

SIDESTEPPING LIMITED LIABILITY IN CORPORATE GROUPS USING THE TORT OF INTERFERENCE WITH CONTRACT

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[This article examines the tort of interference with contract. In particular it analyses the application of the tort to a holding company that 'starves' its subsidiary of funds. In this context the tort provides a potential mechanism to 'sidestep' the principle of limited liability. The elements of the tort are highly malleable and the tort is prone to expansion. Such expansion could erode the benefits of limited liability. For this reason the application of the tort in this context should be constrained with reference to the justifications of limited liability and courts should be reluctant to allow its application by a voluntary creditor who had other available mechanisms to protect their interests.]

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I INTRODUCTION

This article examines the tort of interference with contract.¹ It does so in the context of a potential claim by a third party against a holding company where the third party has contracted with a subsidiary of that holding company.² In

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¹ The tort has been referred to as the tort of 'inducing breach of contract' and similar. However, the tort may be committed even where there is inducement or procurement of actions that fall short of breach: see *Torquay Hotel Ltd v Cousins* [1969] 2 Ch 106, 138 (Lord Denning MR); *Allstate Life Insurance Co v Australia & New Zealand Banking Group Ltd* (1995) 58 FCR 26, 43 (Lindgren J) ('*Allstate Life Insurance*'); *OBG Ltd v Allan* [2005] QB 762, 775–6 (Peter Gibson LJ); John Fleming, *The Law of Torts* (9th ed, 1998) 757; R P Balkin and J L R Davis, *Law of Torts* (3rd ed, 2004) 639. It is for this reason that the term 'interference with contract' is preferable.

² This analysis presumes that the subsidiary is wholly owned. However, the application of the tort is not necessarily restricted by any particular level of formal control or ownership.

particular, this analysis contemplates the application of the tort where a holding company ‘starves’ its subsidiary of funds, with the effect that the subsidiary is unable to perform its contractual obligations to the third party.³

Analysis of this matter is both timely and important. Recently there has been renewed focus on the ability of holding companies to distance themselves from the obligations of their subsidiaries.⁴ Also, the recent High Court decision in *Zhu v Treasurer (NSW)*⁵ has highlighted the application of the tort of interference with contract to commercial dealings and has demonstrated a divergence from the law in England. Discussion of the application of the tort to holding companies allows analysis of these issues and reveals the complexities of their interaction. It also illustrates the potential for the tort to apply in a manner that ‘side-steps’ the principle of limited liability in corporate groups.

The analysis below first places the issue of holding company liability for interference with a subsidiary’s contracts in the context of the limited liability of such a company for the debts of its subsidiary. This is followed by a discussion of the English case of *Stocznia Gdanska SA v Latvian Shipping Co [No 3]*,⁶ a recent Court of Appeal decision that illustrates the potential use of the tort against a holding company. Following this, there is a more detailed critical analysis of the elements of the tort in Australia, with a particular focus on the intricacies of those elements when there is a claim based on the ‘starvation’ of a subsidiary of funds. Finally, there is a discussion of whether a broad or narrow approach towards the scope of the tort should be taken in the case of corporate groups.

II LIMITED LIABILITY AND CORPORATE GROUPS

The issue of holding company liability for interference with a subsidiary’s contract must be seen against the backdrop of two overlapping concepts that are the central legal features of corporate groups: the fact that corporations in groups are treated as separate juridical persons and the fact that limited liability applies to the constituent corporations in a group. These features, although subject to

³ It is not the aim of this article to argue in relation to the value or desirability of the tort generally. There is a significant quantity of literature on this issue, including much based on the ‘efficient breach theory’. Some of this literature critiques the tort based on the notion that it interferes with what would otherwise be ‘efficient’ breaches of contract. Other literature attempts to reconcile efficient breach theory with the tort. For a useful review of the literature see Fred S McChesney, ‘Tortious Interference with Contract versus “Efficient” Breach: Theory and Empirical Evidence’ (1999) 28 *Journal of Legal Studies* 131, 134–43. At the risk of falling foul of what McChesney identifies at 186 as the ‘methodological shortcomings’ of the ‘standard mode of legal rhetoric’ this article leaves for another day economic and empirical analysis of the tort in the corporate group context.

⁴ Evidence of this revived interest can be found in the report on transactions undertaken by members of the James Hardie group of companies that affected the ability of tort victims to recover for their losses: D F Jackson, Special Commission of Inquiry into the Medical Research and Compensation Foundation, *Report of the Special Commission of Inquiry into the Medical Research and Compensation Foundation* (2004). However, it should be noted that the facts that gave rise to this report may not be appropriate for the application of the tort, as the relevant underlying obligations arose in negligence rather than contract.

⁵ (2004) 218 CLR 530 (*Zhu*).

⁶ [2002] 2 All ER (Comm) 768 (*Stocznia Gdanska*).

some limited exceptions,⁷ give rise to the possibility that a holding company may, with limited risk of liability, allow one of its subsidiaries to ‘wither on the vine’ by refusing to provide the subsidiary with sufficient funds to operate. The problem was aptly described in the English context in *Re Southard & Co Ltd* by Templeman LJ, who stated:

English company law possesses some curious features, which may generate curious results. A parent company may spawn a number of subsidiary companies, all controlled directly or indirectly by the shareholders of the parent company. If one of the subsidiary companies, to change the metaphor, turns out to be the runt of the litter and declines into insolvency to the dismay of its creditors, the parent company and the other subsidiary companies may prosper to the joy of the shareholders without any liability for the debts of the insolvent subsidiary.⁸

Where this occurs and losses are left with a subsidiary, it may be that the holding company has ‘externalised’ risks while still taking rewards from its subsidiary.⁹ However, if interference with contract provides a remedy against a holding company to a party contracting with a subsidiary, this may allow an important route to ‘sidestep’ the principle of limited liability. This in itself provides significant justification for an examination of the limits of the tort in this context. The tort is not alone in this regard and the ‘sidestepping’ of the principle of limited liability can be observed in the context of a number of other potential actions against holding companies.¹⁰ The fact that the tort may join a developing range of paths around the corporate veil reinforces the importance of its examination.

III AN ILLUSTRATION OF THE TORT IN A CORPORATE GROUP CONTEXT: *STOCZNIA GDANSKA*

The application of the tort in a corporate group context can be observed in the case of *Stocznia Gdanska*.¹¹ In the case, the Latvian Shipping Company (‘Latvian Shipping’) negotiated for the manufacture and purchase of a number of vessels from *Stocznia Gdanska SA* (‘*Stocznia*’).¹² The negotiations were conducted on the basis that the ultimate purchaser was to be a company nominated by *Latmar Holdings Corporation* (‘*Latmar*’), a subsidiary of *Latvian*

⁷ The courts may lift the corporate veil to impose liability on a holding company, although such decisions are ‘occasional’ and unpredictable: *Briggs v James Hardie & Co Pty Ltd* (1989) 16 NSWLR 549, 567 (Rogers AJA). Statutory provisions may also impose liability on a holding company, most notably *Corporations Act 2001* (Cth) s 588V. See below Part IV.

⁸ [1979] 3 All ER 556, 565. Note that this statement might be updated with reference to some exceptions: see especially *Corporations Act 2001* (Cth) s 588V.

⁹ Henry Hansmann and Reinier Kraakman, ‘Toward Unlimited Shareholder Liability for Corporate Torts’ (1991) 100 *Yale Law Journal* 1879, 1883.

¹⁰ For discussion in the context of the tort of negligence, see Peter Edmundson and Pam Stewart, ‘Liability of a Holding Company for Negligent Injuries to an Employee of a Subsidiary: *CSR v Wren*’ (1998) 6 *Torts Law Journal* 123. For discussion in the context of actions for ‘knowing receipt’, see Peter Edmundson and James Mitchell, ‘Knowing Receipt in Corporate Group Structures’ (2005) 23 *Company and Securities Law Journal* 515.

¹¹ [2002] 2 All ER (Comm) 768.

¹² *Ibid* 773 (Rix LJ).

Shipping.¹³ When negotiations reached their final stages, Stocznia was informed that the purchaser was to be Latreefers Inc ('Latreefers'), a company that was to be a wholly owned subsidiary of Latmar.¹⁴ Stocznia did not seek a guarantee of Latreefers' performance from either Latvian Shipping or Latmar (although there was evidence that Latvian Shipping would have given such a guarantee if pressed).¹⁵

Latreefers was incorporated a few days before the contracts for the manufacture and supply of the vessels were entered into.¹⁶ While the shares in Latreefers were held by Latmar, the directors of Latreefers were employees of a service company called Capco Trust (Isle of Man) Ltd ('Capco'), which was connected with a firm of solicitors on the Isle of Man. Capco and Latvian Shipping had entered into a contract that provided that Latreefers would 'be kept in sufficient funds by [Latvian Shipping] to honour its liabilities as and when they become due'.¹⁷

The contracts required the provision of six vessels (once certain options had been exercised) and the general structure of the consideration was the same in relation to each vessel.¹⁸ A payment of five per cent of the total price was due on signing, to be followed by 20 per cent on the laying of the keel, 25 per cent upon launch and the remaining 50 per cent upon delivery. The five per cent deposit was paid in each case. Unfortunately, the market for the charter of the vessels (and hence the commercial value of the vessels) collapsed and it was suggested that, from the perspective of Latreefers, this made the contracts 'economically unrealistic'.¹⁹ There was evidence that Latreefers, if unsupported by its holding companies, would not have been able to raise sufficient funds to pay for the vessels.²⁰

Notice was given to Latreefers that the 20 per cent keel laying deposit was due for the first²¹ and second²² vessels. No payment was made. Stocznia gave notices of rescission in respect of these two contracts. Stocznia then purported to appropriate the keels laid for the first two vessels to the contracts for the third and fourth vessels and issued 'keel laying notices' in relation to these.²³ Again, the keel laying deposits were unpaid and notices of rescission were issued by Stocznia. A similar process ensued in respect of the contracts for the fifth and sixth vessels.²⁴

As Latreefers was unfunded, any remedies against it would have proved hollow. Therefore, Stocznia brought a number of claims including one against

¹³ Ibid.

