SEPARABILITY DOCTRINE IN INDIA- AN ANALYSIS OF ITS ORIGIN AND EFFECT

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INTRODUCTION

According to the Doctrine of Separability, the arbitration clause in a contract is considered to be separate from the main contract and survives acts such as breach, invalidity and termination of the main contract. This principle is considered to be one of the practical cornerstones of Arbitration. This principle ensures that on a breach of contract, the contract is not destroyed for all purposes but instead, it survives for the purpose of measuring damages arising from the breach and determining the mode of settlement. However, there have been instances where the scope of this doctrine has been misinterpreted in a broader sense. This article analyses the origin and effect of the doctrine especially on unstamped agreements and critically examine the scope of the doctrine in the context of India.

IMPORTANCE AND NEED FOR THE DOCTRINE

An arbitration could lead to an end even before starting if a party who is wishing to evade arbitration argues that the arbitration clause of the agreement is invalid as a result of the main agreement being invalid. Furthermore, the arbitration can also end if the tribunal does not have the jurisdiction to render the award. If such arguments are accepted, then the party would have no choice left but to go for litigation which is against the expressed intention of the parties to solve the disputes through arbitration. When a tribunal faces such challenges, this doctrine comes to the rescue. It was created so as to act as a shield against these arguments. In a recent judgement of Buckeye Check Cashing Inc. vs. Cardegna, the Supreme Court of United States stated how the separability principle permits the court to "enforce an arbitration in a contract that the arbitrator later finds to be void."[1] As stated by Lord MacMillan,

[1] Buckeye Check Cashing Inc. vs. Cardegna 546 U.S. 440 (2006).

"A contract survives for the purpose of measuring the claims arising out of breach, and the arbitration clause survives for determining the mode of their settlement."[2]

ORIGIN

This Doctrine was originated from a French judgement, Etablissements Raymond Gosset v. Frère Carapelli.,[3]where it was decided that arbitration of the complainant's claims was required since he was challenging the general contract rather than the arbitration clause in particular. Furthermore, the court also stated that the principle would not apply in cases where the parties never agreed for arbitration in the first place or were fraudulently induced into signing the agreement relating to arbitration. After few years, the Supreme Court of the United States also acknowledged the doctrine of separability in the case of Prima Paint Corp. v. Flood & Conklin Mfg. Co.[4] the doctrine of separability of the arbitration clause has adopted widely by various courts, legislations, etc. since then.

In 1955, the International Chamber of Commerce (ICC) became the first institutionalized arbitral centre that recognized the doctrine under Article 13 of ICC Rules of Arbitration, 1955. [5] Furthermore in 1984, the UNCITRAL Model Law on International Commercial Arbitration incorporated the doctrine in Article 16 which states that an arbitration clause shall be treated as an agreement which is independent of other terms of the contract.[6]

DEVELOPMENT IN INDIA

The entry of the doctrine was a result of enactment of Arbitration and Conciliation Act, 1996 which is the Indian law of arbitration and is based on the UNCITRAL Model Law. Section 7(2) of the Act states that an arbitration agreement may be in the form of an arbitration clause in a contract or as a separate agreement.[7]Section 16(1)(a) explicitly states that an arbitration clause shall be treated as an agreement independent of the term of the contract[8]. From a combined reading of both the sections, we can extrapolate how the doctrine of separability has been incorporated into Indian Arbitration law.

[2]Heyman and Another v Darwins, Limited AC 356, 374 (1941) (Lord Macmillan)
[3] Etablissements Raymond Gosset v. Frère Carapelli.,French Int'l Arb. L. Rep. 545, (1963).
[4] Prima Paint Corp. v. Flood & Conklin Mfg. Co., 18 L.Ed 2d 1270, (1967).
[5] ICC Rules of Arbitration, (1955), art.13.
[6] UNICTRAL Model Law on International Commercial Arbitration, 1994, art. 16..
[7] The Arbitration and Conciliation Act, 1996, S.7(2), No.3, Acts of Parliament, 1996.
[8] The Arbitration and Conciliation Act, 1996, S.16(1)(a), No.3, Acts of Parliament, 1996.

