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CLIENT ALERT**DIRECT PARTICIPATION LIABILITY IN ILLINOIS FOR CORPORATE TORTS****PRACTICE AREAS**

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PIERCING THE CORPORATE VEIL

A corporation is a legal entity that exists separately from its shareholders, officers and directors, who are not ordinarily subject to liability for acting on behalf of the corporation. For example, an officer who signs a contract typically is immune from liability if the corporation fails to perform its contractual obligations. To sue a corporate officer or director, a plaintiff typically must allege some defect in the legitimacy of the corporate entity that provides a court with a basis to "pierce" the corporate form or "veil" to hold the officer or director accountable.¹

**LIABILITY FOR TORTIOUS CONDUCT IS INDEPENDENT OF
PIERCING THE CORPORATE VEIL**

Under Illinois common (not statutory) law, even if insufficient grounds exist to pierce the corporate veil, liability extends to any individual who commits tortious (or criminal) acts, even on behalf of a corporation. Such liability is sometimes referred to as the "responsible corporate officer doctrine" and is grounded in the simple concept

that an individual should be held responsible for his or her wrongful conduct.

Illinois courts have found officers or directors liable for a variety of tortious conduct, including: fraud (*Veteran Supply Co. v. Shaw, et al.*, 192 Ill.App.3d 286 (1st Dist. 1989)); conversion of property (*National Acceptance Co. v. Pintura Corp.*, 94 Ill.App.3d 703 (2nd Dist. 1981)); and negligence, resulting in personal injury or death (*Stansell v. International Fellowship, Inc.*, 22 Ill.App.3d 959 (1st Dist. 1974) and *McDonald v. Frontier Lanes, Inc.*, 1 Ill. App.3d 345 (2nd Dist. 1971)).

A corporate director or officer may also be held personally liable for *authorizing* tortious acts or *omitting to perform certain obligations*: "A director or officer is . . . liable when . . . he participates in the tortious act, authorized or directed it, acquiesced in it when he knew or by the exercise of reasonable care should have known of it, and should have taken steps to prevent it." *Simon v. Pelouze, et al.*, 263 Ill.App.177 (1st Dist. 1931); *see also, Miller v. Simon*, 100 Ill.App.2d 6 (1968) ("an officer of a corporation is liable for any tort of

1. Illinois courts consider different factors to assess whether the corporate entity should be treated as a fiction (thereby opening the door to officer/director liability), including whether the corporation: (1) is adequately capitalized; (2) issues stock; (3) observes corporate formalities; (4) pays dividends; (5) is solvent; (6) has other functioning corporate officers or directors; (7) keeps corporate records; (8) commingles corporate and individual monies; (9) detrimentally diverts assets from the corporation to individuals or other entities; (10) maintains arms-length relationships among related entities; (11) is merely a facade for the operation of dominant shareholders.

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DIRECT PARTICIPATION LIABILITY IN ILLINOIS FOR CORPORATE TORTS

the corporation in which he participates or authorizes, even though he was acting for the corporation in the commission of the tortious activity”).

FORSYTHE V. CLARK USA, INC.: **“DIRECT PARTICIPATION** **LIABILITY”**

Just like officers and directors generally are not subject to liability for actions taken on behalf of the corporation, a parent company ordinarily is not legally responsible for the acts of its subsidiaries. However, in a case decided in February of this year, *Forsythe v. Clark USA, Inc.*, 224 Ill.2d 274 (Ill. 2007), the Illinois Supreme Court held that liability exists if the parent company “directly participates” in torts committed by a subsidiary. In *Forsythe*, the plaintiffs alleged that the parent company, not the officers or directors of the subsidiary, participated in the tortious acts of its subsidiary that caused the death of two employees of the subsidiary and therefore should be held responsible for plaintiffs’ damages.

The facts involve an oil refinery fire that killed two employees of Clark USA Refining, a subsidiary of Clark USA. After settling the employees’ workers compensation claims, the employees’ estates filed suit against the parent company to avoid the workers compensation bar. In their complaint, the plaintiffs alleged that the parent company was responsible

for the unsafe conditions that caused the accident by creating and implementing a budgetary strategy at the subsidiary that minimized safety and training in favor of maximizing profits to the parent.

The parent company sought to dismiss the case, arguing a parent company is not liable for the acts of its subsidiaries, and plaintiffs had not alleged facts sufficient to pierce the corporate veil and sue the parent.

The Illinois Supreme Court acknowledged that while parent companies are generally not liable for the acts of their subsidiaries, and “mere policy decisions” and supervision of subsidiary activities are insufficient to expose the parent company to liability, the Court held that “direct participation liability” is a valid theory of recovery under Illinois law *and does not require piercing the corporate veil.*²

The Court ruled:

Where there is evidence sufficient to prove that a parent company mandated an overall business and budgetary strategy *and* carried that strategy out by its own specific direction or authorization, surpassing the control exercised as a normal incident of ownership in disregard for the interests of the subsidiary, that parent company could face liability. The key elements to the application of direct par-

ticipant liability, then, are a parent’s specific direction or authorization of the manner in which an activity is undertaken and foreseeability [of resulting damages].

Forsythe, 224 Ill.2d at 290. The Court denied the parent company’s motion to dismiss the case and sent the case back to the trial court to consider plaintiffs’ “direct participation” liability claims.

The Court specifically ordered the trial court to determine whether the parent had directed or authorized the manner in which the subsidiary’s budget was implemented, and, if so, whether the parent did so with reasonable care. Similarly, the Court instructed that if the parent directed the manner in which budget cuts were taken, the parent “had a duty to do so in a non-negligent way.”

Thus, just as corporate officers and directors become exposed to personal liability if they commit tortious acts on behalf of a corporation, per *Forsythe*, parent companies are subject to liability if they “directly participate” in the tortious acts of their subsidiaries.

Please call us if you would like to discuss the implications of *Forsythe*, or any other information regarding corporate officer and director liability contained in this publication.

2. The Court also ruled that a subsidiary’s workers compensation immunity would not protect the parent company from liability.
3. Although *Forsythe* is a tort case, the Court did not preclude another court from extending liability to a parent company that participates in a subsidiary’s breach of contract.

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