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## Control and the Partly Owned Corporation: A Preliminary Inquiry into Shared Control

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# CONTROL AND THE PARTLY OWNED CORPORATION: A PRELIMINARY INQUIRY INTO SHARED CONTROL

*Phillip I. Blumberg\**

I. INTRODUCTION .....	420
II. MEANINGS OF CONTROL AND SHARED CONTROL .....	422
A. <i>Levels of Control</i> .....	422
B. <i>Levels of Shared Control</i> .....	423
III. CONTROL AND SHARED CONTROL IN VARIOUS AREAS OF U.S. LAW APPLYING ENTERPRISE PRINCIPLES .....	424
A. <i>Introduction</i> .....	424
B. <i>Statutes of Specific Application</i> .....	427
1. Introduction .....	427
2. Holding Company Statutes Pervasively Applying Enterprise Principles .....	428
a. <i>Federal</i> .....	428
b. <i>State</i> .....	430
3. Statutes Selectively Applying Enterprise Principles .....	432
a. <i>Securities Industry and Investment Companies</i> ...	433
b. <i>Foreign Investment</i> .....	435
c. <i>Foreign Trade</i> .....	436
(i) Cuban Assets Control Regulations .....	438
(ii) Antiboycott Regulations .....	439
d. <i>Labor Relations, Employment, and Antidiscrimination</i> .....	441
4. Control and Shared Control in Statutes of Specific Application .....	443
C. <i>Statutes of General Application</i> .....	447
1. Enterprise Law .....	447
2. Environmental Law .....	451
a. <i>Construction of "Owner," "Operator," and "Arranger"</i> .....	452
b. <i>Shared Control</i> .....	454

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3. Other Statutes . . . . .	456
IV. THE ROLE OF ADMINISTRATIVE AGENCIES IN THE IMPLEMENTATION OF STATUTORY REGULATORY PROGRAMS . . . . .	457
V. CONTROL IN COMMON LAW CONTROVERSIES . . . . .	459
A. <i>General Standards</i> . . . . .	459
B. <i>Shared Control</i> . . . . .	461
VI. SHARED CONTROL AND CORPORATE JOINT VENTURES . . . . .	462
VII. CONCLUSION . . . . .	466

## I. INTRODUCTION

Multinational corporations are corporate groups typically organized in traditional hierarchical form with a parent corporation and scores of subsidiaries collectively conducting the business of the group around the world.<sup>1</sup> While most U.S. multinational groups operate through wholly owned subsidiaries, a minority of U.S. subsidiaries are partly owned.<sup>2</sup> However, whether wholly owned or partly owned, the members of the hierarchical group operate under the control of the parent corporation.<sup>3</sup> Control is the underlying element that assures the coordinated integration of the activities of the group and forges the numerous affiliates into a firm. In the traditional hierarchical organizational pattern, control is almost never

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1. PHILLIP I. BLUMBERG, *THE LAW OF CORPORATE GROUPS: PROCEDURAL PROBLEMS IN THE LAW OF PARENT AND SUBSIDIARY CORPORATIONS* 30-37 (1983) [hereinafter *BLUMBERG: PROCEDURAL PROBLEMS*]. The development of multinational corporations has been extensively examined by the author. See generally PHILLIP I. BLUMBERG & KURT A. STRASSER, *THE LAW OF CORPORATE GROUPS: PROBLEMS OF PARENT AND SUBSIDIARY CORPORATIONS UNDER STATE STATUTORY LAW* (1995) [hereinafter *BLUMBERG & STRASSER: STATE STATUTORY LAW*]; PHILLIP I. BLUMBERG & KURT A. STRASSER, *THE LAW OF CORPORATE GROUPS: PROBLEMS OF PARENT AND SUBSIDIARY CORPORATIONS UNDER STATUTORY LAW SPECIFICALLY APPLYING ENTERPRISE PRINCIPLES* (1992) [hereinafter *BLUMBERG & STRASSER: SPECIFIC STATUTORY LAW*]; PHILLIP I. BLUMBERG, *THE LAW OF CORPORATE GROUPS: PROBLEMS OF PARENT AND SUBSIDIARY CORPORATIONS UNDER STATUTORY LAW OF GENERAL APPLICATION* (1989) [hereinafter *BLUMBERG: GENERAL STATUTORY LAW*]; 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) [hereinafter *BLUMBERG: SUBSTANTIVE COMMON LAW PROBLEMS*]; 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) [hereinafter *BLUMBERG: BANKRUPTCY PROBLEMS*]. (The seventh and concluding volume of the series, *THE LAW OF CORPORATE GROUPS: ENTERPRISE PRINCIPLES IN COMMERCIAL RELATIONSHIPS*, will appear in 1998.); see also PHILLIP I. BLUMBERG, *THE MULTINATIONAL CHALLENGE TO CORPORATION LAW: THE SEARCH FOR A NEW CORPORATE PERSONALITY* (1993).

2. *BLUMBERG: PROCEDURAL PROBLEMS*, *supra* note 1, at 30-37; HARVEY S. JAMES, JR. & MURRAY WEIDENBAUM, *WHEN BUSINESSES CROSS INTERNATIONAL BORDERS: STRATEGIC ALLIANCES AND THEIR ALTERNATIVES* 48 (1993).

3. *BLUMBERG: PROCEDURAL PROBLEMS*, *supra* note 1, at 30-37.

shared.<sup>4</sup> Shared control is unknown except at the higher level of the shareholder-investors in the parent corporation, who may influence or determine the policies of the enterprise but are not an active participant in it.

This traditional pattern of corporate groups organized in hierarchical form has never been exclusive and increasingly, is being supplemented by other enterprises organized in nonhierarchical fashion in which control is shared. Corporations are joining forces and conducting some aspects of their operations through joint ventures, strategic alliances, and corporate networks.<sup>5</sup>

Hierarchical corporate structures are also dominant in European multinational groups. However, neither the hierarchical form nor the pattern of wholly owned subsidiaries has been as widely accepted in Europe. Thus, there are some major European groups with dual parent corporations, such as Royal Dutch-Shell and Agfa-Gevaert. Partly owned subsidiaries are much more common than in the United States.<sup>6</sup> In addition, strategic alliances and corporate networks have made an increasing appearance.<sup>7</sup> Finally, European groups linked by interlocking stock ownership in a holding company, in which control has been shared, have become increasingly important.<sup>8</sup> These are the so-called European holding groups.<sup>9</sup> European multinational structure is evidently more complex than in the United States, but notwithstanding these departures, European groups, like those in the United States, are typically hierarchical. Comparable developments in Japan in the form of the *zaibatsu* and *keiretsu*, and more recently the *kigyoshodan*, are well known.<sup>10</sup>

Such changing organizational patterns have introduced a new complexity

4. While two corporate groups may join in a corporate joint venture, the joint venture will conduct its own business, typically one that exists in an area of tangency between them.

5. JAMES & WEIDENBAUM, *supra* note 2, at 8-12. Strategic alliances and networks are essentially licenses or contractual understandings and arrangements on certain dealings between the parties. In contrast to the cases applying enterprise principles, they do not present a basis for recognition, at least for the purpose at hand, as having a separate juridical identity in any context. As will be seen, corporate joint ventures have been the only nonhierarchical undertakings that have received judicial scrutiny for these purposes. The courts have uniformly refused to depart from traditional corporate principles in determining the general legal consequences arising from the corporate joint venture structure.

6. See Klaus J. Hopt, Book Review, 32 COMM. MKT. L. REV. 1059, 1062 (1995) (reviewing CORPORATE CONTROL AND ACCOUNTABILITY, CHANGING STRUCTURES AND THE DYNAMICS OF REGULATION (Joseph McCahery et al. eds., 1993)).

7. JAMES & WEIDENBAUM, *supra* note 2, at 61.

8. *Id.* at 97-101.

9. See Cynthia Van Hulle, On the Nature of European Holding Groups, Onderzoeksrapport Nr 9609 (D/1996/2376/9) (The Netherlands).

10. See JOHN SCOTT, CORPORATE GROUPS AND NETWORK STRUCTURE IN CORPORATE CONTROL AND ACCOUNTABILITY 291, 302 (Joseph McCahery et al. eds., 1993); Melissa J. Krasnow, *Corporate Interdependence: The Debt and Equity Financing of Japanese Companies*, 24 CAL. W. INT'L L.J. 55, 58 (1993); Hopt, *supra* note 6, at 1062.

in those areas of the law in which concepts of control have been recognized. In these newer organizational forms, no participating multinational corporation exercises sole control. On the contrary, the essence of the development is the emergence of a nonhierarchical structure in which control is shared.

This article examines the significance of shared control in U.S. regulatory and common law. At the outset, it should be recognized that the doctrine of control has played a central role, and problems involving shared control have been of peripheral importance at the most. Nevertheless, shared control does present special problems that deserve examination.

This article commences with an attempt to delineate the various forms that the concepts of control and shared control can assume in any given case. It then examines shared control as a subset of the larger doctrine of control. After exploring the use of control as the primary legal standard, this article seeks to ascertain the light, if any, cast by the available materials in the various contexts involved on the significance of shared control. It concludes that shared control appears to serve as a basis for liability under enterprise purposes only in a limited area and that the prospects for change are limited.

## II. MEANINGS OF CONTROL AND SHARED CONTROL

### A. *Levels of Control*

In its earliest consideration in common law matters, control commonly referred to a shareholder's power to control the election of the board of directors of a corporation.<sup>11</sup> Through the ability to designate a majority of the board of directors, the shareholder assumed the reins of power over the business of the corporation. As is well known, such control over the election of directors need not rest on majority ownership of the voting shares. Where shares are widely distributed, as in a large corporation, ownership or control over a significant bloc of shares may provide control where no other holder or group of holders has a bloc of comparable size; this is sometimes called "working control."<sup>12</sup>

For statutory purposes, as will be seen, "control" is typically defined in even more expansive terms not only to include the undisputed power to direct the management or business of the subsidiary (or controlled) corporation, but also to have a role of lesser significance in the shaping of

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11. See generally BLUMBERG: SUBSTANTIVE COMMON LAW PROBLEMS, *supra* note 1.

12. *E.g.*, *Essex Universal Corp. v. Yates*, 305 F.2d 572, 579-80 (2d Cir. 1962) (28.3% of voting stock represents working control); *Gottesman v. General Motors Corp.*, 279 F. Supp. 361, 368 (S.D.N.Y. 1967) (23% "power to provide control"); *cf.* 49 U.S.C. § 10102(7) (1994) (stating that "'control' . . . includes actual control, legal control, and the power to exercise control"); see also LOUIS LOSS & JOEL SELIGMAN, *FUNDAMENTALS OF SECURITY REGULATION* 374 (3d ed. 1995) (discussing the determinants of control).

corporate decisions. Not only the significance but also the very meaning of control takes on a different content in different areas of the law.

### B. *Levels of Shared Control*

Shared control may refer to participation in the collective possession or exercise of the underlying power to elect a majority of the board of directors. Alternatively, it may refer to power over the management and the policies of a corporation. Such a broadened use of shared control introduces a wide-range of varietal forms, from the clear-cut power to command to lesser degrees of influence.

Thus, at the outset, it is desirable to recognize that the concept of shared control analytically includes at least six very different levels of the power to control:

- (1) Involvement in a group that by acting in concert has the power to elect a majority of the board of directors of a corporation;<sup>13</sup>
- (2) involvement in the management of the subsidiary (or controlled) corporation, including actual participation in the tort, statutory violation, or other corporate acts of the subsidiary giving rise to alleged liability;
- (3) involvement in the management of the subsidiary including participation in day-to-day affairs but not in the subsidiary's acts giving rise to alleged liability;
- (4) general involvement in the management of the subsidiary but not including day-to-day affairs;
- (5) no involvement in the management of the subsidiary, but having a veto over actions of the parent, including those affecting the subsidiary and its operations; and
- (6) no involvement in the management of the subsidiary, but having a position disposing the management of the parent to consult it and to take its views into account in determining actions of the parent affecting the subsidiary and its operations.

These different interrelationships between the party in question and the controlled companies represent a continuum of instances of shared control. These must be examined in light of the role of control in the various areas of law presented and the circumstances of the particular case.

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13. The power to elect a majority of the board members relates solely to the parent corporation. Other manifestations of shared control relate both to the parent and to the aspects of its interrelationship with the subsidiary, giving rise to the possible imposition of enterprise liability on the parent corporation for acts of the subsidiary.

### III. CONTROL AND SHARED CONTROL IN VARIOUS AREAS OF U.S. LAW APPLYING ENTERPRISE PRINCIPLES

#### A. Introduction

Control plays a crucial role in the application of enterprise principles wherever they have been adopted in U.S. law. Notwithstanding its central role, control is not a transcendental jurisprudential concept to be applied throughout U.S. law irrespective of the particular area under consideration. On the contrary, control is a doctrine whose significance in the application of enterprise principles attributing legal rights or imposing legal obligations on one member of corporate group for the actions of another depends on the global context (the juridical area of law under consideration, that is statutory law or common law), the general context (the particular statute or branch of common law), and the particular context (the particular aspect in issue) in which it arises. It is a fact-specific relationship to be evaluated pragmatically in light of all the dimensions of the law in the area. Accordingly, control (and derivatively shared control) assumes somewhat different meanings and plays somewhat different roles in these various areas.

As noted, shared control, or the possession or exercise of control by more than one party, is a subset of the larger concept of control. Accordingly, any consideration of the significance of shared control for purposes of application of enterprise principles can only take place within the larger structure of the role of control in the particular area of U.S. statutory or common law in question. Further, it is an examination that must be pursued in light of the general underlying policies and objectives of the area in question and the specific context in which it is being applied.

Therefore, this review of the legal significance of shared control makes several interrelated inquiries. The review first examines the different roles of the concept of control in U.S. law, which may be conveniently divided into three major areas for analytical purposes.<sup>14</sup> It then reviews the significance of shared control in each of these three areas. In particular, it seeks to ascertain which of the varying manifestations of shared participation in the decisional process of a corporation may give rise to liability in the areas of U.S. law under consideration.

The best starting point is a review of the evolution of U.S. regulatory

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14. The three major areas of control in U.S. law include: (1) statutes of specific application (*i.e.*, those that make express reference to control, parent, subsidiary, or affiliated corporations); (2) statutes of general application (*i.e.*, those that regulate certain activities but make no reference to control, parent, subsidiary, or affiliated corporations); and (3) common law controversies.

law. Until the end of the first quarter of the twentieth century, regulatory law had followed the traditional principles of corporation law. These principles were grounded on entity law; each corporation had its own juridical identity and its own rights and liabilities including its statutory obligations, separate and distinct from those of its shareholders. With statutory law focusing on the regulated company, the regulatory program did not reach subsidiaries and affiliates of the regulated company. Evasion of the program and frustration of the statutory objectives were easily achieved through manipulation of the corporate structure.<sup>15</sup>

By 1933, it was apparent that the older statutory approaches drafted in terms of conventional principles of corporate law were making effective regulation almost impossible.<sup>16</sup> Confronted by the Great Depression and the financial scandals of the 1920s, the Roosevelt Administration taking office in 1933 rapidly moved forward with major regulatory statutes governing the railroad, securities, public utilities, and investment company industries among others. In these statutes, the Congress departed from past approaches and firmly adopted principles of enterprise law. The statutes utilized control<sup>17</sup> as the fundamental concept to bring an entire enterprise — subsidiaries and affiliated companies of the regulated company as well as the regulated company — under the statutory program. In the ensuing half-century, this model has persisted, and control has been the foundation for innumerable federal and some state regulatory programs.<sup>18</sup>

In these statutory programs, which expressly utilize enterprise principles

15. *E.g.*, *United States v. Elgin, Joliet & Eastern R.R.*, 298 U.S. 492 (1936); *United States v. Delaware & Hudson Co.*, 213 U.S. 366 (1909). At times, the Interstate Commerce Commission has adopted the same emasculating approach. *See Stock of Denver & Rio Grande Western R.R.*, 70 I.C.C. 102 (1921).

