

Achieving balance in the Parent-Subsidiary relationship: Some Practical Tips for Corporate Groups and their Directors

1 Introduction

It is widely accepted that a parent company needs to have a level of control and oversight over its subsidiaries to effectively manage its group interests. Parent companies often place obligations on subsidiaries and put group policies in place to reduce operational risk at a group level. However this must be balanced against the risks for parent companies and directors where a parent company seeks to have excessive control and involvement in the affairs of a subsidiary.

2 Risks

In certain circumstances this can increase a parent company's exposure to liability for the activities of its subsidiary and lead to the directors of the subsidiary being conflicted. For example:

- Directors of Irish companies have a fiduciary duty under the Companies Act 2014 to act in good faith in what the director considers to be the best interests of the company. Primarily, directors owe their duties to the company and while directors must have regard to the interests of its members, the interests of the company must always prevail. Conflicts can arise where the board of the subsidiary feels pressurised by its parent to act in accordance with the parent's interests in circumstances where these interests are not aligned with the interests of the subsidiary.
- The directors of the parent company could be deemed to be shadow directors of a subsidiary and have the same liabilities as the directors of the subsidiary. A shadow director is a person in accordance with whose directions or instructions the directors of a company are accustomed to act.
- There are certain circumstances in which a company's separate legal personality could be disregarded and where the Irish courts have been willing to "lift the corporate veil". One such circumstance is where two or more companies are effectively being carried on as a single entity so that the business primarily carried out by one will be recognised as the business of the group if that reflects the economic reality of the situation.
- Case law in England has found that, in certain circumstances, a parent can assume direct liability for the actions of its subsidiary. The cases in question involve a parent assuming a direct duty of care in circumstances where it takes over the management of its subsidiary's activities or it gives advice to its subsidiary about how to manage a particular risk. The court observed that whether a parent assumes a duty of care in relation to its subsidiary's operations depends on the extent to which it participates in its subsidiary's operations. It further observed that a parent does not need to control a subsidiary to participate in its management.

3 Matheson recommendations

Some practical steps can be taken to assist in striking an appropriate balance between sufficient control by the parent and sufficient autonomy of the subsidiary. For instance:



A parent company should avoid excessively interfering or giving directions in the management of the affairs of the subsidiary. Clear intragroup risk management policies should be put in place which deal with, for example, intragroup conflicts and transactions. Each subsidiary should administer these policies on its own behalf.



The directors of an Irish subsidiary should be facilitated in maintaining their discretion to make decisions relating to the affairs of the company independent of the parent company, in particular, where the subsidiary has opposing interests to the wider group. The day to day management of the affairs of the subsidiary should remain the responsibility of the board of the subsidiary. A parent should make it clear that it is not managing its subsidiaries' affairs.



The boards of the group companies should convene separate and regular board meetings for each group entity and maintain appropriately detailed minutes of those meetings, which outline the rationale for decisions made.



Where possible, groups should avoid constituting the same boards of directors at parent and subsidiary level and appoint independent non-executive directors to the boards where appropriate.



A group seeking to mitigate the risk of potential parent company liability should obtain independent third party advice on subsidiary risk matters rather than relying solely on the advice of the parent.

4 Conclusion

By following these steps it will be easier for directors to clearly identify the interests of each company within the group. Once the interests have been identified, then directors of a subsidiary can make decisions more clearly, always remembering that their primary duty is to act in the best interests of the subsidiary while taking into consideration the interests of the parent company and the group.

For more information on the above, contact [Susanne McMenamin](#), [Veronica O'Donnell](#) or your usual Matheson contact.

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