However, even after the Arbitration and Conciliation Act came into force, the issue of the survival of the arbitration clause after the termination or breach of contract has been the point of discussion in many cases in India. Such cases paved way for the development of the doctrine of separability in India.

In the case of Enercon Ltd. & Ors. V Enercon Gmbh & Anr,,[9] the Supreme Court upheld the independence of the collateral arbitration agreement even when it was contained in the contract which was claimed to be void or voidable. In the case of National Co-op Marketing Federation India Ltd v Gains Trading Ltd,[10] it was held by the Apex Court that "the arbitration clause is a collateral term in the contract which relates to resolution disputes and not performance." In the case of P.Manohar Reddy & Bros. v Maharashtra Krishna Valley Dev. Corp and Ors.,[11] it was held by the Supreme Court how an arbitration clause, since it is a collateral term "may" survive and not perish with coming to an end of the contract. In the case of Mulheim Pipe Coatings GmbH v Welspun Fintrade Ltd[12]., it was held by the Bombay High Court that a direct impeachment of the arbitration agreement, as opposed to a parasitical impeachment based on a challenge to the validity or enforceability of the main agreement, must be brought in order for the arbitration agreement to be declared null and void, inoperative, or incapable of performing its obligations.

UNSTAMPED ARBITRATION AGREEMENTS AND DOCTRINE OF SEPARABILITY

Under Article 35 of the Indian Stamps Act (1999), all instruments executed in a country that are not stamped or insufficiently stamped shall not be read as evidence "for any purpose," with the exception of criminal proceedings.[13] Now the question arises if the arbitration agreement contained in an unstamped document would be precluded from enforcement by applying the provision from the Indian Stamps Act.

In the case of M/S Sms Tea Estates pvt. Ltd. v M/S Chandmari Tea Co. Pvt Ltd.[14], the court was examining an application under section 11 of the Arbitration and Conciliation Act. The court held that examination of the contract on whether it has been duly stamped or not is necessary before

[9] Enercon India Ltd. vs. Enercon GmBH, A.I.R 2014 S.C 3152.,
[10] National Co-op Marketing Federation India Ltd v Gains Trading Ltd, (2007) 5 S.C.C 692
[11] P.Manohar Reddy & Bros. v Maharashtra Krishna Valley Dev. Corp and Ors. (2009) 2 S.C.C 494
[12] Mulheim Pipe Coatings GmbH v Welspun Fintrade Ltd (2014) 2 A.I.R Bom R 196
[13] Indian Stamp Act, 1899, sec.35, No.2, Acts of Parliament, 1899.
[14] M/S Sms Tea Estates pvt. Ltd. v M/S Chandmari Tea Co. Pvt Ltd. (2011) 14 S.C.C 66

admitting the same as evidence. If the contract is not duly stamped as per the procedure laid down under section 35 and 40 of the Indian Stamps Act, it cannot be admitted as evidence. Therefore, it was held that the arbitration clause also would not be acted upon since the whole document must be examined for the purpose of stamp duty.[15]

However, in 2015, the Arbitration and Conciliation Amendment Act came into force which inserted section 11 (6A) into the Act. As a result of the same, the powers of a court while hearing an application filed under section 11 were restrained and confined into the arbitration agreement. The same was confirmed in the case of M/S Duro Felguera v Gangavaram Port Ltd[16]. where the Supreme Court held that as a result of section 11(6A), the courts should look into just one aspect which is the "existence" of an arbitration agreement. However, later in the case of Garware Wall Ropes Ltd. v. Coastal Marine Constructions & Engineering Ltd[17] (The Garware Decision), the specific issue of the mandate of stamping for the enforcement of the arbitration clause was discussed. The court held that the existence of an arbitration agreement would depend on whether the contract "exists" which cannot be considered as existing unless it has been duly stamped. Hence it was concluded that it would not be possible to separate the arbitration clause from such a contract. The same was upheld in the case of Vidya Drolia &Ors. v Durga Trading Corporation [18]by the Supreme Court. It can be observed from the given decisions how the doctrine of separability was not recognized by the courts in deciding. The entire purpose of the doctrine is to make sure that the arbitration agreement be considered valid even when the entire contract is invalid or non-existent or unenforceable due to various reasons.

