liable, commit a crime, can sue and be sued, has a nationality and therefore becomes domicile in nature and even has rights that could be attributed to a natural person though artificial in character. A company acquires the characteristics of a distinct legal person upon incorporation. If the company commits a civil or corporate crime such a company could be sued in its corporate name, if a judgment is obtained against such a corporation, it is only natural that the company complies with the decision of the court but where it fails, the veil covering the incorporation will be lifted to see those natural persons being the company and probably compel them to comply with the judgment of the court or be made to face the direct penalty of the law through committal to prison. A corporate veil could be lifted whenever the court wants to find out who is behind the fraudulent and improper conduct of a company. Apart from the forgoing, this article intends to examine in detailed manner the legal concept of piecing or lifting the veil of incorporation and what warrants it.

Keywords: Corporation, Veil of Incorporation, Lifting the Veil, Separate Legal Personality

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1. Introduction

The introductory aspect of this article will deal with the definitions of some terms to acquaint the readers with the meaning of these terms and clarify some conceptual issues on the subject under consideration.

These words include: Corporation, Separate Legal Personality, Veil of Incorporation, Lifting the Veil and thereafter the work will examine the theories of incorporation before delving into the substance of this article which is the legal reasons for piercing the veil of incorporation of a business.

(i). Corporation

The word corporation is derived from the Latin word *corpus* meaning body or person.¹ The Romans identified a collection of persons considered as a 'corpus' or body out of which the English word for corporations was developed.³ A business corporation is a for-profit firm that is incorporated or registered under the corporate or company law of a state. According to Black's Law Dictionary, a corporation is an entity having authority under law to act as a single person distinct from the shareholders who own it and having rights to issue stock and exist independently, a group of succession of persons established in accordance with legal rules into a legal or juristic person that has legal personality distinct from the natural persons who make it up, exist independently apart from them, and has the legal powers that its constitution gives it.⁴

A corporation is an artificial person or legal entity created by or under the authority of the laws of a state or nation, composed, in some rare instances, of a single person and his successors, being the incumbents of a particular office, but ordinarily consisting of an association of numerous individuals, who subsist as a body politic under a special denomination, which is regarded in law as having a personality

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³ P.W. Duff, *Personality in Roman Private Law*, Oxford University press, London, 1971, p. 26. See also Endalew, Lijalem Enyew, "The Doctrine of Piercing the Corporate Veil: Its Legal Significance and Practical Application in Ethiopia" A Thesis Submitted in Partial Fulfillment for the Requirement of Master's Degree in Business Law (L.L.M) to Addis Ababa University School of Graduate Studies School of Law, 2011, p.13. Available online at <http://chilot.files.wordpress.com/2013/05/the-doctrine-of-piercing-the-corporate-veil.pdf>, accessed 10 April, 2014. See R.C. Clark, *Corporate Law* (Aspen 1986) 2; H Hansmann et al, *Anatomy of Corporate Law* (2004) ch 1.

⁴B.A Garner, (ed), *Black's Law Dictionary*, 7th edn, St Paul, MINN, West Group Publishing, 2000, p.276.

and existence distinct from that of its several members, and which is, by/the same authority, vested with the capacity of continuous succession, irrespective of changes in its membership, either in perpetuity or for a limited term of years, and of acting as a unit or single individual in matters relating to the common purpose of the association, within the scope of the powers and authorities conferred upon such bodies by law.⁵

Another definition of a corporation, given by the American Supreme Court Justice John

Marshall, in the case *Trustees Dartmouth College v. Woodward* states that a corporation is " an artificial being, invisible, in tangible, and existing only in contemplation of law."⁶

A corporation could be described as a franchise possessed by one or more individuals, who subsist as a body politic, under a special denomination, and are vested by the policy of the law with the capacity of perpetual succession, and of acting in several respects; however numerous the association may be, as a single individual. An artificial person or being, endowed by law with the capacity of perpetual succession; consisting either of a single individual, (termed a "corporation sole,") or of a collection of several Individuals, (which is termed a "corporation aggregate.")⁷

A corporation is an intellectual body, created by law, composed of individuals united under a common name, the members of which succeed each other, so that the body continues always the same, notwithstanding the change of the Individuals who compose it, and which, for certain purposes, is considered a natural person.⁸

⁵Henry Campbell Black, *A Law Dictionary*, 2nd St. Paul, Minn. West Publishing Co. 1910, p.273. See Case of *Sutton's Hospital*, 10 Coke, 32; *Dartmouth College v. Woodward*, 4 Wheat. 518, 636, 657, 4 L. Ed. 629; *U. S. v. Trinidad Coal Co.*, 137 U. S. 160, 11 Sup. Ct. 57, 34 L. Ed. 640; *Andrews Bros. Co. v. Youngstown Coke Co.*, 86 Fed. 585, 30 C. C. A. 293; *Porter v. Railroad Co.*, 76 111. 573; *State v. Payne*, 129 Mo. 468, 31 S. W. 797, 33 L. R. A. 576; *Farmers' L. & T. Co. v. New York*, 7 Hill N. Y.) 283; *State v. Turley*, 142 Mo. 403, 44 S. W. 267; *Barber v. International Co.*, 73 Conn. 587, 48 Atl. 758; *Sovereign Camp v. Fraley*, 94 Tex. 200, 59 S. W. 905, 51 L. R. A. 898; *Sellers v. Greer*, 172 111. 549, 50 N. E. 246, 40 L. R. A. 589; *Old Colony, etc., Co. v. Parker, etc., Co.*, 183 Mass. 557, 67 N. E. 870; *Warner v. Beers*, 23 Wend. (N. Y.) 103, 129, 142.

