
NAVIGATING THE STAMP ACT: VALIDITY OF ARBITRATION CLAUSES IN BINDING LETTERS OF INTENT

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ABSTRACT

With the recent judicial pronouncements in *NN Global* in its construction of Arbitration Agreements vis-a-vis unstamped contracts and the inherent validity thereof, it is asserted that a binding letter of intent containing an Arbitration Clause must be construed as a valid reference to arbitration, notwithstanding the *NN Global* verdict. Section 2(1)(b), read with Section 7 of the Arbitration and Conciliation Act, 1996, provides that a reference to arbitration can either be a separate agreement, or a part of a contract in the form of a reference clause. As a norm in modern commercial practice where interim agreements take the form of binding letters of intent, the question of whether such a letter needs to be stamped is inconclusive as neither the Stamp Act nor the Arbitration and Conciliation Act make clear whether a stamp is required for such documents to be given force. It is argued that such a stamping requirement does not exist as the form of letters of intent falls outside the scope of 'agreement' as per the Stamp Act and, therefore, operable as valid references to Arbitration.

Introduction

Arbitration as a legal framework evolved primarily as a consequence of commercial transactions. The 1996 Act¹ sought to consolidate and amend the laws that related to 'arbitration'.² This is not to say however, that the laws relating to arbitration were only introduced in the year 1996.³ Regardless, the concept of arbitration exists to give recourse to parties wishing to settle matters outside of the strict and regulated nature of court⁴ action. The law seeks to do this in two ways – either on mutual agreement of the parties⁵ or alternatively on a reference by the court which is amenable to the parties.⁶ In either instance, it is through party action that an issue is referred to arbitration by a tribunal.

As a matter of practice therefore, a matter is referred to arbitration by party reference when a clause to that effect is entered into the contract in question, or an arbitration agreement is drafted pertaining to a particular commercial relationship.⁷ In either instance when the parties wish to pre-decide on a matter going to arbitration it must be codified as a matter of an arbitration agreement. In such a case therefore, what is important is the intent of the parties to resolve the dispute outside the court infrastructure.

The current position of law on the matter, in lieu of the NN Global decision⁸ indicates that when a reference to arbitration takes the form of an arbitration clause in a contract, the lack of a stamp, or a sufficient stamp, on the parent contract shall deem the reference to arbitration inoperable.⁹ The implication of this decision remains that if a separate agreement to arbitrate was to be exercised between the parties, even that would be influenced by the stamping status on the contract that it is in relation to. This raises a multitude of questions, chief among which is the comparable standard required to test the inoperability of the arbitration agreement. Does,

¹ Arbitration and Conciliation Act, 1996, No. 26, Acts of Parliament, 1996 (India).

² Arbitration and Conciliation Act, 1996, preamble to the Arbitration and Conciliation Act, No. 26, Acts of Parliament, 1996 (India).

³ Anushka Kumar, *Evolution and Development of the Law of Arbitration in India*, 5 INDIAN J.L. & LEGAL Rsch. 1 (2023).

⁴ A Brief History of Arbitration,

https://www.americanbar.org/groups/tort_trial_insurance_practice/publications/the_brief/2018-19/summer/a-brief-history-arbitration/ (last visited Nov 3, 2023).

⁵ Arbitration and Conciliation Act, 1996, § 8, No. 26, Acts of Parliament, 1996 (India).

⁶ *Id.*

⁷ Arbitration and Conciliation Act, 1996, § 7, No. 26, Acts of Parliament, 1996 (India).

⁸ N.N. Global Mercantile (P) Ltd. v. Indo Unique Flame Ltd., (2023) 7 SCC 1.

⁹ *Id.*

for instance, a mail reference to arbitration allow the arbitration procedure relating to a contract that has not been sufficiently stamped, to operate?

In this vein, the fundamental question that this article seeks to answer is in regard to the extent of the term ‘arbitration agreement’¹⁰ vis-à-vis a Binding Letter of Intent (henceforth referred to as LOI) and whether such a document would fall within the stamping requirements of the Stamp Act.¹¹

The root to both of these questions can be found to some extent in the case of NN Global where in no small part the extent of the stamp act’s influence on Arbitration has been analysed and deconstructed.¹² This article shall evaluate the rationale forwarded in that judgement and consider whether such a rationale can be extended to a binding LOI as well.