¹⁴ Ibid 773–4 (Rix LJ).

¹⁵ Ibid 774.

¹⁶ Ibid.

¹⁷ Ibid.

¹⁸ Ibid.

¹⁹ Ibid 775 (Rix LJ).

²⁰ Ibid 774 (Rix LJ).

²¹ Ibid 776 (Rix LJ).

²² Ibid 777 (Rix LJ).

²³ Ibid.

²⁴ Ibid.

Latvian Shipping on the basis that Latvian Shipping had induced Latreefers' breach of contract. It was found at trial that Latvian Shipping had not directly induced Latreefers to breach its contract with Stocznia as Latvian Shipping had not specifically told Latreefers' directors not to pay the relevant instalments.²⁵ However, the trial judge, Thomas J, was satisfied that the task of raising finance for the vessels was the responsibility of Latvian Shipping and not of Latreefers, that Latvian Shipping had instructed Latreefers that it did not intend to provide funds for the instalments (at the time of the keel laying notices) and that Latreefers was told to do nothing to respond to the notices.²⁶ Thomas J further found that this was a deliberate breach of the agreement that Latvian Shipping had with Capco to keep Latreefers in sufficient funds and that the objective of refusing to fund Latreefers was to prevent it performing its contract with Stocznia.²⁷ On this basis it was found at first instance that Latvian Shipping was liable to Stocznia for indirectly inducing a breach of contract by Latreefers.²⁸

Several issues were considered on appeal. In relation to the actions in tort, Rix LJ (with Tuckey and Aldous LJJ agreeing) found that the trial judge's decision that there was no liability for direct inducement of breach should not be disturbed.²⁹ However, Latvian Shipping was liable for 'indirect inducement by unlawful means of Latreefers' breaches of its contracts'.³⁰ Rix LJ stated that the tort is committed where 'a defendant wrongly, that is to say, by unlawful means, withholds that which is necessary to another party to fulfil his contract with a claimant, and does so with the requisite knowledge of that contract and with the requisite intention'.³¹

Therefore, the withholding of funds by Latvian Shipping, in breach of the agreement between Latvian Shipping and Capco to keep Latreefers in funds, with the intention that this was to cause Latreefers to fail to perform its contracts, entitled Stocznia to a remedy in tort.

The reasoning in this case will be examined in more detail below;³² however, the outline above demonstrates the potential use of the tort against a holding company. While resort to the tort was necessary only because of the curious fact that Stocznia did not request a parent company guarantee,³³ the usefulness of the

²⁵ *Stocznia Gdanska SA v Latvian Shipping Co* [2001] 1 Lloyd's Rep 537, 574–7 (Thomas J).

²⁶ *Ibid* 572, 574.

²⁷ *Ibid* 574–7.

²⁸ *Ibid* 581–2 (Thomas J). In addition to the claims based on the tort of inducing breach of contract, a series of complex claims in relation to contract (including breach and rescission) was made: *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 783–96 (Rix LJ). While a number of interesting issues arose, it is not necessary to delve into these matters for the purposes of this article. For discussion of some of these issues see J W Carter, 'Shipbuilding Contracts: The Interaction of Contractual Rights and Common Law Remedies' (1997) 12 *Journal of Contract Law* 65; J W Carter, 'Shipbuilding Contracts: Take 2' (1998) 12 *Journal of Contract Law* 247; J W Carter, 'Shipbuilding Contracts: Not Quite the Final Chapter' (1998) 13 *Journal of Contract Law* 156.

²⁹ *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 797–8.

³⁰ *Ibid* 803 (Rix LJ).

³¹ *Ibid* 799.

³² See below Parts V(C), VI.

³³ This could be partly due to the fact that, in the negotiation of the arrangement, Stocznia did not seek legal advice: *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 773 (Rix LJ).

claim for the contracting party is clear: it allowed Stocznia to look beyond the insolvent party with whom it had contracted towards a better funded target.

IV DOES THE TORT PROVIDE A POTENTIALLY USEFUL REMEDY IN AUSTRALIA?

Whether the tort is potentially useful to a plaintiff in Australia depends upon whether it can operate in circumstances that do not give rise to a remedy by some other mechanism or, in areas of overlap with other remedies, whether the tort provides a procedural or tactical advantage. There would be limited practical role for the tort in the context contemplated if it did nothing beyond what might be achieved through the insolvent trading provisions in Part 5.7B of the *Corporations Act 2001* (Cth) or by means such as lifting the corporate veil. In certain cases the tort may find application when Part 5.7B might not and, in other cases, the tort may provide practical advantages for a creditor even if there may be potential liability under Part 5.7B. The potential advantages of pursuing the tortious remedy (if available) include, but are not limited to:

- the fact that breach of s 588V gives rise to an action by the liquidator of the subsidiary, rather than by individual creditors, with the result that the proceeds of such an action may be pooled. However, a claim in tort by a creditor would be for its benefit alone;³⁴
- the fact that a number of defences may apply in relation to a claim under the insolvent trading provisions;³⁵
- the fact that tortious liability does not rely upon the demonstration of insolvency at any particular point in time;³⁶ and
- the fact that it is not necessary to determine when the subsidiary incurred a debt.³⁷ Where the subsidiary has contracted for the purchase of significant items, such as in *Stocznia Gdanska*, difficult issues may arise in determining when any debt is incurred. The time at which a debt is incurred depends upon the facts and the context of enquiry.³⁸ It has been suggested that in some

³⁴ See *Corporations Act 2001* (Cth) s 588W. Note that under equivalent provisions that apply to the liability of directors in s 588G a creditor may have a direct action: s 588M(3), pt 5.7B div 4(B). This may provide a creditor of a subsidiary some utility in arguing that the holding company was a shadow director of the subsidiary and that liability arises under s 588G, although the difficulty of demonstrating that a company is a shadow director should not be underestimated.

³⁵ *Corporations Act 2001* (Cth) s 588X. For a recent discussion of these defences in the context of analogous provisions in s 588H, see David B Goldman, 'Directors Beware! Creditor Protection from Insolvent Trading' (2005) 23 *Company and Securities Law Journal* 216.

³⁶ See *Corporations Act 2001* (Cth) s 588V(1)(b). Unless the case falls within circumstances listed in s 588E, in which insolvency can be presumed subject to rebuttal, the demonstration of insolvency can be complex and involve practical difficulties: see generally Kerri Eagle, 'Evidentiary Issues in Proving Insolvency' (1999) 7 *Insolvency Law Journal* 196.

³⁷ The time at which the debt is incurred must coincide with the existence of the holding company–subsidiary relationship (*Corporations Act 2001* (Cth) s 588V(1)(a)), the insolvency of the subsidiary (s 588V(1)(b)), the existence of reasonable grounds to suspect insolvency (s 588V(1)(c)) and, where applicable, the awareness of the holding company or its directors of such grounds (s 588V(1)(d)).

³⁸ *Hawkins v Bank of China* (1992) 26 NSWLR 562, 567–8, 572 (Gleeson CJ).

situations a debt will be incurred by a purchaser at the time of delivery and invoice and in other situations the debt will be incurred at the time of contract.³⁹ Pursuit of the action in tort means that such matters do not need to be addressed.

Obviously, in other respects, Part 5.7B provides much broader coverage than the tort, and the tort is not in any danger of usurping the function of these statutory provisions.⁴⁰ However, it appears that the tort may provide a remedy for a creditor in at least some situations where Part 5.7B may not.

Similarly, the tort would not provide a significant remedy if it had no operation beyond other available routes to holding company liability, such as lifting the veil at common law. It often is said that the courts may lift the veil of incorporation in a number of circumstances, including where there is fraud, or where the corporation is held to be an agent of another party.⁴¹

The cases on fraud typically revolve around fraudulent *incorporation*, or the formation of a corporation with the sole or dominant purpose of avoiding a pre-existing legal obligation.⁴² The facts of *Stocznia Gdanska* clearly demonstrate that the tort is not so confined. In that case the intention to induce breach of contract by letting the subsidiary ‘starve’ apparently arose *after* the incorporation of the subsidiary. In such a case it is very unlikely that a court would lift the veil on the basis of fraud.

Holding company liability may also flow from a finding that the activities of a subsidiary were carried on by the subsidiary as an agent of the holding company. The most familiar case in which this occurred is *Smith, Stone & Knight Ltd v City of Birmingham*.⁴³ While unusual for the fact that it is not a case on holding company liability,⁴⁴ it has been suggested that a key reason for the

³⁹ See Hodgson J’s comments in *Leigh-Mardon Pty Ltd v Wawn* (1995) 13 ACLC 1244, 1248, which suggest that the date of contract might be appropriate in relation to goods that were manufactured especially for the purchaser and were not readily saleable elsewhere, such that a refusal to take delivery would give rise to a damages claim approximating the value of the goods. See also references to this case in *Credit Co Pty Ltd v Atkins* (1999) 17 ACLC 756, 768–9 (O’Loughlin J) and discussion of the issue in John Mosley, ‘Insolvent Trading: What Is a Debt and When Is One Incurred?’ (1996) 4 *Insolvency Law Journal* 155; Goldman, above n 35, 219; Paul James, Ian Ramsay and Polat Siva, ‘Insolvent Trading — An Empirical Study’ (2004) 12 *Insolvency Law Journal* 210, 212–13.

⁴⁰ Obvious differences include the fact that an action pursuant to a contravention of the *Corporations Act 2001* (Cth) s 588V does not require there to be any ‘intention’ on the part of the holding company or its directors, and that the section has potential application in relation to debts other than contract debts. Further, the tort is concerned with how a breach came about (and related matters of causation), whereas pt 5.7B is not directly concerned with how the debt was incurred.

