*Page 1440 - 1464* **DOI:** *https://doij.org/10.10000/IJLMH.11657*

# INTERNATIONAL JOURNAL OF LAW MANAGEMENT & HUMANITIES

[ISSN 2581-5369]

**Volume 4 | Issue 3**

**2021**

# The Holistic and Modern Approach of Lifting the Corporate Veil and its Judicial Interpretation in Present Day Scenario

AQUIB ROUF[1]

## ABSTRACT

*The foul play and danger to the greater public interest has given a momentum to break open the insulation of the protective covering (veil), which in legal terminology referred to as " Corporate veil". For the determination of the character especially the negative one which a company might acquire in its long run ruining the public interest and prima facie indulge in such activities which are per se illegal. The piercing of this veil is solely to find out the persons who in reality control the company's affairs. We are aware of the scenario in todays world how the corporate existence are used as vehicles of fraud, sometimes to defraud creditors or to avoid the legal obligations, so this can be only stopped only when the covering is lifted and the real person behind this kind of transaction is pointed. Here we will understand the concept of lifting of corporate veil and the rationale behind doing so, along with judicial pronouncements and interpretation with help of various types of Indian and foreign cases, which will help us to understand the nature and ways the illegalities are committed by the Directors or shareholders or as a whole in the camouflage of the company. The lack of any particular uniformity in Indian and foreign courts in the application of the principles of lifting of corporate veil due to lack of clarity and unanimously accepted appellations gives rise to legal issues on legal jurisprudence and the framework, which we will try to resolve in our current research paper.*

***Keywords:*** *Corporate offences, theories of corporate offence, Judicial interpretation, dynamism of pragmatic world.*

## I. INTRODUCTION

The rudimentary attribute of corporate personality from which all other consequences flow if that the corporation is a legal entity distinct from its members. Hence, it is capable of enjoying rights and of being subjects to duties which are not the same as those enjoyed or borne by its members. Corporate personality has been described as the 'most imbuing of the fundamental

[1] Author is a student at Alliance school of law, Alliance University, Bengaluru, Karnataka, India.

 [ISSN 2581-5369]

principles of company law". It constitutes the underpinning principle upon which corporation is regarded as an entity distinct from the shareholders comprising it. The issue of "lifting the corporate veil" has been considered by courts and scholars for many years and there are instances in which the courts have deviated from the strict application of this doctrine. This doctrine has been established for business efficacy, necessity and ease. In the doctrine of 'Lifting the Corporate Veil', the law goes behind the mask or veil of incorporation in order to determine the real person behind the mask of a company.

One of the main reasons for forming a corporation is the limited liability it offers its shareholders. By this doctrine of limited liability, a shareholder can only lose only what he or she has contributed as shares to the corporate entity and nothing more. But for clarity as to 'Lifting of the Corporate Veil', an understanding of the corporate personality of a company is required, along with study of the provisions of Indian law that paves the way for courts to pierce the corporate veil. The term "piercing the corporate veil" has also been described as, "the Court's unwillingness to permit corporate presence and action to divert judicial course of applying law to ascertain facts". When this principle is importuned, it is permissible to show that the individual hiding behind the corporation is liable to discharge the obligations ignoring the concept of corporation as a separate entity. The acts of malfeasance and acts of peccadillo or violation by the shareholders and directors of a corporation, do not always bind the corporation as such. However so as to apply law to ascertained facts, judicial process can ignore juristic personality of the company and draw-up the directors and in certain cases even shareholders to discharge the legal obligations. When the corporate veil is lifted/pierced, it only means that the Court is assuming that the corporate entity of a concern is a sham to perpetuate the fraud, to avoid liability, to avoid effect of statute and to avoid obligations under a contract.

**(A) Objective**

The objective of our research paper is to find out the discrepancy in selecting or choosing a particular doctrine in lifting of corporate veil by Indian and foreign courts in order to decide a particular case, as there is no set yardstick or uniformity in applying any particular doctrine.

**(B) Scope**

We have limited ourselves to only the application of different principles or doctrines in lifting up of corporate veil in order to establish the fact that there is a dearth or shortfall in legal jurisprudence in choosing a particular doctrine.

**(C) Research Problem**

The legal issue of non-existence of a set benchmark or touchstone in applying a particular

 [ISSN 2581-5369]

doctrine of lifting of corporate veil paves way for many discrepancies in judegement delivered by Indian as well as foreign courts.

**(D) Hypothesis**

The loophole in Legal jurisprudence in selecting a particular principle/doctrine in the purview of lifting of corporate veil gives rise to diverse judicial decisions and judgements due to lack of uniformity.

**(E) Research Question**

1. Does the lack of concrete principles laid down by courts in establishing the lifting of corporate veil gives rise to unruly exemplar and paradigm in major cases?
2. Does the dearth of uniformity in applying a particular doctrine in piercing the corporate veil by different courts gives rise to huge complex scenarios that needs to be simplified?

**(F) Research Technique**

In our Research paper, We have basically used Doctrinal, empirical and comparative case by case analysis techniques in evaluating various aspects that are required for our Research work.

**(G) Method of Writing**

The method of writing followed in the course of research paper is primarily descriptive, objective and case based, which is primarily empirical and doctrinal in nature.

**(H) Literature review**

In our Research paper, we have reviewed and deeply analysed various articles which gave us an insight on how the courts in various jurisdictions apply the various doctrines available to them. The article "Analysis of lifting of corporate veil-Principles of interpretation" By Manish Kumar singh, gives us various grounds on which the veil is lifted and how the camouflage is used by the corporates to escape culpability. The article also mentions the principles used by Apex and high courts in order to ascertain the criminal liability on the corporates. The Research problem in our paper is briefly dealt here in sense, it mentions that there is discrepancy in laying down the rules by different courts in matters of corporate criminal liability. Second article we choose to review is "Piercing of corporate veil in case of sale of shares" by Nishith Desai Associates in their legal Website, also gives us an over view that there is a huge gap in ascertaining different doctrines of lifting of corporate veil and applying them to various cases, which in long run gave rise to various misformities and maladies in different Indian and foreign decisions which are being used as precedent in todays scenario. Due to these discrepancies, there exists a legal loophole which needs to be bridged so that such deviation should not arise

 [ISSN 2581-5369]

in future judgements. The third article we analysed is "overcoming the corporate veil challenge: could legal jurisprudence is still in its evolving stage" by British Institute of International and Comparative Law, shapes and gives us a unidirectional flow towards our research project, that clearly states that various principles are used by different justices around the globe in dealing many similar kinds of corporate cases that prima facie gives rise to various disagreements and inconsistencies.