⁶Blumberg Phillip I., 'The Corporate Personality in American Law: A Summary Review' , *The American Journal of Comparative Law*, Vol. 38, Supplement. U. S. Law in an Era of Democratization, American society of Comparative Law, USA, 1990, p.49.

⁷3 Steph. Comm. 166; 1 Bl. Comm. 467, 469.

⁸Civil Code La. Art. 427.

(ii). Separate Legal Entity

One of the characteristic features of a corporation is the fact that it is a separate entity from the owners under the law. A registered company's legal rights and obligations are wholly separate from its owners', own entitlements and duties.

Property acquired by the company belongs to it and not to its members.⁹ This principle was endorsed emphatically in the case of *Salomon v. Salomon & Co. Ltd.*¹⁰ one of the consequences of forming and incorporating a registered limited liability company is that the members create a body which is recognized as having an independent legal personality. A registered Limited Liability Company, whether created under English law is recognized as a person, with capacity to act as such, although of course not necessarily in the same way that a natural person can act. Moreover, the company's personality is distinct from that of each and all of its members, albeit there may be similarities.¹¹

The mere fact that by incorporation of their business, persons obtain some legal privilege that would be beyond their reach without such incorporation, or they avoid some statutory obligation that otherwise would fall on them, is not in itself reason for rendering aside the wall of incorporation.

(iii) Veil of Incorporation

Veil of incorporation or corporate veil is the legal assumption that the acts of a corporation are not the actions of its shareholders, directors and managers, so that they are exempt from liability for the corporation's actions.¹²

(iv) Lifting or Piercing the Corporate Veil

This phrase is defined as the judicial act of imposing personal liability on otherwise immune corporate officers, directors and shareholders from the corporation's wrongful acts.¹³ This act amounts to disregarding the corporate entity.

2. Theories of Piercing the Veil of Incorporation

⁹ M. Forde, *Company Law*, 3rd edn, Dublin: Round Hall Sweet & Maxwell, 1999, p.65.

¹⁰ (1897) A.C. 22

¹¹ Francis Rose, "Nutshells: Company Law", 6th edn, London: Sweet & Maxwell, 2004, p.35.

¹² B.A Garner, (ed), *supra* note 2.

¹³ *Ibid*, p. 936

The concept of corporate personality endows the incorporated company with a distinct legal personality. However, there are circumstances in which the court will disregard and has often disregarded the company's personality.

In the American tradition, it is referred to as lifting the veil of incorporation or the disregard by the courts of the company's corporate personal or separate existence from its shareholders. In cases where the veil is lifted, the law either goes behind the corporate personality to the individual members or ignores the separate personality of each company in favour of the economic entity constituted by a group of associated companies.¹⁴

There are three principal theories that underlie the legal act of piecing the veil of incorporation and they include: (a). Single economic theory or alter ego theory, (b). the justice theory, and (c). the Façade theory. These theories have been exhaustively examined in the case of *Adams v. Cape Industries Plc*,¹⁵ described as a leading authority on this area of company law.¹⁶

(a). Single Economic Theory or the Alter Ego Theory: This theory proposed that a court can treat a group of companies as a single entity in law because they are/it is a single economic entity is false. The apparent acceptance of the single economic theory by Lord Denning in *DHN Food Distributors Ltd v. London Borough of Tower Hamlets*,¹⁷ can no longer be regarded as good law.

The correctness of the reasoning in the case has been doubted by the House of Lords in *Woolfson v. Strathclyde Regional Council*,¹⁸ in which referencing the DHN decision, Lord Keith of Kinkel said: "I have some doubt whether in this respect the Court of Appeal properly applied in principle that it is appropriate to pierce the corporate veil only where special circumstances exist indicating that it is a mere façade concealing the true facts" DHN involved compensation under the land compensation Act 1961 of United Kingdom. In this case, a group of companies was treated as one single economic unit.

¹⁴ C.S Ola, *Company Law in a Nutshell*, Ibadan: University Press Plc. 2001, p.12.

¹⁵(1990) 1 Ch. 433.

¹⁶Susan McLaughlin, "Unlocking Company Law" 1st edn, London: Hodder Education, 2009, p.89

¹⁷ (1976) 1 WLR 852, (C.A)

¹⁸(1978) SC 90 (HL)

DHN was a parent company which runs a cash and carry grocery business from a warehouse owned by one of its wholly owned subsidiaries called Bronze Investment Limited. Another subsidiary owned the vehicles. The directors were the same in each of the three companies. Tower Hamlets served s compulsory purchase order on the warehouse which they wished to demolish so that the site could be used to build houses on it.

Compensation was available under statute but for the value of the land and for disturbances of the Tower Business Tower Hamlets was prepared to pay bronze investments £360,000 for the land but refused to pay anything for disturbance of business Tower Hamlets argued that Bronze Investments merely owned the land and had no business to disturb, DHN argued that the corporate veil should be lifted and the three companies treated as one, allowing DHN to claim the compensation. The veil was lifted so that DHN and the two subsidiaries were treated as one economic entity, allowing DHN to claim the compensation¹⁹.

