

# Arbitration under special statutes with regard to contractual stipulations

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## Introduction

The freedom to contract principle forms the basis of the Contract Act 1872. A similar concept is also provided for in the Arbitration and Conciliation Act 1996 (Arbitration Act), whereby the courts usually respect and follow party autonomy.

However, the question often arises as to what happens when one party – despite a contractual agreement setting out the scope and ambit of arbitration – seeks recourse to remedies provided for under a special statute.

It is a well-settled principle of statutory interpretation that a special statute that covers a specific field prevails over a general statute in the event of inconsistency or ambiguity. However, it remains unclear whether this principle automatically applies in the context of arbitration.

This article examines this issue in the context of the Micro, Small and Medium Enterprises Development Act 2006 (MSME Act) and looks at the significance of a contractual mechanism of arbitration when a party resorts to the MSME Act, as well as the judicial trend in this regard.

## MSME Act

The long title of the MSME Act sets out the reasons for its enactment – namely, "to provide for facilitating the promotion and development and enhancing the competitiveness of micro, small and medium enterprises and for matters connected therewith or incidental thereto".

## *Steel Authority of India*

The issue of an arbitration agreement's validity in the event that one party invokes the MSME Act came before the Bombay High Court in *M/s Steel Authority of India Ltd v Micro, Small Enterprise Facilitation Council* (AIR 2012 Bom 178).

In this case, the Bombay High Court observed as follows:

- Section 24 of the MSME Act makes clear that Sections 15 to 23 of the MSME Act override any inconsistency with another law.
- Section 18(3) of the MSME Act provides that if conciliation under the MSME Act fails, the MSME Facilitation (MSMEF) Council can either take up the dispute for arbitration itself or refer it to any other centre or institution for arbitration.
- The Arbitration Act applies to disputes referred by the MSMEF Council for arbitration and the procedure prescribed in the Arbitration Act applies to contractual arbitration.

Accordingly, the Bombay High Court held as follows:

*We, thus find that it cannot be said that because Section 18 provides for a forum of arbitration an independent arbitration agreement entered into between the parties will cease to have effect. There is no question of an independent arbitration agreement ceasing to have any effect because the overriding clause only overrides things inconsistent therewith and there is no inconsistency between an arbitration conducted by the Council under Section 18 and arbitration conducted under an individual clause since both are governed by the provision of the Arbitration Act, 1996.*

## Judicial trend following *Steel Authority of India*

Subsequently, in *Hindustan Wires Limited v R Suresh* (2013 SCC OnLine Bom 547), the Bombay High Court held that the proceedings under the existing arbitration agreement between the parties were not affected by the MSME Act's enactment and continued to be governed by the existing agreement.

In *Bharat Heavy Electricals Limited v State of UP* (2014 (4) ALJ 52), the Allahabad High Court diluted the principle set out by the Bombay High Court in *Steel Authority of India* by holding that:

*The proceedings had been entertained by the Council in pursuance of the provisions of the Act. Though there may be an arbitration agreement between the parties, the provisions of Section 18(4) specifically contain a non-obstante clause empowering the Facilitation Council to act as an Arbitrator. Moreover, Section 24 of the Act states that Sections 15 to 23 shall have effect notwithstanding anything inconsistent therewith contained in any other law for the time being in force.*

The principle set out in *Steel Authority of India* was further diluted by the Punjab and Haryana High Court in *The Chief Administrator Officer, COFMOW v MSEFC of Haryana* (CWP 277/2015), wherein it was contended that the pre-existing independent arbitration agreement between the parties specifically provided for a procedure to appoint the arbitrator and that this should be upheld. However, the court eventually held that:

*It must be taken only as an additional method of appointment of an arbitrator and cannot exclude the application of the provisions of this Act... A contract that provides for appointment of an arbitrator must be seen as a contract as recognized by law and that provision will stand eclipsed by the non-obstante clause that Section 18 provides for.*

Subsequently, in *Principal Chief Engineer v Manibhai and Brothers (Sleeper)* (AIR 2016 Guj 151), the Gujarat High Court specifically stated that it disagreed with the view taken by the division bench of the Bombay High Court in *Steel Authority of India*. In *Principal Chief Engineer v M/S Manibhai And Bros (Sleeper)* (Diary 16845/2017), the Supreme Court upheld the Gujarat High Court's decision, holding that the lower court's interpretation was fully justified.