16. *See generally* JAMES C. BONBRIGHT & GARDINER C. MEANS, *THE HOLDING COMPANY: ITS PUBLIC SIGNIFICANCE AND ITS REGULATION* (1932).

17. The holding company statutes and the Investment Companies Act refer not only to “control” but also to “controlling influence.” Public Utility Holding Company Act (PUHCA), 15 U.S.C. § 79b(7)(A), (B) (1994); Investment Company Act (ICA), 15 U.S.C. § 80a-2(a)(9) (1994); Bank Holding Company Act (BHCA), 12 U.S.C.A. § 1841(a)(2)(a-c) (1996). A major, unresolved issue is the extent to which “controlling influence” differs from “control.” *See* 4 LOUIS LOSS & JOEL SELIGMAN, *SECURITIES REGULATION* 1691-1703 (3d ed. 1990).

In an early pronouncement for PUHCA purposes, the Securities Exchange Commission (SEC) made plain the expansive scope of controlling influence. It stated that “the existence of a controlling influence may frequently be the result of complex and subtle intercorporate relationships based upon historical, traditional or contractual associations regardless of the amount of voting stock held.” *In Re United Corp.*, PUHCA, Release No. 35-4478, 13 S.E.C. 854, 885 (Aug. 14, 1943); *see* *Kaneb Pipe Line Co.*, PUHCA Release No. 35-1625043 S.E.C. 976 (1968).

18. *See generally* BLUMBERG & STRASSER: STATE STATUTORY LAW, *supra* note 1, §§ 3 to 7, 10, 13; BLUMBERG & STRASSER: SPECIFIC STATUTORY LAW, *supra* note 1, § 2 to 7, 16 to 23, 25, 29; *see also* BLUMBERG: GENERAL STATUTORY LAW, *supra* note 1.



and are referred to as statutes of specific application,<sup>19</sup> control serves as the linchpin for determining the outer reach of regulatory programs founded on enterprise principles. In order to implement fully their underlying objectives, policies, and purposes, these statutes in many instances go well beyond the corporation directly subject to its provisions to include other corporation(s) (the parent corporation) that controlled the corporation, that it controlled (subsidiaries), and with which it was under common control (sister subsidiaries).<sup>20</sup> Through the concept of control and the complementary doctrine of an affiliate, these statutes reach all components of the enterprise of which the company directly regulated is a part.

This experience contrasts with other federal statutes that are drafted in general terms without any statutory or administrative reference to corporate groups or to control. These are the so-called statutes of general application. Enterprise principles, which make no appearance in these statutes, are introduced, if at all, solely through judicial decisionmaking in determining the scope of statutory application.

Finally, judicial decisionmaking governs the determination of common law controversies involving private parties. In this third area, traditional entity law predominates. With some growing exceptions, the attribution of the rights and liabilities of a subsidiary corporation (or other group affiliate) to its parent corporation (or another group affiliate) is possible only in those "rare" and "exceptional" cases that meet the rigorous requirements of "traditional piercing the veil jurisprudence." Under this traditional view, not simply control but an "excessive" exercise of control over the subsidiary (or controlled) corporation is required, along with other factors.<sup>21</sup>

This is a brief introduction to a summary description of the response of the three great divisions of U.S. law to the legal problems presented by U.S. corporate groups organized in hierarchical form and operating under the control of the parent corporation. While such groups were organized with varying patterns of operational centralization or decentralization, the parent's *power* to control these instances was unquestioned. As reviewed in the succeeding sections, the issue for analysis is the legal significance of the shifting role of control and shared control in these three jurisprudential areas.

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19. In some statutes, such as those under the labor laws, enterprise principles have been incorporated into the regulatory structure by administrative decisions even though the statutes themselves are drafted in general terms.

20. See BHCA, 12 U.S.C. § 1841(k) (1994); ICA, 15 U.S.C. § 80a-2(a)(40) (1994). This supplementary definition is widely employed for the definition of "affiliates," a class subjected to some but not all of the responsibilities imposed by the Act. See CAL. FIN. CODE § 5100.5 (West 1996).

21. See BLUMBERG: SUBSTANTIVE COMMON LAW PROBLEMS, *supra* note 1, § 6.

## B. Statutes of Specific Application

### 1. Introduction

The great U.S. industries are almost uniformly regulated by federal statutes specifically adopting enterprise principles in varying degrees as the foundation of the regulatory programs. These include such key industries as banking and savings and loan institutions, securities, investment companies, transportation, energy, and communications. In addition, numerous federal statutes expressly employ enterprise principles in regulating designated business activities and practices that cross industry lines. These include major federal statutes dealing with foreign trade, including export and import controls, foreign investment, national boycotts, and foreign corrupt practices. All adopt enterprise principles to expand the outer range of application of the regulatory program and to prevent evasion and frustration of the statutory objectives. Except in isolated areas, "control" serves as the statutory key for imposing the regulatory program, broadening the area of application to include controlling persons and other companies in the corporate group of which the regulated corporation is a component.<sup>22</sup> Comparable state statutes adopt enterprise principles in pervasive regulatory programs for governing banking and savings and loan, insurance,<sup>23</sup> and casino gambling holding company systems.<sup>24</sup>

Under all these statutes, as implemented by the administrative regulations thereunder, the concept of control occupies a central role in determining which parties are subject to the regulatory program. Although there are innumerable variations in the statutory definition of control, they are, in the end, very much alike. They all center on an ability to control the decisionmaking of the corporation.

There are two variables when considering the various standards of control. Control assumes a different meaning and significance depending on both the statute and the particular context of the statute at issue. From statute to statute and from context to context, control may play a different role for different purposes. In many areas, the mere possession of control is sufficient to subject a party to the statutory program. This readily permits

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22. See BLUMBERG: PROCEDURAL PROBLEMS, *supra* note 1, § 22.

23. REVISED MODEL INSURANCE HOLDING COMPANY SYSTEM REGULATORY ACT (IHCSRA) (Nat'l Ass'n Ins. Comm'rs 1984), Model Reg. Serv. 440-27 (Jan. 1992); see BLUMBERG & STRASSER: STATE STATUTORY LAW, *supra* note 1, § 7.03, at 286 n.8 (collecting statutes).

24. *E.g.*, Nevada Gaming Control Act, NEV. REV. STAT. § 463.010-.720 (1995); Casino Control Act, N.J. STAT. ANN. §§ 5:12-26, 5:12-28, 5:12-47 (West 1996); see BLUMBERG & STRASSER, STATE STATUTORY LAW, *supra* note 1, § 13.

imposition of statutory obligations on parties sharing control. In other contexts, application of the statute may require some exercise of control, and the significance of shared control depends on the degree of involvement in the operations and decisionmaking of the controlled corporation by each of the parties sharing control. In statutes of specific application, control has the primary role. The legislature and the administrative agency applying the program have spoken: The role of the courts is not to determine the applicable standards but instead to implement the statute in question as construed by the agency. The role of administrative agencies in this area is of great importance. They have typically utilized their enormous discretionary powers to expand significantly the breadth of the statutory coverage. By contrast, the courts under the statutes of general application and in common law matters have been reluctant to undertake such heroic measures.

At the outset, it should be noted that where a statute defines control in terms of a specified proportion, usually a majority of the voting stock, other standards of control become irrelevant. While still not uncommon, this simplistic approach to statutory drafting, which invites corporate manipulation to sidestep a regulatory program, no longer plays a major role in U.S. regulatory law that expressly addresses the problems presented by corporate groups and parent and subsidiary corporations. Most statutes employing enterprise principles rely on functional definitions of control in which arithmetical standards of stock ownership do not play a decisive role. The discussion divides into two classes. First are the statutory programs in which both the statute and the administrative regulations define control. These are generally, but not always, the great holding company statutes. Second are the statutes that either do not refer to control, or if they do, fail to define it. In these, the administrative regulations are the sole source of definition.

## 2. Holding Company Statutes Pervasively Applying Enterprise Principles

### a. *Federal*

The federal holding company statutes, which regulate the banking, savings and loan, and public utility industries, and the state statutes, which regulate the banking, savings and loan, insurance, and casino gambling industries, focus on the parent company and the system or group that it operates. The Public Utility Holding Company Act of 1935 (PUHCA) isolated control as the central defining standard in extending a statutory program to include all component companies of the holding company system,

thereby subjecting the entire enterprise to pervasive regulation.<sup>25</sup> The Investment Company Act of 1940 (ICA) utilized much the same structure in accomplishing its less pervasive objectives.<sup>26</sup> The Bank Holding Company Act (BHCA)<sup>27</sup> and the Savings and Loan Holding Company Act (SLHCA)<sup>28</sup> substantially adopted the PUHCA model. Their variations subsequently became the basis for the Model Insurance Holding Company System Regulatory Act (IHCSRA),<sup>29</sup> which has been substantially adopted in its original or revised form by almost all state jurisdictions.<sup>30</sup>

These are the great holding company statutes that pervasively apply enterprise principles in extending governmental regulation over a key industry. They all employ a series of alternative standards, any one of which will support a finding of control. These standards are very much the same but with incidental variations. To illustrate both the general approach of all these statutes as well as to indicate the nature of the variations, this discussion will review the BHCA and SLHCA models, which are representative of this class of statutes.

Under the BHCA model, control may be established by satisfying any one of three standards.<sup>31</sup> First, control arises from ownership or control of twenty-five percent or more of any class of the controlled company's voting securities, whether arising "directly or indirectly or acting through one or more other persons."<sup>32</sup> Second, control exists if the holder "controls in any manner the election of a majority of the directors."<sup>33</sup> Third, the administrative agency has the power "after notice and hearing, . . . [to determine whether] the company directly or indirectly exercises a controlling influence over the management or policies of the bank."<sup>34</sup> Finally, where control exists, the statutes extend to all other members of the corporate group as

25. PUHCA, 15 U.S.C. § 79(b)(7); see BLUMBERG & STRASSER, SPECIFIC STATUTORY LAW, *supra* note 1, § 2.

26. ICA, 15 U.S.C. § 80a-1-52.

27. BHCA, 12 U.S.C. § 1841-50.

28. SLHCA, 12 U.S.C. § 1467(a)(2) (1994).

29. BLUMBERG & STRASSER, STATE STATUTORY LAW, *supra* note 1, § 7.04, at 290-91.

30. *Id.* § 7.03, at 285; see IHCSRA, Model Reg. Serv. 440-27.

31. BHCA, 12 U.S.C. § 1841(a)(2)(A).

32. *Id.* The SLHCA provisions substantially follow the BHCA in most respects but not without certain interesting variations. Its statutory standard is more than 25% of "the voting shares," 12 U.S.C. § 1467a(a)(2)(A), while the BHCA specifies 25% or more of "any class of voting securities," 12 U.S.C. § 1841(a)(2)(A). Further, while the BHCA refers to control arising "directly or indirectly or acting through one or more other persons," *id.*, the SLHCA refers to persons acting "directly or indirectly or acting in concert with one or more other persons," 12 U.S.C. § 1467a(a)(2)(A). Thus, literally in any event, the BHCA confines itself to persons that are acting in an agent-like capacity while the SHLCA appears more expansive to include a number of persons acting as principals.

33. BHCA, 12 U.S.C. § 1841(a)(2)(B).

34. *Id.* § 1841(a)(2)(C).

affiliates by providing "any company that controls, is controlled by, or is under common control with" the regulated company.<sup>35</sup>

The BHCA and SLHCA administrative regulations establish certain "[r]ebutable presumptions of control."<sup>36</sup> However, it is of note that the tests employed are not identical. The BHCA administrative regulations provide that such a presumption arises in the event of ownership or control of as a little as five percent of the total voting shares.<sup>37</sup> The SLHCA regulations, however, recognize a presumption only in the event of ownership of ten percent or more of any class of voting stock or twenty-five percent of total voting stock.<sup>38</sup> In either case, such holdings must be coupled with certain control factors. The SLHCA requires elements such as the following:

1. The holder is one of the two largest holders of any class of voting stock or owns more than twenty-five percent of the shareholders' equity.<sup>39</sup>
2. The holder is party to any agreement that enables it "to influence a material aspect of the management or policies" of the controlled company.<sup>40</sup>
3. The holder and its nominees constitute at least one member of the board of directors or serve as senior executive officers.<sup>41</sup>

The BHCA regulations specify much the same factors.

#### b. *State*

The states have adopted the model of the federal holding company statutes in regulating corporate groups in bank and savings and loan institutions, the insurance industry, and the casino gambling industry.<sup>42</sup> The state banking and savings and loan holding company statutes largely follow the federal models, thereby facilitating the existing pattern of overlapping federal and state regulation and supervision in the banking savings institution industry.<sup>43</sup>

The Model IHCSRA and the revised IHCSRA, adopted by almost all the

35. *Id.* § 1843(k).

36. 12 C.F.R. §§ 225.31(d)(2), 574.4(b), 574.4(c) (1996).

37. *Id.* § 225.31(d)(2)(ii).

38. *Id.* § 574.4(b)(i)-(ii).

39. *Id.* § 574.4 (c)(1-2).

40. *Id.* § 574.4 (c)(4)(ii).

41. *Id.* § 574.4 (c)(7), (8).

42. *E.g.*, CAL. FIN. CODE § 5100.5 (West 1995) (savings and loan); MISS. CODE ANN. § 75-76-199 (1995) (gambling); NEV. REV. STAT. § 463.010 (1995) (gambling); N.J. STAT. ANN. § 5:12-1 (West 1996) (gambling).

43. *See* CAL. FIN. CODE § 5100.5.

states, also have substantially followed the SHLCA statutory formulations of control and controlling influence.<sup>44</sup> Thus, neither state banking and savings and loan holding company statutes nor the IHCSRA present legal problems that differ significantly from those of the pervasive federal holding company statutes on which they are modelled.

The pervasive enterprise-wide regulatory state statutes that regulate casino gambling comprise the other area in U.S. law comprehensively regulating holding company systems through enterprise principles based on control. Casino gambling in Nevada, New Jersey, Louisiana, Mississippi, and Illinois has become a major U.S. industry.<sup>45</sup> These businesses are frequently operated by casino gambling subsidiaries forming part of holding company systems, in which the parent corporation is often listed on a major stock exchange.<sup>46</sup>

The regulatory statutes substantially follow the federal holding company statutes, and in at least one respect, go far beyond the federal models.<sup>47</sup> The state statutes venture beyond traditional definitions of control and extend the scope of the regulatory program to include any company holding, directly or indirectly, "any part" (presumably, even the tiniest holding) of the securities of a casino licensee.<sup>48</sup> This remarkable provision reflects the legislative concern for measures to protect against potential penetration by criminal elements and corruption into the industry. It also illustrates the widespread drafting principle in U.S. regulatory and revenue statutes that makes statutory application turn on a standard described as control. It does so even where, as in this instance, the definition clearly does not relate to the level of share ownership required to determine or perhaps to influence corporate management or policies.<sup>49</sup>

44. IHCSRA, Model Reg. Serv. 440-1, 440-27; see BLUMBERG & STRASSER, STATE STATUTORY LAW, *supra* note 1, § 7.03 n.8 (collecting statutes); *id.* § 7.04, at 290-91. In at least two respects, its definition of control is more expansive than that of the federal acts. The IHCSRA refers to "possession" of the "power to direct the management and policies" while the federal statutes in some instances refer to the "exercise" of the power. IHCSRA, § 1C; BLUMBERG & STRASSER, STATE STATUTORY LAW, *supra* note 1, § 7.04, at 291. Secondly, the IHCSRA omits any requirement of ownership of a specified proportion of shares. *Id.*

45. Bruce Orwall, *Casino Visits Rose in 1995, Survey Finds*, WALL ST. J., Apr. 12, 1996, at A7A; Pauline Yashihashi, *Gambling: Bonanzas from Riverboat Casinos Buoy Fortunes of More Cities, Gambling Firms*, WALL ST. J., Sept. 9, 1993, at B1, B5.

