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# The possible extension of vicarious liability to cover relations between holding companies and their subsidiaries: Is it plausible and desirable under South African Law?

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# The possible extension of vicarious liability to cover relations between holding companies and their subsidiaries: Is it plausible and desirable under South African Law?

# Abstract

Modern companies in South Africa and elsewhere have embraced the use of corporate group structures. One of the problems arising from such structures is who should bear responsibility towards delictual creditors for unsatisfied judgment debts against insolvent subsidiaries. In such situations, the claims of delictual creditors have often gone uncompensated.

Recent events involving large delictual claims worldwide in hazardous industries such as in mining have shown notable barriers to justice, particularly with regards to subsidiary companies' liability for the harm they cause to third parties. This has been particularly concerning, especially when these large delictual violations have human rights implications. One of the reasons these violations continue to lack adequate recourse is the uneven distribution of risks and liabilities between holding companies and their subsidiaries.

This research is primarily concerned with whether a holding company of an insolvent subsidiary should bear some responsibility towards the latter's uncompensated delict creditors. Traditional considerations of holding company liability of this nature have been mainly located within corporate law. Remedies such as the veil piecing and director's liability have been the primary mechanisms through which holding company liability has been implemented. This research seeks to explore further possibilities by questioning whether the rules of vicarious liability in South Africa ought to be developed to create liability between a parent company and its subsidiary.

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# 1. Introduction

Vicarious liability is a legal remedy that permits the law to impose strict liability on one person for the wrongs of another.[1] There are several theories that justify, to varying degrees, the underlying rationale of this remedy. These theories include the interest and profit theory, the solvency theory, and the risk or danger theory.[2] Vicarious liability is an exception to the general rule that one does not incur delictual liability for harm caused if one is not at fault.[3]

One of the requirements for imposing vicarious liability is the existence of a legally recognised relationship between the actual wrongdoer and the person who is vicariously liable. Four relationships have been recognised by the law as having the capacity to trigger the operation of vicarious liability. These relationships are the employer and employee relationship, the principal and agent relationship, the relationship between a motor vehicle owner and the driver of the vehicle and the state and the organs through which it acts.[4] This list is, however, not a closed one.[5] Potgieter has mooted a further category that should be recognised as having the capacity to trigger the operation of vicarious liability, namely, the relationship between a parent and a child.[6]

From all the above categories of vicarious liability, the most relevant and proximate category for this research is the employment relationship. Three requirements must be met in order to create vicarious liability in terms of the employment relationship. The first being the commission of a delict by an employee, the second being an employment relationship, and the last being that the delict must have been committed within the course and scope of employment.[7]

This research will not deal with all three requirements but will focus exclusively on the second requirement. This is the requirement that there should be an employment relationship between the parties in question. Several tests have been used by the courts to distinguish between an employment relationship and a non-employment one. These tests are: the control test, the organisational test, the dominant impression test and the multiple criterion test.[8] In foreign jurisdictions the akin to employment test has been used for a similar purpose.[9] What will then be argued is that what emerges from all the tests of employment is that the basis for when a relationship is considered as one of employment is the existence of control and economic or business integration between the parties in question.

The next question will pertain to whether aspects of control and economic integration can be used as the basis for testing whether the law would recognise the holding-subsidiary company relationship as

[1] J Neethling & JM Potgieter *Neethling-Potgieter-Visser Law of Delict* 7th Ed (2015) at 389.
[2] Ibid at 390.
[3] Ibid at 389.
[4] Ibid.
[5] J.M. Potgieter "Preliminary thoughts on whether vicarious liability should be extended to the parent-child relationship" (2011) 32 *Obiter* 189 at 202.
[6] Ibid at 203.
[7] J Neethling & JM Potgieter op cit note 1 at 390-396.
[8] S Wagener "The relationship(s) giving rise to vicarious liability in South African law" (2014) 131 *South African Law Journal* 178 at 180.
[9] *John Doe v Bennett* 2004 (1) SCR 436 (SCC) para 27.

one that attracts vicarious liability. In this exercise it is argued that these two central features of the employment relationship can be used to assess whether the holding-subsidiary company relationship is sufficiently similar to the employment relationship for us to conclude that holding companies can attract vicarious liability from their subsidiaries.

In company law, a holding-subsidiary company relationship is created whenever one company controls another company.[10] The various avenues from which this control can be created are elaborated in the Companies Act.[11] Some of the avenues of showing control include, where one company wholly owns another company or has the right to elect the directors that serve on its board of directors.[12] A core tenant of company law of all companies is that all companies enjoy separate legal personality.[13] One of the main consequences of legal personality is that the risks and liabilities of any company belong to it and not its shareholders or related companies.[14] This rule is also applicable to companies in groups and companies in a holding-subsidiary relationship.[15] This means that a holding company that owns shares or the entire subsidiary company cannot be held liable for the acts of such a subsidiary.[16] However, these principles are not without exception.[17] This research will also explore whether the rules of vicarious liability can operate as one of the exceptions to separate legal personality and limited liability.

This research will be written in the following format. Part 1 introduces the rules of vicarious liability and corporate law. It also lays out the approach used to test whether vicarious liability can be extended to the holding-subsidiary company relationship.

The research will start by introducing the tests for employment. It will argue that the employment relationship is the most important recognised relationship of vicarious liability and why it is central to the discussion of establishing the main features of vicarious liability. In terms of the tests of employment, this research also argues that features of control and economic integration are at the heart of the tests of employment. The importance of this part of the research is to show that control and economic integration, in its various forms, are the primary indicators of whether a relationship is one of employment. Further, control and economic integration are also the primary indicators of whether any relationship ought to attract the operation vicarious liability.

