

## Corporations, Crime and the Law: An insight of evolution of the Doctrine of Corporate Criminal Liability

-Dr. Ashutosh Bairagi\*

### Abstract

*Corporations have now become an integral part of our society, and with development of corporations they have become significant actors in our economy, our society runs in the risk of getting victimized by these corporations. Corporations or Corporate bodies reap all the advantages flowing from the acts of the directors and they act to the detriment of the public in the name of the corporate bodies thus the applicability of lifting the corporate veil has unveiled the sheath. There has been a gradual and structural shift in stance taken by Indian courts towards ensuring strong internal control framework to prevent and manage fraudulent activities in business organizations. This paper traces final verdict of the Courts with regard to the concept of Corporate Criminal liability and also throws light over the inability of the Court in properly sentencing the guilty corporates due to inadequacy of law. It also provides the current situation about the corporate criminal liability in the International scenario. Through this paper other forms of punishments are suggested so that the real objective of the punishment i.e. deterrence or the reformation could be achieved.*

### Keywords

Corporations, Corporate Personality, Criminal Liability, Mens Rea, Alter ego.

### Introduction

In simple language, corporation means a group of individuals coming together to carry on a business. The major law relating to Corporations in India is codified in The Companies Act, 2013 and under Indian law the liability of the corporation is essentially liability of the company only.

Corporate Personality is the creation of law. A statutory corporation or company

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\* Assistant Professor (Sr. Scale) –Shri Vaishnav Institute of Law , Indore(M.P.)

is an artificial person enjoying in law capacity to have rights and duties and holding property. It has the legal personality of its own and it can sue and can be sued in its own name. It does not come to end with the death of its individual members and therefore, has a perpetual existence and a common seal, but with such liability on the part of the members to contribute to the assets of the company in the event of its being wound up.<sup>1</sup>

However, unlike natural persons, a corporation can act only through its agents. The concept of a separate legal personality of a corporation was, at one time, exploited by individuals to escape or evade personal liability. As a general rule, common law did not impose criminal liability on corporations. This was based on the belief that a corporation lacked moral blameworthiness or the requisite mens rea, which is an essential element of a crime. Further, the thought that was prevalent was that a corporate has 'no soul to damn, and no body to kick'<sup>2</sup>. Exceptions were restricted to holding a company liable to provide compensation to third parties for wrongful acts of its employees, but did not extend to liability for crimes. It was from the early 20<sup>th</sup> century onwards that courts began to recognize the criminal liability of corporations. By way of timely intervention, courts were able to prevent the use of the corporate shield to perpetrate fraud or escape liability for offences. In more recent times, courts have pierced the corporate veil by attributing individual liability to the persons responsible for wrongful acts of a company, while simultaneously they have developed the law on corporate criminal liability and have thereby retained the legal fiction.

Courts are especially likely to impose criminal liability on a corporation when the criminal act is requested, authorized, or performed by the board of directors, an officer or another person having responsibility for formulating company policy or high level administrator having supervisory responsibility over the subject matter of the offence and acting within the scope of his employment.

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1. Indian Companies Act 2013 (Sec. 9).

2. Cf. John C. Coffee, Jr., "No Soul To Damn, No Body To Kick": An Unscandalized Inquiry into the Problem of Corporate Punishment, 79 MICH. L. REV. 386 (1981).

### **Theories of corporate criminal Liability**<sup>3</sup>

**Theory of vicarious liability** –The doctrine of vicarious liability recognizes that a person may be bound to answer for the acts of another. Similarly in the case of corporations the company may be liable for the acts of its employees , agents ,or any person for whom it is responsible .The traditional theory of vicarious liability holds the master liable for the acts of the servant in the course of the master’s business without proof of any personal fault on the part of the master.

**Identification theory** – In this theory , the corporations are held criminally liable for true crimes and the regulatory offences. This theory recognizes that the acts and the state of mind of certain senior officers in a corporation are the directing minds of the corporation and thus deemed to be the acts and the state of the mind of the corporation itself .The corporation is considered to be directly liable under this theory.

**Aggregation Theory** – Under this theory , the corporation aggregates the composite knowledge of different officers in order to determine liability . The company aggregates all the acts and the mental elements of the important or relevant persons within the company to establish whether in toto they would amount to a crime if they had all been committed by one person. The theory combines the elements of vicarious liability principle and identification theory by portraying the knowledge of agent and identifying it with that of the owner. Through this mechanism, it gets a little difficult for the corporations to save themselves from being liable for a crime by shielding behind the lines of multiple departments that exist within the companies.

