

SC's rendezvous with "Group of Companies" doctrine – a complicated love affair

In its recent judgement¹, the Supreme Court of India ("SC") upheld that a non-signatory can also be bound by an arbitration agreement basis the 'Group of Companies' doctrine.

WHAT IS 'GROUP OF COMPANIES' DOCTRINE?

The 'Group of Companies' doctrine is akin to principles of agency or implied consent, whereby the corporate affiliations among distinct legal entities provide the foundation for concluding that they were intended to be parties to an agreement, notwithstanding their formal status as non-signatories.² This doctrine was initially recognised by SC in the *Chloro Controls*³ case.

FACTS

In 1992, Mahanagar Telephone Nigam Limited ("MTNL") floated certain non-cumulative secured redeemable bonds ("Bonds") through private placement worth INR 425 Crores. MTNL had placed Bonds worth INR 200 Crores with Can Bank Financial Services Limited ("CANFINA") (a wholly owned subsidiary of Canara Bank (hereinafter referred to as "CB")) pursuant to a memorandum of understanding, as a fixed deposit. CANFINA paid around INR 50 Crores of the fixed deposit in 1992 however, since the balance amount was yet to paid, MTNL serviced the Bonds to a partial extent

Post subscription of the Bonds, the secondary market underwent a collapse due to unearthing of security scam. Consequently, CANFINA faced a severe liquidity crunch and CB purchased the Bonds issued by MTNL from CANFINA. When CB requested for the registration of these Bonds with MTNL, MTNL refused to transfer the Bonds and informed CB that it had registered part of the Bonds, in favour of CANFINA. The bond instruments were however retained by MTNL, on the ground that CANFINA had defaulted on the payment of deposit money of INR 150 Crores and interest thereon. Subsequently, MTNL cancelled all the Bonds *inter alia* on the ground that letters of consideration remained with CANFINA and issued a cheque for INR 5.5 Crores as the amount payable to CB. CB, however, returned the said cheque and demanded the restoration and registration of the Bonds. CB filed a writ petition⁴ before the Delhi High Court ("HC") challenging the cancellation of the Bonds and seeking a direction for payment of the interest accrued.

It is relevant to note that CANFINA was joined as a proforma party in the writ petition filed by CB.

THE TWIST

In light of the precedent set in *O.N.G.C. v. Commissioner of Central Excise*⁵, HC, vide its order dated May 30, 2008, referred the dispute to the Committees of Disputes which in turn, expressed its view that parties should resort to arbitration

¹ *Mahanagar Telephone Nigam Ltd. vs Canara Bank and Ors.* [2019(10) SCALE619]

² *Cheran Properties Limited vs. Kasturi and Sons Limited and Ors.* [2018 (3) ARBLR 228 (SC)]

³ *Chloro Controls India Private Limited v Severn Trent Water Purification Inc.* [[2012]13 SCR 402]

⁴ W.P. (Civil) No. 560 of 1995

⁵ (1995) Supp. 4 SCC 541



and to expedite the process, parties should enter into an arbitration agreement.

Pursuant to the aforesaid suggestion, CB shared a draft arbitration agreement with MTNL (having CB and CAFINA on one side and MTNL on the other). HC vide its order dated October 1, 2010, disposed of the pending writ petition⁶ reaffirming the observation made by the Committee of Disputes in the said matter.

The decision in *O.N.G.C. v. Commissioner of Central Excise*⁷ was overruled by a constitutional bench in *Electronics Corporation of India Ltd. v. Union of India*⁸, pursuant to which CB moved back to HC to restore the disposed writ petition⁹; which was allowed by HC vide its order dated September 16, 2011. During the said proceedings, the parties agreed to resort to arbitration and subsequently a sole arbitrator (“**Arbitrator**”) was appointed in the matter, who issued a notice to all the three parties, i.e. MTNL, CANFINA and CB.

CB objected the addition of CANFINA as a party to the arbitration proceedings and the Arbitrator held that since CANFINA did not appear before HC on September 16, 2011, CANFINA cannot be joined a party to the proceedings. This award was objected by MTNL vide an application which was dismissed as “not pressed” on the statement made by the counsel of MTNL. Further recourses taken by MTNL were eventually dismissed by HC.

