

ISSN: 2582-6433



# INTERNATIONAL JOURNAL FOR LEGAL RESEARCH AND ANALYSIS

Open Access, Refereed Journal Multi Disciplinary  
Peer Reviewed 6th Edition

VOLUME 2 ISSUE 7

[www.ijlra.com](http://www.ijlra.com)

## **DISCLAIMER**

No part of this publication may be reproduced or copied in any form by any means without prior written permission of Managing Editor of IJLRA. The views expressed in this publication are purely personal opinions of the authors and do not reflect the views of the Editorial Team of IJLRA.

Though every effort has been made to ensure that the information in Volume 2 Issue 7 is accurate and appropriately cited/referenced, neither the Editorial Board nor IJLRA shall be held liable or responsible in any manner whatsoever for any consequences for any action taken by anyone on the basis of information in the Journal.

Copyright © International Journal for Legal Research & Analysis



IJLRA

## EDITORIAL TEAM

### EDITORS

#### **Megha Middha**



*Megha Middha, Assistant Professor of Law in Mody University of Science and Technology, Lakshmangarh, Sikar*

*Megha Middha, is working as an Assistant Professor of Law in Mody University of Science and Technology, Lakshmangarh, Sikar (Rajasthan). She has an experience in the teaching of almost 3 years. She has completed her graduation in BBA LL.B (H) from Amity University, Rajasthan (Gold Medalist) and did her post-graduation (LL.M in Business Laws) from NLSIU, Bengaluru. Currently, she is enrolled in a Ph.D. course in the Department of Law at Mohanlal Sukhadia University, Udaipur (Rajasthan). She wishes to excel in academics and research and contribute as much as she can to society. Through her interactions with the students, she tries to inculcate a sense of deep thinking power in her students and enlighten and guide them to the fact how they can bring a change to the society*

#### **Dr. Samrat Datta**

*Dr. Samrat Datta Seedling School of Law and Governance, Jaipur National University, Jaipur. Dr. Samrat Datta is currently associated with Seedling School of Law and Governance, Jaipur National University, Jaipur. Dr. Datta has completed his graduation i.e., B.A.LL.B. from Law College Dehradun, Hemvati Nandan Bahuguna Garhwal University, Srinagar, Uttarakhand. He is an alumnus of KIIT University, Bhubaneswar where he pursued his post-graduation (LL.M.) in Criminal Law and subsequently completed his Ph.D. in Police Law and Information Technology from the Pacific Academy of Higher Education and Research University, Udaipur in 2020. His area of interest and research is Criminal and Police Law. Dr. Datta has a teaching experience of 7 years in various law schools across North India and has held administrative positions like Academic Coordinator, Centre Superintendent for Examinations, Deputy Controller of Examinations, Member of the Proctorial Board*



## Dr. Namita Jain



**Head & Associate Professor**

*School of Law, JECRC University, Jaipur Ph.D. (Commercial Law) LL.M., UGC - NET Post Graduation Diploma in Taxation law and Practice, Bachelor of Commerce.*

*Teaching Experience: 12 years, AWARDS AND RECOGNITION of Dr. Namita Jain are - ICF Global Excellence Award 2020 in the category of educationalist by I Can Foundation, India. India Women Empowerment Award in the category of "Emerging Excellence in Academics by Prime Time & Utkrisht Bharat Foundation, New Delhi.(2020). Conferred in FL Book of Top 21 Record Holders in the category of education by Fashion Lifestyle Magazine, New Delhi. (2020). Certificate of Appreciation for organizing and managing the Professional Development Training Program on IPR in Collaboration with Trade Innovations Services, Jaipur on March 14th, 2019*

## Mrs.S.Kalpana

**Assistant professor of Law**

*Mrs.S.Kalpana, presently Assistant professor of Law, VelTech Rangarajan Dr. Sagunthala R & D Institute of Science and Technology, Avadi. Formerly Assistant professor of Law, Vels University in the year 2019 to 2020, Worked as Guest Faculty, Chennai Dr. Ambedkar Law College, Pudupakkam. Published one book. Published 8 Articles in various reputed Law Journals. Conducted 1 Moot court competition and participated in nearly 80 National and International seminars and webinars conducted on various subjects of Law. Did ML in Criminal Law and Criminal Justice Administration. 10 paper presentations in various National and International seminars. Attended more than 10 FDP programs. Ph.D. in Law pursuing.*



