

## NOTE

### **The Grand Trunk Road from *Salomon* to *Mehta*: Economic Development and Enterprise Liability in India**

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*In traditional corporate law, plaintiffs must rely on the common law doctrine of piercing the corporate veil to hold shareholders responsible for a corporation's liabilities. Courts generally respect the decisions of corporate planners and rarely pierce the veil. But some corporate law scholars have grown frustrated with the traditional doctrine of veil piercing, calling it inadequate in an era where multinational corporations use subsidiaries to shift liabilities to destitute tort victims in Third World countries. As an alternative, scholars have pushed for courts to adopt the doctrine of enterprise liability. Under enterprise liability, plaintiffs can hold a corporate parent responsible for the actions of a sibling or subsidiary corporation that is part of the same overall economic unit without having to meet the rigorous standards of traditional veil piercing.*

*Over the past thirty years, India has broken away from the status quo of traditional veil piercing that still holds sway in the United States and England and has approved of enterprise liability. But only a handful of commentators have discussed this seismic shift in the corporate law landscape. Virtually no scholars have examined how or why Indian courts have adopted enterprise liability in the wake of the Bhopal disaster and whether the doctrine is indeed beneficial for the Indian economy.*

*This omission in legal scholarship is surprising given the intense contemporary corporate law debate over enterprise liability and the increasing importance of India in the global economy. This Note fills this gap in legal scholarship in several ways. First, it charts the law in England and the evolution of the law in India to show how economic and social factors drove Indian courts toward enterprise liability in the aftermath of the Bhopal disaster. Second, it explains how Indian courts have consistently treated veil piercing as an economic policy tool rather than a sacrosanct foundation of corporate law. Finally, this Note shows how the current expansion of enterprise liability beyond cases involving ultrahazardous torts could hurt the country's economic interests. In making this argument, this Note combines Indian and English legal history, corporate law, and economic development scholarship.*

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## INTRODUCTION

*“The ghost of Salomon’s case still visits frequently the hounds of Company Law but the veil has been pierced in many cases.”*<sup>1</sup>

The worst industrial tragedy in world history began during the dead of night in northern India, with the silent leak of poisonous gas.<sup>2</sup> A highly toxic chemical called methyl isocyanate spewed out of a chemical plant owned by Union

1. *State of Uttar Pradesh v. Renuagar*, (1988) 1 S.C.R. Supp. 627, 668 (India).

2. *In re Union Carbide Corp.*, 634 F. Supp. 842, 844 (S.D.N.Y. 1986). The Bhopal disaster is still considered the worst industrial disaster in world history by numerous commentators because of its extraordinary death toll. *See, e.g.*, Tony Long, *Dec. 3, 1984: Bhopal, ‘Worst Industrial Accident in*

Carbide India Limited, a subsidiary of the giant American corporation Union Carbide, over December 2–3, 1984.<sup>3</sup> The prevailing winds blew vast amounts of fumes toward thousands of destitute squatters who lived in adjoining huts in the city of Bhopal.<sup>4</sup> The chemicals killed several thousand people, injured hundreds of thousands more, and devastated local crops and cattle.<sup>5</sup>

The Bhopal disaster drew the world's attention to the Janus-faced role played by multinational corporations that operate through subsidiaries in Third World countries such as India.<sup>6</sup> Union Carbide owned 50.9% of the shares of Union Carbide India Limited,<sup>7</sup> employed Indian managers and workers,<sup>8</sup> and produced pesticides that likely improved agricultural yields in a country with millions of malnourished people.<sup>9</sup> However, the Bhopal accident wrecked thousands of lives, spawned costly litigation across two hemispheres, resulted in \$470 million in damages,<sup>10</sup> and prompted a criminal investigation that has still not been fully resolved.<sup>11</sup> The legal and human costs of the disaster<sup>12</sup> renewed scholarly debate about one of corporate law's most difficult questions: When should a court disregard the corporate form and pierce the corporate veil to hold shareholders directly liable for a corporation's actions?<sup>13</sup>

Answering that question is especially difficult in the case of India because it is a developing country that depends on investments by foreign companies to fuel its rapid economic growth.<sup>14</sup> Fear of excessive liability can deter corporations from doing business in countries like India.<sup>15</sup> Yet giving corporations too much protection from liability encourages them to create subsidiaries that are

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History,' WIRED (Dec. 3, 2008), [http://www.wired.com/science/discoveries/news/2008/12/day\\_intech\\_1203](http://www.wired.com/science/discoveries/news/2008/12/day_intech_1203).

3. *Id.*

4. *Id.*

5. *Id.*

6. See *Bhopal Trial: Eight Convicted Over India Gas Disaster*, BBC NEWS (16:39 GMT, Monday, 7 June 2010), [http://news.bbc.co.uk/2/hi/south\\_asia/8725140.stm](http://news.bbc.co.uk/2/hi/south_asia/8725140.stm).

7. *In re Union Carbide*, 634 F. Supp. at 844.

8. Binda Sahni, *The Interpretation of the Corporate Personality of Transnational Corporations*, 15 WIDENER L. J. 1, 26–28 (2005).

9. See Marc Galanter, *When Legal Worlds Collide: Reflections on Bhopal, the Good Lawyer, and the American Law School*, 36 J. LEGAL EDUC. 292, 298 n.20 (1986).

10. See *Union Carbide Corp. v. Union of India*, (1991) 1 S.C.R. Supp. 251, 253.

11. See *In re Union Carbide*, 634 F. Supp. at 844. As of June 2010, rights groups were still seeking criminal charges against other Union Carbide executives. See *Bhopal Trial*, *supra* note 6. The exact cause of the Bhopal disaster is still somewhat unclear. See *Chronology*, BHOPAL INFO. CTR. (Nov. 2010), <http://www.bhopal.com/chronology>. Both Union Carbide and Indian government investigators determined that a large quantity of water was mistakenly introduced into the wrong tank, triggering a chemical reaction. *Id.* Eight former employees of the Bhopal plant were convicted of criminal negligence. See *Bhopal Trial*, *supra* note 6.

12. See *In re Union Carbide*, 634 F. Supp. at 844–45.

13. "Piercing the corporate veil is the most litigated issue in corporate law . . ." Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036, 1036 (1991).

14. Amadeo M. Di Lodovico, William W. Lewis, Vincent Palmade & Shirish Sankhe, *India—From Emerging to Surging*, MCKINSEY QUARTERLY, Dec. 2001, at 28, 31–32.

15. See *id.* at 30.

undercapitalized and poorly monitored while engaged in ultrahazardous activities, producing more large-scale industrial disasters such as Bhopal.<sup>16</sup>

The debate over how to balance these considerations has intensified in recent years with the push to move from the traditional doctrine of piercing the corporate veil to the new concept of enterprise liability.<sup>17</sup> Under traditional veil-piercing doctrine, courts generally only hold a parent corporation responsible for a subsidiary's liabilities if they find that the parent corporation's wrongful use of its control was the proximate cause of damages.<sup>18</sup> Because that standard is difficult to meet, plaintiffs generally fail to pierce the veil in such cases.<sup>19</sup> However, under enterprise liability, courts only need to find that a parent corporation had control of its subsidiary to hold it responsible for the subsidiary's liabilities; mere majority-share ownership or appointment of the subsidiary's directors, for example, can be enough to produce liability for the parent.<sup>20</sup> Scholars anticipate that this more lenient standard will result in greater accountability for parent corporations that try to use subsidiaries to shift risks to tort victims and other creditors.<sup>21</sup>

This Note will focus on India, where the debate over enterprise liability could have significant consequences because of the country's increasing importance in the world economy and the critical contribution of multinational corporations to that rise.<sup>22</sup> The Supreme Court of India has approved of enterprise liability.<sup>23</sup> However, the exact scope of enterprise liability in India remains unclear.

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16. See Meredith Dearborn, Comment, *Enterprise Liability: Reviewing and Revitalizing Liability for Corporate Groups*, 97 CALIF. L. REV. 195, 197–98 (2009). For the purposes of this Note, I will consider ultrahazardous industries to be generally those performing activities described as “abnormally dangerous” in the *Restatement (Second) of Torts*. The *Restatement (Second) of Torts* describes six factors of abnormally dangerous activities, including a “high degree of risk” of harming people and property and a “likelihood” that the harm from the activity “will be great.” RESTATEMENT (SECOND) OF TORTS § 520 (1977); see also William K. Jones, *Strict Liability for Hazardous Enterprise*, 92 COLUM. L. REV. 1705, 1710 (1992) (describing the *Restatement's* definition of ultrahazardous activities as applying to activities that can cause widespread harm such as the use of atomic energy, large storage of toxic gas, or the manufacture of explosives).

17. See, e.g., Phillip I. Blumberg, *The Corporate Entity in an Era of Multinational Corporations*, 15 DEL. J. CORP. L. 283, 360–64 (1990). Scholars still vigorously debate the contours of enterprise liability. Some scholars call for global regulation of multinational corporations. See, e.g., Sudhir K. Chopra, *Multinational Corporations in the Aftermath of Bhopal: The Need for a New Comprehensive Global Regime for Transnational Corporate Activity*, 29 VAL. U. L. REV. 235, 280 (1994). Others call for a modified version of enterprise liability. E.g., PETER T. MUCHLINSKI, *MULTINATIONAL ENTERPRISES AND THE LAW* 316–319 (2d ed. 2007) (considering the need for a multinational scheme based on a “significant degree of economic and commercial integration across borders”).

18. See generally FREDERICK J. POWELL, *PARENT AND SUBSIDIARY CORPORATIONS* (1931) (detailing the traditional theory).

19. See Thompson, *supra* note 13, at 1056–57.

20. See Blumberg, *supra* note 17, at 328–30.

21. See *id.* at 342.

22. See *India's Surprising Economic Miracle*, *ECONOMIST* (Sept. 30, 2010), available at [http://www.economist.com/node/17147648?story\\_id=17147648&fsrc=rss](http://www.economist.com/node/17147648?story_id=17147648&fsrc=rss) (describing the importance of foreign investment to India's economic boom).

23. See *Mehta v. Union of India*, (1987) 1 S.C.R. 819, 844. Indian courts have also responded by adopting a doctrine of absolute liability for companies engaged in ultrahazardous enterprises. *Id.* MC

By examining the evolution of enterprise liability in India from traditional English veil-piercing law, this Note will show how Indian courts have changed the scope of limited liability to respond to national economic and social concerns. This Note will argue that Indian courts should not adopt a broad theory of enterprise liability because doing so would dissuade foreign investment and hurt economic growth. It will argue that Indian courts should instead adopt a narrow theory of enterprise liability. Under this theory, parent corporations would only be held responsible under enterprise liability for the torts of sibling or subsidiary companies that involve ultrahazardous activities. This narrow theory of enterprise liability would better serve the country's current national economic policy interests.

Part I of this Note will briefly explain the advantages of limited liability, the debate over the effectiveness of piercing the corporate veil, and the recent push for enterprise liability. Part II will examine *Salomon v. Salomon & Co.*<sup>24</sup> and other major English decisions on piercing the corporate veil that provided the original legal foundations for Indian courts. Part III will describe how Indian courts began with a restrictive view of veil-piercing that they inherited from England and why they eventually adopted enterprise liability in the wake of the Bhopal disaster. It will also describe the Indian Supreme Court's decision in *Mehta*, a sort of anti-*Adams v. Cape Industries*<sup>25</sup> and *United States v. Bestfoods*,<sup>26</sup> leading cases in England and the United States where courts rejected enterprise liability. Part IV will explain why Indian courts should only adopt a narrow version of enterprise liability.

