WHEN LIABILITY FALLS, THE VEIL PREVAILS: ENVIRONMENTAL OFFENCES AND THE CORPORATE VEIL

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ABSTRACT

Innocent lives are lost and communities devasted due to hazardous environmental practices of corporations. This trend is recurrent in developing nations where multinational organisations set up their subsidiary companies. These parent corporations often structure themselves to avoid liability, engaging in acts through their subsidiaries that violate the environmental norms and overlook international and domestic safety procedures. When harm is caused, they are shielded by the doctrine of corporate veil. This veil allows parent companies to escape liability, thereby saving themselves from paying equitable compensation to victims. This leaves the victims in developing nations helpless. They suffer from chronic health hazards, often lose their homes, and are left with little to no compensation. Indian law lacks clear statutory provisions to address this issue, and the guidelines laid by the courts are vague and ineffective. This calls for an urgent need to reform the jurisprudence on corporate veil in India. The paper critically analyses the precedent originating from Salomon v. Salomon and examines its development through landmark cases such as *Adams v. Cape Industries*, and *Union Carbide Corporation v. Union of India*. Drawing on the UK's evolving jurisprudence and the theory of 'Extending the Veil', the paper advocates for a more robust and effective framework for attributing liability to parent companies. A timely reform in the law will help prevent environmental atrocities committed by multinational corporations and ensure just compensation for victims of environmental harm.

I. Introduction

For far too long, transnational corporations have escaped responsibility for their environmental crimes, leaving communities devastated, ecosystems destroyed, and governments unable to pursue justice.[1]

Upon the incorporation of a company, it births as a legal entity. The law recognises it as a separate legal self, distinct from the individuals working behind the company's name. The company is assigned a mind of its own and becomes a separate artificial and juristic person. Such incorporation awards the directors and shareholders with limited liability for the company's acts. A veil is drawn between the company and its members. The *doctrine of the corporate veil* separates the liability of a company from the liability of its shareholders.[2] Over the years, the corporations have recognised the strength of this veil. Transnational companies have been shielding behind this legal shield, and setting up subsidiary companies in developing countries. In doing so, they escape the accountability and liability for the damages inflicted by the subsidiary companies, often engaged in environmentally hazardous activities.

However, the extent of damage and environmental impact of toxic products and chemicals that these subsidiary company's account for are often lethal, unsafe, and threatening to both the communities and the eco-system. The veil double victimises the developing countries by protecting the transnationals from liability and further limiting the compensation they deserve. This paper examines the landmark case of *Adams v. Cape Industries*[3], one of the earliest instances where a parent company avoided liability for the actions of its subsidiary, despite the harmful environmental violations. The discussion then connects this precedent to the more recent Indian case of *Union Carbide Corporation v. Union of India*[4], where the doctrine of the corporate veil was used by parent companies to evade full accountability. Analysing the precedents, this paper addresses the thesis that the broad discretion granted to courts in deciding when to lift the corporate veil is problematic, particularly in cases of environmental harm. This discretion often results in unjust outcomes for victims and inadequate compensation, as the corporate veil serves to protect companies rather than holding them fully responsible for the

[1] Sharan Burrow, *Speech to the Climate Change Conference*, INTL. TRADE UNION CONFERENCE (Mar.13,2015).
[2] Salomon v. Salomon (1896) AC 22.
[3] Adams v. Cape Industries (1990) CH 433.
[4] Union Carbide v. Union of India, (1992) AIR 248.

damages they cause.

II. The Salomon Precedent and The Doctrine of Limited Liability

The courts have upheld the separate legal nature of a corporation.[5] A company is independent from its members and shareholders and has an identity of its own. The legal precedents enshrined in the case of *Salomon v. Salomon*[6] follows the doctrine of limited liability which protects the members from being personally liable for any wrong or harm committed under the company name. It creates a distinct 'corporate personality' separate from its members. The legal rationale behind the doctrine is rooted in encouraging entrepreneurs to conduct business freely and stimulate entrepreneurial risk-taking. Although the Salomon precedent has been followed strictly by the courts, some scholars had reserved apprehensions against the ambitious legal principles it set. They regarded *Salomon* as immoral and disastrous.[7]

The heavily cited precedent goes against the idea that the beneficial owners running a corporation should be responsible for the actions they undertake under the company name. It creates a wall between the companies that are owned and operated by the same people. The concept of a separate legal entity makes it easier for owners to run away from responsibilities and accountability knowing that the wall will protect them. The precedent takes away the 'parent' status of the holding companies and makes them mere shareholders in the subsidiary companies. This helps them shield themselves from responsibility for any unlawful acts of the subsidiary companies, while still maintaining substantial control behind the scenes.

