

ENFORCEABILITY OF ARBITRATION AGREEMENTS ARISING OUT OF UNSTAMPED OR INSUFFICIENTLY STAMPED CONTRACTS

INTRODUCTION

A seven-judge bench of the Hon'ble Supreme Court ("**Second Constitution Bench**") in *In Re: Interplay between Arbitration Agreements under the Arbitration and Conciliation Act 1996 and the Indian Stamp Act 1899* ("*In re: Interplay*") conclusively answered the issue regarding the enforceability of arbitration agreements contained within unstamped or insufficiently stamped contracts.

The Second Constitution Bench unanimously held that even though such agreements are inadmissible in evidence under Section 35 of the Indian Stamp Act, 1899 (the "**Stamp Act**"), they cannot be rendered *void* or *void ab initio* and once the non-stamping or inadequate stamping is cured, the arbitration agreement contained within the contract can be enforced.

Accordingly, the Second Constitution Bench overturned the majority judgment in *N.N. Global Mercantile Private Limited v. Indo Unique Flame Limited*, (2023) 7 SCC 1 ("**NN Global II**"/"**First Constitution Bench**") which had held that an arbitration agreement contained in an unstamped/inadequately stamped agreement is *void ab initio* and therefore cannot form the basis for constituting an arbitral tribunal

The Second Constitution Bench found that a referral court cannot refuse to refer parties to arbitration under section 8 or 45 of the Arbitration and Conciliation Act, 1996 (the "Arbitration Act") or refuse to appoint an arbitrator under section 11 of the act and then proceed to impound the contract on the ground that it is unstamped or inadequately stamped.



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Post this judgment, the role of the referral court has been curtailed to examining on a prima facie basis the existence of the arbitration agreement under section 7 of the Arbitration Act while leaving all other preliminary issues, including on stamp duty, to the arbitral tribunal.

JUDICIAL HISTORY

A brief history of the judicial authorities leading up to the reference to the Second Constitution Bench is given below.

In *SMS Tea Estates (P) Ltd. v. Chandmari Tea Co. (P) Ltd.*, (2011) 14 SCC 66 (“**SMS Tea**”), a Division Bench of the Supreme Court held that, considering Section 35 of the Stamp Act, which bars the unstamped contract from being admitted in evidence, the arbitration agreement contained in such an instrument will consequently be unenforceable. This allowed courts to interfere at the referral stage and impound contracts before the arbitral tribunal could be constituted.

This position was affirmed in *Garware Wall Ropes Ltd. v. Coastal Marine Constructions & Engg. Ltd.*, (2019) 9 SCC 209 (“**Garware Wall Ropes**”) where another Division Bench of the Supreme Court went on to state that an arbitration agreement in an unstamped contract would be non-existent in the eyes of the law and unenforceable until the underlying contract was duly stamped.

The three-judge bench in *NN Global Mercantile (P) Limited v. Indo Unique Flame Limited*, (2021) 4 SCC 379 (“**NN Global I**”) set aside the finding in *SMS Tea* but considered itself bound by the judgment of the Division Bench in *Garware Wall Ropes* as it was affirmed by a coordinate bench in *Vidya Drolia*, (2021) 2 SCC 1. Accordingly, the three-judge bench referred the following question of law to a five-judge bench:

“Whether the statutory bar contained in Section 35 of the Stamp Act, 1899 applicable to instruments chargeable to stamp duty under Section 3 read with the Schedule to the Act, would also render the arbitration agreement contained in such an instrument, which is not chargeable to payment of stamp duty, as being non-existent, unenforceable, or invalid, pending payment of stamp duty on the substantive contract/instrument?”