Examination of the Parameters of the Arbitration Act vide an Arbitral Clause

The predominant law in the force in the country is that of the Arbitration and Conciliation Act (henceforth referred to as the Arbitration Act), 1996¹³ which seeks to act as a consolidated corpus of laws relating to arbitration and conciliation both in the domestic as well as the international sphere. The act in its attempt to holistically enumerate on all the aspects of arbitration provides within its ambit a clear and concise understanding of what can be considered an ‘arbitration agreement’ provided in section 7 of the act and provides as follows:

“(1) In this Part, “arbitration agreement” means an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not.

(2) An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

(3) An arbitration agreement shall be in writing.

(4) An arbitration agreement is in writing if it is contained in—

¹⁰ *Supra* note 7.

¹¹ The Indian Stamp Act, 1899, § 3, No. 2, Acts of Parliament, 1899 (India).

¹² *Supra* note 8.

¹³ *Supra* note 2.

(a) a document signed by the parties;

(b) an exchange of letters, telex, telegrams or other means of telecommunication 1 [including communication through electronic means] which provide a record of the agreement; or

(c) an exchange of statements of claim and defence in which the existence of the agreement is alleged by one party and not denied by the other.

(5) The reference in a contract to a document containing an arbitration clause constitutes an arbitration agreement if the contract is in writing and the reference is such as to make that arbitration clause part of the contract.”¹⁴

In specifically observing clause (2) of the section, one can draw a distinction between arbitration agreements of two forms – a clause in the contract; *or* a separate agreement.

In either case, the court is mandated to, as per the succeeding section refer all disputes of such a nature appearing before it to arbitration as long as it is not *prima facie evident* that there is no valid arbitration agreement.¹⁵ The language of this section primarily spawns the reasoning of the judiciary in the NN Global judgement¹⁶ that shall be discussed in due course.

The intervention of the court exists at a multitude of levels as per the act, from in referring the dispute¹⁷, to enforcement¹⁸, and even at the stage of appointment of arbitrators.¹⁹ This however does not indicate the broad leave granted to the court to intervene in all matters of arbitration. The role of the court is two-fold under the act, sometimes administrative and sometimes judicial.²⁰ It has been noted that the leave granted in terms of appointment remains in the judicial realm²¹ and therefore an examination of the validity of the arbitration agreement for this purpose would also exist in a judicial setting.²² This would attract action under the relevant

¹⁴ *Supra* note 7.

¹⁵ *Supra* note 5.

¹⁶ *Supra* note 8.

¹⁷ *Supra* note 5.

¹⁸ Arbitration and Conciliation Act, 1996, § 36, No. 26, Acts of Parliament, 1996 (India).

¹⁹ Arbitration and Conciliation Act, 1996, § 11, No. 26, Acts of Parliament, 1996 (India).

²⁰ Garware Wall Ropes Ltd. v. Coastal Marine Constructions & Engg. Ltd., (2019) 9 SCC 209; (2019) 4 SCC (Civ) 324.

²¹ SMS Tea Estates (P) Ltd. v. Chandmari Tea Co. (P) Ltd, 2010 SCC OnLine Gau 762.

²² *Supra* note 8.

provisions of the stamp act requiring a non-recognition of an unstamped document and further also an impounding of that document till such time as the stamp duty is paid on it.²³

It is therefore contended as a matter of application, that an examination of the validity of the arbitration agreement is a matter of judicial action under jurisprudential precedent²⁴ and therefore susceptible to be barred under the stamp act that determines unstamped documents to be inadmissible as evidence²⁵. The Court in NN Global utilised all of this to legally argue that it was bound by the stamp act to impound contracts that were brought to its attention bereft of the ‘appropriate’ stampage. This was held even though the primary applicability of separability doctrine²⁶ would require the court to refer all matters to arbitration regardless of the inherent flaws in the contract – being bound only to consider whether there existed an arbitration agreement.

This judgement detracted from this legal position in two ways – firstly in transposing the insufficiency of stamp duty onto the arbitration agreement, the court seeks to traverse between two agreement – one that requires stamp duty and one that does not. The requirement on the former seems therefore to also transfer to the latter, in which case the inherent divergence between the two agreements becomes meaningless. Concurrently, by acknowledging that the contract has insufficiently been stamped while also holding an arbitration clause, the court is convinced of the contract’s ‘existence’ therefore dispensing with their duty under the Arbitration act²⁷. A further examination of the contract, especially on admissibility as a matter of ‘evidence’²⁸ would be *prima facie* unwarranted under the said act.

