

Liability of Dominant Corporation for Acts of Subsidiary

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upon its discovery.²⁴ But as was said in *Weill v. Weill*,²⁵ "The rule now seems to be that if the fraud be such that had it not been practiced the contract would not have been made, or the transaction of marriage completed, then it is material (*error substantialis*); but if it be shown or made probable that the same thing would have been done by the same parties in the same way if the fraud had not been practiced, it cannot be deemed material (*error accidentalis*)." The materiality of the fraud practiced should not only determine whether the defrauded party is entitled to relief, but from the *Weill* case, *supra*, it should be asked would the marriage have taken place had the fraud not been practiced. If the answer is in the negative then the plaintiff is entitled to relief.

L. L. W.

LIABILITY OF DOMINANT CORPORATION FOR ACTS OF SUBSIDIARY.

The advantages of conducting a business in the corporate style are probably legion, and the limited liability obtained through the use of this "form" is undoubtedly one of the chief inducements to persons to adopt this method. In this connection, the question of liability of the parent corporation for acts of its subsidiary is worthy of consideration and the recent decision of the Court of Appeals in *Berkey v. Third Avenue R. Co.*¹ presents excellent material for a discussion of this interesting proposition.

Plaintiff, alighting from a street car, sustained injuries by reason of the motorman's negligence. The franchise to operate cars over the route used by plaintiff was owned exclusively by the Forty-second Street, Manhattanville and St. Nicholas Railway Co., but the car upon which plaintiff was riding bore the inscription "Third Ave. System," was owned by it and leased to the Forty-second Street Co. It was against the Third Ave. System that plaintiff prosecuted her action. She sought to charge it with liability by the establishment at the trial of facts showing that substantially all the stock of the Forty-second Street Co. was owned by it; that the same persons were officers of both companies and that the two boards of directors were almost identical in membership.

Plaintiff's argument was that defendant controlled the operations of the Forty-second Street Co. and was the real owner thereof dis-

²⁴ "The aggrieved party must act promptly upon discovery or the relief will not be afforded. In this respect at least the parties are bound by the same rules governing the rescission of contracts in equity, and the greatest diligence is required of plaintiff." *Butler v. Butler*, *supra*, note 22, *Wallich v. Wallich*, N. Y. L. J., June 12, 1925.

²⁵ 104 Misc. 561, 562, 172 N. Y. Supp. 589 (Sup. Ct., 1918)

¹ 244 N. Y. 84, 155 N. E. 58 (1926)

guising such ownership by use of the "corporate veil"² in the hope that it would prove an effective barrier to claims for damages.

Defendant contended that ownership of a controlling interest in the stock of the Forty-second Street Co. did not make it liable for the operations of that Company³ and succeeded in having the complaint dismissed, but the Appellate Division, holding that there was a question for the jury, ordered a new trial, from which order defendant appealed. The order of the Appellate Division was reversed.

The judges of the Court of Appeals were not unanimous in their decision for defendant, Judge Crane writing a dissenting opinion in which Judge Pound concurred. The prevailing opinion written by Judge Cardozo states that the Court is unable to satisfy itself that the alleged dominion was exerted. It points out that the books of account, records, etc., were at all times maintained separate and distinct from those of the parent corporation. The law "does not prohibit stock ownership, or at least did not so far as the record shows, when the defendant bought the shares."⁴ But to sustain plaintiff's theory it would be necessary for the Court to presume the existence of a contract between the two corporations. Such a contract, if made, would be illegal unless approved by the Public Service Commission.⁵ Therefore, says the Court:

"We cannot believe that an agreement criminal in conception * * * may be inferred from conduct or circumstances so indefinite and equivocal."⁶

² Plaintiff sought to come within the rules laid down in:

Anthony v. American Glucose Co., 146 N. Y. 407, 41 N. E. 23 (1895); *C. M. & St. P. v. Minn.*, 247 U. S. 490 (1918); *Crown Cork & Seal Co. v. Brooklyn Bottle Co.*, 190 Fed. 323 (E. D. N. Y., 1911); *Davis v. Alexander*, 269 U. S. 114 (1926); *Foard Co. v. State*, 219 Fed. 827 (C. C. A. 4th, 1914); *Lehigh Valley R. Co. v. Delachesa*, 145 Fed. 617 (C. C. A. 2nd, 1906); *Lehigh Valley R. Co. v. Dupont*, 128 Fed. 840 (C. C. A. 2nd, 1904); *Luckenbach v. Grace*, 267 Fed. 676 (C. C. A. 4th, 1920); *Otway v. Snare & Triest Co.*, 167 App. Div. 128, 152 N. Y. Supp. 845 (2nd Dept., 1915); *Summo v. Snare & Triest Co.*, 166 App. Div. 425, 152 N. Y. Supp. 29 (2nd Dept., 1915); *The Willem Van Duell, Sr.*, 252 Fed. 35 (C. C. A. 4th, 1918); *Wilkinson v. Walker*, 294 Fed. 939 (N. D. Texas, 1923).

³ Defendant's case found support in:

Demarest v. Flack, 128 N. Y. 205, 28 N. E. 645 (1891); *Doran v. N. Y. I. Co.*, 239 N. Y. 448, 147 N. E. 62 (1925); *Elenkueg v. Sibrecht*, 238 N. Y. 254, 144 N. E. 519 (1924); *Matter of Vannia v. Anti-Saloon*, 238 N. Y. 457, 144 N. E. 679 (1924); *Stone v. C. C. & St. L.*, 202 N. Y. 352, 95 N. E. 816 (1911).

