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SC: VALIDITY OF AN UNSTAMPED/INSUFFICIENTLY STAMPED AGREEMENT IN RELATION TO SECTION 11(6A) OF THE ARBITRATION AND CONCILIATION ACT, 1996.

30 April 2019

Introduction:

The question that arose before the Supreme Court in the appeal in *Garware Wall Ropes Ltd vs Coastal Marine Constructions & Engineering Ltd*, Civil Appeal No 3631 of 2019 (present case) was whether the earlier judgement of the Supreme Court in the case of *SMS Teas Estates (P) Ltd Vs Chandmari Tea Co (P) Ltd*, (2011) 14 SCC 66 (*SMS Teas Estates*) would continue to apply to the introduction of Section 11 (6A) of the Arbitration and Conciliation Act 1996 (1996 Act), by way of the Arbitration and Conciliation (Amendment) Act 2015 (2015 Act).

The Supreme Court in *SMS Teas Estates* had held that where an arbitration agreement is contained in an unstamped/insufficiently agreement, the provisions of the Indian Stamp Act 1899 (Indian Stamp Act) require the judge hearing the application under Section 11 application under the 1996 Act (Section 11 application) to impound the agreement and ensure that stamp duty and penalty (if any) are paid thereon before proceeding with the Section 11 application.

On 10 April 2019, the Supreme Court in the present case has held 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)*". The basis for arriving at this decision was that an arbitration clause contained in an agreement would not exist when it is not enforceable by law, that is to say, when the agreement is unstamped/insufficiently stamped as per the Indian Stamp Act.

Brief Facts and Arguments of Parties:

The Supreme Court in the present case was hearing a challenge from a decision of the Bombay High Court, which allowed the Section 11 application of the Respondent for appointment of an arbitrator, notwithstanding that the sub-contract agreement between the Appellant and Respondent which contained the arbitration clause was not stamped.

The Appellant challenged the judgement of the Bombay High Court primarily on that the ground that Sections 33 and 34 of the Maharashtra Stamp Act 1958 (Maharashtra Stamp Act), which were similar to the provisions of the Indian Stamp Act viz Sections 33 and 35, required judicial authorities to impound instruments which cannot be admitted in evidence and acted upon until duly stamped. Whilst relying upon the 246th Law Commission Report, it was argued by the Appellant that the introduction of

Section 11 (6A) by the 2015 Act was necessitated as a result of two previous judgments of the Supreme Court in *SBP & Co v Patel Engineering Ltd*, (2005) 8 SCC 618 (*SBP & Co*) and *National Insurance Co Ltd v Boghara Polyfab (P) Ltd*, (2009) 1 SCC 267 (*Boghara Polyfab*) and not because of *SMS Teas Estates*, which remains untouched.

The Respondent referred to Sections 8, 16, and 45 of the 1996 Act and contended that the object of the 2015 Act in introducing Section 11(6A) was to confine the Court hearing a Section 11 application to the examination of the “existence” of an arbitration agreement and nothing more, not even its “validity”. This was supported by the argument that an arbitration agreement is independent of the agreement in which it is contained, and as long as the arbitration agreement is in writing, and therefore, the same “exists” in fact, the Court hearing the Section 11 application ought to appoint an arbitrator, leaving all other preliminary issues to the arbitrator. It was further argued that the Indian Stamp Act/Maharashtra Stamp Act are fiscal legislations intended to collect revenue and, if at all, will go to “validity” of the arbitration agreement and not to its “existence”.

Analysis and Decision by Supreme Court:

In deciding the present case, the Supreme Court considered relevant provisions contained in the 1996 Act and 2015 Act, in addition to provisions of the Maharashtra Stamp Act and Indian Contract Act 1872. The Supreme Court also analyzed the recommendation of the 246th Law Commission Report to introduce Section 11 (6A) as an amendment to the 1996 Act, as it was felt that the earlier judgments in the cases of *SBP & Co* and *Boghara Polyfab* required Section 11 of the 1996 Act to be revisited.

Apart from the above, the Supreme Court examined whether the decision in *SMS Tea Estates* was done away with by the expression “notwithstanding any judgment, decree or order of any Court” contained in Section 11(6A) of the 2015 Act.