The “alter ego” theory also called “another self” theory permits a court to impose liability upon an individual shareholder, officer, director, or affiliate for the acts of a corporation. This theory may also be used to impose liability upon a parent corporation for the acts of a subsidiary corporation when the subsidiary is “organized or operated as a mere tool or business conduit.”²⁰ A court will look at many factors to determine whether an alter ego relationship exists. When dealing with an individual and a corporation, the court will look at the total dealings of the corporation and the individual, including evidence of the degree to which corporate and individual property have been kept separate; the amount of financial interest, ownership, and control the individual has maintained over the corporation; whether the corporation has been used for personal purposes.

In these cases the court will disregard their separate personality and consider them as a single entity working in different form or shape.²¹

¹⁹ Chris Shepherd, *Company Law*, 2nd London: Old Bailey Press, 2002, p.6.

²⁰ Endalew Lijalem, *supra* note 1 at pp.45-46.

²¹*Ibid.*, *Law in Texas Regarding Piercing the Corporate Veil*, pp.1-5, available online at <http://taxlaw.sprouselaw.com/Texas%20Law%20on%20Piercing%20Corporate%20Veil.pdf>, accessed 10 April, 2014. See also the Texas Business Corporation Act (or Sections 21.223, 21. 224, and 21.225 of the Texas Business Organizations Code, where that Code is applicable) (“Article 2.21”).

A “single economic” theory of piercing the corporate veil is another interconnected theory to the theory of “alter ego” which is used to impose liability when businesses integrate their resources. In order to take advantage of the corporate form of limited liability, parties will often incorporate several different business concerns under the belief that each incorporated entity will protect them from any and all personal liability of each business concern.

Courts, however, apply the single business economic theory to pierce the corporate veil in situations where two or more corporations are not operated as wholly separate entities, but instead combine their resources to achieve a common business purpose.²² When courts find that a single business enterprise exists, they will hold each corporation liable for the obligations of the other relating to the common business purpose to avoid an “inequitable outcome.” The courts used a “single economic” theory to pierce the corporate veil in order to reach the assets of a subsidiary’s parent corporation or to reach the assets of any other entity involved in the single business enterprise. Courts have listed several factors that are to be considered when determining whether a single business enterprise exists. These factors, though not cumulative, include having common employees; common shareholders; common officers; centralized accounting; payment of wages by one corporation to another corporation’s employees; services rendered by the employees of one corporation on behalf of another corporation; unclear allocations of profits and losses between corporations; undocumented transfers of funds between corporations etc.²³ Both the “alter ego” and “single economic” theories are inter-related as the purpose and effect of the two theories is identical: to allow a plaintiff to recover from another party when a corporation does not have adequate assets.

(b). Façade Theory: This theory stated that if a company is a “mere façade concealing the true facts”, the corporate veil will be pierced.

The authority for this proposition is the House of Lords decision in *Woolfsan v. Strathclyde Regional Council*,²⁴ though Lord Kinkel cited no authority for this proposition and gave no indication of the meaning of “façade”.

²² Ibid., p.46.

²³ Ibid, pp.6-8.

²⁴ Ibid.

Ten years later, L.J Slade commented on the authorities on “Façade” in the court of Appeal in *Adams v. Cape Industries Plc*,²⁵ “from the authorities cited to us we are left with rather sparse guidance as to the principle which should guide the court in determining whether or not the arrangements of a corporate group involved a façade within the meaning of that word as used by the House of Lords in *Woolfson*”.

For further illustration of this theory, in cases in which the courts have treated the company and the shareholders as one, the terms used to describe the company, apart from ‘façade’, are ‘device’, ‘stratagem’, ‘mask’, ‘cloak’ and ‘sham’, all of which were used in *Gilford Motors Company Ltd v. Horne*²⁶. Finally where a company is formed with the intention of using it to avoid an existing legal liability, the court will pierce the veil based on a finding of sham.²⁷ Again the consequences of finding that the acts or documents are a sham was illustrated by the words of LJ Lindley in *Yorkshire Railway Wagen Co. v. Maclure*,²⁸ speaking in the context of a transaction entered into by a company, he state that “if it were a mere cloak or screen for another transaction one could see through it. If a company is a sham, it is ignored, and this act of ignoring it is a piercing of the corporate veil.

The courts have seen fit to pierce the corporate veil when a company is used by a defendant as a means of evading his obligations. For example: In *Gilford Motor Co Ltd v. Horne*,²⁹ a company through which Mr Horne conducted business which, if he had conducted it himself, would have been a breach of restrictive covenants which he had entered into with the plaintiff company of which he was the former managing director was held to be “a device, a stratagem”. In *Jones and ano v. Lipman and ano*³⁰, the defendant agreed to sell land to the plaintiff, then transferred it to a company, to defeat the plaintiff’s right to specific performance. The company was held to be “the creature of the first defendant, a mask to avoid recognition by the eye of equity.”³¹

In analysis, the case of *Adams & Others v Cape Industries plc* is probably the most important case establishing that the corporate veil should not be pierced just because a group of companies operated as a single economic entity.

²⁵(1990) 1 Ch. 543

²⁶ (1933) Ch, 935

²⁷Susan McLaughlin, *Supra* note 11.

²⁸ (1882) 21 Ch.D 309, 318.

²⁹ (1933) Ch 935

³⁰ (1962) 1 WLR 832

³¹ Katie Brown, “Piercing the Corporate Veil”, March 2011,p.2.available online at <http://www.applebyglobal.com/articles-2011/global-reference-guide-for-litigation-and-dispute-resolution---piercing-the-corporate-veil---by-katie-brown.pdf>, accessed 12 April, 2014.

