CMR UNIVERSITY
Private University Estd in Karnataka State by Act No. 45 of 2013
SCHOOL OF LEGAL STUDIES

CMR University Journal for
Dispute Settlement and Arbitration
Vol. 3 (01), June 2024, PP. 182-187

Cheran Properties Ltd. v. Kasturi & Sons Ltd. & Ors. (2018) 16 SCC 413

Dibyangana Nag*

Introduction

The 1996 Arbitration and Conciliation Act, referred to as the "A&C Act", is a fundamental regulation of arbitration in India. This Act encourages the inclusion of an arbitration clause in legally binding contracts, which provides for a dispute resolution mechanism using arbitration. To initiate arbitration proceedings, the presence of such a clause constitutes evidence of the intention of the Parties to submit to arbitration. The parties to the agreement are legally bound by this provision. However, the arbitration agreement may also be binding on third parties which are not signatories. The Hon'ble Supreme Court of India, in the case of Cheran Properties Limited v. Kuzuri and Sons Limited and Or Kasts, dealt with this specific issue by shining a light on the enforceability of an arbitration agreement against non-signing parties. In the present case, a three-judge panel, chaired by Justice Deepak Mishra, also clarified the competence of the NCLT to award arbitral awards relating to the transfer of shares through the rectification of the register of members.

Background and Arguments

The disputed contract under consideration was the Share Purchase Agreement finalized on July 19, 2004, involving KC Palanisamy ("KCP"), Kasturi & Sons Limited ("KSL"), Sporting Pastime India Limited ("SPIL"), and Hindcorp Resorts Pvt. Ltd. ("Hindcorp"). In this agreement, SPIL, a

* *Student of VIII Semester, B.A., LL.B. (Hons.), School of Legal Studies, CMR University*

subsidiary of KSL, was mandated to allot 240,000 fully paid-up equity shares to KSL against outstanding book debts. Concurrently, KSL proposed to sell 243 equity shares, constituting 90% of SPIL's total paid-up share capital, to KCP or his nominees, for a total consideration of Rs. 2,31,50,000.

The agreement explicitly delineated the parties' intentions, stating that KCP would assume control of SPIL's management post the share transfer, and existing liabilities would be settled effective from the agreement date. Additionally, the agreement stipulated that KCP and its nominees, including the appellant Cheran Properties Limited, held the right to sell or transfer their SPIL shares. A pivotal condition stipulated in the agreement is that the transferees must agree to the terms concerning SPIL's management and its financing. KCP then sent a letter to KSL on August 17, 2004, in which it invoked the agreement and asked for its shares to be transferred to KCP and its nominees. As part of the share consideration, the letter included a draft demand of 2.43 crores. KCP did not fulfill certain obligations laid down in the agreement despite the transfer of the shares by KSL to KCP and other designated parties. Furthermore, an arbitration clause was included in the contract. Accordingly, the arbitration clause was invoked by KSL and Hindcorp, which initiated proceedings against KCP and SPIL.

The Arbitral Tribunal rendered its award on December 16, 2009, specifying that KCP and SPIL were to return the title documents and share certificates of SPIL to KSL and Hindcorp. On the other hand, KSL was ordered to pay back the share consideration with additional interest. In both the Madras High Court and later in the Supreme Court, KCP's appeal against that award was dismissed. Opting to explore all available remedies, KSL approached the National Company Law Tribunal (NCLT) seeking rectification of SPIL's register under Section 111 of the Companies Act, 1956, which provides that if a company unreasonably refuses the legitimate transfer of shares, that provision provides for an appeal. The application to the NCLT aimed to facilitate the return to KSL of the shares held by the appellant, identified as KCP's nominee, under the arbitral award. NCLT granted the application, and this decision was upheld by the National Company Law Appellate Tribunal (NCLAT) and the Madras High Court upon appeal. Both the tribunal and the High Court maintained that the appellant's purchase of shares (Cheran) was not an independent right but rather a nominee of KCP. Consequently, the award could be enforced against the appellant. Dissatisfied with this ruling, the aggrieved appellant sought relief from the Supreme Court, challenging the NCLAT's order in the discussed case.

Issues Before the Supreme Court

Two important legal issues were pending before the Supreme Court of Justice. In the first place, the Court had to determine whether an arbitral award could be binding on a non-signatory third party who did not participate in the arbitration proceedings. The second issue concerns whether a proceeding before NCLT for enforcement of an arbitral award can take place. In particular, it was necessary to determine whether the NCLT has jurisdiction for the enforcement of an arbitral award relating to a transfer of shares through rectification of the register of members.

Judgment

The Supreme Court of India dismissed Cheran Properties Limited's appeal against the arbitral award, holding that the award was binding on Cheran even though it was not a signatory to the shareholder agreement containing the arbitration clause. The Court also ruled that the National Company Law Tribunal (NCLT) was the appropriate forum for enforcing the award, which dealt with the transfer of shares. The Supreme Court of India clarified the circumstances under which the terms of an agreement may bind non-signatory parties to an arbitration agreement in a landmark decision. The Court's ruling, which drew upon its earlier judgment in Chloro Controls Pvt. Ltd. v. Severn Trent Water Purification Inc[1], ("Chloro Controls"), established three categories of relationships under which a non-signatory can be considered a "person claiming under" and thus bound by the arbitral award.

