nerej
EST. 1963 | CELEBRATING 55 YEARS

Corporate shareholders shielded in environmental law case

April 19, 2012 - Connecticut

Last month the Connecticut Supreme Court issued a decision that could allow a corporate entity to avoid paying penalties for environmental noncompliance by sheltering non-culpable shareholders behind a corporate shield. In Commissioner v. State Five Industrial Park, Inc., 304 Conn. 128 (2012), the Connecticut Supreme Court provided a blueprint for corporate entities and attorneys. At the center of this case is Joseph Farricielli, the owner of four parcels of property straddling North Haven and Hamden, Conn., home of the infamous "tire pond" and other solid waste disposal operations. The tire pond was once a clay pit that received between 18 and 30 million used tires without proper permits from the State of Connecticut, creating an environmental and human health hazard. Since 1974, the Department of Energy and Environmental Protection (DEEP) has engaged in a variety of legal actions to force Mr. Farricielli to comply with state waste management laws (including administrative orders, stipulated judgments, injunctions, cease and desist orders, and motions for contempt), but Mr. Farricielli remained resolute and the unpermitted disposal operations continued. Finally, in 2001, DEEP scored a seemingly significant victory when they obtained a judgment requiring Mr. Farricielli to post bonds, fund the closure of two unpermitted waste landfills and pay approximately $3.8 million in civil penalties. As of March, progress has been made towards closing the tire pond and landfills, but the civil penalties remain outstanding.

Having been unable to collect the penalties from Mr. Farricielli, DEEP attempted to collect from State Five Industrial Park, Inc., a closely held corporation, and its president, sole officer and director (and Joseph's wife), Jean Farricielli. State Five has owned portions of the tire pond since 2000, when Mr. Farricielli transferred the land to State Five's predecessor corporation, "Look Investment," which he was the president of. Other owners of State Five include the Farricielli's' two sons, who had no real involvement in the corporation. DEEP argued that the court should apply the equitable doctrines of "piercing the corporate veil" to Mrs. Farricelli and "reverse veil piercing" to State Five in order to hold them liable. The doctrine of piercing the corporate veil allows a creditor to disregard the separate legal identity of a corporation and reach the assets of a corporate insider that would otherwise be shielded by the corporate structure. Conversely, reverse piercing allows a creditor to reach the assets of the corporation to satisfy claims or a judgment obtained against a corporate insider. The goal of both of these doctrines is to prevent corporations from being used as intermediaries to perpetuate fraud or promote injustice.

Based upon the facts in the case, the lower court determined that it was appropriate to hold both Mrs. Farricelli and State Five liable for the 2001 judgment under both piercing theories. The court determined that Mr. Farricelli (as the "alter ego" of State Five) and Mrs. Farricelli exerted complete control over State Five and they used that control to evade satisfying the 2001 judgment. For example, both continually had the authority to draw on the corporation's line of credit, transact business, and direct personnel, regardless of their statuses as shareholders, directors or officers.

Further, both failed to treat State Five as a distinct legal entity, as they co-mingled personal and corporate funds and loaned these funds out to family members.

In a significant ruling the Connecticut Supreme Court reversed the lower court's decision, noting that the lower court had not established the necessary, specific connection between Mr. Farricielli's improper actions vis-Ã -vis State Five and the plaintiffs' inability to collect the 2001 judgment. The Court went on to review and question the reverse veil piercing doctrine, noting, among other things, that the doctrine allows outside creditors to attach a corporation's assets directly, which prejudices non-culpable shareholders who have an interest in the corporation's assets. In light of this concern the Court found that DEEP had failed to demonstrate that the Farriciellis' sons, part owners of State Five, were complicit in State Five's wrongdoing; therefore, piercing was not appropriate. In overturning the lower court's decision the Court did not discuss the continued legitimacy of reverse veil piercing in Connecticut.

The Supreme Court's failure to proclaim the death of the reverse veil piercing doctrine means that it is still a viable equitable remedy in Connecticut. Yet the Court's critical discussion of the doctrine's flaws suggests its days could be numbered. Until the death knell comes, State Five has potentially created a mechanism to shield innocent corporate owners from environmental liability. In light of the uncertainty that State Five has created, it is crucial to seek legal advice when structuring corporate ownership of contaminated properties.

Amanda Brosy is an associate in the Environmental and Land Use Practice Group at Halloran & Sage, Hartford, Conn.