### I. LIMITED LIABILITY AND ENTERPRISE LIABILITY

The economic theories that underpin limited liability play an important role in the current legal debate over its future in India.<sup>27</sup> Limited liability has endured as a cornerstone of corporate law because it offers significant benefits to corporate planners and society.<sup>28</sup> The doctrine of piercing the corporate veil has also persisted because it can police the abuse of the corporate form by corporate planners.<sup>29</sup> An overview of the economic theories that justify limited liability will help show the consequences of India's adoption of enterprise liability. This Part of the Note will briefly explain the value of limited liability. Then, it will explain why frustration with the traditional doctrine of piercing the corporate veil has sparked interest in enterprise liability.

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Mehta is generally considered the most prominent Indian environmental lawyer. See MC MEHTA ENVTL. FOUND., <http://mcmef.org/mcmehta.html> (last visited Nov. 27, 2011).

24. [1897] A.C. 22 (H.L.) (appeal taken from Eng.).

25. [1990] 1 Ch. 433 (C.A.) at 544 (Eng.).

26. 524 U.S. 51, 61–64 (1998).

27. See FRANK H. EASTERBROOK & DANIEL R. FISCHER, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* 40–41 (1991).

28. *Id.*

29. *Id.* at 40.

## A. THE ECONOMIC JUSTIFICATIONS FOR LIMITED LIABILITY

Limited liability helps economic growth in three key ways: it encourages investment in businesses by reducing monitoring costs and risks for shareholders, makes markets more liquid, and allows shareholders to diversify their investments more readily.<sup>30</sup>

First, limited liability reduces monitoring costs for shareholders.<sup>31</sup> It allows shareholders to spend fewer resources monitoring their agents who run corporations because it limits shareholder liability to the value of their shares.<sup>32</sup> It also reduces the need for shareholders to monitor each other because only the corporation, and not individual shareholders, will be liable for the claims of creditors on the corporation.<sup>33</sup>

Limited liability also makes markets more liquid. Without limited liability, the value of a share would depend on the finances of the owner of the share since that owner may be liable personally for a firm's debts.<sup>34</sup> But with limited liability, the value of a share only communicates the present value of the income generated by a firm's assets.<sup>35</sup> This easy valuation of shares enabled by limited liability also makes shares more fungible, aiding the takeover market.<sup>36</sup> The possibility of a takeover, rather than excess monitoring by shareholders, motivates managers to improve corporate earnings.<sup>37</sup>

Finally, limited liability allows for investors to diversify more readily. In a world of unlimited liability, investors would be reluctant to invest in numerous businesses because they risk losing their personal assets if any one of those businesses failed.<sup>38</sup> But with limited liability, investors can invest in a range of businesses because doing so reduces their overall risk while increasing their chances of finding especially valuable investments.<sup>39</sup>

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30. *Id.* at 41–42.

31. *Id.* at 42.

32. *Id.* Limited liability also reduces monitoring costs for creditors since they only stand to lose, at most, their investment in a corporation in the event of a bankruptcy. *Id.* at 45–46. Creditors can also contract to further reduce their liability. *Id.* Secured creditors, for example, can choose to monitor only the state of their security rather than the state of the whole firm. *Id.* at 45. However, creditors may have more specialized knowledge of a corporation than shareholders and may be more efficient monitors than widely dispersed shareholders. *Id.* at 46.

33. *Id.* at 41–42. Scholars have also argued that the most important feature of organizational law is not limited liability for shareholders. See Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 *YALE L.J.* 387, 390 (2000). Instead, they argue, asset partitioning is especially valuable because it allows for a corporation to shield its assets from the creditors of its owners and managers. *Id.*

34. EASTERBROOK & FISCHER, *supra* note 27, at 41–42.

35. *Id.*

36. *Id.*

37. *Id.* at 45.

38. *Id.* at 43.

39. *Id.* at 43–44.

## B. PIERCING THE CORPORATE VEIL

“Piercing the corporate veil” is a common law doctrine under which courts can hold shareholders personally responsible for the liabilities of their corporation.<sup>40</sup> In cases where a shareholder uses his control of a corporation to commit fraud or break the law, courts can pierce the corporate veil to hold the shareholder personally liable for the corporation’s debts.<sup>41</sup> Courts have long relied on the three-part test articulated by Frederick Powell in his 1931 book *Parent and Subsidiary Corporations* in deciding whether to pierce the corporate veil.<sup>42</sup> That test looks at the parent’s control over the subsidiary, whether that control was used wrongfully, and whether the wrongful use of that control was the proximate cause of damages.<sup>43</sup> To determine if those three prongs are satisfied, courts look at various factors such as undercapitalization, fraud, and whether the parent and subsidiary companies followed corporate formalities.<sup>44</sup>

However, empirical studies have largely shown that courts remain reluctant to pierce the corporate veil even in cases where scholars would expect courts to do so.<sup>45</sup> For example, legal scholars have argued that it would be more economically justifiable for courts to pierce the corporate veil when a company commits a tort than when it breaks a contract.<sup>46</sup> But a leading veil-piercing study found that courts were willing to pierce in nearly forty-two percent of contract cases and only thirty-one percent of tort cases, suggesting that the opposite of the scholarly consensus was occurring.<sup>47</sup> Moreover, scholars assumed that courts were more likely to pierce to subsidiary corporations controlled by a parent corporation than to pierce to corporations controlled by individual shareholders.<sup>48</sup> However, that assumption has also been undermined by empirical work that found courts pierced to individual shareholders roughly forty-three percent of the time but to corporate parents only about thirty-seven percent of the time.<sup>49</sup> These empirical results show that courts in practice do not appear to follow the theoretical economic analyses of when veil piercing should occur.

## C. THE PUSH FOR ENTERPRISE LIABILITY

This gap between economic theory and legal reality has prompted some scholars to reexamine the traditional doctrine of veil piercing.<sup>50</sup> They argue that

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40. See Robert B. Thompson, *Piercing the Veil Within Corporate Groups: Corporate Shareholders as Mere Investors*, 13 CONN. J. INT’L L. 379, 383 (1999).

41. See *id.*

42. See *id.* at 390.

43. See FREDERICK J. POWELL, *PARENT AND SUBSIDIARY CORPORATIONS* 4–6 (1931).

44. See Thompson, *supra* note 13, at 1070–74.

45. *Id.*

46. See EASTERBROOK & FISCHER, *supra* note 27, at 58–60.

47. See Thompson, *supra* note 13, at 1058 tbl.9.

48. *Id.* at 1056–58.

49. *Id.* at 1055 tbl.7.

50. See Blumberg, *supra* note 17, at 363–65; see also MUCHLINSKI, *supra* note 17, at 317–21 (discussing new approaches to liability).

a corporation that incorporates a poorly capitalized subsidiary company to engage in a hazardous activity should not be completely insulated from the harm caused by the subsidiary.<sup>51</sup> Hansmann and Kraakman have gone so far as to argue that “limited liability in tort cannot be rationalized for either closely-held or publicly-traded corporations.”<sup>52</sup> The reason for this sentiment is that tort victims are involuntary creditors of such corporations.<sup>53</sup> Contract creditors, who are voluntary creditors, have a chance to secure their liabilities against a corporation through bargaining.<sup>54</sup> Tort creditors, on the other hand, are not able to bargain with a corporation before an injury.<sup>55</sup> Thus, if they are injured by a poorly capitalized subsidiary corporation, they would be unlikely to recover any damages for their injuries.<sup>56</sup> This frustration with the perceived inability of traditional entity law and veil-piercing doctrine to protect the interests of tort creditors has prompted renewed interest in enterprise liability.

In his seminal article *The Corporate Entity in an Era of Multinational Corporations*, Phillip Blumberg argued that traditional entity law, which was based on the idea of individual shareholders investing in a corporation, was “outmoded” in a world of “large multinational corporations with hundreds of thousands of public shareholders and corporate structures of ‘incredible complexity.’”<sup>57</sup> These parent corporations were not “passive investor[s].”<sup>58</sup> Instead, Blumberg argued they were “a major part of the enterprise, engaged along with [their] subsidiaries in the collective conduct of a common business under centralized control.”<sup>59</sup> To adapt the law to this new economic reality, Blumberg called for imposing group liability on corporate groups that were part of the same economic enterprise.<sup>60</sup>

Under this type of liability, courts would examine the economic reality of a corporate group rather than just the legal forms put in place by planners.<sup>61</sup> A court that adopted enterprise liability would determine whether a parent corporation had “control” over a sibling or subsidiary corporation.<sup>62</sup> Blumberg assumed that the existence of this control could be found in most corporate groups because a parent corporation usually controls the shares, directors, and officers of a subsidiary.<sup>63</sup> He also argued that, in most cases, the parent would also

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51. See MUCHLINSKI, *supra* note 17, at 314.

52. Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879, 1880 (1991).

53. See EASTERBROOK & FISCHEL, *supra* note 27, at 58–59.

54. *Id.*

55. *Id.*

56. See Thompson, *supra* note 40, at 392.

57. Blumberg, *supra* note 17, at 286–87 (quoting Hadden, *Inside Corporate Groups*, 12 INT’L J. SOC. L. 271, 273–74 (1984)).

58. *Id.* at 327.

59. *Id.*

60. *Id.* at 365–66.

61. *Id.*

62. *Id.* at 329–30.

63. *Id.*

effectively exercise this control by ensuring that the goals of the subsidiary corporation remained subservient to the goals of the parent corporation.<sup>64</sup> If a court found such control existed, the corporate group would have to stand behind all of its constituent companies, and “[g]roup assets would be available to pay group liabilities.”<sup>65</sup> Blumberg expected that enterprise liability would lead courts to disregard the corporate veil in more cases involving parent corporations and subsidiary corporations than under traditional veil-piercing doctrine.<sup>66</sup>

## II. THE ENDURING APPEAL OF THE *SALOMON* RULE

Despite the scholarship calling for broader enterprise liability, English courts have largely stayed true to traditional entity law and veil-piercing theory. To comprehend the legal battle underway in Indian courts, it is important to first analyze the seminal English decisions Indian courts have relied upon in crafting their own theories of piercing the corporate veil. This section of the Note will examine the English cases on limited liability that have influenced Indian courts: *Salomon v. Salomon & Co.*,<sup>67</sup> *DHN Food Distributors Ltd. v. Tower Hamlets London Borough Council*,<sup>68</sup> *Woolfson v. Strathclyde Regional Council*,<sup>69</sup> and *Adams v. Cape Industries*.<sup>70</sup>

### A. *SALOMON V. SALOMON & CO.*

Aron Salomon, the appellant in *Salomon*, was a leather merchant and wholesale boot manufacturer who formed a company named Aron Salomon and Company, Limited.<sup>71</sup> After creating the new company under the Companies Act of 1862, which allowed for limited liability, Salomon sold his business to the company, receiving cash and secured debentures in return.<sup>72</sup> Salomon held 20,001 of the company’s 20,007 shares, and his wife and five children held the remaining six shares.<sup>73</sup> Unfortunately, a series of strikes crippled the company’s finances.<sup>74</sup> When the company could not keep up with its payments, it went into

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64. *Id.* Blumberg anticipated, however, that his test to examine “control” may vary for the case of corporate conglomerates, or groups of unrelated businesses that operated largely independently of each other. *Id.* at 343–44. In such cases, Blumberg said that a test for control may not be sufficient and that a court may have to examine additional factors such as the economic integration of the companies, the administrative independence of the companies, the financial interdependence of the companies, and whether they used a common public persona for the whole group. *Id.* at 344.

