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CROSSROADS

**- INTERPLAY BETWEEN THE MSME ACT, 2006
AND THE ARBITRATION AND CONCILIATION
ACT, 1996**

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Introduction

In India, most arbitrations are governed by the Arbitration and Conciliation Act, 1996 (“**1996 Act**”). However, in certain cases, statutes provide for a statutory mechanism of arbitration where the Act may or may not apply¹. In the case of the Micro, Small, and Medium Enterprises Development Act, 2006 (“**MSME Act**”), the same provides for statutory arbitration governed by the MSME Act for resolution of disputes between the parties, with the provisions of the 1996 Act also being applicable to such arbitral process.

The MSME Act provides for specific provisions for quick redressal of disputes, under Section 17 and Section 18 of the said statute, in an effort to bring about a quick resolution to any default in payment, in the absence of which a micro, small or medium enterprise (“**MSME**”) may not sustain economically, considering the fact that even when India has been seeing significant growth in out of court resolutions, the same is still an expensive and time consuming process.

Under Section 18(2) of the MSME Act², there are provisions of conciliation under the MSME Act, and any party to a dispute may make a reference to the Micro and Small Enterprise Facilitation Council (“**Council**”) with respect to any amount due to it and thereafter, the Council *shall* either conduct conciliation itself or through any centre providing dispute resolution services. Further, Section 18(3) of the MSME Act provides that where such conciliation is not successful, the Council can take up the arbitration proceedings either through itself or by referring it to any centre or institution providing alternate dispute resolution services.

Be that as it may, it has been noticed that the statutory mechanism of arbitration as contained in the MSME Act, despite the applicability of the 1996 Act to the same, may often give birth to certain issues where the provisions of the MSME Act may come into conflict with those of the 1996 Act as far as the conciliation/ arbitration mechanism is concerned, due to the peculiarities of the MSME Act. The Supreme Court in the case of, *Gujarat State Civil Supplies Corporation Limited v. Mahakali Foods Private Limited*³ while deciding upon a batch of appeals relating to arbitration of MSMEs held that Chapter V (*Delayed Payments to Micro and Small Industries*) of the MSME Act would override the provisions of the 1996 Act. The Supreme Court further observed that ‘*generalia specialibus non derogant*’ i.e. general laws do not prevail over special laws and that whenever

¹ For example, see the arbitration mechanism for disputes related to ‘public works’ as contained in the Madhya Pradesh Madhyastham Adhikaran Adhiniyam, 1983.

² MICRO, SMALL AND MEDIUM ENTERPRISES DEVELOPMENT ACT, 2006 Section 18 - Reference to Micro and Small Enterprises Facilitation Council

“(1) Notwithstanding anything contained in any other law for the time being in force, any party to a dispute may, with regard to any amount due under section 17, make a reference to the Micro and Small Enterprises Facilitation Council.

(2) On receipt of a reference under sub-section (1), the Council shall either itself conduct conciliation in the matter or seek the assistance of any institution or center providing alternate dispute resolution services by making a reference to such an institution or center, for conducting conciliation and the provisions of sections 65 to 81 of the Arbitration and Conciliation Act, 1996 (26 of 1996) shall apply to such a dispute as if the conciliation was initiated under Part III of that Act.

(3) Where the conciliation initiated under sub-section (2) is not successful and stands terminated without any settlement between the parties, the Council shall either itself take up the dispute for arbitration or refer to it any institution or center providing alternate dispute resolution services for such arbitration and the provisions of the Arbitration and Conciliation Act, 1996 (26 of 1996) shall then apply to the dispute as if the arbitration was in pursuance of an arbitration agreement referred to in sub-section (1) of section 7 of that Act.

(4) Notwithstanding anything contained in any other law for the time being in force, the Micro and Small Enterprises Facilitation Council or the center providing alternate dispute resolution services shall have jurisdiction to act as an Arbitrator or Conciliator under this section in a dispute between the supplier located within its jurisdiction and a buyer located anywhere in India.

(5) Every reference made under this section shall be decided within a period of ninety days from the date of making such a reference.”

³ *Gujarat State Civil Supplies Corporation Limited v. Mahakali Foods Private Limited*, [SLP (C) No. 12884/2020, judgment dated October 31, 2022] (Supreme Court).

there is an **apparent conflict** between two statutes, the provision of a general statute must yield to that of a special statute.

