

# Dispute Resolution Hotline

September 07, 2023

## UNSTAMPED AGREEMENT AND ITS ENFORCEABILITY UNDER INDIAN LAW: RECENT DEVELOPMENTS

- An agreement not stamped, or unduly stamped, is not valid under Indian law
- A Court must impound an unstamped agreement before appointing an arbitrator under the Arbitration and Conciliation Act, 1996.
- Non-stamping or insufficient stamping cannot be treated as “curable defect”, such an instrument is not enforceable in law.
- Doctrine of severability does not exempt an arbitration clause from scrutiny under the Indian Stamp Act, 1899.
- Once an agreement has been admitted in evidence by the arbitrator, the arbitral award passed thereafter cannot be set aside on this ground.
- Courts can either expeditiously dispose of impounding proceedings or direct the Collector to dispose the same in time-bound manner.

In April 2023, the five-judge constitutional bench of the Supreme Court of India (“**Supreme Court**”), in *M/s NN Global Mercantile Private Limited (“NN Global”) v. M/s Indo Unique Flame Limited (“Indo Unique”) & Ors.*,<sup>1</sup> has held that an unstamped instrument (including an arbitration agreement contained in it) which is otherwise exigible to stamp duty is non-existent in law and must be impounded by the Court before appointing an arbitrator. In respect of such unstamped agreements, the rights of the parties will remain frozen, or they would not exist until the defect is cured.

In July 2023, the Delhi High Court in *Arg Outlier Media Private Limited v. HT Media Limited*,<sup>2</sup> while considering a challenge to an arbitral award passed on an unstamped agreement held that although in terms of NN Global, the agreement not being properly stamped could not have been admitted in evidence; however, once having been admitted in evidence by the arbitrator, the award passed by relying on such agreement cannot be faulted on this ground. Similar view has been expressed by the Delhi High Court in *SNG Developers Limited v. Vardhman Buildtech Private Limited* (initially by the Single Judge,<sup>3</sup> and later confirmed by the Division Bench<sup>4</sup>).

In another recent judgment in August 2023, the Delhi High Court in *Splendor Landbase Ltd. (“Splendor”) v. Apama Ashram Society & Anr. (“Aparna Ashram”)*,<sup>5</sup> has laid down the guidelines for expeditiously carrying out the process of impounding the agreement, and determining the stamp duty (and penalties, if applicable) payable. The judgment is in the context of appointment of the arbitrator under Section 11 of the Arbitration Act, and as such, not a binding precedent, as clarified by the Supreme Court in *State of West Bengal & Ors. v. Associated Contractors*.<sup>6</sup>

## BACKGROUND TO THE DISPUTE

Indo Unique was awarded a work order and entered into a sub-contract with the NN Global. The work order (which included the sub-contract) contained an arbitration agreement. A dispute arose in relation to encashment of a bank guarantee between NN Global and Indo Unique. NN Global filed a suit against Indo Unique. Indo Flame applied under Section 8 of the Arbitration and Conciliation Act, 1996 (“**Arbitration Act**”) for referring the dispute to arbitration. The application was rejected on the ground that the work order was unstamped, and therefore, unenforceable under Section 35<sup>7</sup> of the Indian Stamp Act, 1899 (“**Stamp Act**”).

Indo Flame filed a writ petition challenging the order of rejection. The Bombay High Court allowed the writ. Subsequently, NN Global approached the Supreme Court, where the primary issue was whether an arbitration clause, contained in an unstamped work order, can be acted upon. A three-judge bench of the Supreme Court, *vide* its judgment dated 11 January 2021 in NN Global vs. Indo Unique,<sup>8</sup> held that an arbitration agreement is a distinct and separate agreement, and can be acted upon even if contained in an unstamped instrument.

## ISSUE BEFORE THE SUPREME COURT

As there existed contrary judgments of the Supreme Court on this issue,<sup>9</sup> the three-judge bench referred the question of law (reproduced below) to be conclusively decided by the five-judge constitutional bench of the Supreme Court:

“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?”