65. *Id.* at 366. Commentators since the 1920s have called for some type of enterprise liability, though courts have generally resisted. See Thompson, *supra* note 40, at 390–91.

66. See Blumberg, *supra* note 17, at 286–87.

67. [1897] A.C. 22 (H.L.) (appeal taken from Eng.).

68. [1976] 1 W.L.R. 852 (C.A.) (appeal taken from Eng.).

69. (1978) S.C. 90 (H.L.) (appeal taken from Scot.).

70. [1990] Ch. 433 (C.A.) (appeal taken from Eng.).

71. See *Salomon*, [1897] A.C. at 23.

72. *Id.* at 24–30.

73. *Id.* at 24.

74. *Id.* at 25.

liquidation.<sup>75</sup> The liquidator argued that Salomon should be personally liable for the company's debts to unsecured creditors and that the debentures issued to him by the company were fraudulent.<sup>76</sup>

Two lower courts agreed with the liquidator and held that Salomon should be personally liable for the company's debts to unsecured creditors.<sup>77</sup> The Court of Appeal declared that the Companies Act should not apply to a company that was essentially a sham for one person.<sup>78</sup> But the House of Lords unanimously reversed, holding that nothing in the Companies Act prohibited Salomon from incorporating a business to shield himself from personal liability.<sup>79</sup> Lord Halsbury endorsed a broad reading of respecting the corporate form, stating: "I am simply here dealing with the provisions of the statute, and it seems to me to be essential to the artificial creation that the law should recognise only that artificial existence—quite apart from the motives or conduct of individual corporators."<sup>80</sup> Salomon received the company's assets and was not liable to the company's creditors.<sup>81</sup>

The *Salomon* case came to stand for the principle that courts should treat corporations and other limited liability companies as distinct legal entities even when they existed largely for the purpose of shielding an individual from liability. Not surprisingly, English courts have since rarely pierced the corporate veil, holding shareholders liable for the actions of the limited company only in "unusual circumstances where the controlling shareholders use the corporate form for an illegal or improper purpose."<sup>82</sup> While *Salomon* involved a case of an individual shareholder who incorporated a company to protect himself from liability, English courts went on to apply the *Salomon* holding to parent companies that used subsidiaries to shift risks to creditors.<sup>83</sup>

B. TWO VIEWS OF THE CORPORATE GROUP: *DHN FOOD DISTRIBUTORS* AND  
*WOOLFSON V. STRATHCLYDE REGIONAL COUNCIL*

After *Salomon*, English courts had to determine how to examine corporate groups in veil-piercing cases. Should they treat them as a single economic entity

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75. *Id.* at 24.

76. *Id.* at 24–30.

77. *Id.* at 26.

78. *Id.*

79. *Id.* at 27.

80. *Id.* at 30.

81. *Id.*

82. Sandra K. Miller, *Piercing the Corporate Veil Among Affiliated Companies in the European Community and in the U.S.: A Comparative Analysis of U.S., German, and U.K. Veil-Piercing Approaches*, 36 AM. BUS. L.J. 73, 113 (1998) (footnotes omitted) (citing *Acatos & Hutcheson v. Watson*, [1995] 1 B.C.L.C. 218 (Ch.) (Eng.)). In *Acatos*, the court stated that "English law insists on recognition of the distinct legal personality of companies unless the relevant contract or legislation requires or permits a broad interpretation to be given to references to members of a group of companies or the legal personality is a mere facade or sham or unlawful device." *Acatos*, 1 B.C.L.C. at 218.

83. See, e.g., *Adams v. Cape Indus.*, [1990] Ch. 433 (C.A.) 544 (Eng.); see generally Miller, *supra* note 82, at 108–09.

or as separate legal entities? This section will examine two important cases where English courts took different views on that issue: *DHN Food Distributors Ltd. v. Tower Hamlets London Borough Council*<sup>84</sup> and *Woolfson v. Strathclyde Regional Council*.<sup>85</sup> The two cases are somewhat unusual because they both involve companies trying to use veil piercing to derive an economic benefit from the government rather than rely on limited liability as a shield from creditors, a strategy known as “self-piercing.”<sup>86</sup> However, the English courts did not address the issue of self-piercing in either case.<sup>87</sup> Instead, they decided *DHN* based on the economic reality of the situation<sup>88</sup> and *Woolfson* under a formalistic legal analysis.<sup>89</sup>

The *Salomon* decision did not completely strip the ability of English courts to examine the economic realities of a corporation. In 1976, the Court of Appeal held in *DHN Food Distributors Ltd. v. Tower Hamlets London Borough Council* that a court could ignore the separate legal entities of companies in a group and “look instead at the economic entity of the whole group.”<sup>90</sup> In *DHN*, a parent company called DHN Food Distributors had divided its assets among two wholly-owned subsidiary companies: one subsidiary owned the land and another company owned the vehicles.<sup>91</sup> The directors of DHN, which owned the business itself, also served as the directors of the two subsidiary companies.<sup>92</sup>

The dispute in *DHN* concerned compensation by the government for taking the company’s property for a housing project.<sup>93</sup> The government argued that it was only required to compensate the subsidiary company for the land.<sup>94</sup> However, DHN argued that it should be compensated both for the land and the loss of business because it and the subsidiary that owned the land were inextricably linked.<sup>95</sup> The company, not the government, argued that courts should look at the economic reality of its corporate structure rather than just the legal form.<sup>96</sup>

To determine the amount of compensation DHN deserved, the court examined the economic reality of the situation. The court noted that DHN owned all

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84. [1976] 1 W.L.R. 852 (C.A.) (appeal taken from Eng.).

85. (1978) S.C. 90 (H.L.) (appeal taken from Scot.).

86. As described in this section, both *DHN*, [1976] 1 W.L.R. at 857–58, and *Woolfson*, (1978) S.C. at 94, involved remarkably similar facts about self-piercing. Corporations are generally unsuccessful in arguing for self-piercing. See Thompson, *supra* note 13, at 1048 tbl.1, 1057–58 (explaining that corporations succeed in self-piercing in about one out of eight cases, significantly lower than the 40% piercing rate for all cases in his study). Courts generally dismiss such cases on equitable grounds, telling corporations that they should bear the burdens as well as the advantages of limited liability. *Id.* at 1058.

87. See *DHN*, 1 W.L.R. at 860; *Woolfson*, (1978) S.C. at 96.

88. See *DHN*, 1 W.L.R. at 860.

89. See *Woolfson*, (1978) S.C. at 96.

90. See *DHN*, 1 W.L.R. at 860 (internal quotation marks omitted).

91. *Id.* at 857–58.

92. *Id.*

93. *Id.* at 858.

94. *Id.*

95. *Id.* at 860.

96. *Id.*

of the shares of its subsidiaries, ensuring that “[t]hese subsidiaries are bound hand and foot to the parent company and must do just what the parent company says.”<sup>97</sup> The court then argued that the integration of the three companies in the same business made them “virtually the same as a partnership in which all the three companies are partners.”<sup>98</sup> Because the three companies were all parts of a single economic unit, the court held that DHN should be compensated for the loss of land and business.<sup>99</sup> The court rejected the argument that it should abide by the legal forms that DHN had chosen because doing so would ignore economic substance in favor of “a technical point.”<sup>100</sup>

*DHN* was a surprising result given the fidelity of English courts to *Salomon*.<sup>101</sup> It marked the high point of the willingness of English courts to disregard the legal structures created by a company and examine the economic substance of a corporate group. Going forward, English courts would treat *DHN* as an exception rather than the rule. However, as described in Part III, the case provided an important legal basis for Indian courts searching for ways to hold multinational corporations accountable for the actions of their subsidiaries.

English courts soon distinguished *DHN* rather than follow it. In *Woolfson v. Strathclyde Regional Council*, the House of Lords dealt with a set of facts remarkably similar to *DHN*, another self-piercing case, but came to a different conclusion.<sup>102</sup> The appellant in *Woolfson* owned a bridal clothing company through two different companies, holding the majority of shares in one company and 999 of the 1,000 shares in the other company.<sup>103</sup> The state planned to take property owned by his second company for the construction of a new highway, but it only offered enough money for the taking of the property by the second company rather than the disruption that would result to the entire business.<sup>104</sup> Citing *DHN*, *Woolfson* argued that “the court should set aside the legalistic view . . . and concentrate attention upon the ‘realities’ of the situation.”<sup>105</sup>

But the lower courts rejected that claim.<sup>106</sup> The House of Lords affirmed those rulings, holding that the *Salomon* rule should only be deviated from in cases where a company was “a mere façade.”<sup>107</sup> The court also found that,

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97. *Id.*

98. *Id.*

99. *Id.*

100. *Id.* The court did not comment on the self-piercing nature of the case. *Id.*

101. See Miller, *supra* note 82, at 113.

102. Compare *Woolfson*, (1978) S.C. 90 (H.L.) 95 (appeal taken from Scot.) (denying self-piercing by a corporation seeking compensation in eminent donation), with *DHN*, 1 W.L.R. at 860 (approving self-piercing by a corporation seeking compensation in eminent donation).

103. (1978) S.C. at 94.

104. *Id.*

105. *Id.* at 95. Even though the Court rejected *Woolfson*'s claim, it did not state that it was doing so because it was a self-piercing case; instead, the Court rejected the *DHN* approach of examining whether a corporate group was a “single economic entity.” *Id.*

106. *Id.* at 94.

107. *Id.* at 95.

unlike in *DHN*, Woolfson did not own all of the shares of the company.<sup>108</sup> Even though his wife held only 1 of the 1,000 shares, the court argued that her interest “though a minor one, cannot be completely ignored.”<sup>109</sup>

In *Woolfson*, the House of Lords reaffirmed its adherence to the *Salomon* rule by distinguishing *DHN* from cases where a parent investor or corporation had *complete* economic control over a subsidiary. A single share, held by the controlling investor’s wife, was enough to defeat the presumption of a single economic entity.<sup>110</sup> English courts would adopt the *Woolfson* view, returning to the broad acceptance of limited liability outlined in *Salomon* and declining to push for the *DHN* view of a single economic entity.

### C. THE ENDURANCE OF *SALOMON* IN THE AGE OF MULTINATIONAL CORPORATIONS

After *Woolfson*, English courts remained true to the *Salomon* rule, affirming the decisions of corporate planners to use limited liability as a risk-shifting device. English courts gained a reputation for rarely piercing the corporate veil.<sup>111</sup> Although English courts frequently justified their decisions on grounds of legal formalism,<sup>112</sup> their decisions also suggest that they were aware of the economic consequences of limited liability. These consequences took on a new dimension when companies like Cape Industries incorporated subsidiaries to shield themselves from tort liabilities in other countries.<sup>113</sup>

In *Cape Industries*, the plaintiffs sued two marketing subsidiaries of the English parent corporation, Cape, in a federal district court in Texas.<sup>114</sup> They alleged they had been hurt by asbestos that another subsidiary of Cape had mined in South Africa.<sup>115</sup> Cape settled one suit but did not take any part in a second asbestos suit.<sup>116</sup> Instead, Cape decided to let its subsidiary corporation, which had few assets, absorb any judgments for damages.<sup>117</sup> The plaintiffs then tried to enforce the judgments in England against the parent corporation by arguing that Cape had consented to jurisdiction in America because it was part of the same economic unit as its subsidiary company, and that, in the alternative, English courts should pierce the corporate veil of Cape’s subsidiary to Cape.<sup>118</sup>

The plaintiffs argued that Cape and all of its subsidiary corporations were

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108. *Id.* at 96.

109. *Id.* at 97.