46. Phillip I. Blumberg, *The Increasing Recognition of Enterprise Principles in Determining Parent and Subsidiary Corporation Liabilities*, 29 CONN. L. REV. 295, 312 (1996).

47. *Id.*

48. See MISS. CODE ANN. § 75-76-199(d), (e)(iii), (f), (k); NEV. REV. STAT. §§ 463.4825, 463.486, 463.488. Interestingly, New Jersey modified this provision to read "any significant part." N.J. STAT. ANN. §§ 5:12-26, 5:12-28, 5:12-47.

49. The most obvious example are the definitions of "control" in the Internal Revenue Code that refer to stock ownership without distinguishing whether the stock is voting stock

The expansive use of control for the purpose of broadening the statutory scope in the holding company statutes reflects the pervasive nature of the regulatory programs.<sup>50</sup> Although the experience obviously provides some guidance in consideration of control under statutes with more selective reliance on enterprise principles, the difference in the structure of such statutes, as well as the differing underlying objectives and policies, must always be taken into account. A final word of caution. One of the unresolved issues in the U.S. law is the extent to which controlling influence differs from control, and decisions finding controlling influence may provide less than firm guidance for a determination of control.<sup>51</sup>

### 3. Statutes Selectively Applying Enterprise Principles

In contrast to the holding company statutes reviewed above, there are numerous statutory programs in which enterprise concepts are not used pervasively throughout the program, but instead are specifically applied to the affiliated or related parties of the company being regulated for selected purposes of the regulatory statutes.<sup>52</sup> The federal statutes of this nature include those dealing with foreign trade and investment; regulation of the securities, communications, transportation, and energy industries; and extraterritorially applying U.S. law to the foreign subsidiaries of an U.S.-based multinational group, as well as to the multinational's own activities abroad,<sup>53</sup> in areas such as antiboycott activity, foreign corrupt practices, and employment discrimination. Like the holding company statutes, these statutes rely on substantially similar standards of control to determine the applicability of the regulatory program. They do not, however, utilize the

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or that refer to ownership of at least 80% of the stock, a requirement that goes far beyond the percentage required for voting control. 26 U.S.C. §§ 368, 1504, 1563 (1994); see BLUMBERG & STRASSER, *SPECIFIC STATUTORY LAW*, *supra* note 1, § 15.

50. See Securities Act of 1933, 15 U.S.C. §§ 77b(3), 77o (1994); Securities Exchange Act of 1934, 15 U.S.C. § 78t (1994); PUHCA, 15 U.S.C. § 79b(a)(7)-(8).

51. Professors Frankel, Loss, and Seligman conclude that the differences between the controlling influence and control are differences of degree. 1 TAMAR FRANKEL, *THE REGULATION OF MONEY MANAGERS: THE INVESTMENT COMPANY ACT AND THE INVESTMENT ADVISERS ACT 501* (1978); 4 LOSS & SELIGMAN, *supra* note 17, at 1727.

52. In many instances, the use of enterprise principles rest on express statutory provisions. In others, such as labor relations, employment, and antidiscrimination, it rests on the use by administrative agencies of enterprise concepts in applying the statutory program or on judicial adoption of such administrative standards in cases involving closely related labor statutes. Application to other areas has been widely rejected.

53. Extraterritorial application of U.S. law based on the effects doctrine of U.S. foreign relations law, not on control also has taken place in U.S. securities and antitrust laws. See generally Dep't of Justice & FTC, *Antitrust Enforcement Guidelines for International Operations* (Apr. 1995); RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 416 (1987) [hereinafter *THIRD RESTATEMENT*]; 10 LOSS & SELIGMAN, *supra* note 17, at 5016-32.

overall definitional framework of the holding company statutes.

The labor relations, employment, and antidiscrimination statutes adopt a somewhat different approach for selective application of enterprise standards. These statutes rely not on control but on the unique “integrated enterprise” standard that focuses on the labor dimensions of the interrelationship between the dominant and subservient parties.

In view of the rich abundance of examples of statutory and administrative references to control as the standard for determining the scope of regulatory programs in these statutes selectively applying enterprise principles, a comprehensive review is beyond the scope of this inquiry. Discussion is confined to several illustrative areas: securities and investment company laws; statutes dealing with foreign investment in the United States, foreign trade, and participation in trade boycotts; and labor relations, employment, and antidiscrimination statutes.

#### a. *Securities Industry and Investment Companies*

The Securities Act of 1933 and the Securities Exchange Act of 1934 are leading statutes that make considerable use of enterprise principles grounded on control, but do so in a selective manner. The ICA has features of both the pervasive and selective statutes, relying on controlling influence as well as control.<sup>54</sup> These statutory programs provide a particularly useful area in which to inquire into the meaning of control. They were among the very earliest of the statutes introducing enterprise principles into U.S. regulatory law. Further, there is a substantial accumulation of decisions and materials dealing with the issue. Finally, the statutory programs in these areas have been superbly reviewed by Professors Loss and Seligman<sup>55</sup> and by Professor Frankel,<sup>56</sup> the leading U.S. scholars in these fields, providing valuable insight into the role of control in the relevant regulatory programs.

Although control plays a major role in the Securities Act of 1933 and the Securities Exchange Act of 1934, neither these statutes nor their legislative history provide any strict definition. This omission was deliberate in order to avoid providing would-be evaders with a blueprint for evasion.<sup>57</sup> In contrast, the ICA substantially follows the definitional model of the PUHCA with an extensive definition of control.<sup>58</sup> It also relies on the concept of

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54. ICA, 15 U.S.C. § 80a-2(a)(9).

55. See 4 LOSS & SELIGMAN, *supra* note 17, at ch. 5.

56. See 1 FRANKEL, *supra* note 51, at ch. 7, *passim*.

57. See *Metge v. Baehler*, 762 F.2d 621, 630 (8th Cir. 1985) (citing H.R. REP. NO. 1383-73, at 26 (1934)), *cert. denied sub nom. Metge v. Bankers Trust Co.*, 474 U.S. 1057, *cert. denied sub nom. Bankers Trust Co. v. Metge*, 474 U.S. 1072 (1986).

58. ICA, 15 U.S.C. § 80a-2(a)(9).



controlling influence to supplement the standard of control.<sup>59</sup>

Professors Loss, Seligman, and Frankel make it plain that while the concept of control is fundamentally the same in the security and investment company areas, its precise formulation and application for purposes of the statute at hand depends on the purpose of the particular statutory provision and the context in which it arises.<sup>60</sup> Professor Frankel further notes that “[c]hanges in context may change the meaning of control even in one statute.”<sup>61</sup> Thus, control may exist for certain purposes of the statute but not for others.<sup>62</sup>

The doctrine of control under the securities and investment company laws has certain fundamental components. First, control is “the power to direct . . . [or command] the management and policies” of a company.<sup>63</sup> For most purposes, the courts and the SEC have held that potential control or the power to control will suffice, and that control need not in fact be exercised.<sup>64</sup> Second, the power to control may not be legally enforceable, but may instead arise from personal, historic, or economic sources.<sup>65</sup> Third, it may be active, or in some contexts it may be latent and passive.<sup>66</sup> Thus, one court has held that control exists for purposes of the securities laws where “major decisions are probably seldom taken without consulting” the controlling person.<sup>67</sup>

The range of statutory liability imposed by the “controlling persons” standard is so extensive that both securities acts contain provisions covering special defenses for controlling person statutory liability under the statutes.<sup>68</sup> In summary, for some purposes of the securities and holding company statutes, the outer circle of impact on decisionmaking, arising from “veto” or “consultation” power, has been accepted as control in the contexts presented. Whether this far reaching view of shared control in the implementation of these statutes will be accepted in other statutory areas is far from clear.

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59. *Id.*

60. 1 FRANKEL, *supra* note 51, at 495-96; 4 LOSS & SELIGMAN, *supra* note 17, at ch. 5.

61. 1 FRANKEL, *supra* note 51, at 496.

62. *Id.*

63. Securities and Exchange Commission, 17 C.F.R. § 230.405 (1996).

64. *See, e.g.*, Phillips v. SEC, 388 F.2d 964, 970-72 (2d Cir. 1968); *In re Chicago Corp.*, 28 S.E.C. 463, 469 (1948); *In re M.A. Hanna Co.*, 10 S.E.C. 581, 588-89 (1941).

65. *See* 1 FRANKEL, *supra* note 51, at 497.

66. *Id.* at 498.

67. *In re Chicago Corp.*, 28 S.E.C. at 468 (citation omitted) (quoting H.R. DOC. No. 77-246, pt. 4, at 2 (1941)); *see* 4 LOSS & SELIGMAN, *supra* note 17, at 1715 n.24.

68. The Securities Act of 1933 excludes liability in cases where there was “no knowledge or reasonable ground to believe” in the alleged underlying facts. 15 U.S.C. § 77o. The Securities Exchange Act of 1934 does much the same thing, excluding liability where the controlling person acts in “good faith and . . . not directly or indirectly induce the act or acts constituting the violation or cause of action.” 15 U.S.C. § 78t(a).

## b. *Foreign Investment*

The statutory programs dealing with foreign investment in the United States, foreign trade, and the antiboycott laws provide additional insight into the use of control in the statutes selectively applying enterprise principles.

Federal controls on foreign investment in the United States present a mixed picture. In some instances, including the Exon-Florio amendment to the Export Administration Act<sup>69</sup> and the International Investment and Trade in Services Survey Act,<sup>70</sup> which require disclosure of foreign direct and portfolio investment, including acquisition of U.S. real estate, control is the decisive factor determining applicability of the legislation.

The proposed regulations to implement the Exon-Florio Amendment defined the critical statutory term "foreign person" to include "any person or entity who 'is or can be' controlled by a foreign interest"<sup>71</sup> and then defined "control" in what appears to be the second most detailed phraseology in U.S. federal law.<sup>72</sup> It was proposed that control be defined as:

69. 50 U.S.C.A. app. § 2170 (1996).

70. 22 U.S.C. § 3103 (1994).

71. 54 Fed. Reg. 29,749, 29,751 (1989), to be codified at 31 C.F.R. §§ 800.211(b), 800.213.

72. *Id.* State law provides an even more extensive example. A Pennsylvania statute dealing with certification as a women's business enterprise for qualification under certain statutory programs first defines a "women's business enterprise" as a concern in which "at least 51% of the stock . . . is owned by one or more women and whose management and daily business operations are controlled by one or more of the women who own it." 18 PA. CONS. STAT. ANN. § 4107.2(b) (West 1995).

The statute expands its definition of control in what appears to be the most complex elaboration of the concept of control in all of U.S. statutory law. Instead of being confined to control of the Board of Directors and the power to direct the policies or management of a company, the statute goes on to deal with the composition of management in remarkable detail. *Id.* In the end, it is not dealing with control at all, as the term is used in the corporation law, but with gender representation in specified aspects of the management structure. *Id.* It provides:

"Control." The exclusive or ultimate and sole control of the business including, but not limited to, capital investment and all other financial property, acquisition, contract negotiation, legal matters, officer-director-employee selection and comprehensive hiring, operating responsibility, cost-control matters, income and dividend matters, financial transactions and rights of other shareholders or joint partners. Control shall be real, substantial and continuing not pro forma. Control shall include the power to direct or cause the direction of the management and policies of the business and to make the day-to-day as well as major decisions in matters of policy, management and operations. Control shall be exemplified by possessing the requisite knowledge and expertise to run the particular business and control shall not include simple majority or absentee ownership. Further, control by a socially and economically disadvantaged individual or woman shall not be deemed to exist in any case where any nonminority owner or employee of the business is disproportionately responsible for the operation of the firm.

the power, direct or indirect, whether or not exercised, and whether or not exercised or exercisable through the ownership of a majority or a dominant minority of the total outstanding voting securities . . . or by proxy voting, contractual arrangements or other means, . . . to determine, direct, take, reach or cause decisions regarding:

- (1) The sale, lease, . . . transfer of . . . the principal assets of the entity . . . ;
- (2) The dissolution of the entity;
- (3) The closing and/or relocation of the production or research and development facilities of the entity; [and]
- (4) The termination or non-fulfillment of contracts.<sup>73</sup>

In the end, however, the agency decided that such detail was “unnecessary,” concluding that administrative adjudication could provide even more expansive construction.<sup>74</sup> Thus, the final Regulations restricted such application only in the case of acquisitions resulting in a foreign person holding ten percent or less of the outstanding voting securities.<sup>75</sup>

In like manner, the International Investment and Trade in Services Survey Act, authorizing the President to collect information on foreign direct and portfolio investment in the United States, includes as “parents” or “affiliates” subject to the Act corporations holding ten percent or more of the voting stock of another corporation.<sup>76</sup>

Notwithstanding such expansive use of the concept of control in these two statutes dealing with foreign investment generally, other federal statutes that restrict foreign investment in such key industries as banking, communications, transportation, and various state statutes that prohibit foreign investment in real estate, particularly agricultural real estate, typically have relied solely on arithmetical tests of control, often majority ownership based solely on stipulated percentages of stock ownership. They do not include any functional standards that look at the economic realities of the relationship, as are by now a commonplace in the great U.S. regulatory statutes.

### c. *Foreign Trade*

Commencing with World War II, the United States has generally extended the outer boundaries of statutes governing foreign trade to include “any person subject to the jurisdiction of the United States.” While sharing

*Id.*

73. 54 Fed. Reg. at 29,751 (1989), codified at 31 C.F.R. § 800.204(a) (1994).

74. Compare Proposed Regulation, 54 Fed. Reg. 29,749, with 31 C.F.R. § 800.204(a).

75. 31 C.F.R. § 800.302(d)(1).

76. 22 U.S.C. § 3102(7),(8) (1994).

this standard, the various statutes incorporating it have made no effort to define it. The Foreign Asset Control (FAC) Regulations, however, rely on enterprise principles and expand statutory coverage based on "persons subject to the jurisdiction" to include all parties controlled by the company subject to the act.<sup>77</sup> In so doing, international law standards with respect to nationality<sup>78</sup> have been brushed aside as not determinative.<sup>79</sup>

Another statutory term, "United States person," which along with "person subject to the jurisdiction" is at the heart of the Export Administration Act,<sup>80</sup> presents the important issue of "nationality." The FAC Regulations ascribe nationality, for purposes of the Act, to a corporation based either on its place of incorporation (or for civil law companies its principal place of management or *siège*)<sup>81</sup> or on the nationality of its shareholders.<sup>82</sup> Thus, it departs from the traditional reliance solely on place of incorporation or *siège*<sup>83</sup> by introducing the nationality of the shareholders as well. In consequence, dual nationality becomes a possibility in the case of a corporation incorporated in one nation-state with shareholders who are nationals of a different nation-state.