There may be certain other issues, where the two statutes may not be in apparent conflict with each other, but which piques legal curiosity as such issues would not be encountered in regular arbitration proceedings under the 1996 Act. This thought paper is aimed at discussing and analysing such issues, i.e., we aim to understand why such issues may arise despite the 1996 Act and the MSME Act being intended to function in apparent harmony with each other, the judicial precedents on the same as well as our thoughts on how such issues may be resolved.

Whether MSME Council can act as Conciliator if a valid arbitration agreement exists? Whether the MSME Council can act as Conciliator as well as Arbitrator?

In the recent judgment of, Gujarat State Civil Supplies Corporation Limited (*supra*), the Supreme Court had held that the presence of an arbitration clause between two parties would not preclude any party to make a reference to conciliation under MSME Act. Therefore, any party to a dispute (where at least one party is a registered MSME) can refer a dispute to the Council, even if a valid arbitration clause exists and provisions of the MSME Act would override the 1996 Act.

Further, it is pertinent to note that, Section 80 of the 1996 Act⁴ provides a bar on the *conciliator* to act in arbitration proceedings or other judicial proceedings between the parties involved, other than such conciliation.

However, from a reading of Section 18 of the MSME Act, we note that the Council can act as arbitrator as well as conciliator under the MSME Act. This seems to be in apparent contradiction with Section 80 of the 1996 Act, as stated hereinabove. This issue fell for consideration of the Chattisgarh High Court in the case of, *Messrs SEW Infrastructure Limited v. Micro & Small Enterprises Facilitation Council*⁵. The Petitioner therein had challenged the appointment of the Council as arbitrator, on the grounds that Section 80 of the 1996 Act creates a bar on the Council acting both as arbitrator and conciliator.

The Court further observed that, Section 24 of the MSME Act has an overriding effect on any other Act and held that, **Section 80 of the 1996 Act will not be create any bar for the Council to act as arbitrator under the MSME Act.** The view was also reaffirmed by the Supreme Court in the case of, Gujarat State Civil Supplies Corporation Limited (*supra*).

We are of the view that, while the parties have the autonomy to **agree** that the conciliator shall appear as arbitrator as per Section 80 of the 1996 Act, Section 18(3) of the MSME Act, read with Section 24 of the MSME Act being special provisions, would automatically override Section 80 of the 1996 Act and become applicable and the mutual agreement of parties as under Section 80 of the 1996 Act would not be required *specifically* for the Council to act as both the conciliator and the arbitrator, as per Section 18 of the MSME Act.

⁴ ARBITRATION AND CONCILIATION ACT, 1996, Section 80 - Role of conciliator in other proceedings:

“Unless otherwise agreed by the parties: –

(a) the conciliator shall not act as an arbitrator or as a representative or counsel of a party in any arbitral or judicial proceeding in respect of a dispute that is the subject of the conciliation proceedings;

(b) the conciliator shall not be presented by the parties as a witness in any arbitral or judicial proceedings.”

⁵ *Messrs. SEW Infrastructure Limited v. Micro & Small Enterprises Facilitation Council*, [W.P.C. no. 4235 of 2021, January 14, 2022] (Chattisgarh High Court).

Since the Council can act as both conciliator and arbitrator can the two processes be clubbed? Is arbitration to be mandatorily referred to by the Council if the conciliation proceedings fail?

Whilst the position that the Council may act as both the conciliator and the arbitrator seems to now have been settled by the Supreme Court in the case of, Gujarat State Civil Supplies Corporation Limited (*supra*), the question also arises that whether arbitration must mandatorily be commenced when the conciliation proceedings fail, since there is no such compulsion provided for in the 1996 Act. In *Jharkhand Urja Vikas Nigam Limited v. the State of Rajasthan*⁶, the Supreme Court dismissed an order arising out of a conciliation proceeding held by Rajasthan Micro & Small Industries Facilitation Council, Jaipur and noted that the Council had failed to initiate arbitration, and the Council did not have any authority to club the proceeding of arbitration and conciliation. The two processes are distinct and arbitration must be mandatorily referred to in case the conciliation proceedings fail.

Whether the Limitation Act is applicable and is counterclaim maintainable in arbitration proceedings under the MSME Act? Whether retrospective benefit of MSME Act can be taken?

Section 23(2A) of the 1996 Act expressly provides for filing of counter-claim and set off in arbitration proceedings under the 1996 Act. Similarly, Section 43 of the 1996 Act states that the Limitation Act, 1963 shall be applicable to arbitrations under the 1996 Act as it applies to judicial proceedings.