## II. THE GROUNDS FOR LIFTING OF CORPORATE VEIL

As early as Solomon, judgments have desired possible exceptions to the separate entity concept. Lord Halsbury recognised the separate entity providing there was "no fraud and no agency and if the company was a real one and not a fiction or myth." As pointed by Lord Denning in *Littlewoods*

*Mail Order Stores Ltd. v. IRC*[2], "cast a veil over the personality of a limited company through which the courts cannot see. The courts can, and often do, pull off the mask. They look to see what really lies behind."

The circumstances under which the Courts may lift the corporate veil may broadly be grouped under the following two heads:

### (A) Under Statutory Provisions

#### 1. When membership is reduced

Under section 45 of the Companies Act, when the number of members of a company are reduced below 7 in case of a public company and below 2 in case of a private company and the company continues to carry on its business for more than 6 months while the number is reduced, every person who is a member of such company, knows this fact, is severally liable for the debts of the company contracted during that time.

#### 2. Improper use of Name

Section 147(4) provides that an officer of a company who signs any Bill of Exchange, Hundi, Promissory note, cheque, wherein the name of the company is not broached in the respective manner, such officer will be held personally liable to the holder of such Bill of exchange, promissory note or cheque as the case may be; till it is duly paid by the company.

#### 3. Fraudulent conduct

If in the natural process of winding up of a company, it appears that any business of the

[2] [1969] 1 WLR 1241

company has been carried on with the intent to defraud the creditors of the company or any other person or for any other fraudulent purpose.

4. **Failure to refund application money**

The directors of a company are jointly and severally liable to repay the application money with interest, if the company fails to refund the application money of those applicants who have not been allotted shares within 130 days from the date of issue of the prospectus.

5. **Misrepresentation in prospectus**

In case of misrepresentation in a prospectus, every director, promoter and every other person, who authorizes such issue of prospectus incurs liability towards those who subscribed for shares on the faith of untrue statement

6. **Holding Subsidiary companies**

A holding company is essential to reveal to its members the accounts of the subsidiaries. Every holding company is supposed to attach to its balance sheet, copies of the balance sheet, profit and loss account, directors report and auditors' report etc. in respect of each subsidiary company. It amounts to lifting of the corporate veil because in the eyes of law a subsidiary company is a separate legal entity and through this mechanism their identity is known.

7. **For facilitating the task of an inspector to investigate the affairs of the company**

If it is necessary for the satisfactory completion of the task of an inspector appointed to investigate the affairs of a company for alleged mismanagement, or oppressive policy towards its members, he may investigate into the affairs of another related company in the same management or group.

8. **For investigation of ownership**

The Central Government may nominate one or more inspectors to investigate and report on the membership of any company for the purpose of determining the true persons who are financially interested in the company and who control its policy influence it.

9. **Liability for ultra vires acts**

Directors and other officers of a company will be personally liable for all those acts which they have done on behalf of a company if the same are ultra vires the company.

**B. Under Judicial Interpretations**

1. **Protection of revenue**

 [ISSN 2581-5369]

In the case of CIT v. Sri Meenakshi Mills Ltd[3] where the veil had been used as means of tax evasion, the court upheld the piercing of the veil to look at the real transaction.

**2. Prevention of fraud or improper conduct**

Where the medium of a company has been used for performing fraud or improper conduct, courts have lifted the veil and looked at the reality of the situation.

**3. Determination of the enemy character of a company**

In times of war the court is prepared to lift the corporate veil and determine the nature of shareholding as it did in the Daimler Co. Ltd. v. Continental Tyre and Rubber Co[4], where a company was incorporated in London for the purpose of selling German tyres manufactured by a German company. Its majority shareholders and all its directors were German. The English Courts held it to be an enemy company on lifting the veil and trading with this company was held to amount to trading with the enemy.

**4. Group enterprises**

Sometimes in the case of group of enterprises the Solomon principal may not be adhered to and the court may lift the veil in order to look at the economic realities of the group itself. In the case of D.H.N. Food products Ltd. v. Tower Hamlets London Borough Council[5], it has been said that the courts may disregard Solomon's case whenever it is just and equitable to do so. The court of appeal thought that the present case where it was one suitable for lifting the corporate veil.

**5. Where a company acts as an agent for its shareholders**

Where a company is acting as agent for its shareholder, the shareholders will be liable for the acts of the company. It is a question of fact in each case whether the company is acting as an agent for its shareholders. There may be an Express agreement to this effect or an agreement may be implied from the circumstances of each particular case.

**6. In case of economic offences**

In Santanu Ray v. Union of India[6] it was held that in case of economic offences, a court is entitled to lift the veil and pay regard to the economic realities behind the legal façade.

**7. Where Company is a sham or cloak**

[3] AIR 1967 SC 819
[4] [1916] 2 AC 307
[5] [1976] 1 WLR 852
[6] 1988 (38) E.L.T. 264 (Del.)

 [ISSN 2581-5369]

When the court finds that company is a mere r sham and is used for some illegal or improper purpose, it may lift veil. In the leading case of P.N.B. Finance v. Shital Prasad[7] where a person borrowed money from a company and invested it into three different companies, the lending company was advised to bring together the assets of all the three companies, as they were created to do fraud with the lending company.

## III. ELEMENTS OF PIERCING

### (A) Control and Domination

Control and determination part of the test that rules the relationship between the shareholder and the corporation. Generally, skimpy majority stock ownership will be insufficient to satisfy this element. Instead, one must show "complete domination, not only of finances, but of policy and business practice in respect to the transaction attacked so that the corporate entity as to this transaction has no separate mind, will or existence of its own."