Now the question that this article seeks to raise and answer is whether two assertions can be made –

- a) A binding LOI is a ‘agreement’ as per the Stamp act and is therefore bound by the same requirements as a agreement under the said act²⁹

²³ See The Indian Stamp Act, 1899, § 33, No. 2, Acts of Parliament, 1899 (India); *see also* The Indian Stamp Act, 1899, § 35, No. 2, Acts of Parliament, 1899 (India).

²⁴ *Supra* note 20.

²⁵ The Indian Stamp Act, 1899, § 35, No. 2, Acts of Parliament, 1899 (India).

²⁶ Arbitration and Conciliation Act, 1996, § 16, No. 26, Acts of Parliament, 1996 (India); *see also* GARY B BORN, INTERNATIONAL COMMERCIAL ARBITRATION 81 (3d ed. 2020) at 377.

²⁷ *Supra* note 5.

²⁸ *Supra* note 8.

²⁹ *Supra* note 11.

- b) An arbitration clause in a binding LOI that is not stamped is an invalid reference to arbitration.

The Applicability and Relevance of the Stamp Act

The Indian Stamp act, a holdout from colonial times, requires certain documents to be stamped in a certain manner.³⁰ It exists as a means of government profiteering aimed at exchanging government acknowledgement for a certain price, oftentimes a percentage of the overall transacted amount.³¹

A contract must be stamped according to the act³², the question raised however, is whether a document that performs the preliminary position of an agreement but has none of the commercial connotations of an agreement³³, is subjected to the same stamping requirements under the act.

The term ‘instrument’ under the act is understood to be any document by which rights and liabilities are transferred or proprot to be transferred regardless of whether the instrument is executed online or otherwise.³⁴ A contract exists as a means of creating a special commercial relation.³⁵ Therefore it does fall within this definition. An instrument of a commercial kind, such as an agreement enshrined under the schedule of the act³⁶, so insufficiently stamped becomes subject to certain scrutiny, chief among which is the provisions of the act mandating impounding reproduced hereunder –

“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 pubic 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.

³⁰ *Supra* note 11.

³¹ The Indian Stamp Act, 1899, Schedule I, Art. 5, No. 2, Acts of Parliament, 1899 (India).

³² *Supra* note 11.

³³ *Infra* note 43.

³⁴ The Indian Stamp Act, 1899, § 2 (14), No. 2, Acts of Parliament, 1899 (India).

³⁵ The Indian Contract Act, 1872, § 2, No. 9, Acts of Parliament, 1872 (India).

³⁶ *Supra* note 31.

(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 1 [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 1989);

(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... ”³⁷

Thus, it is clear that when a document comes before the court, it is mandated to look into its status of stampage. This can be construed as an affirmative duty on the court and takes the form of a clear direction towards an investigative action. The question that the NN Global judgement in some level answered was regarding the nature of the court’s investigative powers under the Arbitration Act.

This position is further exacerbated by the clear enumeration of the schedule itself, which in its wordings provides for a ‘residuary clause’ which creates something of an overarching provision that involves within its ambit ‘all agreements’.³⁸ This therefore, in no small part necessitates stamps on agreements of any kind, that fall within the scope of the definition of an instrument owing to the language of the section 3.³⁹

The Interplay Between the Arbitration Act and the Stamp Act

With respect to general contracts, on a concurrent viewing of the two acts in question it becomes clear that the court is to play a dual role. *Firstly* to identify the existence or lack thereof of the contract, and *secondly* to test its competence vide the stamp act. *Only after*

³⁷ The Indian Stamp Act, 1899, § 33, No. 2, Acts of Parliament, 1899 (India).

³⁸ *Supra* note 31.

³⁹ *Supra* note 11.

dispensing with these two duties can the court forward the procedure into the hands of the Arbitral Tribunal.

The issue comes when contemplating the question of in what capacity the court delves into its second duty. If this investigation is to test the *validity* of the instrument then the court's role self-destructs owing to the arbitration act's provisions vesting the *Competence* to determine the validity of the arbitral proceeding to the tribunal and excluding the court from making such a determination.⁴⁰

If, however, the impounding duty of the court can be envisaged to run separate and parallel to the dispute of the substance of the contract that the tribunal is primarily concerned with, then the court's duties remain distinct. However, in such a case, the power vested in the tribunal is restricted beyond the purview of the act owing to a possibility of contrary determination i.e., the tribunal is disallowed from a finding contrary to the court regarding the sufficiency or lack thereof of stamping on the document. Further, if such concurrent viewing was to be permitted, then the court could be precluded from its duty all together where the parties are bilaterally submitting to arbitration.