110. *Id.*

111. See Miller, *supra* note 82, at 108–09.

112. See, e.g., *Woolfson*, (1978) S.C. at 96 (rejecting argument of enterprise liability on grounds that parent did not own *all of* subsidiary’s shares).

113. See *Adams v. Cape Indus.*, [1990] 1 Ch. 433 (C.A.) 505–06 (Eng.).

114. *Id.*

115. *Id.*

116. *Id.* at 506–07.

117. *Id.* at 507.

118. *Id.* at 531–32.

essentially one large economic entity akin to the enterprise in *DHN*.<sup>119</sup> Citing the court's focus on economic reality rather than legal formality in *DHN*, they claimed that "where legal technicalities would produce injustice in cases involving members of a group of companies, such technicalities should not be allowed to prevail."<sup>120</sup> But the *Cape Industries* court rejected that argument, as well as the theory of enterprise liability, by reaffirming its commitment to the *Salomon* rule.<sup>121</sup> The court said that English law treated "the creation of subsidiary companies . . . as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities."<sup>122</sup>

The court also rejected the plaintiffs' alternative argument that it should pierce the corporate veil because Cape had created a subsidiary company to avoid liability.<sup>123</sup> The court conceded that the plaintiffs were correct in pointing out that such a ruling meant that "Cape would have the practical benefit of the group's asbestos trade in the United States of America without the risks of tortious liability."<sup>124</sup> Such a result, the court argued, was dictated by the principle of respecting the decisions of corporate planners that had become a cornerstone of English corporate law.<sup>125</sup> The court firmly stated that "the right to use a corporate structure in this manner is inherent in our corporate law."<sup>126</sup>

After *Cape Industries*, English courts consistently rejected enterprise liability.<sup>127</sup> They respected the decisions of corporate planners and did not pierce unless they found evidence of fraud or illegality.<sup>128</sup> The advantage of this approach was that it provided certainty to corporations. United States courts have also adopted a similar view that rejects the enterprise liability theory.<sup>129</sup> The result may be a more dynamic economy but more uncompensated tort victims.<sup>130</sup>

While *Cape Industries* was decided on formal legal grounds, the court's decision could also be justified on grounds of economic self-interest.<sup>131</sup> First, the English economy benefitted because limited liability facilitates corporate risk-taking.<sup>132</sup> For example, corporate planners could use subsidiary companies to invest in risky industries such as asbestos production without having to fear the controlling parent corporation being held responsible for the subsidiary's

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119. *Id.* at 532–34.

120. *Id.* at 536.

121. *Id.*

122. *Id.*

123. *Id.* at 543–44.

124. *Id.* at 544.

125. *See id.*

126. *Id.*

127. *See* Miller, *supra* note 82, at 113.

128. *Id.*

129. *See, e.g.,* United States v. Bestfoods, 524 U.S. 51, 68 (1998).

130. *See* Hansmann & Kraakman, *supra* note 52, at 1879–80.

131. *See* Blumberg, *supra* note 17, at 286–87 (discussing incentives limited liability gives to multinational corporations to engage in risky activities).

132. *See* EASTERBROOK & FISCHER, *supra* note 27, at 58–59.

debts and losses.<sup>133</sup> Second, the English economy did not have to deal with uncompensated tort victims who lived abroad.<sup>134</sup> Other countries had to come up with ways to compensate tort victims who were unable to recover for their injuries from undercapitalized subsidiary corporations.<sup>135</sup> Thus, in the age of multinational corporations, the *Salomon* rule allocated the benefits of limited liability, such as a more dynamic economy, to England, while distributing the disadvantages, such as the costs of caring for tort victims, to residents of other countries. As discussed in the next Part, Third World countries had to accept this Hobson's choice in part because they were desperate for foreign investment that could fuel economic growth.<sup>136</sup>

### III. THE MOVEMENT TOWARD ENTERPRISE LIABILITY IN INDIA

Although India became independent in 1947, it preserved much of the legal system that the English had already established.<sup>137</sup> The Indian Constitution, which came into force in 1950, created a supreme court and system of lower high courts for the country's various states.<sup>138</sup> Indian courts heavily relied on decisions by English courts in crafting their own rulings.<sup>139</sup> This Part of the Note will show how Indian courts have gradually moved toward a theory of enterprise liability in recent years because of economic and cultural changes in the country. First, it will examine the early Indian court cases that stayed true to a limited theory of veil piercing derived from *Salomon*. Then, it will explain how Indian courts moved away from the *Salomon* rule after the Bhopal disaster in *M.C. Mehta v. Union of India*.<sup>140</sup> Finally, by examining cases after Mehta, this Part will show that the full reach of enterprise liability in India remains unclear.

#### A. THE EARLY RELIANCE ON SALOMON

In the early years of independence, Indian courts relied on the *Salomon*

133. See, e.g., *Cape Indus.*, (1990) 1 Ch. at 543–44. Many Third World countries have also adopted a limited liability rule similar to *Salomon* because they remain desperate to attract foreign investment. See Larry Cata Backer, *Multinational Corporations, Transnational Law: The United Nations' Norms on the Responsibilities of Transnational Corporations as a Harbinger of Corporate Social Responsibility in International Law*, 37 COLUM. HUM. RTS. L. REV. 287, 337–38 (2006).

134. See EASTERBROOK & FISCHER, *supra* note 27, at 58–60. However, tort victims in England also faced the same barriers to recovery as tort victims abroad. *Id.* Thus, the *Cape Industries* decision seems to endorse the view that society was better off with a more dynamic economy and more uncompensated tort victims. See *id.*

135. *Id.*

136. See Backer, *supra* note 133, at 288. See generally *infra* section IV.A.

137. *Law: Judicial and Legal Systems of India*, in ENCYCLOPEDIA OF ASIAN HISTORY 413 (Ainslie T. Embree ed., Vol. 2, 1988).

138. *Id.*

139. See, e.g., *State of Uttar Pradesh v. Renuagar* (1988) 1 S.C.R. Supp. 627, 668 (“The ghost of Salomon’s case still visits frequently the hounds of Company Law but the veil has been pierced in many cases.”).

140. (1987) 1 S.C.R. 819.

doctrine and approved veil piercing only in rare cases.<sup>141</sup> Still, Indian courts did not just affirm *Salomon* on formal legal grounds. Instead, they affirmed the *Salomon* doctrine because it served the country's economic and policy interests. First, the Indian Supreme Court cited *Salomon* approvingly when it rejected a self-piercing request by a company in *Tata Engineering & Locomotive Co. v. State of Bihar* in 1964.<sup>142</sup> Then, the court affirmed the *Salomon* doctrine again in 1985 in a case involving the country's desire to attract foreign capital in *Life Insurance Corp. of India v. Escorts Ltd.*<sup>143</sup> Both cases show how the Indian Supreme Court defined the scope of veil piercing on the grounds of economic policy.

In *Tata Engineering*, the petitioner, who manufactured and sold automotive parts in Bihar and other Indian states, wanted standing to challenge tax assessments by the government.<sup>144</sup> However, only individual citizens, and not corporations or other artificial entities, could challenge tax assessments under Article 19 of the Indian Constitution.<sup>145</sup> The petitioner argued that the court should pierce the corporate veil and allow its individual shareholders to have standing to challenge the assessments.<sup>146</sup> Citing *Salomon*, the Supreme Court of India ultimately rejected the claim and held it would not pierce the veil.<sup>147</sup> The court affirmed the *Salomon* rule of limited liability that "the entity of the corporation is entirely separate from that of its shareholders."<sup>148</sup>

Although the court decided *Tata Engineering* on formal legal grounds, its decision also suggested that it was viewing the doctrine of veil piercing through the lens of national economic policy. The court stated that "as a result of the impact of the complexity of economic factors, judicial [sic] decisions have sometimes recognised exceptions to the rule about the juristic personality of the corporation."<sup>149</sup> It also stated that "in course of time these exceptions may grow in number and to meet the requirements of *different economic problems*, the theory about the personality of the corporation may be confined more and more."<sup>150</sup> Thus, the court suggested that the economic policies of the time were not favorable for a corporation trying to use veil piercing as a way to avoid government taxation.

Because *Tata Engineering* was a self-piercing case like *DHN*,<sup>151</sup> the unusual

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141. See Chopra, *supra* note 17, at 245–50.

142. (1964) 6 S.C.R. 885, 898.

143. (1985) 3 S.C.R. Supp. 909, 1008–09.

144. See *Tata Engineering*, 6 S.C.R. at 888–89.

145. *Id.* at 888–89. Article 19 of the Indian Constitution refers to rights enjoyed by "all citizens." See INDIA CONST. art. 19, § 1.

146. See *Tata Engineering*, 6 S.C.R. at 888–89.

147. *Id.* at 898.

148. *Id.*

149. *Id.*

150. *Id.* (emphasis added).

151. See *DHN Food Distribs. Ltd. v. Tower Hamlets London Borough Council*, [1976] 1 W.L. R. 852 (C.A.) 857–58 (appeal taken from Eng.). See generally Thompson, *supra* note 13, at 1057–58

circumstances of the case allowed the court to support both the *Salomon* rule of limited liability and increased state economic control.<sup>152</sup> In the 1960s, when *Tata Engineering* was decided, India recorded only modest economic progress due to overregulation and the adoption of socialist economic policies that discouraged foreign investment.<sup>153</sup> Economists derided this dismal era of economic development as one where the country experienced the “Hindu rate of growth.”<sup>154</sup> Traditionally, limited liability helps corporations by shielding shareholders from creditors.<sup>155</sup> In this case, however, limited liability prohibited a corporation from obtaining a benefit—the right to challenge state taxation in a lawsuit.<sup>156</sup> Thus, the court’s decision to affirm limited liability in *Tata Engineering* was consistent with a national economic policy that tried to increase government regulation over private enterprise.

The Supreme Court of India went on to explicitly justify *Salomon* based on the economic policy goals of the country in *Life Insurance Corp. of India v. Escorts Ltd.*<sup>157</sup> In *Life Insurance Corp.*, the court had to decide how to interpret the Foreign Exchange Act of 1973, a law which encouraged limited foreign investment by allowing foreigners and Indians who lived abroad to purchase small amounts of shares in Indian companies.<sup>158</sup> However, although the Indian government wanted to attract more capital, it also enacted limits on such investment in the Foreign Exchange Act because it feared that too much foreign ownership would “destabilize” Indian companies.<sup>159</sup> A non-resident Indian national, for example, could only own a maximum of one percent of the shares of an Indian company.<sup>160</sup> Swraj Paul, an ambitious Indian-born entrepreneur who lived in England, evaded that government limit by using thirteen different companies to purchase more than one percent of the shares of Escorts Limited.<sup>161</sup> When Paul and other investors tried to replace nine directors of Escorts Limited, the company argued that Paul’s ownership of its shares was illegiti-

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(describing how courts generally dismiss self-piercing cases on equitable grounds by holding that corporations should bear the burdens as well as the advantages of limited liability). In *Tata Engineering*, the court did not discuss the potential equitable issues involved in approving the self-piercing request. See 6 S.C.R. at 898.

152. See *Tata Engineering*, 6 S.C.R. at 898.

153. Gurcharan Das, *The India Model*, FOREIGN AFFAIRS, July–Aug. 2006, at 4.

154. *Id.*

155. See *supra* section II.A (discussing advantages of limited liability).

156. See *Tata Engineering*, 6 S.C.R. at 898–99.

157. (1985) 3 S.C.R. Supp. 909.

158. *Id.* at 938–40. Non-residents of Indian nationality or origin who lived abroad could purchase larger amounts of shares with less regulatory scrutiny than could foreigners under revised rules to the Act adopted by the Indian government in 1982. *Id.* at 940–41.