⁴ *Supra*, note 1, at 91.

⁵ N. Y. Publ. Serv. Comm. L., § 54.

⁶ *Supra*, note 4.

Plaintiff, though citing several New York cases,⁷ relies principally upon Federal authorities,⁸ chief of which is *Davis v. Alexander, et al.*,⁹ holding that where one railroad controlled another, and operated both as a single system, and the Director General, after taking them over, pursued the same practice, damages to freight occurring on the subsidiary line, are recoverable against the Federal Agent, as in charge of the dominant carrier.

Of the New York cases, *Summo v. Snare & Triest Co.*¹⁰ probably furnishes the best support to plaintiff's argument. Plaintiff, while in the employ of The Steel and Masonry Contracting Co., was injured during the course of his employment. He contended that the Steel and Masonry Contracting Co. was a mere "dummy" organized and controlled by defendant, Snare & Triest Co., to perform a definite part of its work. It was held that the question whether or not the "Snare & Triest Company was the real principal and the Steel & Masonry Company but an * * * instrument," was properly submitted to the jury.¹¹

Should the parent corporation be held liable for the acts of the subordinate? There is an abundance of authorities both ways.

As to contractual matters, though they are properly within the scope and purview of this article, the writer purposes to content himself with a reference to the divergence of opinion¹² and confine his writing to the treatment of negligence as pertinent to the subject case.

There are numerous cases wherein the dominant corporation was held responsible for its subsidiary's negligence¹³ and just as many to the contrary.¹⁴ However, in the former class of cases, judgment was invariably predicated upon grounds other than those presented in this instance; fraud, agency or an illegal contract entered into the determination of the rights of the litigants. Satisfactory proof of the

⁷ New York cases cited in note 2, *supra*.

⁸ Federal cases cited in note 2, *supra*.

⁹ *Supra*, note 2.

¹⁰ *Supra*, note 2.

¹¹ *Ibid.* 429.

¹² *Ballantine, Separate Entity of Parent and Subsidiary Corporation* (1926) 14 Calif. L. Rev. 12, 15; (1927) 40 Harv. L. Rev. 1011, 1012.

¹³ *Gulf, C. & S. F. Ry. Co. v. Cities Service Co.*, 281 Fed. 214 (C. C. A. 2nd, 1922); *United Laundries Co. v. Bradford*, 133 Md. 363, 150 Atl. 303; *Supra*, note 12, 14 Calif. L. Rev. at p. 15, and cases therein cited.

¹⁴ *Union Sulphur Co. v. Freeport Texas Co.*, 251 Fed. 634, 661 (Del., 1918); *Stone v. Cleveland*, *supra*, note 3; *Bethlehem Steel Co. v. Raymond Concrete*, 141 Md. 67, 118 Atl. 279 (1922); and cases cited in note 3, *supra*.

existence of any one of these would undoubtedly be sufficient to influence the Court to decide without hesitation in plaintiff's favor. But here the plaintiff proceeded solely upon the theory of control. She did not attempt to show fraud or agency, nor raise the question of illegality, though the court considered this last point in its opinion. It seems quite certain that stock ownership alone is insufficient nor does the added feature of identity in officers and directors change the situation. "The mere fact that the parent corporation owns all the stock of the subordinate corporation * * * does not make them the same in law. There must be something in addition to mere unity of interest and ownership."¹⁵

In Thompson's work on Corporations, Third Edition, the author after stating the general rule (Section 5485) proceeds:

" * * * and hence a railroad company which is lawfully a stockholder only in a connecting railroad is not liable for the negligence of the connecting railroad."¹⁶

So also in Fletcher's Cyc. Corporations, at Section 3988.

"Ownership of a majority of the shares of a corporation by another company does not affect the separate existence of the two companies * * * and each will be presumed to be managed in its own interest."¹⁷

The opinion of the Court of Appeals clearly indicates that despite the *element* of control obtained through stock ownership, the Courts of this State will not fasten liability upon the parent corporation so long as the separate existence of the two companies is not clouded by a merger of funds and the interchanging of employees and equipment of the respective lines. There may exist a desire for mutual benefit and welfare by reason of their close relationship, and this may be evidenced by a very high degree of co-operation which, however, does not amount to the control of one by the other, nor subject one to liability for acts of the other.

J. A. M.

¹⁵ *Supra*, note 12, 14 Calif. L. Rev. 12, 17. In an action to oust defendants from charter on ground that one corporation had acquired stock and was conducting the business for which others were incorporated, held that stock ownership enables corporation to influence the policy of other corporation, but that is not taking management of business into its own hands, *State v. Missouri Pac. R. Co.*, 237 Mo. 338, 141 S. W. 643 (1911).

¹⁶ *Atchison, T. & S. F. R. Co. v. Cochran*, 43 Kansas 225, 23 Pac. 151 (1890), a corporation which controlled and operated a business through another corporation is liable for injuries caused by the latter.

¹⁷ *Pullman's Palace Car Co. v. Missouri Pac. R. Co.*, 115 U. S. 587, 29 L. Ed. 499 (1885); *Missouri Pac. R. Co. v. Bolling*, 66 Ark. 646, 48 S. W. 806 (1898); *Bigelow v. Calumet & H. Nim. Co.*, 167 Fed. 721 (C. C. A. 6th Cir. 1909). See also *Fletcher's Cyc. Corporations* § 1133.