Kluwer Arbitration Blog

Stamp Of Invalidity Or Separate But Equal? The Indian Supreme Court Says: If Unstamped, Agreement Cannot Be Acted Upon

Shalaka Patil and Paulomi Mehta (Trilegal) · Wednesday, May 24th, 2023

In an India-seated arbitration, if your contract is unstamped or insufficiently stamped, the Supreme Court of India has now confirmed in its authoritative judgement passed on April 25, 2023, in *N N Global Mercantile Private Limited v. Indo Unique Flame Ltd. & Ors.* (*"NN Global"*) that this would be a valid ground to disallow acting upon the arbitration agreement until such defect is cured. In the judgment passed by a 3 to 2 majority, the dissenting minority view held that the stamping and impounding need not be done at the threshold stage and that non-stamping of the substantive contract would not render the arbitration agreement non-existent in law. In India, the Indian Stamp Act, 1899 (**"Stamp Act"**) requires all agreements or instruments to be stamped or paid up with stamp duty. As a fiscal law, it ensures the government is not deprived of revenue. Under the Stamp Act, a contract which is not stamped or insufficiently stamped is invalid and cannot be relied on for evidence by a party.

NN Global has far-reaching ramifications on all India-seated arbitrations where Stamp Act applies, whether domestic or international.

The decision in *NN Global* was rendered after a three-judge bench, in its 2021 judgment, made a reference to a larger bench to authoritatively settle the question- whether an arbitration clause contained in an unstamped agreement would be rendered invalid. An analysis of the prior 2021 three-judge bench judgement was presented in a blog post here.

This post explores how the determination of the validity of the arbitration agreement is likely to have an impact on litigation strategy, the appointment of arbitrators and how parties will weigh commercially- putting off payment of stamp duty against making upfront payment and opting for arbitration.

Prior decisions on the validity of arbitration agreements in unstamped agreements

In its latest decision *NN Global*, the Supreme Court has reasserted the legal position on this subject, which was previously expounded in *SMS Tea Estates v. Chandmari Tea (SMS Tea Estates)* and was followed in *Garware Wall Ropes v. Coastal Marine (Garware)* as also followed in *Vidya Drolia v. Durga Trading (Vidya Drolia)*. We trace these cases in brief.

In *SMS Tea Estates*, the Supreme Court determined that unless stamp duty and related penalty are paid on an agreement, the court cannot act on such an agreement and could do so only once the requisite duty was paid.

In *Garware*, the Supreme Court held that even a plain reading of Section 11(6A) (appointment of arbitrators) with Section 7(2) (arbitration agreement) of the Arbitration Act and Section 2(h) (an agreement enforceable by law is a contract) of the Contract Act, would make it clear that, an arbitration clause in an agreement would not exist when it is not enforceable by law. In *Vidya Drolia*, a three-judge bench of the Supreme Court affirmed the legal position set out in Garware and asserted that looking for the existence of an agreement would mean looking for its validity, which would include stamping, which is a mandatory requirement.

NN Global's impact on India's world view in its willingness to go to arbitration without hindrances

Some have argued that rendering an agreement, including an arbitration agreement (which would otherwise be severable), unenforceable on account of the contract being unstamped not only militates against the *kompetenz kompetenz* principle (in allowing an arbitral tribunal to decide these issues) but also allows a respondent to temporarily stymie the initiation of arbitration on the ground of a technical (even if legally accurate) argument of fiscal non-compliance which is curable. In practice, the impounding and stamping of instruments can take its own time and course, and during this period, parties will just have to wait until the stamping deficiency or penalty is made whole. If the stamp duty of the given state within India is ad-valorem, it may also disincentivise parties from initiating arbitration since they may consider commercial issues of litigating the dispute versus paying the stamp deficit. In the hands of a respondent, these procedural mechanisms create an opportunity for defence and leverage against a speedily rendered award.

However, the result cannot fault the accuracy of the decision when interpreting the law, even if it may have been the result of a strict, textualist reading of the Stamp Act. This case only reasserts and clarifies the position of law on stamping statutes and the validity of arbitration as well as their underlying agreements. In doing this, the Supreme Court has given primacy to compliance with fiscal requirements as one of the determinants of the validity of all agreements, including arbitration agreements.

