

ENTERPRISE FORMS AND ENTERPRISE LIABILITY: IS THERE A PARADOX IN MODERN CORPORATION LAW?

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SUMÁRIO: *I – Introduction. II – Enterprise Forms and Enterprise Liability.* 1. The Unincorporate Enterprise. 1.1. Enterprise and Entrepreneur. 1.2. The Liability of Unincorporate Enterprises: the Old Mercantile Law. 2. The Singlecorporate Enterprise. 2.1. The Invention of the Dogma of Corporate Autonomy. 2.2. The Liability of Singlecorporate Enterprises. 3. The Polycorporate Enterprise. 3.1. The Rise of the Polycorporate Enterprise. 3.2. The New Feature of Corporate Control. 3.3. The Liability of Polycorporate Enterprises. *III – The Liability Problems of Polycorporate Enterprises: A Comparative Overview.* 1. Preliminary Remarks. 1.1. Its Practical Impact. 1.2. The Unsolved Theoretical Problem. 1.3. The Main Regulatory Strategies. 2. The Entity Law Approach. 2.1. The Liability of Parent Corporation. 2.2. The Liability of Directors. 2.3. Critical Appraisal. 3. The Enterprise Approach. 3.1. The Liability of Parent Corporation. 3.2. The Liability of Directors. 3.3. Critical Appraisal. 4. The Dualist Approach. 4.1. The Liability of Parent Corporation. 4.2. The Liability of Directors. 4.3. Critical Appraisal. *IV – The Polycorporate Enigma and The Paradox of Modern Corporation Law.* 1. The Core of the Enigma. 2. An Enigma Solved? The Principles of Corporate Autonomy and Corporate Control. 2.1. The Legal Perspective. 2.2. The Organizational Perspective. 2.3. The Group as an Hybrid Form of Enterprise. 3. The Paradox of Modern Corporation Law. 4. Conclusion.

I – INTRODUCTION

The *enterprise* (“empresa”, “Unternehmen”, “entreprise”, “impresa”) represents a major economic ⁽¹⁾, social ⁽²⁾, political ⁽³⁾, and even cultural

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(1) DAEMZ, *The Rise of the Modern Industrial Enterprise*, 203 ff.; HORN / KOCKA,

institution ⁽⁴⁾ of the last two centuries, which performs, by definition, a *risky activity*. It may produce losses or even totally collapse, running down with it the hopes of those who invested their wealth on it (owners), of those who extended it credit (creditors), of those who sold their labour for monetary retribution (workers), or even of those who bought their products and services (consumers). It also generates a high variety of costly externalities, in private as well as in public areas: it often undertakes business ventures manufacturing dangerous products, potentially harmful to individual consumers, or operates hazardous activities responsible for ecological catastrophes for society as a whole, such as environment pollution and chemical or nuclear disasters.

Being essentially a risky activity, someone has to bear the burden of such costs and risks. *Who has to pay the price of enterprise business activity?*

II — ENTERPRISE FORMS AND ENTERPRISE LIABILITY

The legal imputation of the costs and risks of entrepreneurial activity has undergone a profound evolution throughout centuries. This evolution has evolved according to the legal forms of business enterprises themselves: these forms are the *unincorporate* enterprise (“*empresa individual*”), the *single incorporated* enterprise (“*empresa social*”), and the *polycorporate* enterprise (“*empresa de grupo*”).

1. The Unincorporate Enterprise

For many centuries, business enterprises have been as such an unknown subject of the Law. Priory to the 19th century, the prevailing economic system was basically a world of small-sized and rural or artisan-type firms, exploited by a single trader or partnerships with few associates.

Recht und Entwicklung der Großunternehmen im 19. und frühen 20. Jahrhundert, 123 ff.; WILLIAMSON, *The Modern Corporation: Origins, Evolution, Attributes*, 131 ff.

(2) SELZNICK, *Law, Society and Industrial Justice*, 43 ff.

(3) LATHAM, *The Body Politic of the Corporation*, 218 ff.; OTT, *Recht und Realität der Unternehmenskorporation*, spec. 127 ff.; STEIMANN, *Das Großunternehmen im Interessenkonflikt*, 36 ff.

(4) CHAYES, *The Modern Corporation and the Rule of Law*, 25.

1.1. Enterprise and Entrepreneur

Even if the ancestry of the modern Corporation is commonly traced back to the large old colonial companies of the seventeenth century ⁽⁵⁾, it would certainly be inaccurate to consider that all or most business enterprises were a kind of miniatures of the mammoth English or Dutch East India Companies: while this genealogical line is probably genuine, the fact remains that the dominant role of the economic system was definitely played by trader proprietorships, with a family-like dimension, assembling very limited financial and labour resources, engaged in a local and one-product market, possessing no business relationships with commercial partners and holding no significant market share ⁽⁶⁾.

Thus, during the 17th and 18th centuries, no doubt that the key figure of the economic system was then the one of the *unincorporate enterprise*, owned by a single trader (“empresario-persona física”, “Einzelkaufmann”, “commerçant individuel”, “imprenditore”) ⁽⁷⁾.

1.2. The Liability of Unincorporate Enterprise: The Old Mercantile Law

Lacking any specific body of legal norms, it is no wonder that the regulation of the formation and life of the unincorporate enterprise, including the one concerning the liability imputation of entrepreneurial risks, has for centuries been abandoned to the most general common law principles.

⁽⁵⁾ Still central on the subject, LEHMANN, *Die geschichtliche Entwicklung des Aktienrechts*, 28 ff.; to others important works about the origin of modern corporation, see LÉVY-BRUHL, *Histoire Juridique des Sociétés de Commerce en France aux XVII^{ème} et XVIII^{ème} Siècles*; GALGANO, *Storia del Diritto Commerciale*, 61 ff., 115 ff.; WIETHÖLTER, *Interessen und Organisation der Aktiengesellschaft in amerikanischen und deutschen Recht*, 53 ff.; SEAVOY, *The Origins of the American Business Corporation 1784-1855*.

⁽⁶⁾ On the earlier stages of enterprise evolution, cf. SEAVOY, *The Origins of the American Business Corporation 1784-1855*, 9 ff., 53 ff.; FREEDMAN, *Joint-Stock Business Organization in France 1807-1867*, 185 ff.; KOCKA / SIEGRIST, *Die hundert größten deutschen Industrieunternehmen im späten 19. und frühen 20. Jahrhundert — Expansion, Diversifikation und Integration im internationalen Vergleich*, 55 ff.

⁽⁷⁾ As HADDEN put it, “the entrepreneur or businessman was still the key figure: it was he who adventure or undertook the risks of directing production, brought together the capital and labour required for the work, arranged or engineered its general plans and superintended its minor details. (...) The corporate form of organization was thus not subjected to serious analysis by the founding fathers of economics” (*Company Law and Capitalism*, 19).

The law of this primary form of enterprise organisation was then basically provided by the old, medieval-rooted *mercantile laws* mainly developed by Civil Law countries (“Derecho Mercantil”, “Handelsrecht”, “Droit Commercial”, “Diritto Commerciale”), as the law of individuals merchants⁽⁸⁾. Since the business enterprise was lacking any type of legal autonomy, this could only mean that it was the enterprise owner or businessman who carried personally the burden of liability for all enterprise debts. As a matter of fact, the most general standard of liability law concerning economic and social behaviours — the *nexus between power and liability* (“Herrschaft und Haftung”) — established that each person that has the control of an action should be liable for the damages and consequences of such action with its entire patrimony (“ubi commoda ibi incommoda”)⁽⁹⁾: therefore, the businessman himself was then fully accountable for both the positive and negative consequences of his business enterprise.

2. The Singlecorporate Enterprise

When at the end of the 19th century, concluding a long historical evolution whose remote source is founded in the struggle for the incorporation privilege, business enterprises were granted the possibility of self-incorporating and were finally made the object of a new set of legal rules all over the world — *Corporation Law* (broadly, “Derecho de Sociedades”, “Gesellschaftsrecht”, “Droit des Sociétés”, “Diritto delle Società”) —, such state of affairs had undergone a profound change⁽¹⁰⁾.

2.1. The Invention of the Dogma of Corporate Autonomy

When incorporated, the business enterprise constitutes not only an economically but also legally independent entity, with its own rights and duties, its own assets and liabilities.

⁽⁸⁾ The merchant is still the paradigmatic legal actor of Commercial Law: cfr. RAISER, *The Theory of Enterprise Law*, 2. To further historical insights on this evolution, see also RAISER, *Das Unternehmen als Organisation*, 15 ff.

⁽⁹⁾ This general principle is a fundamental bulwark of Civil Law systems in the area of liability law: see, for instance, for *Italy*, art. 2740 “Codice Civile” (cf. ROPPO, *Responsabilità Patrimoniale*, 1402 ff.)

⁽¹⁰⁾ On the historical origins of a general statutory Corporation Law, see for a general overview SOLÀ CAÑIZARES, *La Constitution de la Société par Actions en Droit Comparé*; ROTONDI, *I Grandi Problemi delle Società per Azioni nelle Legislazione Vigenti*.

Through the corporate device, business enterprises have reached at last a legal status on its own in the juridical arena, side-by-side with human beings. The attribution of a *legal personality* to the business enterprise lead in turn to a clear-cut separation between the legal sphere of the enterprise owners or investors (shareholders) and the legal sphere of the incorporated enterprise itself. This separation, among other effects, entailed that only the latter would be made accountable for consequences stemming from enterprise activity ⁽¹¹⁾. On the top of this, a revolutionary rule dealing specifically with the allocation of enterprise risks (that has become since then “a fundamental principle of corporate law” ⁽¹²⁾) has been consecrated in order to encourage the widespread investment and capital accumulation required for the growth of enterprises: the rule of *limited liability* of shareholders for the corporate debts. According to this rule, the responsibility of corporate investors was limited to the amount of their capital investment, circumstance which strengthened even more the insulation of such individuals before the liabilities and debts of the corporation ⁽¹³⁾.

2.2. The Liability of the Singlecorporate Enterprise

The dogma of corporate autonomy has been paramount for the regulatory framework of business enterprises. Since its invention, both legis-

⁽¹¹⁾ The attribution of the *legal personality* to corporations is a sort of common denominator of comparative Corporation Law, in both Civil and Common Law systems: this has been expressly consecrated, amongst many others, by § 1 German “Aktengesetz” of 1965, art. 5.^o of the former French “loi du 24 juillet 1966”, art. 2331.^o Italian “Codice Civile” of 1942, or section 1 and 13 British “Companies Act” 1985. As WIEDEMANN put it: “The juridical institution of the legal person gives the basis for the development of the modern public corporation” (original in German) (*Gesellschaftsrecht*, 203).

