CLARITY EMERGES: SUPREME COURT'S RULINGS ON GROUP OF COMPANIES DOCTRINE IN INDIAN ARBITRATION

When a key affiliate company of a signatory plays a crucial role in a commercial arrangement and actively participates in it, even without signing an arbitration agreement, the question arises: Can the non-signatory be compelled to arbitration in case of a dispute? This is a query that the Group of Companies Doctrine aims to address. Courts and tribunals, in arbitration cases, have invoked the Group of Companies Doctrine to bind a non-signatory to arbitration, though it has previously been inaccurately labelled as an 'expansion' or 'extension' of the arbitration agreement.

As the name suggests, when a group of companies is involved in a commercial arrangement and one of its members has signed an arbitration agreement, the other entities within the group may be bound by the arbitration agreement if the circumstances and conduct of the parties indicate that the true intention was to bind both signatories and non-signatories.

The Group of Companies Doctrine originated with explicit endorsement by an arbitral tribunal in the *Dow Chemicals v. Isover Saint Gobain* case[1]. The International Chamber of Commerce (ICC) tribunal emphasized that the determination of the scope and effect of the arbitration agreement should be based on the "common intent of the parties," discernible from the circumstances surrounding the "conclusion, performance, and termination of the contract." In this case, the tribunal found all the members of the Dow Chemical Group to be collectively participating in fulfilling the contract, functioning as a unified 'economic reality' or unit.

I. <u>Chequered application by Indian courts</u>

Initially, the Supreme Court of India ("**Supreme Court**") consistently ruled against binding a non-signatory to an arbitration agreement, adopting this approach for references under Section 8[2] of the Arbitration & Conciliation Act, 1996 ("**Act**") as well as when appointing an arbitrator under Section 11[3] of the Act. In *Indowind Energy Ltd v. Wescare (India) Ltd*[4], the Supreme Court held that a non-signatory could not be a party to the arbitration agreement absent ratification, approval, adoption, or confirmation of the agreement by it.

This approach changed with a series of judgments starting with *Chloro Controls India (P) Ltd v.*

[1] CC Case No. 4131, 23 September 1982.
[2] Sukanya Holdings v. Jayesh H Pandya (2003) 5 SCC 531.
[3] S N Prasad v. Monnet Finance Ltd, (2011) 1 SCC 320.
[4] (2010) 5 SCC 306.

Severn Trent Water Purification Inc[5] ("**Chloro Controls**"), where the Group of Companies doctrine in arbitration was introduced to Indian jurisprudence. This pertained to Section 45 of the Act which provides for reference to arbitration where the arbitration agreement provides for a foreign seat of arbitration. The Supreme Court, noting the wider scope of Section 45 which uses the expression 'any person', interpreted it as enlarging the scope of the arbitration agreement beyond the signatories. Subsequently, Act 3 of 2016 amended the Act, incorporating similar wordings into Section 8. While a new set of judgments thereafter expanded on the Group of Companies doctrine, its application remained inconsistent, leading the Supreme Court in *Cox & Kings Ltd. v. SAP India (P) Ltd.*,[6] to refer the matter to a bench of five judges.

II. Ruling of the Supreme Court

After considering the entire legal landscape concerning the Group of Companies doctrine, including its treatment in foreign jurisdictions, the Supreme Court in *Cox and Kings Ltd. v. SAP India Pvt. Ltd. & Anr.*,[7] upheld the application of the doctrine in India. The key takeaways from the judgment are as follows:

A. An arbitration agreement is a creature of contract bound by privity:

The Supreme Court recognized that an arbitration agreement must satisfy the principles of contract law laid down in the Contract Act, 1872 ("Contract Act") in addition to satisfying the stipulation in Section 7 of the Act. Only an agreement enforceable by law is a contract and Section 10 of the Contract Act provides that all agreements are contracts if they are made *inter alia* with free consent. Further as per Section 13 of the Contract Act two persons are said to consent when they agree upon the same thing in the same sense. Thus, there must be consensus ad idem between the parties to constitute a valid arbitration agreement. The arbitration agreement is also bound by the doctrine of privity which means that a contract cannot confer rights or impose liabilities on any person except the parties to the contract.