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*Existence vs. validity of the arbitration agreement*

The Supreme Court discussed the purpose of insertion of Section 11(6A) in the Arbitration Act.<sup>10</sup> Noting that under Section 11(6A), Courts must confine their examination to the existence of an arbitration agreement in proceedings under Section 11 of the Arbitration Act, it held that the examination of the existence of an arbitration agreement under Section 11(6A) does not mean mere “existence in fact”. In enquiry under Section 11, the Courts must see if the arbitration agreement exists in law, i.e., the arbitration agreement must be enforceable in the eyes of the law.

Reliance was placed on *Vidya Drolia & Ors. vs. Durga Trading Corporation* (“**Vidya Drolia**”),<sup>11</sup> where it was held that for an arbitration agreement to “exist”, it should meet and satisfy the requirements under both Arbitration Act and the Indian Contract Act, 1872 (“**Contract Act**”).<sup>12</sup> Therefore, an arbitration agreement must be a valid and enforceable contract under the law. The phrase “arbitration agreement” under Section 11(6A) of the Arbitration Act must mean a contract, by meeting the requirements under Section 2(h) & (j) of the Contract Act.<sup>13</sup> Any agreement that cannot be enforced under law cannot be said to be a valid contract and therefore cannot be said to “exist”.

*Effect of non-stamping of a document under the Stamp Act*

It was held that under Section 35 of the Stamp Act, an unstamped agreement cannot be “acted upon” by the Courts. Relying on the judgment in *Hindustan Steel Limited vs. Dilip Construction Company*,<sup>14</sup> it was held that to “act upon” an instrument or document would mean to give effect to it or enforce it. Therefore, an unstamped agreement, which is otherwise exigible to stamp duty, cannot be enforced by the Courts and cannot be said to have any existence in the eyes of the law.

Further reliance was placed on *Mahanth Singh vs. U Ba Yi*<sup>15</sup> to observe that Section 2(j) of the Contract Act would only be attracted when a contract is rendered unenforceable by application of a substantive law. While the Stamp Act is a fiscal statute, it was held to be substantive law. Therefore, any unstamped contract exigible to stamp duty shall be rendered void under Section 2(j) of the Contract Act. It was further observed that the rights of the parties under an unstamped agreement would remain frozen or rather would not exist until such an agreement is duly stamped.<sup>16</sup>

Lastly, it was held that Courts are bound under Section 33<sup>17</sup> of the Stamp Act to impound an instrument that has not been stamped or is unduly stamped.

*On the doctrine on severability*

It was observed that doctrine of severability would not play any role in the Courts duty to impound and not give effect to an unstamped instrument under the Stamp Act. While upholding that the arbitration agreement is a separate and distinct agreement from the principal agreement containing the arbitration clause, it was held that the evolution of the doctrine of severability indicates that the same cannot be invoked when dealing with the provisions of the Stamp Act.

It was observed that the doctrine of severability was primarily developed to preserve the arbitration clause in situations where the principal contract is terminated or rescinded for any reason. This was to protect the rights of the parties to resolve their disputes through arbitration, and to ensure that the powers of the arbitrator are not extinguished with the termination of the main contract. The Supreme Court opined that since arbitration agreement by itself is also exigible to stamp duty,<sup>18</sup> the doctrine of severability would not be of help where the main contract, containing the arbitration clause, is unstamped.

## DECISION OF THE SUPREME COURT

In light of the above analysis, the majority held as under:

1. An instrument containing the arbitration clause, if exigible to stamp duty, will have to be necessarily stamped before it can be acted upon. Such instrument, if remains unstamped, will not be a contract and not be enforceable in law, and therefore, cannot exist in law.
2. Section 33 and 35 of the Stamp Act would render an arbitration agreement contained in an unstamped instrument as being non-existent in law, unless the instrument is validated under the Stamp Act.

However, the Supreme Court specifically observed that it is not pronouncing any judgment in relation to the proceedings under Section 9 of the Arbitration Act, i.e., interim protection in aid of arbitration.

