India: Scope of Enquiry by The Court as to Existence of an Arbitration Agreement at The Pre-Arbitral Stage: An Indian Arbitration Law Perspective

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BACKGROUND

In the past few years, the Indian Government has realised that its justice delivery system especially in respect of commercial disputes needs to keep pace with India's economic growth. Though the Indian Arbitration and Conciliation Act, 1996 ("**Act**") is based on the UNCITRAL principles, judicial decisions had virtually obliterated the original intent of the Act and gravely undermined its avowed objective of expeditious dispute resolution. In fact, in certain kind of agreements, the author had started advising his clients not to incorporate arbitration clauses.

In order to resurrect arbitration as an efficient and preferred method of dispute resolution, the Law Commission of India in its 246th Report had suggested sweeping changes to the Act. Pursuant to the said Report, the Act was amended with effect from 23rd October 2015.

One of the significant amendments was insertion of sub-section (6A) in Section 11 of the Act which provided that at the stage of appointment of an arbitrator, the judicial authority exercising the power of appointment is to confine itself to the examination of the existence of an arbitration agreement. However, the judicial decisions which followed have been contrary to the intent of the amendment and have diluted this provision.

This article attempts to trace the history of the exercise of judicial power at the stage of appointment of arbitrators and offers a critical analysis of the most recent

judgment of the Supreme Court on the issue in *Garware Wall Ropes v. Coastal Marine Constructions & Engineering Ltd*.[1] ("Garware Wall Ropes")

Power Under Section 11: Judicial or Administrative

In *Konkan Railway Corporation Ltd. v. Mehul Construction Co.*[2], a three-judge bench of the Supreme Court held that the powers of the Chief Justice under Section 11(6) of the 1996 Act are administrative in nature, and that the Chief Justice or his designate does not act as a judicial authority while appointing an arbitrator. It was further held that when the matter is placed before the Chief Justice or his nominee under Section 11 of the Act it is imperative to bear in mind the legislative intent that the arbitral process should be set in motion without any delay whatsoever and all contentious issues are left to be raised before the arbitral Tribunal itself. This decision was confirmed by a five-judge bench in *Konkan Railway Corporation v. Rani Constructions*[3]

However, in *SBP & Co. v. Patel Engineering Ltd.*[4] **("SBP & Co.")**, a seven-Judge Bench of the Supreme Court overruled this view and held that the power to appoint an arbitrator under Section 12 is judicial and not administrative. It was held that while appointing an arbitrator under Section 11 of the Act, the court is entitled to decide the existence of a valid arbitration agreement, the existence or otherwise of a live claim, the existence of the condition for the exercise of power under Section 11 and the qualifications of the arbitrator(s).

The legal position was further expounded in *National Insurance Co. Ltd. v. Boghara Polyfab (P) Ltd.*[5] ("**Boghara Polyfab**") wherein the preliminary issues which may arise for consideration in an application under Section 11 were divided into three categories: (i) issues which the Chief Justice or his designate is bound to decide; (ii) issues which he can also decide, that is, issues which he may choose to decide; and (iii) issues which should be left to the Arbitral Tribunal to decide.

SPB & Co. and *Boghara Polyfab* widened the scope of enquiry under Section 11 to a large number of issues which could have been left to be decided by the arbitrator under Section 16 of the Act. The said decisions were widely criticised as being opposed to the principle of Kompetenz-kompetenz and contributing to delays in constitution of arbitral tribunals.

246th Report of Law Commission of India and Insertion of Sub-Section (6A) in Section 11

In the aforesaid context, the Law Commission of India in its 246th Report suggested the insertion of sub-section (6A) in Section 11 so as to restrict judicial intervention only to situations where the judicial authority finds that the arbitration agreement does not exist or is null and void. The relevant portion of the Report is extracted below:

"....If the judicial authority is of the opinion that prima facie the arbitration agreement exists, then it shall refer the dispute to arbitration, and leave the existence of the arbitration agreement to be finally determined by the arbitral tribunal. However, if the

judicial authority concludes that the agreement does not exist, then the conclusion will be final and not prima facie."