### **Delhi High Court on scope of Section 18(3) of MSME Act**

In *Bharat Heavy Electricals Limited v The Micro and Small Enterprises Facilitation Centre* (2017 SCC Online Del 10604), the Delhi High Court held that it "respectfully, [was] unable to concur with the view of the Bombay High Court in *M/s Steel Authority of India v. The Micro, Small Enterprise Facilitation Council (supra)*".

The Delhi High Court followed its earlier decision in *Ge T&D India Limited v Reliable Engineering Projects* (OMP (Comm) 76/2016), wherein it was categorically held that the MSME Act overrides the Arbitration Act to the extent that it provides for a special forum for the adjudication of disputes involving a supplier registered thereunder. The court stated that Section 18(3) of the MSME Act contemplates only institutional arbitration and not *ad hoc* arbitration. Accordingly, the Bombay High Court's view in *Steel Authority of India* that independent arbitration agreements would not cease to exist despite providing for *ad hoc* arbitration was unsustainable.

In the recent case of *Mangalore Refinery & Petrochemicals Ltd v Micro and Small Enterprises Facilitation Council* (2019 SCC Online DEL 6860), the Delhi High Court relied on *Bharat Heavy Electricals Limited* to hold as follows:

*Regarding the jurisdiction of the Council to refer the disputes to arbitration that are not covered under the arbitration agreement - the same is no longer res integra. This Court has, in a number of decisions now, held that the reference under Section 18 of the MSME Act is a statutory reference and is de hors any arbitration agreement between the parties.*

### **Comment**

The Bombay High Court's approach in *Steel Authority of India* appears to have stemmed from an attempt to balance the freedom to contract principle with the principle that a special law should prevail over a general law.

Subsequent decisions have strictly followed the non-obstante clause found in Section 24 of the MSME Act and have gone by the traditional and classical view of statutory interpretation, under which a special law must prevail and nullify anything contrary thereto – whether that be a general law or statute or a contract between two parties.

With respect to the validity of a contractual arbitration mechanism following a reference to the MSMEF Council under the MSME Act, the law appears to have been settled after an initial divergence of views by the high courts. The moment that conciliation fails, Section 18(3) of the MSME Act prevails over the arbitration framework contractually agreed by the parties.

The MSME Act also provides for arbitration through the MSMEF Council and, in effect, promotes institutional arbitration. It is also a settled position of law that conciliation under Section 18 of the MSME Act is mandatory and a condition precedent for referring a dispute to arbitration. The provision for a mandatory deposit of 75% of an awarded amount under Section 19 of the MSME Act as a precondition to filing a challenge for setting aside an award passed under the MSME Act is also a major deterrent, aimed at upholding arbitral awards and promoting the interests of micro, small and medium-sized enterprises. On a holistic reading of the MSME Act, it is evident that it aims to:

- promote alternative dispute resolution in the form of conciliation and arbitration;
- promote institutional arbitration (over *ad hoc* arbitration); and
- emphasise giving finality to arbitral awards with reduced judicial interference.

The abovementioned trend aligns with the larger objective of promoting the speedy and efficient adjudication of disputes through arbitration.

*For further information on this topic please contact Jeevan Ballav Panda, Satish Padhi or Gaurav Sharma at Khaitan & Co by telephone (+91 22 6636 5000) or email (jeevan.ballav@khaitanco.com, satish.padhi@khaitanco.com or gaurav.sharma1@khaitanco.com). The Khaitan & Co website can be accessed at [www.khaitanco.com](http://www.khaitanco.com).*

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Jeevan Ballav Panda



Satish Padhi



Gaurav Sharma