From all of this, it is clear that the legislations are in some part mutually exclusive. They cannot, for instance be read together to concurrently test the validity of a contract. To further add to the issue, as per the doctrine of separability⁴¹, the court's duty to test the stamping on the contract would necessarily not extend to the arbitration agreement.⁴²

The Minutia of Difference: An LOI And A Contract with an Arbitration Clause

A contract and a Binding LOI differ in a variety of key factors. While the both of them exist in some small part to further a specific commercial relation⁴³, the fact remains that one exists as a crystallisation of a party's intent towards enacting a *certain set of contractual actions* while the other exists more as a codification of a party's intent to enter into a contract sometime in

⁴⁰ Arbitration and Conciliation Act, 1996, § 16, No. 26, Acts of Parliament, 1996 (India); r/w Arbitration and Conciliation Act, 1996, § 5, No. 26, Acts of Parliament, 1996 (India).

⁴¹ Arbitration and Conciliation Act, 1996, § 16, No. 26, Acts of Parliament, 1996 (India).

⁴² *Supra* note 8.

⁴³ Jean Feriancek, *What Did You Agree to in Your Letter of Intent?*, 23 NATURAL RESOURCES & ENVIRONMENT 42 (2008).

the future.⁴⁴

Thus, one exists as an initiation of a commercial *transaction*, whereas the other works more to initiate a commercial *relation*.⁴⁵

In analysing this vis-à-vis the question of whether an arbitration clause in such a document has any value, it may be prudent to re-visit the wordings of the act in reference to the definition of the same. The act makes it clear that there exists no specific 'binding' requirement in the source document that the arbitration clause is embedded in.⁴⁶ Even if that requirement existed, it would be redundant to the arbitral clause in the first case owing to its separate nature.⁴⁷

Thus, an arbitral clause embedded in a contract is indistinguishable in its effect to one that is not so embedded.⁴⁸ The only difference between the nexus therefore, would be the manifestation of the forthcoming dispute, and therefore the matters that the tribunal shall have to restrict its adjudication on.

From all of this it is clear that the nature of whether the arbitral clause is embedded in a contract or an LOI is irrelevant to the actual arbitration agreement itself while at the same time clearly differentiating between the two types of documents. To further illustrate this difference in the context of an arbitration, it may be prudent to visit the following illustration:

A and B enter into a contract for the temporary lease of a property taken for the purpose of a restaurant. An arbitration clause in such a contract would pertain to all forms of disputes that could arise out of such a lease agreement, including but not limited to a dispute as to the quantum of the lease amount, the duration of occupation and so on. However, if A and B entered instead into an LOI that contemplated the enactment of a contract to lease said property, the nature of the dispute that the arbitration clause would subsume, exists only within the scope of an inaction on the side of one of the parties to enter into the subsequent contract. None of the actual deliverables of the potential contract may be the cause of the dispute referred, due to the fact that such deliverables are not yet legally required to be exchanged.

⁴⁴ South Eastern Coalfields Ltd & Others vs. M/s S Kumar's Associations AKM (JV), Civil Appeals No. 4358 of 2016.

⁴⁵ Dresser Rand S.A. vs. Bindal Agro Chem Ltd. & Anr, (2006) 1 SCC 751.

⁴⁶ *Supra* note 7.

⁴⁷ *Supra* note 26.

⁴⁸ *Supra* note 7.

In either circumstance, the arbitral reference shall remain unimpeded. However, the LOI shall remain distinct from an agreement in the eyes of the stamp act, owing to it not really creating an exchange of rights and liabilities.⁴⁹

Thus from the eyes of the law, an LOI can at best be considered an invitation to offer present in the general jurisprudence.⁵⁰ A contract in the converse, is seen as a culmination of the offer-acceptance cycle.⁵¹

Examining the Application of the Stamp Act and the Arbitration Act on an LOI:

From the points raised over the course of the other parts of this paper, the scope of discussion on applicability becomes clear. The question that an LOI must answer is in the nature of its inclusion in the various criteria of the Stamp Act's ambit. Regardless, it is clear that the terms of the LOI as it pertains to an arbitral clause is valid as demonstrated in the preceding part. Therefore, the only question that a discussion on this matter is regarding whether the impounding requirements under the stamp act⁵² as enunciated by the court⁵³ extends to it.