Aggrieved by the aforesaid orders of HC, MTNL filed the special leave petition, where vide the order dated May 8, 2014, SC issued notices to all parties, including CANFINA.

ISSUES

- (a) Existence of valid arbitration between the parties to the dispute, i.e. MTNL, CB and CANFINA;

- (b) Since CANFINA is not a party to the arbitration agreement, it cannot be impleaded in the proceedings.

ARGUMENTS

CB objected to the joinder of CANFINA as a party to the arbitration proceedings on the ground that an agreement entered into by one of the companies in a group cannot be binding on the other members of the same group as each company is a separate legal entity which has separate legal rights and liabilities.

HELD

A non-signatory can be bound by an arbitration agreement basis the ‘Group of Companies’ doctrine, where the conduct of the parties evidences a clear intention of the parties to bind both the signatory as well as the non-signatory parties. The doctrine has been invoked by courts and tribunals in arbitrations where an arbitration agreement is entered into by one of the companies in the group, and the non-signatory affiliate or sister or parent concern is held to be bound by it if the facts and circumstances of the case demonstrate that it was the mutual intention of all parties to bind both the signatories and non-signatory affiliates in the group.

The circumstances in which the doctrine could be invoked were enumerated by SC: **(i) direct relationship between the party which is a signatory to the arbitration agreement; (ii) direct commonality of the subject matter; (iii) composite nature of transaction between parties**¹⁰.

SC observed that the doctrine has also been invoked where there is a tight group structure with strong organizational and financial links, to constitute a single economic unit or reality. In the present case, CANFINA was set up as a wholly owned subsidiary of CB and was staffed mostly by

⁶ *Ibid* (p.4)

⁷ *Ibid* (p.5)

⁸ (2011) 3 SCC 404

⁹ *Ibid* (p.4)

¹⁰ A 'composite transaction' refers to a transaction which is inter-linked in nature; or, where the performance of the agreement may not be feasible without the aid, execution, and performance of the supplementary or the ancillary agreement, for achieving the common object, and collectively having a bearing on the dispute.



personnel from CB. Further, the Board of CANFINA comprised mostly of senior executives from CB.

The disputes between the parties emanated out of the transactions of a tri-partite nature.

Therefore, the final resolution can only be possible if all three parties are joined in the arbitration proceedings. SC also relied on its earlier decision¹¹ and stated that ***a common-sense approach needs to be adopted to give effect to the intention of the parties to arbitrate the disputes between them.***

SC observed that since there was a case of ***implied or tacit consent by CANFINA to being impleaded***, evident by the conduct of the parties throughout the proceedings and facts of the case, ***there was a clear intention of the parties to bind both CB and CANFINA in the said proceedings.***

Thus, SC allowed the present appeal partly and invoked the ‘Group of Companies’ doctrine to join CANFINA in the arbitration proceedings pending before the Arbitrator¹².

RECENT REFUSALS

Interestingly, SC refused to apply the ‘Group of Companies’ doctrine in the recent case of *Reckitt Benckiser*¹³ as the SC was unable to establish a

clear intention of the parties to bind both the signatory as well as non-signatory parties, basis the facts of the case.

CONCLUSION

SC’s complicated love affair with the ‘Group of Companies’ doctrine is indeed heading in a positive and progressive direction (unlike most relationships) and is reflective of a pro-arbitration demeanour being adopted by the Indian courts. India currently serves as a booming market for complex commercial transactions involving mergers, acquisitions and private equity investments, involving companies and group companies in such transactional structures. This precedent certainly throws a positive light indicating that critical group companies, not being signatories to an arbitration agreement can be made parties to an arbitration. Besides ensuring that such disputes are resolved in a time-bound and efficient manner, this also indicates the critical thinking and rationale of the court of law in order to assess the components to implement this doctrine.

¹¹ Enercon (India) Ltd. and Ors. v. Enercon GMBH MANU/SC/0102/2014: (2014) 5 SCC 1

¹² Ameet Lal Chand Shah v. Rishabh Enterprises, (2018) 15 SCC 678

¹³ *Reckitt Benckiser (India) Private Limited versus Reynders Label Printing India Private Limited and Anr.* (Arbitration Petition (Civil) No. 65 of 2016) which was decided on July 1, 2019.



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