⁽¹²⁾ EASTERBROOK / FISCHEL, *Limited Liability and the Corporation*, 89. Other celebrated expressions come from BALLANTINE (“the most essential privilege of incorporation”: *Law of Corporations*, 4); FULLER (“in the historical development of the corporation probably no single attribute has been more significant than that of limited liability”: *The Incorporate Individual: A Study of the One-Man Companies*, 1376); HENN (“limited liability is probably the most attractive feature of the corporation”: *Laws of Corporations*, 96); HORNSTEIN (“in practical importance this feature for over a century has outranked all the other consequences of incorporation”: *Corporation Law and Practice*, § 20); SOWARDS (“the hallmark of the corporation is limited liability”: *Corporation Law*, 2).

⁽¹³⁾ On the historical development of limited liability, see BLUMBERG, *The Law of Corporate Groups*, III, 7 ff.; BLUMBERG / STRASSER, *Corporate Groups and Enterprise Liability*, 17 ff.

lators and jurisprudence have treated the business enterprise according to the ideal model of the large publicly-held autonomous corporation, composed of a myriad of powerless shareholders and governed by independent managers pursuing its best business interests (14).

This ideal model of the corporation, living under a typical separation between ownership and management (15), provides also the basic “rationale” of the legal system of allocation of enterprise risks created by Corporation Law. While the business of a unincorporate enterprise is directly conducted by the individual merchant himself, thereby justifying the imposition of an unlimited and personal liability, the role of the shareholder of incorporated enterprises in its day-to-day management is extremely scarce, if not purely inexistent (16), reason why his liability should be accordingly limited (17): if unlimited power entails unlimited liability, *limited power should also entail a limited liability* (“keine Haftung ohne Herrschaft”) (18). This was the fundamental “leitmotiv” underlying the very first statutory enactment of the principle of limited liability as a default rule of Cor-

(14) “The received nineteenth century regulatory model is based in the ideal image of the autonomous corporation” (SCHMIDT, *Gesellschaftsrecht*, 400).

(15) See also MANNE, *Our Two Corporations Systems: Law and Economics*, 259 ff., 262.

(16) Except in extreme occurrences (election of directors, adoption of bye-laws, extraordinary corporate matters — amendment of articles of incorporation, mergers, dissolution), the shareholder voice in management is merely passive. See also CHRISTENSEN: “Clearly, unlike the proprietor or partner, the shareholder does not guide the corporation through every day business” (*Concept of Limited Liability in US Business Entities*, 445).

(17) The imposition on such passive or powerless owners of a liability for corporate debts would also expose them to risks originating out from a decision-making process from which they are far removed and over which they do not have any realistic chance of direct control: this would also certainly deter investment, impairing thus ultimately the vocation of the corporation as a capital-raising device. On the economic foundations of limited liability of shareholders of incorporated enterprises, see “ex multi” EASTERBROOK / FISCHER, *Limited Liability and the Corporation*, 89 ff.; HALPERN / TREBILCOCK / TURNBULL, *An Economic Analysis of Limited Liability in Corporation Law*, 117 ff.; KRAAKMANN, *The Economic Functions of Corporate Liability*, 178 f.; LANDERS, *A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy*, 589 ff.; LEHMANN, *Das Privileg der beschränkten Haftung und der Durchgriff im Gesellschafts- und Konzernrecht*, 345 ff.

(18) WIEDEMANN: “More and more, the inverse principle — no liability without dominance («keine Haftung ohne Herrschaft») — goes by itself, since shareholders without any influence on the corporate management, i.e investors, are not willing to incur in personal liability (...). Who extended some assets to an alien enterprise, on which management he has no influence whatsoever, should incur only in a predictable and limited risk” (original in German) (*Gesellschaftsrecht*, 546 and f.).

poration Law, in the article 33.^o of the French “Code de Commerce” of 1807 (19). Ever since that time, in most of the countries, the limited liability of shareholders has been understood as a “correlative” (20) or a “consequence” (21) of their anonymous, powerless membership (22).

With the introduction of such a clear line of demarcation between the corporation (as legal person) and its individual owners (as shareholders), enterprise liability had entered into a completely new era. From that moment on, the incorporated enterprise, as a separate legal entity with its own rights and duties, has alone been held legally liable to meet all types of risks and costs generated by its business activity. This was and still is the general solution foreseen by the law of enterprise liability for the most relevant sector of modern business activity (23).

3. The Polycorporate Enterprise

3.1. The Rise of the Polycorporate Enterprise

This classical statutory model of enterprise, and its attached liability regime, operated satisfactorily as long as the business enterprise has indeed been organised and conducted through a single independent corporation (24).

(19) LEHMANN, *Das Recht der Aktiengesellschaften*, I, 216.

(20) WIEDEMANN, *Gesellschaftsrecht*, 547.

(21) PETERSON: “The limited liability is to be interpreted, not as a privilege, but as a consequence stemming from the fact that members of a corporation may stay anonymous and shares are freely transferable” (original in German) (*Juristische Person und begrenzte Haftung der Aktionäre*, 533).

(22) NÄEGELI: “In the same way that law makes each individual responsible for its own actions, law imposes, under a principle of fairness, that personal liability should be appreciated according to the real power of action or control; in other words, individuals should be liable exclusively for the acts which can really be imputed to them” (*Der Grundsatz der beschränkten Beitragspflicht*, 36).

(23) I am concerned here only with the case of Corporations, by far the dominant legal form of enterprise organisation of modern times. Obviously, company law embraces as well other legal types of enterprises (namely, partnerships) where legal regimes of liability are quite different.

(24) The theoretical and practical validity of the regulatory framework of Corporation Law, including those particular rules concerning the allocation of corporate liabilities, is in fact dependent on the circumstance that the reality of corporations stays in line with such an ideal legal model of autonomy. In other words, the linkage between the economic

However, if one looks to modern world economy at the 20th century, one concludes that enterprises have increasingly chosen to organise and conduct their business operations in the form of a cluster of various separate corporations rather than as a single corporate entity. The major enterprise has typically evolved as a complex large-scale business network, where the different parts of a unitary business are allocated to a group of affiliated corporations (subsidiary corporations), and where global co-ordination is obtained through the submission of such, legally independent, parts to a common economic strategy and management of the whole exercised by headquarters (parent corporation) (25).

As a matter of fact, amongst the largest economic entities in the world, one has 50 States and 50 multinational corporate groups. The total turnover of the eight largest multinational and multicorporate networks (Exxon, GM, Ford, General Electric, IBM, Chrysler, Texaco, Shell) was already at the beginning of the 70s some \$118 billions, a monetary amount identical to the global budget of six European countries all together (Belgium, Germany, France, Italy, Luxembourg, Netherlands). Some of these networks are even stronger economically than individual nations: for instance, the annual revenue of General Motors was estimated to be higher than the gross national product of Belgium, the one of Standard Oil corresponds to the one of a country such as Denmark, and the one of IBM to those of Portugal or Norway (26).

actor “enterprise” and the legal actor “corporation” is a fundamental precondition for the validity of such regulatory framework.

(25) Of the wealth of literature on the development of the modern economic system as a system of intercorporate concentration and of the modern enterprise as a typically polycorporate organisation, see, for *Germany*, KOCKA, *Expansion, Integration, Diversification – Wachstumstrategien industrieller Großunternehmen in Deutschland vor 1914*, 203 ff.; KOCKA / SIEGRIEST, *Die hundert größten deutschen Industrieunternehmen im späten 19. und frühen 20. Jahrhundert*, 55 ff.; for the *UK*, see KINDLEBERGER, *Economic Growth in France and Great-Britain 1851-1950*, 53 ff.; for the *USA*, see CHANDLER, *Strategy and Structure – Chapters in the History of Industrial Enterprise and The Beginning of Big Business in American Industry*, 79 ff.

(26) GROBFELD, *Internationales Unternehmensrecht*, 6. If in 1976 their turnover was already of the order of \$1,600 billion, by 1980 it had rocketed to \$2,635, the equivalent of 30% of the gross domestic product of the world economy in that year, and generating net earnings of around \$100 billion. And they employ about 45 million people, almost half of the total employment in the world manufacturing sector. To some data concerning the topic, see DUNNING / PEARCE, *The World's Largest Industrial Enterprises*.

The enterprise has thus entered into a new evolutionary age of its structural organisational. The earlier model of the singlecorporate enterprise has thus been simply superseded by the more complex model of the *polycorporate enterprise*, which represents what is, by and large, the dominant form of enterprise organisation in the largest world-wide markets (USA, EU, Japan) (27).

3.2. The New Feature of Corporate Control

Surprisingly, this dramatic change of enterprise structures has been a result of also dramatic change of modern Corporation Law. As a matter of fact, how odd this may sound to company lawyers of today, the fact is that the phenomenon of control between corporations (namely, via intercorporate stock ownership) was unanimously prohibited by the founding fathers of Corporation Law — considered as incompatible to the basic idea of corporate autonomy (KLEIN, 1914) (28) or refused as an abnormal situation (KEMPIM, 1883) (29) or an irrelevant phenomenon (MENZEL, 1911) (30). However, under the pressures of the economic and business interests, 20th century legislators all over the world have tacitly begun to comply with some corporate practices and to introduce new legal mechanisms which brought about a new and emergent feature that eclipsed those genealogical roots of classical corporate law: *corporate control* (31).

(27) For an empirical analysis of the impact of the polycorporate enterprise in today world economy, see more extensively ANTUNES, *Liability of Corporate Groups*, 37 ff.

(28) KLEIN, *Die wirtschaftlichen und sozialen Grundlagen des Rechts der Erwerbsgesellschaft*, 67.

(29) KEMPIM is particularly suggestive: “it is obviously an anomaly that one corporation controls another corporation” (*Die amerikanischen Trusts*, 341).

(30) MENZEL, *Die wirtschaftlichen Kartelle und die Rechtsordnung*, 31.

(31) The term *control* is an elusive one, as elusive as the reality it describes. There is no satisfactory formula known to this author for defining the phenomenon of control as a power of dominance over the corporation, capable of embracing all its possible origins, mechanisms, forms, and effects. Although we can intuitively perceived it as a crucial phenomenon of the internal and external dynamics of modern corporations, control represents a manifold reality that is not susceptible to be grasped by a bold theoretical definition. The works on this new feature of corporation law are rather fragmentary: for *France*, STORK, *Définition Légale du Contrôle d'une Société en Droit Français*, 385 ff.; for *Italy*, LAMANDINI, *Il “Controllo” — Nozioni e Tipo nella Legislazione Economica*; for the *UK*, FARRAR, *Ownership and Control of Listed Public Corporations — Revising or Rejecting the Concept of Control*, 39 ff.; for the *USA*, see BERLE, “Control” in *Corporation Law*, 1212 ff.