### (B) Improper purpose or use

This test requires the suer to show that the control exercised by the parent company or dominant stockholder was "used by the defendant to commit fraud or wrong, to perpetrate the violation of a statutory or other positive legal duty, or dishonest and unjust act in contravention of plaintiff's legal right." This inquiry focuses on the relationship between the plaintiff and the corporation.

### (C) Resulting damage or harm

In this test, the litigant must prove that the defendant's control, exerted in a fraudulent, illegal or otherwise unfair manner toward it, caused the harm suffered. In other words, the plaintiff must prove that till the corporate veil is pierced, it will have been treated unjustly by the defendant's exercise of control and improper use of the corporate form and suffer damages.

## IV. CORPORATE CRIMINAL LIABILITY- PROSECUTION OF CORPORATE ENTITIES

Large-scale corporations are the stipulating force on the globe. They are everywhere, in almost every aspect of our lives. Analogous to this, sometimes dominant, corporations have become dangerous criminals as well. However, Corporations being non-human entities, their criminal behaviour is also out of the ordinary. Corporate criminality nags at our sense of reality. It is this characteristic that makes corporate crime a precarious issue. The development of corporate criminal liability has become a problem which a growing number of prosecutors and courts

[7] 1983 54 CompCas 66 Delhi

 [ISSN 2581-5369]

have to deal with at the present time. In the common law, following standing principles in tort law, English courts began sentencing corporations in the middle of the last century for statutory offenses. On the other hand, a large number of European continental law countries have not been able to or not been willing to incorporate the concept of corporate criminal liability into their legal systems. The fact that crime has shifted from almost solely individual perpetrators only 150 years ago, to white-collar crimes on an ever increasing scale has not yet been taken into account in many legal systems. At the same time, crime has also become increasingly international in nature.

Criminal Liability is what unlocks the logical structure of the Criminal Law. Each element of a crime that the prosecutor needs to prove beyond a reasonable doubt, is a principle of criminal liability. There are some crimes that only involve a subset of all the principles of liability, and these are called crimes of criminal conduct. The question of striking criminal liability to a corporation for criminal offences committed by directors, managers, officers and other employees of the corporation while conducting corporate affairs has gained a lot of significance in the jurisprudence of criminal law. Now the question is, *whether a corporation as an artificial person is capable of committing a crime and is criminally liable by the law or not?* The traditional view was that a corporation could not be guilty of a crime because criminal guilt needed intent and a corporation not having a mind could form no intent. In addition, a corporation had no body that could be imprisoned.

## V. CRIMINAL LIABILITY OF CORPORATIONS: PRE-STANDARD CHARTERED BANK CASE LAW

Earlier, Indian courts were of the belief that corporations could not be criminally prosecuted for offenses requiring *mens rea* as they could not possess the requisite mens rea. Mens rea is an essential element for majority, if not all, of offenses that would attract imprisonment or other penalty for its violation. Indian courts held that corporations could not be prosecuted for offenses requiring a mandatory punishment of imprisonment, as they could not be imprisoned.

In A. K. Khosla v. S. Venkatesan[8], two corporations were charged with having committed fraud under the IPC. The Magistrate issued process against the corporations. The Court in this case pointed out that there were two pre-requisites for the prosecution of corporate bodies, the first being that of mens rea and the other being the ability to impose the mandatory sentence of imprisonment. A corporate body could not be said to have the necessary mens rea , nor can it

[8] (1992) 1 CALLT 77 HC

 [ISSN 2581-5369]

be sentenced to imprisonment as it has no physical body.

In Kalpnath Rai v State[9] (Through CBI), a company accused under the Terrorists and Disruptive Activities Prevention (TADA) Act, was alleged to have harbored terrorists. The trial court convicted the company of the offense punishable under section 3(4) of the TADA Act. On appeal, the Indian Supreme Court referred to the definition of the word "harbor" as provided in Section 52A of the IPC and pointed out that there was nothing in TADA, either express or implied, to indicate that the mens rea element had been excluded from the offense under Section 3(4) of TADA Act.

There is variability over whether a company can be convicted for an offence where the punishment prescribed by the statute is imprisonment and fine. This controversy was first addressed in MV Javali v. Mahajan Borewell & Co and Ors[10] where the Supreme Court held that mandatory sentence of imprisonment and fine is to be imposed where it can be imposed, but where it cannot be imposed namely on a company then fine will be the only punishment.

In Zee Tele films Ltd. v. Sahara India Co. Corp. Ltd[11], the court dismissed a complaint filed against Zee under Section 500 of the IPC. The complaint alleged that Zee had telecasted a program based on falsehood and thereby defamed Sahara India. The court held that mens rea was one of the essential elements of the offense of criminal defamation and that a corporation could not have the requisite mens rea. In another case, Motorola Inc. v. Union of India[12], the Bombay High Court revoked a proceeding against a corporation for alleged cheating, as it came to the conclusion that it was impossible for a corporation to form the requisite mens rea, which was the essential ingredient of the offense. Thus, the corporation could not be prosecuted under section 420 of the IPC.

Standard Chartered Bank Case Law- A landmark case in Indian Scenario.

This is the landmark case in which the Supreme court overruled the all other laid down principles. In this case, Standard Chartered Bank was being prosecuted for violation of certain provisions of the Foreign Exchange Regulation Act, 1973. Ultimately, the Supreme Court held that the corporation could be prosecuted and punished, with fines, regardless of the mandatory punishment required under the respective statute.

The Court did not go by the *literal and strict interpretation* rule required to be done for the penal statutes and went on to provide complete justice thereby imposing fine on the corporate.

