

M/S. IBA HEALTH (I) P. LTD.

v.

M/S INFO-DRIVE SYSTEMS SDN. BHD.

(Civil Appeal No. 8230 of 2010)

SEPTEMBER 23, 2010

**[S.H. KAPADIA, CJI AND K. S. PANICKER
RADHAKRISHNAN, J.]**

Companies Act, 1956:

ss.433, 434 – Winding up petition by the creditor – Maintainability of – Held: Not maintainable when there is substantial dispute as to liability – If the debt is bona fide disputed, there cannot be “neglect to pay” within the meaning of s.433(1)(a) – “Bona fide dispute” implies the existence of a substantial ground for the dispute raised – On fact, there was bona fide dispute as to liability – Company Court erred in ordering winding up of the company – The approach of Company Court was very casual as it did not make any endeavour to ascertain as to whether the company sought to be wound up for non-payment of debt had a defence which was substantial in nature.

ss.434(1)(a) – Commercial solvency – Held: An examination of the company’s solvency 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 – If the debt is an undisputedly owing, then it should be paid – If the company refuses to pay, without good reason, it should not be allowed to avoid the statutory demand by proving, at the statutory demand stage, that it is solvent – The commercial solvency cannot be characterized as a stand alone ground.

ss.433, 434 – Winding up proceedings – Abuse of –

- A *Held: 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 and even among the public – 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 – Company Court should be guarded from such vexatious abuse of the process and cannot function as a Debt Collecting Agency and should not permit a party to unreasonably set the law in motion, especially when the aggrieved party has a remedy elsewhere.*

- C *s.433 – Winding up petition – Publication in the newspaper about the filing of petition – Caution – Held: It may damage the creditworthiness or financial standing of the company and may also have other economic and social ramifications – Company Court, at times, has not only to look into the interest of the creditors, but also the interests of public at large and should be more vigilant so that its medium would not be misused – Public policy.*

- E *Words and phrases: "Bona fide dispute" – Meaning of.*

- F **The appellant company was originally incorporated as Medicom Solutions Pvt. Ltd. (Medicom). In Dec., 2005, it was acquired by two Singapore companies. The paid up capital of appellant was in excess of Rs.10.06 crores at the end of 31.3.2009 and its fixed assets and investments were in excess of Rs.23.83 crores. At the end of 31.3.2009, it had made a profit of over Rs.15 crores and there were over 300 employees working in the appellant company. The respondent company was incorporated in Malaysia which was originally incorporated as Bitech. The appellant and the respondent entered into the Cooperation Agreement on 18.2.2002. Pursuant to the said agreement, the respondent introduced the appellant to one M/s. Solution Protoc for the sale and supply of**

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certain software services and the appellant agreed to pay to the respondent company certain commission charges as set out in the said agreement.

The dispute arose between the parties regarding the payment of the commission charges which led the parties entering into a deed of settlement dated 19.12.2003, pursuant to which the terms of the Cooperation Agreement were superseded by the deed of settlement and the appellant agreed to pay the commission charges due to the respondent in accordance with the terms and conditions set out in the deed of settlement. The respondent filed a suit for restraining the acquisition of the appellant company alleging the breach of the terms of the settlement deed. The parties entered into a compromise on 18.3.2006, pursuant to which both the parties agreed to adhere to the terms and conditions of the deed of settlement dated 19.12.2003.

After the compromise was filed, the respondent received an amount of RM1,069,583.29 on 20.3.2006 from the appellant. Alleging that, despite receiving periodical payments from M/s Solutions Protocol, the appellant company had failed to honour its commitments as per the deed of settlement and the compromise, the respondent issued an invoice to the appellant claiming an amount of US\$ 1,065,714.00 allegedly due towards fees for the marketing services. A legal notice dated 16.8.2008 was served on the appellant under Section 434(1)(a) of the Companies Act, 1956 to pay the amount within twenty one days from the date of the receipt of that notice, failing which the appropriate legal proceedings would be initiated. The appellant replied that it had not violated any of the terms and conditions of the said deed of settlement or the compromise entered into by the parties and that whatever amount received by the appellant prior to 31.12.2006 from M/s Solutions Protocol was paid to the

A respondent. The appellant also denied the liability to pay the amount demanded.

B The respondent filed a company petition praying for the winding up of the appellant company. The Company Judge held that the respondent company has established a *prima facie* case and ordered that the matter be re-listed for orders regarding advertisement to be published in the newspaper. The Company Judge also directed the parties to appear before the Mediation Centre at Bangalore for amicably settling the dispute. The appellant C filed appeal before the Division Bench of the High Court which was dismissed. The said order was challenged in the instant appeal.

