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## **A five Judge Constitution Bench of the Supreme Court, in Cox and Kings Ltd. vs SAP Pvt. Ltd. (“Cox and Kings”), delivered a ruling on the Group of Companies’ doctrine (“GCD”).**

For long, the application of GCD was doubted due to its intrusion with well-settled principles of “party autonomy”, “privity of contract”, and “separate legal personality”. The result was an unclear jurisprudence on GCD, since its adoption by the Indian Supreme Court in 2012 in the case of *Chloro Controls (India) (P) Ltd. v. Severn Trent Water Purification Inc. (“Chloro Controls”)*<sup>1</sup>. Significant challenges in applying the doctrine, especially in the context of corporate conglomerates, led to inconsistent decisions.

The Supreme Court in Cox and Kings has reconciled divergent views and has sought to provide clarity on the doctrine’s foundation, scope, and application going forward.

### **SUPREME COURT RULING**

#### **Parties to Arbitration Agreement**

The Supreme Court has held that the basis for GCD and joinder of non-signatories to an arbitration agreement in India arises from an interpretation that definition of “party” can be said to include signatory as well as non-signatories.

For a non-signatory to be bound to an arbitration agreement, the arbitration agreement must satisfy the requirements of, both, the Indian Contract Act, 1872 and Section 7 of Arbitration and Conciliation Act, 1996 (“Act”), and qualify as a valid agreement. In terms of Section 7 of the Act, the arbitration agreement must be (i) in writing, as opposed to an oral agreement, and (ii) arise out of a defined legal relationship, whether contractual or not.

In this regard, the Supreme Court holds that the prime consideration while enjoining a non-signatory to arbitration is to determine whether the non-signatory “intended or consented” to effect legal relationships with the signatory parties and be bound by the arbitration agreement “through dint of their action or conduct.”

Therefore, the Court reaffirms the position that consensus, implied or express, is a *sine qua non* for roping in a non-signatory to an arbitration.

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### Mutual Intention and Preserving Corporate Distinctness

The Court recognized that the GCD is only one of the consent-based doctrines similar to doctrines of agency, assignment, assumption, etc. to bind a non-signatory to arbitration. While invoking GCD, the objective is to identify the “common intention of parties” to bind such a non-signatory while preserving the legal personalities of the group companies. Therefore, GCD is a “mutual intent” driven doctrine, which does not undermine corporate principles of ‘party autonomy’ and ‘separate legal entity’.

The Court also affirmed that the principles of alter ego or piercing the corporate veil, which disregards the separate legal personality cannot be the basis for the application of GCD.

### Invoking the GCD – a twin approach

The Supreme Court has clarified that in most situations, the language of the contract is only suggestive of the intention of the signatories to such contract and not the non-signatories.

For the purposes of invoking the GCD, the Supreme Court held that courts or tribunals need to adopt a two-fold approach i.e. to determine: first, the existence of a group of companies; and second, the conduct of the signatory and non-signatory which indicates their “*common intention*” to join the non-signatory, as a “veritable” party” to the arbitration agreement. Therefore, the intention of both, the signatory and non-signatory, is crucial.

While holding that the presence of a “group of companies” is necessary for invoking GCD, the Supreme Court clarifies that it is not a “*sufficient condition*” in itself.

### Deciphering Mutual Intention

The Supreme Court holds that the factors (as laid down in the case of *Discovery Enterprises*<sup>2</sup>) must be cumulatively considered for deciphering the “mutual intention” of parties to bind the non-signatory to the arbitration. These factors are:

- ▶ relationship of entities within the corporate group;
- ▶ performance of the parties in the underlying contractual obligations;
- ▶ the commonality of the subject matter; and
- ▶ composite nature of the transactions.

The burden to establish the above factors is on the party seeking the joinder of the non-signatory.

### Predominant Participation of Non-Signatory – a veritable party

The Supreme Court held that the participation of a non-signatory in the performance of the underlying contract is the most important factor for ascertaining the “mutual intention” of parties to bind the non-signatory. Therefore, the determination requires to be made whether a non-signatory undertook the mantle of a “true party” or a “veritable party” to the arbitration agreement based on their involvement in the conclusion, performance, or termination of the underlying contract containing the arbitration agreement.