Pursuant to the recommendations of the Law Commission, Section 11(6A) was introduced with effect from October 23, 2015. The same is reproduced hereunder:

"*(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.*"

Judgments on the scope and interpretation of Section 11(6A)

In October 2017, a two-Judge Bench of the Supreme Court in *Duro Felguera S.A. v. Gangavaram Port Ltd.*[6] ("**Duro Felguera**") rightly held that after the 2015 Amendment, "*.... all that the Courts need to see is whether an arbitration agreement exists - nothing more, nothing less. The legislative policy and purpose is essentially to minimize the Court's intervention at the stage of appointing the arbitrator and this intention as incorporated in Section 11 (6A) ought to be respected.*"

In May 2018, a three-Judge Bench of the Supreme Court in *Oriental Insurance Company Ltd. v. Nardheram Power and Steel Private Limited*[7] ("**Oriental Insurance**") while interpreting an arbitration clause in an insurance policy held as under: "*If a clause stipulates that under certain circumstances there can be no arbitration, and they are demonstrably clear then the controversy pertaining to the appointment of arbitrator has to be put to rest.*"

Though the said judgment does not pertain to Section 11(6-A), it formed the basis for another decision by the same three-Judge Bench in *United Insurance Company Ltd. v. Hyundai Engineering and Construction Company Ltd.*[8] ("**United Insurance**"). United Insurance involved a similar insurance policy containing an arbitration clause which provided that no difference or dispute shall be arbitrable if the insurance company had disputed or not accepted liability. The three-Judge Bench in *United Insurance* distinguished *Duro Felguera* and held that the matter before it was not arbitrable as the insurance company had in fact raised a dispute.

The Delhi High Court in *NCC Ltd. v. Indian Oil Corporation Ltd.*[9] analysed the effect of insertion of Section 11(6-A) after referring to *Duro Felguera*, *Oriental Insurance* and *United Insurance* and in the author's, opinion arrived at the correct conclusion. The relevant portion of the said judgment is extracted below:

"*59.1 .....To my mind, once the Court is persuaded that it has jurisdiction to entertain a Section 11 petition all that it is required to examine, is, as to whether or not an arbitration agreement exists between the parties which is relatable to the dispute at hand. The latter part of the exercise adverted to above, which, involves correlating the dispute with the arbitration agreement obtaining between the parties, is an aspect which is implicitly embedded in Subsection (6A) of Section 11 of the 1996 Act, which, otherwise, requires the Court to confine its examination only to the existence of the arbitration agreement. Therefore, if on a bare perusal of the agreement, it is found that a particular dispute is not*

relatable to the arbitration agreement, then, perhaps, the Court may decline the relief sought for by a party in a Section 11 petition. However, if there is a contestation with regard to the issue as to whether the dispute falls within the realm of the arbitration agreement, then, the best course would be to allow the Arbitrator to form a view in the matter.

59.2 Thus, unless it is, in a manner of speech, a chalk and cheese situation or a black and white situation without shades of grey, the concerned Court hearing the Section 11 petition should follow the more conservative course of allowing parties to have their say before the Arbitral Tribunal."

Thereafter, a two-Judge Bench of the Supreme Court in *Vidya Drolia and Ors. v. Durga Trading Corporation*[10] ("**Vidya Drolia**") after referring to Section 11 (6-A), Section 16, the relevant portion of the 246th Law Commission Report, and *Duro Felguera*, observed as follows:

"*It will be noticed that "validity" of an arbitration agreement is, therefore, apart from its "existence". One moot question that therefore, arises, and which needs to be authoritatively decided by a Bench of three learned Judges, is whether the word "existence" would include weeding-out arbitration clauses in agreements which indicate that the subject-matter is incapable of arbitration.*"

In *Gautam Landscapes Pvt. Ltd. v. Shailesh Shah and Ors.*[11] ("**Gautam Landscapes**"), two questions were considered by a Full Bench of the Bombay High Court:

a. Whether any interim relief under Section 9 of the Act can be granted when a document containing arbitration clause is unstamped or insufficiently stamped?
b. Whether an arbitrator can be appointed under section 11 in respect of an arbitration clause in an agreement that is not stamped or is insufficiently stamped?

The Bombay High Court answered the first question in the affirmative and held that awaiting adjudication on stamp duty before granting relief would defeat the scheme and provisions of the 1996 Act. It was further held that the arbitration agreement was separate and distinct from the document in which it was contained and would not require stamping. While answering the second question, it held that the appointment of arbitrators need not await adjudication of stamp duty and penalty.

The Supreme Court has very recently on April 10, 2019 held in *Garware Wall Ropes* that when a court is called upon to decide on an application for appointment of an arbitrator under Section 11 of the Act on the basis of an arbitration clause in an agreement which is unstamped or deficiently stamped, the court must first impound the agreement, send it to the concerned authority for adjudication and payment of stamp duty and penalty (if any), and proceed with the application only after such stamp duty and penalty have been paid.

