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ARBITRATION: THE PROCESS AND THE UNRESOLVED ISSUE OF NON-SIGNATORIES

AUTHORED BY - ADITI MUSADDI

ABSTRACT

Arbitration agreements are certainly the foundational instruments in resolving disputes outside the courts and common legal mechanism. However, the involvement of non-signatory parties in the arbitration proceedings presents a multifaceted challenge which results in legal complexities and practical intricacies. This article analyses the divergent approaches taken by courts and arbitration tribunals in addressing the issue of non-signatory parties. Additionally, through a comprehensive analysis of case laws and legal principles, this article explicates the various scenarios in which non-signatories may become a party to the arbitration agreement through certain doctrines and theories which include agency relationships, alter-ego or piercing the corporate veil, theory of equitable estoppel and doctrine of group of companies. Furthermore, it offers insights into the present stance regarding the issue of non-signatory involvement in the arbitration agreement and also examines its implications. Ultimately, this article sheds light on the reciprocity between the arbitration agreement and the rights and obligations of non-signatory party which therefore gives a deeper understanding of arbitration law.

1. BACKGROUND

According to the scriptural hypothesis, Lord Solomon was the primary arbitrator when he settled the issue between two ladies who were professing to be the mother of a baby boy. A few authors have likewise declared that the method utilized by Lord Solomon was like that is utilized in arbitrations today. Additionally, arbitration was also used by Philip the Second, the dad of Alexander the Incomparable, for settlement of regional debates in Greece as far back as 337 B.C. As it turns out, around 600 B.C., in a debate among Athens and Megara, for the ownership of island of Salamis, the matter was alluded to five simple appointed authorities who ultimately distributed the island to Athens. This way, the footsteps of international arbitration can be traced back in ancient times. Furthermore, Lord Krishna is said to be the first mediator in the hindu scriptures. He was the one who tried to mediate between the Kauravas and Pandavas to cancel the then upcoming war of Mahabharata. In India's pre-independence era, arbitration was primarily governed by the Indian Arbitration Act, 1899, which was based on the English Arbitration Act of

1889. Then, after attaining independence in 1947, India embarked on a process of legal reforms, including the development of a modern arbitration framework. The Indian Arbitration Act, 1940 was enacted, replacing the earlier legislation. It introduced several improvements, but it still had certain limitations, such as lack of provisions for international arbitration. The most significant development in the evolution of arbitration in India came with the enactment of the Arbitration and Conciliation Act, 1996 that aimed to provide a comprehensive legal framework for domestic as well as international arbitration. This act is based on the UNCITRAL model of law i.e. United Nations Commission on International Trade Law.

2. INTRODUCTION

Chapter 5 of the Arbitration and Conciliation Act, 1996,[1] deals with the arbitral proceedings while arbitration agreement is defined in section 7 of the act which states that an "arbitration agreement is an agreement between two or more parties to submit their disputes arising out of a particular legal relationship or any future legal relationship to arbitration".[2] Being the initial footing of the arbitration proceedings, arbitration agreement is the driving force of the dispute mechanism altogether. An arbitration agreement or an arbitration clause both are treated as a separate contract from the main contract deriving its property from the doctrine of severability. However, the problem occurs when a non-signatory party is required to be involved in the arbitral proceedings. A non-signatory party is the one that is not a party to the main contract and thus has not signed or consented to the same. Therefore, the contention here arises when the main party to the contract refers arbitration to another party i.e. a non-signatory. Non-inclusion of the non-signatory party would ultimately be contrary to the principles of good administration of justice and would altogether hamper the ulterior motive of arbitration i.e. transparency and party autonomy. Moreover, it would also result in lack of efficiency of the whole process of arbitration whereas inclusion of the same could be treated as a ground for the refusal of an arbitral award, thus resulting in a major complexity.

3. THEORIES

In arbitration law, there are various theories that allow non-signatories to be bound by arbitration agreements:

1. Equitable Estoppel: This doctrine is largely based on the principles of fairness and equity and is rarely followed outside US courts. The theory of equitable estoppels is applies when

[1] Arbitration and Conciliation Act 1996 (26 of 1996), Chapter 5;
[2] Arbitration and Conciliation Act 1996 (26 of 1996), Section 7;

the non-signatory intends to avail itself of substantive rights under a contract with arbitration clause, it is estopped from denying that it is a party to the arbitration agreement. Courts observed two versions of this doctrine when adjudicating a non-signatory submission to an arbitral proceeding:

a) The first strand [Direct Benefit Theory]: The non-signatory parties are compelled to submit to arbitration when they have embraced the agreement and extracts benefit from it. Courts exercise the doctrine of estoppel to bind a non-signatory to arbitration that consciously exploits the agreement containing the arbitration clause.

b) The second strand: The Court by virtue of this principle, may grant a non-signatory party the powers to bind an unwilling signatory to arbitration, vice versa annex a 'willing' non-signatory to arbitration.