- **Category 1:** Third-Party Beneficiaries, Guarantors, and Assignments

[1] Chloro Controls Pvt. Ltd. v. Severn Trent Water Purification Inc, (2013) 1 SCC 641.

In the first category, the relationship between the signatory and the non-signatory is based on implied consent and good faith. This category encompasses third-party beneficiaries, guarantors, and assignments.

- **Category 2:** Agency, Apparent Authority, Piercing the Veil, Joint Ventures, Succession, and Estoppel

  Relationships based on the force of the applicable law are included in the second category. These include agency, apparent authority, piercing the veil, joint venture relations, succession, and estoppel. This category encompasses various legal concepts, including agent and principal relationships, apparent authority, piercing of the veil, joint venture relations, succession, and estoppel. The force of the applicable law underpins these concepts.

- **Category 3:** The Group of Companies Doctrine

  The Group of Companies Doctrine refers to situations where there are agreements between several entities within a single corporate group. Following that doctrine, where there is evidence of a mutual intention between the parties to bind signatories and non-signatories, a nonsignatory affiliate may be bound by an arbitration agreement entered into by another company within the group. It is worth noting that this English doctrine has been adopted by Indian courts to bind non-signatory parties to arbitration agreements, which will gradually expand its scope in India's arbitration. If there are multiple parties to an agreement, this doctrine shall apply.

The court determined that the transfer of shares from KCP to its nominees, including Cheran, was contingent upon the condition that nominees would adhere to the terms of the share transfer agreement. Consequently, Cheran could not argue against being bound by the arbitration agreement or the award. The court highlighted Section 35 of the Arbitration and Conciliation Act, which states that an arbitration award is binding on parties and those claiming under them, Given Cheran's status as a nominee of KCP and being subject to the share transfer agreement, the court considered Cheran as having the same legal standing as KCP and thus bound by the award under Section 35 of the Act.[2]

Citing Sundaram Finance Limited v Abdul Samad[3], the Court concluded that enforcement proceedings could be initiated anywhere in the country where the judgment debtor's assets are situated. Additionally, the Court affirmed that seeking NCLT intervention for the registration of share transfers and rectification of the register under Section 111 of the Companies Act was not only appropriate but also necessary to implement the transfer of shares.

The Supreme Court emphasized the crucial role of mutual intention in determining whether an arbitration agreement binds a non-signatory. The legal basis for extending the terms of the arbitration agreement to non-signatories within the corporate group is this mutual intention.

Analysis of the Judgment

The judgment of the Supreme Court has significant implications for the practice of arbitration in India. The Court has given greater flexibility in terms of binding non-signatories to arbitration agreements, particularly in complex commercial transactions involving multiple parties by expanding the scope of the "group of companies" doctrine. It is expected that, as an alternative to traditional legal proceedings, this decision will facilitate dispute settlement procedures and improve the effectiveness of arbitration.

To ascertain the mutual intention within the contractual framework, encompassing the relationship of a third party with the signatory party, the courts must consider various factors, including the similarity of subject matter and its composite nature. In a specific instance, the court ruled that Cheran was a 'party claiming under' KCP, thereby rendering the arbitral award binding on the

[2] Naval Sharma and Saket Satapathy, *Supreme Court: An Arbitration Award Can Be Enforced At The NCLT*, MONDAQ (May 14, 2018), https://www.mondaq.com/india/arbitration--dispute-resolution/701306/supreme-court-an-arbitration-award-can-be-enforced-at-the-nclt#_ftn4.
[3] Sundaram Finance Limited v. Abdul Samad, AIR 2018 SC 965.

appellant as per Section 35 of the Act. Notably, the shareholder agreement of July 19, 2004, stipulated that KCP would receive an equity interest in KSL and assume management and financial responsibilities for SPIL. This indicated a shared intention between the parties. Furthermore, KCP, as the authorized signatory, affirmed in its letter of August 17, 2004, that its group of companies had consented to purchase shares in SPIL. Additionally, the appellant Cheran, acting as a nominee and transferee, accepted the terms of the agreement, further signifying mutual intention. In essence, by applying the 'group of companies doctrine' and Section 35 of the Arbitration and Conciliation Act, 1996, the court determined that the appellant fell within the purview of "persons claiming under them," thereby binding them to comply with the arbitral award.

Conclusion

The effectiveness of such an Alternative Dispute Resolution Mechanism, which is intended to reduce the burden placed on the traditional dispute settlement system, will be hindered by its inherent difficulty in enforcing an arbitral award. The Supreme Court of India's judgment in this case is an excellent example of a promising step to improve the efficiency of arbitration by allowing award proceedings against non-signatory parties who are part of the company that signed the arbitration contract. In addition, the Court recognized the appropriate forum for the enforcement of arbitral awards relating to the transfer of shares as the National Company Law Tribunal NCLT. In the context of modern commercial transactions, which often involve complex structures and multiple parties, this is particularly relevant.