
(2013) 05 DEL CK 0143
In the Delhi High Court
Case No : CO. Petition 471 of 2011

IFCI Factors Ltd.

APPELLANT

Vs

Krish International (P) Ltd.

RESPONDENT

Date of Decision : 07-05-2013

Acts Referred:

Companies Act, 1956 — Section 433, 433(1)(a), 433(e), 434, 434(1)(a)
Criminal Procedure Code, 1973 (CrPC) — Section 482
Negotiable Instruments Act, 1881 (NI) — Section 138

Citation : (2013) 179 CompCas 223 : (2013) 4 CompLJ 117

Hon'ble Judges : Dr. S. Muralidhar, J

Bench : Single Bench

Advocate : Anjali Sharma, for the Appellant; Aarohi Bhalla, for the Respondent

Judgement

S. Muralidhar, J.—IFCI Factors Ltd. ("IFL") has filed this petition u/s 439 read with Sections 433(e) and 434 read with Section 439 of the Companies Act, 1956 ("Act") seeking the winding up of the Respondent, Krish International Pvt. Ltd. ("KIPL"). The background facts are that in 2010, KIPL approached IFL to avail of sales bill factoring facility to the tune of Rs. 5,00,00,000. In the petition, the nature of a factoring transaction is explained as under:

Essentially, in a factoring transaction what occurs is that in consideration of finance provided by the Factor (which in this case is the petitioner), the borrower (which in this case is the respondent) assigns its receivables to the Factor under its commercial transaction with a debtor approved by the Factor, and also specifically makes itself liable for rendering all outstanding amounts to the Factor, in the event of the purchaser of goods (approved debtor) defaulting in making payment of the borrower's receivables to the Factor. Effectively, what the respondent would do in this transaction is to sell goods to its purchaser, and in consideration of its executing the relevant factoring documents, the respondent company, as borrower, would then be paid the contracted value of the said goods by the petitioner, i.e., the Factor, against assignment of receivables in favour of

the Factor. On the due date as per the agreement, the payment would then be made by the approved debtor to the Factor; and in the event of default of payment by the debtor, the borrower (which, in the present case, is the respondent hereto) would be liable to make the said payment.

2. Pursuant to the negotiations between the parties, an agreement of factoring of receivables (hereafter "factoring agreement") was executed on 18th February 2010. Mr. Alok Aggarwal, the Managing Director ("MD") of KIPL, gave an undertaking to the effect, inter alia, that the cheques issued by KIPL would be honoured on presentation. Additionally, Mr. Aggarwal also executed a guarantee deed, by which he guaranteed repayment of IFL's dues under the factoring agreement. A separate guarantee deed was executed by Mrs. Kiran Aggarwal, Director of KIPL, whereby she guaranteed payment of IFL's dues under the factoring agreement. A letter dated 18th February 2010 was issued by KIPL along with a promissory note. There was also a notice of assignment of debts dated 16th February 2010 issued by KIPL and counter-signed by KRIL. This was accepted by KRIL by a separate letter dated 17th February 2010 written to IFL.

3. In terms of factoring agreement, the "Approved Debtor" was Koutons Retail India Ltd. ("KRIL") with a funds-in-use ("FIU") limit of Rs. 4,00,00,000. KIPL was described as "Client". IFL was described as "Factor". Under Clause 3 of the factoring agreement, the expression "recourse" was defined as "The right of the Factor to require the Client to repurchase a notified receivable at a price equal to the amount remaining unpaid by the Debtor in respect thereof." Clause 9 of the factoring agreement spelt out warranties and undertakings by the "Client", i.e. KIPL. Clause 11 dealt with "recourse and set-off". Clause 14 of the Schedule to the factoring agreement noted that recourse to the Client will be automatic on the expiry of thirty days from the due date of payment by the Debtor, or earlier, as advised by IFL for each debtor from time to time. Clause 19 of the Schedule specifies the documents which have to be furnished and these include "security cheques for facility amount along with stamped letter of undertaking."