⁴¹ R P Austin and I M Ramsay, *Ford’s Principles of Corporations Law* (12th ed, 2005) 126. Of course, the finding of agency between a company and its shareholders assumes the separate nature of shareholder and company rather than disregards it. On this basis it can only be described as lifting the veil in a very general sense.

⁴² See *Jones v Lipman* [1962] 1 All ER 442; *Gilford Motor Co Ltd v Horne* [1933] Ch 935. If the relevant corporation in *Gilford Motor Co Ltd v Horne* had been formed by a third party before the intention to defeat the existing obligation then the veil would not be lifted: Austin and Ramsay, above n 41, 127. Austin and Ramsay specifically contemplate that the tort of interference with contractual relations may apply on those facts: at 127–8.

⁴³ [1939] 4 All ER 116 (*Smith, Stone & Knight*).

⁴⁴ In fact it was the holding company that was arguing for a finding that agency existed, in order to fall within a statutory compensation regime: *ibid* 118 (Atkinson J).

finding of agency was the fact that the subsidiary was not given sufficient resources by its holding company.⁴⁵ While the case has been applied in Australia,⁴⁶ its value as a precedent has been questioned for some time.⁴⁷ Further, the case falls a long way short of a general rule that the holding company of an under-funded subsidiary will become liable for the subsidiary's debts on the basis of agency.⁴⁸ In the absence of other factors indicating an agency relationship, the mere starvation of a subsidiary of funds with the intention of causing the subsidiary to be unable to perform a contract should not give rise to the lifting of the veil based on the principles found in cases such as *Smith, Stone & Knight*.

What appears from the discussion above is that, in finding application well outside its origins in labour law,⁴⁹ the tort provides a potentially useful means by which a creditor of a subsidiary may seek remedy against a solvent holding company.⁵⁰

V AN EXAMINATION OF THE TORT IN AUSTRALIA

The discussion above demonstrates the potential usefulness of the tort in a corporate group context and provides an example of such use in England. Analysis now turns to more detailed discussion of the elements of the tort as it has developed in Australia, in order to explore the limits of the tort and any ambiguities that may arise from its domestic application against a holding company. However, before these elements are explored, it is appropriate to reflect briefly upon the general basis of any holding company liability.

⁴⁵ Austin and Ramsay, above n 41, 130.

⁴⁶ *Spreag v Paeson Pty Ltd* (1990) 94 ALR 679, 711 (Sheppard J).

⁴⁷ See, eg, *Maclaine Watson & Co Ltd v Department of Trade and Industry; Re International Tin Council* [1988] 3 All ER 523, 310–11 (Kerr LJ).

⁴⁸ In order to determine whether or not a business is merely carried on by a subsidiary as an agent, Atkinson J poses six questions, all of which must be answered in the affirmative. While not stating explicitly that undercapitalisation is a key factor, one of the six questions is 'did the [parent] company govern the adventure, decide what should be done and what capital should be embarked on the venture?': *Smith, Stone & Knight* [1939] 4 All ER 116, 121.

⁴⁹ The modern tort can be said to flow from the case of *Lumley v Gye* (1853) 2 E & B 216; 118 ER 749 in which it was accepted for the first time that the principles behind remedies for 'poaching' the employment of servants extended to broader contractual obligations (in *Lumley v Gye*, the services of an opera singer not under an employment contract). For a fascinating account of the events leading to *Lumley v Gye*, see S M Waddams, 'Johanna Wagner and the Rival Opera Houses' (2001) 117 *Law Quarterly Review* 431, 431–40. Waddams is critical of the spread of the tort so far outside its original context: at 452–4. It has been suggested that around 60 per cent of cases have been in the employment context: David Howarth, 'Against *Lumley v Gye*' (2005) 68 *Modern Law Review* 195, 196–7. It has also been stated that recently the application of the tort to more general commercial dealings has increased: Michael Izzo, 'The Limits of *Lumley v Gye*: Commercial Disputes and the Tort of Interference with Contractual Relations' (2005) 13 *Torts Law Journal* 188, 188.

⁵⁰ In the case of *LMI Australasia Pty Ltd v Baulderstone Hornibrook Pty Ltd* [2003] NSWCA 74 (Unreported, Meagher, Hodgson JJA and Young CJ in Eq, 10 April 2003) [21] ('*LMI Australasia Appeal*'), Young CJ in Eq provides an example of a claim against a company for breach of contract that would be commercially frustrated by the fact that it was a '\$2 company' and an attempt to overcome this by bringing an action against related solvent companies for inducing the alleged breach.

A *The Basis of Holding Company Liability*

The fact that a holding company, like any company, is an artificial legal entity and can only act through natural persons presents some initial issues. The first of these involves whether or how the liability of the holding company is to be separated from the potential liability of those natural persons.⁵¹

It is clear from the case law that, in the simple situation of breach of contract by a corporation, the directors of that corporation will not be liable for inducing that breach.⁵² This principle has been said to flow from the High Court's analysis of the tort of conspiracy in *O'Brien v Dawson*.⁵³ The rationale behind this principle is that, assuming the director is acting within their authority, they are acting 'as' the corporation and their actions should not be separated from those of the corporation.⁵⁴ In other words, the tort must be committed by a third party and this third party 'cannot be the alter ego of one of the parties to the contract'.⁵⁵ This leaves any corporate liability for the tort as primary rather than vicarious, at least in the case of actions by directors. The same reasoning should be applied in relation to the acts of holding companies. Any liability should rest with the holding company itself rather than with the directors of the holding company.

A second issue is whether holding company liability should be precluded on the basis of the principle in *O'Brien v Dawson*.⁵⁶ In *LMI Australasia Pty Ltd v Boulderstone Hornibrook Pty Ltd*, Barrett J, in obiter, stated that on the facts of the case it could not be said that the holding company had interfered with the subsidiary's contracts.⁵⁷ Instead the relevant decision to interfere was made by the subsidiary, 'but that decision proceeds from an exercise of the holding company's will within and through the subsidiary, rather than upon it'.⁵⁸ In other words, the holding company '[was] not in the position of an outsider influencing the independent volition of the subsidiary'.⁵⁹ On this basis Barrett J found that the tort could not apply to the holding company, essentially for lack of interference by a third party.

⁵¹ Such natural persons typically will be appointed directors of the company. However, a company can act through a range of persons including directors (whether or not validly appointed), officers and other authorised parties.

⁵² *Idoport Pty Ltd v National Australia Bank Ltd* [2001] NSWSC 328 (Unreported, Einstein J, 2 May 2001) [29].

⁵³ (1942) 66 CLR 18. See *Idoport Pty Ltd v National Australia Bank Ltd* [2001] NSWSC 328 (Unreported, Einstein J, 2 May 2001) [13]–[29]. For a discussion of this matter, see Izzo, above n 49, 193–5. For discussion of the similar finding in *Said v Butt* [1920] 3 KB 497, see Howarth, above n 49, 226.

⁵⁴ *O'Brien v Dawson* (1942) 66 CLR 18, 32 (Starke J); see also Izzo, above n 49, 194.

⁵⁵ *Idoport Pty Ltd v National Australia Bank Ltd* [2001] NSWSC 328 (Unreported, Einstein J, 2 May 2001) [17].

⁵⁶ See Izzo, above n 49, 195–7.

⁵⁷ (2002) 18 BCL 57, 77 (New South Wales Supreme Court) ('*LMI Australasia First Instance*').

⁵⁸ *Ibid.*

⁵⁹ *Ibid.*

On appeal, Young CJ in Eq disagreed with this approach,⁶⁰ arguing that it relied upon a ‘completely imperfect’⁶¹ analogy between the position of the director of a corporation and the position of a holding company. The approach assumes that the rule in *O’Brien v Dawson* is based merely on the notion that the corporation has not exercised an independent mind, rather than on the different matter of the consequences of acting or thinking through an agent or director.⁶² Just as it cannot be presumed that a subsidiary is an agent of its holding company,⁶³ it cannot be presumed that when a holding company makes a decision in relation to the affairs of its subsidiary it does so as agent of the subsidiary or acting ‘as’ the subsidiary.⁶⁴ Instead, the better approach is to respect the separate nature of the holding company and its subsidiary; the rule that protects directors from a legal action for interference with contracts by their company should not extend generally to prevent holding companies being liable for interference with their subsidiaries’ contracts.⁶⁵ As was pointed out by Young CJ in Eq, to find otherwise would risk ‘the avoidance of contracts by the simple expedient of acting via [a] subsidiary’.⁶⁶ Such an approach is consistent with the English cases in which the courts have been untroubled in finding that a controlling parent company can interfere with the contracts of its subsidiaries.⁶⁷

B *The Mental Element: Knowledge and Intention*

As an initial matter, for the tort to apply the defendant holding company must have some knowledge of the relevant contract.⁶⁸ It must also be the case that the defendant holding company intended to interfere with the contract.⁶⁹ It is clear

⁶⁰ *LMI Australasia Appeal* [2003] NSWCA 74 (Unreported, Meagher, Hodgson JJA and Young CJ in Eq, 10 April 2003) [94]. Indeed, Young CJ in Eq firmly rejects the analysis, stating that ‘one must not allow nice sounding fuzzy dicta to take the place of proper analysis’: at [97]. However, the case is not the strongest precedent: see *Biscayne Partners Pty Ltd v Valance Co Pty Ltd* [2003] NSWSC 874 (Unreported, Einstein J, 3 October 2003) [111], where Einstein J, in referring to the Court of Appeal decision, stated: ‘there are difficulties with discerning a common holding as between the three judges sitting’.

⁶¹ *LMI Australasia Appeal* [2003] NSWCA 74 (Unreported, Meagher, Hodgson JJA and Young CJ in Eq, 10 April 2003) [97].

⁶² *Ibid* [94]–[95] (Young CJ in Eq).

⁶³ *Smith, Stone & Knight* [1939] 4 All ER 116, 121 (Atkinson J).

⁶⁴ Although this raises the difficult conceptual issue of whether a holding company that has sufficient control to make it a ‘shadow director’ of its subsidiary should be treated as acting and thinking ‘as’ its subsidiary in the sense explored in *Tesco Supermarkets Ltd v Natrass* [1972] AC 153.