Though not all holding the same nature and form, all those mechanisms had nevertheless something in common: they opened up the possibility that corporations could be controlled by others corporations and governed according to alien business interests. These *legal mechanisms* of intercorporate control are now multiple, including those of a financial nature (namely, intercorporate stock ownership, cross-shareholdings, concentration of voting rights) ⁽³²⁾, contractual nature (be that by the use of specific inter-enterprise contractual agreements ⁽³³⁾ or of common commercial or civil contracts ⁽³⁴⁾), personal nature (interlocking directorships) ⁽³⁵⁾, or organisational nature (namely, those established through corporate by-laws) ⁽³⁶⁾.

⁽³²⁾ *Investment Trust Corp. Ltd. v. Singapore Traction Co. Ltd.* (1935, 1 Ch. 615) where only one share was capable of outvoting the remaining 399.999 shares, still remains a paramount example of the revolutionary scope of this mechanism of intercorporate control in the realm of the classical model of the autonomous corporation.

⁽³³⁾ Such as management control contracts, business transfer contracts, or profit pools. See ENGLISH, *Les Groupes d'Entreprises à Structure Contractuelle*; MERCADAL / JANIN, *Les Contrats de Coopération Interentreprises*; STROBEL, *Unternehmensvertrag im deutschen und französischen Recht*; VIRASSAMI, *Les Contrats de Dépendance*.

⁽³⁴⁾ Enterprises are increasingly co-operating through a variety of relationships organised by the use of common contractual forms, which are likely to alienate their power of economic self-determination. For instance, *supply agreements* (“Lieferungsverträge”, “contrats de fourniture”) may create a factual control between a corporation which is producing a very specialised product and its monopsonic buyer in the market; *loan contracts* (“Darlehensverträge”, “contrats de prêt”) may also create a factual control of the corporate lender over corporate borrower thanks to clauses eventually included in the contractual agreement attributing supervisory or monitoring rights to the former concerning the management of the later’s business. And the list may goes on: *technology transfer contracts* (“Lizenzverträge”, “accords de transfert de technologie”), *exclusivity contracts* (“Ausschließkeitsbindungen”, “contrat d’exclusivité d’achat ou vente”), *agency contracts* (“Besorgungsverträge”, “sous-traitance”), *franchising contracts*, etc. See DIERDORF, *Herrschaft und Abhängigkeit einer Aktiengesellschaft auf schuldvertraglicher und tatsächlicher Grundlage*, 258 ff.; SURA, *Fremdeinfluss und Abhängigkeit im Aktienrecht*, 54 ff.; WERNER, *Der aktienrechtliche Abhängigkeitstatbestand*, 140 ff.

⁽³⁵⁾ Although prohibited in earlier times, the possibility of the same physical persons of integrating the organs of different corporations has led to the device of interlocking board directorates (“personelle Verflechtung”, “unions personnelles”) as a major institutional mechanism of intercorporate control. See ANDREWS, *The Interlocking Corporate Director*; EBKE, *Interlocking Directorates*, 50 ff.; STOKMANN / ZIEGLER / SCOTT, *Networks of Corporate Power*.

⁽³⁶⁾ Contrary to the original assumptions of the founding fathers of Corporation Law, the incorporated enterprise is not a democratic organisation and the basic rule gover-

3.3. The Liability of the Polycorporate Enterprise

Needless to say, with this deep mutation in the organisation and structure of the modern enterprise, the original regulatory framework provided for by classical Corporation Law has thus enter into a crisis. While the economic forms of enterprise organisation have evolved in the direction of multicorporate structures, the legal forms of its organisation have remained stuck to a statutory model designed and conceived exclusively for the case of single corporate enterprises. As a result of this decoupling between legal and economic model of the enterprise, the polycorporate enterprise has thus become a sort of “explosive shell of classical company law” (Marcus LUTTER).

III — THE LIABILITY PROBLEMS OF POLYCORPORATE ENTERPRISES: A COMPARATIVE OVERVIEW

The present paper is addressed to one of the areas where the challenge set by the polycorporate enterprise to Corporation Law is greater — precisely the area of *enterprise liability*, that is, the treatment of liability issues at parent-subsidiary relationships.

1. Preliminary Remarks

The practical and theoretical importance of the treatment of liability issues in parent-subsidiary relationships is generally recognized ⁽³⁷⁾.

ning its functioning (the so-called majority principle) turns out to function essentially as a strategic mechanism for the appropriation of corporate control in the hands of a few wealthy investors: as EISENBERG put it, “what counts is not shareholders, but shareholdings” (*The Structure of the Corporation*, 44). Furthermore, the controlling and autarchic properties of the basic principle “one share-one vote” may even be strengthened by an appropriated design of the articles of association, which may ultimately enhance the control of one corporation over another or another even in cases of minority stockholdings: examples of this are, for instance, cumulative voting shares (“Mehrstimmenrecht”, “actions à vote plural”, “azioni a voto plurimo”), no voting shares (“actions sans droit de vote”, “azioni senza voto”), “golden shares”, proxies, voting trusts, etc.

⁽³⁷⁾ There is even unanimity on this point amongst corporate lawyers of diverse legal traditions on such circumstance: a leading commentator on the Civil Law systems has considered it as “the crucial problem of parent-subsidiary relationships” (LUTTER, *100 Bände*

1.1. Its Practical Impact

As a practical problem, there is probably no doubt about *the impact of intragroup liability problems in modern business litigation*. The best proof of this impact lies in the gargantuan number of judicial cases where the central question at stake is invariably the plaintiff's complaint about the inequitable outcome of the formal liability insulation between parent and subsidiary corporations in spite of the existence of a substantial linkage of control.

Far from being restricted to one single legal branch, such cases arise across *the entire range of the law*, covering areas as diverse as classical tort liability, contract liability, environmental liability, product liability, labour liability, competition liability, bankruptcy liability, or tax liability: it has been disclosed that plaintiff law firms in metropolitan areas in USA will often have two or three cases a year in which their client's recovery is thwarted by the corporate fiction⁽³⁸⁾. And far from being restricted to cases holding a sole private dimension involving individual voluntary creditors, such cases are frequently reaching *public dimensions* and involving a *mass of involuntary creditors*: catastrophes regularly involving large multinational corporate groups, such as "Hoffmann-La Roche" in Italy (1976), "Amoco Cadiz" in France (1978), "Exxon Valdez" in USA (1983), or "Bhopal" in India (1984), constitute just some of the most vivid and dramatic illustrations of this⁽³⁹⁾. Besides, the problem is likely to increase

BGHZ: Konzernrecht, 458); some scholars from the Common Law tradition go even further, to qualify it as "one of the great unsolved problems of modern company law" (SCHMITT-HOFF, *Banco Ambrosiano and Modern Company Law*, 363).

⁽³⁸⁾ In a handful of decisions, the US courts dealt with mini-corporate groups operating in the taxicab industry whose business was conducted as a single and highly integrated business unity (common management, common personnel, common trade names and logos, common supervisions and dispatching system, holding out to the public as a common operation, etc.), but which was typically fragmented into a number of separate subsidiary corporations. The entire assets of each of these group affiliates were composed of the ownership of a few cabs (sometimes only one) and a derisive liability insurance (the statutory minimum was \$10000), usually insufficient to compensate tort victims injured by its operations (such as passengers and pedestrians). On these so-called "*taxi cases*", see *Walkowszky v. Carlton* (18 N.Y. 2d 414, 223 N.E. 2d 6 [1966]), *Robinson v. Chase Maintenance Co.* (20 Misc. 2d 90, 190 N.Y. 2d 773 [Sup.Ct.1959]), *Teller v. Clear Service Co.* (9 Misc. d 495, 173 N.Y.S. 2d 183 [Sup. Ct. 1958]) and *Mull v. Colt Co.* (31 F.R.D. 154 [S.D.N.Y. 1962]).

⁽³⁹⁾ On the Bhopal case, see in *re Union Carbide Corp. Gas Plant Disaster at Bhopal, India* in December 1984, 634 F. Supp. 842 (S.D.N.Y. 1986), *aff'd and modified* 809 F.2d 195 (2d Cir. 1987). See KOLVENBACH, *Bhopal — Storm over the Multinationals?*, 47 ff.

as it has been asserted by several studies that enterprises operating in many industrial sectors, such as the hazardous-waste, chemical, nuclear, aeronautical, biotechnology sectors, usually expand through insulating in subsidiaries their most risky ventures in order to avoid tort liability exposure.

1.2. The Unsolved Theoretical Problem

But the problem also theoretically proves to be a major challenge. To deal with intragroup liability problems means to scrutinise the legitimacy of the extension of the “*sacred cows*” of classical corporation law, in particular the deep-seated institutions of the *legal personality* of corporations and of the *limited liability* of their shareholders, to new forms of enterprise organisation.

In fact, the typical hybrid nature of polycorporate enterprises⁽⁴⁰⁾ soon raised the problem of the unsuitability of the traditional liability standards, designed by the founding fathers of Corporation Law for the case of single-corporate enterprises. By extending those traditional, highly formal concepts (fashioned to rule the relationships between independent corporations and its individual investors) uncritically to parent corporations, legal orders and courts have thus proceeded without any apparent recognition of the vitally different considerations involved in the regulation of the liabilities of sole independent corporations and of mere parts of a multi-corporate groups whose activity falls entirely under the control of the parent corporation⁽⁴¹⁾. It soon became apparent that the automatic extension of these old archetypes to the new reality of corporate groups led inevitably to untenable distortions and could not be applied indiscriminately without leading to grossly unfair results⁽⁴²⁾. Moreover, when surveying

⁽⁴⁰⁾ See *infra* Part IV.

⁽⁴¹⁾ For a critical revisitiation of the historical, legal and economic rationale of the principle of the autonomy of corporations and of the limited liability of shareholders, as well as of their inconsistency regarding the phenomena of intercorporate control, see BLUMBERG, *The Law of Corporate Groups*, III, 17 ff.

⁽⁴²⁾ This has been clearly portrayed in the argumentation of Government of India in the above mentioned *Bhopal* case: “The complex corporate structure of the multinational, with networks of subsidiaries and divisions, makes it exceedingly difficult or even impossible to pinpoint responsibility for the damages caused by the enterprise to discrete corporate units or individuals. In reality, there is but one entity, the monolithic multinational, which is responsible for the design, development and dissemination of information and technology world-wide, acting through a forged network of interlocking directors,

the state of affairs in comparative law, the first impression received is probably one of some disappointment: not only do the main existing regulatory strategies provide quite disparate liability regimes for parent corporations, but even in themselves they often seem to provide no safe guidance as to the results, it being not rare to find cases, virtually identical as to their facts, where courts have decided in totally opposite senses. No wonder that a leading English scholar could refer recently to the question of intra-group liability as “one of the great unsolved problems of modern company law”(Clive SCHMITTHOFF) (43).

