
AN ANALYSIS ON THE DOCTRINE OF LIFTING OF CORPORATE VEIL

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ABSTRACT

When a business is established, it is considered as a different legal entity from its promoters, directors, members, and workers, resulting in the notion of the corporate veil, which separates these parties from the corporate body. For many years, courts and intellectuals have debated the subject of "lifting the corporate veil." However, the issue has not gotten the attention it deserves in the literature. There is no defined set of standards in place, making it impossible to foresee when the courts may ignore the separate entity concept. The purpose of this article is to compare the corporate veil piercing concepts in India and England. In terms of jurisprudential methods, handling of specific case types, and other related problems, the article emphasises some basic distinctions between the theories. Despite these significant distinctions, the Article indicates that many English corporate veil cases follow a similar analytical approach to the instrumentality concept under Indian law. The article closes with a reintroduction of Lord Denning's much-maligned single economic unit thesis. This revised idea will allow for a more methodical approach to corporate veil piercing cases.

The main goal of this article is to look at the limits of the corporate veil-lifting principle. The first section of this paper will look at the notion of a corporation as a distinct entity. The law of piercing the veil is discussed in Part V. Part VI examines the often-proposed common law grounds for removing the veil in order to establish the underlying causes for judicial disregard of the separate entity concept. The comparative element of the statutory laws addressing veil piercing is addressed in Part VII. And Part VIII compares and contrasts the law of veil piercing in the United Kingdom and India.

Keywords: Corporate veil, separate entity, judicial precedents, company law principles.

Research Question

The author through the present research work aims to deal with the issue of piercing of corporate veil and laws dealing with it in India and How it is different from United Kingdom.

Hypothesis

One of the fundamental concepts of corporate law is that when a company is formed under the Companies Act, it establishes a distinct legal entity from its members. However, if it is discovered that the business engaged in unlawful activity or that its operations were not handled in accordance with the rules, the shareholders may be held personally responsible and their personal assets may be seized. What function does piercing the corporate veil serve?

If a court pierces a corporation's or LLC's corporate veil, its owners, shareholders, or members may be held personally responsible for corporate obligations. This implies that creditors may seize the owners' primary residence, bank account, investments, and other property in order to pay the corporate debt.

Literature Review

1. *Personality of public corporation and lifting the corporate veil, By Bahadur & Krishna*

The term "piercing the corporate veil" refers to a situation in which courts disregard limited liability and hold investors or directors personally responsible for the actions or debts of a business. In closed companies, corporate veil penetration is frequent. While state law differs, courts typically have a strong presumption against breaching the corporation veil and will do so only if significant wrongdoing has occurred. Courts recognise the advantages of limited liability because it "promotes the establishment of public markets for stocks, thus enabling the liquidity and diversification benefits those investors get from such markets." Creditors generally have no recourse against corporate stockholders as long as certain requirements are met. When, on the other hand, the company is formed illegally in order to avoid responsibility, creditors may penetrate the corporate veil.

2. *Piercing the corporate veil: Focussing the inquiry, By Cathy S. Krendl & James R. krendl*

The legal personality conferred to a corporation by legislation, in contrast to the individuals who comprise it, is arguably the most basic concept of company law and serves as a critical

building block of our economic and legal structures. However, the concept is not absolute: courts have sometimes used their authority to ignore the company's distinct identity in order to treat it as one with its controller. However, the basis for and extent of this authority have only been defined seldom by the higher courts. The article discusses previous judicial assessments of penetrating the corporate veil in England and compares them to the Indian courts' most recent approach to the same issue.

3. Wedded to Salomon: Evasion, Concealment and confusion on piercing the veil of the one-man company, By Hannigan & Brenda

This paper examines two principles namely, concealment principle, and evasion principle. The concealment principle is that a company is involved in a transaction to hide the true nature of the transaction. The Evasion principle is that where there is a legal right against a person who is in charge of controlling the company, the company is interposed in such a manner so that the principle of a separate legal entity defeats the legal right against that person. It is concluded that the limited principle of English law applies where a person is subject to an existing legal duty, responsibility, or limitation that he intentionally avoids or whose enforcement is intentionally frustrated by interposing an organisation under his control. To prevent the company or its controller from benefiting from the legal personality of the firm, a court may breach the corporate veil. However, this may only be done in limited circumstances. Even if the criteria are met in virtually every situation when it is applied, the circumstances in practise reveal a legal link between the firm and its controller, therefore piercing the corporation's veil isn't essential.