Recognizing the widespread international distribution of shareholdings in the large multinational corporations, the Regulations further provide that the nationality of shareholders will be attributed to the corporation wherever twenty-five percent or more of the shares are held by nationals of a particular country; where the place of incorporation is in a different country, the corporation is treated as being a national of both.<sup>84</sup> In cases of dual nationality, the FAC Regulations provide that *either* nationality may be utilized to support the application of the Act.<sup>85</sup>

Although the Export Administration Act makes no reference to control, the FAC Regulations and several other regulations that govern trade with

77. 31 C.F.R. § 500.329(d) (1995).

78. *E.g.*, *Sumitomo Shoji Am., Inc. v. Avagliano*, 457 U.S. 176 (1982); *Barcelona Traction, Light & Power Co. (Belgium v. Spain)* Feb. 2, 1970, 1970 I.C.J. 4.

79. Thus, the European Union and other foreign nations have bitterly objected to U.S. extraterritorial implementation of the FAC Regulations as "repugnant" to international law. Joseph E. Pattison, *Extraterritorial Enforcement of the Export Administration Act in*, EXPORT CONTROLS 87, 88 (Michael R. Czinkota & Scot Marciel eds., 1984); Clyde H. Farnsworth, *U.S. to Penalize Those Violating Curbs on Soviet*, N.Y. TIMES, June 24, 1982, at A1.

80. 50 U.S.C. app. §§ 2402(5), 2404(a)(1) (1994).

81. 31 C.F.R. § 500.302. Although the common law countries use the state of incorporation standard, the European civil law countries employ the concept of the *siège* or seat of the principal management. See THIRD RESTATEMENT, *supra* note 53, § 213, reporters' note.

82. 31 C.F.R. §§ 500.302-.303 (FAC Regs.); *id.* § 515.330(a)(4) (Cuban Assets Control Regs.).

83. See *Barcelona Traction*, 1970 I.C.J. at 4.

84. 31 C.F.R. § 500.303(c).

85. *Id.* § 500.303(a).

designated nations apply the prohibitions and licensing requirements of the statute to parties controlled by U.S.-based multinational corporations, thereby including foreign subsidiaries.<sup>86</sup> These include the regulations that established the embargoes against China, North Korea, the Soviet Union, and Cuba.

In some programs, however, concerns about imposing too high a barrier to U.S. trade opportunities or the likelihood of confrontation with nations that are U.S. trading and political partners have resulted in a curtailment of the regulatory program. In these programs, the regulations carefully exclude foreign subsidiaries from some or all of the regulatory program. Such exclusions include the Cuban Assets Control Regulations prior to 1992, the Libyan Sanctions Regulations, the Iraqi Sanctions Regulations, the Former Republic of Yugoslavia and Bosnia-Herzegovina Sanctions Regulations, the Unita (Angola) Sanctions Regulations, and the antiboycott provisions of the Export Administration Act.<sup>87</sup>

#### (i) Cuban Assets Control Regulations

Until 1992, the Cuban embargo was distinctly looser than the comparable embargoes against China in connection with the Korean War<sup>88</sup> and against the Soviet Union in connection with the Siberian Pipeline at the time of its invasion of Afghanistan and intrusion into Poland.<sup>89</sup> Although the Cuban regulations utilized the same sweeping concept of control, the substantive licensing provisions contained a vital exception for thirty years until the passage of the Cuban Democracy Act of 1992.<sup>90</sup> Until then, in the same manner as the China and Soviet Union embargoes, the Cuban regulations defined a "person subject to the jurisdiction of the United States" and "a person within the United States" to include "[a]ny corporation . . . wherever organized or doing business, that is owned or controlled by" U.S. individuals or corporations.<sup>91</sup> However, in contrast to the more far-reaching China and Soviet Union embargoes, for thirty years, the Cuban regulations attempted to avoid or minimize confrontation with other powers. They did so by expressly authorizing certain Cuban transactions by United States-owned or controlled corporations located in third countries "where local law requires,

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86. *Id.* §§ 500.329(d), 500.330(a)(4); §§ 515.329(d), 515.330(a)(4) (Cuba); § 535.329(d) (Iran).

87. 50 U.S.C. app. §§ 2402-2420.

88. 31 C.F.R. pt. 515.

89. 31 C.F.R. pt. 500, § 505.10; 47 Fed. Reg. 27,250 (1982).

90. Pub. L. No. 102-484, 106 Stat. 2575 (1992), (codified at 22 U.S.C. § 6001 (1994)).

91. 31 C.F.R. §§ 515.329(d), 515.330(a)(4).

or policy . . . favors[] trade with Cuba.”<sup>92</sup> To qualify, an affiliate granted such a license had to be “generally independent, in the conduct of transactions of the type for which the license [was] . . . being sought, in such matters as decision-making, risk-taking, negotiation, financing or arranging of financing, and performance.”<sup>93</sup> These references on the role of control in enforcing the Cuban embargo appear to have contemplated the exercise of control in a hierarchical relationship, but throw no light on the treatment of a case of shared control.

This relaxation of the embargo came to an end with the enactment of the Cuban Democracy Act of 1992, subsequently stiffened even further by the Cuban Liberty and Democratic Solidarity (Libertad) Act of 1996.<sup>94</sup> These statutes significantly extended the outer boundaries of the coverage of the Cuban trade controls by giving full range to the concept of control.<sup>95</sup> The 1992 Act expressly prohibited the issuance of further licenses pursuant to the earlier exclusion and thereby barred all foreign subsidiaries of U.S.-based multinationals from trade with Cuba.<sup>96</sup>

## (ii) Antiboycott Regulations

The Antiboycott Act<sup>97</sup> (an amendment of the Export Administration Act) sets forth the general policy of the United States “to oppose restrictive trade practices or boycotts fostered or imposed by foreign countries against

92. 31 C.F.R. § 515.559(b). Subsection 559 authorized the issuance of special licenses for such foreign transactions in cases where:

- (i) The commodities to be exported are non-strategic;
- (ii) United States-origin technical data (other than items related to maintenance, repair and operations data) will not be transferred;
- (iii) U.S.-origin parts and components . . . ha[ve] been authorized by the Department of Commerce;
- (iv) U.S.-origin spares . . . ha[ve] been authorized by the Department of Commerce;
- (v) No U.S. Dollar accounts are involved; and
- (vi) Any financing . . . by a U.S.-owned or controlled firm is granted on normal short-term conditions . . . .

*Id.* § 515.559b(1)(i)-(vi).

93. *Id.* § 515.559(d). No person within the United States, including the parent corporation or any officer or employee, may assist or participate in the negotiation or performance of the transaction in question. *Id.*

94. 22 U.S.C.A. § 6003 (Supp. 1997); Pub. L. No. 104-14, § 102, 110 Stat. 792-94 (1996).

95. 22 U.S.C.A. § 6005; Pub. L. No. 104-14, § 102, 110 Stat. at 792-94. Among other things, the Libertad Act penalizes persons “involved in the confiscation or trafficking in confiscated American property” by denying entry into the United States for any alien who is a controlling person of any such entity.” *Id.* § 401(a)(3), 110 Stat. at 822.

96. 22 U.S.C.A. § 6005 (a)(1).

97. 50 U.S.C. app. §§ 2401-2420 (1994).

other countries friendly to the United States or against any United States person."<sup>98</sup> It was aimed at the secondary and tertiary boycotts of Israel by the Arab States.<sup>99</sup> It also was aimed at personal boycotts of individuals, and organizations that include such individuals, because of their religion, national origin, or the like. Notwithstanding the primary statutory objective to deter U.S. participation in the Arab Boycott, the regulations are tempered by a desire not to impede excessively U.S. trade with Arab nations, particularly where conducted by foreign subsidiaries of U.S. corporations.

The outer boundaries of the antiboycott regulatory program rests on three crucial statutory terms: "United States persons," "controlled in fact," and "commerce of the United States."

*United States persons.* The statute directs the President to "issue regulations prohibiting any United States person" from intentionally complying with or supporting such boycotts in its "activities in the interstate or foreign commerce of the United States."<sup>100</sup> It defines "United States persons" to include "any foreign subsidiary or affiliate . . . of any domestic concern which is controlled in fact by such domestic concern."<sup>101</sup>

*Controlled in fact.* "Controlled in fact" is a statutory standard requiring proof not merely of control but of the "authority or ability of a domestic concern to establish the general policies or to control the day-to-day operations" of its foreign subsidiary, affiliate, or establishment.<sup>102</sup> This definition is remarkably loose. In many cases arising under other contexts, a parent's control over the "general policies" of a subsidiary has been regularly brushed aside as characteristic of many, if not most, group interrelationships and therefore without legal significance.<sup>103</sup> On the other hand, control over day-to-day operations is near universally accepted as a touchstone of vicarious liability or other attribution of legal rights and responsibilities for parent and subsidiary corporations.<sup>104</sup> The statute establishes a rebuttable presumption of control where the same individuals

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98. *Id.* § 2402(5).

99. In a "primary" boycott, the boycotting country refuses to buy the products of boycotted countries. In a "secondary" boycott, the boycotting country refuses to buy products of third parties not observing the primary boycott. In a "tertiary" boycott, the boycotting country brings pressure on third parties to abstain from trading with parties blacklisted for not participating in a primary boycott. *Id.*

100. *Id.* § 2407(a)(1).

101. *Id.* § 2415(2).

102. 15 C.F.R. § 760.1(c) (1) (1997).

103. *See Phoenix Can. Oil Co. v. Texaco, Inc.*, 842 F.2d 1466, 1476-77 (3d Cir. 1988); *Miles v. American Tel. & Tel. Co.*, 703 F.2d 193 (5th Cir. 1976).

104. *E.g.*, *Mylan Labs., Inc. v. Akzo, N.V.*, 2 F.3d 56 (4th Cir. 1993); *Curtis Pub'g Co. v. Cassel*, 302 F.2d 132 (10th Cir. 1962); *Rae Prods. & Chems. Corp. v. Elf Aquitaine, Inc.*, 1994 U.S. Dist. LEXIS 8390, at \*8 (N.D. Ill. June 21, 1994); *see BLUMBERG, PROCEDURAL PROBLEMS, supra* note 1, § 3.05.2.

comprise a majority of the domestic concern and the foreign firm, or where the domestic concern has the authority to appoint a majority of the foreign board or its chief executive.<sup>105</sup>

*Commerce of the United States.* Reflecting the ambivalence of the Act, the regulations carefully restrict the situations that are included within the foreign commerce of the United States to which the Act is directed. These situations include acts of a "United States person" such as "specifically directing the activities" of the foreign concerns, furnishing financing for a foreign transaction, and "providing financial, accounting, legal, transportation, or other ancillary services" in connection with a foreign transaction.<sup>106</sup> This is directed only against the "United States person"; the underlying transaction itself is *not* deemed to be within "United States commerce."<sup>107</sup> Transactions by a foreign concern entirely outside the United States are only in "United States commerce" when they involve United States goods, services, or information acquired from persons in the United States for purpose of filling an order or used in the manufacture of another product for purpose of filling the order.<sup>108</sup>

Supplementing these provisions, section 999 of the Internal Revenue Code denies certain tax benefits to taxpayers cooperating in the Arab or any other proscribed international boycott.<sup>109</sup> In addition, it contains extensive reporting provisions.<sup>110</sup> These include not only the taxpayer, but also any corporate group of which the taxpayer is a member, thereby including all parent, subsidiary, and affiliate companies, including subsidiaries in which it holds directly or indirectly more than ten percent of the shares.<sup>111</sup>

#### d. *Labor Relations, Employment, and Antidiscrimination*

The federal statutes regulating labor relations, discrimination, and other employment problems provide a final illustrative example of the application of statutes selectively introducing enterprise principles. These labor and employment statutes are unique. Resting on administrative and judicial action, these statutes receive a sweeping enterprise construction that, unlike other areas of U.S. law, rests not on the usual standards of control, but on a unique "integrated enterprise" standard.

Reliance on enterprise concepts under these statutory programs originated with the administrative implementation of the labor relations laws. Although

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105. 15 C.F.R. § 760.1(c)(2).

106. *Id.* § 769.1(d)(2)-(5).

107. *Id.* § 769.1(d)(4), (5).

108. *Id.* § 760.1(d).

109. 26 U.S.C.A. § 999 (1996).

110. *Id.*

111. *Id.* § 999(a)(1), (e).



the National Labor Relations Act (NLRA)<sup>112</sup> is entirely silent on the matter, the National Labor Relations Board (NLRB) gave a dramatic enterprise construction to such fundamental terms as “employer” and “employee,” going far beyond their common-law definition.<sup>113</sup> In an action supported by the courts,<sup>114</sup> the NLRB established an integrated enterprise standard for determining a “single employer” for vital purposes of the Act.<sup>115</sup> In determining the jurisdiction of the statute depending on the number of employees, in determining the appropriate collective bargaining unit, and in assessing responsibility for unfair labor practices, the Board abandoned reliance on the separate juridical existence of related parties and replaced the traditional common-law standard with the integrated enterprise standard fashioned for the purpose.<sup>116</sup>

The integrated enterprise standard relies on four operational or structural elements of the related companies: “interrelation of operations, common management, centralized control of labor relations and common ownership” (or financial control of the related companies).<sup>117</sup> It is settled that centralized control of labor relations is the most important of the four elements, and that it is not necessary for all other elements to be present.<sup>118</sup>

The integrated enterprise standard not only governs labor relations law, but also governs numerous other statutory areas in the labor and employment field. As will be seen, the Congress has expressly adopted it for certain employment discrimination questions. The Regulations under the Worker Adjustment and Retraining Notification Act similarly incorporate the integrated enterprise standard to determine when member companies of a corporate group constitute a single employer.<sup>119</sup> Finally, the courts have widely applied it in the construction of other statutes in the labor and employment field, including the Fair Wages and Hours Act and the antidiscrimination employment statutes. Like the NLRA, these statutes contain no reference to control or otherwise endorse enterprise principles.<sup>120</sup>

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112. 29 U.S.C. §§ 151-169 (1994).

113. 21 N.L.R.B. ANN. REP. 14-15 (1956).

114. *Radio & Television Broadcast Technicians Local Union 1264 v. Broadcast Serv. of Mobile, Inc.*, 380 U.S. 255, 256 (1965) (per curiam) [hereinafter *Radio & Television Broadcast Union*].

115. *Id.*

116. 21 N.L.R.B. ANN. REP., *supra* note 113, at 14-15; see *Radio & Television Broadcast Union*, 380 U.S. at 256.

117. *Radio & Television Broadcast Union*, 380 U.S. at 256 (citing *Sakrete of N. Cal., Inc.*, 332 F.2d 902, 903 (9th Cir. 1964)); 21 N.L.R.B. ANN. REP., *supra* note 113, at 14.

118. *E.g.*, *Carpenters' Local Union No. 1478 v. Stevens*, 743 F.2d 1271, 1276 (9th Cir. 1984); *NLRB v. Don Burgess Constr., Corp.*, 596 F.2d 378, 385 (9th Cir. 1979).

119. 29 U.S.C. § 2101 (1) (1994), 20 C.F.R. § 693.3(a)(2) (1997).

120. The antidiscrimination statutes were subsequently amended to incorporate the integrated enterprise standard for purposes of extraterritorial application.