### **Indian Jurisprudence**

All the Penal liabilities are generally regulated under the IPC, 1860 in India. It is this statute which needs to be pondered upon in case of criminal liability of corporation. As per sec. 11 of the code the word person includes corporation or association or body of persons whether incorporated or not . Until recently, Indian courts were of the opinion that corporations could not be

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3. [lex-warrier.in/2014/02/analysis-corporate-criminal-liability-india/](http://lex-warrier.in/2014/02/analysis-corporate-criminal-liability-india/)

criminally prosecuted for offenses requiring mens rea as they could not possess the requisite mens rea.

In **Motorola Inc. v. Union of India**<sup>4</sup> the Bombay High Court quashed a proceeding against a corporation for alleged cheating, as it came to the conclusion that it was impossible for a corporation to form the requisite mens rea, which was the essential ingredient of the offense. Thus, the corporation could not be prosecuted under section 420 of the IPC.

Courts in India were hesitant to attribute criminal liability to a company for an offence that required a criminal intent. Further, courts were of the opinion that they could not prosecute companies for offences that entailed a mandatory sentence of imprisonment.

In India, uncertainty over whether a company can be convicted for an offence where the punishment prescribed by the statute is imprisonment and fine was first addressed in **MV Javali vs Mahajan Borewell & Co and Others**<sup>5</sup> where the Supreme Court held that mandatory sentence of imprisonment and fine is to be imposed where it can be imposed, but where it cannot be imposed — namely, on a company — fine will be the only punishment.

In the **The Assistant Commissioner, Assessment- II, Bangalore and Ors. v. Velliappa Textiles Ltd. and Ors**<sup>6</sup>, the Supreme Court held that since company is an artificial person, it cannot be physically punished to a term of imprisonment. The court opined that where the statute provides for imprisonment or fine, it is not a problem, but where the statute provides for imprisonment and fine, the court is not given the discretion to impose fine in lieu of imprisonment. And, therefore, the company cannot be prosecuted as the custodial sentence cannot be imposed upon it.

A couple of years after this decision, the apex court by majority overruled its own judgment in **Standard Chartered Bank vs directorate of enforcement**<sup>7</sup>. The Supreme Court in this case imposed the sentence of fine on the company as it was

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4. (2004) Cri.L.J. 1576.

5. AIR 1997 SC 3964 .

6. AIR 2004 SCC 86.

7. AIR 2005 SC 2622.

a case of absolute liability for the offence of violation of section 56(1) of the FERA Act, 1973.

The Supreme Court held that: *"We do not think that there is blanket immunity for any company from any prosecution for serious offences merely because the prosecution would ultimately entail a sentence of imprisonment. Corporate bodies undertake activities that affect the life, liberty and property of the citizens. The corporate vehicle now occupies such a large portion of the industrial, commercial and sociological sectors that amenability of the corporation to criminal law is essential for a peaceful society with a stable economy. There is no immunity to the companies from prosecution merely because the prosecution is in respect of offences for which the punishment prescribed is mandatory imprisonment and fine."*

It was further held that:

*"There is no dispute that a company is liable to be prosecuted and punished for criminal offences. Although there are earlier authorities to the effect that corporations cannot commit a crime, the generally accepted modern rule is that except for such crimes as a corporation is held incapable of committing by reason of the fact that they involve personal malicious intent, a corporation may be subject to indictment or other criminal process, although the criminal act is committed through its agents."*

In **Iridium India Telecom Ltd v Motorola Inc**<sup>8</sup> , the Supreme Court held that companies and corporate houses can no longer claim immunity from criminal prosecution on the ground that they are incapable of possessing the necessary mens rea for the commission of criminal offences. The court relied on the principle laid down in **HL Bolton (Engg) Co Ltd v TJ Graham & Sons**<sup>9</sup>.

*"A company may in many ways be likened to a human body. They have a brain and a nerve centre which controls what they do. They also have hands which hold the tools and act in accordance with directions from the centre. Some of the people in the company are mere servants and agents who are nothing more than hands to do*

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8. AIR 2011 SC 20.

9. 1956 3 All ER 624.

*the work and cannot be said to represent the mind or will. Others are directors and managers who represent the directing mind and will of the company, and control what they do. The state of mind of these managers is the state of mind of the company and is treated by the law as such. So you will find that in cases where the law requires personal fault as a condition of liability in tort, the fault of the manager will be the personal fault of the company."*

Based on the aforesaid principle, the Supreme Court further held that:

*"A corporation is virtually in the same position as any individual and may be convicted of common law as well as statutory offences including those requiring mens rea. The criminal liability of a corporation would arise when an offence is committed in relation to the business of the corporation by a person or body of persons in control of its affairs. In such circumstances, it would be necessary to ascertain that the degree and control of the person or body of persons is so intense that a corporation may be said to think and act through the person or the body of persons."*

The notion that a corporation cannot be held liable for the commission of a crime had been rejected by adopting the doctrine of attribution and imputation.