⁶⁵ *Izzo*, above n 49, 201.

⁶⁶ *LMI Australasia Appeal* [2003] NSWCA 74 (Unreported, Meagher, Hodgson JJA and Young CJ in Eq, 10 April 2003) [98].

⁶⁷ See, eg, *Esso Petroleum Co Ltd v Kingswood Motors (Addleston) Ltd* [1973] 3 All ER 1057, 1068 (Bridge J); *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 798 (Rix LJ).

⁶⁸ *Sanders v Snell* (1998) 196 CLR 329, 338 (Gleeson CJ, Gaudron, Kirby, Hayne and Callinan JJ); *Independent Oil Industries Ltd v Shell Co of Australia Ltd* (1937) 37 SR (NSW) 394, 415 (Jordan CJ) (*‘Independent Oil Industries’*).

⁶⁹ *Allstate Life Insurance* (1995) 58 FCR 26, 43 (Lindgren J); *Fightvision Pty Ltd v Onisforou* (1999) 47 NSWLR 473, 512 (Sheller, Stein and Giles JJA) (*‘Fightvision’*). In an interesting recent English decision, the Court of Appeal confirmed that the tort would not be committed where there was an intention to interfere with the right of a party to manage their contractual affairs (in that case by the defective appointment of a receiver), but no intention to interfere with the performance of a contract: *OBG Ltd v Allan* [2005] QB 762, 775 (Peter Gibson LJ), 799

that malicious intention is not required.⁷⁰ However, the tort cannot be committed through mere negligence.⁷¹

Some recent Australian cases demonstrate that the requirements of knowledge and intention are bound together and should not be seen as separate ‘elements’ of the tort. In *Allstate Life Insurance Lindgren J* (with Lockhart and Tamberlin JJ agreeing) stated:

Linguistic confusion can arise in respect of the alleged tortfeasor’s state of mind with respect to breach of the contract. Both ‘intention’ and ‘knowledge’ have been used in this context. But a person’s ‘knowledge’ that what he is inducing will constitute a breach of contract and his ‘intention’ to induce a breach of contract by what he is doing refer to one and the same thing. After all, ex hypothesi, the alleged tortfeasor’s acts are intentional, a breach of contract occurs, and the acts induce the breach. Against that background, ‘knowledge’ and ‘intention’ that the breach will result from the acts do not signify any relevant distinction.⁷²

Further, Lindgren J stated:

the authorities establish conclusively that the gravamen of the tort is intention. Although the requirement of knowledge of the contract is sometimes discussed as if it was a separate ingredient of the tort, it is in fact an aspect of intention. The requirement that the alleged tortfeasor have ‘sufficient knowledge of the contract’ is a requirement he have sufficient knowledge to ground an intention to interfere with contractual rights.⁷³

These comments have been cited with approval recently by the New South Wales Court of Appeal⁷⁴ and are consistent with other formulations of the tort that describe liability as arising where the defendant acted ‘knowingly and intending the breach’⁷⁵ or where the breach was ‘knowingly procured’.⁷⁶

It has long been said that the knowledge of the defendant need not be knowledge of the precise terms of the relevant contract.⁷⁷ It has also been suggested that the courts may assume that knowledge of the contract exists if there is more general knowledge of the relevant business of the contracting party.⁷⁸ In addi-

(Carnwath LJ). However, the fragility of this decision is demonstrated by the dissent of Mance LJ, and Carnwath LJ’s admission of being ‘torn between’ the differing views of Peter Gibson and Mance LJ: at 799.

⁷⁰ *Zhu* (2004) 218 CLR 530, 569–70 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ); *Communications, Electrical, Electronic, Energy, Information, Postal, Plumbing and Allied Services Union of Australia v Corke Instrument Engineering Australia Pty Ltd* (2005) 223 ALR 480, 485 (Finkelstein J); *South Wales Miners’ Federation v Glamorgan Coal Co Ltd* [1905] AC 239, 246 (Lord Macnaghten).

⁷¹ See Fleming, above n 1, 762; Balkin and Davis, above n 1, 639.

⁷² (1995) 58 FCR 26, 37.

⁷³ *Ibid* 43.

⁷⁴ *Fightvision* (1999) 47 NSWLR 473, 510–11 (Sheller, Stein and Giles JJA).

⁷⁵ *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 803 (Rix LJ).

⁷⁶ Fleming, above n 1, 761–2.

⁷⁷ See *J T Stratford & Son Ltd v Lindley* [1965] AC 269, 332 (Lord Pearce); *Boral Bricks NSW Pty Ltd v Frost* (1987) 20 IR 70, 78 (Brownie J); *Australian Liquor, Hospitality and Miscellaneous Workers’ Union v Liquorland (Aust) Pty Ltd* (2002) 114 IR 165, 179 (Cooper J); Fleming, above n 1, 761; Balkin and Davis, above n 1, 641.

⁷⁸ Balkin and Davis, above n 1, 641.

tion, if the defendant knew of the existence of a contract, but reasonably believed that what was being induced or procured was not a breach of the relevant contract or that the alleged contract was no longer binding, the tort would not be committed.⁷⁹

It is clear that the requirements of intention and knowledge are ‘subjective’.⁸⁰ Negligent failure to ascertain the existence of a contract or its terms would not alone satisfy the mental requirement of the tort.⁸¹ However, wilful blindness or reckless indifference might.⁸² This does not usurp the subjective nature of the test as the devices of wilful blindness or recklessness merely provide evidence by which the relevant subjective intention can be found.⁸³ It has been suggested that this matter is complicated by whether or not the interference is ‘direct’ or ‘indirect’. R P Balkin and J L R Davis state:

If the defendant does an act the substantially certain consequence of which is directly to bring about a breach of a contract of which he or she is aware, then it will be presumed that the breach was intended, and liability will ensue unless the presumption is rebutted. An *indirect interference* with a contract, however, *must be a necessary consequence of the defendant's acts* ...⁸⁴

Again, it is submitted that this formulation does not signify a further substantive requirement or element in cases of indirect interference. Rather, it is suggested that it merely illustrates an aspect of inferring intention through recklessness. In cases of indirect interference it may be difficult to find intention through recklessness where the causal link between the defendant's act and the interference is unclear. This is because finding subjective intention through the device of recklessness in one sense may rely upon the notion that the more solid the causal link between an act and the result of the act, the more likely it is that the actor intends to bring about the result.⁸⁵

⁷⁹ *Fightvision* (1999) 47 NSWLR 473, 509 (Sheller, Stein and Giles JJA). This should follow from the fact that in such a case there would not be an intention to induce a breach of contract. Also, there would be no liability if, regardless of the defendant's intentions, there was in fact never a valid contract.

⁸⁰ *Ibid* 511 (Sheller, Stein and Giles JJA), citing *Allstate Life Insurance* (1995) 58 FCR 26, 43 (Lindgren J).

⁸¹ *Fightvision* (1999) 47 NSWLR 473, 512 (Sheller, Stein and Giles JJA).

⁸² *Ibid*; *Allstate Life Insurance* (1995) 58 FCR 26, 37 (Lindgren J).

⁸³ *Fightvision* (1999) 47 NSWLR 473, 510–11 (Sheller, Stein and Giles JJA) and the references there to *Allstate Life Insurance* (1995) 58 FCR 26, 37, 43 (Lindgren J); see also Fleming, above n 1, 761–2.

⁸⁴ Balkin and Davis, above n 1, 638–9 (emphasis added) (citations omitted). See also *Davies v Nyland* (1975) 10 SASR 76, 98 (Bray CJ). Note, however, that in *Davies v Nyland* the proposition is merely dicta and is put on the very conditional basis that ‘[t]here is some suggestion in some of the cases’ to support it: at 98.

⁸⁵ Note, however, that there are limits to this logic and subjective intention cannot be usurped completely by such logic. In *Gollins v Gollins* [1963] 2 All ER 966, 972, Lord Reid pointed out that sometimes a person in fact intends something very different from the likely consequences of their act. His Lordship stated:

To take a trivial example, if I say that I intend to reach the green, people will believe me although we all know that the odds are ten to one against my succeeding; and no one but a lawyer would say that I must be presumed to have intended to put my ball in the bunker, because that was the natural and probable result of my shot.

In the case of a holding company that ‘starves’ its subsidiary of funds, it would have to be shown that the holding company had sufficient knowledge of the subsidiary’s contracts to ground the required intention. The company can only have such knowledge through natural persons. As a practical matter it is likely that the knowledge will be attributed through directors or officers of the holding company.⁸⁶ In the case of significant contracts, there should be little difficulty finding evidence to show knowledge of the existence of those contracts in the minds of directors of the holding company. In many cases it is likely that some of those directors will also be directors of the subsidiary concerned. Only where the subsidiary operates completely independently is it likely that there will not be knowledge in the holding company of significant contracts.

Where there is some knowledge of its subsidiary’s contracts, the holding company’s act of refusing to place the subsidiary in funds must then be intended to prevent performance of those contracts. It is unlikely that the holding company will, through a director or an agent, expressly state its intention in withholding funds. Therefore, the matter is likely to be left to inference. Here much will turn upon whether the holding company was aware of the extent of the subsidiary’s funding and the extent of its financial obligations under the contracts. The more certain it is that failure to fund the subsidiary would cause it to default on a payment under a contract, the more likely it is that the ‘starvation’ of the subsidiary was intended to cause such default.

C Interference with the Contract

At its barest this requirement is a simple one: the defendant must interfere in some way with the performance of a contract. In early cases this was characterised as the requirement to induce or procure breach of the contract.⁸⁷ However, more recent formulations recognise the tort where there has been inducement or procurement of a failure to perform contractual obligations in a manner that may fall short of a breach that gives rise to an action for damages.⁸⁸

A closer examination of the requirement reveals the following potential complexities:

- whether the tort can be committed by a failure to act;
- distinguishing between direct and indirect interference; and

In *Millar v Bassey* [1994] EMLR 44, 62, Peter Gibson LJ emphasised the point in the context of the tort by stating:

it is necessary that [the defendant’s] conduct must have been directed against the plaintiff in the sense that the breach of [the plaintiff’s] contract or the interference with [the plaintiff’s] interests was intended, rather than being merely what probably would result from [the defendant’s] conduct.

