

STAMPING OF ARBITRATION AGREEMENTS: AN ANALYSIS OF THE EVOLVING ARBITRATION LANDSCAPE IN INDIA

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I. INTRODUCTION: FROM WHERE DOES THE QUESTION OF STAMPING OF ARBITRATION AGREEMENTS EMERGE?

The question of whether an arbitration agreement is required to be stamped under prevailing stamp duty laws has loomed large over the arbitration landscape in India for over a decade.

The requirement to pay ‘stamp duty’ on instruments executed in India or instruments executed outside India and received in India, arises from stamping laws i.e., the Indian Stamp Act 1899 [“**Stamp Act**”] or corresponding stamp-related legislation enacted by certain states [“**State Stamp Acts**”]. The broad scheme of stamp duty laws in India is that there is (a) a principal ‘charging provision’ i.e., a section which, in principle, makes instruments executed (or received) in India chargeable to stamp duty; and (b) a Schedule which is comprised of several Articles, prescribing rates of stamp duty payable on various categories of instruments.

Under the Stamp Act, the relevant Article in the Schedule that mentions “agreements” is Article 5, Schedule I. Sub-article (c) of Article 5 is a catch-all provision covering within its ambit all agreements not specifically provided for [“**Residuary Article**”]. The Residuary Article is mirrored in the State Stamp Acts as well. Accordingly, an agreement “not otherwise provided for” would be chargeable to stamp duty under the Residuary Article.

An arbitration agreement being “*an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not*”, would be eligible to stamp duty under the Residuary Article as it is not otherwise provided for separately and specifically in the Schedule.

II. EFFECT OF NON-STAMPING OF INSTRUMENTS

There are two key consequences of non-stamping of an instrument that is otherwise liable to be stamped¹: (a) there is a bar on “*any person having by law or consent of parties authority to receive evidence*” (i.e., courts and tribunals) from admitting such unstamped document in evidence for any

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¹ Indian Stamp Act, 1899, § 35.

purpose; or (b) there is a bar on courts, tribunals or any other public officer from otherwise “acting upon” such instrument in any manner.

From a practical perspective, for appointment of an arbitrator under Section 11 or grant of interim reliefs under Section 9 of the Arbitration Act pursuant to an unstamped arbitration agreement (which ought to have been stamped under the Residuary Entry) would tantamount to “acting upon” the arbitration agreement.

III. A SERIES OF DIVERGENT DECISIONS

In the above backdrop, the Supreme Court of India as well as various High Courts across the country had been taking divergent positions on the question of whether an arbitration agreement is chargeable to stamp duty or not.

The question of stamping of ‘arbitration agreements’ was first adjudicated by the Supreme Court in *SMS Tea Estates (P) Ltd. v. Chandmari Tea Co. (P) Ltd.* [**“SMS Tea Estates”**].² Back in 2011, a 2-judge bench of the Hon’ble Supreme Court held that an unstamped arbitration clause in an agreement that is chargeable to stamp duty cannot be the basis for the appointment of an arbitrator. This is because Section 35 of the Stamp Act prevents the court from “acting upon” an unstamped instrument i.e., the unstamped arbitration agreement. The Supreme Court, therefore, remanded the matter back to the High Court of Gauhati for assessing whether stamp duty had been duly paid on the instrument, and only then appointing an arbitrator.

Following this decision in *SMS Tea Estates*, in *Garware Wall Ropes Ltd. v. Coastal Marine Constructions & Engg. Ltd.*³ [**“Garware”**], the Supreme Court re-affirmed that an agreement that is not enforceable is said to be void in terms of Section 2(g) of the Indian Contract Act, 1872. Therefore, an unstamped arbitration agreement is unenforceable and void. The Supreme Court directed that while deciding Section 11 applications for appointment of arbitrators based on unstamped instruments, courts should first have the unstamped instrument impounded and adjudicated, and only after payment of applicable stamp duty and penalty should the court proceed to decide the Section 11 application. In a bid to harmonise the legislative mandates of the Arbitration Act and the Stamp Act, the court directed that the appointing high court may, while

² *SMS Tea Estates (P) Ltd. v. Chandmari Tea Co. (P) Ltd.* (2011) 14 SCC 66.

³ *Garware Wall Ropes Ltd. v. Coastal Marine Constructions & Engg. Ltd.* (2019) 9 SCC 209.

proceeding with the Section 11 application, the court may impound the instrument and pass it on to the stamp authorities for adjudication of stamp duty in a time-bound manner.

In December 2020, the Supreme Court in *Vidya Drolia v. Durga Trading Corpn.*⁴ [**“Vidya Drolia”**] further affirmed the reasoning in *Garware*. The court held that existence and validity of an arbitration agreement are intertwined. Therefore, an arbitration agreement does not exist if it does not satisfy mandatory legal requirements (such as the requirement to pay stamp duty) – and that an invalid agreement is no agreement.

Finally, in *N.N. Global Mercantile (P) Ltd. v. Indo Unique Flame Ltd.*⁵ [**“NN Global”**], a three-judge bench of the Supreme Court held that arbitration agreement is independent from the underlying commercial contracts and is not chargeable to stamp duty. The Supreme Court further applied the principle of severability, stating that courts can sever the arbitration agreement from the unstamped instrument and appoint an arbitrator based on the valid (although unstamped) arbitration agreement. It also allowed appointments under Section 11 of the Arbitration Act *“pending payment of stamp duty”* on the substantive contract. Thus, in effect, in *NN Global*, the Supreme Court overruled *SMS Tea Estates*, doubted the ratio in *Garware* as well as the reasoning in *Vidya Drolia*. Since the *Vidya Drolia* decision was rendered by a coordinate bench, the question was referred to a 5-judge constitution bench.