1.3. The Main Regulatory Strategies

The central question is thus: *given a polycorporate enterprise, under what circumstances may the parent corporation or its management be obliged to settle the liabilities and debts of its subsidiary corporations?*

Notwithstanding the different degree of legislative, judicial and doctrinal development among the various national legal orders, one may distinguish currently *three major types of regulatory strategies in comparative law*. These strategies are: the traditional strategy of the “*entity law approach*”, the revolutionary strategy of the “*enterprise approach*” and the mitigate strategy of the so-called “*dualistic approach*”.

2. The Entity Law Approach

The so-called “*entity law approach*” is the traditional and still prevailing regulatory strategy concerning intragroup liability for the great majority of Common or Civil Law countries.

2.1. The Liability of the Parent Company

This approach consists in the position of those legal orders that decide intragroup liability questions on the basis of the fundamental principle

common operating systems, financial and other controls. (...) Persons harmed by the acts of a multinational corporation are not in position to isolate which unit of the enterprise caused the harm, yet it is evident that the multinational enterprise is liable for such harm” (Complaint, *Union of India v. Union Carbide Corp.*, ¶ 21, at 8 (no. 85 Civ. 2969 S.D.N.Y., 1985).

(43) SCHMITTHOFF, *Banco Ambrosiano and Modern Company Law*, 361 (363).

according to which *one member of a corporate group, namely the parent corporation, cannot be made liable for the debts or the acts of other group members for the reason that they are distinct legal entities* ⁽⁴⁴⁾. Under this view, the imposition of liability on the parent corporation for debts of group affiliates is considered as a rule to be impossible: only in the most exceptional circumstances will this rule be left aside by *disregarding the corporate entity* of the corporations involved. This approach operates in the basis of a “rule-exception” jurisprudential system: the court starts its analysis with the heavy presumption that the separate corporate entity of affiliate corporations is to be respected for all legal purposes (rule) and is only prepared to pierce or disregard this entity in the most exceptional circumstances (exception) ⁽⁴⁵⁾: in the suggestive image of EASTERBROCK and FISCHER, “piercing seems to happen freakishly: like lightning, it is rare and severe” ⁽⁴⁶⁾. A variety of key expressions are associated with this worldwide stream of judicial development: “levantamiento del velo de la persona jurídica” in Latin Countries, “piercing the corporate veil” in USA, “lifting the corporate veil” in the United Kingdom, and so on ⁽⁴⁷⁾.

⁽⁴⁴⁾ On this universal overarching archetype of American law on corporations, see BLUMBERG, *The Law of Corporate Groups*; HENN / ALEXANDER, *Laws of Corporations and others Business Enterprises*, 15 f., 145, 344 ff.

⁽⁴⁵⁾ The judicial standards of this “veil-piercing jurisprudence” consist usually either of some general open-texture private law principles (e.g., good faith, fairness, justice) or of specific set of cases originally designed to cope with the deviative effects of the exercise of control by individual dominant shareholders or directors (e.g. undercapitalization, commingling of assets, abuse, domination: cf. for *Germany*, WIEDEMANN, *Gesellschaftsrecht*, 224 ff.; for *Spain*, BOLDÓ RODA, *Levantamiento del Velo y Persona Jurídica en Derecho Privado Español*, 314 ff.; for the *USA*, FABRITIUS, *Parent and Subsidiary Corporations Under U.S. Law: a Functional Analysis of Disregard Criteria*). The extension of these disregards categories to corporate groups proved, however, to be quite misleading. Here, the reality of control constitutes an institutional feature of the structure of the polycorporate enterprise in itself rather than a mere instrument of fraud or abuse: phenomena such as commingling of assets and the like are actually to be regarded as a normal outcome of the particular way of functioning of groups as an “organized market” rather than the exceptional result of the deviant behaviour of corporate robber barons.

⁽⁴⁶⁾ *Limited Liability and the Corporation*, 89.

⁽⁴⁷⁾ See BOLDÓ RODA, Carmen, *Levantamiento del Velo y Persona Jurídica en Derecho Privado Español*, Aranzadi: Pamplona, 1996. For a comparative undertakings on the topic, see COHN / SIMITIS, *Lifting the Veil in the Company Laws of the European Continent*, 189 ff.

2.2. The Liability of Directors

In such a context, being liability of the parent corporation on itself a rather exceptional one, no wonder that the liability of its directors is very unlikely to be asserted at all, except for the most egregious cases.

One of the possible lines of development would be to apply the general standards for the exercise of the management powers of directors of single corporations — e.g., “ordentlichen und gewissenhaften Geschäftsleiter” (§§ 76 and 93 AktG), “fiduciary duties” (sec. 309 of “Companies Act 1985”), “deber de diligencia y lealdad” (art. 127 LSA), and the like — to the entire group organization, rendering then directors liable for an *orderly and diligent group management* as a whole (“ordnungsmäßige Konzernleitung”), that is to say, parent directors would be bound to apply the same managerial diligence with regard both of the corporate headquarters and the affiliate corporations⁽⁴⁸⁾. However, this sort of transplanting into poly-corporate enterprises of normative standards of management created to single-corporate enterprises is rather doubtful, given its reliance upon open-ended and rather ambivalent notions such as “autonomous subsidiary interest”, “group interest”, “diligent manager of an independent company” or “orderly and sound group management”⁽⁴⁹⁾. A variant of this trend was set by the so-called “*Rozemblum doctrine*”, developed by French jurisprudence, according to which the directors of the parent corporation may induce subsidiaries to enter into disadvantageous transactions if the group has a sound structure (“politique de groupe cohérente”) and the damages inflicted upon the subsidiary are justified by the interest of the group (“équilibre entre avantages et inconvénients au sein du groupe”)⁽⁵⁰⁾.

Curiously, the most effective and driving forces of change in this topic are coming from the outside of Corporation Law. A major example is given by *Insolvency Law*, where several statutory provisions imposing personal liability on individual managers are also being applied to directors of parent corporations in case of subsidiary bankruptcy — e.g., the con-

⁽⁴⁸⁾ See FORUM EUROPAEUM KONZERNRECHT, *Konzernrecht für Europa*, 672 ff.

⁽⁴⁹⁾ The scope of the entire intragroup liability system would then be ultimately dependent on the (unpredictable) evolution of the jurisprudential construction of a unsuitable borderline: even more difficult than to separate between “normal” and “exceptional” in a piercing veil context, would be to draw a clear borderline between “good” and “bad” group management!

⁽⁵⁰⁾ HANNOUN, *Le Droit et les Groupes de Sociétés*, 89 ff., 229 ff.

cepts of “wrongful trading” and “shadow director” under sec. 213 and 214 of English “Insolvency Act 1986”⁽⁵¹⁾, or the “action en complément de l’insuffisance du passif social” under art. L.624-3 of the French “Code de Commerce 2000”⁽⁵²⁾.

2.3. Critical Appraisal

Firmly anchored in the dogma of corporate autonomy, the major weakness of traditional orthodox “entity law” consists in the fact that it represents an *unprincipled* regulatory strategy to intragroup liability problems, in which results are largely casuistic in present cases and almost unpredictable in future cases. The fundamental reason for this is that the basic question underlying the “rule-exception” approach to the treatment of liability problems at parent-subsidiary relationships — that is, the question of where to place the decisive borderline between “normal” cases, in which the separateness of group constituent corporations will prevail, and “exceptional” cases, where the courts deemed justifiable the disregard of such separateness — still remains today without any consistent answer. Intragroup liability cases, where exceptionally courts have disregarded the corporate entity of affiliate corporations and stepped over the corporate autonomy principle, imputing the acts or debts of subsidiaries to the parent corporation, are being decided according to guidelines that defy any possibility of rational systematisation or predictability⁽⁵³⁾. No wonder that it is not rare to

(51) These sections provide, respectively, that where, in the course of winding up of a company, it appears that any business has been carried on with the intent to defraud creditors, knowingly parties to the transaction can be made personally and unlimitedly liable for the debts of the company; and that where in course of winding up of a company it appears that a director, either a legal or a “shadow director”, has engaged in “wrongful trading”, the court can declare that director personally and unlimitedly liable for the company debts. See FINCH, *Corporate Insolvency Law*, 510ff.

(52) According to this rule, whenever a company undergoes a reorganization or insolvency procedure (“redressement ou liquidation judiciaire”), both their “de jure” and “de facto” managers (“dirigeant de droit ou de fait”) may be held liable for the settlement of all or part of its unpaid debts (GUYON, Yves, *Droit des Affaires*, II, 423 ff.)

(53) The entire judicial reasoning is usually shrouded in a ocean of metaphors which afford no possible understanding of the substantial considerations and the policies underlying the courts’ decisions nor do they help to predict when the courts will or will not pierce the corporate entity veil (cf. BLUMBERG, *The Law of Corporate Groups*, I, 6 ff.). Different metaphors, such as “mere instrumentality” or “alter ego” in the USA, “agent” or “sham” in the UK,

find a number of cases, virtually identical on their facts, in which the courts have reached completely contrary results. As suggestively BLUMBERG put it, “this is a jurisprudence of epithet and metaphor” (54).

Moreover, the formalism of this approach is also *inconsistent with the implementation of the legal policies* underlying the particular legal branches connected with the concrete liability issue at stake. As a matter of fact, the undifferentiated character of the regulatory standards of entity law often prevents that particular objectives pursued in the legal field where the liability issue arose or the specific statute or legal provision applicable in the concrete case at hand may be effectively: for instance, in tort law (the principle of allocation of enterprise risks and cost as a guidance and deterrence mechanism of economic behaviour, the principle effective remedy of tort victims), in contractual law (the principle of implementation of the expectations of the parties and enforcement of their bargain), in bankruptcy law (the principle of equal and fair treatment of creditors in the distribution of bankrupt estate, namely of equitable subordination), in tax law (the principle of irrelevance of the enterprise’s legal form so as to protect the revenue interest of state), and so on (55).

Last but not the least, the entity approach is likely to be the source of important *economic inefficiency* with regard to the management and organisation of polycorporate enterprises themselves. While the limited liability rule is often praised as supporting higher economic and social efficiency regarding all corporate actors involved (shareholders, managers, creditors), its automatic extension to the field of polycorporate groups seriously increases the risk of moral hazard which generates a well-know inefficient allocation of business risks (56) and inevitably jeopardise the

“société de façade” in France or “socio tiranno” in Italy, are just a few of the most celebrated national manifestations of a sole methodological strategy made out of mere conclusory terms, which, in a greater or lesser degree, simply restate the problem rather than solving it.

(54) BLUMBERG P., *The Law of Corporate Groups*, I, 8. See, apparently in the same sense, ROJO, that qualifies this jurisprudence as a sort of “*magical formula*”, intended to achieve “accurated or inaccurated needs of material justice” (original in Spanish) (*Los Grupos de Sociedades en el Derecho Español*, 398).

(55) See BLUMBERG, *The Law of Corporate Groups*, III, 107 ff.; BLUMBERG, *The Increasing Recognition of Enterprise Principles in Determining Parent and Subsidiary Corporation Liabilities*, 299.