The Orissa High Court in the case of, *Shri Mahavir Ferro Alloys Private Limited v. Passary Minerals Limited*⁷, while deciding on the issue of maintainability of counter-claims in MSME proceedings, noted that, the counter-claims by the counter-party could not be adjudicated by the Council under the MSME Act since the Act was only applicable to MSME entities and unless the counter-party was also a registered MSME entity, the Council would lack jurisdiction in this regard.

However, the issue seems to have been settled by the Supreme Court in the case of, *Silpi Industries v. Kerala State Transport Corporation*⁸. In the facts of this case, the Kerala State Transport Corporation (KSRTC) had invited tenders for supply of thread rubber for tyre building and part payment to the appellants therein was subject to the performance of the tyres. Under the arbitration proceedings, the claims of the therein appellants succeeded and the respondent filed an application for setting aside the award. The other issue in question in this matter was whether the provisions of the Limitation Act, 1963 will also be applicable to arbitration proceedings under the MSME Act.

The Supreme Court, while considering whether Limitation Act, 1963 would apply to arbitrations under the MSME Act, relied upon *Andhra Pradesh Power Coordination Committee v. Lanco Kondapalli Power Limited*⁹ and held that, arbitrations pursuant to Section 18(3) of the MSME Act would be governed by the Limitation Act, 1963, in line with arbitrations under the 1996 Act.

With the issue of counterclaim in question, the Bench noted that a provision of counterclaim is expressly available under Section 23(2A) of the 1996 Act. Section 18(3) of the MSME Act specifically provides that the provisions of the 1996 Act would be applicable to the MSME Act as

⁶ *Jharkhand Urja Vikas Nigam Limited v. the State of Rajasthan*, [Civil Appeal no. 2899 of 2021, judgment dated December 15, 2021] (Supreme Court).

⁷ *Shri Mahavir Ferro Alloys Private Limited v. Passary Minerals Limited*, [2018 SCC OnLine Ori 175].

⁸ *Silpi Industries v. Kerala State Transport Corporation with Khyati Engineering v. Prodigy Hydro Power Private Limited*, [AIR 2021 SC 5487].

⁹ *Andhra Pradesh Power Coordination Committee v. Lanco Kondapalli Power Limited*, [(2016) 3 SCC 468].

if the arbitration was pursuant to an arbitration agreement as defined in Section 7(1) of the 1996 Act. Therefore, the Supreme Court held that counterclaims, as applicable as under the 1996 Act, would apply to any arbitrations under the MSME Act as well.

Further, while discussing the retrospective applicability of the MSME Act in this judgment, the Supreme Court held that to enjoy the benefits of the provisions of the MSME Act, the seller would have to be registered as under the MSME Act as on the date of entering the contract. Therefore, clearly, the registration status of the MSME could not impact any contract retrospectively.

This view was also taken by the Supreme Court in the case of, *Messrs Vaishno Enterprises v. Hamilton Medical AG*¹⁰, where the date of registration as MSME was after the date of execution of the agreement. Such view has been reaffirmed by the Hon'ble Supreme Court in *Gujarat State Civil Supplies Corporation Limited (supra)*.

We are of the opinion that the decision of the Supreme Court in *Silpi Industries (supra)* regarding maintainability of counterclaims is the approach that ought to be followed, because any other approach would result in unnecessary multiplicity of proceedings before various *fora* regarding the same dispute (and appurtenant time as well as expenses consumed in such processes).

What is the remedy available to a party for the Council's failure to conduct hearing on the issue of Limitation *vis-à-vis* the proceedings under the 1996 Act and the MSME Act?

Under the 1996 Act, upon the dismissal of an application under Section 16 of the 1996 Act *vide* which a party may challenge the arbitration process on the ground of the claimant's claims being barred by the laws of limitation, the sole relief available to such party is limited to filing of a Section 34 application under the 1996 Act for setting aside of the arbitral award only after such award has been passed¹¹.

This brings us to the question, what remedy would be available for a similar situation, i.e., non-consideration of the issue of limitation by the Council in MSME proceedings. In *Bajaj Electricals Limited v. Micro Small and Enterprises Facilitation*¹², the Orissa High Court took into consideration the judgment of, *Silpi Industries (supra)* and further noted that, the issue of limitation had not been adjudicated (in the facts of the matter before the court) and therefore, held that, the petitioner could not be compelled to seek setting aside of the award in the instant matter. Any alternative remedy under Section 34 of the 1996 Act could not restrict the petitioner from invoking the writ jurisdiction of the Orissa High Court since the petitioner was not heard at all with respect to the point of limitation. The Orissa High Court therefore allowed the writ petition in such case and directed the same be heard by the Council in accordance with the extant law.