Perhaps, the greatest triumph of the enterprise standard has occurred in the employment discrimination area. In this area, the courts have widely refused to approve extraterritorial application. They did so in the case of the labor relations,<sup>121</sup> employment,<sup>122</sup> and antidiscrimination statutes<sup>123</sup> because the statutes fail to include a clear statement by the Congress. In the case of the antidiscrimination statutes, however, the Congress chose to overrule the judicial decisions. It expressly extended the coverage of the antidiscrimination statutes to workers employed abroad by controlled foreign subsidiaries of U.S. corporations.<sup>124</sup> Congress did so by introducing the concept of control, which it defined by incorporating *in haec verba* the NLRB integrated enterprise standard.<sup>125</sup>

With centralized control of labor relations as its key factor, the integrated enterprise standard is a vivid example of how the meaning of control reflects the context in which it is being used. This standard is nearly irrelevant in other contexts. Controlled foreign subsidiaries for labor purposes constitute a very different class than controlled foreign subsidiaries for purposes for which centralized control of labor relations is not an indispensable element. Accordingly, the doctrine is inapplicable in areas other than labor relations, employment, and discrimination matters.

#### 4. Control and Shared Control in Statutes of Specific Application

Under statutes of specific application, the mere possession of control is typically decisive for imposition of statutory liability on the controlling party and frequently for application of enterprise liability to an affiliated corporation. The legislation as implemented by the administrative agency with jurisdiction has so provided. This decisive role for control has led to a correspondingly expanded imposition of liability for a party with shared control.

Many statutes of specific application and the regulations thereunder expressly acknowledge that shared control or some form thereof is sufficient to trigger the application of the statute. They do so by references, making it clear that control may be possessed or exercised by the collective action of several holders. Thus, the statutes and regulations typically provide that

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121. *McCulloch v. Sociedad Nacional de Marineros de Honduras*, 372 U.S. 10, 20 (1963); *Benz v. Compania Naviera Hidalgo, S.A.*, 353 U.S. 138, 143 (1957).

122. *Lauritzen v. Larsen*, 345 U.S. 571, 593 (1953) (Jones Act); *Foley Bros., Inc. v. Filardo*, 336 U.S. 281, 281 (1949) (Eight Hour Day Act).

123. *EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244, 244 (1991) (Aramco).

124. Age Discrimination in Employment Act, 29 U.S.C. § 623(h) (1994) (ADEA).

125. It may be noted that this is still another illustration of the use of control as a legal standard in this area that is entirely unrelated to control over the election of a majority of the members of the board of directors.

control may arise “directly or indirectly.”<sup>126</sup> They refer to “controlling shareholders” in the plural, to shareholders “acting in concert,”<sup>127</sup> or to control arising “pursuant to an arrangement” or “understanding,” or a “contract,” or “otherwise.”<sup>128</sup> They expressly recognize that it is irrelevant whether control is exercised alone or through others.<sup>129</sup>

Control exercised through others adds little to the common law doctrines that otherwise would have governed. Control exercised through agents, intermediaries, or shams remains, notwithstanding the interposition of another juridical entity, the act of the shareholder with control. This is merely a variation of the form in which a shareholder may exercise control without the consultation or participation of others. It is not shared control, it is agency.

Control exercised in concert is something else again. Where control means the power to elect a majority of the board of directors and thereby direct or command the direction of the management and policies of the corporation, as it does in most statutes of specific application to corporate groups, the power may be exercised solely or by a group of shareholders. The participating parties in such a control group collectively occupy the role that has been identified as the triggering factor for the application of the statutory program. Such statutory references in the holding company laws, accordingly, represent an express adoption of the concept of shared control. For a group, however, to have control under these circumstances, it must be cohesive, and the members must act in concert. Their collective action in the election of directors must be accomplished through consultation and coordination.<sup>130</sup>

In light of the foregoing, it is apparent that shared control under such statutes presents no inherent, conceptual difficulties in imposing statutory obligations on all members of the control group. It gives rise only to evidentiary problems when examining the group dynamics in order to determine the nature of the participation of the individual constituents of the group allegedly asserting control.

The antiboycott statute and regulations provide insight into the nature of shared control in a very different context. In this area, the provisions extending the regulatory program to include subsidiaries “controlled in fact” have been given an expansive construction to include certain types of shared

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126. SLHCA, 12 U.S.C. § 1467a(a)(2); BHCA, 12 U.S.C. § 1841(a)(2)(A)(c); Securities Act of 1934, 15 U.S.C. §§ 78t(a); PUHCA, 15 U.S.C. 79b(7); ICA, 15 U.S.C. § 80a-2(a)(9); FLA. STAT. § 665.034(4)(a) (1995).

127. SLHCA, 12 U.S.C. § 1467a(a)(2)(A); FLA. STAT. § 665.034(4)(a).

128. Securities Act of 1933, 15 U.S.C. § 77o; PUHCA, 15 U.S.C. § 79b(a)(7)(B); Securities Act of 1933, 17 C.F.R. § 230.405 (1996) (Rule 405).

129. BHCA, 12 U.S.C. § 1841(a)(2)(A).

130. See 1 FRANKEL, *supra* note 51, at 518-19; 4 LOSS & SELIGMAN, *supra* note 17, at 1722-26.

control. The regulations provide that twenty-five or more percent voting stock ownership will satisfy the controlled-in-fact standard if no one else owns an equal or larger percentage. However, if concerns with minority holdings that in the aggregate satisfy this requirement regularly pool their shares and vote "in concert," they are collectively presumed to have control.<sup>131</sup> For these purposes, all the participants have joined in the final formulation of the corporate action. Participation in the collective process stamps them all as parties with control. This is an active or direct example of shared control. However, the reference plainly does not extend to passive parties possessing no more than a "veto" or "consultation" power.

However, under certain statutes of specific application, including the securities laws and the pervasive holding companies statutes, the statutory program includes not only persons acting in concert, but under certain circumstances, even other shareholders who are distinctly less active, or even passive or inactive. In these areas, the governing statute imposing controlling person liability expressly turns on control, with the mere possession of control or participation in shared control deemed sufficient for statutory liability in many contexts. Thus, it is no surprise that so much of the legal material available on the legal implications of shared control relates to the holding company and securities laws.

Thus, where a party does not participate in the final determination of policy, its indirect or passive participation in the preliminary processes of decisional evaluation before final decision also may be viewed as control for certain purposes. The SEC and the courts have gone further. Even where a party does not participate in the preliminary stages of the decisionmaking process but only is consulted or has a veto power before the other members of the control group proceed with their decision, the SEC and the courts have recognized that this somewhat diminished power still may satisfy the requirements of control (or of controlling influence) for certain aspects of the statutes at issue. This ready acceptance of passive "voice" as sufficient for control is most apparent under the statutes utilizing enterprise principles pervasively.

In other statutes of specific application that apply enterprise principles and the concept of control only in selected areas,<sup>132</sup> shared control no longer plays an important role. As the experience in the foreign trade and investment area illustrates, there are virtually no materials on the role of

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131. Restrictive Trade Practices or Boycotts Act, 15 C.F.R. § 760.3 (1996).

132. While the securities laws should be included as one of the class of statutes selectively using enterprise principles, the SEC administering them has brought into play concepts of control that extend much further than under other selective statutes. The SEC has evidently been influenced by its development of control concepts in its administration of the PUHCA with its pervasive utilization of enterprise principles.

shared control except in its most active form with respect to concerted action in election of the board of directors. Neither the statute nor the regulations provide guidance on whether less active participation in shared control will suffice to trigger the application of the statutory program.

With their standard of the integrated enterprise for determining the existence of a "single employer," the labor relations, employment, and antidiscrimination statutes provide a final example of specific application of enterprise principles.<sup>133</sup> As reviewed above, the crucial factor in this area is not the general control or shared control over the different facilities or operations in question, but the nature of control in their labor operations. If control or shared control result in a "centralized control of [the] labor relations" of the different facilities or operations in question, together with other factors of lesser importance for this purpose, such as interrelationship of operations, common management, and common ownership or financial control, the operations will be deemed a "single enterprise" for purposes of these statutes.<sup>134</sup>

Since these issues primarily relate not to the parties participating in the exercise of such shared control over labor matters, but to the facilities and operations that are subject to it, the decisions in this area are of more limited usefulness. If enterprise liability is found, it has important but not unrestricted consequences. It will result in a finding of statutory jurisdiction or a determination that the separate facilities or operations constitute a single bargaining unit or that one of the controlled companies has committed an unfair labor practice. However, it does not lead to any group liability for other purposes either under the statute or for other areas.

A final word of caution. As previously emphasized, it must be recognized that even where the experience with respect to the statutes of specific application provides instances of shared control sufficient to render a party subject to the statutory program, such instances have application only for the particular statute under consideration and further, only for the particular context of the statute involved.

In summary, in the statutes expressly applying enterprise principles, the statutes, regulations, and administrative adjudications play the primary role in determining the other contours of the doctrines of control and shared

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133. It is irrelevant that for purposes of the problem under review, in some of these statutes, such as the labor relations and employment laws, the governing standards relying on enterprise standards, including control, may be found in administrative regulations and adjudication rather than in the statute. In either case, the applicable standard has been determined when the case reaches the court.

134. See *Radio & Television Broadcast Union*, 380 U.S. at 256; 21 N.L.R.B. ANN. REP., *supra* note 113, at 14. As noted, courts have held the enterprise developments under the labor laws to be irrelevant for purposes of consideration of whether enterprise principles should be applied in nonlabor areas.

control. The courts have a much reduced role, largely confined to enforcing the enterprise principles applied by statute or administrative action.<sup>135</sup>

Thus, in statutes of specific application, control serves as the decisive factor determining the scope of the regulatory program. The picture changes sharply where one moves to other areas of law. These other areas include on the one hand, the construction and application of statutes of general application, in which no specific reference is made either to control or to corporate groups and on the other hand, judicial decisions considering issues of enterprise liability or piercing the veil in common law controversies, either involving the government in issues of great public importance or private parties in which only private concerns are involved.<sup>136</sup>

### C. *Statutes of General Application*

#### 1. Enterprise Law

In addition to the statutory programs specifically employing enterprise principles based on control, there are numerous statutes in which neither the Congress nor the agency administering the program has addressed the problems presented by parent and subsidiary corporations and corporate groups. These are the statutes referred to as the statutes of general application. In construing and applying these statutes, the courts have directly formulated enterprise principles in an impressive number of areas and have widely expanded the range of application of the act, notwithstanding the absence of any express statutory or administrative direction. This part briefly considers this use of enterprise law and control in general before turning to the environmental laws as the leading example of this development and concludes with a discussion of the role of shared control in this area.

In introducing enterprise principles when construing statutes of general application, the courts have utilized a variety of approaches to transcend traditional legal doctrines in order to impose obligations on a parent or subsidiary corporation for the statutory obligations of one of the corporations affiliated with the group. In applying enterprise principles in the absence of any direct statutory or administrative reference to imposition of liability on the parent corporation or other affiliate, the courts have frequently rejected application of state common law, consisting of traditional corporation law, entity concepts, and the rigorous requirements of traditional piercing the veil jurisprudence. They have instead introduced enterprise principles in the formulation of an emerging federal common law that governs the construction of certain statutes. They have done so in order to implement more

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135. See *Tcherepnin v. Knight*, 389 U.S. 332 (1967).

136. See *id.*

effectively the statutory policies and objectives, to prevent frustration of the program, and to close the door to evasion of the law through the interposition of a subsidiary.<sup>137</sup>

This federal route to enterprise law has taken a number of forms. Some courts have used the historic acceptance in federal law that regulatory statutes are "remedial" statutes to be construed in a "broad" or "liberal" manner as a starting point.<sup>138</sup> They have given an expansive construction to statutory terms such as "employer" and "employee" in the labor relations, employment, and antidiscrimination statutes,<sup>139</sup> and "owner" or "operator" in CERCLA by defining the statutory terms pragmatically, according to the economic realities of the enterprise in which they operate rather than by reference to traditional doctrinal concepts of juridical identity.<sup>140</sup> Under this conceptual framework, courts have applied enterprise principles and imposed intra-enterprise liability on group affiliates of companies committing the violations in question. Other courts have rested an enterprise construction of a statute squarely on pragmatic federal considerations without relying on a federal construction of statutory terms. In *General Telephone Co. v. United States*, the Court of Appeals for the Fifth Circuit upheld application of enterprise principles in reliance on the judgment of the administrative agency essential to preventing evasion of the statute.<sup>141</sup> The court said:

Where the statutory purpose could thus be easily frustrated through use of separate corporate entities, the Commission is entitled to look through the corporate form and treat the separate entities as one and the same for purposes of regulation. . . . The Commission has concluded that the ends it sought could not be achieved without drawing carrier affiliates under the aegis of Section 214 and this we

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137. Thus, major provisions of the railroad statutes in the 1920s had been avoided by railroads and shippers conducting proscribed activities through subsidiaries or holding companies. The courts refused to interfere so long as the subsidiaries had some real existence. See *United States v. Elgin, Joliet & Eastern Ry.*, 298 U.S. 492 (1936); *United States v. Lehigh Valley R.R.*, 220 U.S. 257 (1911); see BLUMBERG, *GENERAL STATUTORY LAW*, *supra* note 1, §§ 19.02.1-4.

138. See generally *Peyton v. Rowe*, 391 U.S. 54 (1968); *Tcherepnin*, 389 U.S. at 332; *United States v. Pollution Abatement Servs. of Oswego, Inc.*, 763 F.2d 133, 135 (2d Cir.), *cert. denied sub nom. Miller v. United States*, 474 U.S. 1037 (1985).

139. After 60 years in which this philosophy of statutory construction has been supreme, recent decisions of the Supreme Court indicate that it is reconsidering this approach. *Patterson v. Shumate*, 504 U.S. 753 (1992); *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318 (1992).

140. *Schiavone v. Pearce*, 79 F.3d 248 (2d Cir. 1996); *United States v. TIC Inv. Corp.*, 68 F.3d 1082 (8th Cir. 1995); *FMC Corp. v. Department of Commerce*, 29 F.3d 833 (3d Cir. 1994); *Sidney S. Arst Co. v. Pipefitters Welfare Educ. Fund*, 25 F.3d 417 (7th Cir. 1994); *Jacksonville Elec. Auth. v. Bernuth Corp.*, 996 F.2d 1107, 1110 (11th Cir. 1993); *United States v. Carolina Transformer Co.*, 978 F.2d 832 (4th Cir. 1992).

141. 449 F.2d 846, 855 (5th Cir. 1971).

find is permissible.<sup>142</sup>

Other decisions have utilized federal versions of modified piercing the veil jurisprudence to accomplish an enterprise result. As is well known, the traditional piercing standards will provide a basis for courts of equity to intervene only in "rare" or "exceptional" cases.<sup>143</sup> The traditional piercing doctrine employs standards that are rigorous, involve exaggerated respect for corporate forms, and ignore economic realities. For application of the traditional doctrine, the courts require violation of accepted corporate norms and formalities, the intrusive exercise of the parent's (or controlling shareholder's) power of control, and a demonstration that the corporate form has been used to accomplish a fraudulent or inequitable objective. These traditional standards make enterprise implementation of statutory programs exceedingly difficult in cases where enterprises routinely utilize sophisticated legal advice in establishing their corporate structure, financing, and operational procedures.

Accordingly, in the statutory area, a number of courts have developed a federal version of modified piercing jurisprudence that has significantly broadened the extent of enterprise construction of a statute of general application.<sup>144</sup> They have accomplished this result through a number of techniques.

Many courts have said that piercing in cases involving issues of public policy and statutory law rests on different standards than those governing common-law controversies between private parties. In particular, they have singled out the importance of the corporate form, which plays a major role under the traditional doctrine.<sup>145</sup> Illustrating this approach, the Court of Appeals for the First Circuit, in *Town of Brookline v. Gorsuch*, which was decided under the environmental laws, stated that in applying the federal law on piercing the veil in the statutory area, "federal courts will look closely at the purpose of the federal statute to determine whether the statute places importance on the corporate form, . . . an inquiry that gives less respect to the corporate form than does the strict common law alter ego doctrine."<sup>146</sup>

As another technique for relaxing traditional piercing standards, some other courts have held that the traditional requirement of "fraud or inequity" or other "unfair" conduct victimizing the plaintiff does not apply in statutory

142. *Id.* (citation omitted).