(56) EASTERBROOK / FISCHER put it very plain: “If limited liability is absolute, a parent can form a subsidiary with minimal capitalization for the purposes of engaging in risky activities. If things go well, the parent captures the benefits. If things go poorly, the

interests of both creditors (particularly involuntary creditors) ⁽⁵⁷⁾ and minority shareholders of group constituent corporations ⁽⁵⁸⁾.

3. The Enterprise Approach

The so-called “*enterprise approach*” pleads for a new and revolutionary regulatory strategy on intragroup liability matters, and has found its

subsidiary declares bankruptcy, and the parent creates another with the same managers to engage in the same activities. This asymmetry between benefits and costs, if limited liability is absolute, would create incentives to engage in a socially excessive amount of risk activities” (*Limited Liability and the Corporation*, 111); see also WESTERMANN: “Besides, the possibility of liability segmentation entails growing risks concerning environment damages, which are likely to easily overcome the equity capital of single subsidiaries. From this perspective, one should ask whether grouping should not be treated as an inadmissible motivation for the artificial use of limited liability” (original in German) (*Umwelthaftung im Konzern*, 245). In fact, at a time when business firms are facing potential sources of massive tort liability that can exceed the net worth of even large-scale enterprises, such rule is becoming a major device of evasion of statutory liability for groups by creating incentives for parent corporations to invest in overly risky activities whose costs are externalised to society as a whole without any adequate compensation. Thus, it has been asserted by several studies that enterprises operating in increasing industrial sectors — such as hazardous-waste, oil-transport, chemical, nuclear, aeronautics, biotechnology industry — usually expand through an artificial desegregation of its unitary economic activity into a network of small-sized incorporated tiers whose assets are manifestly insufficient to compensate the magnitude of business risks, in order to reduce the enterprise overall liability exposure. According to RINGLEB / WIGGINS, over the last twenty-five years, a significant proportion of small corporations entering hazardous industries in the USA were motivated primarily by the aim of evading consumer, labour, and environmental liability exposure (*Liability and Large Scale, Long-Term Hazards*, 574 ff.).

⁽⁵⁷⁾ Involuntary creditors of subsidiary corporations (such as tort victims, consumers, employees) are completely unable to contract around liability, thereby preparing adequate adjustments to risk-shifting (“Risikoprämie”): unlike voluntary creditors, they have no choice neither in entering a credit relationship with the corporate debtor nor in negotiating of the terms of that relationship. See HANSMANN / KRAAKMAN: “Limited liability permits the firm’s owners to determine unilaterally how much of their property will be exposed to potential tort claims” (*Toward Unlimited Shareholder Liability for Corporate Torts*, 1920); KÜBLER: “They are the victims of a unilateral risk-shifting, from which «negative externalities» and thereby undesirable allocative effects stem” (original in German) (*Haftungstrennung und Gläubigerschutz im Recht der Kapitalgesellschaften*, 407).

⁽⁵⁸⁾ The protection of minority shareholders is a major legal policy guideline of existing company laws: see, in *Civil Law*, SCHMIDT, *Les Droits des Minorités dans les Sociétés Anonymes*; SCHMIDT, *Gesellschaftsrecht*, 382 ff.; WIEDEMANN, *Gesellschaftsrecht*, 404 ff.; in *Common Law* (although less clearly), cf. GOWER, *Principles of Modern Company Law* (5th ed.), 593 ff.

most expressive recognition in several proposals initiated by EU law during the 70s in the context of its attempts on the harmonisation and co-ordination of company laws of European member states (namely, the proposal of a 9th directive on groups of companies (⁵⁹)).

3.1. The Liability of the Parent Corporation

This strategy pleads that intragroup liability problems should be decided according to the fundamental principle that *the parent corporation shall be liable for all the unpaid debts and acts of its subsidiaries for the reason that the former controls the latter, forming thereby a unitary economic enterprise*. While not yet having become positive law (⁶⁰), this is an interesting approach since it symbolises in a world-wide context the most far-reaching statutory undertaking against the prevailing traditional “entity law approach”. By placing itself in the antipodes of the classical view, which intended to solve intragroup liability cases on the basis of a rigid application of a rule of limited liability, this new solution claims for an automatic application of the opposite rule — the *unlimited liability of the parent corporation*.

3.2. Critical Appraisal

The major weakness of this new approach consists in the *uncertainty*, *automatism* and *rigidity* of the solutions worked out for intragroup liability cases. First of all, one should bear on mind here that the vagueness of the central concept of “group of companies” is likely to create an uncertain legal environment for the operation of polycorporate enterprises: this is particularly serious for parent corporations, exposing them to a permanent threat of unexpected liability disputes potentially hazardous for the entire group’s financial and economic stability whose fate would ultimately depend on the idiosyncrasies of jurisprudential construction (⁶¹). Secondly,

(⁵⁹) *Proposal for a Ninth Directive Based on article 54, 3 (g) of the EEC Treaty on Links between Undertakings and, in particular, on Groups of Companies* (EEC Doc. III-1639/84-E). Similar approaches were adopted by the French “Proposal of a Law on Groups of Companies” of 1978 (commonly known as “*Proposition Cousté*”) and by the Spanish “Preliminary Draft of a Reform of the Law of Corporations” of 1979.

(⁶⁰) See LUTTER, *Stand und Entwicklung des Konzernrechts in Europa*, 362.

(⁶¹) For criticism of this statutory omission, GEBLER, *Das Konzernrecht der S.E.*, 310 f.; GOERDELER, *Überlegungen zum europäischen Konzernrecht*, 399.

as a result of the cascade of legal presumptions which support the group legal concept, in the overwhelming majority of the cases it should be enough for subsidiary creditors to prove the existence of the sole legal or factual instrument from which stems the possibility of the parent exercising a dominant influence over the subsidiary, in order to set in motion a system of unlimited liability for the former ⁽⁶²⁾. Thirdly, by imposing indiscriminately a uniform solution to all types of corporate groups, it fails to provide a flexible and differentiated regime able to accommodate the diversity of organisational and governance structures: as a matter of fact, this approach seems rooted in a sort of “pathological vision of the group enterprise” (GIRGADO PERANDONES) ⁽⁶³⁾. This rigidity is particular serious for polycorporate groups with a highly decentralised governance structure, where unified management is, by definition, exercised at arm’s length by the parent corporation and where then most of the cases of affiliate default are likely to be imputed in first place to subsidiary’s own management. But the same would hold true also for the case of those centralised groups where, in spite of the parent’s tight control over the subsidiary affairs, the particular managerial decision-making process from which the concrete liabilities complained of have been emerged from purely fortuitous and

⁽⁶²⁾ This means that imposition of liability on parent corporations for subsidiary debts would follow almost automatically from their mere formal status of “parent”: not distinguishing between mere potential control and actual control, nor between “good” control and “bad” control, the system would be holding parent corporations inescapably liable for all the debts of its subsidiaries, including those outwith its actual control, those without any causal relation with it, or those stemming from a control which has been exercised in the best interests of the subsidiary itself. See GOERDELER: “(The European group law) starts from an mandatory regime: whenever a group is deemed to exist, the parent company is directly submitted to the application of protective provisions (...). The decisive difference between such general group regulation and the German one rests in the automatic application of the protection of shareholder and creditors by the mere filling of the group legal notion” (original in German) (*Überlegungen zum europäischen Konzernrecht*, 398); HOFFSTETTER: “Thanks to the double presumption of group existence stemming from equity majority, the entire group reality is reduced prima facie to a sole level” (original in German) (*Haftung Multinationaler Konzerne*, 158); SCHILLING: “Due to the chain of presumptions — from majority shareholding to dependence, from dependence to group — than possession of more than 50 per cent. of the equity capital may almost lead to the heavy consequences of outsiders ‘compensation and debts’ liability” (original in German) (*Bemerkungen zum Europäischen Konzernrecht*, 421).

⁽⁶³⁾ GIRGADO PERANDONES, Pablo, *La Responsabilidad de la Sociedad Matriz y de los Administradores en una Empresa de Grupo*, 29 (original is Spanish).

unpredictable circumstances, such as, for instance, natural catastrophes, insolvency of important subsidiary debtors, abrupt modification of market ⁽⁶⁴⁾ or legal environment ⁽⁶⁵⁾.

On the other hand, this approach also entails important *economic shortcomings*. By exposing parent corporations to potential liability for the default risk of each subsidiary and thus to a permanent threat of a group insolvency, such a system is likely to force polycorporate networks to adopt inefficient hierarchically and centralised-oriented organisational structures as to avoid risk exposure ⁽⁶⁶⁾. Moreover, it is also likely to overshoot from the viewpoint of the protection of shareholders and creditors of affiliate corporations. Operating virtually as a sort of liability insurance against subsidiary default risk, it also provides minority shareholders with a sort of windfall for which they have not paid. And it gives a extra-protection against the default risk of the corporate debtor originating from purely fortuitous market or casual circumstances from which creditors of independent corporations under similar circumstances do not benefit at all: as Cándido PAZ-ARES put it, “why one should provide cre-

⁽⁶⁴⁾ E.g. entrance of new aggressive competitors in the same market area taking over a significant market share, causing drastic losses to the subsidiary or even leading to its bankruptcy.

⁽⁶⁵⁾ E.g. new developments in product or environment liability law which lead to costly readaptations of production programs or even to the official closure of the subsidiary firm.

⁽⁶⁶⁾ HOMMELHOFF put it very clearly (though in reference to the liability regime provided for by the new Draft of 9th Directive of 1984): “With this joint liability solution, each debt or risk incurred by the subsidiary is automatically, instantaneously and totally transferred to the level of the parent corporation (...). Therefore, the directive proposal forces the parent’s management to exert an uninterrupted and strict control over the subsidiaries affairs” (original in German) (*Zum revidierten Vorschlag einer EG-Konzernrechtlinie*, 125 ff., 142). Also before DABIN: “By pretending to place all groups of companies at the same level, the proposal ignores the economic reality and imposes such heavy constraints to all groups that it risks to affect the usefulness of the European Company itself as an instrument of the international commerce” (original in French) (*Systèmes Rigides du Type Konzernrecht*, 187, quoting the position of the International Commerce Chamber); GRAFFENRIED: “This strict regulation leads to a reduction of the organisational variety, burden the parent company in an inadmissible way and displays therefore undesirable concentration effects” (original in German) (*Über die Notwendigkeit einer Konzerngesetzgebung*, 167); KEUTGEN: “These type of charges (joint liability) shall often force the parent company to introduce a strong integration between group subsidiaries and to renounce to any decentralization, in spite of all the inherent economic advantages” (original in French) (*Le Droit des Groupes de Sociétés dans la CEE*, 214).

ditors of an affiliated corporation with a better treatment than creditors of a normal corporation?" (67)

4. The Dualist Approach

Somewhere in between these two radical and opposite strategies, a third intermediate regulatory strategy may be here referred to — the so-called “*dualist approach*”. This approach can only be properly understood in the global context of a specific and comprehensive law on affiliated corporations: the landmark case is Germany (1965), followed closely by some other national legal orders, such as Brazil (1976) (68) and Portugal (1986) (69), and, more recently, by Hungary (1988), Czech Republic (1991), Croatia (1993), Slovenia (1993), and Russia (1995).