This research then tests whether control and economic integration can be used to determine whether the holding-subsidiary company relationship is sufficiently similar to the employment relationship for the purpose of vicarious liability. It is argued that in testing for control and economic integration, lessons from other areas of law should be utilised. Insights from South African corporate law, competition law as well as English tort law will be central in this exercise. Here, this research seeks to inquire into how other areas of law have established liability in the holding-subsidiary company

[10] FHI Cassim,M.F Cassim,R Cassim,R Jooste, J Shey and J Yeats *Contemporary Company Law* 2ed (2012) at 183.
[11] The Companies Act 71 of 2008 s1 read with s3.
[12] Ibid.
[13] FHI Cassim et al opcit note 10 at 28.
[14] *Airport Cold Storage (Pty) Ltd v Ebrahim* 2008 (2) SA 303 (C) para 17.
[15] *Ritz Hotel Ltd v Charles of Ritz Ltd* 1988 (3) SA 290 (A) at 303.
[16]Ibid.
[17] See, R Cassim "Piercing the veil under section 20(9) of the Companies Act 71 of 2008: A new direction" (2014) 26 *South African Mercantile Law Journal* 307 at 319 and R Rahman "Holding Company Liability for Subsidiary Company A Critical Analysis under UK Companies Act 2006" (2013) 13 *Journal of Humanities And Social Science* 90 at 95.

relationship and whether there are any useful lessons for a potential scheme of vicarious liability in the holding-subsidiary company relationship.

This research then argues that constitutional values and its interpreting case law should be infused into any potential extension of vicarious liability. This research also points out some of the important potential limitations of the use of the Constitution[18] in the current context. Part 4 will argue that the traditional theories that underpin the operation of vicarious liability can provide useful guidelines in any potential development of vicarious liability. Part 5 will conclude the entire research report.

For ease of reference, this research shall refer to this new relationship between a holding company and its subsidiary company for establishing vicarious liability as the "holdsub relationship" and "vicarious holdsub liability".

[18] The Constitution of the Republic of South Africa, 1996.

# 2. The tests for employment

Stephen Wagener argues that all the traditionally recognised categories of vicarious liability in South Africa, namely, employment, motorcar owner-driver and principal-agent, can be distilled into one relationship.[19] This he terms the "broadly construed employment relationship".[20] In terms of this argument, courts in South Africa do not primary impose vicarious liability based on relationship of service.[21] Rather, they impose liability whenever any relationship shows features of an employment relationship in terms of how they have come to understand this contractual relationship.[22] What this means is that all the traditional relationships capable of triggering vicarious liability should be taken as falling within the ambit of a broadly construed employment relationship.

The primary support for this argument is the *Messina Associated Carriers* case[23] where Scott JA stated that:

> "But even in the absence of an actual employer-employee relationship the law will permit the recovery of damages from one person for a delict committed by another where the relationship between them and the interest of the one in the conduct of the other is such as to render the situation analogous to that of an employee acting in the course and scope of his or her employment"[24]

The implication of this is that employment for vicarious liability should not be understood in terms of its ordinary meaning from labour law. Rather, employment in this sense encapsulates a bundle of tests, some related to ordinary understanding of employment and some that are not related.[25] Further, by implication the features and tests of the employment relationship are at the heart of what should constitute a relationship that can attract vicarious liability. At the very least it can be argued that the employment relationship is an important recognised relationship of vicarious liability for the purposes of understanding why a person who is not at fault can be liable for the wrongs of another.

Several tests have been used by the courts to test whether there is an employment relationship in question. In terms of the organisational test, a person is an employee of another if he is integrated into the business of another.[26] To determine whether one is indeed integrated into the organisation of another, courts consider a range of factors. These include, whether or not one works on a permanent basis or temporary basis in the organisation of another, whether ones tools of trade are your own or form part of the organisation of another person.[27] In addition courts also inquire into whether one is permitted to work on similar work for personal gain or you are bound to only avail your labour in the

[19] S Wagener op cit note 8 at 178.
[20] Ibid.
[21] Ibid at 198-199.
[22] Ibid.
[23] *Messina Associated Carriers v Kleinhaus* 2000 (3) All SA 285 (A).
[24] Ibid para 10.
[25] S Wagener op cit note 8 at 179,198,199.
[26] *Smit v Workmen's Compensation Commissioner* 1979 (1) SA 51 (A) at 161.
[27] *R v AMCA Services Ltd* 1959 (4) SA 207 (A) at 212.

business of another.[28] The organisational test has been criticised for being vague and unworkable.[29] It however, remains instructive for when a relationship can attract vicarious liability.

The dominant impression test has also often been used to test whether there is a relationship of employment.[30] This test is often used when a relationship has features of an employment relationship as well as features of another relationship.[31] According to this test when courts are faced with such situation they must make a value judgement to ascertain whether the relationship in question has features that are predominantly of employment or of another relationship.[32]

The most important test for our purpose is the control and supervision test.[33] This test is often explained in relation to the distinction between a relationship of employment and that between an independent contractor and his principal.[34] This distinction is important because while both a contractor and an employee act on the mandate of their principal or employer, only the delict of an employee gives rise to the operation of vicarious liability.[35] Understanding the distinction between an independent contractor and an employee, as well as how control plays a part in distinguishing between the two sheds light on how courts approach the employer-employee relationship for vicarious liability.

The different capacity under which a person receives his mandate for service is of crucial importance in determining whether he is a contactor or employee.[36] For an independent contractor, he works under a contract for a specified service and the object or main purpose of this relationship is the performance of a specified task or the production of a specific result, in part or in whole.[37] It is therefore the task that is the central aspect of the contract and the relationship between the contractor and the principal.[38]

Whereas for a contract of employment, it is a contract of service and the object of this relationship is to put the productive capacity of the employee at the disposal of the employer.[39] With employment the object of the relationship is therefore the services or labour of the employee. It is in the relationship of employment where one puts his labour and services at the disposal of his employer that is subject to control and supervision.[40] Consequently, the distinction between working on a specified task and putting your labour at the disposal of someone else is the crucial indicator of whether you are an employee or an independent contractor. Only an employee can be subject to the sort of control and supervision that is deemed as capable of triggering the operation of vicarious liability.[41] The right to control and supervise an employee is therefore a key feature that sets apart a

