
(2005) 08 MAD CK 0013
In the Madras High Court
Case No : O.A. No. 46 of 2005

Samayanallur Power Investment Pvt. Ltd.	APPELLANT
Vs	
Covanta Energy India (Balaji) Ltd. and Another	RESPONDENT

Date of Decision : 12-08-2005

Acts Referred:

Arbitration Act, 1940 — Section 9

Citation : (2005) 08 MAD CK 0013

Hon'ble Judges : R. Balasubramanian, J

Bench : Single Bench

Advocate : P. Arvind Datar, for Satish Parasaran, for the Appellant; P.S. Raman, for the Respondent

Judgement

R. Balasubramanian, J.—This is an application u/s 9 of the Arbitration Act seeking certain reliefs pending commencement of the arbitral

proceedings. For brevity sake, in this order I will refer to the applicant as AC (applicant-company); the first respondent as BC (B company) and

the second respondent as HC (holding company). There is yet another company called ""Madurai Power Corporation Ltd."" and it would be called

as MPCL. As on date AC and BC are parties to a shareholders agreement dated April 25, 2000. The shareholders agreement relates to MPCL.

The shareholding pattern in MPCL by AC and BC is defined as 23.36 per cent, and 76.64 per cent. There is a memorandum of association for

MPCL. BC is a wholly owned subsidiary of HC. BC was formerly known as Ogden. Clause 8.3 of the shareholders agreement reads as

hereunder :

8.3. Transfers by Ogden.--Subject to Sections 8.1,1.3 and 11.4, in the event that Ogden desires or is required to sell, transfer or otherwise

dispose of any or all of its shares, it shall offer such shares in the first instance by an offer notice to the other shareholders (the "remaining parties")

in proportion to their respective shareholdings in the company at a place which a third party has offered to pay for such shares. The remaining

parties may exercise their right of first refusal to purchase such shares within a period of thirty (30) days after receipt of the offer notice. In the

event that one or more of the shareholders rejects the offer, the other shareholders may agree to accept such sale shares in proportion to their

respective shareholdings in the company. If the offer is accepted then Ogden and the remaining parties shall proceed to complete the sale and

purchase of the shares within a period of thirty (30) days from the date of acceptance. In case the remaining parties reject the said offer, then

Ogden shall be entitled to sell such shares to a third party within a period of thirty (30) days from the date of rejection on the same terms and at a

price not lower than the price at which such shares were offered to the remaining parties.

2. The same clause finds incorporated as Article 44 in the Articles of association of MPCL. AC has come before this Court complaining that BC is

attempting to transfer its shareholding in MPCL in violation of Clause 8.3 of the shareholders agreement corresponding to Article 44 of the Articles

of association. Apprehending such violation, AC wants to restrain the respondent from proceeding with the proposed alienation of interest in

MPCL either by sale of the holdings of HC in BC or EC's holdings in MPCL without affording to AC the exercise of its right of first refusal as per

the contractual terms extracted earlier.

3. Mr. P. Arvind Datar, learned senior counsel is appearing for AC, His submission is that, there is a binding shareholders agreement between AC

and BC as on date under which AC has a right of pre-emptive purchase of the shares held by BC in MPCL. The Articles of association are

binding between the parties as a contract. It has the force of law. AC and BC are not only parties to the shareholders agreement but also are

bound by the Articles of association. BC is a wholly owned subsidiary of HC and though in law BC may be treated as a separate legal entity, yet it

is seen that the affairs of BC are totally controlled only by HC. In other words, his submission is that, BC has no independent authority to take any

decision on its own and they are out and out guided only by HC. Though in law HC and BC may be different legal entities, yet this Court, on the

facts available, would be in a position to hold that BC and HC constitute a single economic unit and therefore all the rights and obligations of BC

under the Articles Of association, especially in the context of transfer of their shares in MPCL, are equally binding on HC. If what BC under the

shareholders agreement and the Articles of association cannot do, namely, without giving a right of first refusal to AC, then on the principle of single

economic unit, HC also cannot do what BC cannot do.

4. Mr. P.S. Raman, learned senior counsel appearing for the respondents would submit that HC is not bound by the rights and obligations of BC.

