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SUPREME COURT HOLDS THAT AN UNSTAMPED ARBITRATION AGREEMENT IS 'NON-EXISTENT' AT THE PRE-REFERRAL STAGE

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In a judgment with far reaching consequences, a five-judge Constitutional Bench of the Supreme Court of India in the matter of *N.N. Global Mercantile Private Limited v. Indo Unique Flame Ltd.* Civil Appeal No(s). 3802-3803 of 2023 provided clarity on the effects of an unstamped or insufficiently stamped arbitration agreement in proceedings to refer disputes to arbitration on a party's application, answering the reference made to it by the three-judge bench of the Supreme Court in *N.N. Global Mercantile Private Limited v. Indo Unique Flame Limited and Others*, (2021) 4 SCC 379 (N.N. Global). Our Ergo Update on the reference made by the three-judge bench is at [[Ergo Update dated. 20.1.21](#)]

Facts and Background

The first Respondent in the present civil appeal, i.e., Indo Unique Flame Limited (IUFL) was awarded a Work Order and thereafter, entered into a sub-contract with the Appellant, i.e., N.N. Global Mercantile Private Limited. The said Work Order provided for arbitration. Due to disputes arising between the Parties, IUFL sought to invoke the bank guarantee furnished to it by the Appellant under the Work Order. The Appellant filed a Suit against such invocation. In view of the arbitration clause in the Work Order, IUFL applied under Section 8 of the Arbitration and Conciliation Act, 1996 (Arbitration Act) seeking to refer the disputes to arbitration. Upon rejection of the application by the Commercial Court, IUFL filed a Writ Petition challenging the Order before the Bombay High Court. Before the High Court, it was, *inter alia*, contended that the arbitration agreement was unenforceable as the Work Order was unstamped. The Bombay High Court allowed the Writ Petition.

An appeal was filed from this decision of the Bombay High Court before the Supreme Court, leading to the judgment in *N.N. Global*. In *N.N. Global*, a three-judge Bench of the Supreme Court found that an arbitration agreement is a distinct and separate agreement independent of the substantive commercial contract in which it is embedded and held that non-payment or deficiency of stamp duty would not render the agreement invalid, unenforceable, or non-existent even if the substantive contract could not be acted upon on account of such non-payment. In the decision, the Supreme Court also doubted the correctness of its decision in *SMS Tea Estates v. Chandmari Tea Co.*, (2011) 14 SCC 66 (SMS Tea Estates), as well as the decision in *Garware Wall Ropes Ltd. v. Coastal Marine Constructions and Engineering Ltd.*, (2019) 4 SCC (Civ.) 324 (Garware) which was approved by a coordinate bench in *Vidya Drolia v. Durga Trading Corporation*, (2021) 2 SCC 1 (Vidya Drolia) - necessitating the reference to the five-judge Bench.

The Majority Judgment

The Constitution Bench delivered a fractured verdict, with the majority of three judges answering the reference in the affirmative to find that an unstamped arbitration agreement would be non-existent pending payment of stamp duty.

Preliminarily, the Supreme Court noted that in view of the residuary entry in Schedule I of the Stamp Act which deals with an agreement or memorandum of agreement "not otherwise provided for" that was apparently overlooked in *N.N. Global*, it is established that an arbitration agreement itself would be exigible to stamp duty. Accordingly, the reference question as posed in *N.N. Global* was reframed to enquire into whether the statutory bar contained in Section 3 of the Stamp Act "would also render the arbitration agreement contained in such an instrument as being non-existent, pending payment of stamp duty on the substantive contract/instrument".

Reasoning and findings

Having considered the issue in depth, the Supreme Court concluded that the view taken in *SMS Tea Estates*, followed in *Garware* and approved in *Vidya Drolia* represents the correct position in law and approved the reasoning therein.

The Supreme Court examined the statutory scheme and background of the Indian Stamp Act, 1899, (Stamp Act) the Indian Contract Act, 1872 (Contract Act) and the Arbitration Act to arrive at its conclusion. Under the Stamp Act, an unstamped instrument is compulsorily impoundable under Section 33 and only becomes enforceable once it is endorsed under Section 42(2). While the Stamp Act is a fiscal statute, the Supreme Court held that it cannot be considered a procedural law to hold that an unstamped arbitration agreement merely presents a "curable defect" or a "technicality".

Section 11 (6A) of the Arbitration Act requires that the Supreme Court or High Court while considering any application under Section 11 confine itself to the examination of the "existence" of an arbitration agreement. As an arbitration agreement is itself exigible to stamp duty and would not be enforceable without the payment of stamp duty under the Stamp Act, such an arbitration agreement would be void under the Contract Act.

As any sanction in law through a civil action on an unstamped instrument is impermissible, an unstamped arbitration agreement is invalid even though it is not null and void and as such an arbitration agreement may be validated through compliance with the Stamp Act. Till such compliance, such an arbitration agreement would not be "enforceable in law" and could not be said to be in existence under the law.

The Supreme Court, going through the Arbitration Act, observed that it does not require production of the original instrument, and parties seeking reference may submit a certified copy of the agreement. Nevertheless, the Supreme Court noted that while a court cannot impound a certified copy under Section 33, the bar under Section 35 of the Stamp Act would nevertheless operate as the Court may always seek clarification that the stamp duty has been paid.

The Minority View

While the Bench agreed that arbitration agreements must be stamped under the Stamp Act, the judges in the minority diverged in their ultimate decision. The minority judgments took a view that the decision in *SMS Tea Estates* is not the correct legal position and the decisions in *Garware* and *Vidya Drolia* are not correct to the extent that they rely on and approve the decision in *SMS Tea Estates*.

The minority judgements observed that the legislative intent and a plain reading of the provisions of the Stamp Act clearly indicate that non-payment of stamp duty is a curable

defect that does not affect the enforceability of a document or render it invalid/ *void ab initio*. Stamp duty is levied on the instrument and not on the transaction.

Further, in line with the principle of minimal judicial intervention being the legislative intent of the Arbitration Act and the amendments thereto, issues of non-stamping/deficiency in stamping are referable to the arbitrator or arbitral tribunal under Section 16 of the Arbitration Act who may adjudicate the same by virtue of the doctrine of *kompetenz-kompetenz*.

Comment

The Supreme Court has not clarified the status of arbitral proceedings that are presently underway based on arbitration agreements where the extant stamp duty is not paid.

However, as the majority judgment expressly clarifies, the impact of an unstamped arbitration agreement in an application for interim relief under Section 9 of the Arbitration Act remains an open question in view of the limited reference to the Constitution Bench. , Similarly, a challenge to an arbitral award under Section 34 of the Arbitration Act or enforcement of an arbitral award under Section 36 of the Arbitration Act are also not touched upon in the present judgement.

Therefore, in our view, it is now incumbent upon parties to make sure that the applicable stamp duty is paid on agreements containing an arbitration agreement.

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