[28] Ibid.
[29] *Smit* opcit note 26.
[30] *Pam Goldings Properties (Pty) Ltd v Erasmus and* Others 2010 (31) ILJ 1460 (LC) at para 13.
[31] Ibid at 12.
[32] Ibid.
[33] *Colonial Mutual Life Assurance Society Ltd v Macdonald* 1931 A 412 (A) at 431-435.
[34] *Smit* supra note 26 at 153-159.
[35] Ibid.
[36] Ibid.
[37] Ibid.
[38] Ibid.
[39] Ibid.
[40] Ibid.
[41] *Colonial Mutual Life Assurance Society Ltd* supra note 33 at 435.

contractor and an employee.[42] In the *Smit* case the court stated that control involved the right of an employer to decide the type of work to be done by an employee, the manner he is required to carry it out, the means he is going to use, time and place of work and supervision implied the right of an employer to direct and inspect the work of the employee. [43] Even though control is the main feature of the employment relationship the courts have also indicated their preference for a more multiple criteria test.[44] The multiple criteria test considers all the tests, the control and supervision test, the dominant impression test and the organisational test.[45] This position was elaborated by the Appellate Division in the *Transnet* case.[46]

Another useful indicator that the courts have used to determine whether the relationship in issue shows features of employment is to consider whether the relationship is 'akin to employment'.[47] This term was first used in the *John Doe* case.[48] In *JGE*, the English Court of Appeal utilised this new category as the basis for holding a bishop vicariously liable for the delict of a priest.[49] In coming to that decision, the court laid out several key principles. In its decision, the court emphasised that the use of the word 'employment' in vicarious liability should not be conflated with the use of the word in other areas of law such as tax and labour law.[50] For the purposes of vicarious liability, the focus is only placed on the functions of employment and not its legal form.[51] This according to the court means several things. Firstly, that there is no need for a formal contract for this form of employment.[52] Secondly, if the relationship in question displays similar functions to that of the employment relationship, then it is a relationship of employment.[53]

The court then went on to outline the factors that should be considered to determine whether a relationship in question is sufficiently akin to employment for the purpose of vicarious liability. These factors are, whether the defendant controlled the wrongdoer and whether the task required an assessment of the extent to which the wrongdoer was accountable to the defendant.[54] The court also considered if the wrongdoer arranges his own work, uses his own assets, if he owns the business and if he is integrated into the organisation of another.[55]

An analysis of the approach of vicarious liability in South Africa and in English law shows several key features that are central to the discussion at hand. The main tests for employment and the akin to employment test show two central features. the existence of control and economic integration. The centrality of control is seen from the control and supervision test, which is the main test, used to assess when there is a relationship of employment.[56] The centrality of economic integration is seen

[42] Ibid.
[43] *Smit* supra note 26 at 153.
[44] *Midway Two Engineering & Construction Services BK v Transnet Bpk* 1998 (2) All SA 451 (A) at 22-23.
[45] Ibid.
[46] Ibid.
[47] *John Doe* supra note 9 at 27.
[48] Ibid.
[49] *JGE v The Diocese of Portsmouth* 2012 EWCA Civ 938 at 131.
[50] Ibid para 59.
[51] Ibid para 60.
[52] Ibid para 15.
[53] Ibid para 62.
[54] Ibid para 72.
[55] Ibid.
[56] *Smit* supra note 26 at 161.

from the akin to employment test and the organisational test. Both the organisational test and the akin to employment test focus on control and economic integration. In the sense that both tests inquire into how much of a central role one has in the business of another. Here they use indicators such as whether you arrange your own work or the work that you do is arranged by another.[57] Do you use your own tools or the tools of another?[58] Whether you are permitted to work on similar work for personal gain?[59] The organisational and akin to employment tests consequently show a strong focus on the how integrated one is into the business and economic orbit of another as an indicator of whether you are an employee. The dominant and multiple criterion tests can be said to have an auxiliary role supporting the control & supervision test, the organisational test, and akin to employment test.

What emerges from this entire analysis of the tests of employment is that at the core of what courts in South Africa and in English law understand as the basis of what triggers vicarious liability are two main things. First, there must be features of control and supervision. Second, you must inquire into whether the relationship in question has strong features of business and economic integration.

It is from the above basis that this research seeks out features of control and economic integration in other areas of law that have recognised liability between a holding company and its subsidiaries towards third parties. This analysis will focus on the potential implications of the approaches used in different areas of law and whether they can provide insight into how and if the vicarious holdsub liability can and should be developed.

[57] *JGE* supra note 49 at 70-75.
[58] *R* supra note 27.
[59] Ibid.

# 3. Considering the tests for company liability in other areas of law

## 3.1. Holding-subsidiary company liability in corporate law

One of the most important tools that have been used to create liability between holding-subsidiary company relationships in corporate law is termed the piercing of the corporate veil. This has traditionally been a common law remedy that was used to create liability between a corporate entity and its shareholders in circumstances where the corporate entity is being abused by its shareholders.[60] In South Africa the remedy of veil piercing now exits as a statutory remedy but largely guided by the same principles inherited from its common law use.[61] In the *Gore* case, the court extended the application of statutory veil piecing remedy to corporate groups.[62]The specifics of how the statutory veil piercing works extends the ambit of this paper, however the court made several findings that are useful to the discussion of holding-subsidiary company liability.

The application of the statutory veil piercing largely hinges on the phrase "constitutes an unconscionable abuse of the juristic personality of the company as a separate entity"[63] stated in the companies act.[64] Binns-Ward J in the *Gore* case sets out a few guidelines with regards to the words unconscionable abuse of juristic personality. He states that the remedy is not a drastic one and can be invoked "whenever the illegitimate use of the concept of juristic personality adversely affects a third party in a way that reasonably should not be countenanced".[65]

Binns-Ward J then goes on to state that the current statutory provision on the veil piercing broadens the traditional basis from which courts were prepared to disregard the corporate personality.[66] The ultimate test for when it is ideal to disregard the separate personality of the corporate entity rests on a policy-based decision that weighs up all the competing interests.[67]

Binns-Ward J then went on to set out the circumstances where it may be appropriate to ignore the corporate personality of the context of corporate groups. He opinions that it is appropriate where it

> is evident in cases in which the circumstances [indicate that] a corporate group is operating in such a manner as to make each individual entity indistinguishable, and therefore it is proper to pierce the corporate veil to treat the parent company as liable for the acts of the subsidiary.[68]

[60] R Cassim op cit note 17 at 319.
[61] Ibid.
[62] *Ex Parte: Gore NO and Others* 2013 (2) All SA 437 (WCC) para 37.
[63] Companies Act 71 of 2008 s 20(9).
[64] Ibid.
[65] *Ex Parte: Gore NO and Others* supra note 62 para 34.
[66]Ibid para 33.
[67]Ibid para 29.
[68]Ibid para 26.

