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NON-ARBITRABILITY OF DEBT RECOVERY MATTERS: ANALYSING THE EXCLUSIVE JURISDICTION UNDER DEBT RECOVERY LAWS

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INTRODUCTION

Arbitration in India has been consistently growing in different industries and enterprises as a result of the concerted efforts of individuals and the government to build a facilitative infrastructure and congenial environment for its development.¹ The judiciary has played an active role in highlighting the importance of alternative dispute resolutions such as arbitration to relieve the weight of case backlogs on the adjudicating authorities.² While arbitration is an essential mechanism of dispute settlement and its significance has been reiterated by judicial verdicts, it has taken a backseat when it comes to subject matters relating to debt recovery by banks and financial institutions. The Recovery of Debts and Bankruptcy Act 1993 (hereinafter referred as “**RDB Act**”) and Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002 (hereinafter referred as “**SARFAESI Act**”) are pivotal enactments which discuss the legal framework for the expeditious recovery of debts by banks and financial institutions to facilitate effective enforcement of secured and unsecured debt through creation of specialised forums such as Debt Recovery Tribunal (**DRT**) and Debt Recovery Appellate Tribunal (**DRAT**). Considering the special remedies and sole jurisdiction under these debt recovery laws this article attempts to critically examine the non-arbitrability of debt recovery issues and discusses as to how RDB Act and SARFAESI Act trump the general accesses to arbitration, thus establishing a separate statutory paradigm for financial creditors.

JUDICIAL TRENDS

The subject matter on which arbitration proceedings can be initiated has been a topic for discussion for a prolonged period of time as the Arbitration and Conciliation Act 1996 (hereinafter referred as “**A&C Act**”) remains silent on it. The judgement on the *Booz Allen case*³ delivered by the Supreme Court serves as a guiding precedent in determining which disputes can form the subject matter of arbitration stating that disputes arising out of rights in personam would be arbitrable in nature, whereas those relating to rights in rem would be adjudicated by courts and public tribunals. The exclusive jurisdiction to public forums in

¹ The New Delhi International Arbitration Centre Act 2019 (Act 17 of 2019)

² Salem Advocate Bar Assn. v. Union of India (2003) 1 SCC 49

³ Booz Allen & Hamilton Inc. v. SBI Home Finance Ltd. (2011) 5 SCC 532

matters concerning to rights in rem stemmed from the doctrine of public policy in order to maintain transparency and to safeguard the interests of the society at large.

In 2011, with reliance on the ruling laid down in the *Booz Allen case*, the Delhi High Court adjudicated on the issue “whether proceedings initiated under RDB Act can be arbitrable or not?” where the full bench of the Delhi High Court ruled in favour of arbitrability of debt recovery matters with the reasoning that issues relating to debt recovery are matters of "right in person am" and not "right in rem"⁴ and therefore, the claims under DRT Act are arbitrable. The High Court further upheld the freedom of the parties to choose a forum, and stated that by restricting the debt recovery matters to the DRT, that freedom would be lost.⁵

The Apex Court delivered a landmark judgement on the non-arbitrability of the subject matter relating to debt recovery⁶ and laid down a four-fold test to determine when a dispute shall not be arbitrable which includes – (i) when the dispute relates to actions in *rem*; (ii) the dispute affects third party rights; (iii) dispute relates to inalienable sovereign and public interest functions of the State; and (iv) subject-matter of the dispute is expressly or by necessary implication non-arbitrable as per mandatory statute. The *Vijay Drolia case* overruled the 2011 judgement delivered by the Delhi High Court and further clarified that if a special statute provides a prescribed mechanism for the resolution of disputes pertaining to a specific subject matter, parties would lose their ability to arbitrate disputes pertaining to such a subject matter. Therefore, the existence of RDB Act and SARFAESI which lays down a specific mechanism for debt recovery prohibits reference to arbitration.