D Allowing the appeal, the Court

D HELD: 1. When a creditor prefers an application for winding up for discharge of liability and there is a substantial dispute as to such liability, the Company court, at that stage, is not expected to hold a full trial of the matter. It must decide whether the grounds appear to E be substantial. The grounds of dispute, of course, must not consist of some ingenious mask invented to deprive a creditor of a just and honest entitlement and must not be a mere wrangle. It is settled law that if the creditor's debt is *bona fide* disputed on substantial grounds, the court F should dismiss the petition and leave the creditor first to establish his claim in an action, lest there is danger of abuse of winding up procedure. A dispute as to liability would be substantial and genuine if it is *bona fide* and not spurious, speculative, illusory or misconceived. The G Company Court always retains the discretion, but a party to a dispute should not be allowed to use the threat of winding up petition as a means of forcing the company to pay a *bona fide* disputed debt. If the debt is *bona fide* disputed, there cannot be "neglect to pay" within the H 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 under Section 433(e) read with Section 434(1)(a) of the Companies Act, 1956. [Paras 17, 20] [155-H; 156-A-D; 157-C-D]

Amalgamated Commercial Traders (P) Ltd. v. A.C.K. Krishnaswami and another (1965) 35 Company Cases 456 (SC); *Madhusudan Gordhandas and Co. v. Madhu Woollen Industries Pvt. Ltd.* (1971) 3 SCC 632; *Mediquip Systems (P) Ltd. v. Proxima Medical Systems (GMBH)* (2005) 7 SCC 42; *Vijay Industries v. NATL Technologies Ltd.* (2009) 3 SCC 527, relied on.

2. An examination of the company’s solvency 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. If the debt is an undisputedly owing, then it should be paid. If the company refuses to pay, without good reason, it should not be allowed to avoid the statutory demand by proving, at the statutory demand stage, that it is solvent. The commercial solvency cannot be characterized as a stand alone ground. In the instant case, both the parties were in agreement that they were bound by the terms and conditions of the deed of settlement. The deed of settlement stipulated that the parties acknowledged the obligation of Medicom to pay to Bitech the settlement sum subject to Medicom (or its representatives or nominees) having received payments of sufficient value from M/s. Solution Protocol to enable the payment of upto the maximum amount of the settlement sum to be made on or before 31.12.2006, which is the cut-off date. Further one of the terms of the compromise was that the

- A respondent would make reasonable efforts to persuade M/s. Solutions Protocol to settle the invoices of the appellant at the earliest. On a detailed analysis of the various terms and conditions incorporated in the deed of settlement as well as the compromise deed and the
- B averments made by the parties, there is a *bona fide* dispute with regard to the amount of claim made by the respondent company in the company petition which is substantial in nature. The Company Court while exercising its powers under Sections 433 and 434 of the
- C Companies Act, 1956 would not be in a position to decide who was at fault in not complying with the terms and conditions of the deed of settlement and the compromise deed which calls for detailed investigation of facts and examination of evidence and calls for interpretation of the
- D various terms and conditions of the deed of settlement and the compromise entered into between the parties. A company petition cannot be pursued in respect of contingent debt unless the contingency has happened and it has become actually due. In the absence of any
- E evidence, it is not possible to conclude that M/s. Solutions Protocol had in fact paid any amount to the appellant company towards commission charges due to the respondent company before the cut off date. A legal notice prior to the institution of the company petition could be served on the company only in respect of a debt
- F (then due) and a company could be wound up only if it was unable to pay its debts. In the instant case, there is a *bona fide* dispute as to whether the amount claimed is presently due and if, at all, it is due, whether the appellant company is liable to pay the sum unless they have
- G received the same from M/s. Solutions Protocol. Where the company has a *bona fide* dispute, the petitioner cannot be regarded as a creditor of the company for the purposes of winding up. "*Bona fide* dispute" implies the existence of a substantial ground for the dispute raised.
- H Where the Company Court is satisfied that a debt upon

which a petition is founded is a hotly contested debt and also doubtful, the Company Court should not entertain such a petition. The Company Court is expected to go into the causes of refusal by the company to pay before coming to that conclusion. The Company Court is expected to ascertain that the company's refusal is supported by a reasonable cause or a *bona fide* dispute in which the dispute can only be adjudicated by a trial in a civil court. In the instant case, the Company Court was very casual in its approach and did not make any endeavour to ascertain as to whether the company sought to be wound up for non-payment of debt has a defence which is substantial in nature and if not adjudicated in a proper forum, would cause serious prejudice to the company. [Para 22, 23, 24] [158-B-H; 159-A-H; 160-A-F]

