Global Corporate Governance Colloquia 2019

7-8 June 2019

House of Finance

Goethe University Frankfurt

8th June 2019

Protocol – Session 3

The Limits of Limited Liability: Evidence from Industrial Pollution.

Speaker:	Ian Appel
Discussant:	Oren Sussman

Ian Appel is an assistant professor of finance at Boston College Carroll School of Management. His main research interests are corporate governance, law and finance, and institutional investors. His research has been published in the Journal of Financial Economics and Review of Financial Studies and mentioned in media outlets including the New York Times, Wall Street Journal, and Financial Times. He received his PhD in finance from The Wharton School at the University of Pennsylvania.

Oren Sussman's research focuses on financial crisis, financial constraints and the business cycle, economic analysis of insolvency law, cross-border insolvency, sovereign debt and exchange-rate volatility and, recently, Fintech.

Protocol of Session 3, Saturday 8 June (4.00 p.m. – 5.00 p.m.)

In the first part of the session, a joint paper by Pat Akey and Ian Appel is presented. The paper studies how parent liability for subsidiary environmental cleanup costs affects industrial pollution and production. The empirical setting exploits a Supreme Court decision that strengthened parent limited liability protection for some subsidiaries. Using a difference-in-differences framework, it is found that increased liability protection for parents leads to a 5-9% increase in toxic emissions by subsidiaries. Evidence suggests the increase in pollution is driven by lower investment in abatement technologies rather than reallocation across plants or increased production. Cross-sectional tests suggest a harm-shifting motivation for these effects. Overall, results highlight moral hazard problems associated with limited liability.

During the second part of the session, the discussion, Oren Sussmann expressed his appreciation for the paper's high quality. Subsequently, he summarized the topic as 'the legal dilemma' in which legal responsibility for dishonorable actions of affiliated firms causing negative externalities on the society contrasts one of the principles of corporate law, limited liability. Given the findings of the paper, he further discussed if protection offered by limited liabilities is partly too strong. In the course of the discussion, differences between civil law systems in reactions to the US Supreme Court case *United States versus Bestfoods*, which serves as an external shock in the paper, were reviewed. According to one opinion, in a common law system the case could have created a precedent that might have eventually led to substantial changes in the legal treatment of limited liabilities. Thus, the findings' generalizability was debated. Additionally, it was recommended to look for broader implications of the decision by expanding the post-treatment observation period. Further comments suggested to expand the paper by i) looking at the effects of increased pollution on the increasing subsidiaries' parent companies and ii) comparing the *Bestfood* case with other instances of human-caused environmental catastrophes and their consequences.