143. *See, e.g., Baker v. Raymond Int'l, Inc.*, 656 F.2d 173, 179 (5th Cir. 1981).

144. Blumberg, *supra* note 46, at 321, 328-32.

145. *Alman v. Danin*, 801 F.2d 1, 3 (1st Cir. 1986); *Town of Brookline v. Gorsuch*, 667 F.2d 215, 221 (1st Cir. 1981); *Capital Tel. Co. v. FCC*, 498 F.2d 738, 734 (D.C. Cir. 1974); *see United States v. Firestone Tire & Rubber Co.*, 518 F. Supp. 1021, 1039 (N.D. Ohio 1981) ("Thus corporate formalities cannot be used to circumvent a statutory policy.").

146. *Town of Brookline*, 667 F.2d at 221 (citation omitted).



matters. These courts have held that proof of a violation of the statute by the group component performing the proscribed activity satisfied any requirement of this nature.<sup>147</sup> In so doing, the courts were rejecting the traditional view in torts that proof of the commission of the tort was insufficient in itself to constitute the “fraud or inequity” or “unfair” conduct essential for the attribution of liability from one group component to another.<sup>148</sup>

A final technique facilitating judicial use of enterprise principles has been the adoption of liberalized notions of attribution of information and activity from one group component to another because of the role of individuals who simultaneously hold office in both group components involved. These courts have rejected concepts of the traditional corporation law that focused on the offices held and not on the presence of the same individual. The theory relied on by the older law was that the acts and information of the individual could not be attributed from one company to another. It was said that the individual was wearing his or her “hat” as an officer of the particular company in question, and the significance of the act or information was restricted to that company.<sup>149</sup> Some modern decisions have rejected this “hats” theory as grossly unrealistic and utilize the role of the common officer as a significant factor for application of liability for statutory matters;<sup>150</sup> other courts have done the same for common-law purposes, particularly tort matters.<sup>151</sup>

In the foregoing applications of enterprise principles, control plays a very important role, but unlike so many statutes of specific application, it is not decisive. In these instances, it is only one of a number of elements. The emphasis has moved from the possession of control to the manner and extent of its exercise. In consequence, shared control has a sharply reduced significance in this area in contrast to its important role in many statutes of specific application.

With the statutes of general application providing no textual support for the applicability of enterprise principles, the courts in this area must turn to

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147. *E.g.*, *United Steel Workers of Am. v. Connors Steel Co.*, 855 F.2d 1499, 1506-08 (11th Cir. 1988).

148. *See* BLUMBERG, *SUBSTANTIVE COMMON LAW PROBLEMS*, *supra* note 1, § 9.03 (cases not requiring supplemental showing of unfairness); *id.* § 9.02 (cases requiring proof of some fraud, and inequitable, unfair, or morally culpable conduct in addition to the tort for piercing in tort cases). Some cases dispose with the requirement where the subsidiary is devoid of significant indicia of independent existence.

149. *United States v. Jon-T Chems., Inc.*, 768 F.2d 686, 691 (5th Cir. 1985); *Edwards Co. v. Monogram Indus., Inc.* 730 F.2d 977, 985-86, 986 & n.14 (5th Cir. 1984).

150. *Dania Jai-Alai Palace, Inc. v. Sykes*, 450 So. 2d 1114 (Fla. 1984); *see* BLUMBERG, *SUBSTANTIVE COMMON LAW PROBLEMS*, *supra* note 1, § 20.11, at 529-30.

151. *American Pioneer Life Ins. Co. v. Sandlin*, 470 So. 2d 657, 668 (Ala. 1985); *Electric Power Bd. v. St. Joseph Valley Structural Steel Corp.*, 691 S.W.2d 522, 527 (Tenn. 1985); *see* BLUMBERG, *SUBSTANTIVE COMMON LAW PROBLEMS* § 10.2, at 190.

federal or state common law. Thus, choice of law often plays a decisive role at the very threshold of judicial consideration of the problem.<sup>152</sup>

When choice of law is resolved in favor of the adoption of state common law, enterprise liability rarely occurs. State common law means that the matter is determined by traditional corporation law. Corporation law is grounded on traditional entity law concepts, stressing the separate and distinct juridical identity of each corporation, even in the case of subsidiaries collectively conducting parts of an integrated enterprise under the control of a parent corporation. For these courts, entity law inevitably prevails unless the case is the "rare" or "exceptional" case that satisfies the rigorous requirements of traditional piercing the veil jurisprudence. In consequence, enterprise concepts receive no more than isolated recognition.

However, when courts apply federal common law to determine the outer scope of the statute, they are able to turn to a well-developed body of federal jurisprudence that has adopted the application of enterprise principles in statutory construction and application. Such reference to federal common law opens the door to the use of the foregoing liberal concepts of statutory construction or of modified variants of piercing the veil jurisprudence to support the imposition of enterprise liability in the enforcement of the regulatory program.

## 2. Environmental Law

Environmental laws relating to hazardous waste provide a particularly interesting example of judicial construction of a statute of general application leading to the introduction of enterprise principles for expanding the scope of the statutory program.<sup>153</sup> Statutory enforcement of environmental laws has resulted in much litigation, providing numerous decisions that throw considerable light both on the use of enterprise principles in statutes of general application and on the significance of shared control.

Environmental laws comprise a series of statutes dealing with air, water, and hazardous waste. In recent years, hazardous wastes in general, and the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)<sup>154</sup> in particular, have occupied center stage and have been the

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152. Choice of law for this purpose is far from clear. Where the court is proceeding through construction of the federal statutes, they have frequently disagreed on whether federal or state common law governs. Some of the courts applying federal common law have conceded that they are "guided" by state law in so doing. However, where traditional piercing the veil is the test, state law is the accepted standard.

153. For an interesting comparative discussion, see Karl Hofstetter, *The Ecological Liability of Corporate Groups: Comparing US and European Trends in ENVIRONMENTAL LAW AND ECOLOGICAL RESPONSIBILITY* ch. 5 (Gunther Teubner et al. eds., 1994).

154. 42 U.S.C. §§ 9601-57 (1994).

subject of extended litigation. Along with the Resource Conservation and Recovery Act, CERCLA provides an extensive regulatory program controlling the generation, transportation, and disposal of hazardous wastes. It imposes extensive liability on the "owners" or "operators" of facilities at which hazardous wastes were disposed of and on any persons who "arranged" for the disposal of such wastes.

a. *Construction of "Owner," "Operator," and "Arranger"*

Most courts have agreed that the construction and application of the provisions of CERCLA are to be governed by a uniform federal common law.<sup>155</sup> They have further concluded that a "broad and liberal construction" of the statutory terms of "owner," "operator," and "arranger" was required to implement the underlying objectives and policies of the law.<sup>156</sup> This has set the stage for the application of enterprise principles, leading to the imposition of liability on the parent (or controlling shareholder) for the subsidiary's (or controlled corporation's) CERCLA violations.

One of the most widely litigated issues under the statute relates to the circumstances under which a parent corporation (or other controlling shareholder) will be deemed an owner or operator or arranger for purposes of the statute, by reason of the activities of its subsidiary (or controlled) corporation violating the Act. This has become a fiercely disputed issue on which the courts are divided. Numerous decisions, however contradictory in approach and result, provide a substantial body of law and insight into the significance of enterprise principles and the role of control and shared control in this area.

In earlier cases, courts did not tend to distinguish between owner and operator liability.<sup>157</sup> More recently, however, courts have tended to distinguish between the statutory references to "owner" and "operator" in considering the imposition of liability on a parent corporation in connection with a contaminated site owned by a subsidiary so as to make it liable for the environmental violations of the subsidiary.<sup>158</sup>

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155. *United States v. Kayser-Roth Corp.*, 724 F. Supp. 15, 19-20 (D.R.I. 1989), *aff'd*, 910 F.2d 24 (1st Cir. 1990), *cert. denied*, 498 U.S. 1084 (1991); see *United States v. A & F Materials Co.*, 578 F. Supp. 1249, 1254-55 (S.D. Ill. 1984).

156. See, e.g., *Schiavone*, 79 F.3d at 253-55; *B.F. Goodrich Co. v. Murtha*, 958 F.2d 1192, 1198-99 (2d Cir. 1992); *United States v. Reilly Tar & Chem. Corp.*, 546 F. Supp. 1100, 1112 (D. Minn. 1982).

157. See *City of New York v. Exxon Corp.*, 112 B.R. 540 (Bankr. S.D.N.Y. 1990).

158. See *Schiavone*, 79 F.3d at 254-55; *TIC Inv. Corp.*, 68 F.3d at 1091-92; *FMC Corp.*, 29 F.3d at 833; *Sidney S. Arst Co.* 25 F.3d at 421; *Bernuth Corp.*, 996 F.2d at 1110; *John S. Boyd Co. v. Boston Gas Co.*, 992 F.2d 401, 408 (1st Cir. 1993); *Carolina Transformer*, 978 F.2d at 836-37.

The courts have generally agreed that "owner" liability must rest on veil piercing;

Thus, relying on enterprise principles, no less than six Courts of Appeal, joined by many minor courts, have upheld the imposition of enterprise liability on parent corporations as operators.<sup>159</sup> These courts have relied on a variety of factors. Some have relied on the extensive degree of the parent's<sup>160</sup> general exercise of control over the affairs of the subsidiary and of integration of the operations of parent and subsidiary.<sup>161</sup> Some courts have relied on the parent or controlling shareholder's "actual,"<sup>162</sup> "active,"<sup>163</sup> or "day-to-day"<sup>164</sup> involvement in the planning and implementation of the subsidiary's disposal practices in particular. Still others have moved beyond "active" involvement, a standard that borders on traditional tort concepts dealing with direct liability. They have imposed liability on passive controlling persons who have failed to act notwithstanding their "capacity to prevent and abate" the violation.<sup>165</sup>

Thus, among these courts ready to apply enterprise principles, there is significant disagreement over the degree of involvement by the parent corporation (or its controlling shareholders) in the affairs of the subsidiary or in the violations themselves that is required for attributive liability. In its recent decision in *Schiavone v. Pearce*, the Court of Appeals for the Second Circuit recognized this division but declined to resolve it.<sup>166</sup>

Led by the Courts of Appeal for the Fifth and Sixth Circuits, a minority of courts, however, have flatly held that intragroup liability under CERCLA

however, whether "operator" liability is so restricted is a highly controversial issue.

159. These include decisions of First, Second, Third, Fourth, Seventh, Eighth, and Eleventh Circuit Courts of Appeal. See cases cited *supra* note 158.

160. As used in the text, references to parent corporations also include individual or other controlling shareholders and references to subsidiary corporations include controlled corporations.

161. *Colorado v. Idarado Mining Co.*, 916 F.2d 1486, 1490, 1492 (10th Cir. 1990); *Kaysner-Roth*, 724 F. Supp. at 16; *United States v. Nicolet*, 712 F. Supp. 1193, 1202-03 (E.D. Pa. 1989); *Exxon Corp.*, 112 B.R. at 552-53.

162. *Lansford-Coaldale Jt. Water Auth. v. Tonolli Corp.*, 4 F.3d 1209, 1220 (3d Cir. 1993) ("actual control").

163. *Kaysner-Roth Corp.*, 910 F.2d at 27 ("active involvement"); *United States v. Northeastern Pharmaceutical & Chem. Co.*, 579 F. Supp. 823, 848 (W.D. Mo. 1984) ("actively participating"), *aff'd in part, rev'd in part*, 810 F.2d 726 (8th Cir. 1986), *cert. denied*, 484 U.S. 848 (1987).

164. *The Fishbein Family Partnership v. PPG Indus., Inc.* 876 F. Supp. 764, 765 (D.N.J. 1994) ("day-to-day operations"); *City of N. Miami v. Berger*, 828 F. Supp. 401, 410-11 (E.D. Va. 1993).

165. *Carolina Transformer Co.*, 978 F.2d at 836-37; *Nurad, Inc. v. William E. Hooper & Sons Co.*, 966 F.2d 837, 842 (4th Cir.), *cert. denied sub nom. Mumaw v. Nurad, Inc.*, 506 U.S. 940 (1992); *CPC Int'l, Inc. v. Aerojet-Gen. Corp.*, 731 F. Supp. 783, 788 (W.D. Mich. 1989); *Idaho v. Bunker Hill Co.*, 635 F. Supp. 665, 672 (D. Idaho 1986) (finding that the parent company "had the capacity, if not total reserved authority, to make decisions and implement actions . . . to prevent and abate the damage"); see *Berger*, 828 F. Supp. at 409-11; *Quadion Corp. v. Mache*, 738 F. Supp. 270, 274 n.5 (N.D. Ill. 1990).

166. *Schiavone*, 79 F.3d at 254-55.

may be imposed only where the traditional standards of piercing the veil jurisprudence under applicable state law have been satisfied.<sup>167</sup> They have rejected any manipulation of the terms "owner" or "operator" in order to impose liability on parent corporations (and controlling shareholders) for violation by a subsidiary (or controlled) corporation. They have contended that such an important consequence should be imposed by Congress, not the courts.

Where piercing is the standard, the imposition of CERCLA liability on the parent corporations usually does not follow. The cases demonstrate that the rigorous requirements of piercing the veil jurisprudence present a formidable obstacle to attempts to impose enterprise liability under CERCLA through this approach in its traditional form. Only a minority of courts have imposed CERCLA liability based on piercing jurisprudence.<sup>168</sup>

In summary, the controversy over the fundamental standards governing the imposition of CERCLA liability to component companies of corporate groups, pursuant to enterprise concepts, is on-going. This is a fiercely litigated area, and the final answer likely will not be available until the Supreme Court rules.

#### b. *Shared Control*

In a number of CERCLA cases, the courts have been confronted not only with consideration of the role of control in this area, but also with the significance of shared control. In determining liability for purposes of CERCLA, these cases not surprisingly have distinguished among the members of the group sharing control depending on the precise nature of each party's own role in the subsidiary's decisionmaking and management.

Most of these cases have involved the individual, controlling shareholders of smaller business enterprises. *Riverside Market Development Corp. v. International Building Products Inc.*<sup>169</sup> involved two individual shareholders and their controlled corporation, which had violated CERCLA.<sup>170</sup> The court held the president, a fifteen-percent shareholder, potentially liable as an operator.<sup>171</sup> He was at the factory three weeks out of every month and was

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167. *United States v. Cordova Chem. Co.*, 59 F.3d 584, 590 (6th Cir.), *vacated*, 67 F.3d 586 (1995); *Joslyn Mfg. Co. v. T.L. James & Co.*, 893 F.2d 80, 82-83 (5th Cir. 1990), *cert. denied*, 498 U.S. 1108 (1991); *see also* *Trinity Indus., Inc. v. Dixie Carriers, Inc.*, No. CIV.A.90-2349-N, 1992 U.S. Dist. LEXIS 9540, at \*7 (E.D. La. June 23, 1992); *United States v. Arrowhead Ref. Co.*, No. 5-89-202, 1993 WL 170966, at \*7-8 (D. Minn. Mar. 12, 1993).

168. In its recent decision in *Schiavone*, the Court of Appeals for the Second Circuit recognized the difficulty, but expressly declined to resolve it. 79 F.3d at 254 n.5.