For a critical analysis of the issue generally, see Anthony Kenny, ‘Intention and Purpose in Law’ in Robert Summers (ed), *Essays in Legal Philosophy* (1970) 146.

⁸⁶ Indeed, sufficient knowledge may remain with a corporation even where the natural person through whom knowledge was attributed has resigned as a director or is no longer an employee: *Fightvision* (1999) 47 NSWLR 473, 527 (Sheller, Stein and Giles JJA).

⁸⁷ See, eg, *Lumley v Gye* (1853) 2 E & B 216; 118 ER 749.

⁸⁸ *Torquay Hotel Ltd v Cousins* [1969] 2 Ch 106, 138 (Lord Denning MR); *Allstate Life Insurance* (1995) 58 FCR 26, 43 (Lindgren J); *OBG Ltd v Allan* [2005] QB 762, 775–6 (Peter Gibson LJ).

- where the interference is indirect, determining whether it is relevantly unlawful.

As will be seen, these matters are not conceptually independent of each other. However, an attempt is made to deal with them separately as each might operate individually to preclude holding company liability.

1 *Failure to Act*

It has been stated in the context of potential holding company liability that the tort requires an act rather than a mere omission.⁸⁹ In *LMI Australasia Appeal*, Hodgson JA suggested that the fact that a holding company could have taken steps to prevent its subsidiaries from acting in a certain manner by dismissing directors (or threatening to do so) would not form the basis of an action for interference with contract.⁹⁰

While the distinction between an act and an omission may be clear in extreme cases, it is notoriously slippery in others. A holding company might prevent performance of a contract by its subsidiary by taking steps to strip it of its assets.⁹¹ This should amount to a sufficiently positive act by the holding company to form the basis of liability. On the other hand, a subsidiary may independently take on a contractual obligation and, on learning about the obligation, the holding company may decide not to inject further funds into the subsidiary. In this case it is submitted that there is not a sufficient act of interference. Sitting between these two situations are the facts in *Stocznia Gdanska*, where the holding company set the scene for the subsidiary's financial distress by making the subsidiary financially dependent on it⁹² and then refused to provide the funding necessary for performance of the subsidiary's obligations.

The court in *Stocznia Gdanska* saw no reason to preclude the claim against the holding company on the basis that there was a mere omission. While the refusal to provide funds might be described as a failure to act, it should nevertheless amount to a sufficient interference in some cases. What is crucial is that the refusal to provide funds was not the only conduct of Latvian Shipping that could be causally linked with Latreefers' failure to perform.⁹³ Latvian Shipping was involved in Latreefers' agreement to the specific contractual obligations and

⁸⁹ *LMI Australasia Appeal* [2003] NSWCA 74 (Unreported, Meagher, Hodgson JJA and Young CJ in Eq, 10 April 2003) [11] (Hodgson JA), [101] (Young CJ in Eq). See also Izzo, above n 49, 196.

⁹⁰ *LMI Australasia Appeal* [2003] NSWCA 74 (Unreported, Meagher, Hodgson JJA and Young CJ in Eq, 10 April 2003) [11].

⁹¹ See, eg, *Esso Petroleum Co Ltd v Kingswood Motors (Addleston) Ltd* [1973] 3 All ER 1057; *Einhorn v Westmount Investments Ltd* (1969) 6 DLR (3d) 71.

⁹² [2002] 2 All ER (Comm) 768, 781 (Rix LJ).

⁹³ Professors Harold Luntz and David Hambly provide a useful explanation of the distinction between a 'mere omission' and other failures to act in the context of the tort of negligence. It can be said that there is a 'mere omission' where, 'apart from the defendant's failure to act, there is no conduct on the part of the defendant that is causally linked with the plaintiff's harm': Harold Luntz and David Hambly, *Torts: Cases and Commentary* (5th ed, 2002) 486. This is contrasted with the situation where 'positive conduct on the part of the defendant is causally responsible for the plaintiff's harm, although an omission in the course of that conduct may also be seen as a cause': at 486.

caused Latreefers to take on these obligations while that company was dependent on Latvian Shipping for finance.

It is submitted that in circumstances such as those in *Stocznia Gdanska* there is more than a mere omission and hence holding company liability should be possible in an appropriate case. However, there should not be liability in cases where the holding company is not involved in the subsidiary entering into the relevant contract — even where it knows of its subsidiary's actions.

2 Direct and Indirect Interference

The basic requirement of an interference is complicated by the distinction drawn in the cases between a 'direct' and an 'indirect' interference. There is no adequate test that distinguishes between these types of interference.⁹⁴ An indirect interference with the performance of a contract is actionable, but the interference must be 'unlawful'.⁹⁵ As discussed below, this requirement is difficult to define with any precision.⁹⁶ One explanation for these requirements is that the essence of the tort is an intentional *and* unlawful interference with a contract. It has been said that a 'direct' interference is in itself unlawful;⁹⁷ however, an indirect interference is not,⁹⁸ hence the additional requirement to show that any indirect interference is unlawful.⁹⁹

Therefore, an initial and important question is whether or not a refusal by a holding company to fund a subsidiary's contractual obligations to pay an amount is 'direct' or 'indirect' interference with the contract. In analysing the matter in *Stocznia Gdanska*, the trial judge explored three factual possibilities:

- the directors of the subsidiary were told by the holding company not to perform the subsidiary's obligations under the contract;
- the directors of the subsidiary were not told anything by the holding company but instead simply were not provided with the funds needed to perform the contract; and

⁹⁴ Similar and longstanding difficulties are found in the law of trespass. An act is only trespassory if it involves a direct interference with the interest that is protected. Therefore, it is often said, quite loosely, that trespass can only be committed 'directly' rather than 'indirectly'. However, there is little coherent principle in the cases. For instance, it has been held that the release of oil from a ship did not amount to a direct interference with land when the tide carried the oil ashore: *Southport Co v Esso Petroleum Co Ltd* [1954] 2 QB 182. However, an action did lie where a party piled rubbish near another's land in circumstances where it dried and rolled onto that land: *Gregory v Piper* (1829) 9 B & C 591; 109 ER 220. Of course, the tort of trespass belongs to a different 'family' of tort to interference with contract (which has its roots in action on the case), but the difficulty of distinguishing between direct and indirect interference is common to both.

⁹⁵ *D C Thomson & Co Ltd v Deakin* [1952] Ch 646; *Boral Bricks NSW Pty Ltd v Frost* (1987) 20 IR 70, 79 (Brownie J); *Davies v Nyland* (1975) 10 SASR 76, 99 (Bray CJ).

⁹⁶ See below Part V(C)(3).

⁹⁷ *Australian Liquor, Hospitality and Miscellaneous Workers' Union v Liquorland (Aust) Pty Ltd* (2002) 114 IR 165, 180 (Cooper J).

⁹⁸ *Davies v Nyland* (1975) 10 SASR 76, 98 (Bray CJ).

⁹⁹ This reasoning is uncomfortably circular. For a strong critique of the distinction drawn between direct and indirect interference, see A P Simester and Winnie Chan, 'Inducing Breach of Contract: One Tort or Two?' (2004) 63 *Cambridge Law Journal* 132, 164.

- the directors of the subsidiary were told that funds were not going to be provided in response to the notice that required payment and were instructed that the notice was to be ignored.¹⁰⁰

It appears to be accepted in *Stocznia Gdanska* that only the first of these possibilities would involve a direct interference, suggesting that the starvation of a subsidiary of funds alone could only amount to indirect interference.¹⁰¹ However, it was noted by Rix LJ on appeal that the line between being requested to break the contract and being told to do nothing (and not receiving the funds necessary to perform) is a narrow one and the distinction is ‘puzzling’.¹⁰² Despite this, the trial judge’s analysis was not disturbed on appeal.¹⁰³ In contrast with *Stocznia Gdanska*, there is some case law that suggests that withholding finance can amount to a direct interference.¹⁰⁴ However, this case law has not been accepted in Australia nor does it provide a comprehensive analysis of the issue.

Part of the difficulty in this area is that the case law on the distinction between direct and indirect interference generally is far from conclusive. There is no clear general statement in the cases of what the distinction is (if such a statement is even possible). Some discussions approach the matter by describing what the test is *not*. For instance, in *Davies v Nyland*, Bray CJ, while making it clear that the comments were merely dicta, questioned the correctness of an argument that ‘identifies the distinction between direct and indirect with the distinction between immediate and mediate.’¹⁰⁵ To illustrate, Bray CJ posed the following question:

can it be that if A shoots B with a pistol held in his own hand, he has inflicted a direct injury, but that if he shoots B by grasping a pistol held in the hand of C and pressing C’s finger on the trigger, the injury he has inflicted is only indirect?¹⁰⁶

Perhaps the point being illustrated by Bray CJ is that it is the strength of the causal relationship between act and result that determines whether or not there is a direct interference — rather than merely whether or not a third party features between the actor and the party affected, or whether a number of steps is involved. If this is the correct approach it should be noted that in some cases refusal to provide funds to a subsidiary may be just as likely to cause a subsidiary to breach its obligations as an instruction to that effect.¹⁰⁷ However, it is

¹⁰⁰ See *Stocznia Gdanska SA v Latvian Shipping Co* [2001] 1 Lloyd’s Rep 537, 574 (Thomas J).

¹⁰¹ The trial judge found that the third possibility was the most likely and rejected the argument that there was direct inducement: *ibid* 574–7 (Thomas J). On appeal, Rix LJ considered that this third possibility lay somewhere between the other two: *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 781.

¹⁰² *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 796.

¹⁰³ *Ibid* 798 (Rix LJ).

