

# COMPARING STATUTORY ARBITRATION IN INDIA- ANALYSIS IN THE LIGHT OF SILPI INDUSTRIES CASE

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## Introduction

Arbitration is one of the most popular methods of dispute resolution. Parties prefer arbitration over court litigation because of the benefits it provides. Using an arbitration agreement, one can choose the arbitrator, the procedure, the applicable law, and the seat of the arbitration. Around 24 of the Central Acts provide for statutory arbitrations. Statutory arbitration requires that if a dispute arises out of the provision of the statute, it goes for arbitration under that respective Act rather than under Arbitration and Conciliation Act, 1996 [**“Arbitration Act”**]. Section 46 of the Arbitration Act of 1940<sup>1</sup> introduced statutory arbitrations, which are now recognised under Section 2(4) of the Arbitration Act.<sup>2</sup> Even then, there is conflict as to whether the case will go for statutory arbitration or arbitration under the Arbitration Act.

Such a conflict exists between the Arbitration Act and the Micro, Small and Medium Enterprises Development Act, 2006 [**“MSMED Act”**]. The Hon’ble Supreme Court recently cleared the position regarding this conflict in the case of *M/S Silpi Industries v. Kerala State Road Transport Corporation*<sup>3</sup> [**“Silpi Industries”**]. However, the Supreme Court failed to clarify what will happen if the buyer wants to invoke the arbitration under an arbitration agreement signed between the parties.

This article examines conflicting judgements regarding this issue and how the Silpi Industries judgement finally clarifies the position regarding the same. This article, further, draws a parallel between Electricity Act, 2003 [**“Electricity Act”**], the National Highways Authority Act, 1956 [**“NH Act”**] and the Indian Telegraph Act, 1885 [**“Telegraph Act”**] and MSMED Act to show that just like how statutory arbitrations are mandatory under Electricity Act, they have been made mandatory under MSMED Act too. It concludes by observing that in the Silpi Industries judgment, the Supreme Court has taken a strong stance regarding mandatory arbitrations under the MSMED Act, which aligns with other statutes having similar provisions.

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<sup>1</sup> The Arbitration Act 1940, s 46.

<sup>2</sup> The Arbitration and Conciliation Act 1996, s 2(4).

<sup>3</sup> *M/S Silpi Industries v. Kerala State Road Transport Corporation* AIR 2021 SC 5487.

## The conundrum of statutory arbitration under the MSMED Act

The MSMED Act aims to boost the growth of micro, small and medium enterprises [“**MSMEs**”] in India by ensuring that defaulting buyers do not burden these enterprises. It provides a tier-wise statutory dispute resolution mechanism to resolve defaults in payment by buyers. Parties in a dispute regarding payments under Section 17 of the MSMED Act<sup>4</sup> can refer to the Micro and Small Enterprises Facilitation Council [“**Council**”] under Section 18.<sup>5</sup> When such conciliation is unsuccessful and terminated, the Council can take it up for arbitration (or refer it to an institution providing ADR services). Here, the provisions of the arbitration act will apply to the dispute as if it was in pursuance of an arbitration agreement under Section 7(1) of the Arbitration Act.<sup>6</sup> This creates an overlap between the provisions of the MSMED Act and the Arbitration Act.

There has been a constant debate and conflicting High Court decisions over the overlap of the MSMED Act and the Arbitration Act regarding whether Section 18 has an overriding effect over independent arbitration mechanisms agreed between parties. The specific question here is whether the specific provisions of the MSMED Act will override the general ones in that of the Arbitration Act. In this context, it is also important to note that Section 24 of the MSMED Act<sup>7</sup> categorically states that the provisions of Sections 15 to 23 will override the effects of any other law.

This facet was initially considered in detail by the High Court of Bombay in the case of *Steel Authority of India Limited v. Micro, Small Enterprise Facilitation Council*<sup>8</sup> [“**Steel Authority**”]. Concerning Section 24, the Court stated that it would not have the effect of negating an arbitration agreement because it only overrides whatever is inconsistent with Sections 15-23. The Court noted that there is no inconsistency between arbitrations conducted under Section 18 and an arbitration clause since both are governed by the Arbitration Act. Similarly, in *Porwal Sales v. Flame Control Industries*<sup>9</sup> [“**Porwal Sales**”], the Bombay High Court noted that if the legislature intended to bar arbitration agreements between parties, it would have expressly provided the same. “*In case one such party falls under the present Act, the arbitration agreement, as entered between the parties would not be of any effect, and the parties would be deemed to be governed under the MSMED Act in that regard.*”

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<sup>4</sup> The Micro, Small and Medium Enterprises Development Act 2006, s 17.