## Avinash Kumar



*Avinash Kumar has completed his Ph.D. in International Investment Law from the Dept. of Law & Governance, Central University of South Bihar. His research work is on "International Investment Agreement and State's right to regulate Foreign Investment." He qualified UGC-NET and has been selected for the prestigious ICSSR Doctoral Fellowship. He is an alumnus of the Faculty of Law, University of Delhi. Formerly he has been elected as Students Union President of Law Centre-1, University of Delhi. Moreover, he completed his LL.M. from the University of Delhi (2014-16), dissertation on "Cross-border Merger & Acquisition"; LL.B. from the University of Delhi (2011-14), and B.A. (Hons.) from Maharaja Agrasen College, University of Delhi. He has also obtained P.G. Diploma in IPR from the Indian Society of International Law, New Delhi. He has qualified UGC - NET examination and has been awarded ICSSR - Doctoral Fellowship. He has published six-plus articles and presented 9 plus papers in national and international seminars/conferences. He participated in several workshops on research methodology and teaching and learning.*

## **ABOUT US**

INTERNATIONAL JOURNAL FOR LEGAL RESEARCH & ANALYSIS ISSN 2582-6433 is an Online Journal is Monthly, Peer Review, Academic Journal, Published online, that seeks to provide an interactive platform for the publication of Short Articles, Long Articles, Book Review, Case Comments, Research Papers, Essay in the field of Law & Multidisciplinary issue. Our aim is to upgrade the level of interaction and discourse about contemporary issues of law. We are eager to become a highly cited academic publication, through quality contributions from students, academics, professionals from the industry, the bar and the bench. INTERNATIONAL JOURNAL FOR LEGAL RESEARCH & ANALYSIS ISSN 2582-6433 welcomes contributions from all legal branches, as long as the work is original, unpublished and is in consonance with the submission guidelines.

IJLRA

**A CRITICAL STUDY ON ARBITRATION AS AN  
EFFECTIVE CONTRACTUAL DEBT RECOVERY  
MECHANISM AND A LOCAL REMEDY**

**Authored by-Shushaanth. S,  
LL.M (ADR) Student at O.P.Jindal Global University,  
Jindal Global Law School (2021-2022)**

**Abstract**

Seldom does a commercial dispute before a court of law gets to see its end in an expeditious manner. Traditional litigation is often plagued with straitjacket rules, procedures, exorbitant costs, inordinate delays and unwanted uncertainty. While an effective and efficient mechanism to settle commercial disputes is a desideratum, the financial institutions, Creditors (Financial & Operational) view arbitration and other alternative dispute resolution methods with great alacrity, and as an effective debt recovery mechanism. Financial institutions have adopted this method internationally and the same has been gaining swift momentum ever since the 2000's<sup>1</sup>. In light of the present trend, financial institutions and creditors increasingly show a predilection for arbitration for recovery of contractual debts and is often preferred as a local remedy before a dispute is referred to a Court or a Tribunal. Contracting parties explicitly mention in their contracts or agreements that in case of a dispute arising out of or in connection with the contract, the same would be referred to arbitration for amicable settlement. But the question to be qualified in this context is as to how far arbitration could facilitate the recovery of contractual debts and whether it can substitute the traditional procedures like filing of recovery suit, application under the CPC 1908, RDDBFI Act 1993, SARFAESI Act, 2002 and the IBC, 2016<sup>2</sup>. Thus, this article is an earnest endeavor to elucidate and determine if arbitration could be an effective mechanism to recover contractual debt arising out of commercial transactions.