4. The case of IFL is that both the approved debtor, i.e. KRIL as well as KIPL committed defaults. It is stated that on 30th September 2011, KIPL was liable to pay IFL Rs. 3,32,82,472.47. IFL also relies upon the correspondence between the parties, and in particular, the letter dated 17th March 2011 written by KIPL to IFL acknowledging its liability and enclosing two cheques for Rs. 10,00,000 and Rs. 5,00,000 respectively and assuring that it would "endeavour to deposit Rs. 25.00 lacs to Rs. 35.00 lacs within month of March 2011" and to "take care of our outstanding by July 2011." Reliance is also placed on the letter dated 8th July 2011 from KIPL to IFL stating that on account of the defaults committed by KRIL "We are in serious trouble as their non payment of other dues exceeding Rs. 20 crores have made our business operations impossible." IFL was requested to hold back the legal action against KIPL and it was requested that the action should "jointly be directed at M/s. Koutons Retail India Ltd." Further assurances were given by another letter dated 12th August 2011 from KIPL to IFL.

5. On 29th December 2010 itself, IFL had issued a legal notice u/s 433 read with Section 434 of the Act to KIPL pointing out that as on 30th November 2010 the outstanding balance was as under:

6. Meanwhile, the cheques issued by KIPL, when presented to the Bank by IFL for payment, were dishonoured with the remarks "insufficient funds". Thereafter, on 17th January 2011, notice was issued to KIPL calling upon it to make payment of Rs. 3,00,00,000 against the dishonoured cheques together with interest @ 24% p.a., failing which the proceedings will be initiated u/s 138 of the Negotiable Instruments Act, 1881 ("NI Act"). It is stated that the criminal proceedings initiated by IFL under the NI Act against KIPL are pending. It is in the above circumstances that the present petition was filed.

7. Pursuant to the notice issued in the petition on 24th November 2011, a reply was filed by KIPL admitting to the factoring agreement entered into between the parties. The defence was that it was KRIL who was the Approved Debtor and the actual beneficiary of the goods and, therefore, liable for paying all outstanding amounts to IFL. Reliance is placed on the letter of undertaking dated 17th February 2010 executed by KRIL in favour of IFL. Secondly, it is submitted that inasmuch as IFL has filed a separate winding up petition, being Co. Pet. No. 329 of 2011, against KRIL for non-realisation of debts, the present petition is not maintainable as "two companies cannot be wound up for non-payment of the same amount." Thirdly, it is contended that the cheques issued by KIPL, which were dishonoured, were issued by way of security and not by way of acknowledgment of liability. It is submitted that IFL has purchased the receivables for consideration from KIPL and, therefore, KRIL continues to be the principal debtor from which the amount needs to be recovered. It is submitted that KIPL had, while selling receivables to IFL paid discount charges at 13.5% p.a. along with 0.20% of the total invoices factored on the Approved Debtor and 0.75% of the prepayment limit. It is stated that if the commercial decision taken by IFL has gone wrong then the only party from whom the debts could be recovered was KRIL.

8. By an order dated 13th July 2012, this Court restrained KIPL, its directors, officers and agents from parting with possession of, transferring, alienating or otherwise creating third party rights over the assets in its possession, both movable and immovable, in the ordinary course of business. The MD of the KIPL was directed to file, on an affidavit, the details of KIPL's bank accounts as well as its audited balance sheet. The said order has, however, not been complied with by KIPL.

9. Pursuant to the order passed by the Court issued on 11th February 2013, IFL filed an affidavit giving the details of the other pending litigation involving the parties. A summary suit, being CS (OS) No. 92 of 2012, has been filed by IFL against Alok Aggarwal and Kiran Aggarwal both of whom had furnished guarantees for repayment of IFL's debts by KIPL. Apart from two criminal complaints filed by IFL against KIPL u/s 138 of the NI Act, two other complaints

have been filed by it against KRIL as well.

10. By judgment dated 30th January 2013 in CrI. M.C. 905 and 906 of 2012 (KIPL v. State), a learned Single Judge of this Court dismissed the two petitions filed by KIPL u/s 482 of the Code of Criminal Procedure, 1973 ("Cr. P.C.") seeking the quashing of the two criminal complaints filed by IFL against it u/s 138 of the NI Act.

11. At one stage of these proceedings, Mr. Arun Bhardwaj, learned Senior counsel appeared for KIPL and stated that KIPL would make an offer in writing to IFL, without prejudice to its rights and contentions, for settlement of all disputes. It is stated by Ms. Anjali Sharma, learned counsel for IFL, that the offer made to IFL by KIPL was both unreasonable and unrealistic and, therefore, unacceptable to IFL.