4. Lifting the corporate veil, By P. M. Bakshi

This paper mentions that earlier in the year 1897 the legal world witnessed the literal interpretation of the law by the House of lords neglecting the notions of equity and fairness. However, the idea of the lifting of the corporate veil involves moving the iron curtain a bit to peer into the backstage of the firm to see who're individuals behind the company and to also know about the genuine brains behind a corporation. The paper covers a plethora of cases when raising the iron curtain becomes important to glimpse the backstage of a corporation simply to comprehend the objective of its incarnation better in the first place. The theory of the removal of the corporate veil functions as a check on anybody seeking to gain out of their wrongful conduct hiding behind the firm taking refuge and performing acts which the law otherwise

bans. This paper attempts at describing how this concept have questioned, and yet has assisted in enriching the jurisprudence. It also gives an evaluation of the cases where lifting of the veil is justified for attaining the purposes of justice. Further, this article constructs an analysis from the genesis of the doctrine to its present form.

Introduction

Corporations are now regarded as a necessary component of modern civilization. It has a significant impact on almost every aspect of human activity, including work and play. The beginning of corporations in Europe can be traced back to the early 17th century. In exchange for granting them the right to exist, the monarchs of the time granted these corporations a public commission on which they could rely. These organisations were established as early as the colonial period. In order to facilitate the implementation of a trade mission, the monarchs granted a group of investors some of their privileges. The corporations worked for both the monarchs and a group of investors at the same time. In the early days, incorporations were primarily used for public bodies such as monasteries, which had been granted corporate personality by the crown through a charter or by a prescription, or by a combination of both. The beginning of the history of company law can be traced back to 1844. The formation of joint stock companies was the first step. It did away with the requirement of obtaining permission from the Queen through the Royal Charter or a sanction from Parliament. The right to incorporate was now to be obtained through the process of registering with the government. A great deal has changed since then to accommodate the changes that have occurred throughout the world.

Corporate personality

One of the main principles of corporate law is that when a company gets registered under the Companies Act, it becomes an artificial legal entity and is separate from its members. This principle was adopted in 1897 in unequivocal terms in *Saloman v Saloman & amp Co Ltd*.¹ The House of Lords concluded that a company is a separate legal entity and is distinct from its members. Even though Saloman possesses maximum shares of the company, it does not mean he is liable for its debts. It supported the principle that the Limited Liability Companies are separate from its members. The decision given in this case is considered a landmark judgement and is one of the cornerstones of modern company law. This case is often referred by the judges

¹ *Saloman v. Saloman & amp Co Ltd*, (1897) A.C. 22.

while dealing with cases related to a company's distinct and legal entity.² All companies are equal in the eyes of the law. Since a company is an artificial person, it has to operate through natural persons, it has the right to sue and be sued. Ashu Bala stated in one of her articles that the veil of incorporation does not mean the company's internal affairs would be hidden. Now here comes the concept of the corporate veil. Different people have a different understanding of the term "corporate veil". This terminology has come up before various judges, in courtrooms and before renowned researchers, and everyone has a different perspective and definition of this term. Terms like a sham, curtain, etc., have come up while discussing this term. To understand this in simpler terms, it is a sort of privilege which is given to a person who is operating the company. That privilege is that if a person is handling the company legally and fulfilling all the formalities, then his assets would be protected from being liable for the company's debts or any other legal obligations. However, if it is found that the company was involved in illegal activities or the operations of the company were not conducted as per the provisions, then the shareholders can be held personally liable, and their personal assets can be taken away.

Piercing the corporate veil: India and UK

The concept of piercing the corporate veil has been allotted several meanings over the years. It is one of the most discussed doctrines in corporate law. Many have not accepted the "separate legal entity" perspective and have given numerous reasons for the same. There are several cases that have taken place in the U.K., and *Prest v. Petrodel Resources Ltd*³ is one of the landmark cases in this regard. Lord Sumption said that if a person in charge of handling the company's operation is at fault, he can be held liable. He gave two principles. One is the concealment principle, and the other is the evasion principle. The concealment principle is that a company is involved in a transaction to hide the true nature of the transaction. The Evasion principle is that where there is a legal right against a person who is in charge of controlling the company, the company is interposed in such a manner so that the principle of a separate legal entity defeat the legal right against that person.⁴ If we look at the approach adopted by the European unions, we will see that they shift the liability and expand it. This results in the weakening of the companies' limited liability and increasing the group's liability. When we talk about India,

² Bahadur & Krishna, *Personality of public corporation and lifting the corporate veil*, vol. 14, no. 2, JOURNAL OF THE INDIAN LAW INSTITUTE, 207–227 (1972).

³ *Prest v. Petrodel Resources Ltd*, [2013] UKSC 34.