159. *Id.* at 945.

160. *Id.* at 940.

161. *Id.* The court did not specify the total percentage of shares Paul held but suggests that it was between one percent and five percent. *Id.* Swraj Paul was a non-resident of Indian nationality or origin, or Indian who lived abroad. *Id.* He was a highly successful entrepreneur and steel-industry magnate in England, founding the Caparo Group, and went on to obtain a knighthood and become the first person of Indian origin to be appointed Deputy Speaker of the House of Lords. See *U.K. Deputy Speaker is*

mate because he had used corporations under his control to evade the statutory limit on the percentage of shares he could have bought as a lone investor.<sup>162</sup> As the court put it, the company argued that “one had only to pierce the corporate veil to discover Mr. Swraj Paul lurking behind.”<sup>163</sup>

The court analyzed the case by trying to determine which interpretation of the statutory limits on foreign ownership would best address the economic interests of the country.<sup>164</sup> First, the court pointed out that “India needs foreign exchange and, lots of it, to meet the demands of its developmental activities.”<sup>165</sup> This need for foreign capital, the court reasoned, was best served by encouraging foreign investment under the *Salomon* rule of respecting corporate entities—even if investors used different corporations to maximize the total percentage of shares they could purchase and evade the limit in the text of the statute.<sup>166</sup> Stressing the importance of supporting a “national economic interest” in attracting foreign capital, the court rejected the argument that it should pierce the corporate veil.<sup>167</sup> The court held that Paul could avoid the statute’s “one percent” limit by establishing corporate entities to buy shares, because allowing him to do so would encourage foreign investment, which was a more valuable national economic interest than providing maximum protection from corporate control battles for Indian companies.<sup>168</sup>

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*Indian-Born*, BBC NEWS (17:28 GMT, Wednesday, 10 December 2008), at [http://news.bbc.co.uk/2/hi/south\\_asia/7776220.stm](http://news.bbc.co.uk/2/hi/south_asia/7776220.stm). He is now Lord Paul. *Id.*

162. *Life Insurance Corp.*, 3 S.C.R. Supp. at 964–66. Escorts Limited was engaged in a complicated battle in which it was trying to prevent Paul’s Caparo Group, Life Insurance Corp., and other financial institutions from replacing nine of its directors at a special meeting. *Id.* at 973–78.

163. *Id.* at 1006.

164. *Id.* at 1008. The court stated that its statutory interpretation of the investment limits was based on its understanding of national economic policy: “When construing statutes enacted in the national interest, the Courts must necessarily take the broad factual situations contemplated by the Act and interpret its provisions so as to advance and not to thwart the particular national interest whose advancement is proposed by the legislation. *Traditional norms of statutory interpretation must yield to broader notions of the national interest.*” *Id.* at 927 (emphasis added).

165. *Id.* at 931.

166. *Id.* at 1008. A company in which at least sixty percent of the shares were owned by non-resident Indians could also purchase up to one percent of the shares of an Indian company under the Act. *Id.* at 1005.

167. The court also held that it was possible to “lift the corporate veil” for informational purposes to determine if non-resident Indians owned at least sixty percent of the shares of companies they used to make investments. *Id.* at 1008. However, the Court held that this “lifting” was only available to learn the nationalities of investors to ensure compliance with Indian law, not their identities. *Id.* Thus, this allowance of “lifting” was very limited and did nothing to hinder investors like Paul who could easily establish multiple corporations and own at least sixty percent of the shares in all of them. *See supra* note 166 and accompanying text. Paul purchased shares in the thirteen companies he used to buy a stake in Escorts Limited through his company The Caparo Group; 61.6% of the shares of Caparo Group Limited were held by the Swraj Paul Family Trust, whose beneficiaries were Swraj Paul and family members, all of whom were non-resident Indians. *Id.* at 945.

168. *Id.* at 1008. The Indian Supreme Court noted that another provision in the Act prohibited “any single foreign investor or a combination of foreign investors” from owning more than five percent of the shares of a company. *Id.* at 1008–09. Paul’s use of corporations to buy shares thus allowed him to own more than one percent but less than five percent of the shares in the company. *Id.* However, his

By the time the Indian Supreme Court decided *Life Insurance Corp.* in 1985, the economic policies of the country had significantly changed from the strict state controls of the 1950s and 1960s. Frustrated by decades of lackluster growth, the country began scaling back the infamous “Permit Raj,” a labyrinthine government bureaucracy that frustrated entrepreneurs by requiring them to obtain numerous permits to conduct even simple business transactions.<sup>169</sup> The increased acceptance of foreign investors in *Life Insurance Corp.* was representative of the country’s emerging economic policy of aiding private enterprise.<sup>170</sup> Adhering to the *Salomon* rule had served the state economic interest of increased government regulation in the 1960s when the court decided *Tata Engineering*.<sup>171</sup> Now, the *Salomon* rule encouraged the new economic interest of increased foreign investment by allowing an entrepreneur to avoid government regulation.<sup>172</sup> In the years to come, the *Salomon* doctrine would open up traditional advantages of limited liability such as shielding shareholders from a corporation’s liabilities.<sup>173</sup> This approach encouraged the growth of multinational corporations in India.<sup>174</sup> It also set the stage for new concerns in the age of ultrahazardous torts.

#### B. THE BHOPAL DISASTER AND THE MEHTA DOCTRINE

Although some scholars have long criticized the ability of corporations to use limited liability to shift risks to tort creditors, a new wave of scholarly criticism emerged in the era of ultrahazardous mass torts.<sup>175</sup> After the Bhopal disaster in 1984, Indian courts similarly began to question the *Salomon* doctrine and turned toward enterprise liability.<sup>176</sup> The massive financial and human costs of ultrahazardous torts led Indian courts to declare that enterprise liability better served the country’s economic policy goals than the *Salomon* rule.

When poison gas leaked from Union Carbide’s Bhopal plant and killed thousands of poor villagers, a massive public outcry erupted.<sup>177</sup> The spill was

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ability to own the additional shares was critical in the corporate control battle because Paul and other financial institutions owned a total of 52% of the shares of Escorts Limited, giving them just enough power to win any director election. *Id.* at 1010–11.

169. See Das, *supra* note 153, at 4–5. The chairman of the Indian company Infosys said that it took the company “about 12 to 24 months and about 50 visits to Delhi to get a license to import a computer worth \$1,500” at the height of the Permit Raj. *The Commanding Heights*, (PBS television broadcast May 22, 2003), transcript available at [http://www.pbs.org/wgbh/commandingheights/shared/minitextlo/tr\\_show02.html#4](http://www.pbs.org/wgbh/commandingheights/shared/minitextlo/tr_show02.html#4).

170. See Das, *supra* note 153, at 4–6 (explaining that the government’s attitude toward the private sector began to change in the 1980s, nearly doubling the rate of growth).

171. See *Tata Eng’g & Locomotive Co. v. State of Bihar*, (1964) 6 S.C.R. 885.

172. See *Life Insurance Corp.*, 3 S.C.R. Supp. at 1008–09.

173. See EASTERBROOK & FISCHER, *supra* note 27, at 58–60.

174. See Chopra, *supra* note 17, at 246–49.

175. See, e.g., Hansmann & Kraakman, *supra* note 52, at 1880–81.

176. See Dearborn, *supra* note 16, at 228–29 (discussing the effect of the *Mehta* decision in India).

177. See *In re Union Carbide Corp.*, 634 F. Supp. 842, 844 (S.D.N.Y. 1986).

considered “the most tragic industrial disaster in history.”<sup>178</sup> Union Carbide India Limited only had \$20 million in assets at the time of the Bhopal spill.<sup>179</sup> However, its parent corporation Union Carbide had assets of \$6.5 billion and insurance protection of \$200 million.<sup>180</sup> The Indian government’s legal battle to obtain restitution for the families of the thousands of the dead and injured provoked widespread anger in India.<sup>181</sup>

Union Carbide contested jurisdiction in India, saying it only owned shares in the subsidiary that operated the plant and had no other connections to the forum.<sup>182</sup> The Indian government responded by suing Union Carbide on behalf of the victims in the Southern District of New York so it could obtain an enforceable judgment against the parent company in the United States.<sup>183</sup> The U.S. court was not receptive to the proposal to preside over the case and dismissed it in 1986 based on forum non conveniens.<sup>184</sup> Still, the U.S. court conditioned its dismissal on the grounds that Union Carbide had to submit to the jurisdiction of Indian courts.<sup>185</sup> Union Carbide accepted the decision but continued to fight other aspects of the case in the Indian court system for years.<sup>186</sup>

In 1987, as the legal battle over damages from Bhopal still raged in India, the Supreme Court of India decided another case involving an ultrahazardous tort in *M.C. Mehta v. Union of India*.<sup>187</sup> The *Mehta* case involved a 1985 leak of poisonous oleum gas from a chlorine plant in Delhi that resulted in 340 injuries and one fatality; the plant was owned by a company called Shriram, a subsidiary of Delhi Cloth Mills Limited.<sup>188</sup>

The Supreme Court took on the case at an intermediate stage to clarify novel legal issues.<sup>189</sup> In its decision, the Supreme Court laid out several important principles. First, it adopted a new doctrine of absolute liability for companies engaged in ultrahazardous activities.<sup>190</sup> Second, the court said that damages should be proportional not just to the size of the harm, but also to the size of the

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178. *Id.*

179. *See Sahni, supra* note 8, at 26.

180. *Id.*

181. *See, e.g., Marc Galanter, Legal Torpor: Why So Little Has Happened in India*, 20 *TEX. INT’L L.J.* 273, 280–81 (1985).

182. *In re Union Carbide Corp.*, 634 F. Supp. at 863–67.

183. *See id.*

184. *Id.* at 867.

185. *Id.*

186. *See infra* notes 199–213 and accompanying text.

187. (1987) 1 S.C.R. 819.

188. *Id.* at 826.

189. *Id.*

190. *See id.* at 843. The court did not specify the exact amount of damages that the enterprise should pay or examine the issue of whether Delhi Cloth Mills Limited “controlled” Shriram for the purposes of enterprise liability. *Id.* at 844. Instead, the court remanded the case so a legal aid board could determine the total number of people who may have claims against Shriram; it also did not address the question of how to apply its new holding that the entire “enterprise” should be absolutely liable for an ultrahazardous tort. *Id.* at 844–45.

*enterprise* that committed the harm so they would have a deterrent effect.<sup>191</sup> Finally, the court suggested that it was also adopting a theory of enterprise liability under which the entire economic unit, or “enterprise,” that controlled the plant could be held liable.<sup>192</sup> The court stated:

We are of the view that *an enterprise* which is engaged in a hazardous or inherently dangerous industry which poses a potential threat to the health and safety of the persons working in the factory and residing in the surrounding areas owes an absolute and nondelegable duty to the community to ensure that no harm results to anyone on account of hazardous or inherently dangerous nature of the activity which it has undertaken.<sup>193</sup>

The court said it was adopting these broader theories of liability in response to the economic changes sweeping the country.<sup>194</sup> As the country developed new industries, including ultrahazardous ones, the court argued that the law should “evolve new principles and lay down new norms [w]hich would adequately deal with the new problems which arise in a highly industrialised economy.”<sup>195</sup> However, the *Mehta* decision left some room for interpretation. The court’s holding was unclear as to whether it was embracing enterprise liability in all cases or just in cases of companies responsible for ultrahazardous torts. That ambiguity has produced some discord among legal scholars and lower courts on the reach of the *Mehta* decision.<sup>196</sup> The court did not discuss *Salomon* in its opinion.<sup>197</sup>

The *Mehta* case had enormous ramifications in the Indian courts. In 1988, in *Union Carbide Corp. v. Union of India*,<sup>198</sup> the Madhya Pradesh High Court cited the *Mehta* decision in examining whether Union Carbide was liable for the actions of its subsidiary corporation Union Carbide India Limited.<sup>199</sup> In the case, Union Carbide argued that it was only a shareholder that “did not exercise control over any action” of its subsidiary corporation, Union Carbide India Limited, which owned and operated the Bhopal plant.<sup>200</sup> It also claimed that the court could not pierce the corporate veil unless it found that “the corporation

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191. *Id.* at 844.

