

Dispute Resolution Hotline

November 10, 2023

TESTAMENTS ON ARBITRABILITY OF CONSUMER DISPUTES: PART I - INDIA

- In India, consumer disputes can only be subject to arbitration if the consumer opts for it after the dispute arises, notwithstanding any pre-existing arbitration agreements between them.
- Since consumer disputes are protected by a welfare legislation (i.e. the Consumer Protection Act, 2019), such disputes are non-arbitrable unless the consumer willingly opts for arbitration over the remedy before public fora.
- Under the Indian Arbitration Act, 1996, a court can refuse to appoint an arbitrator if the dispute in question is non-arbitrable.

SYNOPSIS

In *M Hemalatha Devi & Ors. v. B. Udayasri I* ("**Hemalatha**"),¹ the Indian Supreme Court held that consumer disputes can only be subject to arbitration if the consumer opts for it after the dispute arises, notwithstanding any pre-existing arbitration agreements between them. Accordingly, the court did not set aside the Telangana High Court's orders refusing to appoint an arbitrator for a dispute when the consumer sought redress before the district consumer forum instead.

This decision builds on the precedent set in *Emaar MGF Land Ltd. v. Aftab Singh* ("**Emaar**")² in the context of Section 11(6A) of the Indian Arbitration Act ("**Arbitration Act**") and the Consumer Protection Act, 2019 ("**Consumer Protection Act**"). *Emaar* had established that consumers may not be mandatorily referred to arbitration under Section 8(1) of Arbitration Act, if they opt to seek redress through consumer courts instead.

The criteria for arbitrating consumer disputes vary across legal jurisdictions. The position recently taken by the England and Wales High Court in *Payward, Inc., Payward Ventures, Inc., and Payward Limited v. Maxim Chechetkin* ("**Payward**")³ has been discussed in Part II to this hotline.

FACTUAL BACKGROUND

The dispute arose from an agreement for sale that included an arbitration clause ("**Construction Agreement**"). According to this agreement, the builder was obligated to complete the construction of a residential house or villa and transfer its possession to the consumer within a stipulated period of three years. Despite the consumer paying the requisite advance sum, the builder failed to hand over possession of the property after the three-year period had elapsed. Instead, the builder unilaterally terminated the Construction Agreement, claiming that the consumer's failure to sign the agreement was a ground for its termination.

Following the termination, the builder initiated proceedings by filing an application under Section 11 of the Arbitration Act before the Telangana High Court ("**High Court**"), seeking the appointment of an arbitrator ("**Section 11 Application**"). Concurrently, the consumer filed a complaint with the District Consumer Forum. The consumer contested the Section 11 Application by arguing that the builder has an option to approach the District Consumer Forum to seek a referral to arbitration. On 19 May 2022, the High Court denied the Section 11 Application and granted the builders the liberty to request a referral to arbitration from the District Consumer Forum under Section 8 of the Arbitration Act ("**First Order**"). However, the District Consumer Forum rejected the subsequent application filed by the builder under Section 8 of the Arbitration Act.

Upon the District Consumer Forum's rejection of its application, the builder petitioned the High Court again for a review of the First Order. However, the High Court dismissed this review application by an order dated 25 November 2022 ("**Second Order**"). The court reasoned that the builders had already acted in accordance with the First Order and were, therefore, estopped from seeking its review. The builders challenged the First and Second Orders before the Supreme Court, contending that the High Court had overstepped its bounds. Specifically, they argued that the High Court erroneously considered factors beyond the mere existence of an arbitration agreement while evaluating the Section 11 Application, thereby contravening Section 11(6A) of the Arbitration Act.⁴

JUDGMENT

The Supreme Court dismissed the challenge to both the orders. Relying on *Booz Allen and Hamilton Inc v. SBI Home Finance Limited*,⁵ the Supreme Court held that notwithstanding sub-section (1) of Section 8 of the Arbitration Act, a court must evaluate not only the presence of an arbitration agreement but also the arbitrability of the dispute in question. This question arose because Section 8(1) of the Arbitration Act states that a judicial authority "*shall*" refer parties to arbitration unless it *prima facie* finds that "*no valid arbitration agreement exists*".⁶

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The court ruled that since consumer disputes are protected by a welfare legislation (i.e. the Consumer Protection Act), such disputes are non-arbitrable unless the consumer willingly opts for arbitration over the remedy before public fora. The law gives the choice to the consumer to either avail a remedy under the Consumer Protection Act, or to go for arbitration. Consequently, an existing arbitration agreement does not deprive consumers of specialized remedies under the Consumer Protection Act if they choose to pursue them. Citing *Secretary, Thirumurugan Cooperative Agricultural Credit Society v. MLalitha*,⁷ the court explained that this is because the Consumer Protection Act provides for special remedies otherwise unavailable in arbitration. Further, consumer courts have a wider range of powers than an arbitral tribunal, including the power to impose penalties for non-compliance with their orders. The fact that the builder approached the High Court first would not oust the jurisdiction of the consumer courts.