4.1. The Liability of the Parent Corporation

The German law on affiliated companies and groups of companies (“Konzernrecht”), enacted by the Stock Corporation Law of 1965, develops essentially along a two-level structure, regulating group reality on the basis of a fundamental distinction between *two types of groups* (70).

(67) PAZ-ARES, Cándido, *Uniones de Empresas y Grupos de Sociedades*, 1344. Furthermore, it creates a virtual discrimination between creditors of sound and unsound subsidiaries: the former might well be unduly subsidising the later since, under an automatic rule of group liability, creditors who dealt with subsidiaries with adequate assets to pay its own debts could find that creditors of insolvent subsidiaries possess a potential claim on the same assets just because the subsidiary have been dragged into an eventual group insolvency.

(68) Cf. “Lei das Sociedades Anonimas”, enacted by the Law n.º 6404, of 15-12-1976, Chapter XX-XXII, arts. 243.º-270.º On Brazilian law, see COMPARATO, *Les Groupes de Sociétés dans la Nouvelle Loi Brésilienne des Sociétés par Actions*, 845 ff.; EMBID IRUJO, *Los Grupos de Sociedades en la Nueva Ley Brasileña de Sociedades Anonimas*, 461 ff.

(69) Cf. “Código das Sociedades Comerciais”, enacted by DL n.º 262/86, of 2-9-1986, Title VI, arts. 481.º-508.º On the Portuguese law, see ANTUNES, *The Law of Affiliated Companies in Portugal*, 355 ff.; LUTTER / OVERRATH, *Das portugiesische Konzernrecht von 1986*, 394 ff.

(70) On the regulation of groups of companies provided for by the Stock Corporation Law of 6-9-1965 (“Aktengesetz”), see for a general introduction GEBLER / HEFERMEHL / ECKARDT / KROPFF, *Kommentar zum Aktengesetz* (1973 and seq.), Bd. 1, 178-291, Lief. 6 (with commentaries of Gebler and Kropff); Zöllner (ed.), *Kölner Kommentar zum Aktengesetz* (1986-87), Bd. 1, 141-285, Bd. 6, 1-577 (with commentaries of H.J. Kop-

On the one hand, there are the so-called “*legal groups*” or “contractual groups” (“Vertragskonzerne”), where parent’s control has been embodied “*de iure*” in a special organisational contract, the contract of domination (“Beherrschungsvertrag”), following which the law has expressly recognised to parent corporations a broad legal power of control over its subsidiaries in open deviation from some of the classical canons of corporation law, and consequently imposed on the former a duty to cover all the annual losses or even a joint liability for the settlement of debts of the latter (§§ 291 ff. AktG). On the other hand, there are the so-called “*factual groups*” (“faktische Konzerne”), where the parent’s control is exercised as a mere “*de facto*” power, following which parent corporations found themselves bound basically to the traditional canons of corporation law, being permitted to use its controlling influence only in the best interests of the subsidiary, but being as well only obliged to a duty of compensation for single established detriments that have emerged from the use of such influence (§§ 311 ff. AktG) ⁽⁷¹⁾.

Therefore, intragroup liability solutions will follow automatically from the accommodation of group reality within one of these two pre-established types of groups: either a *system of global compensation in legal groups* (where the parent is bound to assume all the annual losses of its subsidiary), or a *system of mere punctual compensation in factual groups* (where the parent has only to compensate concretely established patrimonial prejudice caused to the subsidiary) ⁽⁷²⁾.

pensteiner); HOFFMAN-BECKING (ed.), *Münchener Handbuch des Gesellschaftsrecht*, Bd. 4 — *Aktiengesellschaft* (1988), 705-898 (by Gerd Krieger); EMMERICH / SONNENSCHNEIN, *Konzernrecht* (1992). For a global overview of the bibliography on German group law, see KIRCHNER, *Bibliographie zum Unternehmens- und Gesellschaftsrecht 1950 bis 1985*, 482-530.

⁽⁷¹⁾ For a general overview, see *ex multi* EMMERICH / SONNENSCHNEIN, *Konzernrecht*, 26 ff.

⁽⁷²⁾ While these rules representing the very core of the German intragroup liability system, one should be aware of the existence of other residual and functional equivalents, such as the jurisprudential “*piercing the corporate veil*” (cf. the *Herrstadt* case: BGH, “Neue Juristische Wochen” 1979, 1823 ff., 1828) and the *Sonnenring* case: BGHZ 81, 311 ff., 317); LUTTER, *Die zivilrechtliche Haftung in der Unternehmensgruppe*, 244 ff., 247 ff.; SCHMIDT, *Zum Haftungsdurchgriff wegen Sphärenvermischung und zur Haftungsverfassung im GmbH-Konzern*, 2074 ff.), the existence of *private-made arrangements on parent liability* (e.g., “Patronatserklärungen”), and, above all, an important body of non-codified *judge-made liability rules* applicable to private companies (cf. decisions in *ITT*, *Autokran*, *Tiefbau* and *Video* cases) and partnerships (cf. the *Gervais-Danone* case).

4.2. The Liability of Directors

The liability of directors of the parent company follows from this fundamental distinction.

Concerning legal groups, the directors of the parent company are given an almost *unrestricted power of direction* over the management of the affairs of the subsidiary corporation (e.g., 308 AktG, art. 493.º, n.º 1, CSC), including the right to issue instructions disadvantageous or contrary to the interests of the latter. This power of direction is not unlimited, directors might being held liable whenever they issue instructions in matters unrelated to the management of the subsidiary (e.g., invading the competences of its general meeting), instructions which are voided by subsidiary's articles of association or by other branches of the law (v. g., labour law, tax law), instructions on intragroup transfers of assets without an appropriate compensation, or, generally, instructions that being disadvantageous to the interests of the subsidiary do not serve the interest of the parent corporation or other group affiliate ⁽⁷³⁾. Particularly relevant is the establishing of a general standard of diligence regarding, not only the parent company, but also the *entire group*, to which are bound the directors of the parent company (e.g., art. 504.º CSC).

By contrast, in *de facto groups* the power of direction of the parent corporation over its subsidiary exists, at best, as a pure matter of fact and not as a legal power. That means that directors of the parent corporation are bound to comply with autonomous business interests of the subsidiary company (§ 76 AktG): any breach of such standard, namely by causing the latter to undertake a disadvantageous transaction, gives it a right of compensation (§ 311 AktG), for which fulfilment are held joint liable the directors of the parent company (§ 317 AktG). Of course, since the enforcement of this right depends on the initiative of subsidiary managers themselves, one cannot realistically expect that the system would work ⁽⁷⁴⁾.

⁽⁷³⁾ See on German law, SINA, *Grenzen des Konzernweisungsrechts nach § 308 AktG*, 1 ff.; on Portuguese law, ANTUNES, *The Law of Affiliated Companies in Portugal*, 382 f.

⁽⁷⁴⁾ Also KIRCHNER: "Since the members of the executive board of the dependent company aim to be reelected or even to be granted others posts within the group organization, it is not likely that subsidiary management would raise any objections to instructions given by the group management" (original in German) (*Ansätze zur ökonomischen Analyse des Konzernrechts*, 244).

4.3. Critical Appraisal

Almost forty years passed since its enactment, it has become quite clear that such a “dual approach” has not succeeded in reaching its most basic legal policy goals in the treatment of parent-subsidiary liability problems: as bluntly put it a leading German commentator, “the regulatory principle has fail” (Klaus HOPT) (75).

Looking closer at this approach, one clearly perceives that the entire legal system is based on a *clear-cut regulatory borderline* which approaches the entire group fauna on the basis of two formal legal-organisational models. On the one hand, the “de facto” groups, whose regulation aims legally to preserve the autonomy of the subsidiary corporation according to the canons of the classical corporation law (76) and organisationally to provide a model, at most, for very decentralised groups (77). On the other hand, the contractual groups whose regulation aims legally to legitimise the control of parent corporation in breach of such traditional canons (78) and

(75) *Le Droit des Groupes de Sociétés*, 381(original in French). See also IMMENGA: “It has become increasingly clear that the effects produced by the group at the level of its constituent companies is independent from its juridical shape. This means that outside control may also impose itself even when a contract of domination has not been celebrated” (original in German) (*Abhängige Unternehmen und Konzerne in der europäischen Gemeinschaftsrecht*, 48 ff., 58); SAUVAIN: “On may well ask whether the distinction is not purely formal, in the sense that from a *factual power* may issue attempts on the corporate patrimony as serious as those caused by a *legal power*. The existence of these two systems permits thus to the controlling company to enjoy a power similar to the one granted by the law without incurring in the liability legally attached to it (which constitutes an inadmissible privilege)” (original in French) (*Droit des Sociétés et Groupes de Sociétés*, 121).

(76) In the case where the parent corporation exercises a factual power of control over the affairs of its subsidiaries, group law has been essentially conceived of as a mechanism of maintenance and protection of the *corporate autonomy* of group affiliates, basically reaffirming the traditional canons of the law of the individual independent corporation (e.g., §§ 317, I = 117; §§ 317, II = 76, 93; §§ 318 = 93, 116 AktG). See also EMMERICH / SONNENSCHNEIN, *Konzernrecht*, 3th ed., 325 f.

(77) See HOMMELHOFF: “Only the factual group with very decentralised management structures is compatible with the global regulation of corporation law, particularly with the compensatory regime of §§ 311-318” (original in German) (*Die Konzernleitungspflicht*, 139); SCHMIDT: “§§ 311 ff. legalise the exercise of factual domination over a corporation only in case of very weak and non-centralised unified management” (original in German) (*Gesellschaftsrecht*, 804).

(78) See IMMENGA: “In German corporation law, the domination contract gives the basis for the legalisation of the group and for its juridical organisation” (original in Ger-

organisationally to provide the only admissible model for centralised groups ⁽⁷⁹⁾.

This is paramount to understand the failure of this regulatory strategy. Since the intragroup liability regimes have been rigidly and automatically attached to this narrow choice between two group models, and since, consequently, the treatment of liability issues of parent-subsidiary relationships follows automatically from the accommodation of the concrete group at stake within one of these two legal-organisational models, an inevitable gap between law and reality emerges whenever, as it often happens, *the living governance structures of groups in the concrete cases at hand diverge from that juridical model*. Thus, the liability regime of “contractual groups”, by automatically linking heavier parent’s liability (duty of compensation for subsidiary losses and joint direct liability for subsidiary debts) to the formal performance of mere formality (celebration of a contract of domination) ⁽⁸⁰⁾, unduly penalises parent corporations and often overshoots from the viewpoint of subsidiary creditors’ protection whenever the former’s legal power of control did not cause directly or indirectly the concrete liabilities of the latter ⁽⁸¹⁾. Inversely,

man) (*Abhängige Unternehmen und Konzerne in der europäischen Gemeinschaftsrecht*, 48 ff., 56).

