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Parent Company Liability – Mitigating Jurisdictional Risk in the U.K.?

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Financial sponsors customarily adopt structures for platform investments that presume that the fund or parent company will be insulated from liability for the acts or omissions of its portfolio assets by using corporate entities with limited liability. Whilst the legal principle of separate legal identity remains unaffected, a line of cases in the English courts indicates that such structures are not completely watertight, and a court could, in exceptional circumstances, find that a parent has assumed a duty of care to persons who suffer loss as a result of transgressions by its subsidiary.

Recent cases

In *Okbapi and Ors v. Royal Dutch Shell & Anor [2021]*, the Supreme Court held that the English courts could take jurisdiction over claims brought against Royal Dutch Shell plc ("RDC") (a U.K. domiciled company) in relation to the wrongdoing of its Nigerian subsidiary. In doing so, it affirmed the decision in *Vedanta Resources plc v. Lungowe [2019]* that parent companies *could* be so exposed and the kind of circumstances that would be taken into account in determining such liability.

Background

A group of claimants alleged that unremedied environmental damage in the Niger delta was caused by the negligence of Shell Petroleum Development Company of Nigeria Ltd ("SDPC"), a subsidiary in which RDC held a 55% interest. Separate claims in the English courts were brought against SDPC *and* RDC. The Supreme Court assessed whether the claimants could establish jurisdiction to bring a claim in the English courts. In finding for the claimants, it merely confirmed that there was a real prospect of the claim against RDS succeeding, should it proceed to trial. Critically, it did not make a full assessment of whether a duty of care was owed to the claimants by RDS. This will need to be established by the claimants at trial. *Vedanta* concerned the same issue: the English courts established jurisdiction to hear the proceedings; however, the case was subsequently settled without the defendant admitting liability before the trial was held. The summary nature of the judgments should not be ignored, and the findings set out below will be subject to further scrutiny if *Okbapi* proceeds to trial.

Findings

No presumption of a duty of care arises by virtue of parent-subsidiary relationship itself. In deciding whether a parent could (in certain circumstances, assessed on the particular facts) assume liability for wrongdoing of a subsidiary, the court cited or approved the following factors outlined in *Vedanta* that may be indicative of a parent assuming a duty of care to a third party (but fall short of establishing a bright line test):

- parent taking over the management of the subsidiary (in place of or jointly with existing management);

- parent taking active steps, via training, supervision, or enforcement, to ensure policies are implemented by its subsidiaries;
- where a parent has given advice to a subsidiary as to how it should manage risk;
- if a parent holds itself out as exercising control over or supervision of its subsidiaries in published materials (even if it, in fact, does not);
- promulgation of group-wide policies by the parent that, for example, are defective and result in harm to a third party; or
- reporting protocols are structured such that persons with operational authority at subsidiary level are ultimately accountable to a person engaged at parent company level, and that structure is used to exercise significant control over the subsidiary.

How can risks be mitigated?

Both *Okbapi* and *Vedanta* involved groups operating in higher risk industries and geographies. Litigation risk can never be excluded, and there may be other forums other than the U.K. to consider. Based on the above cases, the risk of English courts assuming jurisdiction in respect of a claim against a parent entity can be limited by reference to the below measures. These should be balanced against other needs of the group as part of a holistic risk assessment.

Fund level

- Establish governance structures whereby portfolio boards are staffed with persons with appropriate expertise and authority to conduct business without undue deference to the fund.
- Portfolio companies should ideally commission their own advice as to the scope and implementation of policies/procedures, especially where ESG concerns have been raised.
- Establish reporting lines such that portfolio boards report to the fund on implementation of policies, avoiding active and unnecessary intervention by the fund.
- Avoid documenting provision of advice or services to a portfolio asset by a fund that may suggest an undue level of control, management, or responsibility.

Portfolio company level

- Identify business lines that may involve greater risk of claims. Are they managed locally with a view to insulating the rest of the group?
- Ensure policies refer to the proposed governance structure explicitly and that evidence of decisions (board resolutions) reaffirms that decisions are taken locally, without assumption of any control by a parent.
- Ensure governance structures do not, in fact, require or promote deference to a parent in management of local business.
- Where policies are implemented on a group-wide basis (e.g., compliance/training), establish clear evidence of the rationale for implementing them locally. Whilst reporting may be made to senior management at parent company level, effective control at subsidiary level reduces the risk of the parent assuming liability.

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