3. There has been an attempt by the respondent company to force the payment of a debt which the respondent company knows to be in substantial dispute. 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. It is seen that the jurisdiction of the Company Court is being abused by filing winding up petitions to pressurize 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. 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

A damage the company's creditworthiness or its financial standing with its creditors or customers and even among the public. [Para 25] [160-H; 161-A-D]

B 4. A creditor's winding up petition, in certain situations, implies insolvency or financial position with other creditors, banking institutions, customers and so on. Publication in the Newspaper of the filing of winding up petition may damage the creditworthiness or financial standing of the company and which may also have other economic and social ramifications. Competitors will be all the more happy and the sale of its products may go down in the market and it may also trigger a series of cross-defaults, and may further push the company into a state of acute insolvency much more than what it was when the petition was filed. The Company Court, at times, has not only to look into the interest of the creditors, but also the interests of public at large and should be more vigilant so that its medium would not be misused. A Company Court, therefore, should act with circumspection, care and caution and examine as to whether an attempt is made to pressurize the company to pay a debt which is substantially disputed. A Company Court, therefore, should be guarded from such vexatious abuse of the process and cannot function as a Debt Collecting Agency and should not permit a party to unreasonably set the law in motion, especially when the aggrieved party has a remedy elsewhere. [Paras 26, 27] [161-E-H; 162-A-B]

G 5. In the facts and circumstances of the case, the order passed by the Company Court ordering publication of advertisement in the newspaper would definitely tarnish the image and reputation of the appellant company resulting in serious civil consequences and, thus, the order passed by the Company Court and the judgment of the Division Bench of the High Court is set H

aside. [Para 28] [162-C-E]

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Case Law Reference:

(1965) 35 Company Cases 456 (SC) referred to Para 18

(1971) 3 SCC 632 referred to Para 19

(2005) 7 SCC 42 referred to Para 19

(2009) 3 SCC 527 referred to Para 19

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CIVIL APPELLATE JURISDICTION : Civil Appeal No. 8230 of 2010.

From the Judgment & Order dated 21.10.2009 of the High of High Court of Karnataka at Bangalore in OSA No. 36 of 2009.

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R.F. Nariman, Chetan Chopra, Dheeraj Nair for the Appellant.

R.S. Hegde, P.P. Hegde for the Respondent.

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The Judgment of the Court was delivered by

K. S. PANICKER RADHAKRISHNAN, J. 1. Leave granted.

2. A Company Petition No. 41 of 2009 was filed by the respondent herein under Sections 433(e) & (f), 434 and 439 of the Companies Act, 1956 before the High Court of Karnataka at Bangalore (hereinafter referred to as the Company Court) praying for winding up of the appellant company on the ground that it had failed to pay a sum of US\$ 1,065,714.00 in terms of the Deed of Settlement entered into by the parties on 19.12.2003 towards the fees for the marketing services undertaken by the respondent for the appellant.

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3. Prior to the filing of the company petition, a legal notice

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- A dated 16.8.2008 was served on the appellant under Section 434(1)(a) of the Companies Act, 1956, calling upon the company to pay the amount within twenty one days from the date of the receipt of that notice, failing which the appellant was informed that appropriate legal proceedings would be initiated.
- B Specific reference was also made to the deed of settlement dated 19.12.2003 and the terms of the Compromise entered into by the parties on 18.3.2006 in O.S. No. 9655 of 2005 before the City Civil Court at Bangalore.

C 4. The appellant replied to the said notice vide its letter dated 28.8.2008 stating that it had not violated any of the terms and conditions of the said deed of settlement or the compromise entered into by the parties and that whatever amount received by the appellant prior to 31.12.2006 from M/s Solutions Protocol Sdn. Bhd., a company incorporated in D Malaysia, was paid to the respondent. The appellant also denied the liability to pay the amount demanded. The respondent was advised not to indulge in any frivolous litigation against the appellant which would be at their risk and costs.

E 5. The Company Judge, however, admitted the company petition vide its order dated 17.9.2009 holding that the respondent company has established a *prima facie* case and ordered that the matter be re-listed for orders regarding advertisement to be published in the newspaper. The Company F Judge also referred to certain clauses in the deed of settlement and the compromise petition and concluded *prima facie* that the appellant had undertaken to make future payments to the respondent. The Company Judge also directed the parties to appear before the Mediation Centre at Bangalore for amicably settling the dispute. Aggrieved by the above mentioned order, G the appellant company filed OSA No. 36 of 2009 before the Division Bench of the High Court of Karnataka which was dismissed vide its judgment dated 21.10.2009 and hence, the present appeal before this Court.