**Keywords: - Arbitration, Debt Recovery, Contract, Commercial, Local Remedy**

---

<sup>1</sup> James Freeman & Louise Fisher, 'The rise and rise of Arbitration in Banking & Financial Disputes', ALLEN & OVERY, 9 February, 2018, <<https://www.allenoverly.com/en-gb/global/news-andinsights/publications/the-rise-and-rise-of-arbitration-in-banking-and-finance-disputes>>, Accessed on 5<sup>th</sup> June, 2022

<sup>2</sup>Nishta Arora & Sounak Chakraborty, SNG & Partners, 'Effectiveness of arbitration in financing document disputes June 20, 2019 <<https://law.asia/effectiveness-arbitration-financing-document-disputes/>> Accessed on 6th June, 2022

## Introduction

It is axiomatic to note that there are various ways in which contractual debts arising out of commercial transactions could be recovered with the aid of Courts and Tribunals. But, pursuing these conventional methods for the recovery of contractual debts often has a hidden cost in addition to the costs incurred during the tenure of the Case which is presented before a Court or a Tribunal for adjudication. The hidden costs are swathed in the form of litigation expenses, time, frustrated relationships and unwanted uncertainty. According to the National Judicial Data Grid (District & Taluka Courts of India)<sup>3</sup> approximately there are around 1,09,14,432 and approximately 43,05,556 (High Courts of India)<sup>4</sup> civil cases that are pending before the Courts in India as on July 2022. The stupendous case pendency is not only alarming but dismal and demands a serious alternative to reduce the burden of the Courts and Tribunals. The primary objective of this article is to analyze and evaluate the effectiveness of arbitration in recovering contractual debts and on how arbitration can be made as the mandatory local remedy in contractual disputes.

### I. Recovery of debts arising out of commercial transactions through arbitration:

=

Though the notion of referring cases relating to contractual debt recovery to arbitration as an alternative to traditional litigation may seem very promising, the question of process, enforcement, extent of judicial intervention, subject matter and arbitrability of the dispute has always remained a moot topic.

It is pertinent to note in this juncture that not all commercial disputes are arbitrable. A commercial dispute generally revolves around disputes relating to trade and commerce between merchants, bankers, financiers, traders, etc<sup>5</sup>. The Arbitration and Conciliation Act, 1996 (*hereinafter referred to as the “Arbitration Act”*) fails to define explicitly as to what all disputes are non-arbitrable. Hence, it is imperative to first discuss the question of arbitrability before discussing the possibility and efficacy of contractual debt recovery through arbitration.

---

<sup>3</sup> National Judicial Data Grid (District and Taluka Courts of India), <[https://njdg.ecourts.gov.in/njdgnew/?p=main/pend\\_dashboard](https://njdg.ecourts.gov.in/njdgnew/?p=main/pend_dashboard)>, Accessed on 2<sup>nd</sup> June 2022

<sup>4</sup> National Judicial Data Grid (High Courts of India), <[https://njdg.ecourts.gov.in/hcnjdgnew/?p=main/pend\\_dashboard](https://njdg.ecourts.gov.in/hcnjdgnew/?p=main/pend_dashboard)> Accessed on 2<sup>nd</sup> June 2022

<sup>5</sup> The Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts Ordinance, 2015, PRS Legislative Research, 23<sup>rd</sup> October, 2015, <<https://prsindia.org/billtrack/the-commercial-courts-commercial-division-and-commercial-appellate-division-of-high-courts-ordinance-2015>>, Accessed on 2<sup>nd</sup> June 2022.

## Arbitrability:

Section 2(3) of the Arbitration Act, expressly states that “Part 1 shall not affect any other law for the time being in force by virtue of which certain disputes may not be submitted to arbitration”. Further, Section 34(2)(b)(i) of the Arbitration Act provides that the arbitral award would be set aside if the Court finds that “the subject-matter of the dispute is not capable of settlement by arbitration under the law for the time being in force”<sup>6</sup>.

To understand more in detail, reliance has to be placed on the observations made by the Hon’ble Supreme Court in *Booz Allen & Hamilton Vs SBI Home Finance Ltd & Ors*<sup>7</sup>, wherein in paragraph No. 22 & 23 it was observed that “disputes arising out of rights *in personam* would be amenable to arbitration, whereas those relating to rights *in rem* would be adjudicated by courts and public tribunals”. In other words, if a public forum has been vested with the exclusive jurisdiction to adjudicate that dispute by virtue of a public policy, then the same could not be adjudicated through arbitration<sup>8</sup>.