The Court went on to explain that the threshold for the involvement of the non-signatory in the contract should be “direct”, “positive”, and “substantial.” Therefore, what is contemplated is “active” participation by the non-signatory and mere incidental involvement of the non-signatory is not enough to bind the non-signatory.

### Guard Rails against misuse of GCD

Interestingly, the Supreme Court also provided much-needed clarity to prevent the misuse of the GCD by restricting its contours. In various instances, owing to the presence of a corporate group, financially stable members of a corporate group, particularly the listed companies, having no connection to the underlying contract, have been roped in, merely because the signatories defaulted on their obligations. Claimants found this a convenient approach to assert liability on more solvent non-signatories. The Court cautioned that:

- ▶ The mere presence of a “commercial relationship” between a signatory and a non-signatory is not sufficient to infer a legal relationship between the parties. The Court has specifically urged against impleading a “related entity” within a group even when “*it does not have any rights or obligations under the underlying contract and did not take part in the performance of the contract.*”
- ▶ The presence of common shareholders or directors cannot lead to the conclusion that the subsidiary company will be bound by the acts of the holding company.
- ▶ The statements or representations made by promoters or directors in their personal capacity would not bind a company.
- ▶ GCD cannot be applied solely based on the principle of “Single Economic Entity”. Imposing liability on a non-signatory within a group for the acts of other members merely because they belong to a “Single Economic Unit” will ride roughshod over the principles of separate corporate personality, which GCD aims to preserve.

### Phrases “claiming through or under”

The Court held that GCD can be used to bind a non-signatory de hors the expression “*claiming through or under*” in Sections 8/45 of the Act. Accordingly, it was held that *Chloro Controls (supra)* to the extent that it traced the doctrine to the phrase “*claiming through or under*”, is erroneous.

### WAY FORWARD

The Supreme Court has provided clarity on the scope and contours of GCD. The ruling also highlights that GCD applies only to parties to an “arbitration agreement” and not the underlying contract. The Supreme Court also refers to a situation where a non-signatory could be held to be a party to the arbitration agreement without becoming a formal party to the underlying contract.

As per Gary B. Born, it is entirely possible for non-signatories to become party to an agreement to arbitrate without thereby becoming a party to the underlying

commercial contract. Gary B. Born says *“It bears emphasis that the parties’ intentions – both actual and presumed – will often be different with regard to their arbitration agreement, and its dispute resolution mechanism, than with regard to their underlying commercial contracts. That is, there will readily be cases where the parties desire a unified, “one-stop” dispute resolution mechanism, particularly one extending to all the members of a corporate group involved in a particular transaction, without altering the allocations of substantive contractual rights contained in the underlying contract.”*<sup>3</sup>

Therefore, what remains to be seen is whether merely by virtue of being bound to the arbitration agreement, a non-signatory can be held to be substantively liable under the underlying agreement. This is the key commercial consideration that conglomerates would be most concerned and judicial authorities must guard against overreach.

Further, the Supreme Court has given the task of applying GCD to bind non-signatories to the Arbitral Tribunal, before a non-signatory can apply for interim reliefs under Section 9 of the Act. It has been held that *“...Once a tribunal comes to the determination that a non-signatory is a party to the arbitration agreement, such non-signatory party can apply for interim measures under Section 9 of the Arbitration Act.”*

In our view, this approach of the Supreme Court does not create a level playing field. While a signatory party can approach the court to seek interim relief against a non-signatory party, a non-signatory party would have to first seek a determination from an arbitral tribunal before seeking interim relief. A harmonious reading of the judgment would possibly convey that even in those rare cases, where a non-signatory seeks recourse to interim reliefs under Section 9 of the Act, the Court would be empowered to make a *prima facie* determination in this regard.

In our view, GCD is a consensual doctrine to facilitate non-signatories who may be necessary for an arbitration to be brought together in one forum. GCD ought not to become a “device” at the hands of parties to make a non-signatory as an effective party to the underlying commercial contract so as to impose substantive obligations. This distinction ought to be recognized and maintained.

<sup>1</sup> Chloro Controls India (P) Ltd. v. Severn Trent Water Purification Inc., (2013) 1 SCC 64.

<sup>2</sup> ONGC v. Discovery Enterprises Pvt Ltd (2022) 8 SCC 42.

<sup>3</sup> Born, International Commercial Arbitration (3rd edn, Kluwer Law International 2021)p. 1526, 1566–67, 1602.

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