192. *Id.* at 843.

193. *Id.* (emphasis added).

194. *Id.*

195. *Id.*

196. See MUCHLINSKI, *supra* note 17, at 315–16. Although the *Mehta* doctrine in Indian law often refers to the principle of absolute liability in ultrahazardous torts, the case is also widely recognized for introducing the Indian supreme court’s approval of enterprise liability. *Id.* at 314.

197. See *Mehta*, (1987) 1 S.C.R. 819.

198. *Union Carbide Corp. v. Union of India*, Civil Revision No. 26, (1988), Madhya Pradesh H.C., reprinted in UPENDRA BAXI & AMITA DHANDA, VALIANT VICTIMS AND LETHAL LITIGATION: THE BHOPAL CASE 332 (1990) [hereinafter *Union Carbide Civil Revision*].

199. *Id.* at 373–75.

200. *Id.* at 348–49.

has been set up to evade or defraud government revenue or shareholders.”<sup>201</sup>

The Madhya Pradesh High Court did not apply a traditional veil piercing analysis<sup>202</sup> to examine whether Union Carbide had wrongfully used its control of a subsidiary to commit harm.<sup>203</sup> Instead, Judge Seth stated that Indian courts had long held that the scope of limited liability and veil piercing had to adapt to economic changes in the modern world, such as “a mass disaster and in which on the face of it the assets of the alleged subsidiary company are utterly insufficient to meet the just claims of multitude of disaster victims.”<sup>204</sup> Therefore, the court examined the case under the doctrine of enterprise liability.<sup>205</sup> It noted that Union Carbide held the majority of shares in its subsidiary, Union Carbide India Limited.<sup>206</sup> The court then stated that majority share ownership meant that Union Carbide not only “controlled the composition of the Board of Directors of the Indian company but also had full control over the management of the Indian company.”<sup>207</sup>

The court also argued that it was irrelevant whether Union Carbide actively managed the affairs of Union Carbide India Limited.<sup>208</sup> Majority share ownership, the court reasoned, was sufficient for a parent corporation to “control” a subsidiary.<sup>209</sup> Because Union Carbide owned a majority of Union Carbide India Limited’s shares, the court held that it had sufficient control over its subsidiary to be held liable for the Bhopal disaster under the *Mehta* doctrine.<sup>210</sup> The Madhya Pradesh High Court’s decision was widely considered an affirmation of enterprise liability; majority share ownership was now enough to deem that a parent had enough “control” over a subsidiary to be held responsible for a mass tort.<sup>211</sup> After the decision, Union Carbide quickly agreed to a \$470 million

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201. *Id.* at 349.

202. *See supra* notes 40–44 and accompanying text.

203. Union Carbide Civil Revision, *supra* note 198, at 378–79.

204. *Id.* The court cited language in *Tata Engineering, Life Insurance Corp.* and *DHN* to support its argument that courts should adapt their doctrines of limited liability and veil piercing to the economic needs of the country. *Id.* at 378. The court also said that “much water has flown down the Ganges since it was first held in *Saloman v. Saloman and Company* [sic] (1897 A.C. 22) as an absolute principle that a corporation or company has a legal and separate entity of its own.” *Id.* As explained previously, Union Carbide India Limited only had \$20 million in assets at the time of the Bhopal spill. However, its parent corporation Union Carbide had assets of \$6.5 billion and insurance protection of \$200 million. *See Sahni, supra* note 8, at 26.

205. Union Carbide Civil Revision, *supra* note 198, at 379.

206. *Id.*

207. *Id.* Union Carbide held 50.9% of the shares of Union Carbide India Limited. *Id.* at 348.

208. *Id.* at 379 (“If, as alleged by the defendant-UCC, it chose to follow the policy of keeping itself at arms length from the Indian company in certain respects, it was entirely its choice and such policy could not absolve it from its liability.”). Union Carbide’s corporate policy manual stated that it was “the general policy of the Corporation to secure and maintain effective control of an Affiliate.” *See Sahni, supra* note 8, at 27.

209. *See* Union Carbide Civil Revision, *supra* note 198, at 378–79.

210. *Id.*

211. *See* MUCHLINSKI, *supra* note 17, at 315. While the court’s finding of control also turned on a finding that the parent retained control over the subsidiary’s board and management, *see* Union Carbide

settlement that was later upheld by the Supreme Court of India.<sup>212</sup>

In 1996, the Supreme Court of India reconsidered the *Mehta* doctrine in another case involving ultrahazardous torts committed by a corporate group. In *Indian-Council for Enviro-Legal Action v. Union of India*, the Supreme Court reaffirmed its decision in *Mehta* without clarifying it.<sup>213</sup> In *Enviro-Legal Action*, a group of affiliated companies in the village of Bichri operated various chemical plants where they produced toxic chemicals.<sup>214</sup> All of the plants and companies were “controlled by the same group of individuals”<sup>215</sup> and had a common president.<sup>216</sup> Toxic chemicals from the plants leaked and polluted the soil and waters, devastating the local agricultural economy.<sup>217</sup> Citing the *Mehta* doctrine, the court held that all of the affiliated companies were “absolutely liable to compensate for the harm caused by them to villagers in the affected area, to the soil and to the underground water.”<sup>218</sup> The court stated again that “[i]t is that the *enterprise* [carrying on the hazardous or inherently dangerous activity] *alone* has the resource to discover and guard against hazards or dangers.”<sup>219</sup>

While the Court did not define the scope of enterprise liability in *Enviro-Legal Action*, it applied the doctrine with limited analysis. Common ownership and management of the various chemical companies was enough to hold all of them liable for the pollution.<sup>220</sup> Moreover, the court stressed its concerns with the costs of rapid economic growth. It criticized the “contempt for law and lawful authorities on the part of some among the emerging breed of entrepreneurs, taking advantage, as they do, of the country’s need for industrialization and export earnings.”<sup>221</sup> The court’s stringent language and quick application of enterprise liability suggests that it was committed to adapting the law to meet the challenges of industrialization and economic change.

Without enterprise liability, the victims of the Bhopal spill would most likely not have been able to receive any payments for damages.<sup>222</sup> Also, Union Carbide would have little additional incentive to better monitor new subsidiaries

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Civil Revision at 378–79, as a practical matter, those findings essentially followed automatically from the finding of majority share ownership.

212. See *Union Carbide Corp. v. Union of India*, (1991) 1 S.C.R. Supp. 251, 253. Given that the Union Carbide settlement was finalized seven years after the accident, the protracted legal struggle frustrated many contemporaneous observers. See, e.g., Galanter, *supra* note 181, at 275–80.

213. (1996) 3 S.C.C. 212 (India).

214. *Id.* at 2.

215. *Id.*

216. *Id.* at 5.

217. *Id.* at 4–5.

218. *Id.* at 38.

219. *Id.* (second alteration in original) (emphasis added). The court did not specify the total amount of the liability the enterprise faced in its decision. *Id.*

220. *Id.* at 2, 38.

221. *Id.* at 1.

222. See MUCHLINSKI, *supra* note 17, at 322 (noting that victims of ultrahazardous torts in Third World countries are often uninsured).

it incorporates to carry out other dangerous activities.<sup>223</sup> However, with enterprise liability, companies that committed ultrahazardous torts could no longer use limited liability to shift risks to tort victims.<sup>224</sup> This adoption of enterprise liability in the wake of Bhopal by the Indian courts indicates that they began viewing the traditional doctrines of limited liability and veil piercing as insufficient to deal with the modern world of ultrahazardous industries and mass torts.<sup>225</sup> The rhetoric used by Indian judges also shows their increasing suspicion of multinational companies that used subsidiaries to shift risk to destitute Indians.<sup>226</sup> In the past, Indian courts had affirmed the *Salomon* rule because it was consistent with national economic policies.<sup>227</sup> Now, they moved away from the *Salomon* rule, finding it inadequate for the economic challenge of policing corporations that used the corporate form to shift the liabilities of ultrahazardous torts to victims.

C. AFTER *MEHTA*: DEFINING THE SCOPE OF ENTERPRISE LIABILITY IN INDIA

The exact scope of enterprise liability in India remains somewhat unclear. The Indian Supreme Court has not clarified the extent of enterprise liability since its decision in *Indian-Council Enviro-Legal Action v. Union of India*. However, the Indian Supreme Court and other Indian courts have applied enterprise liability, instead of traditional veil piercing, to cases that do not involve ultrahazardous torts. These cases suggest that Indian courts believe in a broad application of enterprise liability.

The Supreme Court of India first suggested its openness to expanding enterprise liability beyond ultrahazardous torts in *State of Uttar Pradesh v. Renusagar*.<sup>228</sup> Renusagar, a wholly owned subsidiary of Hindalco, wanted to be treated as part of the same economic entity so Hindalco could pay a lower duty rate for electricity.<sup>229</sup> But the local government considered it as a separate legal entity from Hindalco, producing a higher duty rate under the law.<sup>230</sup> In evaluating the issue, the Supreme Court of India first explained that “the concept of lifting the corporate veil is a changing concept and is of expanding horizons.”<sup>231</sup> It then declared that Renusagar was wholly owned and “completely controlled” by

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223. *Id.*

224. *Id.* at 316–19.

225. *See* M.C. Mehta v. Union of India, 1 S.C.R. 819, 843 (1987) (arguing that the law should “evolve new principles and lay down new norms [w]hich would adequately deal with the new problems which arise in a highly industrialised [sic] economy”).

226. *See, e.g., Enviro-Legal Action*, 3 S.C.C. at 1 (criticizing the “contempt for law and lawful authorities on the part of some among the emerging breed of entrepreneurs, taking advantage, as they do, of the country’s need for industrialization and export earnings”).

227. *See supra* section III.A.

228. *See* (1988) 1 S.C.R. 627, 629–30 (explaining that “Hindalco and Renusagar [should] be treated as one concern . . . [making both] liable to duty on that basis”).

229. *Id.* at 628–30.

230. *Id.* at 629.

231. *Id.* at 630.