[9] 1997 (2) ALD Cri 805
[10] https://indiankanoon.org/doc/360726/
[11] AIR2005SC2677
[12] 2004 CriLJ 1576

 [ISSN 2581-5369]

The Court looked into the interpretation rule that that all penal statutes are to be strictly construed in the sense that the Court must see that the thing charged as an offence is within the plain meaning of the words used and must not strain the words on any notion that there has been a slip that the thing is so clearly within the mischief that it must have been intended to be included The court held that the FERA statute was quite clear: corporations are vulnerable to criminal prosecution, and allowing corporations to escape liability based on the difficulty in sentencing would do violence to the statute. *The Court did not develop its reasoning far enough so as to specifically hold that a corporation is capable of forming mens rea and acting pursuant to it*. However, the Court held that corporations are liable for criminal offenses and can be prosecuted and punished, at least with fines. Criminal Liability of Corporations: Post-Standard Chartered Bank Case Law

There is no privilege to companies from prosecution merely because the prosecution is in respect of offences for which punishment prescribed is mandatory imprisonment. In Iridium India Telecom Ltd. v. Motorola Incorporated and Ors[13], the Supreme court held that a corporation is virtually in the same position as any individual and may be convicted under common law as well as statutory offences including those requiring mens rea. The criminal liability of a corporation would arise when an offence is committed in relation to the business of the corporation by a person or body of persons in control of its affairs and relied on the ratio in *Standard Chartered Bank Case*[14].

The apex court held that corporations can no longer claim immunity from criminal prosecution on the grounds that they are incapable of possessing the necessary mens rea for the commission of criminal offences. *The notion that a corporation cannot be held liable for the commission of a crime had been rejected by adopting the doctrine of attribution and imputation.*

In another landmark judgment in July 2011 of CBI v. M/s Blue-Sky Tie-up Ltd and Ors[15], the apex court reiterated the position of law held that corporations are liable to be prosecuted for criminal offences and fines can be inflicted on the companies.

## VI. ASSESSING COMMON LAW THEORIES OF CORPORATE CRIMINAL LIABILITY-

The advocacy of criminal liability of corporations has largely been a twentieth century judicial development, influenced by the "sweeping expansion" of common law principles. The majority of theories of corporate criminal liability are typical of common law developments that have

[13] (2011) 1 SCC 74
[14] AIR 2005 SC 2622
[15] (2011) 15 SCC 144

 [ISSN 2581-5369]

been constructed on a case-by-case basis. Despite their importance, these theories have proved to be ineffective, for their lack of strong theoretical basis and their individualistic roots.

**(A) Agency Theory**

The agency theory was first developed in tort law and slowly was carried over into the criminal arena. According to this theory, the corporation is liable for the intents and acts of its employees.

Vicarious liability (or respondeat superior) is commonly used and applied in the United States. In other jurisdictions, this theory is restrictively established in relation to some strict liability and hybrid offences that deal with matters such as pollution, food, drugs, health and safety at work but not to mens rea offences.

The agency theory is based on the premise that criminal violations normally entail two elements, actus reus and mens rea. Since corporations are considered to be purely incorporeal legal entities, they do not own any mental state and the only way to impute intent to a corporation is to consider the state of mind of its employees. The theory surrounds a simple and logical method of attributing liability to a corporate offender, if corporations do not have intention, someone within the corporations must have it and the intention of this individual as part of the corporation is the intention of the corporation itself. Courts in the United States, where the theory is widely used, have developed a three-part test to determine whether a corporation will be held vicariously liable for the acts of its employees. First, the employee must be acting within the scope and course of his employment. Secondly, the employee must be acting, at least in part, for the benefit of the corporation, yet it is irrelevant whether the company actually receives the benefit or whether the activity might even have been expressly prohibited. Thirdly, the act and intent must be imputed to the corporation.

In United States v. Investment Enters Inc[16] , the company was convicted of violating obscenity laws where the corporation's president conspired to transport obscene videos in interstate commerce. The president's unlawful acts could be imputed to the corporation because he was an undisputedly authorized agent.

Federal courts have persistently held that a corporation may be liable for the actions of its agents regardless of the agent's position within the corporation. These Courts have found that an employee's act can bind the corporation even where the corporation has implemented *policies prohibiting the behaviour*. *When an employee's conduct is contrary to the company's*

[16] 498 U.S. 292

 [ISSN 2581-5369]

*compliance policies and specific directives, the company can still be held liable*. The company can prove that it has established corporate policies in an effort to reduce crime, but this does not prevent a court from establishing it criminally liable. The existence of an effective compliance policy will not provide an absolute defence from criminal liability, but the company may qualify for a reduced penalty.

The concept of *scope of employment* is common and has broad interpretations. Thus, courts have held that even non-employees conduct can be attributed to be as the corporation's action. In *United States v. Parfait Powder*[17], it was held that independent contractors might act for the benefit of the corporation thereby exposing it to criminal liability. Many states have adopted specific legislative strategy to deal with corporations that requires criminal acts be committed by high managerial agents in order to trigger liability. This position closely resembles the identification theory. In some states, however, the rule is that the actions taken by a corporation's agents need not have been ratified by the corporation's directors, officers, or other high managerial agents in order to be chargeable to the corporation.

**(B) Identification Theory**

The doctrine of identification is the traditional method by which companies are held liable in most countries under the principles of the common law. The limitations of the agency theory led to the construction of a direct liability theory. This theory was developed as an attempt to overcome the problem of imposing primary, as opposed to vicarious, corporate criminal liability for offences that insisted on proof of criminal fault. In Lennard's Carrying Co Ltd v. Asiatic Petroleum Co Ltd,[18] Viscount Haldane fashioned a model of primary corporate criminal liability for offences that require mens rea that would later be known as the *identification theory*. A corporation is a wool-gathering. It has no mind of its own any more than it has a body of its own; its active and directing will must consequently be sought in the person of somebody, who for some purposes may be called an agent, but who is really the directing mind and will of the corporation; the very ego and centre of the personality of the corporation.

As in the agency theory, the identification theory depends on an individual to attribute liability to a corporation. However, while the former doctrine simply imitates tort principles, the latter adjusts these principles to the reality of corporate misconduct. Furthermore, the identification theory introduces the personification of the corporate body. According to this theory, the solution for the problem of attributing fault to a corporation for offences that require intention

[17] 163 F.2d 1008
[18] [1915] AC 705

was to merge the individual within the corporation with the corporation itself. Unlike the agency theory, the individual employee is assumed to be acting as the company and not for the company. The theory de-emphasized the need for the development of vicarious liability. The agency theory has now been considered as unjust and lacking in defensible penal rationale

The main underlying principle of the identification theory is the detection of the guilty mind, the recognition of the individual who will be identified as the company itself, who will be the company's very ego, vital organ, or mind.

