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GROUPS OF COMPANIES AND ABUSE OF LEGAL FORM

Abstract

This paper examines the issue of abuse of legal form within groups of companies, with particular attention to the ways in which such groups may rely on complex structures and formal legal separation to evade liability. It analyzes the consequences of these practices for legal certainty, market competition, and the protection of creditors. The paper further considers the legal mechanisms developed to limit abuse of legal forms, including piercing the corporate veil and the rules governing liability within groups of companies. The conclusion emphasizes the need to strike a balance between respect for the autonomy of separate legal entities and effective protection against abusive practices, as well as the importance of improving regulatory frameworks in response to contemporary challenges in company governance.

Key words: *groups of companies, abuse of legal form, separate legal personality, limited liability, piercing the corporate veil.*

I. INTRODUCTION

The doctrine of separate legal personality is one of the foundations of company law, yet its application within contemporary groups of companies has become increasingly difficult to justify without reservation.[1] While limited liability performs important economic and organizational functions, its operation in large and highly integrated group structures often creates layers of legal separation that do not correspond to the underlying economic reality.[2] As a result, groups of companies may use formal fragmentation to allocate risk strategically, diminish the asset base available to creditors, and weaken effective accountability.[3]

For this reason, liability in groups of companies continues to represent one of the most difficult unresolved issues in modern company law. Existing legal frameworks are still largely shaped by entity-based reasoning and therefore often fail to capture the group as a functionally integrated organization.[4] When risky activities are conducted through subsidiaries with limited

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[1] M Petrin and B Choudhury, 'Group Company Liability' (2018) 19 *European Business Organization Law Review* 771, 772; U Bold, 'An Exploration into Liability of Corporate Groups: A Comparative Perspective' (doctoral thesis, University of Pécs 2022) 30–31.

[2] S Belenzon, H Lee and A Patacconi, 'Managing Risk in Corporate Groups: Limited Liability, Asset Partitioning, and Risk Compartmentalization' (2023) 44 *Strategic Management Journal* 2888.

[3] Jennifer Dickfos, 'Enterprise Liability for Corporate Groups: A More Efficient Outcome for Creditors' (2011) 25 *Australian Journal of Corporate Law* 242, 244.

[4] Bold (n 1) 31–32.

assets, the costs of failure may be shifted to creditors, tort victims, and society more broadly.[5] This raises a broader question whether classical company law concepts remain sufficient in an era in which business power is increasingly exercised through complex group structures.[6]

Against this background, this paper examines the principal mechanisms through which the corporate form may be abused within groups of companies and considers the challenges involved in regulating such abuse. The second part defines corporate groups and explains their main legal and economic characteristics. The third part analyses the ways in which separate legal personality may be abused within group structures, particularly through the strategic allocation of risk and assets. The fourth part discusses the main difficulties involved in regulating such practices under existing company law doctrines. The paper concludes by reflecting on the limits of the current entity-based approach and the possible need for a more coherent model of liability.

II. DEFINITION AND CHARACTERISTICS OF GROUPS OF COMPANIES

Groups of companies are one of the most significant developments in modern company law, as they reveal the growing distance between established legal doctrine and contemporary economic reality. While the traditional theory of the corporation is built upon the concept of a single, autonomous legal entity, modern business practice is increasingly characterized by groups of related companies that operate as an economically integrated whole.[7]

Any definition of groups of companies must begin with the tension between entity theory and enterprise theory. The former treats each company within the group as a separate legal entity with its own rights and liabilities, while the latter emphasizes the economic unity and functional integration of the group. Entity theory reflects the conventional approach adopted in most legal systems.[8] According to this approach, each member of the group is treated as a separate legal entity with independent legal rights and limited liabilities.[9] As a result, the parent company and its subsidiaries are, as a rule, not liable for each other's debts or obligations.[10] This approach is grounded in the doctrine of separate legal personality, according to which the company remains distinct from its shareholders, even where another corporation is its sole shareholder.[11] Enterprise theory, by contrast, views the group as a single business reality. Rather than focusing exclusively on formal legal separation, it emphasizes the economic unity of the group and the functional integration of its constituent companies.[12] This theory seeks to close the gap between legal fiction and economic reality.[13] As stated in the literature, within the economic enterprise, each legal entity dedicates its assets and activities to the success of the common venture.[14] This divergence between legal form and economic reality also explains why groups of companies occupy such a central