⁽⁷⁹⁾ See STROHN: “The contractual groups is the most desirable group form particularly in cases of strong organisational intertwining” (original in German) (*Die Verfassung der AG im faktischen Konzern*, 20); ZÖLLNER qualifies also the existence of “centralised domination relationships” as the “typical case of the domination contract” (original in German) (*GmbH-Gesetz*, I, Rz. 29).

⁽⁸⁰⁾ The contract of domination usually constitutes the last link in a long chain of events leading to the full integration of a corporation within the group structure, which eventually can find a last upshot in a merger between the two corporations: therefore, as a rule, a contract of domination does not create “ab initio” for a corporation a power of control but merely legalises its exercise and effects; the subsidiary does not become dependent *because of the contract, but in spite of the contract*. This means that the decision about the “if” and, to a great extent, the “when” and “how” of the conclusion of a contract of domination depends ultimately on parent corporation itself. See SURA: “The connection of the protective legal provisions with the ending point instead with the departure point of the group formation turns up side down the sense of the effects stemming from corporate control” (original in German) (*Fremdeinfluß und Abhängigkeit im Aktienrecht*, 44).

⁽⁸¹⁾ This situation is likely to occur in the case of *highly decentralised contractual groups*, where the parent entrust local subsidiary managers with a high level of decision-making authority regarding the conduct of their own business affairs. But it may well happen in groups with centralised structures whenever the concrete liabilities in dis-

the liability regime of “factual groups”⁽⁸²⁾, by automatically linking smoother liability burdens to the mere formal absence of such a contract (given, of course, the existence of an intercorporate dependency relationship of other kind), is likely to give rise to the opposite problem, that is, to unjustifiably benefit parent corporations and to underprotect their subsidiaries⁽⁸³⁾.

IV – THE POLYCORPORATE ENIGMA

The polycorporate enterprise (“*empresa de grupo*”, “*Konzern*”, “*groupe de sociétés*”, “*gruppo di società*”) is conventionally defined *as a new form of enterprise organization where a plurality of separate legal entities, the subsidiary companies* (“*sociedades dominadas*”, “*Tochtergesellschaften*”, “*sociétés filiales*”, “*società controllate*”) *are submitted to a common uni-*

pute (registered in the balance sheet of the contractually dominated subsidiary) can be entirely imputed to a decision-making process entirely unrelated to the parent’s exercise of control (e.g. the subsidiary incurs annual net losses because of the political instability of the host country, such as lower productivity caused by political strikes).

⁽⁸²⁾ Considering that the great majority of existing corporate groups are still constituted as “*de facto*” groups, it is clear today that the dissuasive effect attempted by the original draftsman and the channelling of the factual power of control of parent corporations into “*de iure*” contractual schemes has failed (see BÄLZ, *Einheit und Vielheit im Konzern*, 306 ff.

⁽⁸³⁾ This problem is particularly striking since the failure of the intragroup liability system provided specifically for factual groups reaches virtually all types of non-contractual groups irrespective of their organisational patterns. Particularly revealing in this regard is the disclosure in some recent German jurisprudence of the so-called “*factual centralised groups*” (“*qualifizierte faktische Konzerne*”), an hybrid form of corporate group which destroyed the theoretical elegance of the rigid two-stage regulatory framework: see the fundamental decision of BGH in the landmark of case *Autokran* of 1985 (BGHZ 95, 330: “*Zeitschrift für Wirtschaftsrecht*” [1985], 1263), as well further decisions in the *Tiefbau* case (BGHZ 107, 7: “*Zeitschrift für Wirtschaftsrecht*” [1989], 440) and the *Video* case (BGHZ 115, 187: “*Zeitschrift für Wirtschaftsrecht*” [1991], 1354). On literature, see DEILMANN, *Die Entstehung des qualifizierten faktischen Konzerns*; DRUEY, *Zentralisierte und Dezentralisierte Konzern – ist die Differenzierung rechtlich wünschbar oder realisierbar?*, 89 ff.; HIRTE, *Der qualifizierte faktische Konzern*; HOFFMANN-BECKING, *Der qualifizierte faktische AG-Konzern*, 68 ff.; HOMMELHOFF / STIMPEL / ULMER, *Der qualifizierte faktische GmbH-Konzern*; LUTTER, *Der qualifizierte faktische Konzern*, 179 ff.; SCHEFFLER, *Der qualifizierte faktische Konzern*, 173 ff.; TIMM, *Grundfragen des “qualifizierten” faktischen Konzerns im Aktienrecht*, 977 ff.

tary economic strategy defined by parent corporation (“*sociedad matriz*”, “*Muttergesellschaft*”, “*société-mère*”, “*cappo-gruppo*”).

1. The Core of the Enigma

The central difficulty of the regulation of the polycorporate enterprise — which has become one of the most controversial topics of modern private law ⁽⁸⁴⁾ since it was discovered one century ago ⁽⁸⁵⁾ — has a great deal to do with *this enigmatic and paradoxical tension* between plurality (multiplicity of legal entities) and unity (unity of economic entity). As a matter of fact, while traditional corporate laws are designed to regulate individual incorporated enterprises and to preserve their autonomy, the polycorporate group represents a sort of “super-enterprise” without legal personality which existence is made possible thanks to the loss of such autonomy ⁽⁸⁶⁾.

⁽⁸⁴⁾ Cf. GALGANO: “The major difficulty concerning the legal treatment of the group of companies is to be founded in how the unity of the group is to articulate with the plurality of the constituent companies” (original in Italian) (*Qual è l’Oggetto della Società Holding*, 327); SCHILLING: “This (tension) is so old as the group itself, representing the very first question with which lawyers were confronted” (original in German) (*Entwicklungstendenzen im Konzernrecht*, 530); SCHMIDT: “A crucial problem of group law consists in knowing whether one multicorporate group enterprise should be seen as a unity or as a plurality” (original in German) (*Gesellschaftsrecht*, 405); GUYON: “The groups of companies are at the very heart of all the problems of company law” (*Examen Critique des Projets Européens en Matière de Groupes de Sociétés*, 155 (original in French)). This is also well illustrated by the more than one thousand articles have been published on this subject in the last 35 last years in Germany alone: see extensive bibliographic references in KIRCHNER, *Bibliographie zum Unternehmens- und Gesellschaftsrecht 1950 bis 1985*, 482-530; other general bibliographic sources can be found in RUEDIN, *Vers un Droit des Groupes de Sociétés*, 147 ff.; WIEDEMANN, *Die Unternehmensgruppe in Privatrecht*, 130 ff.; WYMEERSCH / KRUTHOF, *The Law of Groups of Companies. An International Bibliography*.

⁽⁸⁵⁾ The concept of group has been for the first time employed in the legal doctrine by the Austrian lawyer LANDEBERGER, in his work “Welche Maßnahmen empfehlen sich für die rechtliche Behandlung der Industrielle Kartelle”, in “Gutachen für die 26. DJT II” (1902), 294 ff., 301.

⁽⁸⁶⁾ Of course, this tension brought about a complete subversion of the classical model of the corporation at the level of each of the affiliated companies of multicorporate networks: while the law conceived each corporation as an autonomous business entity, subsidiaries may well be deprived of any patrimonial and organisational independence. On the crisis of this statutory model, see extensively ANTUNES, *Liability of Corporate Groups*, 52 ff.

In a very famous expression coined by Ludwig RAISER already half a century ago, “the polarity between unity of the total and the multiplicity of the parts constitutes the central problem” ⁽⁸⁷⁾ ⁽⁸⁸⁾.

2. An Enigma Solved? The Principles of Corporate Autonomy and Corporate Control

I submit that the enigmatic core of phenomenon of the polycorporate enterprise — the polarity between “unity and diversity” (“Einheit und Vielheit”) — is to be understood as the ultimate result of *an internal paradox of modern Corporation Law*, a legal branch which is based in two competing and contradictory principles — the principles of “corporate autonomy” and of “corporate control”.

The principles of corporate autonomy and corporate control are thus the two constituent principles of the legal and organizational structure of corporate groups.

2.1. The Legal Perspective

From a *legal* point of view, the typical *legal plurality* of multicorporate networks is nothing but the direct and necessary consequence of the existence of the rule of *corporate autonomy*: without the existence of this rule, enterprises wishing to expand their businesses would have to choose between only two rigid options — either the road of internal growth or of merger. Accordingly, the historical evolution from the singlecorporate to the polycorporate enterprise, that occurred throughout the 20th century, would not had ever been possible ⁽⁸⁹⁾. Likewise, the cha-

⁽⁸⁷⁾ RAISER, *Die Konzernbildung als Gegenstand rechts- und wirtschaftswissenschaftlicher Untersuchung*, 54.

⁽⁸⁸⁾ Yet the core of the problematic is still unresolved and the results achieved so far are rather unsatisfactory. See TIMM: “Despite numerous efforts during the last two decades on this topic, the basic problematic of group law has not yet been settled” (original in German) (*Minderheitenschutz und unternehmerische Entscheidungsfreiheit*, 60); WIEDEMANN: “In any case, for the time being, it seems not possible to present a ‘general theory’ of group law, which would be valid for all the private law areas and in which could be founded the common root for the law of the affiliate enterprise” (original in German) (*Die Unternehmensgruppe in Privatrecht*, 5).

⁽⁸⁹⁾ No wonder than before intercorporate control devices were admitted by the law, the merger (prevailing in Civil Law systems) and the trust (dominant at Common

racteristic *economic unity* of these multicorporate networks would be impossible without the existence of legal mechanisms of corporate control: without these devices, the creation of a stable unified management would be unthinkable, since, as Blumberg put it, “the vital link” would then be missing ⁽⁹⁰⁾.

2.2. The Organizational Perspective

From an *organizational* point of view, autonomy and control also represent the two basic patterns of allocation of decision-making power within corporate groups.

In one of the extremes of the organisational spectrum, autonomy reflects those situations where the subsidiary corporations enjoying of an high power of self-determination concerning the conduct of its own business affairs (*decentralised groups*). At the other extreme, control gives in the inverse situation in which the parent corporation intervenes deeply in the entire business activity and management of their subsidiaries (*centralised groups*). One should notice, however, that *autonomy or control are all of a piece*: full autonomy and full control represent just the polar situations of a spectrum for distribution of governance power in parent-subsidiary relationships, as centralisation and decentralisation represent the two limits of a scale of numerous alternative orga-

Law countries) have been the main legal instruments of enterprise concentration. Historical examples of the former are the mergers cases of Salt Union in 1888, of the US Steel Corporation in 1901 or of the American Tobacco Company in 1904; classical illustrations of the latter remain the Standard Oil Trust in 1882, the “Sugar Trust” and “Whisky Trust” in 1887, the National Lead Trust in 1887 and the American Cotton Oil Trust in 1889. See CURTIS, *The Trusts and the Economic Control. A Book of Materials*, 35 ff., 52 ff.; CHANDLER, *The Visible Hand — the Managerial Revolution in American Business*, 320 ff.