Therefore, whilst writ petitions ordinarily would not lie against arbitrations under the 1996 Act¹³, this is one instance where the Court had allowed the invocation of its writ jurisdiction, for non-consideration of the essential issue of limitation by the Council.

¹⁰ *Messrs. Vaishno Enterprises v. Hamilton Medical AG*, [2022 SCC OnLine SC 355].

¹¹ *Deep Industries Limited v. Oil and Natural Gas Corporation Limited*, [2019 SCC Online SC 1602].

¹² *Bajaj Electricals Limited v. Micro Small and Enterprises Facilitation*, [2022(I)ILR-CUT363].

¹³ *Zonal Manager, Central Bank of India v. Devi Ispat Limited*, [(2010) 11 SCC 186].

Section 19 of the MSME Act-Mandatory or not?

Section 19 of the MSME Act¹⁴ provides that for any application for setting aside a decree, award or order, made by the Council or any institution to which the disputes have been referred, to be maintainable, a pre-deposit of 75% of such decretal sum or award amount has to be made by the challenging party.

As opposed to the above, the *proviso* to Section 36(3) of the 1996 Act, states that while considering an application for stay of award of arbitration, the court should have due regard to the provisions for grant of stay of a *money decree* under the provisions of the Code of Civil Procedure, 1908. Essentially, it appears that while considering an application under Section 36(3) of the 1996 Act, the Court could direct deposit of award money, as per its discretion as in the case of a money suit.

The Bombay High Court, in *Ecopack India Paper Cup Private Limited v. Sphere International*¹⁵, noted that Section 36(3) of the 1996 Act is discretionary as is apparent from the bare provision. While there were other courts who had taken divergent views, holding Section 36(3) of the 1996 Act was mandatory in nature, the view of the Supreme Court's decision in *Pam Developments Private Limited v. State of West Bengal*¹⁶, has clarified the position that Section 36(3) of the 1996 Act is discretionary. In view of the same, let us see whether such discretion is available under Section 19 of the MSME Act as well, despite its express mandate.

The Punjab and Haryana High Court at Chandigarh in *Messrs Mahesh Kumar Singla v. Union of India*¹⁷, held that Section 19 of the MSME Act is discretionary and while exercising such discretion the Court should keep in mind the timely need to ensure credit to small and medium enterprise to minimize the incidence of sickness.

The Hon'ble Allahabad High Court however differed in *Messrs Tirupati Stationary Private Limited v. State of U.P.*¹⁸, where the Court held that Section 19 of the MSME Act is *mandatory* and prevails over the provisions of Order XXVII Rule 8 of the Code of Civil Procedure, 1908 and any other law that may allow the courts' discretions while dealing with the requirement to pre-deposit the disputed amount of award in an application filed under Section 34 of the 1996 Act.

A similar view was taken by the Supreme Court in *Messrs Tirupati Steels v. Messrs Shubh Industrial Component*¹⁹, where the Court allowed the appeal and held that Mahesh Kumar Singla (*supra*) can no longer be considered good law, and that Section 19 of the MSME Act is **mandatory and not discretionary**.

¹⁴ Micro, Small and Medium Enterprises Development Act, 2006.

"Section 19 - Application for setting aside decree, award or order

No application for setting aside any decree, award or other order made either by the Council itself or by any institution or center providing alternate dispute resolution services to which a reference is made by the Council, shall be entertained by any court unless the appellant (not being a supplier) has deposited with it seventy-five per cent of the amount in terms of the decree, award or, as the case may be, the other order in the manner directed by such court:

Provided that pending disposal of the application to set aside the decree, award or order, the court shall order that such percentage of the amount deposited shall be paid to the supplier, as it considers reasonable under the circumstances of the case subject to such conditions as it deems necessary to impose."

¹⁵ *Ecopack India Paper Cup Private Limited v. Sphere International*, [Appeal no. 101 of 2018, judgment dated March 14, 2018] (Bombay High Court).

¹⁶ *Pam Developments Private Limited v. State of West Bengal*, [AIR 2019 SC 3937].

¹⁷ *Messrs Mahesh Kumar Singla v. Union of India*, [W.P.C. 23668 of 2015, judgment dated March 27, 2017], (Punjab and Haryana High Court).

¹⁸ *Messrs Tirupati Stationary Private Limited v. State of U.P.*, [Writ-C no. 46388 of 2013, judgment dated March 3, 2022] (Allahabad High Court).

¹⁹ *Messrs Tirupati Steels v. Messrs Shubh Industrial Component*, [AIR 2022 SC 1939].