¹⁰⁴ See *Thermo King Co v Provincial Bank of Canada* (1981) 130 DLR (3d) 256.

¹⁰⁵ (1975) 10 SASR 76, 99.

¹⁰⁶ *Ibid*.

¹⁰⁷ This is because a refusal to provide funds may determine the matter of performance absolutely where, as in *Stocznia Gdanska*, the subsidiary had no other means of raising the funds: [2002] 2 All ER (Comm) 768, 781 (Rix LJ). However, an instruction by a holding company to a director

questionable whether this is (or should be) the correct test, as some case law suggests that withholding something that is essential to perform a contract may only be indirect interference, despite the certainty of nonperformance in this situation.¹⁰⁸

Distinctions drawn in the commentary do not clarify the matter. It is suggested in a leading Australian text that:

Direct interference may be brought about either by words (persuasion or procurement) or by deeds (disabling the person with whom the plaintiff has contracted from continuing with performance of the contract). Indirect interference is, in general, occasioned by the defendant's procurement of others to bring about the disablement of the plaintiff's contract.¹⁰⁹

The generalisations in this quotation are justifiable. It is suggested that the authors' aim was not to set out the test for what is direct or indirect interference but rather to illustrate the types of conduct that have been found to be direct or indirect. However, the quotation suggests that disabling performance in some cases might be direct interference.

While it is difficult to find clear explanations of the distinction between direct and indirect interference, there are clear statements, both in the case law and commentary, about the function of the distinction. As is outlined above, the distinction is drawn to allow the imposition of the added requirement of 'unlawfulness' in some cases. This added requirement can then be relied upon as a method of controlling the expansion of an otherwise potentially expansive tort. Since the test for 'directness' operates as a precondition for any added requirement of 'unlawfulness', the policy justifications for the tests are intertwined. In *Torquay Hotel Co Ltd v Cousins*, Lord Denning MR described the requirement in the commercial context as helping to prevent liability for someone who, through lawful means, 'corners the market',¹¹⁰ even though in doing so the person knows that they might prevent others from performing their contracts.¹¹¹ Similarly, as Peter Cane states, 'the best justification for the requirement of unlawfulness in commercial contexts is to prevent the ordinary use of market power being branded illegal, so as to facilitate and preserve the free market.'¹¹²

Clearly such policy issues are relevant in an action between competitors in a market.¹¹³ However, where the plaintiff and the defendant are not competitors in

of a subsidiary, while persuasive in practice, is subject to the independent exercise of judgement by that director. In theory, a holding company might only control that director's decision through the threat of dismissal (or a refusal to re-elect the director).

¹⁰⁸ See *D C Thomson & Co Ltd v Deakin* [1952] Ch 646, 694 (Jenkins LJ).

¹⁰⁹ Balkin and Davis, above n 1, 642.

¹¹⁰ [1969] 2 Ch 106, 138.

¹¹¹ The justification may vary according to the type of case involved and it is probably worth drawing a distinction between 'commercial' matters and 'employment' matters. See Peter Cane, 'Tortious Interference with Contractual Remedies' (1995) 111 *Law Quarterly Review* 400, where the author states that the requirements in the employment context 'are best explained as the common law's attempt to redress somewhat the imbalance of power between capital and worker arising from the former's ownership of the means of production': at 403.

¹¹² *Ibid* 405.

¹¹³ See, eg, *Independent Oil Industries* (1937) 37 SR (NSW) 394.

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a market the justification is less persuasive. In analysing *Law Debenture Trust Co v Ural Caspian Oil Co Ltd*,¹¹⁴ Cane comments:

[The defendant] was not engaged in ordinary competitive activity — it was not selling goods and services in competition with [the plaintiff] or competing with it for limited business. Why should it matter that what it did was not independently unlawful?¹¹⁵

While these comments were in the context of a case with quite unique facts¹¹⁶ they can be applied with equal force to the circumstance in which a contractor with a subsidiary brings an action against the holding company for starving the subsidiary of funds.¹¹⁷ Perhaps the ‘directness’ and ‘lawfulness’ tests are too firmly rooted to suggest that they simply should be ignored in the context of an intra-group action.¹¹⁸ However, it is submitted that when applying the very flexible and fuzzy ‘directness’ test there is ample scope to bear in mind that the apparent rationale for the test may have little relevance in the corporate group context.¹¹⁹

In summary, *Stocznia Gdanska* suggests that starving a subsidiary of funds is merely indirect interference. However, the case also noted the flexibility of the test and it was commented that the defendant had acted in a manner that ‘could not have been far from’ direct interference.¹²⁰ Therefore, it appears that there is sufficient uncertainty and flexibility in the test for a future finding that the same or similar interference is ‘direct’. Room for such a finding is enhanced by the fact that the apparent rationale behind the requirement may not be particularly relevant to a claim against a holding company.

3 *Is the Interference Unlawful?*

If it is decided that a holding company has interfered with its subsidiary’s contract but only indirectly, it must then be determined whether or not such interference was unlawful. Again, this raises problems of definition: what in this context is unlawful?

¹¹⁴ [1995] 1 All ER 157.

¹¹⁵ Cane, above n 111, 405–6.

¹¹⁶ The case involved an action in tort against a company that was controlled by the same entity that controlled another company that had contracted with the plaintiff. It was not a case about starving a subsidiary of funds. Rather, dealings between several commonly controlled companies gave rise to the question of whether it is tortious to deprive intentionally a person of an opportunity to make a claim for interference with contract: *Law Debenture Trust Co v Ural Caspian Oil Co Ltd* [1995] 1 All ER 157.

¹¹⁷ This ignores the convoluted situation where the defendant holding company was in competition with the contractor for the subsidiary’s goods or services.

¹¹⁸ The High Court in *Zhu* described the elements of the tort as being ‘well-settled’ in Australian law: (2004) 218 CLR 530, 577 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ). For the time being, structural changes to the tort in Australia seem unlikely, not least for the reasons recently given by Carnwath LJ in *OBG Ltd v Allan* [2005] QB 762, 799: ‘the boundaries of economic torts are a sensitive area in which it is difficult to anticipate the consequences of re-definition.’

¹¹⁹ Additional reasons may exist for keeping a tight rein on the tort in the intra-group context: see below Part VI.

¹²⁰ *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 804 (Rix LJ).

Some commentators describe this requirement in terms that require the relevant act to be ‘*independently* unlawful’.¹²¹ This highlights one curious aspect of the test: the facts that make the interference independently unlawful might have little to do with the relationship between the plaintiff and the defendant holding company. This might lead to liability turning on ‘fictitious and, from a practical viewpoint, even irrelevant factors.’¹²²

In *Stocznia Gdanska*, Rix LJ analysed what made an unlawful act ‘relevant’. There it was decided that the unlawful means must be more than ‘a merely incidental or collateral failure’.¹²³ Rix LJ stated that ‘[t]he issue might be put in terms of the importance and relevance of the causative nexus between the unlawful means in question and the intention to procure the breach of the contracts’.¹²⁴

The unlawful act (the breach by Latvian Shipping of its agreement with Capco to keep Latreefers in funds)¹²⁵ was found to be relevantly unlawful because Rix LJ regarded it as

impossible to think of the proper financing of Latreefers under the Capco terms as an incidental matter, or insufficiently connected with [Latvian Shipping’s] intentions towards Latreefers and its contracts with [Stocznia]. Moreover, when it came to [Latvian Shipping’s] strategy for dealing with those contracts, it did not merely decide to withdraw its financial support for Latreefers: it deliberately used the withdrawal of its financial support as the means to bring about the destruction of those contracts ...¹²⁶

This causation-based approach would be successful in weeding out obviously irrelevant factors. For example, it would not be sufficient if the directors of the holding company made their decision not to fund the subsidiary during a meeting that was held in breach of workplace safety requirements. However, in holding a matter to be relevantly unlawful because it provided the intended means of interference, the test does not address the fact that the unlawfulness of the means may arise from factors that do not flow from the relationship between the plaintiff and the defendant holding company.¹²⁷

In *Stocznia Gdanska* the Capco agreement formed part of the retainer of the professional service company that provided the Isle of Man directors for the subsidiary.¹²⁸ While the terms of that agreement might be said to be relevant to the interests of the plaintiff and the defendant, given they required the subsidiary to be kept in funds, presumably the terms were simply insisted upon by the service company in order to provide some insulation to the directors against a claim for insolvent trading, rather than for the benefit of a creditor. It is unlikely

¹²¹ See, eg, Fleming, above n 1, 760 (emphasis added); Cane, above n 111, 405–6 (emphasis added).

¹²² Fleming, above n 1, 761.

¹²³ *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 802.

¹²⁴ *Ibid.*

¹²⁵ See above n 27 and accompanying text.

¹²⁶ *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 802.

¹²⁷ In a dissenting judgment in *OBG Ltd v Allan* [2005] QB 762, 786, Mance LJ appeared to adopt a similar (but perhaps broader) test of whether or not the unlawful act had an *effect* on the relevant contracts.

¹²⁸ [2002] 2 All ER (Comm) 768, 774 (Rix LJ).

that Stocznia knew of the agreement, let alone relied upon it, and from the perspective of Stocznia the agreement's existence was merely fortuitous.

Presumably the result of the case would have been different if Latreefers was incorporated in the same jurisdiction as its holding companies and had directors from within the corporate group who did not insist upon any form of undertaking from the parent companies.¹²⁹ Thus, with the slightest change of facts — a change that might have little to do with the interaction between the plaintiff and the defendant — liability might not be found. It is this type of unpredictability that has led to the test being described as unsatisfactory.¹³⁰

In summary, the test for what is relevantly unlawful is neither clear nor satisfactory. There is nothing inherently unlawful about refusing to provide finance to a subsidiary. Therefore, if it is decided that this can only amount to indirect interference, holding company liability for the tort might depend upon finding unlawfulness in factors that are only loosely connected with the relationship between the plaintiff and the defendant.