⁴ Hannigan & Brenda, *wedded to Salomon: Evasion, Concealment and confusion on piercing the veil of the one-man company*, 50 IRISH JURIST, 11–39 (2013).

similar cases have come up before the courts, and verdicts have been given in the same manner as the U.K.⁵ In *Delhi Development Authority v Skipper Construction Co.(P) Ltd*,⁶ the Supreme Court held that where the company character is being used for the purpose of committing fraud, the court can look beyond the corporate character of the company. *Kapila Hingorani v. the State of Bihar*⁷ is another case that took place in 2003. The court held that the corporate veil of the company could be pierced if the company was found to be detrimental to the interest of the public or workman. Thus, these cases make it clear that common law countries have upheld the decision given in the *Saloman* case and allowed the piercing of the corporate veil in exceptional cases. Piercing of veil is a rare option in the U.K. as illegality or any fraud committed by the company does not amount to a prima facie case.

Comparison

If we compare the case in UK with the Indian Jurisdiction, we will see differences in perspective despite both being common law countries. Let us look at the justification for the same.

Indian Company Law developed in U.K. Companies Act, 1956 marked the beginning of Company Law in our country. Many changes have taken place in the business environment since then, and thus, these changes resulted in the formation of the Companies Act, 2013. The principle laid down in *Saloman* is considered a fundamental principle of corporate law in India. The doctrine of the corporate veil is also incorporated in this act. The adoption of the corporate veil doctrine had far-reaching consequences, and thus, a need was felt to narrow down its scope. This was done to accommodate the complex corporate structure. The doctrine was narrowed down by making changes to the *Saloman* principle. It was decided that the corporate veil can be pierced in certain circumstances, and the shareholders or directors of the company can be held liable and asked to share the liabilities of the company.

The *Saloman* Principle has been involved in a number of cases that took place in India. It has been cited in criminal, fraudulent as well as constitutional law cases. It has been frequently referred to in taxation cases. The Income Tax Act does not have any express provision talking about the piercing of the corporate veil. The revenue authorities in India have allowed the courts to look at the taxation cases through the legal structure. In 2012, one such case came into the

⁵ Bakshi, P. M., *Lifting the corporate veil*, 36(3) JOURNAL OF THE INDIAN LAW INSTITUTE, 383–84 (1994).

⁶ *Delhi Development Authority v. Skipper Construction Co. (P) Ltd.*, 1996 4 SCC 622.

⁷ *Kapila Hingorani v. State of Bihar*, (2003) 6 SCC 1

picture. The case was *Vodafone International Holdings B.V. v Union of India*.⁸ In this case, the revenue authorities sent a show-cause notice to the company. They said that the transfer of 67 per cent shares of an Indian entity resulting from the purchase of shares of another offshore company would attract the capital gain tax of ₹12000 crores. The company argues that the company was incorporated abroad, and thus the revenue Authorities have no jurisdiction to make the demand for the payment of taxes. Multiple entities were separating these two parties, and the authorities wanted to ignore them all by looking at only one motive of ascribing the share of one company as the acquisition of another.

The High court allowed the piercing of the veil. The matter went to Supreme Court, and the decision of the High court was overturned. Chief Justice Kapadia said that foreign investors enter into Indian through foreign holding companies and SPVs, which have got recognition by the Indian Tax laws and corporate. The acknowledgement of this practice is a sort of relief to the foreign investment companies. The majority was of the opinion that the tax authorities would be allowed to pierce the veil if they could prove that the transaction in question was tax avoidant in nature. The court said that the revenue department must focus on the purpose of the transaction by taking into account a number of indicators. Thus, the tax authorities have lower chances of piercing the corporate veil. In conclusion, the verdict given in this case is a sort of relief to the foreign investors but has given enough opportunity to the tax authorities to pierce the veil in future. Guidelines have been given, and they can be interpreted while looking at cases involving foreign investors. The verdict given in this case should be kept in mind, and legal counsels have to ensure that the deals are framed in such a manner so as to safeguard the interest of the client and avoid scrutiny from the tax authorities.

Conclusion

As the foregoing debate comes to a close, we can see that UK and India have come to essentially the same understanding with regard to this situation, taking into consideration the history of both countries and the similarities of their respective legal systems. Focusing on the cases at hand, the *Prest* verdict, while consistent with the *Salomon* principle, can be considered unfair. With relevance to the common law countries, they follow the *Salomon* case and believe it to be the Bible of all like nature cases. All their judgment is based on it. Every case after that has only built on the same, which is an excellent approach if the situation calls for it, as with

⁸ *Vodafone International Holdings B.V. v. Union of India*, (2012) 6 SCC 613.

regard to civil law. So, to summarise, even though the outcome in the Prest case was unjust for the other spouse. Even though the Indian government was denied billions of rupees in the Vodafone case as a result of this strict application of company law, it has provided clarity regarding the grounds on which the piercing of corporate veil can be done.

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