169. No. CIV.A.88-5317, 1990 U.S. Dist. LEXIS 6375, at \*1 (E.D. La. May 22, 1990), *aff'd*, 931 F.2d 327 (5th Cir.), *cert. denied*, 502 U.S. 1004 (1991).

170. *Id.* at \*5.

171. *Id.*

actively involved in general management as well as in waste disposal.<sup>172</sup> However, the court rejected liability for the chairman of the board who held eight-five percent of the stock.<sup>173</sup> He had no involvement in management and participated in the enterprise only through review of financial materials and board deliberations.<sup>174</sup>

*Nurad v. William E. Hooper & Sons Co.* involved a closely held family business.<sup>175</sup> The court imposed liability on the father, who acted as president and exercised day-to-day control of the company.<sup>176</sup> However, it rejected the imposition of liability upon his two sons, who also were officers but were less active in the business.<sup>177</sup>

A third decision of this nature, *City of N. Miami v. Berger*, imposed liability on two individual shareholder-officers, both holding thirty-two percent of Munisport and fifty percent of ABC, who exercised day-to-day operational and financial responsibility over the controlled corporation that had committed the CERCLA violation.<sup>178</sup> The court stressed the authority of the officer-shareholders to control the management as well as the actual control that they exercised over the operations.<sup>179</sup> However, the court refused to impose liability on a third shareholder-officer who held fifteen-percent ownership but had no active management responsibilities.<sup>180</sup>

In these cases, it was not shown that the active (or less active) parties sharing control had notice or knowledge of any statutory violation. Accordingly, the courts did not have to consider whether possession of the power to stop the violation could serve as the basis for imposition of liability.

*United States v. McGraw* involved a corporate joint venture in which the shares were divided with fifty-one percent held by one shareholder and forty-nine percent held by another shareholder.<sup>181</sup> The fifty-one-percent shareholder having settled the litigation, the issue before the court was the CERCLA liability of the forty-nine-percent shareholder, which was a corporation.<sup>182</sup> The corporation holding forty-nine percent of the shares provided technical expertise, and one of its officers served as an officer of the subsidiary.<sup>183</sup> The court found that even these circumstances were

172. *Id.* at \*6-8.

173. *Id.* at \*5.

174. *Id.* at \*6.

175. *Nurad*, 966 F.2d at 841.

176. *Id.* at 844.

177. *Id.*

178. *Berger*, 828 F. Supp. at 404, 410-11. *Accord* *United States v. TIC Inv. Corp.*, 866 F. Supp. 1175 (N.D. Iowa 1994).

179. *Berger*, 828 F. Supp. at 410-11.

180. *Id.* at 411.

181. 718 F. Supp. 154, 156 (W.D.N.Y. 1989).

182. *Id.* at 154-55.

183. *Id.* at 157.

sufficient to defeat the shareholder's motion for summary judgment.<sup>184</sup>

With active involvement in management as the critical factor, liability readily arises under shared control where any of the parties sharing control is so engaged. Thus, in *John S. Boyd Co. v. Boston Gas Co.*, the Court of Appeals for the First Circuit held both a parent and its subsidiary independently accountable as owner and as operator, respectively, for the same activities.<sup>185</sup> By the same token, any party that only participates in the exercise of control for purposes of the election of the board of directors of the corporation at issue remains remote from operation.

In summary, the CERCLA decisions ready to apply enterprise principles other than piercing the veil to impose CERCLA liability through "broad" construction of the statutory terms agree that shared control neither defeats the imposition of enterprise liability nor automatically results in liability. They look to the degree of involvement of the party sharing control in the management of the affairs of the controlled corporation. This is the very standard employed by such courts in determining the application of enterprise principles to impose CERCLA liability on parent corporations (and other controlling shareholders) possessing sole control.<sup>186</sup> Where the requisite degree of operational involvement has been established, it is apparently irrelevant whether the party exercising it has sole control or is sharing control.

### 3. Other Statutes

Under the statutes of general application other than the environmental laws, control plays a central role in determining the imposition of statutory liability on a parent corporation (or controlling shareholder) for statutory violations of a subsidiary (or controlled corporation). As may be expected, the existence and degree of exercise of control is the starting point for analysis wherever the application of enterprise principles superseding traditional entity law is under consideration in this context.

In contrast to the consideration of control and even shared control in CERCLA matters, cases considering the imposition of enterprise principles in the implementation of statutes of general application provide only limited insight into the legal significance of shared control. In the handful of cases involving shared control under such statutes, the courts, like the courts imposing enterprise liability for CERCLA purposes, have disregarded the

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184. *Id.* at 158.

185. 992 F.2d 401, 407-08 (1st Cir. 1993).

186. See BLUMBERG & STRASSER, GENERAL STATUTORY LAW, *supra* note 1, § 18.01-.07; see also Kurt A. Strasser & Denise Rodosevich, *Seeing the Forest for the Trees in CERCLA Liability*, 10 YALE J. ON REG. 493, 511-13 (1993).

forms of separate juridical identity to impose liability only when the party sharing control has been actively involved in the operational matters that have given rise to the statutory violation.

#### IV. THE ROLE OF ADMINISTRATIVE AGENCIES IN THE IMPLEMENTATION OF STATUTORY REGULATORY PROGRAMS

In statutory programs supervised by administrative agencies, the agencies have far-reaching powers in the determination of the precise contours of control. In fact, some major statutes, including the Securities Act of 1933 and the Securities Exchange Act of 1934, although using the term control, did not define it; by design, the drafters of these statutes left its formulation and reformulation to the rulemaking and case-by-case determination of the regulatory agency.<sup>187</sup> Even where a statute defines control in considerable detail, as in the great holding company statutes, the administrative regulations provide refinements of importance. Finally, in some areas such as the labor laws and foreign trade laws, the statutes make no reference to control at all. However, as a result of administrative construction of statutory terms such as "employer" and "subject to the jurisdiction of the United States," respectively, the administrative agencies supervising statutory programs have introduced far-reaching enterprise doctrines based on expansive definitions of control.

In the accommodation of U.S. jurisprudence to the growing prominence of administrative agencies in the extensive body of regulatory law enacted by the Franklin D. Roosevelt and subsequent administrations, the Supreme Court has greatly enhanced the role and influence of such agencies. Through doctrines like the primary jurisdiction doctrine, which requires prior submission of certain matters to agencies rather than to courts, the final order doctrine, which bars appeal of interlocutory and interim orders, and the requirement of prior exhaustion of administrative remedies, the Court substantially strengthened the scope of the role of agencies in the legal system.

In *Rochester Telephone Co. v. United States*,<sup>188</sup> a decision of profound importance, the Court further enhanced agency power by allocating to administrative rulemaking and adjudication the near exclusive responsibility for determining the role and meaning of control in delineating the outer boundary of statutory liability in the area being administered.<sup>189</sup> In

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187. See *Metge v. Baehler*, 762 F.2d 621, 630 (8th Cir. 1985), *cert. denied sub. nom. Metge v. Bankers Trust Co.*, 474 U.S. 1057, 1072 (1986), (citing H.R. REP. NO. 1383-73, at 26 (1934)), *cert. denied*, *Bankers Trust Co. v. Metge*, 474 U.S. 1072 (1986).

188. 307 U.S. 125 (1939).

189. *Id.* at 145.



*Rochester*, the Court gave control an expansive functional meaning, holding that control was to be determined by a regard for “actualities . . . [of] intercorporate relation.”<sup>190</sup> In *Gilbertville Trucking Co. v. United States*, the Court also has stated that control “encompass[ed] every type of control in fact.”<sup>191</sup> However important, this was only a prelude. The Court went on to uphold the leading role of administrative agencies in applying the concept of control.<sup>192</sup> It held that control was “an issue of fact,” and that the agency’s determination of control was conclusive if supported by substantial evidence in the record.<sup>193</sup> The Court later characterized *Rochester* as rejecting all “artificial tests of control.”<sup>194</sup> As stated by a lower federal court, control is an issue for which the agency given its expertise and experience is “uniquely qualified” to determine.<sup>195</sup>

Although the courts theoretically have the final authority to determine whether an agency’s regulations fall within its discretionary authority in light of the statutory text and history, the reality is that with respect to the issue of control, the courts have almost never interfered with administrative rulemaking defining the extent of control. Further, in view of the breadth of the *Rochester* doctrine, the courts have almost never overturned an administrative adjudication of control.

This is a factor of crucial significance. The very wide area of discretion available to administrative agencies, naturally ready to take a most expansive view of the range of their authority, has inevitably meant the fullest flowering of enterprise principles in U.S. jurisprudence. The cases involving the role of control under statutory regulatory programs that involve agency rulemaking and adjudication can be understood only against this background.

This contrasts sharply with other areas in which administrative agencies have played a minor role or no role at all, and the courts have had the decisive role in determining the construction and application of regulatory statutes or disputes between private parties arising at common law. In these areas, the courts have been more reluctant to introduce expansive concepts of control that go beyond the accepted concepts of corporation law and the narrow limits of piercing the veil.

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190. *Id.* at 146.

191. 371 U.S. 115, 125 (1962).

192. *Rochester*, 307 U.S. at 138.

193. *Id.* at 145-46.

194. *See Alleghany Corp. v. Breswick & Co.*, 353 U.S. 151, 163, *reh’g denied*, 353 U.S. 989 (1957).

195. *See B.F. Goodrich Co. v. Northwest Indus., Inc.*, 303 F. Supp. 53, 57 (D. Del. 1969), *aff’d*, 424 F.2d 1349 (3d Cir.), *cert. denied*, 400 U.S. 822 (1976).

## V. CONTROL IN COMMON LAW CONTROVERSIES

### A. General Standards

In common law areas, U.S. courts have traditionally applied the concepts of entity law. The concept of the juridical person with his or her own rights and liabilities separate from those of any other juridical person has been the foundation of the U.S. legal system as well as other Western legal systems.<sup>196</sup> The traditional safety valve, permitting disregard of juridical identity, has been traditional piercing the veil jurisprudence. With occasional exceptions,<sup>197</sup> piercing has typically provided the only route to disregard of entity in common law controversies between private parties.<sup>198</sup> As noted, traditional piercing requires, among other elements, an excessively intrusive exercise of control by the controlling shareholders. In this area, control means dominance over the affairs of the controlled corporation, not merely the power to choose the majority of the board. Such "dominance" goes well beyond the parent's determination of the general policies of a subsidiary or the establishment of ceilings on a subsidiary's independent decisions on matters such as budget or capital expenditures. Under the traditional doctrine, such measures are typically of little or no legal consequence in the consideration of the imposition of intragroup liability. The courts widely accept such restraints as the conventional pattern in U.S. business.

The exercise of control must be so extensive as to impair the very core of the managerial independence of the subsidiary and its decisionmaking process. As one much quoted passage has put it: Piercing requires "[c]ontrol, not mere majority or complete stock control, but complete

196. PHILLIP I. BLUMBERG, *THE MULTINATIONAL CHALLENGE TO CORPORATION LAW* 3-8 (1993).

197. The railroad industry, until the decision in *Berkey v. Third Ave. Ry.*, 244 N.Y. 84, 155 N.E. 58 (1926), and the taxi industry to date are examples of such exceptions. *See, e.g.*, *Davis v. Alexander*, 269 U.S. 114, 117 (1925); *Mull v. Colt, Co.* 31 F.R.D. 154, 166-67 (S.D.N.Y. 1962); *Walkovszky v. Carlton*, 29 A.D.2d 763, 287 N.Y.S.2d 546 (App. Div.), *aff'd*, 23 N.Y.2d 714, 244 N.E.2d 55 (1968) (The Court of Appeals of New York, in *Walkovszky v. Carlton*, 18 N.Y.2d 414, 418, 223 N.E.2d 6, 8, 276 N.Y.S.2d, 585, 588-89 (1966), stated: "[I]t is one thing to assert that a corporation is a fragment of a larger corporate combine which actually conducts the business . . . [and which] would be held financially responsible."); *Mangan v. Terminal Transp. Sys., Inc.*, 157 Misc. 627, 284 N.Y.S. 183, 187-88 (Sup. Ct. 1935), *aff'd per curiam*, 247 A.D. 853, 286 N.Y.S. 666 (3d Dep't 1936), *leave to appeal denied*, 272 N.Y. 676 (1937); *see also* BLUMBERG, *CORPORATE GROUPS: SUBSTANTIVE COMMON LAW*, *supra* note 1, § 12 *passim*.

198. By contrast, where public policy concerns of magnitude are involved, the Supreme Court has rejected the standards of piercing the veil as mechanical and artificial. *See* *First Nat'l City Bank v. Banco Para El Comercio Exterior de Cuba*, 462 U.S. 611, 623 (1983) (warning "against permitting worn epithets [such as piercing the veil jurisprudence] to substitute for rigorous analysis").

domination, not only of finances, but of policy and business practices in respect to the transaction attacked so that the corporate entity . . . had at the time no separate mind, will or existence of its own.”<sup>199</sup> In such a setting, shared control manifestly occupies a very different role than under the statutory law.

The traditional doctrine appears to present less of a barrier in the case of individual controlling shareholders sharing control of a controlled corporation than in the case of large corporate groups. The reduced size, the greater informality, and the personalized role of the individual shareholder contribute in the aggregate to an atmosphere more conducive to intrusive participation in the operations and management of the controlled corporation. Although individual controlling shareholders who share control have often been subjected to liability at common law by reason of their active, personal involvement in the operations of the controlled corporation, individuals doing no more than sharing control in the election of the board of directors and not participating in operations have almost never been subjected to liability.

In the case of large corporate groups sharing control in a corporate joint venture, the vastly increased size, the much greater formality of operations and procedures, and the representative nature of the parent’s designees involved in subsidiary affairs establish a very different atmosphere, less conducive to the “dominance” required under the traditional view. As will be seen, there is little litigation in this area except for the silicone gel breast implant litigations. These decisions, readily rejecting the imposition of shareholder liability, throw no significant light on the degree of shareholder involvement that would have been required for imposition of liability.

In certain common law areas, including jurisdiction, some areas of procedure, and torts, U.S. law has seen the emergence of decisions rejecting traditional concepts of piercing the veil and applying enterprise principles. These courts have in effect looked pragmatically at the economic realities of the common enterprise rather than applying the formalism of entity law, the separate juridical identity of the related corporations, and formal indicia of separate existence. They have done so where they have concluded that enterprise principles rather than entity law more effectively implemented the underlying objectives and policies of the law in the area.

As noted, the primary factors for such liability are: the extensive exercise of control, even though less than the dominance required by the traditional doctrine, and the economic and operational interrelationship of the group affiliates, as shown by factors such as the economic integration of their operations, their financial interdependence, their administrative interdepen-

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199. *Lowendahl v. Baltimore & Ohio R.R.*, 247 A.D. 144, 157, 287 N.Y.S. 62, 76 (1st Dep’t), *aff’d*, 272 N.Y. 360, 6 N.E.2d 56 (1936).

dence, the group integration of personnel assignments and benefits, and the common conduct of group operations under a common public persona.<sup>200</sup> Nevertheless, this emergence of recognition of enterprise principles, however pronounced, for most purposes still reflects only a minority view.

In proceeding in this manner, the courts have been typically concerned with hierarchical corporate groups and accordingly, have not had occasion to examine the role of shared control. In view of the emphasis on the integration of the related corporations in the collective enterprise under common control, the application of enterprise principles in the case of a corporate joint venture with shared control requires a very different emphasis. On this, the cases to date provide little guidance.