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6. Mr. R. F. Nariman, learned senior counsel appearing for the appellant company submitted that no grounds have been made out even *prima facie* warranting interference by the Company Court and to proceed further calling for an advertisement in the newspaper or directing the parties to appear before the Mediation Centre for amicably settling the dispute. Learned senior counsel submitted that the Company Judge as well as the Division Bench have completely misunderstood the terms and conditions of the deed of settlement dated 19.12.2003 and the compromise entered into by the parties on 18.3.2006. The learned senior counsel also submitted that if at all the respondent is aggrieved, the remedy open to the respondent is to approach in the Civil Court and not by way of a winding up petition, especially when there is substantial dispute between the parties. Learned counsel also submitted that the company is commercially solvent and capable of discharging its debts, if legally due.

7. Mr. R. S. Hegde, learned counsel appearing for the respondent company submitted that the Company Court as well as the Division Bench of the High Court have correctly come to the conclusion that *prima facie* grounds have been made out under Section 433(e) & (f) read with Section 434 of the Companies Act. The learned counsel submitted that the appellant company has failed to comply with the terms and conditions of the deed of settlement dated 19.12.2003 and the compromise entered into by the parties dated 18.3.2006. Learned counsel submitted that the appellant company is not in a position to pay off its debts and it is just and equitable that the appellant company be wound up.

FACTS IN BRIEF

8. The appellant [M/s IBA Health (India) Private Limited] was originally incorporated as Medicom Solutions Private Limited. The name of the appellant company was changed to M/s IBA Health (India) Private Limited in December 2005 following its acquisition by IBA Health (Asia) Holding Pte.

A Limited and IBA Health (Singapore) Pte. Limited, both of which are entities incorporated in Singapore. The paid up capital of the appellant company was in excess of Rs.10.06 crores at the end of 31.3.2009 and its fixed assets and investments were in excess of Rs.23.83 crores. At the end of 31.3.2009, it had made a profit of over Rs.15 crores and there were over 300 employees working in the appellant company. The respondent is a company incorporated in Malaysia which was originally incorporated as Bhari Information Technology Systems Sdn. Bhd. and subsequently changed its name to Info-Drive Systems Sdn. Bhd.

9. Pursuant to a Cooperation Agreement dated 18.2.2002 entered into by the appellant and the respondent, the respondent introduced the appellant to one M/s. Solutions Protocol Sdn. Bhd. for the sale and supply of the appellant's Hospital Information Systems (HIS) Software applications and for that service, the appellant company agreed to pay the respondent company certain commission charges as set out in the said agreement. The dispute arose between the parties regarding the payment of the commission charges which led the parties entering into a deed of settlement dated 19.12.2003, pursuant to which the terms of the cooperation agreement were superseded by the deed of settlement and the appellant agreed to pay the commission charges due to the respondent in accordance with the terms and conditions set out in the deed of settlement.

10. Alleging breach of the terms of the deed of settlement, the respondent filed a civil suit being O.S. No. 9655 of 2005 before the City Civil Court, Bangalore for restraining the acquisition of the appellant by IBA Health (Asia) Holding Pte. Limited and IBA Health (Singapore) Pte. Limited. The parties entered into a compromise on 18.3.2006, pursuant to which both the parties agreed to adhere to the terms and conditions of the deed of settlement dated 19.12.2003.

11. After the compromise petition was filed, the respondent

received an amount of RM1,069,583.29 on 20.3.2006 from the appellant. Alleging that, despite receiving periodical payments from M/s Solutions Protocol Sdn. Bhd., the appellant company had failed to honour its commitments as per the deed of settlement and the compromise entered into by the parties, the respondent issued an invoice dated 2.2.2007 to the appellant claiming an amount of US\$ 1,065,714.00 allegedly due towards fees for the marketing services. Since the appellant declined to pay the amount demanded, the respondent issued a legal notice dated 4.7.2007 calling upon the appellant to pay the above mentioned amount within fifteen days from the receipt of the notice, failing which the appellant was informed that the legal proceedings would be initiated against it. Reference was also made to various terms and conditions incorporated in the deed of settlement.

