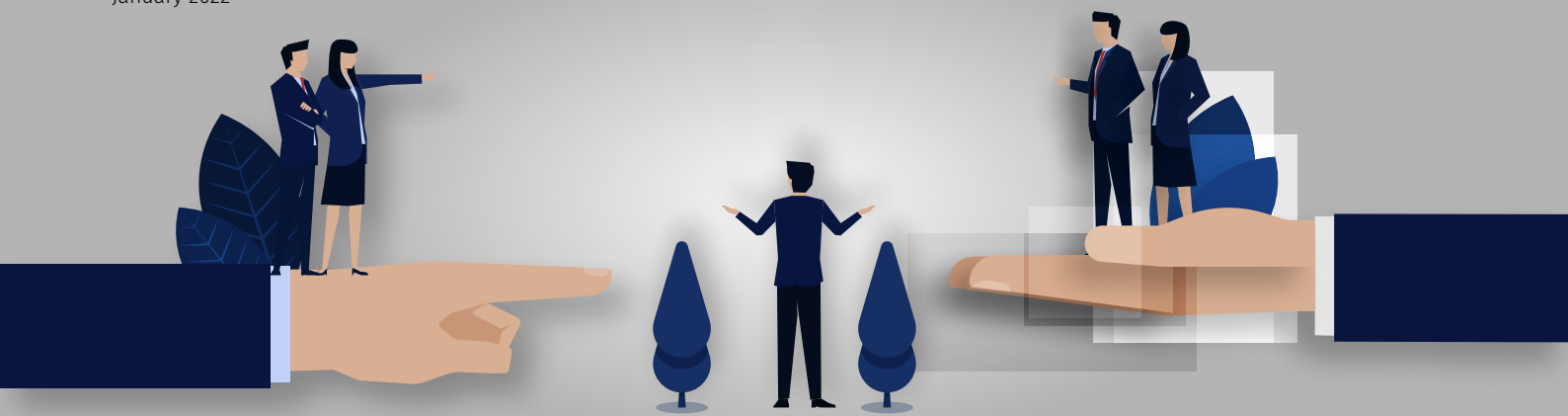


January 2022



## Supreme Court holds that if conciliation fails under the MSMED Act, the dispute has to be resolved by arbitration<sup>1</sup>

### Brief Facts

Jharkhand Urja Vikas Nigam Limited (“**Appellant**”), entered into a contract with M/s. Anamika Conductors Ltd., Jaipur (“**Respondent No. 3**”) for supply of ACSR Zebra Conductors. In relation to the said contract, Respondent No. 3, claiming to be a small scale industry, approached the Rajasthan Micro and Small Enterprises Facilitation Council, (“**Council**” or “**Respondent No. 2**”) for their claim of INR 74,74,041/- and INR 91,59,705.02/- towards the principal amount of bills and related interest, respectively. Since the Appellant failed to respond to earlier notices for conciliation, the Council issued summons to the Appellant on 18 July 2012. Thereafter, the Council passed an order dated 6 August 2012 directing the Appellant to make the requisite payment to Respondent No. 3 on the ground that the Appellant had failed to appear before the Council (“**Impugned Order**”). The Appellant challenged the said Impugned Order by way of a writ petition before the High Court of Rajasthan, Jaipur Bench, which petition was dismissed by the Single Judge and the decision was confirmed by the Division Bench.

In the present civil appeal, it was argued by the Appellant that: (i) under Section 18(3) of the Micro, Small and Medium Enterprises Development Act, 2006 (“**MSMED Act**”), the Council is required to initiate arbitration proceedings when conciliation fails; (ii) the Impugned Order is in violation of the MSMED Act as it was passed without giving any opportunity to the Appellant to participate in such arbitration proceedings; and (iii) thus, the said Order is a nullity and cannot be termed as an award under the Arbitration and Conciliation Act, 1996 (“**Arbitration Act**”).

Respondent Nos. 2 and 3 made similar arguments, stating that: (i) when the Appellant did not respond to the notices and summons issued by the Council, it took up the dispute and passed the award; (ii) the said award was open to challenge under Section 34 of the Arbitration Act within a specified period; and (iii) however, the Appellant made a belated challenge to the Impugned Order by way of the writ petition, which was rightly dismissed.

### Issues

**Issue (i):** Whether the Council was required to initiate arbitration when the Appellant did not appear in the conciliation proceedings ?

**Issue (ii):** Whether the Appellant is precluded from approaching the writ court on account of not having availed the specified remedy under Section 34 of the Arbitration Act?

### Judgment

**Issue (i):** The Supreme Court examined Sections 18(2) and 18(3) of the MSMED Act to hold that the Council is obligated to conduct conciliation or refer the matter to any institution or centre to conduct

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the conciliation in terms of the Arbitration Act, as if the conciliation was initiated under Part III of the Arbitration Act. When the conciliation fails and stands terminated, the dispute between the parties is to be resolved by way of arbitration. The Council is empowered either to take up arbitration on its own or refer the arbitration proceedings to a prescribed institution. In this context, the Court also highlighted the difference between conciliation and arbitration. While the conciliator assists the parties to arrive at an amicable settlement, an arbitral tribunal adjudicates the disputes between the parties. The claim has to be proven before the tribunal, if necessary, by adducing evidence and oral hearings are to be held, unless otherwise agreed. Therefore, if the Appellant failed to appear at the conciliation stage, the Council could have, at best, recorded the failure of conciliation and proceeded to initiate arbitration proceedings in accordance with the provisions of the Arbitration Act. Proceedings for conciliation and arbitration cannot be clubbed together.

**Issue (ii):** The Court also held that the Impugned Order was patently illegal and a nullity as it was contrary to the provisions of the MSMED Act and the Arbitration Act. Therefore, the Impugned Order was not an arbitral award in the eyes of law and Section 34 of the Arbitration Act will not apply.

In view of the above, the Court allowed the civil appeal and quashed the Impugned Order. Respondent No. 2 was allowed to either take up the dispute for arbitration on its own or refer the same to any institution or centre providing alternate dispute resolution services.

## Analysis

The Supreme Court reiterated the well-established understanding that conciliation and arbitration are two distinct processes and it is only the arbitral tribunal that is endowed with adjudicatory powers. It has been made clear that the Council has to mandatorily comply with the multi-tiered dispute resolution mechanism specified in the MSMED Act. Thus, the Court through its judgment prevented the arbitration provision under the MSMED Act from being rendered redundant. The Court also clarified that if an order is passed without recourse to arbitration, the challenge to such an order cannot be rejected on the ground that the party has not availed the remedy under Section 34 of the Arbitration Act.

## Endnotes

- 1 Authored by Smarika Singh, Partner, Yashna Mehta, Senior Associate and Adya Jha, Associate; *Jharkhand Urja Vikas Nigam Limited v. The State of Rajasthan & Ors.*, Civil Appeal No. 2899/2021, Supreme Court of India, 2021 SCC OnLine SC 1257, judgment dated 15 December 2021.

**Coram:** Indira Banerjee and R. Subhash Reddy, JJ.

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