### B. *Shared Control*

In the application of traditional concepts of piercing the veil in common law controversies, cases involving several individual controlling shareholders and a controlled corporation present a very different pattern from those involving parent and subsidiary corporations. This appears to reflect the substantial differences in size that typically exist between these two classes of controlled corporations. Individually owned corporations in the United States tend to be closely held and typically function on a much smaller scale than parent and subsidiary corporations, which in many cases are very widely held and operate on an incomparably large scale.

In the close, intimate setting of the individually controlled corporation, shared control is a common place. The few shareholders frequently also are officers and employees of the controlled business. The very smallness of the undertaking encourages both informality of operations and actions by the controlling shareholders that depart, sometimes grossly, from conventional corporate formalities. Under such circumstances, decisions imposing liability under traditional piercing doctrines on persons sharing control are numerous. This tells us little, however, about the very different setting of the large corporate group.

Shared control in corporate groups is uncommon. The parent corporation typically is firmly in control, and for this purpose, it is entirely irrelevant whether the parent maintains control through total or partial ownership of the shares of its subsidiaries. One special area in U.S. law provides an exception. Where one corporate group joins another in a joint venture conducted by a jointly owned subsidiary, the issue of the significance of shared control is squarely presented.

Corporate joint ventures are only one example of the newer types of nonhierarchical structure in U.S. economic undertakings. Other developments

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200. See BLUMBERG, *SUBSTANTIVE COMMON LAW PROBLEMS*, *supra* note 1, § 6 *passim*.

include strategic alliances and corporate networks. All of these developments are efforts to move outside the firm and join forces with a marketing, distribution, or manufacturing partner in the conduct of a discrete part of their respective enterprises.

Strategic alliances involve the establishment of a relationship in the form of a license or supply contract pertaining to a particular stage of production or distribution rather than the conduct of an overall business undertaking. As such, a strategic alliance does not constitute a fully integrated enterprise that may be deemed an "economic entity" on its own and thereby, contribute to its recognition as a new form of legal entity.<sup>201</sup> Accordingly, strategic alliances do not present the important issue of whether shared control of the activities of the alliance may give rise to some form of enterprise liability.

Corporate networks refer to economic interrelationships resting on extensive cross-ownership such as in the Japanese *zaibatsu*, *keiretsu*, and *kigyoshudan*,<sup>202</sup> and the European holdings companies.<sup>203</sup> By contrast, such structures are uncommon in the United States. While the relatively minor amounts of securities in these cross-holdings are sufficiently significant to create some pressure for the corporate policies of the corporations involved to be conducted in a congruent fashion with mutual awareness of each other's objectives, typically they do not present the reality of shared control to the degree required to give rise to the enterprise issues considered in this article.

In contrast to such forms of nonhierarchical relationships, corporate joint ventures do present serious issues of the significance of shared control and its implications for the application of enterprise principles.

## VI. SHARED CONTROL AND CORPORATE JOINT VENTURES

In contrast to strategic alliances and corporate networks, corporate joint ventures are an area in which problems of shared control have arisen in connection with common law controversies involving large corporate groups.<sup>204</sup> A commercial joint venture is a collective undertaking by two or more parties to conduct a business operation separate from their own

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201. See RICHARD M. BUXBAUM, 6 CORPORATE GOVERNANCE AND CORPORATE MONITORING: THE WHYS AND HOWS, AUST'L J. CORP. L. 309 (1996).

202. See Krasnow, *supra* note 10, at 56 (discussing the evolution of Japanese business groups); see also SCOTT, *supra* note 10, at 291, 302.

203. Both corporate networks and so-called holdings companies that have made their appearance on the European scene are virtually unknown in the United States. See Van Hulle, *supra* note 9. Accordingly, they fall outside the scope of this article.

204. Another departure is the rapidly increasing phenomena of strategic alliances in which two groups enter into a long-term interrelationship with respect to a discrete fragment of their operation to satisfy common interests. Such alliances typically involve licenses or contracts. They do not involve the common conduct of a separate enterprise and, accordingly, do not represent a case of shared control of the activity in question.

operations. Except in those cases where the joint venture is conducted in corporate form, such an undertaking for profit does not have its own juridical identity. Instead, it is treated essentially as a partnership organized for a limited time and purpose and is governed by analogy to partnership principles.<sup>205</sup>

Where two participating parties conduct their collective undertaking in the form of a corporation in which they own the shares, a so-called corporate joint venture is involved.<sup>206</sup> It is a jointly owned subsidiary corporation with two parent corporations who share control. This is a significant departure from the traditional monolithic hierarchical structure of the multinational corporation, involving a pyramidal structure with a single parent corporation exercising control through stock ownership, directly or indirectly, of sufficient shares of the various subsidiaries to control the election of their boards of directors.

The courts have uniformly refused to recognize corporate joint ventures as "joint ventures," to be treated for legal purposes according to principles developed for noncorporate joint ventures rather than as a corporation governed by corporation law. Without exception, the courts have rejected attempts to impose liability on shareholders sharing control in reliance on joint venture law based on partnership principles drawn from cases involving unincorporated joint ventures. They have concluded that corporation law governs jointly owned corporations of such a nature just as much as other corporations. Under the established view, "[t]he two forms of business are mutually exclusive, each governed by a separate body of law."<sup>207</sup> The established doctrine has been most recently applied and liability rejected against the controlling shareholders in a corporate joint venture in the celebrated mass tort litigation over alleged product liability involving silicone gel breast implants.<sup>208</sup>

The issue of shareholder liability for corporate joint venture obligations that is based on shared control has arisen most dramatically in the litigation,

205. See, e.g., *Itel Containers Int'l Corp. v. Atantrafik Express Serv. Ltd.*, No. C-1313-RLC, 1988 U.S. Dist. LEXIS 7051, at \*1 (S.D.N.Y. July 13, 1988); *Hellenic Lines, Ltd. v. Commodities Bagging & Shipping, Process Supply Co.*, 611 F. Supp. 665, 679 (D.N.J. 1985); 2 SAMUEL WILLISTON & WALTER H.E. JAEGER, A TREATISE ON THE LAW OF CONTRACTS § 318 (3d ed. 1959).

206. The term, "corporate joint venture" is, thus, self-contradictory; so long as this is kept in mind, the term, nevertheless, is a useful means by which to identify the jointly owned subsidiary of two corporate parents.

207. *Weisman v. Awnair Corp. of Am.*, 3 N.Y.2d 444, 449, 144 N.E.2d 415, 418 (1957); see *In re Silicone Gel Breast Implants Prod. Liab. Litig.*, 837 F. Supp. 1128 (N.D. Ala. 1993) [hereinafter *Dow Corning*], *confirmed*, 887 F. Supp. 1455 (N.D. Ala. Apr. 25, 1995); *Jackson v. Hooper*, 76 N.J. Eq. 592, 599, 75 A. 568, 571 (1910).

208. *Dow Corning*, 837 F. Supp. at 1128.

involving Dow Corning Corporation.<sup>209</sup> This case involves the alleged product liability of the manufacturers and distributors of a product developed and manufactured by the Dow Corning Corporation (Dow Corning), a corporate joint venture of the Dow Chemical Company (Dow) and Corning Fiberglas Corporation (Corning).<sup>210</sup>

Dow and Corning organized Dow Corning fifty years ago to conduct a business involving the manufacture and sale of silicone products, combining Dow's chemical processing and manufacturing expertise and Corning's silicone technology.<sup>211</sup> They divided the shares of Dow Corning equally between them.<sup>212</sup> Over the years, Dow Corning became one of the 500 largest U.S. corporations with several billion dollars of gross assets.<sup>213</sup> It operated its own plants in seven states and nine countries with its own employees.<sup>214</sup>

Thousands of lawsuits have now been filed against Dow Corning, its two parents — Dow and Corning — and others by persons alleging to have been injured by Dow Corning silicone breast implants.<sup>215</sup> There are potential claims by thousands of other persons not yet filed.<sup>216</sup> This represents one of the most massive tort liability litigations in the history of U.S. law. Most cases in the federal courts have been consolidated and are being heard in a single proceeding in the federal district court in Alabama.<sup>217</sup> Other cases have gone to judgment before a federal district court in Illinois.<sup>218</sup>

In the Alabama proceeding, motions by Dow and Corning for judgment on the pleadings or for summary judgment sharply presented the issue of whether the two parents could be liable for the torts allegedly committed by their jointly owned subsidiary.<sup>219</sup> The plaintiffs relied on traditional concepts of piercing the veil and a new view of joint venture law.<sup>220</sup> The court rejected their contentions and granted the defendants' motion.<sup>221</sup> As noted in the preceding section, the court sharply rejected the contention that

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209. *Id.*

210. *Id.* at 1130.

211. *Id.* at 1131.

212. *Id.*

213. *Id.*

214. *Id.*

215. *Id.*

216. *Id.* at 1130.

217. *Id.*

218. *In re TMJ Implants Prod. Liab. Litig.*, 880 F. Supp. 1311 (D. Minn. 1995).

219. *Dow Corning*, 837 F. Supp. at 1130-31.

220. *Id.* at 1132 & n.5.

221. *Id.* at 1142-43. The court subsequently confirmed and certified its order as a final judgment in favor of Corning but vacated its order insofar as it related to the plaintiffs' direct liability claims against Dow. *In re Silicone Gel Breast Implants Prod. Liab. Litig.*, 887 F. Supp. 1455, 1463 (N.D. Ala. 1995).

the legal relationships of a corporate joint venture such as Dow Corning were to be determined by partnership concepts resting on its joint venture aspects.<sup>222</sup> The court regarded the problem of corporate joint ventures to be governed by traditional corporation doctrines<sup>223</sup> and accordingly, analyzed the problem by application of the concepts of piercing the corporate veil.<sup>224</sup>

The court noted numerous strong links between Dow and Corning and their jointly owned subsidiary in addition to the fifty percent stock ownership of each.<sup>225</sup> Among other things, the court found that Dow and Corning directors, officers, and current or former employees had comprised all the directors of Dow Corning in early years, and that thereafter Dow and Corning directors or officers comprised a majority of the Dow Corning board of directors.<sup>226</sup> The two corporate parent corporations provided substantial financial support to Dow Corning including short term loans, guaranties of Dow Corning debt, and purchase of Dow Corning long-term debt.<sup>227</sup> Dow and Corning allowed Dow Corning to utilize their facilities and personnel to conduct silicone-related research for which Dow Corning reimbursed the parents for their expense.<sup>228</sup> There was significant personnel integration with parent stock utilized in the Dow Corning stock option and purchase plans and the transfer of some personnel.<sup>229</sup> Dow listed Dow Corning as a coinsured on Dow's excess liability insurance policy issued by Dow's captive insurance company.<sup>230</sup>

Notwithstanding this close interrelationship between the affiliated companies, the court concluded that it did not support "an inference of excessive or otherwise improper involvement" by the parent corporations in Dow Corning affairs.<sup>231</sup> The court further found that the subsidiary had complied with all corporate formalities, and by conducting large-scale operations of its own, had all the indicia of separate corporate existence. It held that the facts "clearly demonstrate a separate corporate existence for Dow Corning, recognized and respected by it and its parent corporations."<sup>232</sup>

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222. *Dow Corning*, 837 F. Supp. at 1139.

223. *Id.*

224. *Id.* at 1133-38.

225. *Id.* at 1138-39.

226. *Id.* at 1135.

227. *Id.* at 1136-37.

228. *Id.* at 1135.

229. *Id.* at 1135-36.

230. *Id.*

231. *Id.*

232. *Id.* at 1134.



Noting that Dow Corning had retained fifty-six percent of its earnings in the last ten years, had doubled its working capital, and had trebled its total assets and shareholder equity during this period, the court rejected the allegation that Dow Corning had been undercapitalized.<sup>233</sup>

Finally, the court held that there had been no showing of any kind of inequitable or unfair behavior.<sup>234</sup> Dow Corning had not been incorporated in an effort to escape liability; there was no intermingling of funds, improper loans, or asset draining. Under all the circumstances, the court held that the requirements of piercing the veil for purposes of imposing tort liability on either Dow Chemical or on Corning had not been satisfied.<sup>235</sup> However, it did hold that the plaintiff had made a sufficient showing of Dow Chemical's direct liability for its own negligence to defeat the latter's motion for summary judgment.<sup>236</sup>

*In re TMJ Implants Products Liability Litigation*<sup>237</sup> was the Illinois litigation involving silicone gel product liability claims against Dow and Corning for breast implants manufactured by Dow Corning.<sup>238</sup> Following the decision in *Dow Corning*, the court granted the summary judgment motions of Dow and Corning on the plaintiffs' joint venture and piercing the veil claims.<sup>239</sup>

Since the courts in these two cases did not find the exercise of control so excessive as to satisfy piercing standards, they never had the occasion to consider the special problems presented by shared control. In its review of the facts, however, the Alabama court appeared to be focusing separately on the conduct of each parent in determining whether its own exercise of control was "excessive." The Alabama court was not concerned about the fact that each parent shared control with the other. It does not appear that this factor would have presented an obstacle to the imposition of liability if the court had concluded that one of the parents had exercised control to an impermissible degree.

## VII. CONCLUSION

Shared control must be analyzed as a subset of control, and its significance primarily determined by the significance of the role of control in the area of the law in question and the particular context involved. United States law appears to treat the possession or exercise of shared control by one of the

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233. *Id.* at 1137.

234. *Id.* at 1138.

235. *Id.*

236. *Id.* at 1133.

237. 880 F. Supp. 1311 (D. Minn. 1995).

238. *Id.*

239. *Id.* at 1322.

parties sharing control very much as it responds to a comparable manifestation of control by the party with sole control. The crucial element is the nature of the actual manifestation of control in light of the significance of control in the area of the law at issue.

Where, as in the statutes of specific application, a crucial factor for determining statutory application is control over the election of the board of directors, participation by a principal shareholder as a member of the control group in a concerted action to control the election of the board of directors, although representing shared control, does not present a different problem than control. In either case, statutory liability follows.

In statutes of general application, and even more plainly in common law controversies involving private individuals, control of the election of the directors is not sufficient in itself for imposition of shareholder liability. Accordingly, in this area, the imposition of shareholder liability on a party with shared control must, as in the case of a party in sole control, rest on the manner in which the party exercises it. As noted, this means that the party must participate in the exercise of control over operational and other managerial matters in a manner comparable to parties with sole control who have been subjected to enterprise liability in this area.

In some statutes of general application, such as CERCLA, this test for liability may require direct personal involvement in the operations of the controlled corporation giving rise to liability. In other statutes or in common-law controversies, other factors such as economic integration, financial and administrative interdependence, enterprise conduct of personnel matters, and conduct of business under a common business persona appear to be required in addition to an excessive exercise of control. Where such factors are indeed required, the operational circumstances of the enterprise appear highly unlikely to present these interrelationships for the party sharing control, except in some cases of corporate joint ventures. Accordingly, imposition of liability on those with shared control in these areas is unlikely.

In sum, shared control appears to give rise to serious prospect for enterprise liability only in a limited area. It would appear necessary either that control play a decisive or near decisive role in the implementation of enterprise principles in the area as frequently occurs in statutes of specific application or that the party sharing control has actively participated in the aspect of the operations of the controlled corporation giving rise to the statutory violation.

Corporate joint ventures may differ from other forms of shared control and present a more serious case for imposition of enterprise liability. However, aside from the *Dow Corning* litigation, there is little guidance available on whether the enterprise principles applied to date by some courts in the case of hierarchical corporate groups may be adapted to serve as a basis for liability when control has been shared in corporate joint venture

form. The *Dow Corning* decisions have firmly applied traditional concepts and have refused to do so. Thus, although the prospects for further legal changes in the area appear limited, it is still too early to conclude that U.S. courts have provided a final answer.