In its decision that it decided that is was appropriate in the circumstances to pierce the corporate veil and hold the shareholders liable to creditors for the debts of the entire group. It further elaborated that the corporate group acted as an integrated single entity with one controlling mind.[69] The holding company and its subsidiaries mixed investor funds within the corporate group with little regard to the purpose of the funds.[70] The court describes the affairs of the group as dishonest and chaotically administered.[71]The court found that the way in which the entire group managed and owned by their main shareholders did not respect the separate legal identity of the separate companies that made up the entire group.[72]

Several insights can be drawn here for a court tasked with assessing the suitability of vicarious holdsub liability. First, the standard required to trigger the application of the statutory veil piercing for corporate groups is lower than that of the common law or other jurisdictions were this remedy is applied.[73] Likewise the standard of control required for vicarious holdsub liability should not be too high that it would be impossible to show. Neither should it be so low that a mere allegation can meet this threshold of control. What is rather required is flexible approach that focuses on whether the corporate group acts as a highly integrated entity with a single controlling mind.

In deciding whether the holding and subsidiary companies are integrated and controlled by one mind the court may consider whether there is a sharing of management and ownership within the holding-subsidiary company relationship,[74] and whether or not the movement of funds between the holding-subsidiary company relationship is at arm's length and respects the separate legal identities between both companies.[75] These two factors are among the indicators that can show the true nature of the control structures within the holding-subsidiary company relationship. Irregular and fraudulent movement of funds within the corporate group can also be an indicator that there is control.[76]

Courts in delict should not treat the remedy of vicarious liability in the holdsub relationship as exceptional or a measure of last resort. Rather they should treat it as a remedy that can be invoked "whenever the illegitimate use of the concept of juristic personality adversely affects a third party in a way that reasonably should not be countenanced".[77] What this scheme of vicarious holdsub liability should be suitable whenever there is strong evidence of abuse of the holding-subsidiary company relationship. In corporate law focus is on whether there is abuse of the juristic person. Features of control and economic integration are only used as part of the evidence that show abuse of the corporate person. In this sense before a court recognises vicarious holdsub liability, it should also look at whether the holding-subsidiary company relationship is being abused or used for an illegitimate purpose and not focus only on control and economic integration.

There is another important lesson to note. On one end, the approach taken in group veil piercing can provide lessons for the development of holdsub vicarious liability. But on the other hand, it may

[69] Ibid para 6.
[70] Ibid para 8.
[71] Ibid para 11.
[72] Ibid para 6.
[73] Ibid.
[74] Ibid.
[75] Ibid para 8.
[76]K Strasser "Piercing the Veil in Corporate Groups" (2005) 637 *Connecticut Law Review* 637 at 640.
[77] *Ex Parte: Gore NO and Others* supra note 62 para 13.

serve as a bar for the development of holdsub vicarious liability. In the sense that if corporate law has already developed mechanisms of rectifying the abuse of juristic persons why then should the law of delict be developed to rectify the same problem. The existence of a more appropriate remedy in corporate law may be a core barrier for the potential development of holdsub vicarious liability. It may be possible that what holdsub vicarious liability seeks to rectify can be remedied by the statutory veil piercing.

The last important implication for corporate law is on whether a scheme of vicarious holdsub liability undermines the principles of separate legal identity and limited liability. Morgan argues that vicarious liability is compatible with the principles of separate identity and limited liability in the holding-subsidiary company relationship.[78] He bases this position on the following logic – a natural person has separate legal identity and limited liability and is therefore not liable for the delict of others, however, this does not operate without exception.[79]The exception is the operation of vicarious liability where he may be liable for the actions of others.[80] In the same way that a natural person enjoys limited liability and separate legal identity and can be vicarious liability. So too should a juristic person or a group of related juristic persons be capable of attracting vicarious liability on the same basis as a natural person.[81] He further argues that this is not veil piercing but rather simply taking the legal fiction of a juristic person to its natural consequence and logical conclusion.[82] In the same way that a company can be liable for a natural person or vice versa, it should follow that vicarious liability ought to flow between two juristic persons.[83] For Morgan, this would align the rights and responsibilities of a juristic person closer to that of a natural person as intended by the cardinal principle of corporate law.[84]

The compatibility of separate legal identity with vicarious liability will likely be a key question in the inquiry of whether it is possible to extend it to the holding-subsidiary company relationship. On this intersection, Morgan's argument provides a good starting point in addressing the tension that may exist between the operation of vicarious liability and the core tenants of corporate law. Morgan's argument has one key limitation. Considerations around limited liability are not only concerned with aligning the rights and duties of juristic persons with those of natural ones. They are also concerned with the central function and role of limited liability in companies and within the broader economy.[85] The perception alone, of the potential erosion of limited liability in corporate groups may be a strong enough factor that will weigh against the acceptance of vicarious holdsub liability. It is on the economic considerations that Morgan's argument will likely fail.

Ultimately, a court tasked to develop vicarious holdsub liability can draw several lessons from corporate law. First, the use of veil piercing in corporate groups shows that the remedy is not exceptional and is appropriate whenever there is a finding of unconscionable abuse of the group

[78] P Morgan "Vicarious Liability for Group Companies: The Final Frontier of Vicarious Liability?" (2015) 31 *Journal of Professional Negligence* 276 at 297
[79] Ibid.
[80] Ibid.
[81] Ibid.
[82] Ibid.
[83] Ibid.
[84] Ibid.
[85] A Imanalin "Rethinking Limited Liability" (2011) 89 *Cambridge Student Law Review* 88 at 90.

personality. Second, features of control and integration only serve as part of the indicators of when that abuse is present. Third, a court may conclude that the existence of the veil piercing shows evidence of a more appropriate mechanism of rectifying the abuse of the corporate person in corporate law. Lastly, the potential implications of vicarious liability on separate legal and limited liability in corporate groups will be a central consideration on whether vicarious holdsub liability is suitable.