12. Ms. Sharma submitted that all the elements of Sections 433 and 434 are fulfilled in the present case. There is a clear acknowledgment of liability by KIPL in its correspondence with IFL. The clauses of the factoring agreement made it clear that in the event of default by KRIL in paying its debts to IFL, the client, i.e., KIPL would be called upon to make good the amount. She submitted that the fact that the cheques issued by KIPL were dishonoured on presentation was further proof of the admission of liability by KIPL and its proven inability to pay the admitted debt. She placed reliance on the decision in IBA Health (I) Pvt. Ltd. Vs. Info-Drive Systems Sdn. Bhd.,

13. Appearing for KIPL, Mr. Aarohi Bhalla, learned advocate submitted that IFL had instituted criminal complaints against KRIL for dishonour of cheques to the extent of Rs. 180 lacs, although the total outstanding amount was Rs. 517 lacs. Therefore, IFL ought to explain whether it had actually received the payment of Rs. 337 lacs, and if it had not, as to why it would not proceed against KRIL for recovering the said amount. He submitted that the inference was that IFL had received some amount from KRIL, which it was not willing to disclose. In the circumstances, there was no clarity regarding the amount claimed by IFL. Secondly, he submitted that there was no question of admission of liability by KIPL. The mere fact that certain letters were written by KIPL to IFL did not mean that they had admitted the entire liability. He pointed out that the factoring arrangement was not a bill discounting arrangement. It was KRIL which had defaulted in making the payment and not KIPL. He pointed out that KIPL had, on its own, paid IFL in excess of Rs. 1,50,40,065 and, therefore, it could not be said that KIPL was either unwilling or unable to make payment. He submitted that the winding up proceedings ought not to be used only for recovery of moneys. He disputed the outstanding amount as claimed by IFL. He referred to Clause 10 of the factoring agreement and submitted that till such time KIPL was not reverted to the position in which it was prior to the execution of the factoring agreement and unable to pursue its remedies against KRIL, it cannot be asked to settle the dues of IFL.

14. The above submissions have been considered. The scope of proceedings under Sections 433 and 434 of the Act has been explained by the Supreme Court in several decisions. In *Madhusudan Gordhandas and Co. Vs. Madhu Wollen Industries Pvt. Ltd.*, the Court explained two rules which govern the issue as under:

Two rules are well settled. First if the debt is bona fide disputed and the defence is a substantial one, the court will not wind up the company. The court has dismissed a petition for winding up where the creditor claimed a sum for goods sold to the company and the company contended that no price had been agreed upon and the sum demanded by the creditor was unreasonable (See *London and Paris Banking Corporation* [1874] L.R. 19 Eq. 444). Again, a petition for winding up by a creditor who claimed payment of an agreed sum for work done for the company when the company contended that the work had not been done properly was not allowed. (See *Re. Brighton Club and Norfolk Hotel Co. Ltd.* [1962] Ch. 406)

Where the debt is undisputed the court will not act upon a defence that the company has the ability to pay the debt but the company chooses not to pay that particular debt (See *Re. A Company* 94 S.J. 369). Where however there is no doubt that the company owes the creditor a debt entitling him to a winding up order but the exact amount of the debt is disputed the court will make a winding up order without requiring the creditor to quantify the debt precisely (See *Re. Tweeds Garages Ltd.* [1865] 35 Beav. 204, 208) The principles on which the court acts are first that the defence of the company is in good faith and one of substance, secondly, the defence is likely to succeed in point of law and thirdly the company adduces prima facie proof of the facts on which the defence depends.

(emphasis supplied).

15. In *Mediquip Systems Pvt. Ltd. Vs. Proxima Medical System GMBH*, the Supreme Court was held that if the defence raised by the company was a substantial one and not a mere moonshine, then the winding up proceedings would not lie. The principles were reiterated in *Vijay Industries Vs. NATL Technologies Limited*,

16.1 In *IBA Health (India) Private Limited v. Info-Drive Systems Sdn. Bhd.*, which has been relied upon by both the parties, the facts were that a settlement was entered into between the creditor and the company in certain proceedings before the City Civil Court in Bengaluru. Thereafter, upon the company defaulting in making payment in terms of the settlement, winding up proceedings were initiated. Relying on certain clauses of the settlement deed, the Company Court admitted the petition. In appeal the company contended that it had paid the creditor a certain sum in terms of the deed of settlement, but that was not by way of an acknowledgment of liability. The Supreme Court summarised the principles as under:

23. The principles laid down in the abovementioned cases indicate that if the debt is bona fide disputed, there cannot be "neglect to pay" within the meaning of Section 433(1)(a) of the Companies Act, 1956. If there is no neglect, the deeming provision does not come into play and the winding up on the ground that the company is unable to pay its debts is not substantiated and non-payment of the amount of such a bona fide disputed debt cannot be termed as "neglect to pay" so as to incur the liability u/s 433(e) read with Section 434(1)(a) of the Companies Act, 1956.