A series of other judgments have similarly upheld the non-arbitrability on subject matter of debt recovery such as in the *Kohinoor Creations v. Syndicate Bank*⁷ the court affirmed the jurisdiction of DRT under RDB Act and stated even if an arbitration agreement exists under the A&C Act, the DRT will still have the jurisdiction to adjudicate upon the matter as specific statute, RDB Act will prevail over the general law, A&C Act. Further, the Bombay High Court upheld the jurisdiction of DRT making it mandatory for financial institutions to approach DRT for the adjudication and crystallisation of the debt recoverable from the borrower.⁸

HOW THE DEBT RECOVERY LAWS CREATE BAR TO ARBITRATION

The debt recovery legislations, the RDB Act and SARFAESI Act, were brought into force with the main aim of offering a specialized, time-bound framework for the recovery of debts by financial institutions and banks. A key characteristic of both the Acts is the overriding effect they confer over other legislations, including the A&C Act, as explicitly provided under Section 34 of the RDB Act and Section 35 of the SARFAESI Act. These overruling provisions of the said act excludes the jurisdiction of the arbitral tribunal in debt recovery cases. Further, even if the parties are said to be in an arbitration agreement out of their own will, such agreement cannot supersede the legislative intent of the RDB Act and SARFAESI Act as these statutes provide a comprehensive legal framework to settle the dispute between the defaulting borrowers and financial institutions.

⁴ HDFC Bank Ltd. v. Satpal Singh Bakshi 2012 SCC OnLine Del 4815.

⁵ HDFC Bank (n 13), 575 para 8.

⁶ Vidya Drolia v. Durga Trading Corpn., (2021) 2 SCC 1

⁷ Kohinoor Creations v. Syndicate Bank 2005 SCC OnLine Del 650

⁸ Tata Motors Finance Solutions Ltd. v. Naushad Khan 2023 SCC OnLine Bom 2716

The RDB Act establishes forums for debt recovery such as DRTs and DRATs with an exclusive jurisdiction to adjudicate upon debt recovery related issues. Section 17 of the SARFAESI Act affirms the jurisdiction of DRT as a grievance mechanism for a person aggrieved by the action of a secured creditor under the Act may move to the DRT as it has been declared as the which has sole forum to resolve such grievances. Similarly, the provisions under the RDB Act mandates that all recovery applications for debts of a certain amount to be filed only before the DRT and DRAT acts as an adjudicating authority to entertain appeals arising from DRT. Lastly, to secure an exclusive jurisdiction for DRT, the RDB Act imposes a bar on the jurisdiction of all courts and authorities through Section 18.

This uniform system not only provides efficiency and swiftness in the settlement of financial disputes but also serves the greater economic interest by providing banks and financial institutions with a time-bound forum. Allowing arbitration to run parallel or override such legislative forums would result in fragmentation of disputes, non-uniformity of results, and delays which will defeat the very purpose for which these specialised forums were established. Further, the conferral of exclusive jurisdiction on DRTs and DRATs ensures that adjudication is done by forums that have subject-matter competences in banking, finance, and debt enforcement matters.

CONCLUSION

The evolution of arbitration as an effective forum for the resolution of disputes in India has indeed come a long way in easing the burden of traditional courts and increasing party autonomy. But its sphere is not untrammelled, particularly where the legislature has painstakingly created exclusive, statutory forums with overriding jurisdiction like where recovery of debts by banks and financial institutions is concerned. Judicial precedents, especially the landmark judgments in *Vijay Drolia*, have laid down that legal stance under the law that debt recovery cases, according to special legislation like the RDB Act and SARFAESI Act, are of that kind of disputes which are non-arbitrable by necessary implication.

In the context of judicial doctrine and statutory law, it is clear that disputes relating to debt recovery are outside the purview of arbitration so as to ensure consistency of procedure, enforcement, and protection of the greater economic interest. Thus, the non-arbitrability of such disputes is not a procedural technicality but an intentional choice of the legislature, in favour of protecting public interest and financial stability over private contractual whim.