III. How Cape industries used Corporate Structuring to Protect Itself from Liability

Following *Salomon*, in 1990 the UK courts dealt with corporate shield between the transnational holding company, Cape Industries Plc, and its subsidiary based in the US, NAAC. NAAC was a wholly owned subsidiary, with Cape owning all 1000 shares. The corporation engaged in mining, processing and marketing of asbestos, a carcinogenic mineral. The holding company was well aware that their subsidiaries were using products lethal in nature for over half a century. The fatal exposure to asbestos caused occupational and environmental injury

[5] Salomon v. Salomon (1896) AC 22.
[6] *Id*.
[7] Geoffrey Tweedale & Laurie Flynn, *Piercing the Corporate Veil: Cape Industries and Multinational Corporate Liability for a Toxic Hazard, 1950—2004*, 8 ENTERPRISE & SOCIETY 268 (2007).

which led to mesotheliomas among office staff, construction workers, and railwaymen.[8] Mr. Justice Scott accepted that NAAC had been an integral part of the Cape group, which operated widely as a single economic entity, yet dismissed Adam's claims on the grounds that NAAC, despite all the claims, was a separate legal entity.

The court's resistance to lift the corporate veil denied justice to the victims. Cape industries had cleverly organised its corporate structure across different jurisdictions to shield itself from any liability. This gave Cape a free pass to directly avoid paying damages for the health hazards caused by the asbestos exposure. The ruling undermined the principles of justice and equity, leaving victims without adequate compensation. While the courts recognised the individual personality of NAAC, they overlooked how Cape had consciously structured itself to avoid liability. Cape had deliberately designed themselves a corporate framework that leveraged the doctrine of corporate veil to its advantage and ensured that none of the legal and financial consequences of partaking in hazardous activities would reflect on it. The courts turned their eyes from the reports showing that NAAC was an important contributor to Cape's economic performance.[9] The important question to ask is, If NAAC's success benefitted the parent company, why should the veil shield the parent company when liabilities arose? By maintaining such a legal separation between the parent and subsidiary company, Cape escaped due accountability for the actions of NAAC that were de facto being overlooked by Cape Industries.

IV. The Issue of Puppet Subsidiaries

There has been a wide discretion on the courts on when to raise this corporate immunity veil. The presence of this wall between corporations is not justified in cases where corporations are freely committing environmental crimes by establishing puppet subsidiaries in developing countries. By exploiting the corporate veil, the multinational parent companies profit from the hazardous activities carried out under the names of their subsidiaries. This leaves the local communities to bear the brunt of environmental destruction and the serious health crisis without receiving fair compensation. This profit structure is often found in developing countries. The law should be specifically stricter in cases involving hazardous environmental torts, which cause long-lasting and life-threatening damages upon the victims.

[8] Morris Greenberg, *Cape Asbestos, Barking, Health and Environment: 1928-1946*, 43 AMERICAN JOURNAL OF INDUSTRIAL MEDICINE (2003), https://onlinelibrary.wiley.com/doi/10.1002/ajim.10147.
[9] Geoffrey Tweedale and Laurie Flynn, *supra* note 7. at 276

India's most famous case in this field is *Union Carbide Corporation v. Union of India*[10]. It is one of the first cases where the courts dealt with the question of whether a holding company is liable for the environmental hazards caused by its subsidiary company. The catastrophic gas leak of methyl isocyanate occurred at the factory under Union Carbide India Limited (UCIL), a subsidiary of a U.S. based company, Union Carbide Corporation (UCC). [11] The impact of the leak has been life-threatening for generations of families who lived in the city. Hospitals were filled with people suffering from breathing problems and other illnesses caused by the toxic gas.[12] However, when the victims approached the courts to seek relief, the courts turned a blind eye to the extent and impact of the damage caused to the victims.