While this exact question may not have been particularly engaged with by the broader corpus of literature that exists, it is nonetheless extrapolatable from the juristic position therein. By concluding that a requirement under the stamp act ought be curable in the realms of the stamp act itself⁵⁴, the authors seem to extrapolate all 'agreements' to fall within the scope of the specific requirement⁵⁵, as has also been enumerated in the parts above. On a charitable visitation, such a position might be to some degree meritorious.

This is because, the language of the definition of an instrument analysed above seems to involve within its ambit anything that could create a potential exchange of liabilities and rights.⁵⁶ Thus, owing to the nature of an LOI that would precede an agreement that falls within the scope of

⁴⁹ *Supra* note 34.

⁵⁰ *Harvey v. Facey*, [1893] AC 552.

⁵¹ *Supra* note 35.

⁵² *Supra* note 37.

⁵³ *Supra* note 8.

⁵⁴ Tejas Karia & Vrinda Pareek, *Stamping of Arbitration Agreements: An Analysis of the Evolving Arbitration Landscape in India*, 3 INDIAN REV. INT'L ARB. 44 (2023).

⁵⁵ *Id.*

⁵⁶ *Supra* note 34.

the Stamp Act⁵⁷ tending to create in the future, on the enactment of said agreement, an exchange of rights and liabilities, the stamping requirement would flow.

This position argues therefore, that by creating an LOI one would necessarily create a future exchange of rights and liabilities and therefore would require a stamp be affixed in the manner prescribed by the act.

This position however, is flawed.

The argument that an LOI can fall within the scope of an 'instrument' underpins the core of this contention. It is asserted by the author, that there can be no such conclusion made. To form an active exchange of rights and liabilities, an LOI must act as something greater than a mere invitation to offer as enunciated above.

This however does not seem to correctly characterise the nature of an LOI. As has been noted above, the letter of intent merely exist as a crystallisation of a party's intent to enter into an agreement *in the future* as that intent exists *at that point of time*. No legal rights are derived from such a letter except insofar as it evidences such an intent.

Therefore, it cannot fall within the scope of the requirements of an 'instrument' as pervaded in the stamp act, and thereafter in applicable under the heading of an agreement as per the Ist schedule.

Conclusion:

In conclusion, the analysis of the validity of an arbitral clause within a letter of intent is marred with complex deliberations on the confluence of multiple legislations. Throughout the analysis forwarded over the course of this paper, the author has attempted to highlight the lack of clarity and consistency in the legal framework regarding the stamping requirements for such documents.

One of the key arguments presented in this paper is that binding letters of intent do not fall within the scope of the Stamp Act's definition of an "instrument" or an "agreement." It is asserted that these letters merely serve as a crystallization of a party's intent to enter into a

⁵⁷ *Supra* note 31.

future agreement, and therefore, no legal rights are derived from them. As a result, it is contended that stamping requirements should not apply to binding letters of intent.

Furthermore, in exploring the issue of whether an unstamped arbitration clause in a LOI can be considered a valid reference to arbitration, the Arbitration and Conciliation Act's position becomes pertinent. While the Stamp Act requires stamping on all instruments, including arbitration agreements, the Arbitration and Conciliation Act provides for the validity of arbitration agreements contained in documents that may not be stamped. This discrepancy raises questions about the enforceability of arbitration clauses in binding LOIs.

Furthermore, the doctrine of separability, which asserts that an arbitration agreement is separate from the underlying contract, indicates that the validity of the arbitration agreement should not be affected by any deficiencies in stamping of the contract itself. However, the analysis reveals that the court's duty to test the stamping on the contract may impede the tribunal's authority to determine the validity of the arbitration proceedings. This creates a potential conflict between the court and the tribunal in determining the enforceability of the arbitration clause.

In light of these complexities, it is clear that there is a need for greater clarity and consistency in the legal framework surrounding the stamping requirements for LOIs and the validity of arbitration clauses within them. The lack of clear guidelines leaves parties uncertain about the enforceability of their agreements and may lead to unnecessary disputes and delays in the resolution of disputes through arbitration.

In conclusion, the analysis presented in this paper highlights the complexities and uncertainties surrounding the stamping requirements for binding letters of intent and the validity of arbitration clauses within them. The lack of clarity in the legal framework calls for a comprehensive review and potential amendments to ensure consistency and certainty in the enforceability of these agreements.