It is true that BC is a wholly owned subsidiary of HC. HC is not attempting to transfer the shares held by BC in MPCL but on the other hand, HC

is only trying to transfer the entire entity namely, BC, owned by it. Therefore, when HC exercises such a right available to it as a owner, AC cannot

obstruct such a lawful exercise of right by HC. In other words, according to Mr. P. S. Raman learned senior counsel, by the intended sale by HC

of its assets in India namely, its wholly owned subsidiary, i.e., BC, no transfer of shares of BC in MPCL is involved but transfer of ownership alone

is involved. According to him, if the intended sale is put through, there is no variation in the shareholding pattern in MPCL and it remains the same,

since the successful buyer would get substituted for BC in the shareholders agreement as well as in the Articles of association. Under these

circumstances, HC, as the owner of its assets, cannot be prevented by an order of court from selling its assets, which it does in its lawful exercise

of power as the owner thereof. It is then submitted that though BC may be a wholly owned subsidiary of HC, yet, BC acts on its own authority as

a separate legal entity with no control whatsoever from HC. "Therefore, whatever rights and obligations BC has contracted for in exercise of its

independent authority, HC cannot be burdened by having those rights and obligations of BC telescoped into HC. Mr. P. S. Raman, learned senior

counsel, then submitted that it is not as though the move made by HC to sell BC had been done in a clandestine manner. But on the other hand,

transparency is writ large in the move of HC, especially when it had sent the confidential information memorandum, in short called as CIM,

worldwide including AC. In response to CIM, AC participated and submitted its bid ; such bid was analysed; accepted by HC and the parties

have gone to the second stage of consideration. Therefore, AC cannot be allowed to complain now, after participating in the bid as referred to

above, that the pre-emption clause is violated. It is then submitted that AC cannot now be allowed to fall back upon the pre-emption clause and

bring the act of HC to a grinding halt. In answer to this, Mr. P. Arvind Datar, learned senior counsel, would submit that AC submitted its letter of

intent in response to CIM believing that it is for getting transfer of shares of BC in MPCL and only later on, AC had come to know that HC and

BC are trying to violate the pre-emptive clause.

5. Let me now consider the case of the respective parties in the light of the arguments advanced. I have already extracted Clause 8.3 in the

shareholders agreement, which corresponds to Article 44 of the Articles of association. It does confer a pre-emptive right on AC. But such pre-

emptive right does not appear to be absolute namely, whatever may the situation, AC must be given the right to buy the shares of BC in MPCL. In

fact, the submission of Mr. P. Arvind Datar, learned senior counsel, itself is that, an ""offer notice"" given by BC to AC in the event of it deciding to

transfer its shares in MPCL, AC fails to match the price that may be offered by a third party for such transfer of shares, then BC can deal with the

transfer of shares in favour of a third party. It is clear from the clause referred to above that if BC decides to transfer its shares in MPCL, it shall

give the first offer to AC informing of the price which a third party offers to it in respect of such transaction and if AC matches that offer, then alone

AC has the right to get the shares transferred to it. Otherwise it loses its right. To my mind, one way of getting the best price from a third party

would be to advertise the transfer of shares which BC has in MPCL. Therefore, there is an inherent right in BC itself to advertise the transfer of

shares it holds in MPCL ; get offer from third parties and then put it across to AC to find out its response. From the light of the discussion as

referred to above, I have no doubt at all that AC has no right to compel BC to transfer the shares which it has in MPCL to it at a price as it may

offer, de hors the price which a third party may offer. Therefore, it is clear that the pre-emptive clause in favour of AC is a qualified pre-emptive

clause. Radhakisan Laxminarayan Toshniwal Vs. Shridhar Ramchandra Alshi and Others, , the Supreme Court held that there are no equities in

favour of a pre-emptor. It refers to an earlier judgment of the Supreme Court in the case reported in Bishan Singh and Others Vs. Khazan Singh

and Another, , where the Supreme Court held that ""the right being a very weak right, it can be defeated by all legitimate methods ...