12. Appellant replied to the said notice on 19.7.2007 stating that it had not violated any of the terms and conditions of the deed of settlement dated 19.12.2003 and pointed out that whatever amounts received by the appellant from M/s Solutions Protocol Sdn. Bhd. were paid over to the respondent. It was stated that the appellant company had received no other payments till 31.12.2006 after they made payment to the respondent on 20.3.2006. Further, it was pointed out that the invoice dated 2.2.2007 had no basis as it has been issued to M/s IBA Health Limited, a company incorporated in Australia and was not a party to the cooperation agreement or the deed of settlement. The respondent company was advised not to indulge in any frivolous proceedings against the appellant, which it was stated would be at their risk and costs. The respondent company then issued a legal notice dated 16.8.2008 under Section 434 of the Companies Act calling upon the appellant to pay the amount demanded within twenty one days from the date of receipt of notice, failing which the appellant was informed that appropriate legal proceedings would be initiated. The notice was replied by the appellant company vide letter dated 28.8.2008 denying its liability.

A Further, it was also pointed out that any attempt to initiate proceedings under Section 433(e) of the Companies Act, 1956 has to fail as there is no debt payable by the appellant.

B 13. We are, in this case, primarily concerned with the terms and conditions of the deed of settlement followed by the terms of the compromise entered into by the parties on 18.3.2006 in O.S. No. 9655 of 2005. In order to examine the rival contentions raised by the parties, it is useful to refer to the terms and conditions incorporated in the above mentioned documents.
C The relevant terms and conditions of the deed of settlement dated 19.12.2003 are as follows:

- D “1. MEDICOM has agreed to pay and BITECH has agreed to accept up to the maximum amount of Ringgit Malaysia Eight Million Six Hundred Thousand (RM 8,600,000) only as full and final settlement subject to terms and conditions hereinafter contained (hereinafter referred to as the “Settlement Sum”).
- E 2. The Parties hereto agreed that the Settlement Sum is formulated based on the following proportions of the total amounts of MIDICOM produce license fee and/or all other payments received by MEDICOM from SP and/or SP/JV by virtue of the HICT Package I Contract:
- F i. Eleven (11%) percent of the MEDICOM HIS software applications produce license fee, subject to a maximum of Ringgit Malaysia Six Million Two Hundred Thousand (RM 6,200,000) only;
- G ii. Subject to a maximum of Ringgit Malaysia Two Million Four Hundred Thousand (RM 2,400,000) only:

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- a. Twelve (12%) percent for implementation and business process re-engineering fees only, for payments received by MEDICOM on or before 31st December, 2003; A
 - b. Five (5%) percent for implementation and business process re-engineering fees only, for payments received by MEDICOM after 31st December, 2003; B
 - iii. The Settlement Sum as indicated in subparagraphs (i) and (ii) above is only towards the amount received from SP and/or SP/JV for any of the 13 named hospitals along with scope of modules/deliverables agreed as part of HICT Package I Contract. BITECH shall not be entitled to any amount in respect of any new hospitals added to HICT Package I Contract or replacement hospitals to HICT Package I contract or change in methodology and scope of supply; C
D
 - iv. BITECH shall have no claims either now or anytime in future on payments received by MEDICOM from SP and/or SP/JV on any other items of deliverables not specified in Clause 2(i) or Clause 2(ii) above, howsoever designated, including Software Maintenance, Annual Maintenance Charges (AMC), customization, per diem charges, local expenses, airfare & travel expenses, accommodation expenses and the like. E
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3. The Settlement Sum shall be valid for payments received by MEDICOM from SP and/or SP/JV under the HICT Package I Contract and/or the HIS software applications modules contracted for the HICT Package I Contract with SP/JV only and it is G
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A conclusively agreed to that BITECH shall not in any
circumstances whatsoever be entitled in law or
otherwise for any payment for any other contracts
including contracts involving MEDICOM and
B Solutions Protocol from the Government of Malaysia
or otherwise, whether in Malaysia or any other
country.

4. The Parties hereto hereby acknowledge that the
obligation of MEDICOM to pay BITECH the
C Settlement Sum shall always be subject to
MEDICOM (or its representatives or nominees)
having received payments of sufficient value from
SP and/or SP/JV to enable the payment of up to
D the maximum amount of the Settlement Sum to be
made on or before 31st December, 2006
(hereinafter referred to as the "Cut-Off Date") and
in the event that such payments are not received on
or before the Cut-off Date, the Parties agree that
BITECH shall receive a proportion of the total value
of payments received by MEDICOM (or its
E representatives or nominees) to be calculated in
accordance with Clause 2(i) and (ii) above.