Cape an English company headed a group which included many wholly owned subsidiaries. The arguments for piercing the corporate veil were split into three. First, the single economic unit argument, being that a group of companies should be treated as a single economic entity. Secondly the argument in *Woolfsan v Strathclyde Regional Council* which established that the veil can be lifted where special circumstances exist indicating that it is a mere façade concealing the true facts. Thirdly the agency argument.

On the first argument it was held that the mere fact that a parent and subsidiary are one entity for economic purposes should not mean they can be treated as one unit for legal purposes; each company in a group of companies is an independent entity. To lift the veil would require exceptional circumstances. On the second argument it was held that a company's separate personality should not be ignored simply because it is controlled by another person³². Cape Industries plc had made a legitimate use of the corporate form and this did not constitute a ground for piercing the corporate veil. The third argument also failed as it is difficult to establish an agency relationship unless there is express agreement.³³

(c). Justice Theory: Justice theory was developed under the premise that if justice requires it, a remedy should be available against the shareholder for a wrong done by the company. Presented in these general terms, the argument offends against the doctrine of legal certainty and may be rejected for this reason alone. There are, however, many situations when courts will look through a company and ignore its existence. The façade theory discussed earlier, provide example of this. Other example exist that do not fit together neatly into a theory. Rather than attempting to create a general theory for when courts will pierce the corporate veil... is to examine the purpose of the legal rule or principle in issue in each case.³⁴

It is sometimes said that the corporate veil can be pierced where "the interests of justice require" or where there has been impropriety.

³² Mayson, French & Ryan (2005).

³³ "Lifting the *veil* of incorporation - FISMA", www.fisma.org/_.../1314297012_coco-misc---lifting-the-veil-of-incorpo..., accessed 13 April, 2014

³⁴ Susan McLaughlin, *Supra* note 13 p.95.

An example is the Cayman case of *Bonotto and others v. Boccaletti and others*.³⁵ The defendant had transferred properties from his and his wife's name into the names of companies under his control, to make himself judgment proof. The Judge held "the cases... show that the court will use its powers to pierce the corporate veil if it is necessary to achieve justice irrespective of the legal efficacy of the corporate structure under consideration". The English Court of Appeal rejected arguments based on the "interests of justice" in *Adams v. Cape Industries and Ord v. Bellhaven Pubs Ltd*.³⁶

In *Trustor v. Smallbone*,³⁷ the Judge also doubted whether impropriety of itself constituted sufficient grounds for piercing the veil. It is therefore suggest that arguments based on vague notions of "the interests of justice" or impropriety should not succeed unless accompanied by evidence that the company in question is a sham or a façade. It would have been open to the Court in *Bonotto v. Boccaletti*³⁸ to conclude that the corporate veil should be pierced on that basis.³⁹

Of the three theories that could explain the concept of lifting the veil of incorporation, the single legal entity theory seems to have been rejected by the court. In *Adams v. Cape Industries Plc*,⁴⁰ the court rejected this theory in a case involving tort victims of a subsidiary company who had suffered physical injury, unlike others who have suffered purely economic loss. The court in this case denied the tort victims access to parent company funds to pay unpaid judgments obtained against subsidiary companies.⁴¹ Two theories exist for piercing the corporate veil: the "alter-ego" (other self) theory and the "instrumentality" theory. The alter-ego theory examines the indistinctive nature of the boundaries between the corporation and its shareholders. While, the instrumentality theory focuses on the use of a corporation by its owners in ways that benefit the owners rather than the corporation.⁴²

3. Circumstances under which the Veil of Incorporation is Lifted

³⁵ (2001) CILR 120

³⁶ (1998) BCC 607.

³⁷ (2001) 1 WLR 1177

³⁸ (2001) CILR 120

³⁹ *Ibid.* p.2.

⁴⁰(1990) 1 Ch. 433

⁴¹ *Ibid.*

⁴²Piercing The Corporate Veil, available online at <http://www.radford.edu/content/dam/colleges/cobe/SBDC/Documents/24piercethecorporateveil.pdf>, accessed 12 March, 2014.

Francis Rose have argued that though the decision in Salomon's case is still a good law, there is a large number of situations in which the veil of corporate personality may be said to be lifted so as to expose the identity of the company's members or officers. On one hand, it may be said that the number of exceptions has become so numerous that *Salomon case* has been reduced to a shadow. On the other hand, it is possible to find some consistency between those exceptions and Salomon case.⁴³ Though, these exceptions are found more in English law. The facts in the leading case of *Salomon v. Salomon*,⁴⁴ is that Salomon formed a company with 20,007 shares.

Each of the six members of his family held one share as his nominee, he held the rest. He sold his existing business to the company in return for the shares and debentures issued to him for (10,000.00 British Pounds) ten thousand pounds, thereby making him a secured creditor for that sum. The company quickly went into liquidation and its unsecured creditors, whose claims could not be met in full, tried to press their claims against Salomon himself on the basis that the company was his *alter ego*, or agent. Those claims failed. The requirements of the legislation for setting up the company had been complied with and it was immaterial that Salomon held all the shares beneficially. The company had been established as a separate entity and it was that, not Salomon, with which the creditors had contracted.

(i). Lifting the Veil of Incorporation under CAMA

If it appears to the Corporate Affairs Commission of Nigeria that there is a good reason to investigate the true ownership of a company in order to determine the true persons who are or have been interested in the success or failure of a company or who are able to control or materially influence the policy of the company it may appoint one or more competent inspectors for the purpose. In the same vein, it may investigate and determine the true ownership of any company securities such as shares or debentures under sections 325 to 328 of Companies and Allied Matters Act.⁴⁵

The importance of this provision is quite obvious. In the past and even at present, persons of dubious intent often foreigners, operated under the guise of corporate personality as they perpetuate various economic crimes.