<sup>5</sup> The Micro, Small and Medium Enterprises Development Act 2006, s 18.

<sup>6</sup> The Arbitration and Conciliation Act 1996, s 7 (1).

<sup>7</sup> The Micro, Small and Medium Enterprises Development Act 2006, s 24.

<sup>8</sup> *Steel Authority of India Limited v. Micro, Small Enterprise Facilitation Council* AIR 2012 Bom 178.

<sup>9</sup> *Porwal Sales v. Flame Control Industries* 2019 SCC OnLine Bom 1628.

The view expressed in *Steel Authority* was categorically rejected by the Gujarat High Court in the case of *Principal Chief Engineer v. M/s Manibhai and Brothers (Sleepers)*.<sup>10</sup> Placing reliance on the overriding nature of Section 18, the Court gave primacy to the arbitration that was being conducted by the Council over that of independent arbitration proceedings. This decision was upheld by the Supreme Court on appeal.<sup>11</sup> The Delhi High Court also rejected the *Steel Authority* decision in *Bharat Heavy Electricals Ltd. v. The Micro and Small Enterprises Facilitations Centre*.<sup>12</sup> It stated that the non-obstante clause in Section 24 providing for the overriding effect of Sections 15-23 implies that Section 18(3)<sup>13</sup> cannot be diluted and “*must be given effect to notwithstanding anything inconsistent, including the arbitration agreement in terms of section 7 of the Arbitration Act*”. The Supreme Court clarified the constant confusion on whether the provisions of the MSMED Act or the Arbitration Act would prevail recently in the case of *Silpi industries*.

### **Analysis of Silpi Industries case**

The Kerala State Road Transport Corporation [“**KSRTC**”] (Buyer) invited tenders for the supply of thread rubber. Silpi Industries (Seller) was awarded the contract that required them to pay 90 per cent of the total purchase price upon delivery of the material. The remaining 10 per cent was to be paid upon the final performance report of the material delivered. Silpi Industries approached the Council under Section 18, MSMED Act, 2006 (erstwhile Interest on Delayed Payments to Small Scale and Ancillary Industrial Undertakings Act, 1993 [“**IDPASC Act**”]), after the remainder of 10 per cent was not paid. The conciliation proceedings, however, were unsuccessful, and the case was transferred to arbitration under the Arbitration Act.

The award favoured Silpi Industries, prompting KSRTC to file an appeal with the Kerala High Court under Section 37, Arbitration Act.<sup>14</sup> While setting aside the arbitral award, the High Court found that the Limitation Act applies to procedures brought under the Arbitration Act arising from the MSMED Act and that the counter-claim is admissible in such proceedings. Furthermore, since the parties already had an agreement to arbitrate, KSRTC’s application filed under Section

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<sup>10</sup> *Principal Chief Engineer v. M/s Manibhai and Brothers (Sleepers)* AIR 2016 Guj 151.

<sup>11</sup> *Principal Chief Engineer v. M/S Manibhai And Bros (Sleepers)* AIR 2016 Guj 151.

<sup>12</sup> *Bharat Heavy Electricals Ltd. v. The Micro and Small Enterprises Facilitations Centre* 2017 SCC OnLine Del 10604.

<sup>13</sup> The Micro, Small and Medium Enterprises Development Act 2006, s 18 (3).

<sup>14</sup> The Arbitration and Conciliation Act 1996, s 37.

11(6), Arbitration Act,<sup>15</sup> was allowed by the Court. Silpi Industries, enraged by the High Court's judgement, filed this appeal with the Supreme Court.

Silpi Industries objected to the maintainability of KSRTC's claims, claiming that the MSMED Act is solely intended to defend the interests of sellers. It argued that the MSMED Act's benefit to an "unpaid seller" could not be made otiose and that the benefit of a statutory body established to consider the seller's claims could not be rejected only due to the buyer's counter-claims.

The Hon'ble Supreme Court noted that the MSMED Act, which repealed the IDPASC Act, was enacted in 2006 to help and facilitate the development and competitiveness of MSMEs. The MSMED Act is a comprehensive Central legislation enacted to address the loopholes in the IDPASC Act. The Supreme Court further noted that the IDPASC Act was limited to late payments owed to small-scale/ancillary undertakings; whereas the MSMED Act covers all types of MSMEs, deals with buyer liability, and provides a mechanism in case of default under Chapter V of the MSMED Act<sup>16</sup> (covering Sections 5 to 19).