Following the decision in *Booz Allen & Hamilton Inc*<sup>9</sup>, the Supreme Court in *Vidya Drolia & Ors Vs. Durga Trading Corporation*,<sup>10</sup> by overruling the judgment of the full bench decision of the Delhi High Court in *HDFC Bank Ltd Vs. Satpal Singh Bakshi*<sup>11</sup>, which had initially held that matters covered under the DRT Act (RDB Act, 1993) are arbitrable, observed that “if the claims of banks and financial institutions covered under the DRT Act were arbitrable, the same would deprive and deny those institutions of the specific rights including the modes of recovery specified in the DRT Act”. The Court, amongst other notable findings, also ruled that the claims covered by the DRT Act were not arbitrable. Further, the Hon’ble Court, also propounded a four-fold test to ascertain when a dispute would be non-arbitrable.

The quintessence of these rulings is that when the cause of action or the subject matter of the dispute is covered specifically by a special statute such as the RDB Act 1993, SARFAESI ACT 2002, IBC, 2016 etc., the same can only be adjudicated at those specific public forums and cannot be arbitrable as such claims fall under Right *in Rem*.

---

<sup>6</sup> Kingshuk Banerjee, ‘Non-arbitrable disputes - the law in India’, International Bar Association, 3<sup>rd</sup> June 2021 <[https://www.ibanet.org/nonarbdisputesindia#\\_edn3](https://www.ibanet.org/nonarbdisputesindia#_edn3)>, Accessed on 7<sup>th</sup> June 2022.

<sup>7</sup> (2011) 5 SCC 532.

<sup>8</sup> Ibid.

<sup>9</sup> See n.7.

<sup>10</sup> (2019) 20 SCC 406.

<sup>11</sup> (2012) SCC OnLine Del 4815.

In light of the four-fold test in *Vidya Drolia*<sup>12</sup> and the examples of non-arbitrable disputes as laid out in paragraph 36 of *Booz Allen & Hamilton*<sup>13</sup>, there is an implied understanding as to the non-arbitrable disputes.

Now, banks and financial institutions can be compelled to approach DRT's for the recovery of debts, when the default amount is over Rupees twenty lakhs<sup>14</sup>. However, the gateway to arbitration for debt recovery is opened when the debt falls below Rupees twenty lakhs, as the DRT's would lack the pecuniary jurisdiction to adjudicate that dispute and the same could be more effectively and efficiently recovered through arbitration.

## **Recovery & IBC**

Using of the terms "Financial Creditor" and "Operational Creditor" in the context of recovery of contractual debts may give rise to the notion of placing IBC proceedings and civil recovery proceedings on the same pedestal. However, it would not be right to do so as the Supreme Court and the NCLAT in a catena of judgments have categorically enunciated that "IBC is not intended to be a substitute for recovery forum".

In *Indus Biotech Private Limited vs. Kotak India Venture (Offshore) Fund*,<sup>15</sup> the Supreme Court observed that when an admission of a Section 7 petition under the IBC, 2016 was still pending and an application under Section 8 of the Arbitration Act has been filed, the adjudicating authority has to first decide on the Section 7 petition and has to ascertain whether there is a default for the consideration of the CIRP. Further, the Court noted that in the contrary situation, when the adjudicating authority is satisfied that there is no default, then the authority could allow the application under Section 8 of the Arbitration Act. The reasoning given by the Supreme Court is that an insolvency petition becomes Right *in Rem* only when the petition is admitted as it would concern the rights of third parties as well.

Moreover, the admission of Section 7 or Section 9 petition under the IBC, 2016 for the purpose of insolvency and liquidation can only be allowed when the default is Rs.1 crore and above<sup>16</sup>. When the default amount is less than Rs.1 crore, the creditors have to take recourse to the civil proceedings or arbitration for the recovery of the contractual debts.

---

<sup>12</sup> See n.10.

<sup>13</sup> See n.7.

<sup>14</sup> Government of India, Debts Recovery Tribunal, <<https://drt.gov.in/front/actrules.php>>, Accessed on 9<sup>th</sup> June 2022

<sup>15</sup> (2021) SC 187.

<sup>16</sup> Government of India, Ministry of Corporate Affairs, Notification No.2803 of 2020, (30<sup>th</sup> September, 2020), <[https://www.mca.gov.in/Ministry/pdf/Notification\\_28032020.pdf](https://www.mca.gov.in/Ministry/pdf/Notification_28032020.pdf)>, Accessed on 10<sup>th</sup> June 2022.