⁴³ Francis Rose, *supra* note 9, p.38.

⁴⁴ (1897) AC 22 (HL).

⁴⁵ Deji Sasegbon (ed), *Nigerian Companies and Allied Matters Law and Practice*, 1st edn, Vol. 1. Ikorodu: DSc Publication, 1991, pp.18-19. See Companies and Allied Matters Act, Cap C20, LFN 2004

The foreigners used Nigerians as front in running the economy of the nation aground. The devise was used to beat expatriate quota, to circumvent government regulations on expatriate participation in various sectors of the economy and of the ownership of certain enterprises. They run all types enterprise without regards to the enterprise provisions of the Nigerian Enterprise Promotion Act.⁴⁶ They did all these shady transactions under the mark of corporate personality using Nigerian subscribers and Directors. By virtue of these provisions, the commission may now lift the veil or mask of ownership in order to uncover the true actors behind the scene of the economic crime.⁴⁷

According to Gower, it has always been recognized that the legislature can forge a sledgehammer capable of cracking open the corporate shell⁴⁸ and even without the aid of the legislative sledgehammer, the courts have sometimes be prepared to have a crack.⁴⁹ In such cases, the law goes behind the corporate personality of the individual members or ignores the separate personality of each company in favour of the economic entity constituted by a group of associated companies.⁵⁰ In *NBCI v. Integrated Gas Nigeria Ltd*,⁵¹ it was held that: A company must be accorded the status of a separate personality from the biological persons that do run it. The consequences of recognizing the separate personality of a company is to draw a veil of incorporation over it and one is generally not entitled to go behind or lift the veil. However, there are many situations, in law, where consequences attach to the acts, motives or opinions of persons working for and inside the "separate personality", the company. Though circumstances in which a court may pierce the veil of incorporation may differ for example in *Public Finance Securities Ltd v. Jafia*,⁵² the court of Appeal clearly demonstrated some of the instances where the veil of incorporation will be lifted when it held as follows: The court can lift the veil. It can pull down the mask. The courts will lift the veil of incorporation to find out who was behind the fraudulent and improper conduct of the company.

⁴⁶ Now reenacted as Nigerian Investments. and Promotion Council Act Cap. N117 LFN 2004, ("NIPC Act").

⁴⁷ *Ibid.* See Nigerian Company Law and Practice by Orojo, pp.90-94.

⁴⁸ Per Delvin J in *Bank voor Handel en Scheepvaart N.V. v. Slatford* (1953) 1 O.B 248 at 278.

⁴⁹ L.C.B Gower, *Gower's principles of Company Law*, 4th edn, London: Stevens and Sons 1979, p.112.

⁵⁰ J.A Dada, *Principles of Nigerian Company Law*, 2nd edition, Calabar: Wusen publishers, 2005, p.90. See also *A.C.B Ltd v. Apugo* (1995) 6 NWLR pt 399 at 65.

⁵¹ (1999) 8 NWLR (pt.613) 119 at 129.

⁵² (1998) 3 NWLR (pt.543) 602.

This will be necessary where the canopy of legal entity is used to defeat public convenience, justifying wrong perpetuate and protect fraud and crime... or involved in reckless or fraudulent trading activities tainted with fraud.⁵³ This paper will discuss the circumstance under which the veil of incorporation could be pierced under the law.

(ii). Reduction in the Number of Directors

Under section 93 of CAMA,⁵⁴ if at any time the number of members falls below two and it carries on business for more than six months while the number is so reduced, every director or officer to the company during the time it so carries on business after those six months who knows that it is carrying on business with only one or no director member, shall be liable jointly and severally with the company for the debts of the company contracted during that period.⁵⁵

Under section 246(1) of CAMA, every company registered upon or after the commencement of the Act (CAMA) must have a minimum of two directors, while companies which came into existence before the Act must, before the expiration of six months from the commencement of the Act, must have a minimum of two directors. By section 246(2) provided that a company with less than two directors must within a month appoint a new one failing which it shall not carry on business again unless such new directors are appointed. The consequence of failure to adhere to these provisions is that the veil of incorporation will be lifted in that by section 246(3) where the number of the directors of a company falls below two and the company nonetheless continues to carry on business after sixty days of such depletion and every director or member of the company who knows that the company so carries on business after that period shall be liable for all the liabilities and debts incurred by the company during that period.⁵⁶

⁵³ J.A Dada, supra note 48.

⁵⁴ Companies and Allied Matters Act, Cap C20, LFN 2004, Section 93.

⁵⁵ Olakanmi & Co. Companies and Allied Matters Act, Cap. C.20 LFN, 2004, Lagos & Abuja: Law Lords Publications, 2006, pp.8-9.

⁵⁶ J.A Dada, supra note 48. p.94

(iii). Declaration of Shares by Substantive Shareholders of a Company

By section 95, a person who is a substantial shareholder in a public company shall give notice in writing to the company stating his name and address and giving full particulars of the shares held by him or his nominee by virtue of which he is a substantial shareholder. Failure to comply with this requirement may warrant the lifting of the veil of incorporation. Again where shares in a company are held upon trust and the management of the company is in the hands of the trustees, the court may lift the veil of incorporation so as to reconcile the company's properties with the terms of the trust.⁵⁷ In *The Abbey, Malvern Wells Ltd. v. Ministry of Local Government Planning*,⁵⁸ Dankwerts J. was prepared to accept the fact that a company held all its property on charitable trust when all the shares in it were so held and its articles of association provided that the trustees were to be its governing body.