[5] P Kara, *Tort Liability in Multinational Corporate Groups: A Comparative Analysis with Particular Focus on Turkey* (Springer Cham 2023) 60.
[6] Dickfos (n 3) 4–5.
[7] U Bold, 'Corporate Law Principles versus Corporate Groups' (eWorkcapital, 31 August 2020) https://eworkcapital.com/corporate-law-principles-versus-corporate-groups/ accessed 16 February 2026.
[8] Bold (n 1) 39-40.
[9] Bold (n 1) 39-40; Kara (n 5) 22.
[10] Bold (n 1) 39–40.
[11] Kara (n 5) 22.
[12] Bold (n 1) 39–40
[13] Bold (n 7).
[14] Bold (n 7).

place in debates on liability, creditor protection, and abuse of legal form. At the same time, it shows that groups of companies are not uniform structures but may take different legal forms depending on the basis and organization of control.

In legal theory, groups of companies may be classified according to the legal basis and structure of control. A common distinction is made between factual groups and contractual groups. Factual groups arise through capital participation or de facto dominant influence, whereas contractual groups are established through a formal control agreement requiring the subsidiary to follow the parent's instructions. Groups may further be vertical, where control is hierarchical, or horizontal, where coordination exists among legally independent companies under common management or common interests.[15]

Despite these structural differences, comparative analysis shows that groups of companies share several core features that distinguish them from individual companies. A central feature of any group of companies is control. A group exists where one entity is able to exercise decisive influence over one or more subordinate companies, whether through ownership, voting power, contractual arrangements, or other forms of dominant influence.[16] Such influence extends beyond the formal exercise of shareholder rights and includes the power to direct management, coordinate business strategy, and align the conduct of individual companies with the broader interests of the group.[17]

Another defining feature is economic unity. Although each company retains separate legal personality, the group often operates as a single economic unit in which strategic decisions, business coordination, and commercial objectives are determined from a central point. In practice, subsidiaries are integrated into a wider business structure and may, to a greater or lesser degree, relinquish operational autonomy to serve the efficiency, stability, and commercial objectives of the group as a whole.[18] Although the entity-based approach continues to dominate company law, elements of the enterprise approach have gradually gained recognition in specific fields such as tax law, insolvency law, environmental law, and human rights law, where strict adherence to formal separateness may undermine substantive justice[19].

The complexity of modern corporate groups exposes the limits of classical company law doctrine, particularly where group structures are used to facilitate abuse of legal form or to avoid liability.[20] The following section therefore examines the principal ways in which separate legal personality may be used abusively within groups of companies.

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[15] Tatjana Jevremović Petrović, *Grupe privrednih društava* (Pravni fakultet Univerziteta u Beogradu, Centar za izdavaštvo i informisanje 2014) 70–72, 89-90, 102, 152-153

[16] W Mierzejewska and P Dziurski (eds), *Business Groups and Strategic Coopetition* (Routledge 2023).

[17] Bold (n 7).

[18] F Wagner-von Papp, 'Managerial Liability, Managerial Duties, and Liability Within Corporate Groups: Optimal Competition Law Sanctions by Rearranging the Deckchairs Within the Undertaking?' in Florence Thépot and Anna Tzanaki (eds), *Research Handbook on Competition and Corporate Law* (Edward Elgar 2025) 474, 529.

[19] M Koutsias and J Dine, 'The Three Shades of Tax Avoidance of Corporate Groups: Company Law, Ethics and the Multiplicity of Jurisdictions Involved' (2019) 30(1) European Business Law Review 149, 164; Vinod Kothari and Sikha Bansal, 'Entity Versus Enterprise: Dealing with Insolvency of Corporate Groups' (12 March 2019) SSRN Electronic Journal https://ssrn.com/abstract=3350877 accessed 6 April 2026; Tori Loven Kirkebø and Malcolm Langford, 'The Commitment Curve: Global Regulation of Business and Human Rights' (2018) 3(2) Business and Human Rights Journal 157, 172.

[20] E Vaccari and T Van Ho, 'Insolvency Law through the Lens of Human Rights Theories' in E Ghio, JM Wood and JLL Gant (eds), *Re-examining Insolvency Law and Theory: Perspectives for the 21st Century* (Edward Elgar 2023) 190.