D *Damage*

The final matter that must be shown by a plaintiff is that the defendant's interference caused the relevant damage to the plaintiff. It is clear that the tort is not actionable per se.¹³¹ It was stated recently that 'in order to complete the cause of action there must be special damage, ie more than nominal damage caused to the claimant by the breach of contract'.¹³² If such damage (and the elements above) can be shown, the only issue that remains is the defence of justification.

E *Justification*

A party may interfere with the performance of another's contract if it is justified in doing so. The defence of justification has long been recognised as applying to the tort and is possibly the only applicable defence.¹³³ In *Zhu* the High Court addressed in detail the matter of what the proper formulation of the test of justification should be.¹³⁴

The High Court looked to the analysis of Jordan CJ in *Independent Oil Industries*.¹³⁵ This analysis suggests that an interference can only be justified where

¹²⁹ This appears to have been noted by counsel for Stocznia: see *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 802 (Rix LJ).

¹³⁰ Fleming, above n 1, 761.

¹³¹ *Zhu* (2004) 218 CLR 530, 584–5 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ); *Independent Oil Industries* (1937) 37 SR (NSW) 394, 414 (Jordan CJ).

¹³² *Australian Liquor, Hospitality and Miscellaneous Workers' Union v Liquorland (Aust) Pty Ltd* (2002) 114 IR 165, 180 (Cooper J), citing *Greig v Insole* [1978] 3 All ER 449, 484–5 (Slade J).

¹³³ *Independent Oil Industries* (1937) 37 SR (NSW) 394, 415 (Jordan CJ).

¹³⁴ The appeal to the High Court was argued only on the basis of justification: (2004) 218 CLR 530, 546 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ). For a description of the facts of the case and a general discussion of the decision, see Louise Jarrett and Kanaga Dharmananda, 'Interfering with Contracts: Limits on the Justification Defence' (2005) 33 *Australian Business Law Review* 142.

¹³⁵ (1937) 37 SR (NSW) 394.

the party that interferes has ‘an actually existing superior legal right’.¹³⁶ The High Court accepted this approach, at least in the application of the tort outside the context of employment relationships.¹³⁷ This left the Court to consider what such a ‘superior legal right’ might be. It was decided that a competing contractual right would not be superior, even where it was prior to the contractual rights with which there was interference.¹³⁸ Instead, it is the nature of the right that must be examined to determine its superiority. Relevant superiority is established if the right is proprietary in nature or is found in statute.¹³⁹ A proprietary right would be superior because the competing contractual right is at most ‘quasi-proprietary’.¹⁴⁰

In determining that the test for justification relies upon the finding of some form of proprietary right, the High Court also clarified what the test is *not*. The test in Australia does not involve ‘a discretionary “balancing” of social and individual interests’.¹⁴¹ This is in contrast with the test in England which looks to whether or not the defendant was ‘carrying out a legal, moral or social duty.’¹⁴² The High Court also held that the defence is not made out merely by the defendant demonstrating a desire to further or protect its own interests.¹⁴³

Finally, the High Court found that it is not enough merely to have an actually existing superior legal right. In order to be justified in interfering, a party must be doing no more than is reasonably necessary to protect that right.¹⁴⁴ This

¹³⁶ Ibid 416.

¹³⁷ *Zhu* (2004) 218 CLR 530, 579–80 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ). The High Court found it unnecessary to consider whether the test would also apply in the employment context.

¹³⁸ Ibid 587 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ).

¹³⁹ Ibid 582 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ).

¹⁴⁰ Ibid 580 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ). The High Court here was making reference to the notion of ‘quasi-proprietary’ rights that was explored by Kitto J in *A-G (NSW) v Perpetual Trustee Co Ltd* (1952) 85 CLR 237, 294–5. The High Court acknowledged that such a distinction is not clear and

seems to rest on the view that proprietary rights are stronger than quasi-proprietary rights in that while the former are marked by a combination of characteristics like alienability of benefit and burden and a right to exclusive possession or use enforceable against the world ... quasi-proprietary rights do not have the totality of those characteristics.

Zhu (2004) 218 CLR 530, 573 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ).

¹⁴¹ *Zhu* (2004) 218 CLR 530, 570–1 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ).

¹⁴² Howarth, above n 49, 195. In *Stoczniak Gdanska* the Court of Appeal stated that the law on justification in England ‘has not been clearly worked out’ and referred only generally to the possibility that ‘moral or perhaps economic factors’ may mitigate actions to the point of removing liability: [2002] 2 All ER (Comm) 768, 804 (Rix LJ). David Howarth argues in favour of a similarly unstructured but broader approach based on whether or not the interference was ‘fair, just and reasonable’: Howarth, above n 49, 225, 232. A somewhat similar argument was rejected in *Zhu*, where the defendant argued unsuccessfully for the defence to be based on whether the relevant conduct was done ‘without just cause or excuse’: (2004) 218 CLR 530, 566 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ). For an earlier critical analysis of the English position, see generally Richard O’Dair, ‘Justifying an Interference with Contractual Rights’ (1991) 11 *Oxford Journal of Legal Studies* 227.

¹⁴³ *Zhu* (2004) 218 CLR 530, 571 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ). Contrast this with the approach in the United States where it appears that the justification defence may be available to a holding company on the basis that it should be permitted to protect its financial interest in its subsidiary: Izzo, above n 49, 196.

¹⁴⁴ *Zhu* (2004) 218 CLR 530, 587–8 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ). Again, the High Court drew upon the reasoning of Jordan CJ in *Independent Oil Industries* (1937) 37 SR (NSW) 394, 415.

involves contemplation of ‘how a reasonable and prudent person or body in ... [the defendant’s] position would have behaved’.¹⁴⁵

Reliance on concepts of property has some interesting consequences in the context of an action against a holding company. As a starting point it must be recognised that the holding company will have some proprietary rights through its shares in the subsidiary.¹⁴⁶ However, it is submitted that this is not the appropriate right with which to undertake a comparison with the third party contractor’s rights.

The rights held in the shares of the subsidiary cannot be said to be rights that compete directly with the third party’s right to performance. While the performance of the subsidiary’s contract might affect the value of the holding company’s property, it will not ordinarily interfere with the holding or enjoyment of that property. Besides, if the shares in the subsidiary amounted to the necessary proprietary interest, *prima facie* the defence would always be available to a holding company (subject to whether the interference is reasonably necessary). This result is difficult to support. It is submitted that the more appropriate approach is to look for proprietary rights of the holding company that compete more directly with those of the plaintiff contractor, such as rights, if any, in the subject matter of the subsidiary’s contract.¹⁴⁷

The fact that a holding company generally has no proprietary interest in the property of its subsidiary¹⁴⁸ then forms a natural impediment to the availability of the defence. Further, there is no general statutory provision that gives a holding company the right to interfere with the performance of its subsidiary’s contracts.

In summary, the High Court’s formulation of the justification defence in non-employment cases is significant for a number of reasons including:

- the fact that it demonstrates divergence from the English approach, which is based on a broader enquiry into the merits of the interference; and
- the apparent difficulties that will arise for holding companies seeking to use the defence in the context contemplated in this article, because the separate legal entity principle will tend to prevent the holding of the required rights.¹⁴⁹

¹⁴⁵ *Zhu* (2004) 218 CLR 530, 588 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ).

¹⁴⁶ Indeed, in its analysis of the defence of justification in *Zhu* the High Court made reference to the rights of an owner of a share being proprietary rather than quasi-proprietary: *ibid* 573 (Gleeson CJ, Gummow, Kirby, Callinan and Heydon JJ).

¹⁴⁷ For example, such rights might arise from security interests held by a holding company over assets that are affected by the contract.

¹⁴⁸ *Macaura v Northern Assurance Co Ltd* [1925] AC 619, 626–7 (Lord Buckmaster).

¹⁴⁹ It is interesting to contemplate here the fact that the corporate veil might work in some small way *towards* holding company liability rather than in its more familiar role in *preventing* such liability.

VI THE BREADTH OF THE APPLICATION OF THE TORT IN THE CORPORATE GROUP CONTEXT

The exploration above reveals that the elements of the tort contain significant flexibility. It also reveals that there is uncertainty in the application of the tort to a holding company that starves its subsidiary of funds. In particular:

- there is uncertainty about when a failure to fund a subsidiary would amount to a sufficiently positive act to be an interference;
- there is significant malleability in the test for whether the interference is direct and, despite *Stocznia Gdanska*, there is scope for a future finding that the ‘starving’ of a subsidiary by a holding company is a direct interference with its subsidiary’s contracts; and
- determining what is relevantly unlawful in a given case may depend upon unpredictable factors that are not immediately relevant to the dealings between the plaintiff and the defendant.

This flexibility is such that in Australia there is potential for the application of the tort in circumstances similar to *Stocznia Gdanska*, or even beyond, without the need to modify any of the elements of the tort. As was acknowledged in *Stocznia Gdanska*, the flexibility of these elements may be a strength. Commenting on the elements, Rix LJ stated:

These considerations are designed to keep a wide-ranging tort within bounds. It is therefore important that they are not applied mechanically and that regard is had to the balancing demands of moral constraint and economic freedom. For these purposes the concepts of knowledge and intention, direct participation, the causative relevance of unlawful means, and the possibilities of justification, are presumably sufficiently flexible to enable the principles of the tort to produce the right result.¹⁵⁰

The question then arises: should this flexibility be used to expand the scope of the application of the tort to holding companies that starve their subsidiaries of funds? Or has *Stocznia Gdanska* already travelled too far down this path? In addressing these questions it is appropriate to consider the general demands that need to be balanced.

On the most basic level, the tort reflects the sentiment that ‘contracts should be kept rather than broken.’¹⁵¹ However, balanced against this should be the knowledge that the expansion of the tort could act to ‘undermine the distribution of benefits and burdens established by another area of law.’¹⁵² In particular, the application of the tort to a holding company could have the practical effect of

¹⁵⁰ [2002] 2 All ER (Comm) 768, 804. Although it should be noted that *Zhu* (2004) 218 CLR 530 sets down a less flexible framework for the defence of justification in Australia.