## 3.2. Holding-subsidiary company liability in competition law

In competition law, there is a concept called the single economic entity doctrine. According to this concept, companies can sometimes be so closely related to each other that it would be artificial to treat them as separate economic entities for competition law purposes.[86] In South Africa the single economic entity is regulated by the Competition Act.[87] In *The Delatoy Investments* case, the single economic entity doctrine was used to hold two shareholders liable for the anti-competitive conduct of subsidiary companies that were affiliated to them.[88] Case law precedent from competition law is not directly transferable to the law of delict but the approach used by the court in this case provides useful insight into how vicarious holdsub liability may be approached.

The key requirement for a finding that a group of companies are operating as a single economic entity is summarised as follows:

> "The crucial question, therefore, is whether the parties to an agreement are independent in their decision-making or whether one is able to exercise decisive influence over the other, with the result that the latter does not enjoy 'real autonomy' in determining its commercial policy on the market."[89]

Whether there is decisive influence or real autonomy will require an assessment of one or more of the following factors. "The shareholding of a parent company in its subsidiary, the composition of the company's board of directors and the extent to which the parent company influences the strategy of the subsidiary"[90]

The court in the *Delatoy Investments* case was tasked to inquire into whether the thirteen corporate respondents in the case were acting as a single economic unit.[91] The Competition Tribunal found that respondents were part of an illegal cartel and were acting as a single economic entity with a single controlling mind.[92] The Tribunal took into account that the common thread of control was the two

[86] N Mackenzie, I Rogers and S Langbridge "Single Economic Entity Doctrine in South Africa and its implications for competition policy" http://www.compcom.co.za/wp-content/uploads/2014/09/The-Single-Economic-Entity-Doctrine-in-SA.PDF (Last accessed12September2017)
[87] Competition Act 89 of 1998 s4.
[88] *Competition Commission v Delatoy Investments (Pty) Ltd and Others* [2016] 1 CPLR 67 (CT) at 83.
[89] N Mackenzie op cit note 86 at 4.
[90] *Competition Commission* supra note 88 at 71- 72.
[91] Ibid at 70.
[92] Ibid at 83.

main directors and shareholders of all the entities in the corporate group.[93] Another factor was the way entities were constantly reconstructed to conceal the true nature of the group's activities.[94] Finally, the two directors had breached their roles as directors by conflating the exercise of their fiduciary duties and ownership within the entire group.[95]

From an analysis of the operation of the single economic entity doctrine in South Africa, several lessons can be extracted from how competition law approaches holding-subsidiary company liability. Courts in competition law consider evidence of control and economic integration as part of the basis of liability within corporate groups. The focus is on whether the corporate subsidiaries have true autonomy and whether they can exercise independent discretion in the management of their affairs or not? Courts also look at the management practices of the company. As seen in the *Delatoy* case courts in competition law also consider evidence that there is a predatory mix of management and ownership. Were persons being ordinarily both the owners and the management of the company, they do not violate any law. However as seen in *Delatoy*, it attracts liability for the shareholders when it leads to conduct such as the transfers of soft loans at less than market value within the corporate group and irregular and unaccounted movement of funds within the corporate group.[96] That sort of abusive control is then the basis for liability.

The above analysis in competition law shows that the existence of control and economic integration can form part of the basis for liability in the holding-subsidiary company relationship.[97] Further, the approach used by courts in competition law show that courts in this area of law look at evidence that shows high levels of economic integration in the holding-subsidiary company relationship. This can be seen by the courts focus on how the controllers of the corporate group used the juristic personality of the entire group towards a single objective of advancing their illegal cartel.[98] In competition law, anti-competitive economic integration therefore forms part of the main basis of creating liability in the holding-subsidiary company relationship.[99] A court dealing with the suitability of a vicarious holdsub liability should therefore take into account the approach used in competition law and use features of control and economic integration to determine the suitability of a scheme of vicarious holdsub liability.

[93] Ibid at 73.
[94] Ibid at 77.
[95] Ibid.
[96] Ibid at 74-75.
[97] N Mackenzie op cit note 86 at 11.
[98] Ibid at 16.
[99] Ibid.

# 4. Control and integration aspects in foreign case law

The *Chandler v Cape plc* the court held that a holding company based in the United Kingdom was liable for the delict of its subsidiary company in a foreign jurisdiction. [100] The court reasoned that the control exercised by the holding company over its subsidiary was of such a close nature and proximity that it created an assumption of responsibility on the part of the holding company for the harms done by its subsidiary company.[101] This assumption of responsibility created a direct duty of care between the holding company and the harmed third parties in question.[102] In coming to the decision that the holding company was directly liable for the delicts of its subsidies the court considered the following factors:

> (1) The businesses of the parent and subsidiary are in a relevant respect the same. (2) The parent has, or ought to have, superior knowledge on some relevant aspect of health and safety in the particular industry. (3) The subsidiary's system of work is unsafe as the parent company knew, or ought to have known; And (4) the parent knew or ought to have foreseen that the subsidiary or its employees would rely on its using that superior knowledge for the employees' protection. For the purposes of (4) it is not necessary to show that the parent is in the practice of intervening in the health and safety policies of the subsidiary. The court will look at the relationship between the companies more widely. The court may find that element (4) is established where the evidence shows that the parent has a practice of intervening in the trading operations of the subsidiary, for example production and funding issues."[103]

In its application of these factors to the facts, the court found that the holding company was in the practice of issuing out instructions to its foreign subsidiary such as on product mixes, capital expenditure and on adherence with group policy on its product operations.[104] The court also noted that the holding company had substantially involved itself in the health and safety policy of its subsidiary and it cited how the holding company had made decisions on the employability of those that had contacted tuberculosis.[105] The reasoning of the court and the considerations taken into account by the court are useful for the control and economic integration test in the following ways.