## EMERGING CHALLENGES IN THE AFTERMATH OF THE JUDGMENT

The judgment of the Supreme Court will have far reaching implications on the pro-arbitration trend that started in 2012 with the BALCO judgment by the Supreme Court. The process for impounding an unstamped or unduly stamped instrument is generally marred by extreme delays, which would in turn cause delays in initiating arbitral proceedings. From a policy perspective, the judgment will also impede the implementation of the institutional arbitration in India, as recommended by the high-level committee chaired by Justice Srikrishna (retd.), as the arbitral institution may not be able to appoint an arbitrator in proceedings arising from unstamped arbitration agreements governed by Indian law. However, the Delhi High Court has provided guidance on the expeditious disposal of the impounding proceedings in cases where the agreement has to be impounded in relation to appointment of arbitrator under Section 11 of the Arbitration Act.<sup>19</sup>

The finding that an unstamped agreement does not exist in law, and the rights of the parties under such an agreement would rather not exist may adversely impact foreign-seated arbitrations. For example, an unstamped agreement, executed outside India, and subject to Indian laws, may not be given effect to by the foreign-seated tribunal, as such an agreement would not exist under the Indian laws. Moreover, while the Supreme Court has stated that it has not pronounced on the matter in relation to Section 9 of the Arbitration Act, it remains to be seen if the Courts would grant any interim reliefs in an agreement that does not “exist” in law.

Lastly, as recognized in the dissenting opinion of Justice Hrishikesh Roy, there have been technological advances in the manner of execution of agreements (such as electronic signatures through DocuSign, etc.) and the advent of the

smart contract arbitration. The majority judgment has not considered such developments. This may threaten the developing ecosystem of dispute resolution through deployment of technological and artificial intelligence tools.

– Parva Khare, Alipak Banerjee & Vyapak Desai

You can direct your queries or comments to the authors.

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<sup>1</sup>*Ms NN Global Mercantile Private Limited vs. Ms Indo Unique Flame Limited & Ors.*, 2023 SCC OnLine SC 495.

<sup>2</sup>2023 SCC OnLine Del 3885

<sup>3</sup>2021 SCC OnLine Del 5301

<sup>4</sup>2022 SCC OnLine Del 3273

<sup>5</sup>2023 SCC OnLine Del 5148

<sup>6</sup>(2015) 1 SCC 32.

<sup>7</sup>The Indian Stamp Act, s 35:

Instruments not duly stamped inadmissible in evidence, etc.—

No instrument chargeable with duty shall be admitted in evidence for any purpose by any person having by law or consent of parties authority to receive evidence, or shall be acted upon, registered or authenticated by any such person or by any public officer, unless such instrument is duly stamped:

Provided that—

(a) any such instrument shall be admitted in evidence on payment of the duty with which the same is chargeable, or, in the case of any instrument insufficiently stamped, of the amount required to make up such duty, together with a penalty of five rupees, or, when ten times the amount of the proper duty or deficient portion thereof exceeds five rupees, of a sum equal to ten times such duty or portion;

(b) where any person from whom a stamped receipt could have been demanded, has given an unstamped receipt and such receipt, if stamped, would be admissible in evidence against him, then such receipt shall be admitted in evidence against him on payment of a penalty of one rupee by the person tendering it;

(c) where a contract or agreement of any kind is effected by correspondence consisting of two or more letters and any one of the letters bears the proper stamp, the contract or agreement shall be deemed to be duly stamped;

(d) nothing herein contained shall prevent the admission of any instrument in evidence in any proceeding in a Criminal Court, other than a proceeding under Chapter XII or Chapter XXXVI of the Code of Criminal Procedure 1898 (V of 1898);

(e) nothing herein contained shall prevent the admission of any instrument in any Court when such instrument has been executed by or on behalf of the Government, or where it bears the certificate of the Collector as provided by section 32 or any other provision of this Act.

<sup>8</sup>(2021) 4 SCC 379.