Indian courts did not expressly pierce the corporate veil of Union Carbide, despite there being evidence that UCC owned and controlled the subsidiary.[13] While the courts ordered UCC to compensate the victims, however the amount of compensation was heavily criticised as it was inadequate in proportion to the magnitude of the tragedy.[14] The defaulting company was U.S. based. While, the judgement imposed the liability on UCC to pay the compensation, the amount was not comparable to the amount that is granted in similar cases in the U.S. The compensation awarded was unjust. While the judgement on the face seemed to protect the interests of the harmed, in reality it did not provide substantial and adequate relief to the victims. These were very narrow victories.[15]

V. Holding the Multinational Companies Accountable: The Degree of Control Test

The Indian courts, while ordering the compensation, failed to fully address the larger question of holding the multinational parent companies like UCC accountable to the extent of the environmental damage that is caused. With no clear ruling or guideline on the extent of liability that must fall on the parent multinational companies committing environmental hazards, incidents like these are bound to continue. It would lead to a continual of injustice to victims

[10] Union Carbide Corporation v. Union of India, (1990) AIR 273.
[11] *Id.*
[12] Aryan Gupta, *Union Carbide Corporation vs Union of India Etc on 4 May, 1989*, THE LEGAL QUORUM (Apr. 2024), https://thelegalquorum.com/union-carbide-corporation-vs-union-of-india-etc-on-4-may-1989/#:~:text=Regarding%20the%20issue%20of%20corporate,accountable%20for%20the%20damages%20incurred.
[13] Sharmishtha Bharde, *Lifting of the Corporate Veil for Environmental Degradation: Enterprise Liability in India*, 3 SYMBIOSIS LAW SCHOOL, PUNE (2018).
[14] Aryan Gupta, *supra* note 12.
[15] Tomas Mac Sheoin & Frank Pearce, *Introduction: Bhopal and After*, 41 SOCIAL JUSTICE 135 (2014).

of environmental hazards. While the damage to a human life can still be accounted for, however the industrial damage through toxins to the environment is irreparable. The existing *'Degree of Control'*[16] test used by the Indian courts to establish whether or not the parent company should be held liable for the acts of its subsidiary is insufficient. It is very easy for multinationals, backed up by their team of lawyers, to mislead the courts and portray an image that is favourable to them. Likely, Cape Industries had strategically structured themselves to show that they neither had any presence in the U.S., nor were they controlling NAAC. The company argued that it had no physical office or visible presence and hence was not subject to U.S. jurisdiction or taxation as a domestic company.[17]

The degree of control test is narrow and inadequate for cases involving multinational corporations, particularly regarding environmental hazards. Such big transnational companies are well aware of the risks their subsidiaries pose. They ought to have known the likelihood of the irreversible environmental damage the acts of their subsidiaries would cause. With the resources they have, they are well capable to foresee when and how such huge environmental damage is caused. In reality, multinational parent companies exert significant influence over their subsidiaries without being involved in their daily management. In the UCC case, an internal memo was found proving that the company had knowledge about the potential risk of the plant.[18] Similarly, a chemist verified that he had continually warned Cape industries about the health hazards of asbestos, yet neither Cape nor the NAAC ever placed warning labels on asbestos products.[19] The courts are overlooking the strategic oversight of the parent companies in a corporate structure and that policy decisions of multinational companies are carefully constructed and made keeping in mind the impact it would have on its subsidiaries. The test fails to capture this form of indirect yet substantial influence that the parent companies are bound to have on their subsidiaries. In cases of environmental damage, the corporate veil should not remain a shield for multinational corporations.