*Tesco Supermarket v. Nastrass*[19] is the leading authority in this area. Tesco Supermarket was a large chain store which was charged with an offence against the Trade Descriptions Act 1968 by selling goods to consumers at a price different than had been announced. The prosecution pertubed the advertisement of soap powder at a lowered price. A shop assistant had mistakenly placed normally priced soap powder on the shelf. The manager had failed to make sure that the powder was available at the advertised price. There was a defence of due diligence which could be pleaded by the company, unless the manager's lack of due diligence could be attributed to the company. The question was whether the manager of the store could be identified with the company via the common law doctrine, or in other words, whether natural person or persons are to be treated as being the corporation itself. The House of Lords held that the manager was not a person of sufficiently important stature within the corporate structure to be identified as the company for this purpose and by reason of there had been due diligence at the level of top management, the company could use the defence.

In *Canadian Dredge and Dock*[20]case, The application of identification rule in Tesco, may not accord with the realities of life in our country. Then it is said that the simple size of Canada means that corporations may be widespread, and consequently may have a decentralized control, which implies that the directing minds and will can be found in different geographic locations. This should be a particularly so in a country such as Canada where corporate operations are often geographically widespread. The transportation companies, must of necessity operate by the delegation and sub-delegation of authority from the corporate centre: by the division and subdivision of the corporate brain; and by decentralizing by delegation the guiding forces in the corporate undertaking.

In the case of Director of Public Prosecutions v. Kent and Sussex Contractors Ltd[21], where the defence was taken that the company is incapable of forming criminal intent as it did not have

[19] [1971] UKHL 1 (31 March 1971)
[20] [1985] 1 SCR 662 (23 May 1985)
[21] [1944] KB 146

the will or a state of mind, the Court held that the company can form its intentions through its human agents and in certain circumstances the knowledge of the agent has to be imputed to the body corporate.

In H.L. Bolton Company v. T.J. Graham & Sons[22], Lord Denning as explained the position and said that the company could in many terms be equated with a human body. They have a brain and nervous centre which controls the entire body. They have people as their hands and legs, under instructions of whom work of the nervous centre is carried out. Lord Denning equated the brain and nervous system to the directors and managers who represent the directing will of the company.

In Lennard's Carrying Co. v. Asiatic Petroleum Co[23], Viscount Haldane propounded the "alter ego" theory and distinguished that from vicarious liability. The House of Lords stated that the default of the managing director who is the "directing mind and will" of the company, could be attributed to him and he be held for the wrongdoings of the company.

Again in *R v. Redfern & Dunlop Ltd. (Aircraft Division)*[24] , the Court held that where the employees who were not in the decision making level could not be ¨identifiable¨ with the company and therefore were not deemed to be the controlling mind of the company. The question that comes up is that if a person at a lower level commits a crime in the name of the company, the company cannot be held liable for the same. This may pose to be a problem in the sense that the company may make a division between the senior management and the employees to avoid criminal proceedings against them.

The Indian cases where the Courts have followed the *doctrine of identification* are *Union of India v.*

*United India Insurance Co. Ltd*. and others[12] and *Assistant Commissioner, Assessment –II, Bangalore and others v. Velliappa Textiles Ltd. & Ors*[25].

### (C) Aggregation Theory

The aggregation theory is grounded in a resemblance to tort law in the same way as the agency and identification doctrine. Under the aggregation theory, the corporation aggregates the composite knowledge of different officers in order to determine liability. The company aggregates all the acts and mental elements of the important or relevant persons within the

[22] [1957] 1 QB 159
[23] [1915] A.C. 705
[24] (1991) 93 Cr.App
[25] 2004 AIR (SC) 86

 [ISSN 2581-5369]

company to establish whether in toto they would amount to a crime if they had all been committed by one person. According to Celia Wells, aggregation of employees' knowledge signify that corporate culpability does not have to be contingent on one individual employee's satisfying the relevant culpability norm. The theory of aggregation is a result of the work of American Federal Courts. The leading case is *United States v. Bank of New England*[26], In this case, the question was if any knowledge and will could be attributed to the corporate entity. The trial judge found that the *collective knowledge model* was entirely appropriate in such context, and stated as much in addition, however, you have to look at the bank as an institution. As such, its knowledge is the sum of all the knowledge of all its employees. That is, the bank's knowledge is the totality of what all of the employees knew within the scope of their employment. So, if employee X, knows of one facet of the currency reporting requirement, Y knows another facet of it, and Z a third facet of it, the banks know them all. So, if we find that an employee within the scope of his employment knew that the reports had to be filed, even if multiple checks are used, the bank is deemed to know it if each of the several employees knew a part of the requirement and the sum of what the separate employees knew amounted to the knowledge that such a requirement existed. The supporters of collective knowledge explain that the difficulty of proving knowledge and willfulness in a compartmentalized structure such as a corporation should not be an obstacle to the formation of the corporation's knowledge as a whole.

## VII. VICARIOUS LIABILITY VIS-A-VIS IDENTIFICATION DOCTRINE

Vicarious liability is a doctrine wherein the company is held liable for the negligent acts of the servants / agents. The doctrine of identification assumes a situation where the crimes committed by the company can be directed towards the directors / managers of the company who are the directing mind and will of the company and they are held liable for the acts committed by a separate legal entity namely the company. Vicarious liability is a reverse concept where the negligent agents of a servant/ agent during the course of his employment or agency, are deemed to be the acts of the company and the company is held liable to make good the same. In the doctrine of vicarious liability, the servants/ agents are being protected under law for the negligent acts done by them, during the course of their employment / agency. On the other hand, doctrine of identification holds the directors / managers who are involved in the criminal activities through the company, liable.