(iv). Failure to Comply with Established Business Ethics under CAMA

Section 548 requires that the name of the company shall be (a) fixed outside every office where it carries on business; (b) engrave on its common seal (c) mentioned in all Bills of Exchange, business letters, notices, advertisements and official publications. Any director or manager who knowingly and willfully authorizes or permits a default in this regard shall be personally liable accordingly (section 548(1)).⁵⁹ Again under section 631(4) of CAMA, it is required that the name of every company be mentioned in legible characters in all bills of exchange, promissory notes, endorsements and cheques issued by the company. If any officer of a company issued or authorizes the issue of any bill of exchange, promissory notes, cheques or other negotiable instruments without the name of the company so mentioned, he will be liable to the holder of any such bill of exchange for the amount thereof unless the company acknowledge and pays same as it was decided in the case of *Nathaniel Abodun Adeniji v. The State*.⁶⁰ In *Durham Fancy Good Ltd. v. Michael Johnson Fancy Goods Ltd.*,⁶¹ it was held that if the holder of the company's document is responsible for the misdescription, he will be stopped from enforcing the company's liability.

⁵⁷M.O. Sofowora, *Modern Nigerian Company Law*, 2nd edn. Lagos: Soft associates, 2002, p.86

⁵⁸ (1951) Ch.728.

⁵⁹Olakanmi & Co. *Supra* note 53.

⁶⁰ (1992) 4 NWLR p.248

⁶¹ (1968) 2 Q.B. 839.

(v). Fraudulent Transactions by the Company after Winding Up

If where a company is wound up, it is shown that proper books of account were not kept by the company throughout the period of two years immediately preceding the commencement of the winding up of the period between incorporation and commencement of winding up whichever is the shorter every officer of the company who is in default, unless he shows that he acted honestly, shall be liable to a fine subject to section 506 of CAMA. If a company is wound up or in the process of being wound up, the court is satisfied that its business has been carried on with the intent to defraud its creditors or the creditors of another person, or for any fraudulent purpose, the court may on the application of the official receiver or the liquidator or any creditor or contributor of the company, declare that any person who was knowingly party to the carrying on of the business in that manner shall be personally responsible without any limitation of liability for all the debts or other liabilities of the company as the court may direct.⁶²

According to J.A Dada, the provisions of this section is though wide and far reaching, it can only be invoked where the persons responsible for managing the business of the company have been guilty of dishonesty which they commit or in which they participate.⁶³ For a person to incur liability, he must have actively participated in the management of the company. So a shareholder cannot be made personally liable for a company's debts no matter how large his shareholding is, merely because he nominated or procured the appointment of directors who are guilty of fraudulent trading.⁶⁴

⁶²J.A Dada, *supra* note 47. p.92. from a different perspective, if in the course of the winding up of a company, it appears that any business of the company has been carried on in reckless manner or with intent to defraud creditors of any other person for any fraudulent purpose, the court on the application of the official receiver or the liquidator or any creditor or contributory of the company, may, if it thinks proper so to do, declare that any person who were knowingly parties to the carrying on of the business in manner aforesaid shall be personally responsible for all or any of the debts or other liabilities of the company subject to the provisions of section 506 of CAMA

⁶³ See *Re Gerald Cooper Chemicals Ltd.* (1978) 2 All ER 49.

⁶⁴ *DPP v. Schildecamp* (1971) A.C 1. H.L

(vi). Failure to keep upto Date Financial Statement of Account

If at the end of a year a company has subsidiaries, the directors shall, as well as preparing individual accounts for that year, also prepare group financial statements being accounts or statements which deal with the state of affairs and profit or loss of the company and the subsidiaries subject to the provision of section 336 of CAMA.⁶⁵ This is a common occurrence to create a pyramid of inter-related companies each of which is theoretically a separate entity a part of one concern presented by the group as a whole. The group company is what is known as holding company while the interrelated companies so created are known as the subsidiary companies. Where at the end of its financial year a company have subsidiaries, group accounts dealing with the state of affairs and the profit and loss of the company and the subsidiaries must be presented in the general meeting when the company's own balance sheet and profit and loss account are so laid. This is the purport of Section 336 of CAMA. The circumstances in which this provision may not be adhered to are laid down in sub-section 2 of the section. But where this is impracticable or the amount involved is so insignificant; or a lot of expenses would thereby be occasioned, or where the result would be misleading or the business of the company is different, then this provision may be impracticable.⁶⁶

(vii). Improper or Dubious Control and Management of the Company

By virtue of section 234 of CAMA a written resolution signed by all the members of a private company entitled to attend and vote shall be as valid and effective as if passed in a general meeting notwithstanding that no formal meeting was in fact held. It may be necessary for the purpose of companies' income tax to go behind the veil of incorporation in order to ascertain where the control and management of the company is exercised, because this determines whether or not a company is a "Nigeria Company".⁶⁷

⁶⁵ Ibid.

⁶⁶ Ibid. See also J.A Dada, *supra* note 47. pp. 94-95.

⁶⁷ Ibid. See the Income Tax Act of 1979.

(viii). Investigation of the Affairs of Companies under the Statutes

According to J.A Dada, he stated that in order to enhance effective and proper management of companies, provisions are made for investigation of their affairs.