16.2 Responding to the contention of the company that it was commercially solvent, the Supreme Court in IBA Health (India) Private Limited observed that the said factor by itself would not be sufficient to reject the petition for winding up. It held:

If there is no dispute as to the company's liability, the solvency of the company might not constitute a standalone ground for setting aside a notice u/s 434(1)(a), meaning thereby, if a debt is undisputedly owing, then it has to be paid. If the company refuses to pay on no genuine and substantial grounds, it should not be able to avoid the statutory demand. The law should be allowed to proceed and if demand is not met and an application for liquidation is filed u/s 439 in reliance of the presumption u/s 434(1)(a) that the company is unable to pay its debts, the law should take its own course and the company of course will have an opportunity on the liquidation application to rebut that presumption.

16.3 It was further explained in para 25 as under:

25. An examination of the company's insolvency may be a useful aid in determining whether the refusal to pay debt is a result of a bona fide dispute as to the liability or whether it reflects an inability to pay. Of course, if there is no dispute as to the company's liability, it is difficult to hold that the company should be able to pay the debt merely by proving that it is able to pay the debts. If the debt is an undisputedly owing, then it should be paid. If the company refused to pay, without good reason, it should be able to avoid the statutory demand by proving, at the statutory demand stage, that it is solvent. In other words, commercial solvency can be seen as relevant as to whether there was a dispute as to the debt, not as a ground in itself, that means it cannot be characterized as a standalone ground.

16.4 On the facts of that case, it was noted that there was a bona fide dispute as to the claim made by the creditor against the company, which was of a substantial nature and, therefore, a winding up petition could not have been entertained. In that context, in para 33 of the judgment, it was observed as under:

33..... A party to the dispute should not be allowed to use the threat of winding up petition as a means of enforcing the company to pay a bona fide disputed debt. A Company Court cannot be reduced as a debt collecting agency or as a means of bringing improper pressure on the company to pay a bona fide

disputed debt. Of late, we have seen several instances where the jurisdiction of the Company Court is being abused by filing winding-up petitions to pressurise the companies to pay the debts which are substantially disputed and the courts are very casual in issuing notices and ordering publication in the newspapers which may attract adverse publicity. Remember, an action may lie in appropriate court in respect of the injury to reputation caused by maliciously and unreasonably commencing liquidation proceedings against a company and later dismissed when a proper defence is made out on substantial grounds. A creditor's winding-up petition implies insolvency and is likely to damage the company's creditworthiness or its financial standing with its creditors or customers an even among the public.

17. Reverting to the facts of the case in hand, it is seen that the factoring agreement makes it abundantly clear that if the approved debtor, i.e. KRIL, defaults in making the payment to IFL, then the Client, i.e. KIPL herein, would become liable to perform its obligations under the factoring agreement. Clause 11(1) makes it absolutely clear that "As regards each receivable which the Debtor is or claims to be unable to pay whether by reason of legal constraints or acts", the factor, i.e. IFL, would have recourse to the Client, i.e. KIPL "on the expiry of the notice to the client of the length specified in paragraph 14 of the Schedule or on the insolvency of the approved debtor whichever is earlier." In the instant case, there has been an exercise of "recourse" by IFL when it called upon KIPL by notice dated 29th December 2010 to make good the payment of the amount outstanding as on that date. The factoring agreement has not been terminated and is binding on the parties. Although there is an arbitration clause in the factoring agreement, the right of IFL to seek recourse to other remedies in law for the recovery of the admitted debt is not precluded. On its part, IFL has satisfied the requirements of Clause 14 of the Schedule read with Clause 11(1) (a) of the factoring agreement and has notified the Client "to repurchase" the notified receivables at a price equal to the amount remaining unpaid by KRIL.