VI. U.K. Jurisprudence and The Theory of Extending the Veil

"Even if piercing would be harsh to a passive parent corporation that did not participate in

[16] Union Carbide Corporation v. Union of India, (1990) AIR 273.
[17] Geoffrey Tweedale and Laurie Flynn, *supra* note 5, at 280.
[18] Evelina Singh, *Parent Company Liability for Environmental Disaster Caused by Subsidiary Company*, 2 IMPERIAL JOURNAL OF INTERDISCIPLINARY RESEARCH (IJIR) (2016).
[19] Geoffrey Tweedale and Laurie Flynn, *supra* note 5, at 11.

the wrongful action, it would seem to be outweighed by the harshness of those injured."[20]

While the courts have recognised that the veil should be pierced only in exceptional cases, it is also crucial that courts come up with stricter guidelines for environmental liability. The courts must interpret a technique of lifting the veil that holds the parent companies accountable, especially when such cases of hazardous environmental damages are caused by the subsidiary companies. The Indian courts can apply one of the techniques to manoeuvre the corporate veil referred by the Companies Act, 1985 of the United Kingdom. S. Ottolenghi refers to it as 'Extending the Veil'.[21] It is a technique of extending the veil so that it embraces a bunch of companies, treating them as a single unit. Here, the veil is lifted from each company, but instead of focusing on them individually, they are all seen as one large entity working together. The acts of the companies are interconnected and the theory assumes the parent company to be able to foresee and oversee the acts of its subsidiaries. Rather than dealing with each company separately, we can look at them as one enterprise. The veil is extended over the entire group as one entity.

This discourse on the corporate veil should be incorporated within the Indian corporate laws as well. To prevent such further environmental degradation by multi-national parent companies, India must adopt the concept of 'Extending the Veil'. A recent UK precedent set pivotal guidelines on when to assign accountability.[22] To determine, one must look at the extent to which the parent company took over, or shared in, the management of the relevant activity. Whether the parent company had provided any defective advice or policies which were followed by the subsidiary, promulgated group-wide safety or environmental policies and taken steps to ensure their implementation. These guidelines lay down a comprehensive criteria for attributing liability, moving beyond the rigid confines of the victorian doctrine of separate legal personality.

VII. Conclusion

Having discretion in an area of law which has not been fully explored and left ambiguous will let many transnational corporations run liability-free. It risks creating legal loopholes for parent

[20] Robert B. Thompson, *Unpacking Limited Liability: Direct and Vicarious Liability of Corporate Participants for Torts of the Enterprise*, 47 VANDERBILT LAW REVIEW (1994).
[21] S. Ottolenghi, *From Peeping behind the Corporate Veil to Ignoring It Completely*, 53 THE MODERN LAW REVIEW 338 (1990).
[22] Vedanta Resources PLC v Lungowe & Ors (2019) UKSC 20.

companies. Indian courts have to read the doctrine of corporate veil in a manner that doesn't leave blind spots for multinational parent companies to shield their assets while causing hazardous damage to people and the environment we all share together. Recognizing the urgency of the issue, Australia recently passed amendments holding the directors and related corporate bodies liable for environmental offences.[23] They would be held liable to pay an amount equivalent to the financial gain they received from committing the environmental offence.

While the doctrine of the corporate veil historically intended to encourage entrepreneurship and limit personal liability, over time it has become a tool of exploitation for multinational companies. The present 'degree of control' test is insufficient to account for the reality of how the multinational companies function. Courts must identify cases when corporate structures are deliberately designed to shield parent companies from liability. The law must not remain silent when the environmental harm is widespread and hazardous. It is imperative that Indian courts reinterpret and lay down clear and effective guidelines on the doctrine of corporate veil. Indian courts must take notes from the UK Jurisprudence on corporate veil, which acknowledges the real control and power in the hands of parent companies and enables courts to assign liability when necessary.

Environmental damage is irreparable and its health hazards are lethal to the victims. The compensation that the victims receive are often insufficient and unjust. The Companies Act must be amended to include provisions that ensure just and adequate compensation is provided to the victims of environmental hazards. A regulatory body should be created under the National Green Tribunal to oversee the corporate environmental activities. Taking measures in this direction will not only protect the environment but also ensure justice for the victims in the face of environmental harm.

[23] Tanmay Gupta & Prerna Sengupta, *Environmental Piercing of Corporate Veil: Assessing the Liability of Directors and Parent Companies*, NLU DELHI (May 24, 2022), https://www.cbflnludelhi.in/post/environmental-piercing-of-corporate-veil-assessing-the-liability-of-directors-and-parent-companies.