## **Analysis & Interpretation**

Not all processes for recovery of contractual debts arising out of commercial transactions have a special statute to govern them or demand the remedy provided under it to be exhausted first. Contractual debts that are in the nature of financial debt or an operational debt between parties that are not banks or financial institution can be arbitrated by following the due process of arbitration proceedings under the Arbitration Act.

Most common areas in which arbitration is extensively used are in ad hoc arbitrations. Wherein, the creditor or lender or a goods & service provider invokes the arbitration clause in order to recover the dues they are legally entitled to in an expeditious and efficacious manner<sup>17</sup>. Another notable area in which arbitration thrives as an effective debt recovery mechanism is in the area of vehicle loan financing where the financier on default of the borrower invokes the arbitration clause in the hire purchase agreement or the loan cum hypothecation agreement to recover the dues and in some cases take repossession of the vehicle. It is to be noted that the financier remains the owner of the vehicle until all installments are paid<sup>18</sup>.

## **Feasible Alternatives**

Traditional forms of recovery like filing money suit, summary suit under the CPC or filing a commercial suit under the Commercial Courts Act 2015, can switch to Arbitration for more effective and expeditious disposal of the dispute. In fact, Section 89 of the CPC, gives the Court, the power to refer a matter to arbitration or any other alternative dispute resolution methods when it is satisfied that there is an element of settlement which may be acceptable to the parties<sup>19</sup>. The CPC, being purely procedural in nature gives the autonomy to the parties to get their disputes settled by arbitration.

Therefore, it can be rightly pointed out that all civil or commercial disputes which can be decided by a court, is in principle arbitrable unless the jurisdiction of the arbitral tribunal is specifically ousted by a statute either expressly or by necessary implication<sup>20</sup>. Thus, when traditional methods of recovery under the CPC and other general statutes are compared to arbitration, it can be appropriately said that arbitration has all the necessary characteristics of a

---

<sup>17</sup> Prakhar Chandel, '*Arbitrability of Banking Disputes*', SSRN (August 14, 2020), <<http://dx.doi.org/10.2139/ssrn.3673769>>, Accessed on 15<sup>th</sup> June 2022.

<sup>18</sup> Magma Fincorp Ltd Vs. Rajesh Kumar Tiwari, CIVILAPPEAL NO. 5622 OF 2019,

<sup>19</sup> Civil Procedure Code, 1908, Section 89

<sup>20</sup> See n.7 at para 35

traditional recovery mechanism and can effectively recover contractual debts arising out of commercial transactions.

## II. Arbitration as a mandatory local remedy: -

Most business agreements have an arbitration clause clearly embedded in it as the primary local remedy in case of any dispute, that arises between the parties relating to the interpretation of the contract, or any breach thereof. On the existence of an arbitration agreement for dispute settlement, if one of the parties ignoring the presence of an arbitration agreement, refers the dispute to a civil court for adjudication, the other party may approach the court under Section 8 of the Arbitration Act by objecting and challenging the jurisdiction of that court in deciding that dispute. Due to the peremptory nature of Section 8 of the Arbitration Act, the Courts direct the parties to go for arbitration on the grounds of existence of an arbitration clause/agreement, provided the precondition mandated under sub clause 2 and 3 of Section 8 are fulfilled<sup>21</sup>.

In *SBP & Co. v. Patel Engineering Ltd. and Another*<sup>22</sup>, the Supreme Court observed in paragraph 16 that when one of the parties ignoring the existence of an arbitration agreement files an action before a judicial authority and the other party raises an objection, the judicial authority has to consider that objection if that objection is found to be sustainable to refer the parties for arbitration. The Constitutional bench also noted that the expression used in Section 8 was “shall” and by referring to its earlier decisions<sup>23</sup>, opined that the judicial authority is bound to refer the matter to arbitration once the existence of a valid arbitration clause was established.

The Supreme Court in *Consolidated Engineering Enterprises v Principal Secretary, Irrigation Department & others*<sup>24</sup> held that the Arbitration & Conciliation Act was a special law, consolidating and amending the law relating to arbitration and matters connected therewith or incidental thereto. Similarly in another notable decision,<sup>25</sup> the Supreme Court held that where an arbitration clause existed, the court has a mandatory duty to refer that dispute to the arbitrator.