The Court held that the Limitation Act applies to the arbitration proceedings under the MSMED Act. The Supreme Court stated that if a dispute arose under Section 17, MSMED Act, a referral to the Council was required. Under Section 18, MSMED Act, the Council has to first submit the parties to conciliation. If the conciliation fails, the Council has to refer the issue to arbitration (either handled by itself or by any institution or centre deemed appropriate by the Council). The Arbitration Act would apply to these procedures.

The Court came to this conclusion after referring to Section 43, Arbitration Act,<sup>17</sup> which states that the Limitation Act applies to arbitration proceedings. The Supreme Court further pointed out that the High Court appropriately relied on the judgement in the matter of *Andhra Pradesh Power Coordination Committee*,<sup>18</sup> which addresses the issue of the applicability of the Limitation Act to arbitrations under Section 18, MSMED Act and thus upheld the findings of the Kerala High Court. The Court observed that in such cases, the provisions of the Arbitration Act are applied as if the parties have reached an agreement under Section 7(1), Arbitration Act.

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<sup>15</sup> The Arbitration and Conciliation Act 1996, s 11 (6).

<sup>16</sup> The Micro, Small and Medium Enterprises Development Act 2006, Ch V.

<sup>17</sup> The Arbitration and Conciliation Act 1996, s 43.

<sup>18</sup> *Andhra Pradesh Power Coordination Committee & Ors. v. Lanco Kondapalli Power Ltd. & Ors.* [2016] 3 SCC 468.

For the issue of counter-claims, the Supreme Court held that the counter-claim is maintainable in arbitration proceedings because the MSMED Act is a beneficial legislation, and so, even if the buyer has a claim or counter-claim, the Council has jurisdiction to try such claim or counter-claim under the MSMED Act. Section 23, Arbitration Act,<sup>19</sup> which governs the filing of a statement of claim and defence, will apply. Furthermore, Section 23(2A), Arbitration Act,<sup>20</sup> will apply, granting the buyer the right to file a counter-claim, as long as the pleas and claims were within the scope of the arbitration agreement in question.

This judgement resolved the issue of the Limitation Act's applicability and the maintainability of the counter-claim in the MSMED Act-related arbitration proceedings. It is clear from the judgement that a tribunal established under the MSMED Act will be recognised as the "exclusive forum" before which the buyer must present its counter-claim. The decision is in line with the Supreme Court's decision in *Principal Chief Engineer v. Manibhai and Bros. (Sleeper)*,<sup>21</sup> in which it affirmed the Gujarat High Court's interpretation.

However, the Court's reasoning raises the question of whether the Arbitration Act will be applicable in its entirety if the conciliation processes were unsuccessful under Section 18, MSMED Act or under limitation provisions that are not in conflict with the MSMED Act. For example, Section 18(5), MSMED Act,<sup>22</sup> allows for a 90-day time period to decide on a decision, whereas the Arbitration Act mandates that any arbitral award be issued within a 12-month period. Further, it is currently unclear whether a person that has received services or supplies from an MSME and has a claim against that MSME must seek remedy under the contract, or whether Section 18 of the MSMED Act will apply and such a party must also approach the Council.

According to the MSMED Act, a disagreement can only be referred to the Council if the amount owing to an MSME from the buyer/service recipient is in dispute. What happens, however, if the buyer wants to invoke the parties' arbitration agreement in circumstances where the MSME has performed poorly or failed to perform at all and is thus obligated to refund the cash received or pay damages under the contract? If the buyer has to raise such disputes before the Council, then this may amount to increasing the scope of the MSMED Act. In the case of *Porwal Sales*, the Bombay High Court held that the buyer would be allowed to invoke the parties' arbitration

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<sup>19</sup> The Arbitration and Conciliation Act 1996, s 23.

<sup>20</sup> The Arbitration and Conciliation Act 1996, s 23 (2A).

<sup>21</sup> *Principal Chief Engineer* (n 10).

<sup>22</sup> The Micro, Small and Medium Enterprises Development Act 2006, s 18(5).

agreement; otherwise, it would render the arbitration agreement between parties meaningless. However, it is not clear from the present judgement if the Supreme Court wants to follow the same interpretation or not.

The Hon'ble Supreme Court, through its judgement, clarified the conundrum created by the interplay of the MSMED Act and the Arbitration Act by upholding the significance of the MSMED Act. It leaves the buyers in a quandary about the options available to them in the event of a dispute.

