Goodmans LLP Update

U.K. Supreme Court Opens Door to Broader Scope of Liability of Parent Company for Subsidiary's Operations

In its recent decision in *Vedanta Resources PLC v. Lungowe*, the Supreme Court of the United Kingdom (which is the highest appellate court in the U.K.) signalled a broadening of liability that a parent company may have to third parties who are harmed by the actions of a subsidiary.

Background

The dispute arose out of a mining operation in Zambia. Local residents allege that discharges of toxic materials from the mine polluted local watercourses, rendering their water supply unsafe. The owner of the mine – Konkola Copper Mines plc ("KCM") – is a company incorporated in Zambia and some questions were raised in the evidence as to its solvency. The Zambian government has a minority stake in KCM, but KCM's majority (and controlling) shareholder is part of a multinational group of companies, whose ultimate parent is a U.K. company, Vedanta Resources PLC. Vedanta itself has only 19 employees. However, its direct and indirect subsidiaries employ in excess of 80,000 people worldwide.

The plaintiffs have sought damages from both KCM and Vedanta for negligence. The claim against KCM is, as is to be expected, based on its operation of the mine. As for the claim against Vedanta, it is based on the "high level of control and direction" that Vedanta allegedly exercised over the mining operations of its subsidiary, which control and direction are alleged to give rise to a duty to care owed directly by Vedanta to the plaintiffs. More specifically, the claim alleges that Vedanta's supervision and control of the mine are evidenced by, among other things, public statements proclaiming Vedanta's group-wide environmental controls and sustainability standards, and by Vedanta's implementation of those controls and standards throughout the corporate group by training, monitoring and enforcement.

The defendants brought a motion to dismiss the claim on jurisdiction grounds, arguing that the action should proceed in Zambia rather than in the U.K.

Supreme Court's Decision

In the course of determining whether the case should be allowed to proceed in the U.K., the U.K. Supreme Court had to consider whether a tenable cause of action in negligence had been pleaded against the parent company.

At the outset of its analysis, the Court reaffirmed the basic principle of corporate separateness, noting that, while ownership gives a parent company the ability to exert control over the subsidiary, it does not impose any duty to exert such control. Accordingly, the parent-subsidiary relationship does not, in and of itself, impose any legal liability.

However, the Court went on to note that the parent may incur liability if it avails itself of "the opportunity to take over, intervene in, control, supervise or advise the management of the relevant operations of the subsidiary". The Court discussed two examples of the type of activity by a corporate parent that might result in the imposition of a duty of care owed (and, accordingly, the risk of liability for breach of that duty) to third parties. First, it gave the well-known (and uncontroversial) example of a parent having "in substance taken over the management" of the subsidiary. Such activity has long been known to create a substantial risk that the corporate separateness of parent and subsidiary may not be recognized and enforced, leading to a risk of liability being imposed on the parent for the acts that otherwise would have been viewed as the acts solely of the subsidiary.

The second example given by the Court, however, is more noteworthy, because it has the potential to extend liability of parent corporations beyond the bounds that have historically been seen in the common law. The Court described this second type of activity as covering instances where the parent "has given relevant advice to the subsidiary about how it should manage a particular risk". Thus, the Court said that the parent company may assume a duty of care to third parties and potentially incur liability, if it lays down "group-wide policies and guidelines"

and if those policies or guidelines contain "systemic errors" that, when implemented by the subsidiary, cause harm to third parties. Similarly, even if the group-wide policies do not, in and of themselves, impose a duty of care, the same result may follow, if the parent takes "active steps, by training, supervision and enforcement" to see that the policies are implemented by the subsidiaries. Finally, the Court stated that a parent may owe a duty of care to third parties if it merely "holds itself out as exercising" a degree of supervision over its subsidiaries.

Applying those principles to the facts before it, the Court noted that Vedanta had made public statements which could be interpreted as indicating an "assumption of responsibility for the maintenance of proper standards of environmental control over the activities of its subsidiaries". The Court also referred to Vedanta having "implemented those standards by training, monitoring and enforcement".

On that basis, the Court held that the plaintiffs had established a triable issue as to whether Vedanta owed a duty of care to third parties who might be harmed by the operations of its indirect subsidiary. In this regard, the holding by the U.K. Supreme Court appears to take the law of negligence in the corporate context well beyond the bounds that currently exist in Canada.

Implications

The decision appears to broaden the scope of liability of parent companies for harmful actions of their subsidiaries. By creating a framework for liability based on such things as group-wide environmental or safety policies, group-wide training and/or enforcement relating to such policies, or even public pronouncements by the parent holding itself out as supervising the implementation of such policies by its subsidiaries, the principles expressed by the U.K. Supreme Court could, if adopted in Canada, fundamentally change the risks faced by corporate groups arising out of the operations of individual subsidiaries.

The lower appeal court's decision in *Vedanta Resources* was considered by the Ontario Court of Appeal in its recent decision in *Das v. George Weston Limited*, but it was ultimately held to be of little assistance, since the dispute in the Das case did not arise out of a parent-subsidiary relationship. Accordingly, it remains to be seen whether, when faced with facts analogous to those in *Vedanta Resources*, Canadian courts will follow the U.K. Supreme Court's lead and broaden the scope of liability imposed on parent corporations for the harmful operations of their subsidiaries.

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