Finally, the Supreme Court in deciding the case of Mercantile Pvt. Ltd. v M/s. Indo Unique Flame Ltd. & Ors held how the court was wrong in deciding the Garware Decision and did not lay down the right position in law. In this case, the Apex Court was examining the question on whether the arbitration clause would become invalid or unenforceable due to the non-payment of stamp duty on the substantive commercial contract. The court recognized the doctrine of separability and said that "an arbitration agreement contained in a commercial contract is independent and separate from the underlying contract." The court also said that the arbitration agreement is an agreement which provides for the mode of dispute resolution which shall survive independent of the substantive contract. Therefore, on applying the doctrine, the arbitration agreement cannot be held invalid or

[15] i.b.i.d
[16] M/S Duro Felguera v Gangavaram Port Ltd (2017) 9 S.C.C 729
[17] Garware Wall Ropes Ltd. v. Coastal Marine Constructions & Engineering Ltd (*2019) S.C.C OnLine SC 515.*
[18] Vidya Drolia &Ors. v Durga Trading Corporation (2019) SCC OnLine S.C 358

unenforceable even if the substantive contract is inadmissible due to the non-payment of stamp duty. Since there is a difference in law that has been created, the issue has been referred to a 5-judge Constitution Bench to settle the issue once and for all.

In my opinion, there is no reason why this doctrine should not be extended to the cases related to unstamped contracts, especially when there is no loss in Revenue for the State as the parties are ordered to pay the stamp duty following the adjudication. However, the scope of the doctrine has been discussed in detail in the next section.

SCOPE OF THE DOCTRINE

Though the doctrine has been well defined, there is a conflict regarding the scope of this doctrine- whether the scope of this doctrine is broader than the main aim of the doctrine that it intends to achieve. One of the reasons why it has been given a broader scope is by arguing that the arbitration agreement and the main contract are governed by different laws generally because they are distinct from each other.[19] According to the definition of the doctrine, there are two agreements which are independent of each other- the main commercial contract and the arbitration agreement. They both are separate from each other and have to be interpreted separately which means that the contents of the main contract cannot have any effect on the arbitration clause.

However, it is important to note that the arbitration clause would not have any meaning without the main contract that lays down objects of the agreement. Furthermore, the doctrine is limited to the validity of the arbitration clause which arises only in case of invalidity of the main agreement. The main objective of the doctrine of separability is enforcing the agreement of the parties to arbitrate by safeguarding the jurisdiction of the arbitral tribunal and not to determine the governing law of the arbitration clause or treat the arbitration clause separate from the main agreement.

For better understanding, let us consider an example. In case of an invalidity of the main agreement, the parties would not argue that the both agreements are always separate and thus the arbitration clause would not become invalid just because the main agreement is invalid. Instead, the parties would defend the validity of the arbitration clause by arguing that the invalidity would be limited to the main

[19] Doctrine of Separability and determination of the proper law of an Arbitration agreement Bar and Bench - Indian Legal news, https://www.barandbench.com/columns/doctrine-of-separability-and-determination-of-the-proper-law-of-the-arbitration-agreement (last visited Jun 30, 2021)

contract because it is the common intention of parties to arbitrate and safeguard the jurisdiction of the arbitral tribunal.

According to Article 16 of the UNCITRAL Model Law which enshrines the doctrine of separability, it is provided that

"the arbitral tribunal may rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement. For that purpose, an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. A decision by the arbitral tribunal that the contract is null and void shall not entail ipso jure the invalidity of the arbitration clause."[20]

The words "for that purpose" clearly indicate the scope of the doctrine which is to safeguard the jurisdiction of the arbitral tribunal.