III. ABUSE OF SEPARATE LEGAL PERSONALITY IN CORPORATE GROUPS

The doctrine of separate legal personality and the principle of limited liability represent the foundations of modern company law, initially designed to protect individual investors and promote economic development.[21] However, their extensive application within groups of companies has created conditions in which structural or recurrent forms of abuse may arise. The main difficulty stems from the fact that these principles were developed in a legal context that did not fully anticipate the complexity and economic integration of modern corporate groups.[22] More specifically, although the separate legal personality of each company within the group facilitates organizational structuring and independent financing[23], it may also allow the parent company to shift risk and avoid responsibility for conduct carried out through its subsidiaries, particularly in complex multinational groups where economic unity exists behind formal legal separation[24].

One of the most common forms of abuse is the strategic use of specially incorporated subsidiaries to carry out high-risk business operations.[25] In such cases, the parent company places the risk of liability on a legally separate entity, thereby protecting the core assets of the wider group.[26] If those activities result in harm to third parties, limited liability may prevent creditors from reaching the assets of the group that ultimately benefits from the venture[27]. As a result, the group retains the economic advantages of the risky activity, while the potential costs of loss or damage are shifted onto society or involuntary creditors.[28]

The abuse further manifests through the practice of intentional undercapitalization of operational subsidiaries. Groups of companies often retain valuable assets within the parent company or separate holding entities, while subsidiaries that deal directly with the market and third parties are left with only minimal capital.[29] As a result, such subsidiaries may lack sufficient resources to satisfy claims if litigation arises.[30] This vulnerability may be further intensified through intra-group loans, dividend extractions, or other internal financial arrangements that weaken the financial position of the subordinate entity for the benefit of the group as a whole.[31]

The most severe consequences of such abuse are borne by involuntary creditors.[32] Unlike contractual creditors, who may assess a company's solvency and negotiate protective terms, involuntary creditors have no opportunity to choose their debtor or protect themselves in advance.[33] When harm occurs, they are often confronted with the formal barrier of separate legal

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[21] Bold (n 7).
[22] H Anderson, 'Piercing the Veil on Corporate Groups in Australia: The Case for Reform' (2009) 33(2) *Melbourne University Law Review* 333, 356.
[23] E Micheler, 'Separate Legal Personality – an Explanation and a Defence' (2024) 24(1) *Journal of Corporate Law Studies* 301, 325–326.
[24] PI Blumberg, 'Asserting Human Rights against Multinational Corporations under United States Law: Conceptual and Procedural Problems' (2002) 50(suppl 1) *The American Journal of Comparative Law* 493; J Dine and M Koutsias, 'The Three Shades of Tax Avoidance of Corporate Groups: Company Law, Ethics and the Multiplicity of Jurisdictions Involved' (2019) 30(1) *European Business Law Review* 149.
[25] Bold (n 7).
[26] Anderson (n 24) 333, 356; Petrin and Choudhury (n 1) 771, 781.
[27] Petrin and Choudhury (n 1) 790.
[28] Anderson (n 24) 333, 356.
[29] Petrin and Choudhury (n 1) 771, 781; Anderson (n 24) 333, 356.
[30] Petrin and Choudhury (n 1) 771, 774.
[31] Dickfos (n 3) 242.
[32] Kara (n 5) 26; Petrin and Choudhury (n 1) 771, 789–790.
[33] Anderson (n 24) 333, 356; Kara (n 5) 26.

personality, which prevents them from reaching the assets of the entity that effectively controls the business activity.[34] This asymmetry of risk may also weaken incentives for groups of companies to invest adequately in safety and prevention, since liability is in practice confined to the assets of an already undercapitalized subsidiary.

Although the doctrine of "piercing the corporate veil" is intended as a remedy for such abuses, in practice it is applied extremely rarely and only in extreme cases of fraud or where the company is an obvious façade.[35] Due to the strict formalism of the courts, which often upheld the principle of separate legal personality until the very end of the company's existence, many abuses remain without legal sanction.[36] This leads to the conclusion that the classical rules of corporate law are inadequate for regulating modern groups, which function as integrated enterprises but are held accountable as isolated entities.[37]

In this sense, the abuse of the principle of separate legal personality in corporate groups should not be seen merely as an exceptional deviation, but as a structural risk inherent in the gap between legal doctrine and economic reality.