The directors/ managers try to avoid the penalty by taking the defense that the company being

[26] 821 F. 2d 844 (1st Cir. 1987)

a separate legal entity, should be prosecuted separately. The problem that arises in particularly criminal cases is that, the punishment for the crimes are fine and / or imprisonment. If the offender is a company, only a monetary penalty can be imposed. This led to more offences being committed on the name of the company by the directors/ managers, who are protected under the ¨separate legal entity¨ theory. By this doctrine of identification, those offenders are being held liable for the acts committed by the company. The main objective of the doctrine is to punish the people who are actually committing the crime who are the brain and mind of the company through which the crime is being committed.

Recently, the Supreme Court in *Iridium India Telecom Ltd. v Motorola Inc*[27] considered the issue of a company being criminally responsible for the actions of its employees.

The special vicarious liability provisions were in play in *K.K. Ahuja v V.K. Vora*[28], a Supreme Court judgement. A company issued cheques that, to use the commercial parlance, bounced i.e. the cheques were dishonoured because the company's bank balance was not adequate. The legislation on negotiable instruments criminalises the issuance of cheques that are found to be dishonoured. The dishonour of an issued cheque can result in criminal prosecution for the company that issued the cheque as well as the officers under terms that are identical to section 278B of the ITA. Mr. Ahuja, the Deputy General Manager of the company, was prosecuted under the SVL provisions of the negotiate instruments legislation because he was said to be 'in charge of, and responsible to the company for the conduct of the business of the company.

*Is there a milder version of vicarious criminal liability?*

The United Kingdom follows what, at least on the face of it, might be considered as a more liberal version of vicarious criminal liability. A recent example of this version is the Bribery Act, 2010. Under the Bribery Act, a corporate officer is liable for the same offence as that committed by his company if he or she is a senior officer of the company and the offence committed by the company has been committed with the consent or connivance of the senior officer. A person is a senior officer of the company if he or she is the director, manager, secretary or other similar officer of the company.

The test of consent or connivance has been discussed in the House of Lords decision in *R v Chargot Ltd*[29].

This case consists of the unfortunate death of an employee while he was operating a truck on

[27] 2011 AIR (SC) 20
[28] 2009 ALL SCR 1524
[29] [2008] UKHL 73

a the farm owned by the defendant company. The company and its director were subject to criminal prosecution for the violation of legislation relation to health and safety at work. The relevant legislation contained the vicarious liability provisions relating to 'consent or connivance' mentioned above. The House of Lords held that the application of these provisions would depend very much on the particular circumstances in which the corporate offence was committed. Where the legislation defined an offence by virtue of a failure to achieve or prevent a result (a person must not do X), it could be inferred, from the fact that a corporate officer had a supervisory function over the state of affairs that led to the offence, that the corporate officer had consented to or connived in the commission of the offence.

Indian courts have interpreted the special vicarious liability provisions quite strictly and have pointed out that "*even if the corporate officer is formally responsible to the company for the conduct of the business of the company, the prosecution has to prove that in fact the corporate officer was in charge of the overall (not merely one part of the business) day to day business of the company".* This is likely to be a high portal and would, in all probability, cover only the top management of the company such as the managing director and the whole time directors. Very recently the Companies Act, 2013 has brought in harsher provisions regarding the vicarious criminal liability of corporate officers. Under this legislation, for a variety of offences identified under the legislation, certain corporate officers identified by the legislation as officers in default are vicariously liable without any requirement to prove that these officers were actually in charge of the affairs of the company.

*When the Indian position on vicarious liability is compared with the UK position, one notices that the major economic offences statutes in the United Kingdom do not have a special vicarious liability position. Instead these statutes impose liability on the corporate officers for the offences committed by the company only if they have consented to or connived in the commission of the offences or their negligent behaviour has led to the commission of the offences. However, UK Courts have interpreted this provision in such a way that the position of a corporate officer would in most instances be the single most important factor in determining his vicarious liability*

**(A) Doctrine of Alter Ego**

Under this doctrine of Alter Ego, it is described as someone's personality which is not seen by others. The owners and persons who manage the company are considered as the Alter Ego of the company. The directors and other persons who manage the affairs of the company can be held liable for the acts committed by or on the behalf of the company under this doctrine since

the corporation has no mind, body or soul so the people are the directing mind and will.

Thus in denouement we can finally arrive at presumption that

"The Court emerges to be using the term 'doctrine of identification' for a broad set of principles on which actions of an individual who is 'identified' with a company can be attributed to the company and considered to be actions of the company itself. This is distinct from vicarious or agency-based liability. In the case of vicarious liability, the company would be liable for the acts of its servants/ agents. In the case of attribution, the acts will be in law the acts of the company itself"

## VIII. LEGAL POSITION OF "ALTER EGO" IN UNITED STATES

In the case of MCI Telecommunications Corp. v. O'Brien Mktg[30], it was reiterated that the federal common law alter ego rule requires that three elements be proved in order to pierce the corporate veil, the essentials for applicability of alter ego rule are:

"(1) Control, not mere majority or complete stock control, but complete domination, not only of finances, but of policy and business practices in respect to the transaction attacked so that the corporate entity as to this transaction had at the time no separate mind, will or existence of its own; and

(2) Such control must have been used by the defendant to commit fraud or wrong, to perpetrate the violation of a statutory or other positive legal duty, or a dishonest and unjust act in contravention of plaintiff's legal rights; and

(3) The aforesaid control and breach of duty must proximately cause the injury or unjust loss complained of."

In fact, it is interesting to note that the concept of alter ego has also been extended by the Appellate court in an appeal from Circuit court to a criminal case. The doctrine fastens liability on the individual or entity that uses a corporation merely as an instrumentality to conduct that person's or entity's business. It was held in the case of *A.G. Cullen Construction, Inc. v. Burnham Partners*[31], in the context of "piercing the corporate veil," an alter ego analysis starts with examining the factors which reveal how the corporation operates and the particular party's relationship to that operation.

Generally, did the corporation function simply as a facade for the dominant shareholder?