2. Alter-ego or piercing the corporate veil: According to this theory, even if there is a doctrine of separation between a corporation and its shareholders, officers and directors, the accountability of all of them would be as that of the corporation. Expansion of the arbitration agreement to a third-party is envisaged when a signatory party is found to address them, and such portrayal isn't only emerging out of being important for a corporate body under Group of Companies doctrine, and such arrangement was created to evade arbitration. Such strategies add up to a abuse of rights and privileges making exposure for piercing the corporate veil. Additionally, this doctrine is applicable in cases of abuse of rights and obligations of a natural or legal person. Therefore, courts and tribunals avoid applying this doctrine.
3. Agency: This theory applies in the situation where an agent executes a contract on behalf of a principal. Here, the view exists that an agent while entering into a contract on the behalf of a principal would be liable for all the actions as the agent would be. Although the principal being the non-signatory would have the same accountability. Mere natural parent-subsidiary relationship does not confer Agency privileges; therefore, the Agency relationship will only hold when it has been sculpted as a contract without any ambiguity. If an Undisclosed Principal is the beneficiary to an arbitration agreement executed by their Agent, they may enforce arbitration as a non-signatory, even though the signatory party was not apprised of their existence.[3] The appellate court in the English case of **Interbras Cayman Co. V Orient Victory Shipping Co.,**[4] passed judgement based on this principle.

[3]Aatisha Bhatia and Dipshi Swara, 'Compelling a non-signatory party to arbitrate', <https://blog.ipleaders.in/compelling-a-non-signatory-party-of-a-contract-to-arbitrate/> accessed on 20 July 2024;
[4] *Interbras Cayman Co. V Orient Victory Shipping Co., 509 F.Supp. 1067;*

4. Assignment: Where a transfer of rights and obligations have occurred like in cases of insurance contracts, mergers, acquisition etc., it is believed that an automatic transfer of the arbitration clause takes place, from the transferor to the assignee, thus observing all the rights and obligations by the latter.
5. 'Group of companies' doctrine: This doctrine derives its basis from the fact that separate legal entities within a corporation where it can be treated as a single unit. It requires ownership, control or unity of purpose.

   This doctrine was applied in a landmark case of **Dow Chemical v. Isover-Saint-Gobain,**[5]. It was held that this doctrine can be applied either in negotiation, conclusion or termination of a contract when formally another company is subject to the arbitration clause. Further, the common intention of parties must be examined and therefore, this doctrine is applied mostly by French courts and rejected by English courts. The doctrine is found to disobey the principles of Privity of Contract as one of the founding factors of any kind of commercial contract. Moreover, it fails to recognize the paramountcy of Free Consent in legal contractual relationships.

   On account of **Sukanya Holdings case**,[6] disputes emerged between a few parties in regards to the very exchange that was fraudulently executed a few times. These parties are not signatories to the arrangement subsequently can't be bound under the arbitration clause contained in the principal agreement. The Apex Court was satisfied that any non-signatory party can't be viewed as privity to arbitration, maintaining the essence of Section 8 of Arbitration and Conciliation Act,1996. It additionally highlighted that cause of action can't be subject of bifurcation, thus arbitration ought to be confined to the parties that have executed an agreement and also the involvement of parties are to be strictly contemplated. The judgment of **Chloro Controls Pvt Ltd v. Severn Trent Water Purgings Inc.,**[7] which depended upon the doctrine of Group of Companies, found precedence in the Cheran Properties judgment[8]. In this case, the contracting parties were Sports Pastime India Limited ["SPIL" - an subsidiary of Kasturi and Sons Limited and Ors] and KC Palaniswamy ["KCP"] and Hindcorp Resorts Pvt. Ltd., where the SPIL consented to transfer their shares to KCP and their chosen nominee, Cheran Properties Limited ["Cheran"]. The Section 35 of the Mediation and Mollification Act, 1996 makes arbitral awards binding upon parties and their relaatives, therefore, the arbitration agreement

[5] *Dow Chemical v. Isover-Saint-Gobain [1983] ICA , 110 J. Du Droit Int'l 899;*
[6] *Sukanya Holdings Pvt. Ltd. v. Jayesh H. Pandya & Anr. [2003], CLC 585 SC;*
[7] *Chloro Controls India (P) Ltd. v. Severn Trent Water Purification Inc. [2013] SC Civ Appeal 7134, [2012];*
[8] *Cheran Properties Ltd v. Kasturi and Sons Ltd. [2018] NCLT New Delhi Company Appeal (AT) 125, [2017];*

between the signatories becomes binding on Cheran by referring to the share-transfer agreement between KCP and Cheran.