Hindalco to such an extent that “Renusagar had in reality no separate and independent existence apart from and independent of Hindalco.”<sup>232</sup> Thus, even though it faced a set of facts remarkably similar to *Tata Engineering*, the court held that “the corporate veil should be lifted and Hindalco and Renusagar be treated as one concern.”<sup>233</sup> The court’s decision meant that Hindalco could pay a lower rate for electricity.<sup>234</sup>

The court’s analysis looked at the economic reality of the situation rather than just accepting the legal forms originally created by planners.<sup>235</sup> The *Salomon* rule, the court seemed to suggest, was somewhat outdated.<sup>236</sup> Finally, the court stated that when it came to lifting or piercing the corporate veil, the “frontiers are unlimited.”<sup>237</sup>

Lower courts have also adapted enterprise liability to situations that do not involve ultrahazardous industries or mass torts. In *Novartis Ag v. Adarsh Pharmaceuticals*, for example, the Madras High Court used enterprise liability to resolve a patent and marketing battle.<sup>238</sup> Novartis, a Swiss pharmaceutical company, was fighting with another company over the patent and marketing rights to a new drug in India.<sup>239</sup> Novartis had obtained the rights to make and sell the drug in other countries, such as Australia, but Adarsh claimed that Novartis did not have the rights to make and sell the drug in India through its subsidiary.<sup>240</sup> Adarsh argued that each company was “a separate legal entity.”<sup>241</sup> However, the court turned to enterprise liability, reasoning that “it is clear that the concept of a single economic unit is an accepted position in law.”<sup>242</sup> The court stated that Novartis owned 50.93% of the shares of its subsidiary.<sup>243</sup> Then, the court held that Novartis owned the rights to the drug in India because its majority share ownership was sufficient for it to be considered part of the same economic unit as its subsidiary.<sup>244</sup>

The decisions in *Renusagar* and *Novartis* demonstrate how Indian courts are expanding enterprise liability to a variety of contexts rather than just limiting it to the area of ultrahazardous torts. Both cases involved parent companies trying

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232. *Id.*

233. *Id.* at 629. The court did not mention *Tata Engineering* in its decision, nor did it comment on the self-piercing nature of the case. Instead, it delved into analyzing the situation through enterprise liability. *Id.*

234. *Id.* at 630.

235. *Id.* at 629–30.

236. *See id.* (“The veil of corporate personality even though not lifted sometimes is becoming more and more transparent in modern company jurisprudence. The ghost of [Salomon’s case] still visits frequently the hounds of Company Law but the veil has been pierced in many cases.”) (internal citation omitted).

237. *Id.* at 629.

238. (2004) 3 C.T.C. 95, ¶ 14, available at <http://indiankanoon.org/doc/1454766>.

239. *Id.* ¶ 2–4.

240. *Id.* ¶ 3.

241. *Id.* ¶ 5.

242. *Id.* ¶ 13. The court cited *DHN* and *Renusagar* for support. *Id.*

243. *Id.*

244. *Id.* ¶ 14.

to use enterprise liability to their advantage in self-piercing situations, and the courts in both cases approved of piercing through the use of enterprise liability.<sup>245</sup> Those decisions, along with recent legal scholarship,<sup>246</sup> show that Indian courts are accepting a broad view of enterprise liability that applies to a variety of situations rather than only ultrahazardous torts.

Moreover, Indian courts appear to require little to trigger enterprise liability other than a parent company's ownership of a majority of a subsidiary's shares.<sup>247</sup> This bar for control is very low and relatively easy for plaintiffs to meet.<sup>248</sup> It appears that a plaintiff needs to do little more than demonstrate that a parent corporation owns more than fifty percent of a subsidiary's shares for a court to apply enterprise liability in India.<sup>249</sup> However, although enterprise liability seems to have broad reach in India, it is unclear whether the current expansive application of enterprise liability is beneficial for the country's economic policies.

#### IV. THE DANGERS OF ENTERPRISE LIABILITY

The previous Part of this Note explained how Indian courts have examined limited liability, veil piercing, and enterprise liability based on the economic policy goals of the country. This Part will explain why the country's economic policy goals would be best served if courts restricted enterprise liability to corporations engaged in ultrahazardous activities. First, it will argue that a broad expansion of limited liability will provide minimal benefits because the country still has a notoriously inefficient and backlogged court system. Then, it will argue that the costs of expanding enterprise liability too broadly are high because such expansion could drive away industrial investment that the country needs to fuel rapid economic growth.

##### A. THE DEFICIENCIES OF THE INDIAN LEGAL SYSTEM

Scholars have argued for the adoption of some form of enterprise liability since at least the 1920s.<sup>250</sup> But the recent push for enterprise liability has come in the modern age of multinational corporations and ultrahazardous torts.<sup>251</sup> Scholars have been most likely to advocate for eliminating limited liability in tort cases—especially ultrahazardous mass tort cases—because the massive

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245. See (1988) 1 S.C.R. at 628–30; *Novartis*, (2004) 3 C.T.C. 95 ¶ 4.

246. See Dearborn, *supra* note 16, at 228–29 (discussing the expansion of enterprise liability in India after the Union Carbide disaster).

247. See, e.g., *Novartis*, (2004) 3 C.T.C. 95 ¶ 14 (holding that Novartis's majority share in its subsidiary triggers enterprise liability, which also allows Novartis to sell the pharmaceutical in India based on the subsidiary's patent).

248. See *supra* text accompanying notes 230–46.

249. See, e.g., *Novartis*, (2004) 3 C.T.C. 95 ¶ 13–14.

250. See Thompson, *supra* note 40, at 390–91 (discussing the courts' resistance to enterprise liability despite scholars' endorsement).

251. Hansmann & Kraakman, *supra* note 52, at 1880–81.

human and financial costs make the advantages of limited liability difficult to justify.<sup>252</sup> It is not surprising that the Supreme Court of India approved of enterprise liability in the *Mehta* decision while outrage over the Union Carbide disaster was still fresh.<sup>253</sup> One scholar even suggested that the court outlined such a harsh theory of liability in *Mehta* expressly so other courts could use it against Union Carbide in the ongoing Bhopal litigation.<sup>254</sup> Without enterprise liability, victims of the Bhopal spill would not have been able to collect much money from Union Carbide India Limited, the subsidiary corporation of Union Carbide. Even traditional veil piercing may have been of little use since there was no indication of fraud or other intentional wrongdoing by Union Carbide.<sup>255</sup> The Bhopal litigation shows how enterprise liability can prevent corporations from shifting the risks of ultrahazardous torts to destitute creditors.

However, the Bhopal litigation also demonstrated one of the great deficiencies of the Indian court system: its extraordinary sloth. The Bhopal disaster happened in 1984.<sup>256</sup> It was considered the worst industrial disaster in world history at that time.<sup>257</sup> Yet, it still took the Indian court system *seven years* to approve a \$470 million settlement with Union Carbide.<sup>258</sup> Although the case ultimately produced a large financial judgment against Union Carbide, it also demonstrates a major disadvantage of the Indian legal system that makes financial recovery difficult and expensive for tort victims.

India has a strikingly underdeveloped and underutilized tort law. One survey of cases in the *All India Reporter*, the Indian equivalent of Westlaw, only uncovered fifty-six non-motor-vehicle tort cases in the entire country between 1975 and 1984.<sup>259</sup> Many of these cases did not involve complicated facts.<sup>260</sup> The most common scenarios involved downed electrical lines and railway crossings.<sup>261</sup> Still, the backlog in Indian courts meant that cases took an average of twelve years to resolve, a lengthy period of time for matters that generally did not involve difficult legal or factual issues.<sup>262</sup> During the Union Carbide litigation, the Indian government itself argued that U.S. courts should hear the case because few tort victims were able to obtain any meaningful relief due to the inadequate Indian judicial system.<sup>263</sup>

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252. *See, e.g., id.* at 1882–83.

253. *See* M.C. Mehta v. Union of India, (1987) 1 S.C.R. 819, 844.

254. Marc Galanter, *Law's Elusive Promise: Learning from Bhopal*, in *TRANSNATIONAL LEGAL PROCESSES* 172, 179 (Michael Likosky ed., 2002).

255. *See* Thompson, *supra* note 13, at 1070–74 (discussing what a party must show to overcome a presumption of limited liability).

256. *In re* Union Carbide Corp., 634 F. Supp. 842, 844 (S.D.N.Y. 1996).

257. *Id.*

258. *See* Union Carbide Corp. v. Union of India, (1991) 1 S.C.R. 251, 252–53 (explaining that a settlement was not reached until 1989).

259. Galanter, *supra* note 9, at 296.

260. *Id.*

261. *Id.*

262. *Id.*

263. *In re* Union Carbide Corp., 634 F. Supp. 842, 847–49 (S.D.N.Y. 1986).

The Indian government could push for a resolution to major tort cases as it did in the case of the Bhopal disaster.<sup>264</sup> Still, the Indian government would presumably not expend such resources to expedite many relatively minor tort claims. And, if the Indian legal system delays relief for even minor torts for years, then enterprise liability will likely produce minimal benefits for tort victims by the time the cases are finally resolved.

In addition, although torts can occur in any industry, mass torts like Bhopal that result in large death tolls and environmental damage typically do not occur in more common manufacturing industries, such as automobile or appliance manufacturing.<sup>265</sup> These industries may result in some torts, but they are generally not the industries engaged in ultrahazardous activities such as toxic chemical production referred to in *M.C. Mehta v. Union of India*, where the court deemed that the costs of such activities outweighed the economic benefits of limited liability.<sup>266</sup>

To be sure, enterprise liability could benefit corporate parents in some self-piercing cases. In *Renusagar*<sup>267</sup> and *Novartis*,<sup>268</sup> parent corporations were able to take advantage of enterprise liability to self-pierce and obtain benefits from the state. Other companies could potentially use enterprise liability to obtain lower tax rates or patent protections. Yet if the same companies were responsible for torts, the tort victims would most likely have little chance of obtaining a speedy recovery for the reasons discussed above. A villager injured by a power company's negligent construction of electrical lines, for example, would still face a lengthy legal battle to obtain any compensation.<sup>269</sup> Thus, the likely result of broad enterprise liability could be that corporations benefit from easier self-piercing in some cases while tort creditors still remain unlikely to recover any significant damages in many tort cases. However, even though corporate parents would benefit in some self-piercing cases under enterprise liability, such cases will most likely be too scattershot<sup>270</sup> to allow corporate planners to effectively account for them as a positive factor when creating corporate structures. This uncertainty means that enterprise liability is likely to be, at best, an ambiguous benefit for corporations.

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264. See *Union Carbide Corp. v. Union of India*, (1991) 1 S.C.R. Supp. 251, 252–53 (involving the Indian government as representative of tort victims).

265. See RESTATEMENT (SECOND) OF TORTS § 520: ABNORMALLY DANGEROUS ACTIVITIES (1997) (describing six factors of abnormally dangerous activities, including a “high degree of risk” of harming people and property, and a “likelihood” that the harm from the activity will be great); William K. Jones, *Strict Liability for Hazardous Enterprise*, 92 COLUM. L. REV. 1705, 1710 (1992) (describing the *Restatement's* definition of ultrahazardous activities as applying to those that can cause widespread harm such as atomic energy, large storage of toxic gas, or the manufacture of explosives).

266. *M.C. Mehta v. Union of India*, (1987) 1 S.C.R. 819, 844.

267. (1988) 1 S.C.R. Supp. 627, 628–30.

268. (2004) 3 C.T.C. 95 at ¶ 13–14, available at <http://indiankanon.org/doc/145476>.

269. See Galanter, *supra* note 9, at 296.

270. See Thompson, *supra* note 13, at 1057–58 (describing the relatively small proportion of successful self-piercing cases in an empirical study).

## B. THE NEED FOR INDUSTRIAL INVESTMENT

Enterprise liability also carries a large potential cost: the threat of liability and litigation expenses can deter corporations from investing in India. Even though lawsuits can linger in the Indian court system for years, resulting in greatly delayed compensation for tort victims, corporations still have to bear the costs of defending lawsuits in protracted litigation as well as face the lingering uncertainty of the eventual damages they may have to pay.<sup>271</sup> Thus, despite the inefficiencies of the Indian court system that produce minimal benefits for tort victims, corporations still face significant legal costs and risk in an expanded system of enterprise liability.