6. Let me now examine the issue as to whether HC is bound by the rights and obligations of BC ? I have already found and it is not in dispute that

BC is the wholly owned subsidiary of HC. The Hon"ble Supreme Court of India in a long line of decisions had settled the power of the court to lift

the corporate veil for the purpose of finding out whether a group of companies in operation or when there is a relationship of holding

companies/subsidiary companies would constitute a single economic unit or do they operate on their own in their own sphere without any control

from the other. Therefore, I am of the opinion that this Court would not be committing any error at all in finding out whether HC and BC, though in

law they are separate legal entities, constitute a single economic unit ? In this context, I applied my mind to certain materials available on record.

HC had issued the CIM dated September 13, 2004. Under the caption ""important notice"", the following is found disclosed :

HC owns power assets and operations in China, India and Bangladesh ; the recipient of the CIM must make its own investigation and assessment

of the assets in the CIB portfolio (China, India and Bangladesh).

7. MPCL is one of the power projects. The other one is at Samalpatti. The major shareholder in MPCL power project is BC and AC holding the

remaining shares. From the memorandum of association of MPCL it is seen that one of the objects is to carry on the business of conventional

electricity generation as well as non-conventional power generation. MPCL has other objects as well. Therefore, it is clear that the business of

MPCL is in the hands of the board of directors consisting of members of AC and BC. In the constitution of the board of MPCL, HC, has no say.

But from the clause in CIM issued by HC and as extracted above, HC claims to be the owner of MPCL along with the other power projects. HC

holds 100 per cent, shares in BC and BC holds 76.24 per cent, shares in MPCL. In the CIM issued by HC (see paragraph 1.1 under the heading

Executive Summary) where HC claims that it is the owner and operator of various power projects located in China, India, etc. . . It is also seen

from there that HC had declared that BC ; MPCL and the operating company ""Coventa Madurai Operating Pvt Ltd,"" are for sale. HC has also

declared in that context that the buyer would have the opportunity to acquire either the whole or individual assets--the asset being the power

project. It is not in dispute that HC completely owns BC and BC alone has 76.24 per cent, shares in MPCL. Of course, it is also seen from

paragraph 1.1 referred to above that HC had declared that it is seeking to sell 100 per cent, of its interest in the Mauritius holding companies--BC

being one such company. When by the intended sale, BC tries to get out of its contractual obligations, in my opinion a need arises to lift the

corporate veil. Justice D. P. Wadhwa, as his Lordship then was, constituting a Division Bench, in the case of M/s. New Horizons Limited and

another Vs. Union of India and others, , quoted with approval the law on the subject as found in Palmer's Company Law (25th edition). The

following are a few of the instances in which, as could be seen from the above referred to judgment, the corporate veil can be lifted.

(a) where the business affairs of both the parent company and subsidiary are intertwined and the business transactions, property, bank and other

accounts, employees, management, etc., are intermingled ;

(b) where the subsidiary is inadequately financed as a separate business as regards meeting its formal obligations ; and

(c) where the parent company and the subsidiary are operating portions of a single business and the financing as well as the managerial activities

come from the holding or parent company.

8. In Ramaiya on Companies Act, 15th edition, it is found stated as follows :

The modern tendency is that in the case of groups of companies, where there is identity and community of interest between companies in the

group, especially where they are related as holding company and wholly owned subsidiary of subsidiaries, to ignore that separate legal entity and

look instead at the economic entity of the whole group.

9. From the materials on record, it is seen that HC has a number of companies in China, India and Bangkok and HC itself appears to be a wholly

owned subsidiary of a company in the United States. Therefore, there are

enough room to legally infer that HC and BC constitute a single economic unit and in my opinion, the cat is out of the bag. It is the contention of Mr. P. Arvind Datar, learned senior counsel, appearing for AC that though BC may be treated as a separate legal entity, yet for all practical purposes, BC is constituted as a special purpose vehicle by HC for investment in India (BC having its registered office at Mauritius), so as to avail of the tax benefits available in that country. From the materials noted above, it is not possible to brush aside the said argument. BC is definitely not the power project and it only has major shares in MPCL. Therefore, when HC says that it is the owner of the power project, then it must be held, as contended by Mr. P. Arvind Datar, learned senior counsel, that the activities of BC are totally controlled by HC. In MPCL, BC has a shareholding of 76.64 per cent, only and the balance is with AC. By the intended transfer of BC as an entire entity, the shareholding of BC in MPCL is attempted to be transferred. Since this Court is of the view that HC and BC constitute a single economic unit, the argument of Mr. P. Arvind Datar, learned senior counsel, appearing for AC that if what BC cannot do, HC also cannot do (in the context of transfer of shares in violation of Clause 8.3 of the shareholders agreement corresponding to Article 44 of the Articles of association), deserves acceptance. There is nothing on record to show that BC, except being constituted as a special purpose vehicle to invest in MPCL, has any other activities. Therefore, without any hesitation, I conclude that though HC and BC are two separate legal entities by themselves, yet they constitute a single economic unit. If that is the legal position, then the rights and obligations of BC under the shareholders agreement and the Articles of association is binding on HC, which means, HC also cannot violate Clause 8.3 of the shareholders agreement corresponding to Article 44 of the Articles of association.