From the reasoning of the court we know that the nature of control in the case created the assumption of responsibility. This in turn was the basis of the duty of care and the eventual liability of the holding company towards the third parties. What is clear from the case is that where the holding company and its subsidiaries are in the same business and where there is relevant control of the subsidiaries business that can form the basis of the holding company's liability towards third parties. What is less clear is how much control is required to constitute the relevant control required by the court. The court gives a few guidelines as to what may constitute relevant control. The court stated

[100] *Chandler v Cape plc* (2012) EWCA Civ 525 at 659.
[101] Ibid 655 -660.
[102] Ibid.
[103] Ibid at 659.
[104] Ibid at 658.
[105] Ibid.

that the scope of the entire group policy is instructive on whether there is relevant control or not.[106] The policy that the court was referring to was on areas such as management, production and sales.[107] The more detailed and far reaching the holding company creates policies in these areas for its subsidiaries the more there is an inclination towards a finding that there is the relevant control required to trigger the operation of liability.

Petrin argues that the understanding of control used in *Chandler* is too broad and imprecise.[108] He argues that while the case revolved on whether the holding company had assumed responsibility in health and safety measures in that subsidiary.[109] The court did not create a test that requires control to be specific to health and safety policy.[110] Rather the court only required that it be shown that the parent company had a general practice of interfering in the trading operations of its subsidiary company.[111] A holding company may find itself liable for the delicts of its subsidiaries even when the policies it controlled and informed in its subsidiary were completely unrelated to the harm causing activity.[112] According to such an approach a holding company intricately involved in the finance and sales of its corporate subsidiary can find itself liable for defective health and safety standards in its subsidiary.[113] Such an approach would be overly far reaching on the autonomy of corporate groups and would produce adverse results.[114]

A court tasked with developing vicarious holdsub liability should rather seek to analyse the control that is most proximate to the harm creating activity. In the *Chandler* case, this would require a court to inquire into whether the holding company exercised control over the health and safety policy of its subsidiary and not the general policy of the subsidiaries entire operation. It may well be justified that an overall analysis of the control exercised by the parent company is warranted to get a full picture, but this should be certain instances as an exception as opposed to the general rule. However, a narrower analysis of control such as the one advocated by Petrin may be more suitable.

The Chandler case offers useful lessons for the present purposes, but it is important to note that the concerned the use of direct liability and not vicarious liability, consequently the lessons from the case are not directly transportable to questions of vicarious holdsub liability. The chandler case is however, important because it helps build insight into how features of control and economic integration can be part of the basis from which liability can flow between a holding company and its subsidiary.

[106] Ibid.
[107] Ibid at 643.
[108] M Petrin "Assumption of Responsibility in Corporate Groups: *Chandler v Cape plc"* (2013) 76 *Modern Law Review* 603 at 611-614.
[109] Ibid.
[110] Ibid.
[111] Ibid.
[112] Ibid.
[113] Ibid.
[114] Ibid.

# 5.The constitutional implications of vicarious holdsub liability

Constitutional considerations of what are important for the discussion on whether the holdsub relationship should be recognised as a category of vicarious liability will ultimately hinge on policy discussions and the Constitutional Court cases of *K*[115] and *F*[116] which have deliberated on how the doctrine of vicarious liability should be approached. Any policy discussion should be led by the values of Constitution as the supreme law of the land.[117] In that sense, it would be wise to use the Constitution and its interpreting case law as the ultimate guide on whether it is plausible to add the holdsub relationship to the list of relationships capable of attracting vicarious liability.

The Constitutional Court in both the *K* and *F* cases put normative considerations at the heart of the tests of vicarious liability. In *K*, O'Regan J stated that: "[i]n considering the common-law principles of vicarious liability, and the question of whether that law needs to be developed in that area, the normative influence of the Constitution must be considered"[118]

The Court further elaborated

> "[o]ne realises that characterising the application of the common-law principles of vicarious liability as a matter of fact untrammelled by any considerations of law or normative principle cannot be correct. Such an approach appears to be seeking to sterilise the common-law test for vicarious liability and purge it of any normative, social, or economic considerations. Given the clear policy basis of the rule as well as the fact that it is a rule developed and applied by the courts themselves, such an approach cannot be sustained under our new constitutional order. What is clear, however, is that as a matter of law and social regulation, the principles of vicarious liability are principles which are imbued with social policy and normative content" [119]

The approach in *K* was subsequently followed by the same Constitutional Court in the *F* case.[120] These two cases show that the Court's approach to vicarious liability prefers a policy driven analysis that considers a wide range of normative factors in its analysis, while guided by the spirit and values of the Constitution. This is contrary to the traditional technical legal approach of vicarious liability that has been largely insulated from the normative value system of the Constitution.[121] The question of recognising holdsub vicarious liability will ultimately require a court to consider whether it is suitable and just for it to discharge its duty in terms of section 39 (2)[122] to develop the common law in line with the constitution.

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[115] *K v Minister of Safety and Security* 2005 (6) SA 419 (CC).
[116] *F v Minister of Safety and Security* 2012 (3) BCLR 244 (CC).
[117] The Constitution op cit note 18 s2.
[118] *K* Supra note 115 para 19.
[119] Ibid para 22.
[120] *F* Supra note 116 paras 49- 50.
[121] JA Linscott "a critical analysis of *the majority judgement in F v minister of safety and security* 2012 1 SA 536 CC*" (2014) 17 Potchefstroom Electronic Law Journal* 2916 at 2924.
[122] The Constitution Op cit note 18 at s39 (2).

A court tasked with considering the development of vicarious liability to cover the holdsub relationship will most certainly have to apply its mind in one way or the other as to how and if constitutional imperatives should be considered in the discharge of this duty. A court must consider several key limitations that may limit the utility of the Constitution and the cases of *K* and *F* in deciding whether vicarious liability should be extended to the holdsub relationship.

First, in both *K* and *F* cases the task of the court involved a vertical application of the constitution between the state and private persons.[123] The court did not deal with the horizontal application of the Constitution between two private citizens.[124] In our case a court will be required to inquire into the horizontal application of the Constitution. This is between a company and natural persons. Consequently, the fact that the precedents in both *K* and *F* where mainly tailored for vertical application of the constitution presents an obstacle for their usefulness in these enquiries.