[30] 913 F. Supp. 1536 (S.D. Fla. 1995)
[31] 2015 IL App (1st) 122538

## IX. POSITION IN THE UNITED KINGDOM

The Alter ego doctrine is also referred to as the "Identification Theory" in the United Kingdom. As the company and the individual are considered as a single entity, any agreement with a third party is considered a bipartite agreement. Lord Denning, J. in the case of *H L Boulton (Engineering) Co. Ltd v. T J Graham and Sons Ltd*[32]

Since, the company and the individual are considered to be a single entity, there is no applicability of concept of vicarious liability and the company becomes directly liable for offences involving mens rea responsibility.

In the case of *Tesco Supermarkets Ltd. v Nattrass*[33] , the House of Lords further stated that the basis of the doctrine of alter ego is that a living person has a mind which can have knowledge or intention or be negligent and has hands to carry out his intentions. Whereas, a corporation has none of these it must act through living persons. In such a situation, person who acts is not speaking or acting for the company, but as the company itself. He does not act as a servant, representative, agent or delegate. If his mind is a guilty mind, then that guilt is the guilt of the company.

## X. POSITION IN INDIA

The Supreme Court of India, in the judgment of *Sunil Bharti Mittal v Central Bureau of Investigation*[34], clarified the law of "alter ego". In the instant case the Special Judge had summoned and proceeded against the Directors of the Company. The Special Judge, had held "On the other hand, the reason for summoning these persons and proceeding against them are specifically ascribed in this para which, prima facie, are:

- These persons were/are in the control of affairs of the respective companies.
- Because of their controlling position, they represent the directing mind and will of each company.
- State of mind of these persons is the state of mind of the companies. Thus, they are described as "alter ego" of their respective companies.

The Supreme Court while overruling the decision of the Special Judge, observed that while the Special Judge had applied the principle of alter ego, it had done so in reverse. *The criminal mens rea had been attributed to the directors on the assumption that they are the directing*

[32] [1956] 3 All ER 624
[33] [1971] UKHL 1
[34] AIR 2015 SC 923

*minds behind the acts of the Corporation*. The Supreme Court observed that the Special Judge had ignored the fact that such *an interpretation of the alter ego doctrine would go against the position of law that there is no vicarious liability in criminal law, unless expressly provided in the statute*. Justice Sikri relied on various judgements of the Supreme Court, including the landmark judgment of *Maksud Saiyed v. State of Gujarat*[35] stated – "No doubt, a corporate entity is an artificial person which acts through its officers, directors, managing director, chairman etc. If such a company commits an offence involving mens rea, it would normally be the intent and action of that individual who would act on behalf of the company. It would be more so, when the criminal act is that of conspiracy. However, at the same time, it is the cardinal principle of criminal jurisprudence that there is no vicarious liability unless the statute specifically provides so."

The Supreme Court then relied on the case of *Iridium India Telecom Ltd. vs. Motorola Incorporated and Ors*[36] and held that "*the criminal intent of the "alter ego*" of the company/body corporate i.e. the person or group of persons that guide the business of the company, would be imputed to the corporation." The Court based its decision on the *doctrine of attribution and imputation*. By this rationale, the mens rea can be attributed to a corporation in criminal cases when the affairs of the corporation are carried out by a person or a body person who are in charge of the affairs of the corporation in course of its business. The control should be such and so intense that the company can be said to be functioning through the actions of the person or body of person. Hence, a corporation would be convicted of both statutory as well as criminal offences.

The position concerning the concept of *doctrine of alter ego* or *imputation* of criminal liability to corporations was confusing in India. However, the Supreme Court has definitely brought some clarity regarding the applicability of the doctrine of attribution and imputation in cases of criminal liability of corporations. However, it is still left open to be seen on how a company will be independently attributed with criminal liability when the directors of the corporation have not been held guilty for the criminal offence.

## XI. CORPORATE CRIMINAL LIABILITY - CHALLENGES AND NECESSITY

In the evolving era of technology and new regime of crimes, the strong effect of activities of corporations is phenomenal on the society. In our daily chores, not only do the corporations affect the lives of the people as a blessing but also many a times proves catastrophic which

[35] (2008) 5 SCC 668
[36] (2011) 1 SCC 74

 [ISSN 2581-5369]

then falls under the category of crimes. Despite so many disasters, the law was unwilling to impose criminal liability upon corporations for a long time. This was for basically two reasons that are:

- That corporations cannot have the mens rea or the guilty mind to commit an offence; and
- That corporations cannot be imprisoned.

These two hindrances were managed to survive till late 20th and very early 21st century. The general belief in the early 16th and 17th centuries was that corporations could not be held criminally liable. In the early 1700s, corporate criminal liability faced at least four obstacles, i.e.

- Firstly, attributing acts to a juristic fiction, the corporation. Eighteenth-century courts and legal thinkers approached corporate liability with an obsessive focus on theories of corporate personality; a more pragmatic approach was not developed until the twentieth century.
- Secondly, the legal scholars did not believe corporations could possess the moral blameworthiness necessary to commit crimes of intent.
- Thirdly, the ultra vires doctrine, under which courts would not hold corporations accountable for acts, such as crimes, that were not provided for in their charters.
- Finally, the fourth obstacle was court's plain understanding of criminal procedure; for example, judges needed the accused to be brought physically before the court.

## XII. PRIME CHALLENGE-CORPORATE PUNISHMENT

In India, certain statutes and provisions like the Indian Penal Code relates about different types of punishments that can be imposed upon the convict and as per Section 53 include death, life imprisonment, rigorous and simple imprisonment, forfeiture of property and fine. In certain cases the sections speak only of imprisonment as a punishment like in case of offence under Section 420. Thus the problem arises as to how to apply those sections on the companies since a criminal statute needs to be strictly interpreted and in such statutes there is no scope for corporations to be imprisoned. Going with the above rationale and with the growing trend of corporate criminality, the Courts in India have finally recognized that a corporation can have a guilty mind but still were reluctant to punish them since the criminal law in India does not allow this action.