The constitution bench decided the questions as to: (a) whether stamp duty under and in terms of the Stamp Act is payable on an arbitration agreement or clause contained within an overarching agreement, and (b) if the non-payment or deficient payment of such stamp duty renders the arbitration agreement unenforceable.

IV. CONSTITUTION BENCH SETTLES THE LEGAL POSITION

In *N.N. Global Mercantile Limited v. Indo Unique Flame Limited and Ors.*⁶ [**“NN Global Reference”**], the constitution bench held by a 3:2 majority that an arbitration agreement or clause would not be enforceable under Indian contract law, if the instrument containing the arbitration agreement is not stamped in terms of the Stamp Act. Accordingly, such an arbitration agreement

⁴ *Vidya Drolia v. Durga Trading Corpn.* (2021) 2 SCC 1.

⁵ *N.N. Global Mercantile (P) Ltd. v. Indo Unique Flame Ltd.* (2021) 4 SCC 379.

⁶ Civil Appeal No(s). 3802-3803 of 2020.

was held to not ‘exist in law’ or be capable of being acted upon – thereby requiring that at the stage of appointment of arbitrators by courts under Section 11 of the Arbitration Act, the appointing court must ascertain whether appropriate stamp duty has been paid on the underlying instrument as well as the arbitration agreement.

Some of the key considerations on the basis of which the Supreme Court has rendered this decision are:

- i. the position that an arbitration agreement, of itself, is not liable to be charged with stamp duty is incorrect;
- ii. an unstamped agreement cannot be taken notice of for any purpose, as contemplated in Section 35 of the Stamp Act – and therefore, remains unenforceable. Thus, even an arbitration agreement which is unstamped, does not exist in law;
- iii. The fact that the Stamp Act is a ‘fiscal enactment’ intended to raise revenue does not take away from the fact that it is required to be implemented with full rigour; stamp duty is not just a question of ‘technicality’;
- iv. Even in a reference under Section 11 of the Arbitration Act, the mandate of Sections 33 and 35 of the Stamp Act (dealing with impounding of unstamped instruments and adjudication of requisite stamp duty) must be given effect to by courts. The ‘shirking’ or relegating of this function to the arbitral tribunal appears unjustifiable. However, in case of deficiently stamped agreements, if the claim of deficient stamp duty appears untenable to the court, the court may refer the matter to arbitration on the basis of ‘existence’ of the arbitration agreement and leave the function of impounding of the agreement to the arbitrator.

V. RAMIFICATIONS OF THE DECISION IN NN GLOBAL: WHAT NEXT?

The decision in the NN Global Reference has certainly put to rest long-standing questions in connection with the validity and enforceability of unstamped arbitration agreements or arbitration agreements contained in unstamped instruments. This provides commercial parties with clarity on an important step to be completed after the execution of contracts i.e. payment of appropriate stamp duty in terms of the relevant Article under the Stamp Act Schedule.

Having said that, the NN Global Reference decision has also created several procedural inefficiencies in the operation of the Arbitration Act. For instance, the decision will cause severe

delays in cases where arbitrators are required to be appointed or where interim reliefs are sought, on the basis of an arbitration agreement (or underlying instrument) that is unduly stamped, because the agreement will first get impounded and adjudicated before it is acted on by courts. While the Supreme Court expressly left the question of Section 9 applications (concerning interim reliefs) open in the NN Global Reference, the same principle enunciated in relation to appointment of arbitrators can be applied for not granting interim reliefs until the agreement is duly stamped, even though the main objective of Section 9 is to protect the subject matter of the arbitration. Another procedural hurdle created by the decision is that it has created room for jurisdictional challenges (under Section 16 of the Arbitration Act) in ongoing arbitrations, on the ground that the arbitrator has been appointed pursuant to an unstamped agreement.

The decision in the NN Global Reference derogates from the twin objectives of the Arbitration Act, as amended and updated from time to time i.e., minimal judicial intervention at the pre-arbitration stage and efficient disposal of arbitrations and related matters. This has had the unintended effect of assisting defaulting parties in creating unwarranted delays in the arbitral process. As a result, India's growing image and reputation as a pro-arbitration jurisdiction and an alternative dispute resolution hub has been slightly dented.

A more harmonious and arbitration-friendly approach to the NN Global Reference would have been for the Supreme Court to hold that non-payment of stamp duty is a curable defect under the scheme of the Stamp Act itself. Accordingly, so long as arbitration agreement prima facie exists in terms of the Arbitration Act, it should not interfere in proceeding with appointment of arbitrators. The procedural function of impounding of the instrument and adjudication and payment of stamp duty could and should have been entirely delegated to the arbitration tribunal and the jurisdictional stamp duty authorities at the post-appointment stage. While the decision in the NN Global Reference certainly interprets the Stamp Act correctly and strictly, it may have taken a hyper-technical view of the same without according due significance to the objectives of the Arbitration Act.

Unless the law is amended or the NN Global Reference decision is reviewed, as the law currently stands, the issues highlighted above will continue to haunt the arbitrations in India in cases of non or insufficiently stamped arbitration agreement or underlying instrument. The answer to this anomaly would be in delegating the appointment to the designated arbitration institutions – and the function of resolving technical issues (such as undue stamping of the arbitration agreement or

instrument) will be left to the domain of the arbitrator. This will negate the impact of NN Global Reference on India's global image as a pro-arbitration jurisdiction.