¹⁵¹ *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 803 (Rix LJ). However, note Howarth’s claims that justifications of the tort based on such arguments are built on ‘flawed assumptions’: Howarth, above n 49, 207.

¹⁵² Howarth, above n 49, 227. See also Izzo, above n 49, 197. As Peter Gibson LJ notes in *Millar v Basse* [1994] EMLR 44, 64, one significant concern is that the expansion of the tort may undermine the rule of privity of contract: see discussion of this case in *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 803 (Rix LJ).

eroding the limited liability of the holding company. This concern, rather than concerns about impeding ordinary competition, should be primary when considering the application of the tort to holding companies.

Finding the point at which the principle of limited liability should yield to other pressures is difficult. Few coherent principles have developed in the doctrine on lifting the veil.¹⁵³ It has been argued with force that many of the justifications for limited liability are of limited relevance when applied to constituent companies of corporate groups, particularly in wholly owned structures.¹⁵⁴ A particular justification that may survive in the corporate group context is one of the original and most significant arguments in favour of limited liability: that it will encourage economic activity through risk-taking ventures that otherwise might not be undertaken.¹⁵⁵ This complicates the balancing exercise for two main reasons. First, it raises the prospect that one must attempt to balance broad arguments in favour of promoting economic activity generally against the fairness of a dealing to an individual party affected by the corporation or against the culpability of an individual party adopting the device of incorporation.¹⁵⁶ Second, a related problem is that there is not yet any convincing way of measuring the economic benefits to society of maintaining limited liability between a holding company and its subsidiary.

Despite these difficulties, it has been suggested that limited liability should yield where there has been undercapitalisation of a subsidiary.¹⁵⁷ While such undercapitalisation may be relevant to the finding of agency using the formulation in *Smith, Stone & Knight*,¹⁵⁸ in the United States it appears to take on a more significant role in the ‘veil lifting’ cases,¹⁵⁹ particularly in cases involving

¹⁵³ In a widely quoted passage, Rogers AJA stated ‘there is no common, unifying principle, which underlies the occasional decision of courts to pierce the corporate veil.’: *Briggs v James Hardie & Co Pty Ltd* (1989) 16 NSWLR 549, 567.

¹⁵⁴ Phillip I Blumberg, ‘Limited Liability and Corporate Groups’ (1986) 11 *Journal of Corporation Law* 573, 623–6; Ian M Ramsay, ‘Holding Company Liability for the Debts of an Insolvent Subsidiary: A Law and Economics Perspective’ (1994) 17 *University of New South Wales Law Journal* 520, 536–7.

¹⁵⁵ Phillip I Blumberg, *The Multinational Challenge to Corporation Law: The Search for a New Corporate Personality* (1993) 125. Interestingly, the arguments about risk-taking have common roots with policy concerns about preventing the tort from restricting competition. Ultimately, both are based on a desire to avoid stifling economic activity.

¹⁵⁶ The point is illustrated dramatically (in the context of tort liability) by contemplating the facts of *Briggs v James Hardie & Co Pty Ltd* (1989) 16 NSWLR 549, 557 (Rogers AJA). How could it be explained to the survivors of Mr Briggs — an illiterate, negligently killed employee of an asbestos mining business — that his death should not be compensated because to do so would offend the principle of limited liability and potentially hamper economic activity?

¹⁵⁷ Blumberg, *Multinational Challenge*, above n 155, 86; John Farrar, *Corporate Governance in Australia & New Zealand* (2001) 251.

¹⁵⁸ [1939] 4 All ER 116, 121 (Atkinson J).

¹⁵⁹ Phillip I Blumberg, *The Law of Corporate Groups: Tort, Contract, and Other Common Law Problems in the Substantive Law of Parent and Subsidiary Corporations* (1987) 465–6. For a useful summary of the law based on Professor Blumberg’s work, see Ian Ramsay’s memorandum in the Submission to Special Commission of Inquiry into the Medical Research and Compensation Foundation, 14 July 2004, attachment A (The Medical Research and Compensation Foundation, MRCF (Investments) Pty Ltd, Amaca Pty Ltd and Amaba Pty Ltd).

contractual obligations rather than tortious liability.¹⁶⁰ In such cases the failure to provide adequate capital for a subsidiary corporation to carry on its intended business¹⁶¹ may alone allow the court to lift the corporate veil.¹⁶² However, the matter is far from settled.¹⁶³ Interestingly, the undercapitalisation itself may not be the ultimate justification for removal of limited liability in these cases. Rather, undercapitalisation may be seen as a form of misleading conduct towards creditors.¹⁶⁴ Therefore, a creditor who has contracted with an undercapitalised subsidiary knowing of its financial vulnerability might find it difficult to argue for lifting the veil.¹⁶⁵ To adapt the words of Lord Macnaghten in *Salomon v Salomon & Co Ltd*, provided such creditors are voluntary they have nobody to blame but themselves for their misfortunes.¹⁶⁶

In this regard the plaintiff in *Stocznia Gdanska* did not start from the highest moral ground. The plaintiff negotiated for a significant contract with a company of apparent substance, yet allowed the arrangement to proceed with a newly formed subsidiary without seeking a guarantee from the holding company.¹⁶⁷ Despite the fact that the defendant holding company also was not without blame (having acted upon an intention to interfere with a contract) it is questionable whether limited liability should give way in such a case when the plaintiff was not misled and had clear options available to protect itself.¹⁶⁸ If anything, *Stocznia* was in a better position to protect its interests than the unsophisticated trade creditors of *Salomon & Co Ltd*.

It is submitted that, from a policy perspective, *Stocznia Gdanska* is not the most deserving case in which to 'sidestep' the corporate veil (which may potentially reduce desirable risk-taking economic activity). Any application of *Stocznia Gdanska* in Australia in the corporate group context should be done

¹⁶⁰ Blumberg, *Tort, Contract and Other Common Law Problems*, above n 159, 225, 465. A strong theme in Professor Blumberg's writing is that the mixing of jurisprudence on lifting the veil in contract matters and tort matters is 'unacceptable': at 108–9.

¹⁶¹ The emphasis in the cases is on the initial capitalisation of the corporation. The depletion of a subsidiary's capital through ordinary business transactions (in contrast with deliberate asset stripping) is not as persuasive a factor in favour of lifting the veil between holding company and subsidiary: see Lynn M LoPucki, 'The Death of Liability' (1996) 106 *Yale Law Journal* 1, 22–3; Blumberg, *Tort, Contract and Other Common Law Problems*, above n 159, 470–2.

¹⁶² Blumberg, *Tort, Contract and Other Common Law Problems*, above n 159, 465–6.

¹⁶³ See LoPucki, above n 161, 22–3. See also Phillip I Blumberg and Jonathan Fowler, *The Law of Corporate Groups: Problems in the Bankruptcy or Reorganization of Parent and Subsidiary Corporations, Including the Law of Corporate Guaranties — 1992 Supplement* (1992) 264–8 for a discussion of a number of bankruptcy cases in the United States where it was found that undercapitalisation must be accompanied by another factor such as fraud in order to justify lifting the veil between holding company and subsidiary.

¹⁶⁴ Blumberg, *Tort, Contract and Other Common Law Problems*, above n 159, 472.

¹⁶⁵ *Ibid.*

¹⁶⁶ [1897] AC 22, 53.

¹⁶⁷ In this manner, the position of a typical contract creditor can be contrasted with the more vulnerable tort victim, who will normally have no chance to consider the financial substance of the tortfeasor before becoming a contingent creditor: see Hansmann and Kraakman, above n 9, 1919–20; Blumberg, *Multinational Challenge*, above n 155, 135–6.

¹⁶⁸ See Phillip I Blumberg, *The Law of Corporate Groups: Problems in the Bankruptcy or Reorganization of Parent and Subsidiary Corporations, Including the Law of Corporate Guaranties* (1985) 599, where Professor Blumberg states that the refusal to lift the corporate veil 'is obviously sound where creditors have bargained for the credit of a particular component of a group without reliance on the credit of other components of the group.'

cautiously. The mere fact of undercapitalisation should not be enough to justify the effective removal of limited liability in such cases, particularly where the creditor had reason to suspect the undercapitalisation. As a tentative starting point, the tort should not be allowed to expand beyond the *Stocznia Gdanska* situation unless the contract creditor is vulnerable in the sense that it had no practical opportunity to manage its credit risk.¹⁶⁹ It is not suggested that vulnerability of the plaintiff should be another formal element or requirement of the tort. However, in utilising the flexibility of the elements of the tort to get the 'right result'¹⁷⁰ the vulnerability of the plaintiff is a relevant policy consideration. Where the plaintiff is a large, sophisticated contract creditor, the defendant's behaviour should be particularly blameworthy before this should be allowed to outweigh the longstanding argument that limited liability brings broader economic benefits, at least until there is clearer evidence that such benefits are illusory.

VII CONCLUSION

The tort of interference with contract could provide a useful remedy against a solvent holding company as an alternative to a hollow remedy in contract against an insolvent subsidiary. As illustrated by *Stocznia Gdanska*, the tort may apply where a holding company starves its subsidiary of funds. The scope of the tort in this context (and generally) is uncertain because of the malleability of its elements. This flexibility could allow the tort to expand significantly as a remedy against holding companies. However, any such expansion should be cautious and its effect on limited liability should be acknowledged. It is particularly difficult to justify an expanded application of the tort as a means of sidestepping limited liability where the contracting party had the ability and opportunity to protect its own interests through means such as a parent company guarantee.

¹⁶⁹ For a discussion of contract creditors who might be vulnerable in this sense, see Blumberg, *Multinational Challenge*, above n 155, 136–7. Professor Blumberg suggests that the practical opportunity to bargain over credit typically is missing in 'employment contracts, retail consumer purchases, and in small trade contracts': at 137.

¹⁷⁰ *Stocznia Gdanska* [2002] 2 All ER (Comm) 768, 804 (Rix LJ).