An inspector appointed to investigate a company may also investigate the affairs of a related company if he considers it necessary for the investigation of the company and which he was appointed to investigate.⁶⁸ When this is done, it involves lifting the corporate veil.⁶⁹

4. Lifting the Veil of Incorporation under Case Law

Experience has shown that the courts are reluctant to lift the veil of incorporation principally because of the decision in the case of *Salomon v. Salomon* and to save the corporate image of the company as discussed above in Salomon's case. The idea of lifting the veil of incorporation is last resort for a company's defiance of established legal procedures guiding business corporations in Nigeria.

(i). Status of a Company as a distinct personality to the Shareholders and Directors

The general position of the law is that the company is a separate legal entity from its shareholders and directors with the result that the acts of any of these biological persons carried out within the ambit of the memorandum and article of association of the incorporated company is solely the act of the incorporated company for which it alone is responsible. In effect the consequence of recognizing the separate personality of a company is to draw a veil of incorporation over the company generally. No one is entitled to go behind or lift the veil except the court or operation of the statutes. Since a limited liability company only exists in the eyes of the law, it can only operate by means of human beings; usually a company acts through its directors and managers whose actions can be attributed to the company hence in *Adeyemi v. Baker (Nig) Ltd*,⁷⁰ the Lagos Court of Appeal held that on when the veil of incorporation will be lifted, if it is discovered from the materials before the court that

⁶⁸ See Sections 314-330 of CAMA dealing with investigation of companies and their affairs and section 316(1) of CAMA.

⁶⁹ J.A Dada, *supra* note 48, p.95.

⁷⁰ (2000) 7 NWLR (pt.663), 33 at 37-38.

a company is the creature of a biological person, be he a managing director or a director and the company is a device or r sham or mask which he hold before his face in an attempt to avoid recognition by the eyes of equity, the court must be ready and willing to open the veil of incorporation to see the characters behind the company in other to do justice.

(ii). Liability for Fraud and Doing Justice to Victims

In *Alade v. Alice (Nig) Ltd*,⁷¹ Galadima JSC stated that one of the occasions when the veil of incorporation of a company could be lifted by the court is when the company is liable for fraud. The consequences of recognizing the separate personality of a company is to draw a veil of incorporation over the company. One is generally therefore not entitled to go behind or lift this veil. However, since a statute will not be allowed to be used as an excuse to justify illegality of fraud, it is in a quest to avoid the normal consequences of the statutes which may result in grave injustice that the court as occasion demands have to look behind or pierce the corporation veil. While Munktaka-Coomassie J.S.C delivering his judgment stated that, "it must be stated that unequivocally that this court as the last court of the land, will not allow a party to use his company as a cover to dupe, cheat or defraud an innocent citizen who entered into lawful contract with the company, only to be confronted with the defense of the company's legal entity as distinct from is directors.

Most companies in this country are owned and managed by an individual, while registering the members of his family as the shareholder. Such companies are nothing more than one-man-business. Thence, the tendency is there to enter into contract in such company name and later turn around to the claim that he was not a party to the agreement since the company is a legal entity".

(iii). Misappropriation of Company's Fund

Justice Rhodes Vivour, J.S.C.(As he then was) in *Alade v. Alice (Nig) Ltd*,⁷² is of the view that by virtue of section 290 of the companies and Allied Matters Act, where a company receive money by way of loan for a specific purpose or receives money or other property by way of advance payment for the execution of a contract or project and with intent to defraud fails to apply the money or other property for the purpose for which it was received, any director or other officer of the company

⁷¹ (2010) 19 NWLR (Pt.1226) at 116-117

⁷² Ibid. at 120.

who is in default is personally liable to the property from whom the money or property was received for refund of the money or property so received and not applied for the purpose for which it was received.⁷³

(iv) Reasons of Public Policy or Interest

According to Frank Rose and J.A Dada, considerations of public policy are likely to override particular legal rules. Also, injustice may clearly result from improper conduct and the courts are particularly unwilling to permit the use of the corporate form in other to further improper conduct. They may go farther. While Dada is of the view that the principle of separate legal entity will be disregarded and the personal qualities of its shareholders or the persons in control of it will be investigated if there is an overriding public interest to be served by doing so. This is an exception to the recognition and preservation of the concept of legal personality is mostly applicable in war time situations.⁷⁴

(v) Nationality or Residence Status of the Company

A company as a legal person is expected to have a residence. The same goes for its members. The determination of the nationality or residence status of a company usually occurs in cases involving multinational or transnational companies. The court may intervene to determine the character of person making up the company as directors and shareholders. Where the company is suspected for instance as being owned and controlled by enemies of a nation or similar persons, the residence of its controlling members may be treated as the residence of the company.⁷⁵ This principle of law was applied in the case of *Daimler Co Ltd, v. Continental Tyre and Rubber Co.*⁷⁶ Continental sued Daimler for the price of goods delivered but not paid for, Continental was registered in England, but all of its directors, and all but one of its shareholder were German nationals and resided in Germany. The company's secretary held one share, and although he too was born in Germany, he resided in England and in 1910 became a naturalized Englishman. Daimler argued that to allow continental to sue in English courts would amount to

⁷³ It is clear in this case that that substantial part of the sum of N240, 000.00 obtained for the partnership was used in settling the 1st respondent's indebtedness to IBWA.

⁷⁴ Francis Rose, supra note 9. p.40. See also J.A Dada, supra note 48. p.96.

⁷⁵ C.S Ola, supra note 13, p.15.