5. BITECH may designate a nominee to receive
payments from MEDICOM constituting the
F Settlement Sum, the identity and address of which
shall be communicated MEDICOM and Solutions
Protocol in writing upon the execution of this Deed
of Settlement.

G xxx xxx xxx
xxx xxx xxx

7. The Settlement sum shall be initiated for the
process of payment by MEDICOM to BITECH in
H the following manner:

i. For all or any amounts received by MEDICOM up to 31 December 2003, MEDICOM shall issue and establish an irrevocable Letter of Credit (LC) to BITECH in the proportions set out in Clause 2(i) and (iia) within 10 working days from 31st December, 2003; and

ii. For any amounts received by MEDICOM from SP/JV after 31 December 2003 onwards, MEDICOM shall issue and establish an irrevocable Letter of Credit (LC) to BITECH in the proportions set out in Clause 2(i) and (iib) within 21 working days from the date the payment is received by MEDICOM.

xxx xxx xxx
xxx xxx xxx

19. This Deed of Settlement shall be governed by and construed in accordance with the law of India and the parties hereto submit to the exclusive jurisdiction of the courts of Bangalore, India."

14. Following the above deed of settlement, we have already indicated that the parties had entered into a Compromise on 18.3.2006 in O.S. No. 9655 of 2005. Reference may also be made to clauses 2 to 6 of the said Compromise deed, which are extracted hereunder:

" xxx xxx xxx
xxx xxx xxx

2. The Defendant has agreed that it will provide report once in two months to plaintiff, of defendant's invoices raised on M/s Solution Protocol Sdn. BHD,

A Malaysia and reports once in two months, of
payment effected by M/s. Solutions Protocol Sdn.
BHD, Malaysia in favour of the defendant pertaining
to the transactions under HICT Package I Contract
as referred in Clause 2(i)(ii) & (iii) of the Deed of
B Settlement. Plaintiff assures that it will make
reasonable efforts to persuade M/s. Solutions
Protocol to settle the invoices of the defendant at
the earliest.

C 3. The Defendant agreed to make future payments to
the plaintiff as per Plaintiff's entitlement and as per
the defendant's obligation under the Deed of
Settlement.

D 4. The Defendant, based on transactions pertaining to
the Deed of Settlement has paid the amount having
become due and payable to the Plaintiff as on date.
The Plaintiff accepts that it has received all
payments due to it as on date from the defendant
as per the terms of the deed of settlement.

E 5. The Defendant has already disclosed the right of
the Plaintiff in respect of Deed of Settlement
mentioned in the suit, to M/s IBA Health Limited,
Australia in the understanding entered with them.

F 6. This compromise shall be binding on the parties
and shall not be construed as creating an
executable decree.

xxx xxx xxx

G xxx xxx xxx"

15. The respondent company in company petition alleged
that the appellant had failed to comply with the terms and
conditions of the deed of settlement and since no payment w
H s forthcoming from the appellant company and, it was under

such circumstances, that a legal notice legal notice dated 16.8.2008 was issued on the appellant reminding of its obligations under the deed of settlement. Further, it is also stated that the respondent had reliably learnt that substantial payment had been received by the appellant from M/s Solutions Protocol Sdn. Bhd. and, in spite of that, the appellant company had failed to honour its commitments under the deed of settlement. Reference was also made to clause (4) of the deed of settlement.

16. Appellant company in its statement of objections stated that it had paid the amount of RM 1,069,583.89 to the respondent company in due compliance with the terms of the deed of settlement. Further it was pointed out that the appellant company had not received any amount from M/s Solutions Protocol Sdn. Bhd. since its payment in March 2006. Further, it is also pointed out that the appellant company had no subsisting commercial dealings with M/s. Solutions Protocol Sdn. Bhd. and that the respondent company should be put to strict proof with regard to the transactions completed before 31.12.2006 and also the payments effected by M/s Solutions Protocol Sdn. Bhd. to the appellant company. Further, it was pointed out that the documents Annexure J1 to J9 did not pertain to the appellant company and it had not received any payment thereunder. Further, it was pointed out that the allegations raised by the respondent company are totally frivolous which would require detailed investigation, recording of evidence and adjudication of the rights and obligations of third-party entities and would fall beyond the scope of enquiry to be conducted by the Company Court under Sections 433, 434 and 439 of the Companies Act, 1956 and if, at all, the respondent is aggrieved, the remedy open is to approach the Civil Court for adjudication of its claims.