Drawing upon *Emaar*, the Supreme Court held that its findings are unaffected by the insertion of sub-section 6A to Section 11 of the Arbitration Act, which aims to minimize judicial interference in arbitration. Like Section 8(1), Section 11(6A) provides that while appointing an arbitrator, a court should “*confine to the examination of the existence of an arbitration agreement*”. The court recognized that the 2019 amendments to the Arbitration Act have technically removed sub-section 6A to Section 11 of the Arbitration Act. However, it noted that this change has not yet been officially notified and remains unimplemented. Yet, it held that Section 11(6A) of the Arbitration Act cannot minimize judicial interference to the extent that non-arbitrable disputes are referred to arbitration.

The court reasoned this stance by pointing to Section 2(3) of the Arbitration Act, which states that Part I of the Arbitration Act does not override laws that categorize certain disputes as non-arbitrable.⁸ While the findings in *Emaar* were made in the context of Section 8(1) of the Arbitration Act and the Consumer Protection Act of 1986, the Supreme Court held *Emaar*'s reasoning equally applies to Section 11 of the Arbitration Act as well as the Consumer Protection Act of 2019.

OUR ANALYSIS

It is now a settled principle under Indian law that an arbitration agreement does not preclude the jurisdiction of consumer courts, if the consumer opts to seek redress through such consumer courts after the dispute arises.

In *Hemalatha*, the Supreme Court highlighted that the main reason behind granting such discretion to the consumers is that consumer courts have wider powers than arbitral tribunals to award certain specialized remedies and penalize non-compliance with their orders.

It may be argued that an arbitral tribunal has the power to grant many remedies that can be granted to a consumer under the Consumer Protection Act, including compensation, refunds or injunctions to cure deficiency in goods or services. Further, arbitrators as well as courts have powers to penalize and discourage non-compliance with arbitral awards. This includes the arbitrator's powers to impose costs (for interim awards) as well as the court's powers to initiate contempt proceedings once an award has been enforced as a decree of the court. Thus, in many cases, arbitration may offer the remedies sought for by a consumer.

However, there are multiple factors that could render arbitration unsuitable for resolving certain consumer disputes. For instance, cases involving the provision of potentially hazardous goods or services may carry implications for public welfare. In such scenarios, the inherently private nature of arbitration in India could prevent these matters from becoming public knowledge. Although arbitration proceedings are not automatically confidential, specific provisions, like Section 42A of the Arbitration Act⁹ and/or confidentiality provisions in rules of several arbitral institutions, protect confidentiality of arbitration proceedings and awards. The discretion granted to consumers, in *Emaar* or *Hemalatha*, to choose arbitration may not sufficiently safeguard the public's right to information about disputes that have broader societal ramifications.

Instead, the position taken in *Emaar* or *Hemalatha* primarily targets scenarios where consumers, often cornered by their lesser bargaining strength, consent to arbitration clauses. These contracts, typically standard-form contracts, compel consumers to agree to arbitration as a precondition for obtaining goods or services. By permitting consumers to approach consumer courts after a dispute has materialised, the courts aim to counterbalance the inherent inequities of such agreements. This seeks to ensure that consumers are not irrevocably bound by earlier agreements to arbitrate, which they may have entered into under duress or without the leverage to negotiate fairer terms.

The Indian position on arbitrability of consumer disputes resonates with that adopted by several jurisdictions. In some jurisdictions, courts find that pre-dispute arbitration agreements are binding upon consumers only such agreements are entered into independently, without conditioning the provision of goods or services on the consumer's consent to arbitrate. In Part II to this hotline, we examine the EWHC's *Payward* decision and compare international perspectives on the arbitrability of consumer disputes.

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You can direct your queries or comments to the authors.

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¹Civil Appeal Nos. 6500 □ 6501 of 2023.

²*Emaar MGF Land Ltd. v. Aftab Singh*, (2019) 12 SCC 751.

³[2023] EWHC 1780 (Comm).

⁴*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.”* Section 11(6A), Arbitration Act.

⁵(2011) 5 SCC 532.

⁶*A judicial authority, before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party to the arbitration agreement or any person claiming through or under him, so applies not later than the date of submitting his first statement on the substance of the dispute, then, notwithstanding any judgment, decree or order of the Supreme Court or any court, refer the parties to arbitration unless it finds that prima facie no valid arbitration agreement exists.”* Section 8, Arbitration Act.

⁷(2004) 1 SCC 305.

⁸*"This Part shall not affect any other law for the time being in force by virtue of which certain disputes may not be submitted to arbitration."* Section 2(3), Arbitration Act.

⁹*"Confidentiality of information — Notwithstanding anything contained in any other law for the time being in force, the arbitrator, the arbitral institution and the parties to the arbitration agreement shall maintain confidentiality of all arbitral proceedings except award where its disclosure is necessary for the purpose of implementation and enforcement of award."* Section 42A, Arbitration Act.

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