When the scope of the doctrine is made broad by the legal practitioners and apply the doctrine to separate the arbitration agreement from the main contract, it can be misused by habitual litigants to delay the resolution process. As a consequence, it leads to mounting of expenses to the parties and increasing frivolous cases in the court wasting time. It would all negate the purpose of arbitration which is to reduce costs and time.

ARGUMENTS AGAINST SEPARABILITY DOCTRINE

The foundation of arbitration is based on the aspect of autonomy of contracting parties. Essentially, the parties are given the right to formulate the contract on their own terms, and one of the indispensable parts of this contract is the dispute resolution clause. The main conflict, when it comes to the doctrine is whether the arbitration clause should stand while the contract has been proven to be illegal from its very inception. The autonomy of the contracting parties, in this case conflicts with the public policy requirements that all contracts are subject to. To combat this conflict, the Arbitration and Conciliation Act gives jurisdiction to the Arbitration tribunals to decide upon the validity of the arbitration clause and the nullity of a contract does not ipso jure make the arbitration clause invalid.

In the landmark judgement of M/s. Today Homes & Infrastructure Pvt. Ltd. v. Ludhiana Improvement Trust & Anr[21] (hereinafter 'the judgement') The Supreme Court clarified and held that

[20] UNICTRAL Model Law on International Commercial Arbitration, 1994, art. 16.
[21] M/s. Today Homes & Infrastructure Pvt. Ltd. v. Ludhiana Improvement Trust & Anr 2013 (5) TMI 381.

an arbitration agreement could stand independent of the main agreement and did not necessarily become otiose, even if the main agreement, of which it is a part, is declared void. However, this judgement has its own implications. *One of the main criticisms of such a principle is that it takes away from the parties right to approach the court in cases of grave illegality in the contract.* The right to litigate is hampered by this position given to the arbitration clause and in my opinion, a blanket principle such as this one should be modified and more discretion must be given to the party negatively affected to choose a preferred remedy.

In contrast to the practice of separating arbitration provisions from allegedly invalid contracts as a means of encouraging the parties' apparent purpose to arbitrate their disputes, separating arbitration provisions from purportedly non-existent contracts appears to defy the logic of the situation. Arbitration cannot be conducted where a contract does not exist since there is no consensus on which to base the decision. As a result, an allegation of nonexistence may be investigated by a national court of competent jurisdiction in the relevant country. It is possible to split contracts that are void ab initio into two categories: those whose formation was flawed and those that are void due to mistake. In the instance of the former, the parties reached a consensus but were unable to bring their agreement to a technically valid conclusion. It is a violation of the expansive wording of most arbitration agreements as well as the core objective of arbitration to refer issues involving void contract formation to national courts of competent jurisdiction. However, in the latter scenario, the parties were unable to achieve a resolution due to a shared misunderstanding of the issues. As a result, because a contract is non-existent and there is no basis for the arbitrator's jurisdiction to adjudicate on a dispute, any accusation of non-existence may be investigated by a national court of competent jurisdiction.

CONCLUSION

The Doctrine of Separability, in my opinion, is highly necessary for speedy resolution of commercial disputes. While taking a pro-arbitration stance, I do believe that the scope and application of the doctrine has not been clearly delineated in India which leads to confusing and unstable jurisdiction. The Indian courts have constantly provided differing views on the matter and the stance keeps shifting leading to serious implications. Unless and until the courts are not able to give clear and concise guidelines as to when the doctrine is applicable and when it is not, affected parties will keep approaching courts instead of tribunals to solve their disputes and litigate over whether the matter is arbitrable or not- leading to unnecessary and long pending litigation. Indian jurisprudence on the

matter is in need of a fresh start wherein they can provide clarity on the above-mentioned issues so that Arbitration in the country can be speedy and efficient. Furthermore, all these looming doubts must be cleared in the favour of arbitration and the scope of interpretation must be widened for the advancement of this modern dispute resolution system as opposed to lengthy litigation processes.