18. There is a clear admission of liability by KIPL in more than one way. In its letter dated 17th March 2011 addressed to IFL, KIPL has, after mentioning the default committed by KRIL, informed IFL that it had till then deposited Rs. 1,29,40,065 and was enclosing two further cheques of Rs. 10,00,000 and Rs. 5,00,000 respectively. It undertook to pay a further sum of Rs. 25,00,000 and Rs. 35,00,000 in March 2011 and to take care of outstanding by July 2011. Again, by letter dated 8th July 2011, KIPL requested IFL to "hold your legal action against us as this action should jointly be directed at M/s. KRIL. We undertake to make arrangements to pay you additional Rs. 10,00,000 by 15th July 2011. Further, we will take care of our dues by September by selling the goods which we are going to release from the port. We understand your difficult situation, but kindly also bear in mind our position caused due to default of M/s. Koutons Retail who actually owes this amount." Even in the letter dated 12th August 2011, a further undertaking was given by KIPL to IFL stating that "We undertake to make arrangements to pay you additional amount of Rs. 5,00,000

vide cheque No. 057394 dated 12.08.2011 and Rs. 5,00,000 vide cheque no. 057395 dated 31.08.2011. Further, we will take care of our dues by November 2011 by selling the goods which we are going to release from the port. We understand your difficult situation, but kindly also bear in mind our position caused due to default of M/s. Koutons Retail who actually owes this amount."

19. After the above repeated assurances given by KIPL to IFL consistent with its obligations under the factoring agreement, it is futile for KIPL to contend either that there is no admitted liability of KIPL or deny its inability to make payment of the admitted liability. There is also no denial of the fact that the cheques issued by KIPL to IFL were on presentation dishonoured. That has resulted in IFL instituting proceedings against KIPL under the NI Act. This constitutes both an admission of liability by KIPL and its inability to make payment. On the facts of the present case, the decision in IBA Health (India) Private Limited v. Info-Drive Systems Sdn. Bhd. cannot come to the aid of KIPL. On the other hand, that said decision holds that "if a debt is undisputedly owing, then it has to be paid. If the company refuses to pay on no genuine and substantial grounds, it should not be able to avoid the statutory demand."

20. The Court is satisfied that IFL has made out a case for admission of the petition and for appointing a provisional liquidator ("PL") for KIPL. The defence of KIPL is not bona fide. It is a case of an admission of liability and the demonstrated inability of KIPL to make good the liability. On behalf of IFL it was submitted that to the extent that KIPL is able to pay the amount owing to IFL, the claims against KRIL to that extent would stand abated. In any event, that is contingent upon KIPL being able to make good the entire amount together with interest owing to IFL.

21. For the aforementioned reasons, the petition is admitted. The Official Liquidator ("OL") is appointed as a PL of KIPL. The OL is directed to take over all the assets, books of accounts and records of the Respondent from the date this order is made effective as indicated hereafter. A complete set of the paper book be served on the OL. The OL shall also prepare a complete inventory of all the assets of the Respondent before sealing the premises in which they are kept. He may also seek the assistance of a valuer to value the assets. He is permitted to take the assistance of the local police authorities, if required.

22. Publication of the citation of the petition be effected in the Official Gazette, "The Times of India" (English) and "Jansatta" (Hindi) in terms of Rule 24 of the Companies (Court) Rules, 1959 ("Rules"). The cost of publication shall be borne by IFL. The Directors of KIPL are directed to strictly comply with the requirements of Section 454 of the Companies Act, 1956 and Rule 130 of the Rules and furnish to the OL a statement of affairs in the prescribed form verified by an affidavit within a period of 21 days from the date the order is made effective in terms of para 24 below. They will also file affidavits in this Court, with advance copies to the OL, within four weeks thereafter setting out the details of all the assets, both movable and immovable, of KIPL and enclose therewith its

balance sheets, profit and loss accounts and copies of the statements of all the bank accounts for the last three years.

23. However, this order is kept in abeyance for eight weeks to enable KIPL to make payment of the sum as set out in the petition, failing which this order will be made operational and further steps will be taken by the OL in terms of this order. If the payment is not made by KIPL within the time granted, IFL will inform the OL forthwith to enable to OL to take further steps in terms of this order. In that event, a compliance report will be filed by the OL before the next date of hearing. List on 25th September 2013.