B. Parties to an arbitration agreement may be non-signatories:

Though the signature of a party on the agreement is the most profound expression of consent, the corollary of it that persons who have not signed the agreement are not bound by it may not be correct.

[5] (2013) 1 SCC 641
[6] (2022) 8 SCC 1.
[7] 2023 INSC 1051.

A written contract need not require the parties to put their signature to it. A non-signatory is a person that is implicated in a dispute which is a subject matter of the arbitration, although it has not formally entered into the arbitration agreement. The Supreme Court held that, it is not necessary for the persons to be signatories to a contract to enter into a legal relationship. The only important aspect to be determined is whether they intended or consented to enter into the legal relationship by dint of their action or conduct. To determine whether a non-signatory is bound by an arbitration agreement, the courts and tribunals apply typical principles of contract law and corporate law.

C. Separate legal entity & piercing the veil:

The Supreme Court acknowledged that entities within a corporate group possess separate legal personalities, a fact that should not be overlooked except in extraordinary circumstances such as fraud. The fundamental distinction between a parent company and its subsidiary remains intact and cannot be easily set aside for the sake of economic convenience. It held that from a legal standpoint, the rights and liabilities of a parent company cannot be transferred to the subsidiary, and vice versa, unless a robust legal foundation justifies such a transfer. Further, the court opined that the alter ego principle sets aside corporate separateness and the parties' intentions in favor of prevailing considerations of equity and good faith. On the contrary, the Group of Companies Doctrine enables the identification of parties' intentions to ascertain the true participants in the arbitration agreement without compromising the legal identity of the involved entity. Consequently, the application of the alter ego principle or piercing the corporate veil cannot serve as the foundation for applying the Group of Companies Doctrine.

D. Test for Group of Companies doctrine:

While holding that the applicability of the Group of Companies Doctrine requires a study of the facts, the Supreme Court approved of the cumulative factors laid down in *Oil and Natural Gas Corporation Ltd v. Discovery Enterprises Pvt. Ltd.*[8] which are as follows-

(i) the mutual intent of the parties;

(ii) the relationship of a non-signatory to a party which is a signatory to the agreement;

(iii) the commonality of the subject-matter;

[8] (2022) 8 SCC 42.

(iv) the composite nature of the transactions; and

(v) the performance of the contract.

The Supreme Court mandated that the above factors must be considered while determining the applicability of the doctrine. While doing so the court also clarified that the application of the above factors has to be case specific and the Supreme Court cannot tie the hands of the courts or tribunal by laying down how much weightage they ought to give to the above factors.

E. Limited intervention of courts:

When a non-signatory person is enjoined as a party to Section 8 or 11 proceedings under the Act, the Supreme Court has laid down that the referral court should prima facie determine the validity or existence of the arbitration agreement as the case may be. The question of whether the non-signatory is bound by the arbitration agreement would instead be determined by the arbitral tribunal as it requires a detailed factual analysis. Once a tribunal concludes that a non-signatory is a party to the arbitration agreement it may even apply for interim measures under Section 9 of the Act.

F. Chloro Controls interpretation overruled:

In Chloro Controls the Supreme Court reasoned that non-signatories being a part of the same group of companies were "claiming through or under" the signatory parties. A larger bench of the Supreme Court has now expressly overruled this interpretation holding it to be erroneous and against well-established principles of contract and commercial law. The Supreme Court held that the phrase "claiming though or under" only applies to entities acting in a derivative capacity and not with respect to joinder of parties in their own right. As such the judgment in Chloro Controls has been overruled to the extent it traces the Group of Companies Doctrine to the phrase "claiming through or under".

III. <u>Conclusion</u>

The Supreme Court's judgment brings clarity to the working, scope, and application of the Group of Companies Doctrine in arbitration. It reflects an evolution from a rigid stance against binding non-signatories to a nuanced approach basis case specific facts. The ruling emphasizes that arbitration agreements, being contractual, don't require direct signatories for its enforceability. The Court recognizes the distinct legal personalities of entities within a corporate group, establishing that the

alter ego principle cannot serve as the foundation for applying the Group of Companies Doctrine. The Court's elucidation includes a comprehensive test, allowing flexibility in assessing factors and acknowledging the complexity in determining the doctrine's applicability in specific cases.If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to reach out to:

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