In holding so, the Supreme Court reiterated its earlier judgment in *SMS Tea Estates v Chandmari Tea Company Pvt. Ltd.*[12] ("SMS Tea Estates") and stated that the law laid

down in *SMS Tea Estates* continues to apply even after introduction of Section 11(6A). It has also overruled the judgment of the full bench of the Bombay High Court in *Gautam Landscapes* expressly with respect to the 2nd question mentioned above.

Comments

Garware Wall Ropes lays down that even though Section 11(6A) requires the courts to examine only the existence of an arbitration agreement, it would include within its sweep the issue whether the agreement is duly stamped or not. While this judgment is binding and would have to be followed as of now, the following issues may require a re-examination by a larger bench at an appropriate time:

a. The legislature seems to have deliberately used the term "existence" in Section 11(6A) as opposed to the word "valid" as used in Sections 8, 36, 48 and 54. An agreement on account of not being sufficiently stamped, may not be capable of being acted upon or enforced. However, it cannot be said that such an agreement is not in existence. As correctly observed in *Vidya Drolia*, this issue needs to be decided by a three-judge bench.
b. Section 11(6A) requires the court to confine itself to examination of the existence of an arbitration agreement "*notwithstanding any judgment, decree or order of any Court*". It is clear that the intent behind introduction of Section 11(6A) was to avoid a comprehensive examination at the pre-arbitral stage and to nullify the effect of any prior judgment to the contrary whether it be *SPB & Co.*, *Boghara Polyfab* or *SMS Tea Estates.* However, it has been held in *Garware Wall Ropes* that since there is no mention of *SMS Tea Estates* in the Law Commission Report, it continues to be binding. If the intent of Section 11(6A) was only to address the mischief caused on account of the two judgments mentioned in the Report, i.e., *SPB & Co.* and *Boghara Polyfab*, Section 11(6A) would not have used such wide language.
c. In the course of the judgement, the bench also observed that an arbitration clause contained in an agreement does not have an independent existence. However, it has been repeatedly held by the Supreme Court in prior judgments especially, *Reva Electrical Car Company Private Ltd. v. M/s Green Mobil*[13], *Today Homes and Infrastructure Pvt. Ltd. v. Ludhiana Improvement Trust*[14] and *Enercon (India) Ltd. & Ors. v. Enercon GmbH & Anr.*[15] that an arbitration clause which forms part of a contract has to be treated as an independent agreement. The observation of the Supreme Court in paragraph 83 of *Enercon (Indihyup) Ltd.* in this regard is extremely pertinent and is reproduced below:

> "*83. The concept of separability of the arbitration clause/agreement from the underlying contract is a necessity to ensure that the intention of the parties to resolve the disputes by arbitration does not evaporate into thin air with every challenge to the legality, validity, finality, or breach of the underlying contract. The Indian Arbitration Act, 1996, as noticed above, under Section 16 accepts the concept that the main contract and the arbitration agreement form two independent contracts. Commercial rights and obligations are contained in the underlying, substantive, or the main contract. It is followed by a second*

contract, which expresses the agreement and the intention of the parties to resolve the disputes relating to the underlying contract through arbitration. A remedy is elected by parties outside the normal civil court remedy. It is true that support of the national courts would be required to ensure the success of arbitration, but this would not detract from the legitimacy or independence of the collateral arbitration agreement, even if it is contained in a contract, which is claimed to be void or voidable or unconcluded by one of the parties."

d. If a document were to be impounded at the stage of an application under Section 11(6), the 60-day period provided in Section 11(13) of the Act would most likely be breached and the avowed objective of the amendment to expedite the arbitration process and ensure minimal intervention of the courts would be defeated. It may have been more prudent to appoint an arbitrator while simultaneously impounding the agreement and directing the party responsible for payment of stamp duty to submit the duly stamped agreement with the arbitrator(s) during the course of arbitration proceedings. This would have ensured expeditious disposal of the Section 11 application while at the same time avoiding any delay to the arbitration proceedings.

Footnotes

1. 2019 SCC OnLine SC 515

2. (2000) 7 SCC 201

3. (2002) 2 SCC 388

4. (2005) 8 SCC 618

5. (2009) 1 SCC 267

6. (2017) 9 SCC 729

7. (2018) 6 SCC 534

8. 2018 SCC OnLine SC 1045

9. ARB.P 115/2018

10. Civil Appeal No. 2402 of 2019

11. (2019) SCC OnLine Bom 563

12. (2011) 14 SCC 66

13. 2012 (2) SCC 93

14. (2014) 5 SCC 68

15. (2014) 5 SCC 1

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

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