Validity of this doctrine:

According to the 2021 ICC rules, this doctrine is followed when the obligations under article 7.5 are met. [9] According to 2021 Swiss rules, the requirement is the fulfilment of article 6.3 which asks to 'take into account all relevant circumstances'. [10] According to the latest SCC rules, this doctrine is restrictive and it requires the SCC to ensure that it does not lack jurisdiction over the dispute between the parties, including any additional party.[11]

4. ENFORCEMENT OF AWARD

In case of the involvement of non-signatories, ground for the refusal of enforcement of award arises. This can be backed by the absence of an appropriate arbitration agreement between the parties under article V (1)(a) of the New York convention.[12]

The refusal would be that as per Article V (1)(c) of the New York convention, award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration or contains decisions on matters beyond the scope of the submission to arbitration.[13]

5. PRESENT SCENARIO

The latest case on the issue of non-signatories is **Cox & Kings Ltd. v. SAP India Pvt. Ltd.,**[14] wherein a five-judge bench examined the doctrine of group of companies which states that an arbitration agreement made by a company within its group may extend to the non-signatories, provided that the surroundings suggest a relation between both signatories and non-signatories. Chief Justice D.Y. Chandrachud held that the concerned doctrine finds genesis in section 2(h) and 7 of the Arbitration and Conciliation Act, 1996.[15] In a contrary opinion, J. Narsimha held that this doctrine finds genesis in section 7(4)(b) of the act.[16] The court also described how a non-signatory can be bound by an arbitration agreement in **Chloro Controls India (P) Limited v. Severn Trent Water Purification Incorporation (2013).**[17] The court suggested certain factors to consider while determining the issue of non-signatories. These include the existence of a direct relationship

[9] International Chamber of Commerce 2021 (founded in 1919), article 7.5;
[10] Swiss Rules 2021, article 6.3;
[11] Stockholm Chamber of Commerce 2023 (was entered into force in 1917) SCC;
[12] New York Convention 1958 (entered into force on 11 October 1960) article V (1)(a);
[13] New York Covention 1958, Article V (1)(c);
[14] *Cox & Kings Ltd. V. SAP India Pvt. Ltd. [2020] SC Arbitration Petition Civ 38, [2020];*
[15] Ibid at 7;
[16] Arbitration and Conciliation Act 1996 (26 of 1996), S. 7 (4)(b).
[17] Ibid at 5;

with a signatory, subject-matter similarity and the existence of a composite transaction.

The points of criticism of the Chloro Controls include, failure to differentiate between consensual and non-consensual theories; the court contradicted itself indeed while it says that the non-signatory shall intend to be bound by the arbitration agreement as there are limited instances when it can be held bound without any prior consent. This contradiction was taken into account by J. Surya Kant where he noted that the ability to bind non-signatories is essential for maintaining the efficiency of arbitration.[18] Several other judgements dealt with the issue if non-signatories including: **Cheran Properties Ltd v. Kasturi and Sons Ltd. (2018),[19] Ameet Lalchand Shah v. Rishabh Enterprises (2018),**[20] **Reckitt Benckiser (India) Pvt. Ltd. v. Reynders Label Printing India Pvt. Ltd. (2019),[21]** and **Mahanagar Telephone Nigam Ltd. v. Canara Bank (2019).[22]**

> In **Discovery Enterprises (2022),[23]** Supreme Court held that there are multiple factors that are to be considered before binding non-signatories which include mutual intent, relationship between signatory and non-signatory, composite transaction, subject-matter commonality and the performance of contract.
>
> The Supreme Court, in Cox & Kings recognized that the non-signatories can be bound to the arbitration agreement by two ways: first, the consent-based path where a non-signatory party can consent in multiple ways while the second, non-consensual path which could involve piercing the corporate veil or theory of assignment and agency. The court held that group of companies is a consent-based doctrine and is independent in nature.