10. The next question that follows is, whether AC can, in exercise of its power of pre-emption available under the contracts referred to earlier, preempt the respondents from proceeding with the intended action complained of in this application ? At this stage, I am proceeding on the basis of the legal premise that the second respondent is amenable to the jurisdiction of this Court u/s 9 of the Arbitration Act. In other words, I make it clear that in deciding the above referred to issue, namely, whether AC can

enforce its pre-emptive right, I am not deciding legally as to whether this application filed u/s 9 of the Arbitration Act is maintainable against HC and I leave it open to be decided later, if necessity arises. A pre-emption clause is a contractual term. It is needless to state that a party to any contract, in whose favour there is a beneficial clause, is at liberty to waive that clause provided, such waiver is not against public policy. In the earlier portion of this order, I have already referred to the judgment of the Supreme Court in the case reported in Radhakisan Laxminarayan Toshniwal Vs. Shridhar Ramchandra Alshi and Others, and Bishan Singh and Others Vs. Khazan Singh and Another, , which lay down that there are no equities in favour of a pre-emptor and the pre-emptive right being very weak right, it can be defeated by all legitimate methods. Under the CIM issued by HC, an information is made available to all interested to bid for the projects mentioned therein, which includes MPCL. AC, in response to that CIM, had given its intent letter dated October 14, 2004. CIM and the letter of intent referred to above are in the paper book furnished by AC itself. Under that letter of intent, AC had expressed its offer to buy 100 per cent, shares of BC, which in turn owns 76.64 per cent, of shares in MPCL and 99.808 per cent, shares of the operating company, which AC had collectively referred as ""Madurai Power"" or the ""company"" on the terms and conditions to be mutually agreed upon. Therefore AC had offered to purchase the entire shares of HC in BC and 99.808 per cent, shares of HC in the operating company. AC had also in that letter mentioned about the advantages of HC accepting AC's offer on the stated grounds therein, which includes, ""no delay due to first right refusal procedure"". AC had also, in the form enclosed described as ""form of indication of interest"" stated as follows :

(i) CPIH targets to be bought : (i) 100 per cent, of the shares of Covanta Energy India (Balaji) Ltd. which owns 76.64 per cent, of the shares of Madurai Power Corporation Pvt. Ltd., and (ii) 99.808 percent, of the shares of Covanta Madurai Operating Pvt. Ltd.

11. In the context of HC declaring in CIM that it is inclined to sell its power "

project (MPCL) and the terms of offer made by AC in the letter of intent that it proposes to acquire 100 per cent, of the shares of BC it can be said that AC proposed to buy the entire interest of HC in BC and not the interest of BC in MPCL. In any event, such a legal inference is not totally shut out, though in the later part of the "form of indication of interest under the heading "Acquisition Structure" it stands indicated that AC has an alternate, would cause the buy back a part of the shares of MPCL held by BC. In fact, such an alternate offer would reinforce this Court's conclusion that AC proposed to buy the entire interest of HC in BC to start with.

12. If this is the position, which can be legally inferred, then cannot AC be deprived of its pre-emptive right on the principle of waiver ? The law on waiver" had been dealt with in a number of judgments by the Supreme Court. I have already stated that the pre-emptive clause is like any other clause in an ordinary contract and a party, having the benefit of such a contract, can waive it. Associated Hotels of India Ltd., Delhi Vs. S.B.