The criminal intent of the 'alter ego' of the corporation, i.e., the persons or the group of the persons that guide the business of the corporation, would be imputed to the corporation. In another judgment in July 2011 of **CBI vs. M/s Blue-Sky Tie-up Lt and Others**<sup>10</sup>, the apex court reiterated the position of law and held that companies are liable to be prosecuted for criminal offences and fines may be imposed on the companies.

The Supreme Court recently in **Sunil Bharti Mittal v. Central Bureau of Investigation ("CBI") and Others**<sup>11</sup> (Criminal Appeal No. 35 of 2015 (arising out of Special Leave Petition (Crl.) No. 3161 of 2013)) held that the principle of alter ego can only be applied to make the company liable for an act committed by a person or group of persons who control the affairs of the company as they represent the alter ego of the company; however it cannot be applied in reverse

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10. Crl. Appeal No(s). 950 of 2004.

11. Criminal Appeal No. 35 of 2015 (arising out of Special Leave Petition (Crl.) No. 3161 of 2013).

direction to make the directors of the company liable for an offence committed by the company. The Supreme Court has clarified that the application of the principle of vicarious liability to make the directors of the company liable for an offence committed by the company can only be done if the statute provides for it. While doing so, the Court has set aside the order of the Special Court wherein the Special Court had issued summons to the directors of the companies by stating that they represent the alter ego of the companies.

**Thus it has now become possible to hold a corporation criminally liable for acts committed through their agents and employees, and attribute mens rea to them.** In this day and age of economic advancement where corporations have a say in almost every aspect of life, such a principle has assumed paramount importance in corporate governance.

### **International Scenario**

A basic principle of German law is “*societas delinquere non potest*”, which means that a corporate body cannot be liable for a criminal offence. The argument is that the human element is missing and that the creation and operation of slush funds, as well as giving bribes, are all human acts and not the acts of the company itself<sup>12</sup>. But Germany has developed an elaborate structure of administrative sanctions, which includes provisions on corporate criminal liability. These so-called *Ordnungswidrigkeiten* are handed down by administrative bodies. The key provision for sanctioning the corporation is Section 30 *Ordnungswidrigkeitengesetz* (Code of Administrative actions), which calls for the imposition of fines on corporate entities<sup>13</sup>.

**In the US and the UK, it has been a settled principle that corporates can be held criminally liable. Way back in 1909, in New York Central and Hudson River Rail Road Co v. United States**, Supreme Court in the US held that a corporation is liable for crimes of intent and stated: "We see no good reason why corporations may not be held responsible for and charged with the knowledge and

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12. Konstantin Zens, Susan Watson, "Enforcement instruments in transnational corporate bribery: an overview", 2012 International Company and Competition Law Review 271 available at [www.westlaw.com](http://www.westlaw.com)
  13. Markus Wagner, "Corporate Criminal Liability National and International Responses" available at <http://www.icclr.law.ubc.ca/publications>

purposes of their agents, acting within the authority conferred upon them.

The Supreme Court concluded that criminal liability could be imputed to the corporation based on the benefit it received as a result of the criminal acts of its agents. This case essentially imported the *doctrine of respondeat superior* from tort law into criminal law. There are a plethora of federal statutes applicable to corporations under which criminal liability may be imposed<sup>14</sup>.

In **HL Bolton (Engg) Co. Ltd. vs TJ Graham & Sons**<sup>15</sup> Lord Denning stated that, "The state of mind of these managers is state of mind of company, and it is treated by law as such. So, in cases where the law requires personal fault as a condition of liability in tort, the fault of the manager will be the **personal fault of company.**"

**In the case of Tesco Supermarkets Limited v. Natrass**<sup>16</sup>, Tesco relied on the defence of the "act or omission of another person" who in this case was a store employee, to show that they had taken all reasonable precautions and due diligence necessary not to be criminally liable. Lord Reid held that, in order for liability to attach to the actions of a person, it must be the case that "The person who acts is not speaking or acting for the company. He is acting as the company and his mind which directs his acts is the mind of the company. If it is a guilty mind then that guilt is the guilt of the company."

Beginning in the 1970s, nations throughout western Europe began creating or expanding corporate criminal liability, rather than contracting or eliminating it<sup>17</sup>.

France had also not recognized corporate criminal liability since the French Revolution, In 1982 the "*Conseil Constitutionnel*" made it clear that the French Constitution did not prohibit the imposition of fines on a corporation<sup>18</sup>.