### **Statutory arbitration under other Acts**

Statutory arbitration might be aimed toward the quick resolution of disputes, but the conflicting nature of these provisions with that of the Arbitration Act creates undesirable confusion. Such confusion is evident regarding the MSME Act and other statutes, including the Electricity Act, the Telegraph Act and the National Highways Act.

For instance, under the Electricity Act, Section 86(1)(f)<sup>23</sup> is a special provision that enables the State Electricity Regulatory Commission to adjudicate the disputes between the licensees and electricity-generating companies and refer any dispute for arbitration. In *Chief General Manager, HIEF General Manager (IPC) MP. Power Trading Company & Anr v. Narmada Equipments Pvt. Ltd.*<sup>24</sup> there was a dispute about whether the Respondents could appoint arbitrators under Section 11 of the Arbitration Act.<sup>25</sup> The Appellants claimed that the State Commission has the exclusive jurisdiction to adjudicate disputes between licensees and electricity-generating companies. The Supreme Court held that where conflict between Arbitration Act & Electricity Act arises, the latter will prevail as being a specialised provision. Section 11 thus will not be applicable in this scenario and only Section 86(1)(f) shall apply. This position has previously also been approved by the Supreme Court in the three-Judge judgement of *Hindustan Zinc Limited v. Ajmer Vidyut Vitran Nigam Limited*.<sup>26</sup> The Court also emphasised the role of Section 174 of the Electricity Act,<sup>27</sup> which stated

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<sup>23</sup> The Electricity Act 2003, s 86(1)(f).

<sup>24</sup> *Chief General Manager, HIEF General Manager (IPC) MP. Power Trading Company & Anr v. Narmada Equipments Pvt. Ltd.* Civil Appeal No. 1051 of 2021.

<sup>25</sup> The Arbitration and Conciliation Act 1996, s 11.

<sup>26</sup> *Hindustan Zinc Limited v. Ajmer Vidyut Vitran Nigam Limited* [2019] 17 SCC 82.

<sup>27</sup> The Electricity Act 2003, s 174.

that the provisions of the Electricity Act, 2003 would have an overriding effect in the event of a clash/conflict with any other existing law in force.

One another example could be of Indian Telegraph Act. Section 7B of the Indian Telegraph Act, 1885<sup>28</sup> states that in case of a dispute between the telegraph authority and the person availing the services of the authority, the case shall go to arbitration under an arbitrator appointed by the Central Government either especially for the determination of that dispute or generally for the determination of disputes under this section. In the case of *ML Jaggi v. Mahanagar Telephones Nigam Ltd.*,<sup>29</sup> the Court held that the arbitrator is empowered under Section 7B to give the award after giving the reasons for the same. The remedy under Arbitration Act is taken away in such cases because the statutory remedy is available under the Telegraph Act. Further, the Court held that the only obvious remedy available to the aggrieved person against the award is a judicial review under Article 226 of the Constitution.<sup>30</sup>

A similar situation can be observed regarding the National Highways Authority Act, 1956, where the Central Government is empowered to appoint an arbitrator under Section 3G(5).<sup>31</sup> The Supreme Court in *NHAI v. Sayedabad Tea Company Limited*<sup>32</sup> held that so far as the appointment of an Arbitrator is concerned, the power being exclusively vested with the Central Government as envisaged under sub-section (5) of Section 3G of Act 1956, Section 11 of the Arbitration Act has no application.

## Conclusion

The unresolved disagreement between the MSME Act and the Arbitration Act used to cause much dilemma for both buyers and sellers. The Silpi judgement finally resolves the dilemma and paves the way for MSMEs to adjudicate their disputes with the Council without engaging in ancillary litigation involving jurisdiction. This judgement will reduce the vexatious litigation concerning the forum of the dispute arising under the MSME Act. Through this judgment, the Court has clarified that when a statute requires something to be done a certain way, it must be done that way only. Further, the Court has upheld the importance of the MSME Act. The MSME Act was

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<sup>28</sup> Indian Telegraph Act 1885, s 7B.

<sup>29</sup> *ML Jaggi v. Mahanagar Telephones Nigam Ltd.* 1996 (3) SCC 119.

<sup>30</sup> Constitution of India, Article 226.

<sup>31</sup> The National Highways Authority Act 1956, s 3G (5).

<sup>32</sup> *NHAI v. Sayedabad Tea Company Limited* [2020] 15 SCC 161.

enacted to benefit MSME entities, and such entities should be allowed to raise their disputes under the Act. Finally, this judgement brings the conflict between MSME Act and Arbitration Act in line with other statutes having similar statutory arbitration provisions.