Since at least the 1960s, Indian courts have defined the scope of limited liability by deferring to the economic policies of the Indian government.<sup>272</sup> After the Bhopal disaster, the Indian government pushed to hold companies engaged in ultrahazardous activities responsible for their actions under enterprise liability.<sup>273</sup> As discussed extensively in this Note, enterprise liability can help victims of mass torts recover damages for their injuries. In cases like Bhopal, countries are justified when they conclude that corporations should not be allowed to shift the costs of major disasters to thousands of tort victims.<sup>274</sup> Moreover, in such cases, traditional veil piercing may not be helpful because many industrial accidents can result from negligence rather than an intentional tort like fraud that is often required for veil piercing.<sup>275</sup>

However, the Indian government has also moved aggressively in recent years to encourage economic growth, especially in the industrial sector of the economy, and to reduce government regulation.<sup>276</sup> This current national interest of rapid economic growth is not consistent with the expansion of enterprise liability to all cases. Therefore, Indian courts should reserve enterprise liability for companies that engage in ultrahazardous activities because expanding the doctrine to all cases would hurt an important national economic priority: fueling rapid growth by encouraging industrial investment.

Limited liability has long been critical for industrial growth. For example, the

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271. See, e.g., *Union Carbide Corp. v. Union of India*, (1991) 1 S.C.R. Supp. 251, 253 (describing procedural history in which compensation awarded to plaintiff fluctuated significantly from court-to-court).

272. See *supra* Part III.

273. See *supra* section III.B.

274. See generally *supra* section IV.B (discussing how Indian courts determined that the large human and financial costs of large mass torts like Bhopal and Shriram (in the *Mehta* case) outweighed the economic benefits).

275. See Peter B. Oh, *Veil Piercing*, 89 TEX. L. REV. 81, 125-26 (2010) (describing the greatly increased likelihood of successful veil piercing where a court finds fraud).

276. India recently announced that it would aim for economic growth of 9% to 9.5% of GDP through 2017. See Unni Krishnan & Kartik Goyal, *India Targets Economic Growth of at Least 9% to 2017, Singh's Adviser Says*, BLOOMBERG NEWS (Apr. 21, 2011), <http://www.bloomberg.com/news/2011-04-21/india-targets-economic-growth-of-as-much-as-9-5-ahluwalia-says.html>. Consumer demand for houses, cars, and household appliances has surged in recent years. *Id.* In addition, the nation's biggest carmaker plans to boost capacity by twenty-one percent this year to meet growing demand. *Id.*

rise of limited liability in the United States coincided with industrialization and the growth of railroad companies.<sup>277</sup> While few massive corporations existed before 1865, railroads, oil and steel companies all needed large amounts of capital to grow and compete.<sup>278</sup> Avi-Yonah has explained that “between 1865 and the 1890s the widely held, publicly traded, non-owner managed enterprise gradually became the norm for U.S. business activities.”<sup>279</sup> Today, India is navigating similar economic straits.

India is in the middle of an economic renaissance spurred by the growth of private businesses and foreign investment.<sup>280</sup> Limited liability has helped fuel that economic growth by helping small businesses grow into large corporations.<sup>281</sup> The encouragement of the free market has spurred high levels of economic progress in India in recent years.<sup>282</sup> The Indian economy was expected to grow 8.5% percent in 2010, and its growth rate was projected to potentially overtake China’s growth rate by 2013.<sup>283</sup> Much of this growth has come from a boom in the private sector; India’s public sector remains mired in inefficiency.<sup>284</sup> Some scholars have argued that this economic growth in the aftermath of the *Mehta* decision shows that enterprise liability may not hurt economic growth as much as critics claim.<sup>285</sup> Still, scholars who make such criticisms concede that India’s continuing economic expansion has largely been due to its decision to greatly encourage foreign investment in other ways, such as by reducing regulation.<sup>286</sup>

However, numerous economists have shown that India has had trouble growing its domestic manufacturing industry in recent years. While China has built much of its economic progress on robust domestic manufacturing and exports, India has not.<sup>287</sup> Some Indians “wonder fearfully if India is going to skip an industrial revolution altogether, jumping straight from an agricultural economy to a service economy.”<sup>288</sup> Services account for roughly fifty percent of India’s GDP, agriculture makes up twenty-two percent, and industry takes up

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277. See Reuven S. Avi-Yonah, *To Be or Not to Be? Citizens United and the Corporate Form* 10 (Univ. of Mich. Pub. Law and Legal Theory Working Paper Series, Working Paper No. 184 & Univ. of Mich. Empirical Legal Studies Ctr., Working Paper No. 10-005), available at <http://ssrn.com/abstract=1546087>.

278. *Id.*

279. *Id.*

280. See Das, *supra* note 153, at 3, 6.

281. See *supra* section I.A (describing advantages of limited liability such as reduced monitoring costs, diversification, and liquid capital markets).

282. See *India’s Surprising Economic Miracle*, *ECONOMIST* (Sep. 30, 2010), [http://www.economist.com/node/17147648?story\\_id=17147648&fsrc=rss](http://www.economist.com/node/17147648?story_id=17147648&fsrc=rss) (describing the importance of foreign investment to India’s economic boom).

283. *Id.*

284. See *id.*

285. See Dearborn, *supra* note 16, at 229.

286. See *id.* at 229 n.205.

287. See Das, *supra* note 153, at 7.

288. *Id.*

twenty-seven percent.<sup>289</sup> By comparison, industry constitutes forty-six percent of China's GDP.<sup>290</sup> Economists estimate that India still has the potential to expand its manufacturing sector significantly, a move that could lift tens of millions of rural agricultural workers out of poverty.<sup>291</sup>

The Organization for Economic Cooperation and Development has stated that “[a]n improved policy environment for private sector and foreign investment has played a major part” in India’s “impressive acceleration in economic growth.”<sup>292</sup> The Indian government’s encouragement of private entrepreneurship and foreign investment has “led to an acceleration of economic growth and a reduction in poverty.”<sup>293</sup> But a big portion of future economic growth depends on India successfully being able to shift millions of destitute rural workers from agriculture into the manufacturing sector.<sup>294</sup> Aware of this need to develop industry, the Indian government has responded by loosening restrictions on foreign investment in industrial companies and boosting expenditures on infrastructure.<sup>295</sup> Anand Sharma, the country’s Commerce and Industry Minister, recently announced that the government is on the verge of enacting a new National Manufacturing Policy to further expand foreign investment in industry, saying “India will soon change its growth strategy and increase manufacturing exports in [the] near future.”<sup>296</sup>

An expanded doctrine of enterprise liability would stunt this development of new industry and manufacturing that the Indian government has stated is an important component of national economic policy.<sup>297</sup> So far, India appears to be relatively isolated in its broad application of enterprise liability.<sup>298</sup> Even after the U.N. recently endorsed enterprise liability as a way to regulate the behavior of multinational corporations, member states have not been receptive.<sup>299</sup> Rather than adopting enterprise liability, other countries seem to be moving toward traditional veil-piercing law.<sup>300</sup>

289. *Id.*

290. *Id.*

291. *See id.* at 3, 7. Economists also expect many more jobs to be generated by entrepreneurs, who have taken out eighty percent of all loans in the country. *Id.* at 7.

292. ORG. FOR ECON. COOPERATION & DEV., *OECD Investment Policy Reviews: India 2009* 11 (2009), [http://www.oecd.org/document/50/0,3746,en\\_2649\\_34893\\_44153906\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/50/0,3746,en_2649_34893_44153906_1_1_1_1,00.html).

293. *Id.* at 21–22.

294. *See id.* at 23–24. The OECD has stated that having a large labor pool in the agricultural sector of the economy impedes economic growth because agriculture generally has a much lower growth rate than other sectors of the economy. *Id.* at 23. In 2005, agriculture accounted for 56.1% of all employment in India, while industry accounted for just 18.8%. *Id.* at 24.

295. *See id.* at 21, 25, 27–28.

296. *See Effort To Give Big Push to Manufacturing Growth*, THE HINDU (Mar. 18, 2011), <http://www.thehindu.com/business/Economy/article1550713.ece>.

297. *See id.*

298. *See Dearborn, supra* note 16, at 228–29.

299. *See id.* at 229.

300. *See, e.g.*, Mark Wu, Comment, *Piercing China's Corporate Veil: Open Questions from the New Company Law*, 117 YALE L.J. 329, 330 (2007) (noting that China's new Company Law aligns with the majority of market economies in permitting limited veil piercing).

For example, China has recently adopted a new Company Law<sup>301</sup> that resembles traditional veil-piercing doctrine in England and the United States. The Chinese law allows veil-piercing in cases that involve “abusing the independent status of juridical persons or the shareholder’s limited liabilities.”<sup>302</sup> Thus, the Chinese veil-piercing law appears to require some type of misuse or abuse of corporate control rather than the mere existence of corporate control endorsed by enterprise liability.<sup>303</sup>

If companies face the prospect of more liability, they would be more likely to abandon plans to create new jobs and factories in India and move elsewhere, such as China, that impose a greater burden on plaintiffs seeking to recover from corporate parents. Assuming all other factors are the same, it would be logical for a company to minimize potential liabilities by establishing a subsidiary in another jurisdiction where the corporate form is not so easily disregarded.<sup>304</sup> For example, consider an American car company that incorporates a subsidiary in India and owns just over fifty percent of the subsidiary’s shares. Under the theory of enterprise liability applied by Indian courts, the American corporation could be liable for any contract disputes involving its subsidiary. This liability would apply even if the American parent company had no involvement in the subsidiary’s independent decision to commit a fraud or breach a contract. Because of the increased risks and costs companies would have to assume under such a framework, they could easily choose to abandon their plans to invest in India and move their capital to another country with more rigorous standards for veil piercing.<sup>305</sup>

Scholars have explained that “limited liability was, and remains, essential to attracting the enormous amount of investment capital necessary for industrial corporations to arise and flourish.”<sup>306</sup> Thus, expanding enterprise liability too far would significantly hurt India’s efforts to recruit industrial investment. If Indian courts adopted such an approach, they would be contradicting decades of jurisprudence in which they have consistently defined the scope of limited liability to serve national economic priorities. To avoid this result, the Supreme Court of India should limit enterprise liability to cases involving ultrahazardous torts.

#### CONCLUSION

This Note has shown how a judicial theory of limited liability can evolve

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301. *Id.*

302. *Id.* at 332 (quoting Gongsī fǎ [Company Law] (promulgated by the Standing Comm. Nat’l People’s Cong., Oct. 27, 2005, effective Jan. 1, 2006), art. 20).

303. *Id.* at 331–32.

304. *See, e.g.*, Stephen M. Bainbridge, *Abolishing Veil Piercing*, 26 J. CORP. L. 479, 492–93 (2001) (discussing the prospect of “incorporation havens”).

305. *Cf. id.* at 492 n.59 (discussing capital flight from Massachusetts in the early 1800s—a period in which Massachusetts corporations did not confer the benefit of limited liability).

306. *Id.* at 495.

along with a country's national economic policies. The decisions that courts make on protecting limited liability or disregarding it can accelerate or halt a country's economic progress. To their credit, Indian courts have recognized that limited liability is a rule of law that is best examined in conjunction with economic policies. This awareness gave them a normative basis for finding that the country's economic needs were better served by applying enterprise liability rather than traditional veil piercing in tort cases involving companies engaged in ultrahazardous activities. Going forward, courts in India and other developing countries should not rush to move from limited liability to enterprise liability in all cases. Instead, they should continue to carefully examine whether their application of limited liability is consistent with national economic priorities. In India, that means returning in many cases to a hoary old chestnut of corporate law that still has remarkable resilience in the modern era—the *Salomon* rule.