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14. New York Central R. Co. v. United States, 212 U.S. 481 (1909) available at <http://supreme.justia.com/cases/federal/us/212/481/>

15. HL Bolton (Engg) Co Ltd vs TJ Graham & Sons, [1957] 1 WLR 454

16. [1971] UKHL 1

17. Thomas Weigend, "Soecietas delinquere no potest? A German Perspective", 6 J. INT'L CRIM. JUST. 927, 928 (2008) (noting quick spread of corporate criminal liability to the Netherlands, Switzerland, Austria, and Italy) available at [http://www.law.yale.edu/documents/pdf/cbl/Beale\\_paper.pdf](http://www.law.yale.edu/documents/pdf/cbl/Beale_paper.pdf)

18. Stessens, Guy. "Corporate Criminal Liability: A Comparative Perspective" International and Comparative Law Quarterly, v. 43, July 1994, p.501



Corporate criminal liability is an integral part of Japanese law. There are currently more than 700 criminal provisions on the national level alone, which can punish entities other than individuals, and this number is likely to increase in the coming years<sup>19</sup>.

The Concept of Criminal liability of Corporation is also mentioned under various International documents. A number of conferences have dealt with the same issues since the end of World War II. Among them are the 8th International Conference of the Society for the Reform of Criminal Law in 1994 in Hong Kong and the International Meeting of Experts on the Use of Criminal Sanctions in the Protection of the Environment in Portland, in 1994<sup>20</sup>.

The Seventh United Nations Congress on the Prevention of Crime and the Treatment of Offenders of 1985 in Milan mentioned that “due consideration should be given by Member States to making criminally responsible not only those persons who have acted on behalf of an institution, corporation or enterprise, or who are in a policy-making or executive capacity, but also the institution, corporation or enterprise itself, by devising appropriate measures that could prevent or sanction the furtherance of criminal activities.”<sup>21</sup>

In 1998, the Council of Europe passed the Convention on the Protection of the Environment through Criminal Law, which stipulated in Article 9 that both “criminal or administrative sanctions or measures” could be taken in order to hold corporate entities accountable<sup>22</sup>.

### **Conclusion & Suggestions**

In the case of corporate criminal liability, the settled position of law is now that a company is virtually in the same position as any individual and may be

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19. Ito, Kensuke. “Criminal Protection of the Environment and the General Part of Criminal Law in Japan.” *International Review of Penal Law*, v. 65, n. 3-4, p. 1043

20. International Centre for Criminal Law Reform and Criminal Justice Policy. “International Meeting of Experts on the Use of Criminal Sanctions in the Protection of the Environment: Internationally, Domestically and Regionally.” Portland/OR, March 1994.

21. A/RES/40/32. Guiding Principles for Crime Prevention and Criminal Justice in the Context of Development and a New International Economic Order. 29 November 1985  
<http://www.un.org/documents/ga/res/40/a40r032.htm>

22. ETS No. 172. Council of Europe. Convention on the Protection of the Environment through Criminal Law. 4 November 1998. available at <http://conventions.coe.int/Treaty/en/Treaties/Html/172.htm>

convicted of offences including those requiring mens rea. Furthermore, a company cannot escape liability for a criminal offence merely because the punishment prescribed is that of imprisonment and a fine. Shortcoming of fine as a form of punishment is that it pins the poor and eases the rich. The rich can easily get away by paying a huge fine while the poor may have to toil hard even to get a hundred rupees. Nevertheless, its efficacy in specific crimes has made it a necessary mode of sanction. This shows that the biggest drawback in restricting fine as the sole form of punishment to corporates is that with their massive bank accounts, it is easy for them to get away with the criminal liability and it also does not solve the purpose of punishment since neither the corporates would be deterred nor would they be retributed for the crimes like corporate killings that they have committed (for instance: using poor quality of material in building dams which would soon collapse thereby dislocating and even killing inhabitants around the area or the laborers themselves).

Looking into the above drawbacks, there is a need to evolve new forms of punishments which could effectively deter the corporates from engaging into any criminal activity. The new forms of punishment may be putting economic and social sanctions on the corporates such as :

- Corporate Death or order for winding up only in cases of continuous criminal behaviour in the given field.
- Temporary closure of the company for a given period depending upon the gravity of the act .
- Rehabilitation of victims of crime by corporates.
- Payments of high sum as compensation to the victims of crime as were paid in the Bhopal gas tragedy.
- Delisting of the corporations .

It is time that the government concentrates on formulating rigorous laws and regulations on this aspect. It is essential to combine diverse methods of punishment, which shall stimulate voluntary self-observance of legal processes and dissuade corporations from indulging in fraudulent and criminal practices.

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