Sardar Ranjit Singh, , the Supreme Court had laid down the principle as hereunder (page 937) :

A waiver is an intentional relinquishment of a known right. There can be no waiver unless the person against whom the waiver is claimed had full knowledge of his rights and of facts enabling him to take effectual action for the enforcement of such rights.

13. Motilal Padampat Sugar Mills Co. Ltd. Vs. State of Uttar Pradesh and Others, , the Supreme court had an occasion to deal with the same principle and I extract hereunder as to what the Supreme Court said in that judgment (page 338) :

"Waiver" means abandonment of a right and it may be either express or implied from conduct, but its basic requirement is that it must be "an

intentional act with knowledge" per Lord Chelmsford L.C. in Earl of Darnley v. London Chatham and Dover Rly. Co. [1867] 2 HL 43 57. There

can be no waiver unless the person who is said to have waived is fully informed as to his right and with full knowledge of such right, he intentionally

abandons it. It is pointed out in Halsbury's Laws of England (4th ed.), volume 16 in paragraph 1472, at page 994, that for a "waiver to be

effectual it is essential that the person granting it should be fully informed as to

his rights" and Isaacs J., delivering the judgment of the High Court of Australia in *Craine v. Colonial Mutual Fire Insurance Co. Ltd.* [1920] 28 CLR 305 has also emphasised that waiver "must be with knowledge, an essential supported by many authorities". Therefore the law of "waiver" is well-settled.

14. Now, this Court has to decide whether on the principle of "waiver", AC can be denied its right? From the contents of CIM referred to in this

order, it is clear that HC wanted to sell its power project, meaning MPCL, among others. AC had submitted its proposal to buy the said power

project. AC is fully aware of its right of pre-emption. It has knowledge about its right of pre-emption. In the letter of intent submitted by AC, it had

made it clear that one of the advantages in accepting its offer is that there would be "no delay due to first right refusal procedure". That procedure

is as per Clause 8.3 of the shareholders' agreement corresponding to Article 44 of the Articles of association. Therefore, with eyes open and

knowing fully well what its rights are, including the pre-emptive right, AC had submitted its proposal to buy the entire interest of HC in BC. HC

accepted the letter of intent given by AC and moved the parties to the second stage. By letter dated December 13, 2004, HC informed AC that

the deadline for final bid submission stands moved to January 28, 2005. AC filed this application before this Court only on January 24, 2005. This

is after the disclosed schedule dated January 11, 2005, sent by HC to AC. In the affidavit filed in support of the application, AC has stated that its

letter of intent is to acquire the balance shares in MPCL only, which prima facie is contrary to the letter of intent itself. AC has stated in paragraph

No. 8 of the affidavit that "it believed that its right of first refusal and purchasing the shares of MPCL would remain unaffected and that it was

interested only in getting the controlling stake in MPCL and not interested in the other assets that were offered for sale". These averments are

contrary to the details available in CIM and the contents of the letter of intent. AC had stated in paragraph No. 10 of its affidavit that only after the

e-mail dated December 13, 2004, already referred to in this order, it had come to know what exactly is the subject of the intended transfer. I have

already found that AC, knowing the contents of CIM very well; knowing its rights under the pre-emption clause and with full knowledge of the

property offered for sale, participated in the said transaction. By such conduct, AC had waived its pre-emptive rights. Therefore I have no hesitation at all to hold that there cannot be any order at all in favour of AC as prayed for. I must also place on record that neither of learned senior counsel addressed arguments before this Court pin pointedly on the issue of ""waiver"". The argument of Mr. P. S. Raman, learned senior counsel, appearing for the respondent to the effect that the applicant having participated in the bid cannot complain of any violation of rights, could be traced only to the plea of ""waiver"". I do find from the applicant's affidavit filed in support of the application that they had taken a stand that under the belief that their right of pre-emption would stand protected, they submitted their letter of intent. Therefore, there cannot be any doubt that there are pleadings on either side touching on the plea of ""waiver"". Since the issue on ""waiver"" can be decided on the pleadings available, I have taken it up as an issue and decided.

15. Since the pre-emptive right claimed by AC in this application is found against it on the basis of waiver, I am not deciding the question whether this application u/s 9 of the Arbitration Act is maintainable or not against HC, which claims that it is not a party to the arbitration agreement and I leave that question open.