---

<sup>21</sup> Singhanian & Partners LLP, India: ‘Section 8 Of The Arbitration And Conciliation Act, 1996: A Saving Beacon’, (Mondaq), <<https://www.mondaq.com/advicecentre/content/2786/Section-8-Of-The-Arbitration-And-Conciliation-Act-1996-A-Saving-Beacon#:~:text=A..parties%20to%20go%20for%20arbitration>>, Accessed on 15<sup>th</sup> June 2022.

<sup>22</sup> (2005) 8 SCC 618.

<sup>23</sup> (2000) 4 SCC 539, *see also* (2003) 6 SCC 503

<sup>24</sup> (2008) 7 SCC 169.

<sup>25</sup> (2003) 6 SCC 503.

Though the aforementioned cases and the application of Section 8 under the Arbitration Act may mandate the courts to refer a dispute for arbitration, there are some exceptions to this rule. Recently, in *Uttar Pradesh Power Transmission Corporation Ltd. Vs. CG Power And Industrial Solutions Limited*<sup>26</sup>, the Supreme Court observed that the existence of an arbitration clause in contractual matters would not debar the courts from entertaining a writ petition. The bench also noted that the availability of an alternative remedy would not disable the High Courts from entertaining a writ petition in an appropriate case. Hence, in these circumstances, a reference under Section 8 would be allowed only after due deliberations.

Hence, it can be said that on the existence of an arbitration clause in a commercial agreement, the parties to a dispute, normally cannot jettison arbitration for judicial proceedings when arbitration is the local remedy as per the agreement. It is to be noted that due to the mandatory overtones given to Section 8 of the Arbitration Act, the Courts in the absence of compelling reasons, have to refer the matter for arbitration. It is pertinent to note that there are divergent views on this position of law based on the different facts and circumstances of a case. However, it can be inferred that by virtue of Section 8 of the Arbitration Act, arbitration can be mandated as the mandatory local remedy by virtue of Section 8 of the Arbitration Act unless there is a prima facie reason not to.

### **Rationale Behind Mandatory Arbitration**

The use of arbitration as an effective contractual debt recovery mechanism should be adopted as a mandatory local remedy before an arbitrable dispute is referred to a judicial authority for adjudication. The judiciary, instead of restricting the scope of arbitration and limiting the arbitrability of a subject matter, must try to expand it so as to encompass other subject matters. Existing statutes must be amended in a way where arbitration is mandated as a mandatory local remedy. For example, Section 12A of the Commercial Courts Act, 2015 mandates the exhaustion of pre-institution mediation before initiation of a commercial suit. Another conspicuous example is the CIC Act, 2005, wherein section 18 expressly provides for arbitration and conciliation when there is no remedy provided under the Act for a dispute that arises relating to the business of credit information. Hence, arbitration could transform into a more effective alternative to adversarial methods if the statutes itself mandate the use of arbitration as the local remedy.

---

<sup>26</sup> (2021) 6 SCC 15.

## Conclusion

In an attempt to illuminate the significance of arbitration in the commercial sphere, it can be understood from the aforementioned discussions that arbitration and other alternative dispute resolution mechanisms are of paramount importance in today's legal sphere. The idea of Arbitration as an effective replacement for adversarial methods is still in an evolving pace and more reforms are needed.

It is pertinent to note that the main objectives of arbitration cannot be achieved if the root of the problem which is the scope of arbitration is not expanded. In light of the recent judicial observations, it is an undisputable fact that arbitration is barred from where it is needed the most which is in the area of recovery of debts by banks, financial institutions, NBFC's etc.

Due to the exclusive jurisdiction of the special forums in handling claims by banks, financial institutions, NBFC's etc., arbitration exist only as a Hobsons choice for debt recovery when the special public forums lack the pecuniary jurisdiction to adjudicate that dispute. Though commercial transactions relating to trade and commerce in India has witnessed and benefitted greatly from the use of arbitration, a pragmatic approach has to be adopted by the courts in order to extend the application of arbitration to all commercial disputes.

Hence it can be suggested that if arbitration is mandated as the mandatory local remedy in commercial disputes and if the scope of arbitration is expanded to cover other types of commercial disputes, the backlog of cases in the Indian Courts could be reduced to a significant extent.

IJLRA