Further, the policy reasons that informed the development of vicarious liability in both *K* and *F* were mainly aimed towards the States duty to protect the rights of citizens as enshrined in the constitution.[125] These cases did not affect vicarious liability as it operates between private citizens.[126] This is because no private person has a positive constitutional obligation to the constitutional rights of another citizen.[127] Consequently, it is unclear how a court tasked with the development of holdsub vicarious liability will interpret the lessons of *K* and *F* between a juristic person and a natural person.

In addition, both *K* and *F* also focused on the third requirement for employment vicarious liability. The requirement that the delict must have been committed in the course and scoop of employment and on the implication of deviation cases.[128] This limits the applicability of *K* and *F* to holdsub vicarious liability in our case for the following reasons. Before a court can engage on the matters of course and scoop it must first decide whether the relationship in question is one that is recognised as capable of attracting vicarious liability. This is principally the enquiry in question and on this question both *K* and *F* offer little in sight. Ultimately, a court tasked with the potential development of holdsub vicarious liability ought to apply its mind on how and whether it should incorporate normative constitutional values. What is less clear is that the value of *K* and *F* in this exercise.

[123] *K* at Supra note 115 at 60 and *F* Supra note 116 at 27.
[124] *Khumalo and Others V Holomisa* 2002 (5) SA 401(CC) at para 33.
[125] *F* Supra note 116 at 20.
[126] *Minister of Safety and Security v Van Duivenboden* 2002 (3) All SA 741 (SCA) para 19.
[127] Ibid at 20.
[128] *K* at Supra note 115 at 21-33 and *F* Supra note 122 at 40.

# 6. Consideration of traditional policy factors underlying vicarious liability

Several traditional theories of vicarious liability have been used to justify the existence and imposition of vicarious liability. The interest or profit theory[129], the deterrence theory[130], the risk or danger theory[131], the loss distribution theory[132], the control test[133] and lastly, the social convenience or otherwise known as rough justice[134]. All these theories will overlap and have varying levels of application in any given case.

None of the theories should be understood as being decisive but a court must certainly apply its mind to their applicability when deciding on the suitability of holdsub vicarious liability.it will be argued that the theories of vicarious liability are compatible with a scheme of vicarious holdsub liability. Ultimately whether and when the theories are applicable will depend on the value attached to them by a court.

## 6.1The interest or profit theory

The premise of this theory is that if you receive any benefits from an activity you should also bear its burdens as a corollary to those benefits.[135] This theory finds the most relevance for holding companies that directly own part or the whole of the subsidiaries and receive dividends from the business activities of these subsidiaries. A court when deciding on issues of the extension of vicarious liability to the holdsub relationship, should consider the fact that the holding company receives a benefit from the activity that caused the delict. It is therefore fair for the holding company to share in the risks associated with the business of the corporate subsidiary if it shares in the benefits of the harm causing activities.

## 6.1 The deterrence theory

Deterrence as a basis for extending vicarious liability between an employer and employee is justified on the basis that if an employer is constantly faced with the risk of being held vicariously liable, such an employer [136]"has every incentive to encourage its employees to perform well on the job and to discipline those who are guilty of wrongdoing and to adopt strategies to minimize the risk of loss or injury to third parties by his or her employee"[137] Alan o Sykes describes an additional benefit to deterrence that is inspired by vicarious liability. He states that:

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[129] *RH Johnson Crane Hire (Pty) Ltd v Grotto Steel Construction (Pty) Ltd* 1992 (3) SA 907 (C) at 500.
[130] *London Drugs Ltd v Keuhne and Nagel International Ltd* (1992) 3 SCR 299 at 340.
[131] Calitz K "Vicarious liability of employers: Reconsidering risk as the basis of liability" (2005) 3 *The Journal of South African Law* 215 at 216.
[132] *Smith v Eric S Bush* (1990) 1 AC 831 at 858 and *Scott v Davis* (2000) 175 ALR 217 at 295-296.
[133] J.M. Potgieter op cit note 6 at 191.
[134] *Imperial Chemical Industries Ltd v Shatwell* (1965) AC 656 (HL) at 685 and *Kooragang Investments Pty Ltd v Richardson & Wrench Ltd* (1982) AC 462 at 471- 472.
[135] *RH Johnson Crane Hire (Pty) Ltd* supra note 129.
[136] J.M. Potgieter op cit note 6 at 199.
[137] *London Drugs Ltd* supra note 130.

> "Vicarious liability has yet another benefit. Because the principal enterprise no longer earns excessive profits from the evasion of liability judgments by Vicarious Liability of the insolvent agent, the incentive for inefficient expansion disappears, and the scale of the enterprise (or its industry) contracts to its socially efficient level"[138].

Holding companies often have a lot of control over their subsidiaries; they control and monitor the activities of their subsidiaries. At the very least holding companies will have some influence on how their subsidiaries conduct themselves?[139] This influence may be created by a range of factors. It may be the case that the business models, intellectual property, expertise in terms of corporate management practice or financial assistance that the subsidiary uses comes from the holding company. In such a situation if vicarious liability is extended to the holding companies it increases the incentive for it to encourage this subsidiary that it controls or has influence over to adopt prudent business strategy that minimises the occurrence of delictual harm on third parties. Vicarious liability may also discourage holding companies from supporting careless and unplanned business expansion of their subsidiaries that has the potential to cause delictual harm to third parties.[140]

## 6.2 The Enterprise risk or danger theory

> "The basic tenet of enterprise liability is that with benefits come burdens. An enterprise introduces risks into society; if those risks materialise then the enterprise should pay for them."[141]

> "The Enterprise risk liability theory is not an economic model of liability, rather a moral one; it also uses a language of control and enterprise integration however it must not be confused with joint liability. There is a moral notion underpinning the doctrine of vicarious liability that where I assign a purposeful role to another, I am liable for the other if I have the power (legal or factual) to control exactly how they carry out this role (even if I do not exercise this power and would never exercise it), and I can exercise sufficient control over the day-to-day side. [142]