Power of the arbitral tribunal:

In the opinion of the court, it is wise for the tribunal to determine the involvement of non-signatories rather than court especially in the situations addressing section 8 and section 11 of the arbitration act considering the competence-competence mechanism. The court also beholds that courts may be referred to in some cases exercising judicial restraint and only to determine the validity of the arbitration agreement. It grants the non-signatory party to seek interim measures from the court under section 9. Further, the court noted that this doctrine would not preclude the

[18] Durga Priya Vanda & V.P. Singh, 'Binding non-signatories to arbitration-bringing India on par with international arbitration' (*Supreme Court Observer*, 27th December 2023) <https://www.scobserver.in/journal> accessed on 6th April 2024;
[19] Ibid at 6.
[20] *Ameet Lalchand Shah v. Rishabh Enterprises [2018] SC Civ 4690, [2018] SLP(C) No.16789 [2017];*
[21] *Reckitt Benckiser (India) Pvt. Ltd. v. Reynders Label Printing India Pvt. Ltd. [2019] 5 ALL WC 4263 [2019];*
[22] *Mahanagar Telephone Nigam Ltd. v. Canara Bank [2019] SC Civ 33, [2020];*
[23] *Oil & Natural Gas Corporation Ltd. v. M/S Discovery Enterprises Pvt. Ltd. [2022] SC Civ 2042 [2022].*

other theories (assignment, agency and novation) that are non-consensual and would bind the non-signatories to the contract.

In **Moneywise Financial Services v. Dilip Jain (2023),**[24] J. Jasmeet Singh referred to the case of Cox & Kings while addressing the issue. It was held that the claims related to company are arbitrable even though it is found that it is a non-signatory to arbitration agreement. A non-signatory party's active involvement in the performance of commercial and corporate obligations that are linked to the underlying subject-matter will eventually symbolise that firstly, it intended to be bound by the arbitration agreement and secondly, it is not an alien to the dispute amid the signatory parties.

6. MECHANISMS FOR BINDING A NON-SIGNATORY

There are three mechanisms for binding a non-signatory: joinder, consolidation and intervention.

1. Joinder: Joinder or Extension is a method for third-party incorporation ratified by a unique party to a pending arbitration proceeding or post-commencement of proceedings. The third-party might be joined as a supplementary respondent at a later phase of arbitral procedure. On consenting to a bi-party arbitration, the third-party presence synthesises the arbitration into a multi-party proceeding. Joinder is a mechanism coherent to the Group of companies doctrine. Additionally, joinder is allowed under the principle of Equitable Estoppel. Joinder effectuates when the all-signatory parties to arbitration have consented unanimously. Moreover, where the third-party has consensually submitted to be bound vide joinder, the intercession which in any case has capacity to volatilize the process of arbitration, ceases to jeopardize the enforceability of the arbitral award; though a joinder that doesn't have endorsement of either any of the signatory or the third-party might deliver contradicting results.
2. Consolidation: Alternative Dispute Resolution is pivoted in conveying speed redressal; accordingly, it sends procedural tools to dismiss parallel or successive fragmented arbitrations in attempts to accomplish redressal and decide claims collectively. Consolidation is an approach to incorporating interrelated two-party, one-guarantee cases into one conglomerate case. The union is given solely after the cases have been recorded independently. The course of consolidation is seen to be financially effective and an astounding mechanism to dodge contradictory outcomes. Factors like the governing law of the particular seat of arbitration, the essentials in the arbitration clause agreed by both

[24] *Moneywise Financial Services v. Dilip Jain [2023] Arb. P. 702 [2023].*

the parties, and the principles of the arbitral institution - impact the consolidation of arbitration.

3. Intervention: The predominance of multi-party transactions and their related complex discrepancies have made third-party intervention unavoidable. Such intervention is nonetheless unorthodox in the course of litigation but in extraordinary situations, a third-party may be given limited rights of intervention, provided the said right is expressly permitted. A willing non-signatory will request joinder to arbitration alone, either prior or post-commencement of the proceedings.

7. CONCLUSION

In India, the family business culture is one of the reasons that it is essential to include non-signatory parties for effective dispute mechanism. In such cases, it is common to involve certain entities in the negotiations of a contract and others in execution and performance as in many large-scale infrastructure projects. The factual conduct laid down by the courts determine that a non-signatory should have a direct and substantial interest involved in the negotiation, performance or termination of the contract and thus results in incidental involvement as insufficient. Furthermore, the burden of proof is on the party that seeks to join the non-signatory in the contract to prove conscious involvement of the non-signatory on the basis of objective evidence. The arbitral tribunals must be given more power in terms of determining the contended scenarios and assessment of facts from case-to-case. However, the Supreme Court has somewhat managed to weave in sufficient flexibility in maintaining the balance and on the approach of binding non-signatories.

Prof. S. Brekoulakis stated, we should try to reach "a more consistent, more inclusive, and eventually, intellectually more honest approach to non-signatories", in order to achieve greater efficiency and coherence of the arbitral process. With respect to this statement of learned professor, we can conclude that this emerging issue requires a balance between the consensual nature of arbitration and modern reality wherein the non-signatory parties are constantly implicated in commercial and corporate matters in order to maintain the effectiveness of the arbitration procedure.[25]

[25] Merrills, J.G Journal of International Dispute Settlement, 1(8) (2018), pg 1-34.