The provision for the appointment of arbitrators under Section 11(6A) came from an amendment to the Arbitration Act in 2015. Under Section 11(6A), a court, while appointing arbitrators, is to be confined to the examination of the existence of an arbitration agreement. Although the Section was introduced in 2015 after the *SMS Tea Estates* case in 2011 and contains the words "*…notwithstanding any judgement, decree or order of any court…*", it is not to be construed that the mandatory provisions of the Stamp Act are not applicable to a court exercising discretion under Section 11(6A). This is plainly asserted in Garware in the following words:

> *It is clear, therefore, that the introduction of Section 11(6A) does not, in any manner, deal with or get over the basis of the judgment in SMS Tea Estates (supra), which continues to apply even after the amendment of Section 11(6A).*

Upholding both these decisions, the Supreme Court in the present case has held that the court appointing an arbitrator while inquiring into the existence of an arbitration agreement would have to consider the validity of the agreement itself and is duty-bound to act under Section 33 of the Stamp Act to examine and impound agreements found to be unstamped. Although a 2019 amendment has sought to delete Section 11(6A) from the Arbitration Act, the amending act has not been notified and is hence not in force.

None of the above means that the arbitral tribunal constituted by mutual agreement would be bereft of the jurisdiction to determine the validity of the arbitration agreement that constitutes it. However, parties now seeking to stymie or delay the appointment of arbitrators itself can raise questions of the validity of the arbitration agreement at the Section 11 stage and need not wait to file an application under Section 16 (Competence of tribunal to rule on its jurisdiction) before an already constituted tribunal.

Pertinently, the case fully relies on Section 35 of the Stamp Act along with Section 2(g) (an agreement not enforceable by law is said to be void) and 2(j) (a contract which ceases to be enforceable by law becomes void when it ceases to be enforceable) of the Indian Contract Act, 1872 and also with Section 7(2) (arbitration agreement) of the Arbitration Act such that an unstamped agreement and an insufficiently stamped agreement are both treated as unenforceable and consequently not to be acted upon unless the defect is removed with payment of the full duty or deficient duty with a penalty that may be applicable.

What does this case mean for the enforcement in India of agreements executed out of India? Section 3 of the Stamp Act broadly sets out what agreements are chargeable with stamp duty. Specifically, sub-section (c) of Section 3 makes an agreement executed out of India chargeable with stamp duty if it relates to property or a matter in India and the agreement is received in India.

Depending on the seat of arbitration within India, as stamping statutes vary from state to state, parties would have to pay an additional duty along with a penalty that a local statute may require.

The Supreme Court has clarified that it does not deal with this issue of non-stamping or insufficient stamping in the context of Section 9 petitions. It may therefore be argued that urgent interim reliefs can still be granted even if an agreement and arbitration agreement is unstamped or insufficiently stamped.

Conclusion

NN Global is an authoritative reassertion of the law on stamping and validity of arbitration agreements that is developed from *SMS Tea Estates* and continued in *Garware* and *Vidya Drolia*. Some may argue that insisting on stamping prior to initiation of arbitration is not efficient for the process itself, and an approach that could be adopted and which has been adopted in some courts would have been to appoint the arbitrator or arbitral tribunal, commence the arbitration but also impound the instrument for stamping and adjudication. This was achieved in *Shangrila Corporate Service Pvt. Ltd. v. Sanmina-Sci Technology India Pvt. Ltd.* before the Bombay High Court. In the context of an insufficiently stamped instrument, a similar approach was adopted by the Supreme Court previously in *Intercontinental v. Waterline* where since the agreement was insufficiently stamped but not unstamped, it was not complete “deadwood”, and the tribunal was appointed. This would achieve the twin objective of getting on with the arbitration and also paying the requisite

duty. The Supreme Court, however, has taken a strict view of the legal provision. In doing so, the commencement of arbitration through the appointment of a tribunal can be stalled on this ground.

In terms of litigation strategy, parties should carefully examine whether their agreements are sufficiently stamped as per the law of the state of the seat before they commence arbitration so as not to be met with this objection. Similar questions may be raised even if the agreement is being brought into another venue for arbitration. As pointed out above, stamping statutes vary state-wise and are prone to amendments that can alter the quantum of stamp duty and penalty to be paid. This also needs to be factored in as an upfront litigation cost before any commencement of an action.

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