SUBSTANTIAL DISPUTE – AS TO LIABILITY

17. The question that arises for consideration is that when

- A there is a substantial dispute as to liability, can a creditor prefer an application for winding up for discharge of that liability? In such a situation, is there not a duty on the Company Court to examine whether the company has a genuine dispute to the claimed debt? A dispute would be substantial and genuine if it is *bona fide* and not spurious, speculative, illusory or misconceived. The Company Court, at that stage, is not expected to hold a full trial of the matter. It must decide whether the grounds appear to be substantial. The grounds of dispute, of course, must not consist of some ingenious mask invented to deprive a creditor of a just and honest entitlement and must not be a mere wrangle. It is settled law that if the creditor's debt is *bona fide* disputed on substantial grounds, the court should dismiss the petition and leave the creditor first to establish his claim in an action, lest there is danger of abuse of winding up procedure. The Company Court always retains the discretion, but a party to a dispute should not be allowed to use the threat of winding up petition as a means of forcing the company to pay a *bona fide* disputed debt.

18. In this connection, reference may be made to the judgment of this Court in *Amalgamated Commercial Traders (P) Ltd. v. A.C.K. Krishnaswami and another* (1965) 35 Company Cases 456 (SC), in which this Court held that "It is well-settled that 'a winding up petition is not a legitimate means of seeking to enforce payment of the debt which is *bona fide* disputed by the company. A petition presented ostensibly for a winding up order but really to exercise pressure will be dismissed, and under circumstances may be stigmatized as a scandalous abuse of the process of the court."

19. The above mentioned decision was later followed by this Court in *Madhusudan Gordhandas and Co. v. Madhu Woollen Industries Pvt. Ltd.* 1971) 3 SCC 632. The principles laid down in the above mentioned judgment have again been reiterated by this Court in *Mediquip Systems (P) Ltd. v. Proxima Medical Systems (GMBH)* (2005) 7 SCC 42, wherein

this Court held that the defence raised by the appellant-company was a substantial one and not mere moonshine and had to be finally adjudicated upon on the merits before the appropriate forum. The above mentioned judgments were later followed by this Court in *Vijay Industries v. NATL Technologies Ltd.* (2009) 3 SCC 527.

20. The principles laid down in the above mentioned 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 under Section 433(e) read with Section 434(1)(a) of the Companies Act, 1956.

COMMERCIALLY SOLVENT

21. Appellant company raised a contention that it is commercially solvent and, in such a situation, the question may arise that the factum of commercial solvency, as such, would be sufficient to reject the petition for winding up, unless substantial grounds for its rejection are made out. A determination of examination of the company's insolvency may be a useful aid in deciding whether the refusal to pay is a result of the *bona fide* dispute as to liability or whether it reflects an inability to pay, in such a situation, solvency is relevant not as a separate ground. If there is no dispute as to the company's liability, the solvency of the company might not constitute a stand alone ground for setting aside a notice under Section 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 under Section 439 in reliance of the presumption under Section

A 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.

B 22. An examination of the company's solvency 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 undisputedly owing, then it should be paid. If the company refuses to pay, without good reason, it should not 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 stand alone ground.

E 23. We have gone through various terms and conditions of the deed of settlement as also the compromise agreement and the allegations raised in the company petition and the objections filed by the appellant company. Both the parties are in agreement that they are bound by the terms and conditions of the deed of settlement. The respondent maintained the stand that substantial payments have been released by M/s Solutions Protocol Sdn. Bhd. in respect of various invoices raised by the appellant on or before 31.12.2006, this is the cut off date mentioned in the deed of settlement. The appellant company categorically denied that it had received payments on or before 31.12.2006, except the amount already received from M/s Solutions Protocol Sdn. Bhd. had been paid over to the respondent. Clause (2) of the deed of settlement states that the parties had agreed that the settlement sum was formulated based on the following proportions of the total amounts of MEDICOM produce license fee and/or all other payments

received by MEDICOM from SP and/or SP/JV by virtue of the HICT Package I Contract. Further, it is stated therein that the settlement sum shall be valid for payments received by MEDICOM from SP and/or SP/JV under the HICT Package I Contract and/or the HIS Software applications modules contracted for the HICT Package I Contract with SP/JV only and it was conclusively agreed to that BITECH shall not in any circumstances whatsoever be entitled in law or otherwise for any payment for any other contracts including contracts involving MEDICOM and Solutions Protocol from the Government of Malaysia or otherwise, whether in Malaysia or any other country. Further, Clause (4) also stipulated that the parties have acknowledged that the obligation of MEDICOM to pay BITECH the settlement sum shall always be subject to MEDICOM (or its representatives or nominees) having received payments of sufficient value from SP and/or SP/JV to enable the payment of upto the maximum amount of the settlement sum to be made on or before 31.12.2006, which is the Cut-off date. Further, it is seen that one of the terms of the compromise was that the respondent would make reasonable efforts to persuade M/s. Solutions Protocol to settle the invoices of the appellant at the earliest.