In a judgment of the Calcutta High Court in *Optimal Power Synergy India Private Limited v. Bharat Heavy Electricals Limited*,²⁰ the Hon'ble Court observed that the scope of discretion on imposing conditions for stay of award or order under Section 19 of the MSME Act, is wider than Section 36 of the 1996 Act. The Court observed that Section 19 of the MSME Act allows the Court to decide and impose terms of withdrawal of a part of the deposit money for the MSME entity to sustain itself and survive, and the MSME was allowed to withdraw the deposit, without furnishing **any corresponding security considering that the MSME was struggling to keep itself afloat**. In *Goodyear India Limited v. Norton Intech Rubbers (P) Limited*²¹, the Supreme Court expanded the scope of discretion and interpreted the words “as it deems necessary to impose”, as appears in the *proviso* to Section 19 of the MSME Act and allowed the payment of pre-deposit to be done in *instalments*.

We note that the law is now settled that Section 19 of the MSME Act is mandatory and a buyer within the definition of the MSME Act, if it wishes to challenge any order or award under Section 19 of the MSME Act, must mandatorily make deposit of 75% of the award sum. Further, the court has significant discretionary powers under Section 19 of the MSME Act, as compared to the provisions of the 1996 Act, to decide how and on what terms such pre-deposit is to be made by the judgment-debtor and/ or withdrawn/ utilized by the judgment-creditor.

Whether Section 29A of the Act is applicable to arbitrations under the MSME Act?

Section 29A of the 1996 Act provides the time limit for delivery of arbitral award by the arbitral tribunal and the extension that may be granted by the court for extension of such time limit. Naturally, the question would arise as to whether the advantage of Section 29A of the 1996 Act can be taken by parties in case of arbitrations under the MSME Act.

Reference is made in this regard to the decision in *Lots Shipping Company Limited v. Cochin Port Trust*²², where the Kerala High Court interpreted the word “court” contained under sub-section (4) of Section 29A of the 1996 Act to hold that the term “court” contained in Section 29(4) has to be interpreted as the ‘Supreme Court’ in the case of international commercial arbitrations and as the ‘High Court’ in the case of domestic arbitrations, since under Section 29A of the 1996 Act the power of the Court is akin to the power of appointment of arbitral tribunal under Section 11 of the 1996 Act. The Court held that, Section 29(4) of the 1996 Act requires purposive interpretation and literal interpretation of ‘Court’ as specified in Section 2(1)(e)(1) of the 1996 Act, should not be applied in such case. In other words, in the case of an international arbitration only the Supreme Court has the power to extend the time limit of arbitration as specified under Section 29A and only the High Court has the power to extend the time limit of domestic arbitration. Now the issue may arise, whether such interpretation may extend to arbitrations under the MSME Act as well.

We now refer to the decision in *Messrs Magirsha Industries v. Messrs Gujarat State Fertilizer and Chemicals Limited*²³, where the Ahmedabad High Court after considering Section 18(3) of the MSME Act, has held that, “*in respect of the references made by MSME, the provisions of Arbitration and Conciliation Act, 1996 would be applicable and thereby this Court is empowered under Section 29A to extend the mandate where the period prescribed under the Act for concluding the arbitration proceedings has expired.*”

²⁰ *Optimal Power Synergy India Private Limited v. Bharat Heavy Electricals Limited*, [RVWO/15/2021, judgment dated February 21, 2022], (Calcutta High Court).

²¹ *Goodyear India Limited v. Norton Intech Rubbers (P) Limited*, [2012 (2) CTC 829].

²² *Lots Shipping Company Limited v. Cochin Port Trust*, [AIR 2020 Ker 169].

²³ *Magirsha Industries v. Messrs. Gujarat State Fertilizer and Chemicals Limited*, [R.Petn under the Arbn. Act no. 68 of 2020, judgment dated March 4, 2022] (Ahmedabad High Court).

Therefore, only a High Court can extend the mandate of an arbitrator where a reference has been made under the provisions of the MSME Act.

Conclusion

The Micro, Small, and Medium Enterprises Development Act, 2006 is a fairly new statute and is therefore not yet backed by a plethora of judicial precedents. As we have seen from the issues we have discussed hereinabove, while the 1996 Act is made applicable to arbitrations under the MSME Act, the interplay of the two statutes may not always be seamless and could lead to divergent views, which raises doubts as to which of the two would take precedence. However, with significant jurisprudence now developing on these issues, we can expect the same to be gradually and conclusively settled by the judiciary.

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