In *SMS Tea Estates*, the lease deed was neither stamped nor registered and it was therefore held therein that “when a lease deed or any other instrument is relied upon as contending the arbitration agreement, the court should consider at the outset, whether an objection in that behalf is raised or not, whether the document is properly stamped. If it comes to the conclusion that it is not properly stamped, it should be impounded and dealt with in the manner specified in Section 38 of the Stamp Act. The court cannot act upon such a document or the arbitration clause therein. But if the deficit duty and penalty is paid in the manner set out in Section 35 or Section 40 of the Stamp Act, the document can be acted upon or admitted in evidence”

SMS Tea Estates had taken account of the mandatory provisions contained in the Indian Stamp Act and held them applicable to judicial authorities, which would include the Supreme Court and High Courts acting under Section 11 of the 1996 Act. This would mean that if the document was found to be not duly stamped, Section 35 of the Indian Stamp Act barred the said document from being acted upon, including the arbitration clause contained therein. The document was to be impounded and thereafter dealt with as per the provision of the Stamp Act.

The Supreme Court in the present case also discussed *SBP & Co* and held that Section 16 of the 1996 Act cannot be used to contend that an arbitration agreement has an independent existence of its own, and as such ought to be applied to Section 11 applications as well.

In the present case it was held that when an application under Section 11(4) to 11(6) of the 1996 Act is before a court, and it comes across as an arbitration clause in an agreement which is unstamped, the court is enjoined by the provisions of the Indian Stamp Act to first impound the agreement and see that stamp duty and penalty (if any)

is paid, before the agreement, as a whole, can be acted upon, including the arbitration clause therein. It was further held that Indian Stamp Act applies to the agreement as a whole and the arbitration clause cannot be bifurcated in order to give it an independent existence for certain limited purposes. Hence, introduction of Section 11 6A vide the 2015 Act would not in any manner override *SMS Tea Estates*, which continues to apply.

This was further cemented by the Supreme Court by its declaration that an agreement only becomes a contract if it becomes enforceable under the law, and under the Indian Stamp Act, an agreement does not become enforceable under law if the same is unstamped or insufficiently stamped. Hence, an arbitration clause contained in any such an agreement would not exist when it is not enforceable.

The Supreme Court also dealt with the “existence” of an arbitration agreement as opposed to the “validity” of an arbitration agreement, whilst understanding the expression “existence” as arrived at by the Supreme Court in *United India Insurance Co Ltd and Ors v Hyundai Engineering and Construction Co Ltd and Ors*, 2018 SCC OnLine SC 1045 (*United India Insurance Co*), wherein it was found that the insurer repudiated the claim, though an arbitration clause did “exist” in the policy, because it would not exist in law, when the insurer has not admitted or accepted liability. Similarly, if an arbitration clause forms part of an insufficiently/unstamped instrument, the arbitration clause would not exist as a matter of law until the instrument was duly stamped.

Recent Bombay High Court Judgment:

A recent judgment delivered on 4 April 2019 in the case of *Gautam Landscapes Private Limited Vs Shailesh Shah and Ors*, 2018 SCC OnLine SC 1045, by a Full Bench of the Bombay High Court had decided that a Court could act upon a document containing an arbitration agreement while considering an application under Sections 9 or 11 (6) of the 1996 Act, notwithstanding that the document was unstamped or insufficiently stamped.

The Supreme Court in the present case held that the latter decision was incorrectly made by the Bombay High Court, thus effectively overriding the Bombay High Court’s judgment, as far as its applicability to an application under Section 11(6) of the 1996 Act was concerned.

Conclusion:

This judgment may be viewed as a step back in the pro-arbitration direction adopted by most Courts in the recent past.

In addition to this, it can open the floodgates to parties raising such objections with the motive to stall the arbitration proceedings at the very nascent stage of appointment of arbitrators.

Further, the endeavor to have the stamp authorities decide the issue of payment of deficient stamp duty and penalty (if any) within 45 (forty five) days from receipt of the instrument is a far cry from what may be actually achievable.

Also, what is left to be tested, is the applicability of this judgment to applications under section 9 of the 1996 Act. The natural corollary would be that this judgment would also apply to such cases, which in turn could delay and affect the substantive rights of the aggrieved party.

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