IV. CHALLENGES IN REGULATING ABUSE WITHIN GROUPS OF COMPANIES

Regulating abuse within groups of companies remains one of the central challenges of modern company law, largely because of the persistent tension between legal formalism and the economic reality of the enterprise. Although groups of companies function as integrated systems, the law still predominantly relies on the principle of separate legal personality, which allows wide room for manipulation.[38]

The traditional mechanism for addressing such abuse - piercing the corporate veil - has often proved both inadequate and conceptually uncertain in practice.[39] Courts are frequently faced with difficult questions of fact and with the application of indeterminate concepts such as sham, façade, or alter ego, which are open to differing interpretations and often result in lengthy and complex disputes.[40] At the same time, companies with careful legal planning can often avoid meeting the conditions for veil piercing. This mechanism is also limited because it usually focuses on the parent company and does not work well when the relevant assets are held by other companies within the group, such as sister companies.[41]

The alternative approach to imposing a direct duty of care on the parent company also faces significant difficulties.[42] One of the main problems is determining exactly what kind and level of control should be enough to create such a duty. Parent companies may also seek to avoid responsibility by operating as holding companies and maintaining formal distance from the day-to-day operations and safety management of their subsidiaries.[43] In strongly integrated groups,

[34] Petrin and Choudhury (n 1) 771, 771.
[35] Micheler (n 25) 58.
[36] Bold (n 7).
[37] Petrin and Choudhury (n 1) 771, 789–790.
[38] Dickfos (n 3) 771, 772–773.
[39] Petrin and Choudhury (n 1) 771, 783.
[40] Ibid 783
[41] Ibid 783
[42] Ibid 783
[43] Ibid 783

where key decisions are made centrally, it is often difficult to identify just one entity as responsible for the harm, which makes regulation even more challenging.[44]

Groups of companies often use strategies that protect valuable assets from creditors' claims.[45] By relying on common branding, integrated financing, and intra-group arrangements, corporate groups may blur the distinction between separate entities, making it difficult for creditors to identify the company with which they are actually dealing and the asset base against which claims may realistically be enforced.[46] In practice, this often means that the most valuable assets are kept in the parent company, while higher-risk activities are carried out through subsidiaries with very limited capital.[47]

At both the global and regional level, attempts to introduce broader regulation of abuse within groups of companies, often face strong political and economic resistance.[48] In the European Union, for instance, the proposed Ninth Directive was never adopted because member states were unwilling to accept stricter rules on the liability of dominant companies.[49] Efforts to reform this area are often met with concerns that broader liability would reduce the ability of corporate groups to raise capital efficiently and spread business risk. Because of this, the law often remains unchanged.[50]

In essence, the central challenge lies in the fact that groups of companies function as economically integrated enterprises, while the law continues to regulate them as formally separate entities. As long as that structural disconnect remains unresolved, effective control of abuse will remain limited.

V. CONCLUSION

This paper has shown that the doctrine of separate legal personality, while essential to the development of modern company law, may also create space for abuse within groups of companies.[51] It has highlighted how group structures can be used to shift risk, protect assets, and limit responsibility in ways that leave creditors and other affected parties without effective protection.[52] The analysis also suggests that traditional legal mechanisms, especially piercing the corporate veil, are often too narrow and uncertain to respond adequately to these problems.

For that reason, the regulation of groups of companies requires a broader and more realistic legal approach. If the law continues to focus only on formal legal separation, it risks overlooking the economic reality of the group as an integrated enterprise. A more balanced framework should therefore consider the actual structure, control, and functioning of the group, while still preserving the legitimate economic benefits of limited liability.

Ultimately, the main challenge is to ensure that company law does not allow legal form to be used as a means of avoiding responsibility. A more coherent approach to liability in groups of

[44] Ibid 790
[45] Dickfos (n 3) 242.
[46] Dickfos (n 3) 242, 244
[47] Petrin and Choudhury (n 1) 771, 781.
[48] D Akšamović and S Stupar, 'Pojam, pravna priroda i neka otvorena pitanja faktičnih koncerna u domaćem i komparativnom pravu' (2018) 39(3) *Zbornik Pravnog fakulteta Sveučilišta u Rijeci* 1119, 1129; Dickfos (n 3) 242, 243.
[49] Akšamović and Stupar (n 50) 1129.
[50] Dickfos (n 3) 242, 243.
[51] Petrin and Choudhury (n 1) 771.
[52] Dickfos (n 3) 242.

companies is therefore necessary, not only for the protection of creditors, but also for the fairness and credibility of the legal system.[53]

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[53] H Hovenkamp, 'The Corporation's Split Personality' (1994) 92(6) *Michigan Law Review* 1792.