In *The Assistant Commissioner, Assessment- II, Bangalore and Ors. v. Velliappa Textiles Ltd.*

*and Ors*[37] B.N. Srikrishna J. said that corporate criminal liability cannot be imposed without making corresponding legislative changes. For example, the imposition of fine in lieu of imprisonment is required to be introduced in many sections of the penal statutes. The Court was of the view that the company could be prosecuted for an offence involving rupees one lakh or less and be punished as the option is given to the court to impose a sentence of imprisonment or fine, whereas in the case of an offence involving an amount or value exceeding rupees one lakh, the court is not given a discretion to impose imprisonment or fine and therefore, the company cannot be prosecuted as the custodial sentence cannot be imposed on it. Later this judgement was overruled in *Standard Chartered Bank Case*[38] which set a bench mark or touchstone for upcoming legal issues and inducing punishment to corporations.

## XIII. SUGGESTIONS/RECOMMENDATION

- Corporate bodies reap all the advantages flowing from the acts of the directors and they act to the damage or handicap of the public in the name of the corporate bodies. From the above analysis, it is clear that 'corporate criminal liability' is not an outlandish term. This category of liability existed since time immemorial. However, the legislature kept its mouth shut when the question of imposing punishment arose with respect of corporate liability. With the evolution of various theories, the most vital issue with regard to corporate criminal liability settled i.e., the issue of mens rea. Concept of vicarious and strict liability is an important aspect of corporate criminal liability. Therefore strict legislation needs to be evolved in present scenario which takes all different criminal activities of the corporate into accountability
- The criminal law jurisprudence relating to imposition of criminal liability on corporations is fixed on the point that the corporations can commit crimes and hence be made criminally liable. However, the statutes in India are not in pace with these developments and the above analysis shows that they do not make corporations criminally liable and even if they do so, the statutes and judicial interpretations impose no other punishments except for fines. Apart from fines, punishments such as winding up of the company, temporary closure of the corporation, heavy compensation to the victims, by stepping on the weakness of the corporation i.e., its goodwill, etc. Such means of punishment would have a deterrent effect on the corporate and the sole aim of punishment under criminal jurisprudence would be achieved. A balanced and steady approach should be followed by Indian Courts

[37] 2007 AIR (SC) 2204
[38] AIR 2005 SC 2622

 [ISSN 2581-5369]

- By referring to many Indian and Foreign case laws, we can easily state that different theories and principles/doctrines have been inculcated by different jurists on their own opinion which they feel fit to the case, but there exists a "dissent" too, which should be respected and given a view too. In India, Many land mark cases have been made precedent by a narrow majority due to lack of effective legislature and no proper penalizing statute. "Jurismetrics" of Indian origin is weak per se and needs rampant growth which will make India a blooming economy and to make India a nation of "Justice".
- Presently, all the penal provisions of various statutes inculcate only fine as a form of punishment that can be imposed on a corporation. So is the case with judicial pronouncements on the aspect of sentencing. In inclusion to this, the Law Commission in its 41st Report also speaks of introducing only fine as an additional punishment to be imposed upon corporations in lieu of fines. This *restrictive thinking*, according to Courts is based on the maxim *lex non cogit ad impossibilia*, which shows that law does not contemplate something which cannot be done. This rationale in itself shows that the law lacks in a non-holistic viewpoint in the concept of corporate criminal liability. The Courts have no doubt been efficient in evolving the concept of criminal liability of corporate and have imposed the same on the convicts but the only way of punishing them that has been thought of is by way of fines.
- Few doctrines of Corporate criminal liability like Alter ego or imputation and Vicarious liability and special vicarious liability provisions are still in its accouchement or natal stage, where our high courts and apex courts held different views, sometimes very contrasting to each other, which paves a way for dual justice or divergence justice, which are different for similar kinds of corporate criminal cases. A judgement with a very narrow majority always gives rise to many questions of law, which if left unanswered might bring a havoc to present corporate criminal justice system of India.

## XIV. CONCLUSION

The doctrine of piercing the corporate veil is not subject to any glittering and beaming line tests. Courts have struggled for years to develop and refine their analysis of these contentions. Nevertheless, each new step brings a separate set of facts and circumstances into the calculation and a disparate verification must be made as to whether the plaintiff has adduced sufficient evidence of control and domination, improper purpose, or use and resulting damage. The decision whether to pierce the corporate veil may be assisted, at least in part, upon the opinion of qualified experts. In particular, expert testimony would be helpful to the jurist in deciding

 [ISSN 2581-5369]

whether the corporation has been adequately sponsored for its intended purpose. Ultimately, the judgment whether to disregard the corporate entity will be based upon a balancing of various factors all or some of which are necessary but may not be sufficient to pierce the veil.

The art of piercing the corporate veil until now remains one of the most controversial subjects in corporate law. There are categories such as fraud, agency, sham or facade, unfairness and group enterprises, which are believed to be the most peculiar basis under which the Law Courts would pierce the corporate veil. But these categories are just guidelines and by no means far from being exhaustive. New criterias are still emerging from time to time and case to case analysis and as the proverb goes "The words of a man's mouth are deep, the wellspring of wisdom is a flowing brook" Basically the true and legitimate intent of jurists and the law makers are the need of the hour to unveil the real transgression and to bring justice within the scope of symmetry.

*****

 [ISSN 2581-5369]

## XV. BIBLIOGRAPHY


1. Mondaq- connecting knowledge and people
2. Vicarious Criminal Liability for Corporate Officers in India: Problems and Prospects by Nigam Nuggehalli
3. Corporate criminal liabilty- An analysis by Soumya Suman Faculty of Law, Jamia Millia Islamia, New Delhi
4. Lifting of corporate veil by Vasundhara Majithia, Yamini Rajora, National Law University Jodhpur
5. Analysis of lifting of corporate veil-Principles of interpretation" By Manish Kumar singh
6. Piercing of corporate veil in case of sale of shares" by Nishith Desai Associates
7. Piercing the Corporate Veil: An Empirical Study by Robert B. Thompson
8. Piercing the Corporate Veil: Historical, Theoretical and Comparative Perspectives- Berkeley Business Law Journal, 140-204 (2019)
9. Piercing of the corporate veil for evasion of tort obligations- Stefan HC
10. Piercing the Corporate Veil: Focusing the Inquiry by Cathy S Krendl & James R Krendl.


*****

 [ISSN 2581-5369]