Morgan argues that the corporate group introduces risk to the society when it jointly acts with its subsidiary on a business venture.[143] The holding company benefits from this venture by extracting profits from the subsidiaries activities, but it is exempted from any liability when harm from the venture to falls on third parties.[144] This should be the basis for the application of the enterprise risk theory in the holding-subsidiary company relationship.[145]

Several South African courts have also argued that the risk theory is the true rational for vicarious liability, in particular when it comes to the employer employee relationship.[146] The justifications that

[138] A Sykes "The Economics of Vicarious Liability" (1984) 93 *Yale Law Journal* 1231 at 1242.
[139] K Strasser op cit note 76 at 638.
[140] A Sykes Op cit note 138 at 1263.
[141] *Bazley v Curry* (1999) 2 SCR 534 at 31.
[142] P Morgan Op cit note 78 at 290.
[143] Ibid.
[144] Ibid.
[145] Ibid.
[146] *Minister of Police v Rabie* 1986 (1) SA 117 (AD) at 134-135.

are often cited for holding a person liable who introduces new risks into the society is the need to ensure fairness and justice.[147]

For a court tasked with deciding on vicarious holdsub liability, it would have to decide whether holding companies that set up a subsidiary company are indeed introducing a new risk into the society. In addition, courts would have to decide if such a risk justifies the imposition of vicarious liability in the holding-subsidiary company relationship. The enterprise risk liability theory can be persuasive in sectors such as mining where the harms caused by mining companies to employees or third parties have been substantial.[148] In such situations it is often argued that group companies have not been allocated sufficient liabilities for the harms that are caused by their subsidiary companies and yet they receive substantial profits through these operations.[149] It may therefore be suitable to use the enterprise risk liability theory to better align the risks that holding companies create in societies and the economic benefits they derive from the use of the subsidiary company.

## 6.3 The loss distribution theory

This consideration has similarities with considerations such as the solvency theory. It's certainly true that not all these considerations are watertight and cannot be interchangeable, but with this consideration this research report leans on insurance and economic theory and simply asks. Where exactly, from a purely economic perspective should the undue loss suffered by third parties lie? On this question Alan O Sykes makes the following observations:

> "Empirically, principals are usually better risk bearers than their agents. Agents are often individuals of limited means who may be quite risk averse as to the prospect of even modest financial losses. Principals, by contrast, are often wealthier individuals, and intuition suggests that aversion to risk of a given magnitude often declines as wealth increases."[150]
>
> To the extent that the risks of civil liability are insurable," a principal often can obtain insurance more cheaply than his agents. A principal with many agents presents the insurance company with a ready- made pool of risks. Moreover, the issuance of one policy to a principal rather than many individual policies to his agents surely reduces administrative costs. The theory of optimal risk sharing thus predicts that privately Pareto optimal agency agreements will often allocate the bulk of civil liability to business principals rather than to their agent."[151]

This section on the theories of vicarious liability gives two main insights. First, it is plausible that is it economically sound to allocate liability risks to corporate holding companies for the delicts for their subsidiaries in certain circumstances. Second, the foundational pillars of the theories of vicarious liability permit us to create a scheme of vicarious holdsub liability. A court must still apply its mind to other factors for and against the allocation of this form of vicarious liability.

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[147] J Neethling & JM Potgieter op cit note 1 at 390.
[148] P Carrington "Asbestos Lessons: The Unattended Consequences of Asbestos Litigation" (2007) 26 *The Review of Litigation* at 584-589.
[149] Ibid at 584.
[150] A Sykes Op cit note 138 at 1235.
[151] Ibid at 1236.

# 7 Conclusion

This research has considered whether the rules of vicarious liability in South Africa can be extended to the holding-subsidiary company relationship or the holdsub relationship, as termed in here. This question has been inspired by the need to rectify the problem of delict creditors who have been left without adequate legal recourse against insolvent subsidiary companies. It explores the question of whether holding companies should take some of the responsibility towards uncompensated delict creditors.

In exploring this question, the following approach was used. First, the research argued that the employment relationship is the most relevant relationship for analysing the basis of vicarious liability. The research then went on to look at the basis of the employment relationship. At this stage, this research argued that the central pillars of the employment relationship are control and economic integration. At this stage, the research went on to test whether features of control and economic integration can be transported to the scheme holdsub vicarious liability. The aim was to test whether the holdsub relationship was sufficiently similar to the employment relationship for the purposes of vicarious liability. Several findings were made in relation to how corporate law, competition law and foreign tort law have used features of control and economic integration can be used as a basis for such a scheme of liability.

In corporate law, holding-subsidiary companies' liability requires that there be a level of abuse by the holding company towards the personality of the subsidiary company. Courts in corporate law only consider whether there were features of control and integration. Liability will ultimately depend on whether the holding company unconscionably abused the juristic personality of the subsidiary company. The implication of a scheme of holdsub vicarious liability on limited liability and separate legal identity will also be central to how courts receive a scheme of vicarious holdsub liability. In competition law, the focus is on whether the corporate group is acting as a single entity. It looks at features of autonomy and whether the corporate group acts under the mandate of a single controlling mind. Features of control and economic integration are central in findings of liability in competition law. In foreign tort law, the court in *Chandler* recognised that features of control can form part of the basis for liability in the holding-subsidiary company relationship. This research however argued that the courts use of control is too wide.

This research then went on to look at two other important questions. The first question relates to the implications of the constitution on the development of vicarious liability. The *K* and *F* cases were central in answering this question. Both the *K* and *F* cases showed that any inquiry into vicarious liability will ultimately hinge on the purpose, spirit and values of the South African constitution. These constitutional values require courts to consider a wide range of normative considerations when they are faced with deciding on the suitability of extending vicarious liability. It was also noted that several limitations should be considered carefully before the constitution is used extended the current operation of vicarious liability. This research then went on to consider the traditional policy or philosophical underpinnings. It was argued that the theories of vicarious liability are compatible with a scheme of vicarious holdsub liability.

In sum, this research report showed some of the preliminary considerations that should go into inquiring whether it is possible and desirable to extend the operation of vicarious liability to the holding-subsidiary company relationship. The weight of the evidence of this research seems to point towards a conclusion that courts are unlikely to accept vicarious holdsub liability.

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