This was answered in the affirmative by the majority (3:2) in *NN Global II* who affirmed *Garware Wall Ropes*, whilst the minority considered it to be bad law. The Second Constitution Bench summarised the findings of the majority in the *NN Global II* succinctly as follows:

- a. *An unstamped instrument containing an arbitration agreement is void under Section 2(g) of the Contract Act;*

- b. *An unstamped instrument, not being a contract and not enforceable in law, cannot exist in law. The arbitration agreement in such an instrument can be acted upon only after it is duly stamped;*
- c. *The “existence” of an arbitration agreement contemplated under Section 11(6A) of the Arbitration Act is not merely a facial existence or existence in fact, but also “existence in law”;*
- d. *The Court acting under Section 11 of the Arbitration Act cannot disregard the mandate of Sections 33 and 35 of the Stamp Act requiring it to examine and impound an unstamped or insufficiently stamped instrument; and*
- e. *The certified copy of an arbitration agreement must clearly indicate the stamp duty paid.*

The matter was referred to the Second Constitution Bench having regard to the large ramifications and consequences of the view of the majority in *NN Global II*.

FINDINGS OF THE SECOND CONSTITUTION COURT

The main findings of the Second Constitution Bench are summarised as follows:

An agreement that is inadmissible in evidence for being inadequately stamped or unstamped is not a void agreement

The Second Constitution Bench found that the admissibility of an instrument in evidence is distinct from its validity or enforceability in law. The Court found that Section 35 of the Stamp Act renders the instrument inadmissible and not void and that *NN Global II* erred in conflating these distinct concepts. The Second Constitution Bench held that it is well established under the scheme of the Stamp Act, specifically under proviso (a) to section 35, that non-payment of stamp duty is treated as a curable defect.

Under the principles of separability and kompetenz-kompetenz that the arbitral tribunal has the primary responsibility to rule on jurisdictional issues

According to the Second Constitution Bench, the separability presumption under section 16(1) of the Arbitration Act “encapsulates the general rule on the substantive independence of an arbitration agreement”. Under section 16(1)¹ of the Arbitration Act, the arbitration agreement is treated as a distinct and separate agreement to the underlying contract which will not be affected by the invalidity, illegality, or termination of such contract. This allows the arbitral tribunal when faced with

¹ Section 16(1) of the Arbitration Act provides that jurisdictional objections are to be heard and determined by the arbitral tribunal itself and, to that end, provides that the arbitration agreement is independent of the other terms of the contract. Similarly, the section provides that if a contract is found to be null and void, this will not, in and of itself, mean that the arbitration clause is also invalid.

the contention that the underlying contract is void, to assume jurisdiction to decide on its own jurisdiction. This is referred to as the doctrine of “*kompetenz-kompetenz*”. The Second Constitution Bench defines this principle as a rule “*whereby arbitrators must have the first opportunity to hear challenges relating to their jurisdiction, which is subject to subsequent review by courts*”(commonly at the challenge stage under section 34 of the Arbitration Act).

Issue of stamp duty is a jurisdictional one which ought to be determined by arbitral tribunals and not by courts

Upon reviewing past authorities, specifically its judgment in *Uttarakhand Purv Sainik Kalyan Nigam Limited v. Northern Coal Field* (2020) 2 SCC 455 where it was held that section 16 of the Arbitration Act is an inclusive provision that contemplates “*all preliminary issues touching upon the jurisdiction of the Arbitral Tribunal*”, the Second Constitution Bench concluded that the issue of stamping – like that of limitation – is a jurisdictional one for the arbitral tribunal to determine under the principle of *kompetenz-kompetenz*.

The Second Constitution Bench therefore held that the scope of the arbitral tribunal’s jurisdiction under section 16 of the Arbitration Act is wide enough for it to adjudicate the claims between the parties even when stamp duty has not been paid on the underlying contract. A corollary of this is that once an arbitral tribunal is formed and determines on appraising the evidence that stamp duty is unpaid or lacking, it will be bound to impound the contract under section 33 of the Stamp Act.

The First Constitution Court erred in interpreting the scope of the referral court’s powers under section 11(6A)

The Second Constitution Court notes that section 11(6A) of the Arbitration Act still holds the field as the amendment under the Arbitration and Conciliation (Amendment) Act, 2019 omitting this section has not yet been notified by the Central Government. The Second Constitution Bench found that *NN Global II* erred in its interpretation of section 11(6A) by giving the referring court a broader jurisdiction than Parliament had contemplated. It is evident from a plain reading of section 11(6A) that the referral court is only required to examine the existence of an arbitration agreement. It is well settled that this is based on a *prima facie* standard of review.² According to the Constitution Court, the issue of non-payment or inadequacy of stamp duty cannot be decided on a *prima facie* basis as this will require detailed consideration of evidence and submissions and can only be done by the arbitral tribunal.