24. On a detailed analysis of the various terms and conditions incorporated in the deed of settlement as well as the compromise deed and the averments made by the parties, we are of the considered view that there is a *bona fide* dispute with regard to the amount of claim made by the respondent company in the company petition which is substantial in nature. The Company Court while exercising its powers under Sections 433 and 434 of the Companies Act, 1956 would not be in a position to decide who was at fault in not complying with the terms and conditions of the deed of settlement and the compromise deed which calls for detailed investigation of facts and examination of evidence and calls for interpretation of the various terms and conditions of the deed of settlement and the compromise entered into between the parties. A company

A petition cannot be pursued in respect of contingent debt unless the contingency has happened and it has become actually due. In the absence of any evidence, it is not possible to conclude that M/s. Solutions Protocol Sdn. Bhd. had in fact paid any amount to the appellant company towards commission charges due to the respondent company before the cut off date. A legal notice prior to the institution of the company petition could be served on the company only in respect of a debt (then due) and a company could be wound up only if it was unable to pay its debts. In this case, there is a *bona fide* dispute as to whether the amount claimed is presently due and if, at all, it is due, whether the appellant company is liable to pay the sum unless they have received the same from M/s. Solutions Protocol Sdn. Bhd. Where the company has a *bona fide* dispute, the petitioner cannot be regarded as a creditor of the company for the purposes of winding up. “*Bona fide* dispute” implies the existence of a substantial ground for the dispute raised. Where the Company Court is satisfied that a debt upon which a petition is founded is a hotly contested debt and also doubtful, the Company Court should not entertain such a petition. The Company Court is expected to go into the causes of refusal by the company to pay before coming to that conclusion. The Company Court is expected to ascertain that the company’s refusal is supported by a reasonable cause or a *bona fide* dispute in which the dispute can only be adjudicated by a trial in a civil court. In the instant case, the Company Court was very casual in its approach and did not make any endeavour to ascertain as to whether the company sought to be wound up for non-payment of debt has a defence which is substantial in nature and if not adjudicated in a proper forum, would cause serious prejudice to the company.

G **MALICIOUS PROCEEDINGS FOR WINDING UP**

H 25. We may notice, so far as this case is concerned, there has been an attempt by the respondent company to force the payment of a debt which the respondent company knows to be

in substantial dispute. 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 pressurize 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 and even among the public.

PUBLIC POLICY CONSIDERATIONS

26. A creditor's winding up petition, in certain situations, implies insolvency or financial position with other creditors, banking institutions, customers and so on. Publication in the Newspaper of the filing of winding up petition may damage the creditworthiness or financial standing of the company and which may also have other economic and social ramifications. Competitors will be all the more happy and the sale of its products may go down in the market and it may also trigger a series of cross-defaults, and may further push the company into a state of acute insolvency much more than what it was when the petition was filed. The Company Court, at times, has not only to look into the interest of the creditors, but also the interests of public at large.

27. We have referred to the above aspects at some length to impress upon the Company Courts to be more vigilant so

A that its medium would not be misused. A Company Court, therefore, should act with circumspection, care and caution and examine as to whether an attempt is made to pressurize the company to pay a debt which is substantially disputed. A Company Court, therefore, should be guarded from such
B vexatious abuse of the process and cannot function as a Debt Collecting Agency and should not permit a party to unreasonably set the law in motion, especially when the aggrieved party has a remedy elsewhere.

C 28. In the above mentioned facts and circumstances of the case, we are of the view that the order passed by the Company Court ordering publication of advertisement in the newspaper would definitely tarnish the image and reputation of the appellant company resulting in serious civil consequences and, hence, we are inclined to allow this appeal and set aside the order
D passed by the Company Court dated 17.9.2009 in Company Petition 41 of 2009 and the judgment of the Division Bench of the High Court of Karnataka dated 21.10.2009 passed in OSA No. 36 of 2009, and we order accordingly. However, we make it clear that the observations and findings rendered by this Court
E in this proceeding will not prejudice the parties in approaching the appropriate forum for redressal of their grievances and, in the event of which, that forum will decide the case in accordance with law.

D.G.

Appeal allowed.