<sup>9</sup>See *Garware Wall Ropes Ltd. vs. Coastal Marine Constructions & Engg. Ltd.*, (2019) 9 SCC 209, as affirmed in *Vidya Drolia & Ors. vs. Durga Trading Corporation*, (2021) 2 SCC 1.

<sup>10</sup>The Arbitration and Conciliation Act, 1996, s 11(6A):

Appointment of arbitrators.—

...

(6A) The Supreme Court or, as the case may be, the High Court, while considering any application under sub-section (4) or sub-section (5) or sub-section (6), shall, notwithstanding any judgment, decree or order of any Court, confine to the examination of the existence of an arbitration agreement.

<sup>11</sup>(2021) 2 SCC 1.

<sup>12</sup>*Vidya Drolia & Ors. vs. Durga Trading Corporation*, (2021) 2 SCC 1 (paras 146, 147, 147.1-147.11); The Supreme Court in *Vidya Drolia* has specifically upheld the findings in the decision in *Garware Wall Ropes vs. Coastal Marine Constructions & Engineering Ltd.* ("**Garware Wall Ropes**"), (2019) 9 SCC 209 (para 29). (For our hotline on *Garware Wall Ropes*, see Alipak Banerjee & Bhavana Sunder, "Arbitration Clause in an Unstamped Agreement? Supreme Court Lays Down the Law", available at <https://www.nishithdesai.com/SectionCategory/33/Dispute-Resolution-Hotline/12/57/DisputeResolutionHotline/4520/2.html>).

<sup>13</sup>The Indian Contract Act, 1872, s 2(h) & (j):

Interpretation clause.—

...

(h) An agreement enforceable by law is a contract;

...

(j) A contract which ceases to be enforceable by law becomes void when it ceases to be enforceable.

<sup>14</sup>(1969) 1 SCC 597.

<sup>15</sup>AIR 1939 PC 110.

<sup>16</sup>*Ms NN Global Mercantile Private Limited vs. Ms Indo Unique Flame Limited & Ors.*, 2023 SCC OnLine SC 495 (para 69(ii)).

<sup>17</sup>The Indian Stamp Act, s 33:

Examination and impounding of instruments.—

(1) Every person having by law or consent of parties authority to receive evidence, and every person in charge of a public office, except an officer of police, before whom any instrument, chargeable, in his opinion, with duty, is produced or comes in the performance of his functions, shall, if it appears to him that such instrument is not duly stamped, impound the same.

(2) For that purpose every such person shall examine every instrument so chargeable and so produced or coming before him, in order to ascertain whether it is stamped with a stamp of the value and description required by the law in force in India when such instrument was executed or first executed:

Provided that—

(a) nothing herein contained shall be deemed to require any Magistrate or Judge of a Criminal Court to examine or impound, if he does not think fit so to do, any instrument coming before him in the course of any proceeding other than a proceeding under Chapter XII or Chapter XXXVI of the Code of Criminal Procedure, 1898 (V of 1898);

(b) in the case of a Judge of a High Court, the duty of examining and impounding any instrument under this section may be delegated to such officer as the Court appoints in this behalf.

(3) For the purposes of this section, in cases of doubt, —

(a) the State Government may determine what offices shall be deemed to be public offices; and

(b) the State Government may determine who shall be deemed to be persons in charge of public offices.

<sup>18</sup>However, it is to be noted that while the Supreme Court held that the arbitration agreement by itself is exigible to stamp duty, but the stamp duty for an arbitration agreement is extremely meagre. Therefore, the Courts can proceed on the basis that there is very little likelihood of such an arbitration agreement not being stamped; see, *Ms NN Global Mercantile Private Limited vs. Ms Indo Unique Flame Limited & Ors.*, 2023 SCC OnLine SC 495 (para 114(i)).

<sup>19</sup>Reliance placed on the judgment of Delhi High Court in *Uho Minda Ltd. vs. Revenue Department*, 2023 SCC OnLine Del 3598.

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