² *Pravin Electricals Pvt. Ltd. v. Galaxy Infra and Engineering Pvt. Ltd.*, (2021) 5 SCC 671

The Court reiterates that the legislative intent behind the Arbitration Act is to minimise the role of courts and limit it to a more supportive or facilitative role to arbitral proceedings. Consequently, it is held that the views of the referral court – which are *prima facie* in nature – will not be binding on the arbitral tribunal nor on the court enforcing the award.

To summarise, the Second Constitution Bench held that when a party produces an arbitration agreement before the referral court, the court must examine, on a *prima facie* basis, whether the arbitration agreement exists under section 7 of the Arbitration Act. It is not required to, for example, examine whether a certified copy of the agreement discloses the fact of payment of stamp duty on the original.

An ancillary but nevertheless important issue that the Second Constitution Court touches upon is the role of courts in an application under section 9 of the Arbitration Act³ when the respondent party challenges the validity of the arbitration agreement for inadequate stamp duty. The Second Constitution Bench clarifies that in such an event, “*courts are not required to deal with the issue of stamping at the stage of granting interim measures under section 9*”. Therefore, based on this finding, interim measures will be available irrespective of whether the underlying instrument is adequately stamped.

The Arbitration Act and the Stamp Act are capable of co-existing harmoniously

The Second Constitution Bench categorically held that its analysis does not render provisions under the Stamp Act inapplicable as arbitral tribunals remain bound by its provisions. The Court adopted a harmonious interpretation of the Arbitration Act and the Stamp Act by ensuring that neither statute rendered the other one ineffective. It noted that the legislative objective behind the Stamp Act is to secure revenue for the state and that of the Arbitration Act is to, *inter alia*, ensure an efficacious process of arbitration and minimize the supervisory role of the courts. It also noted that the Arbitration Act, which is a consolidation of India’s arbitration laws, will have primacy over the Stamp Act in relation to arbitration agreements based on the principle of *lex specialis* as well as due to the fact that Parliament was aware of the Stamp Act when it enacted the Arbitration Act and did not specify that stamping is a pre-condition to the existence of a valid arbitration agreement. The Court affirmed that the Stamp Act is a fiscal measure to secure revenue for the state and was not enacted to arm a litigant with a “*weapon of technicality*” against his opponent.

³ Section 9 of the Arbitration Act provides for various interim measures of protection that may be granted by a court at any stage before the formation of the arbitral tribunal, or during arbitration proceeding, up until the time the award is enforced.

The Second Constitution Bench found that *NN Global II* erred in giving effect exclusively to the Stamp Act at the cost of the Arbitration Act. It also overturned the ratio of the court in *Garware Wall Ropes* (i.e., that an arbitration agreement in an unstamped or insufficiently stamped instrument would be *non-est* in law) as it does not give recognition to the principles of separability and kompetenz-kompetenz as well as the legislative intent behind the Arbitration Act vis-à-vis the Stamp Act, which are well settled under Indian jurisprudence.

CONCLUSION

The Second Constitution Bench has put to rest the uncertainty surrounding this issue. It has done so by undertaking an in-depth and comprehensive look at the framework of under the Arbitration Act and the Stamp Act and respective legislative intentions behind them. The result is another arbitration friendly judgment that has correctly, in our opinion, done away with the judicial trend of treating the issue of stamp duty as a litigant's "*weapon of technicality*", whilst recognising the significance of the law on stamp duty as a fiscal measure that is binding on an arbitral tribunal (who will ultimately have to rule on any disputes arising under the Stamp Act). The present judgment ensures, however, that the issue of stamp duty will no longer be a factor in protracting proceedings before the referring court.