⁷⁶ (1916) 2 AC 307.

trading with the enemy contrary to Trading with the Enemy Act 1914, as we were at war with Germany at the time the action was commenced. The Court of appeal upheld a decision to grant Continental summary judgment. Continental appealed to the House of Lords and the appeal was successful and the action was struck out. The company secretary lacked the authority to commence the action and continental had acquired an enemy character. This was determined by looking behind the veil of incorporation to discover the nationality of its controllers.⁷⁷

(vi). Tax Evasion

In the corporate world, companies are formed for different purposes but such purposes are enshrined in their memorandum and articles of association. Companies are expected to compulsorily pay tax to the government as part of corporate social responsibility and revenue for the government. Where a company is found cheating or is formed to evade tax which amounts to defrauding the Inland Revenue office of the country. The Inland Revenue can always challenge the company in court and under such situation; the court will lift the veil of incorporation of the company.⁷⁸

5. Justification of the Power of a court to Life the Veil of Business Incorporation

In business law, the power of a court to life the veil of incorporation is premised on the consequence of recognizing the separate personality of a company. The veil of incorporation makes it to assume the status of a separate personality distinct from those of its directors and shareholders and therefore one is generally not entitled to go behind or lift this veil but since a statutes will not be allowed to be used as an excused to justify illegality or fraud, it is in quest to avoid the normal consequences of the statutes which may result in grave injustice that the court as occasion demand have to look behind or pierce the corporate veil.⁷⁹ The court may also on grounds of public interest lift the corporate veil where the company is formed to carryout unlawful and or illegal acts.⁸⁰ For example where a company is suspected or legally indicted as supplying funds for insurgents' activities within or outside a country or where a company is used for money laundering and terrorist funding in a country, or sponsoring organized crimes like human trafficking, trade in harmful weapons and drug trafficking, public policy demands that the court should

⁷⁷ Chris Shepherd, *supra* note 17, pp.4-5.

⁷⁸ M.O. Sofowora, *supra* note 53 p.87. See *Marina Nominees v. Board of Inland Revenue*, (1986)2 NWLR (Pt.20) 48.

⁷⁹ *FDB Financial Serv. Ltd v. Adesola* (2000) 8 NWLR (Pt.668), 174 as per Aderemi J.C.A.

⁸⁰See, *J.A Dada*, *supra* note 48. p.97.

approached to crack the veil of incorporation to enable the government and members of the public know those directors or shareholders behind the nefarious activities of the company and find out their intents and purposes.

Where such veil is lifted the certificate of incorporation of the company will be produced as it is only by the production of that certificate that its legal personality can be proved in such circumstances stated under this sub-issue.⁸¹ This was stated in the case of *Chinwo v. Owhonda*,⁸² that the court observed that allegation of crime lifts the veil of incorporation or voluntary associations and opens up the body to judicial inquiry upon good and substantial facts, placed before a court of competent jurisdiction. Hence the court stated in *Adeyemi v. Lan Baker Nig. Ltd*,⁸³ that: "there is nothing sacrosanct about the veil of incorporation of a company, thus if it is discovered from the materials before a court that a company is the creature of a biological persons be he a managing director or a director and that the company is a devise or a sham or mask which he holds before his face in an attempt to avoid recognition by the eye of equity, the court must be ready and willing to open the veil of incorporation to see the characters behind the company on order to do justice."

6. Conclusion

This article have explained that the concept of lifting the veil of incorporation is an age long corporate rule spanning almost two centuries going by the decision in *Salomon v. Salomon*. It is enunciated in this article that the sanctity of a business corporation rest on the veil of its incorporation without which the company is prone to corporate assault and litigation from all and sundry. By incorporation, therefore, a veil may be said to be drawn between persons dealing with a company and its members, so that direct proceedings may not generally be taken against the members themselves. Just like a third party cannot proceed against the members by ignoring the company, he may be similarly unable to proceed against the company through the medium of one of its members too.⁸⁴

⁸¹ See, *A.C.B Plc v. Emos Trade Ltd.*(2002) 8 NWLR (pt 770), 501 at 517. See *Trustees, P.A.W Inc. V. Trustees, A.A.C.C.* (2002) 15 NWLR (Pt.424) at 446.

⁸² (2008) 3 NWLR, Pt. 1074, 341 at 362.

⁸³(2000) 7 NWLR (Pt 663) p.33 at 51.

⁸⁴ In *B. v. B.* (1978). Fam 181. A wife was unable to obtain discovery of a company's documents by asking the court to order her husband, who had a right as a director to inspect them, to produce them. it was held that a discovery order obtained by a wife against her husband was not effective against the husband's company as it was not named in the order and was separate and distinct from him. Although

But despite the protection offered by the corporate veil, there are dare circumstances in which the veil of incorporation of a company can be lifted without doubt. These are by virtue of the statutes or company's Act dealing with the incorporation and operation of of Companies like the CAMA as in the case of Nigeria and by the Court in the event that the terms of the statutes is being violated or there is illegality of fraud being perpetuated by the corporation because the court will not allow a piece of legislation no matter how weak to be used as an engine for fraud.

The court may still use a sledge-harmer to crack open the corporate shell in any of the following cases: Agency Relationship, Prevention of Fraud, Public Policy Reasons, and for the sake of Associated Companies among others.⁸⁵

it did attach to documents within the husband's custody or control. See also Francis Rose, *supra* note 7, p.36.

⁸⁵Olakanmi & Co. *Supra* note 53. p.10-11.