⁽⁹⁰⁾ “This is the vital link: without the existence of control, the corporations do not constitute a corporate group” (BLUMBERG, *The Law of Corporate Groups*, II, 14). In other words, had the law not provided for the existence of juridically-based mechanisms of intercorporate control, it is most probable that the history of enterprise organisation in the twentieth century would have been very different and that multicorporate groups would have never impose themselves as the major form of enterprise organisation. At best, one could imagine informal and rather unstable vehicles of intercorporate control being used to construct the ties of such networks and sustain their global co-ordination, as happened, for instance, with the former Japanese “zaibatsu”, largely based on a community of interest and a tradition of co-operation (see TINDALL, *Multinational Enterprises*, 36 ff.).

nisational structures for polycorporate enterprises ⁽⁹¹⁾. Reality is being therefore always situated somewhere in between ⁽⁹²⁾. And there lies precisely the specificity of the polycorporate enterprise: an hybrid form of enterprise organisation where a unitary business is conducted through extremely flexible governance structures, where a chameleonic-like, opportunistic blend of the autonomy of parts and the control of the whole is being constantly processed.

2.3. The Group as an Hybrid Enterprise Form

The polycorporate enterprise appears then as sort of *hybrid enterprise form* whose possibility and specificity results precisely from the creative and dialectical interplay of these two central and contradictory features of modern Corporation Law. It can be considered neither as simply the result of the dogma of corporate autonomy nor as the product of the competing device of corporate control, being instead the outcome of the paradoxical combination between them.

From this perspective, the traditional enigmatic core of the group, which attracted an entire generation of scholars, *looks rather plain*: the paradoxical tension between the juridical autonomy of their parts and the economic unity of the whole is nothing but the ultimate result of the paradoxical situation of a branch of law that at the same times promotes the autonomy of the corporation and permits the control of the same corporation, with the consequent virtual destruction of that autonomy.

⁽⁹¹⁾ See WALLACE: "It is this attempt to obtain this delicate balance between autonomy and control which has spawned the wide range of legal and organizational forms (of multinational groups)" (*Legal Control of the Multinational Enterprise*, 17).

⁽⁹²⁾ See LANGENEGGER: "These two organisational forms never emerge in their absolute shape, but in a mixed way. The quest "centralisation or decentralisation" is besides the point, since the question is always one of knowing in which proportion these organisational parameters are combined" (original in German) (*Konzernunternehmenspolitik – Grundlagen, Grundfragen und Zielsetzung*, 48); OECD: "Although this topic is frequently discussed in terms of centralised/decentralised decision-making, it is clear that the polar situations of total centralization and full autonomy do not exist" (*Structure and Organization of Multinational Enterprises*, 10); SLONGO: "The basic organizational principles of Centralisation and Decentralisation appear (almost) always mixed in the group reality" (original in German) (*Der Begriff der einheitlichen Leitung als Bestandteil des Konzernbegriffs*, 100).

3. The Paradox of Modern Corporation Law

This hybrid nature of polycorporate enterprises call our attention to what might be considered an unexpected and polemical proposition: *Corporation Law is a branch of law based upon a paradox.*

As a matter of fact, Corporation Law was born historically and is still today, by and large, *the law of the autonomous corporation.* How odd and surprising this might sound to company lawyers of today, control of a corporation by another corporation was unanimously prohibited by the founding fathers of Corporation Law, both in statutes⁽⁹³⁾, courts⁽⁹⁴⁾ and doctrine⁽⁹⁵⁾. Control was then considered as being incompatible with the dogma of corporate autonomy (KLEIN, 1914)⁽⁹⁶⁾, therefore refused as an abnormal situation (KEMPIM, 1883)⁽⁹⁷⁾ or even as an irrelevant phenomenon (MENZEL, 1911)⁽⁹⁸⁾. This historical pedigree is decisive to

⁽⁹³⁾ The case of USA law is paradigmatic. Although the rule of limited liability was enacted as a general default rule of corporation law in 1830 and the self-incorporation system was established in most federal states long after 1855, the process leading to the admitting intercorporate stock ownership — that is, to authorize that a corporation owned the stock capital of another corporation — only began in 1888, with the adoption by the State of New Jersey, for the very first time, of the famous “holding company clause” (FREEDLAND, Martin, *History of the Holding Company Legislation in New York State: Some Doubts as to the “New Jersey First” Tradition*, 369 ff.).

⁽⁹⁴⁾ The former jurisprudence of American courts, through an extensive use of the “ultra vires” doctrine outlawing intercorporate ownership, is a good example of that train of thought: see *Central RR v. Collins*, 40 Ga. 582 (1869); *Hazelhurst v. Savannah, G. & NARR*, 43 Ga. 13 (1871); *First National Bank v. National Exchange Bank*, 92 U.S. 122, 128 (1875); *Franklin Co. v. Lewiston Inst. for Sav.*, 68 Me. 43, 46 (1877); for the German courts, cf. the famous decisions of the Reichsgericht in the “rumänischen Eisenbahn” case of 1881 (RGZ 3, 123) and the “Petroleum” case of 1913 (RGZ 82, 308).

⁽⁹⁵⁾ TELLKAMPF argued that the majority of the German corporate scholars were against the admission of intercorporate stockownership (*Über die neuere Entwicklung des Bankwesens in Deutschland*, 71 ff.). Even after the introduction of express legal consecrations of intercorporate stock ownership, some national doctrines and courts remained sceptical of the legitimacy and coherence of this admission: this was namely the case of Italy (e.g., *Saffra/Bonfante, Società in Nome Colectivo fra Società Anonime?*, 609 ff.; decisions of Cass., 20 marzo 1930 [Foro Italiano, 1930, I, 562], Cass., 27 aprile 1936 [Foro Italiano, 1936, I, 992]).

⁽⁹⁶⁾ KLEIN, *Die wirtschaftlichen und sozialen Grundlagen des Rechts der Erwerbsgesellschaft*, 67.

⁽⁹⁷⁾ KEMPIM is particularly suggestive: “it is obviously an anomaly that one corporation controls another corporation” (*Die amerikanischen Trusts*, 341).

⁽⁹⁸⁾ MENZEL, *Die wirtschaftlichen Kartelle und die Rechtsordnung*, 23 ff., 31.

understand this legal branch nowadays, since, in the most part of countries, such a “received legal model of corporation” ⁽⁹⁹⁾ (“*Idealtypus der Aktiengesellschaft*” ⁽¹⁰⁰⁾, “*société anonyme typique*” ⁽¹⁰¹⁾) is still the prevailing one: and by that I mean that the regulation of the formation, governance, financing, functioning and dissolution of the corporation is still carried out largely according to the fundamental archetype of the corporate autonomy ⁽¹⁰²⁾.

However, a true paradox was about to take place. Only some decades after its official birth, under the pressure of business interests or just by chance, Corporation Law all over the world started to comply with practices and to introduce legal provisions aiming to permit corporations to control others corporations — soon becoming thus *a law aiming to built and ensure the control of corporations*: as a result, multiple legal mechanisms of intercorporate control were offered in the most part of legislations and admitted by courts (*v. g.*, intercorporate simple or cross-shareholdings, voting agreements, proxy rights, management control contracts, interlocking directorships, and so on) ⁽¹⁰³⁾. Gradually, the same legal branch that had so zealously worked out the model of the corporation as an autonomous, sovereign and closed entrepreneurial entity was responsible for the enactment of institutional and juridical devices that were likely to pierce that closure, to subvert that sovereignty and to destroy that autonomy.

Therefore, one might say that the system of modern Corporation Law is truly based upon an *odd, almost schizophrenic, self-contradiction*: the regulation of the corporation is being achieved through a branch of law that is based in conflicting regulatory models — the corporation as an autonomous and independent entity “versus” the corporation as an affiliated and

⁽⁹⁹⁾ EISENBERG, *The Structure of the Corporation*, 1.

⁽¹⁰⁰⁾ CAFLISCH, *Die Bedeutung und die Grenzen der rechtlichen Selbständigkeit der abhängigen Gesellschaft im Recht der Aktiengesellschaft*, 32.

⁽¹⁰¹⁾ SAUVAIN, *Droit des Sociétés et Groupes de Sociétés*, 53.

⁽¹⁰²⁾ See Cándido PAZ-ARES: “Company Law has been traditionally based upon the model of the independent company, with a self-determination power emanating from its own organs and pursuant a business interest on its own” (original in Spanish) (*Uniones de Empresas y Grupos de Sociedades*, 1336). Similarly SCHMIDT: “The nineteenth century inherited statutory model of company law is based on the ideal of the autonomous company: the will of each company is formed by itself internally” (original in German) (*Gesellschaftsrecht*, 400).

⁽¹⁰³⁾ See *supra* Part II, 3.2.

controlled entity — and that promotes competing types of enterprise organisation — singlecorporate enterprise “versus” polycorporate enterprise ⁽¹⁰⁴⁾.

4. Conclusion

One reaches then a surprising final conclusion.

Polycorporate enterprises are strange business creatures that were generated in the womb of the self-contradictions brought about in the course of the historical evolution of Corporation Law: the reasons that made them possible to exist are the very same reasons that explain the failure attempts and deadlocks to regulate them. The future shape of any successful regulation of this phenomenon — if not of the entire Corporation Law itself — is thus likely to only become possible whenever this legal branch would call in question and clarify its own paradoxical genealogy. And as long as this genealogy has not been object of independent consideration by literature, and this conflict has not been solved coherently by legislators, no relevant changes are unfortunately to be expected to occur.

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⁽¹⁰⁴⁾ This paradox has been often noticed by commentators, who have steadily denounced the existence of a serious “gap between law and reality” (see LUTTER, *Stand und Entwicklung des Konzernrechts in Europa*, 330; PAILLUSSEAU, *Les Fondements du Droit Moderne des Sociétés*, 3148; PAZ-ARES, Cándido, *Uniones de Empresas y Grupos de Sociedades*, 1336). One should stress, however, that the problem is not one of discrepancy between legal and living models of the corporation, but instead a truly *internal contradiction in the system of corporation law itself*. In other words, the dilemma does not relate, as it is commonly asserted, to a mere divorce between corporate practice and corporate law, but really to a deep-seated paradox at the very core of the existing regulatory framework of Corporation Law, a single legal branch obeying to contradictory legal policies and containing norms which lead to conflicting results.

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