

NATIONAL COMPANY LAW APPELLATE TRIBUNAL
PRINCIPAL BENCH, NEW DELHI

Company Appeal (AT)(Insolvency) No. 763 of 2023
& IA No.2573 of 2023

[Arising out of order dated 24.03.2023 passed by the Adjudicating Authority, National Company Law Tribunal, Mumbai Court-III, Court-II in CP(IB) No.367 of 2022]

IN THE MATTER OF:

**Manoj Stone Infra Pvt. Ltd.
104, Jai Shankar C.H.S., Opp. Axis Bank,
L.B.S. Marg, Naupada,
Thane (W) – 400602**

...Appellant

Versus

**Railsys Engineers Pvt. Ltd.
503, Trishla Apartment, B-Wing,
Dada Saheb Phalke Road,
Near Ranjeet Studio,
Sant Dadge Maharaj Lane,
Dadar, Mumbai - 400014**

...Respondent

Present:

For Appellant: Advocate Viplav Acharya

For Respondent: Advocate Nakul Mohta and Advocate Riya Mukherjee

J U D G M E N T

[Per: Barun Mitra, Member (Technical)]

The present appeal filed under Section 61 of Insolvency and Bankruptcy Code, 2016 (“**IBC**” in short) by the Appellant arises out of the Order dated 24.03.2023 (hereinafter referred to as “**Impugned Order**”) passed by the Adjudicating Authority (National Company Law Tribunal, Mumbai Court-III) in CP (IB) No. 367 of 2022. By the impugned order, the Adjudicating Authority has dismissed the Section 9 application filed by the Appellant seeking to bring the Corporate Debtor under the rigours of Corporate Insolvency Resolution Process (**‘CIRP’** in short). Aggrieved by this impugned order, the present appeal has been preferred by the Operational Creditor.

2. The Learned Counsel for the Appellant has filed I.A. No 2490/2023 seeking condonation of 8 days delay in refiling the present appeal. Cause shown is sufficient. The IA is allowed and delay in refiling the appeal is condoned.

3. The Learned Counsel for the Appellant submitted that Manoj Stone Infra Pvt. Ltd., the present Appellant/Operational Creditor is a government contractor engaged in manufacturing and selling of aggregates for civil works. The Appellant was approached by Railsys Engineers Pvt. Ltd., the present Respondent/Corporate Debtor for supply of signaling cables and other electronic items for which purpose purchase order was also issued. In pursuance of the purchase order, goods were supplied by the Appellant to the Corporate Debtor for onward supply to RITES Ltd. It is also submitted that since RITES accepted goods only when supplied by RDSO (Research Designs and Standard Organization) approved vendors, the Appellant supplied goods to the Corporate Debtor after

purchasing the same from RDSO approved vendors and hence quality of goods was ensured.

4. The Learned Counsel for the Appellant further submitted that the goods were directly consigned to the site of the Corporate Debtor and two related invoices totaling Rs. 2,57,26,234/- were raised. The said invoices had been acknowledged by the Corporate Debtor with the remarks that material had been received on site along with an endorsement "Proceed for Payment". It has been asserted that the Corporate Debtor had not only acknowledged the receipt of supplies but received them without ever raising any dispute regarding the quality of goods supplied. The Learned Counsel for the Appellant stated that these invoices were sent to the Corporate Debtor on three occasions along with request for payment. However, the Corporate Debtor paid only an amount of Rs.62,85,000/- as part payment and an outstanding amount of Rs.1,94,41,234/- remained due and payable. The Appellant was compelled to finally issue a demand notice on 08.02.2022 under Section 8 of IBC. However, the Corporate Debtor did not reply to the demand notice nor made any further payments in spite of having received the Section 8 notice. The Appellant thereafter filed the Section 9 application before the Adjudicating Authority.

5. The Learned Counsel for the Respondent making his submissions stated that there was no debt to be paid by the Corporate Debtor. Moreover, there was a pre-existing dispute between the parties relating to quality of goods supplied. It was pointed out that in terms of business understanding arrived with the Appellant, payment was to be made by the Corporate Debtor to the Appellant only after they received money from RITES. No money was to be paid to the Appellant

by the Corporate Debtor unless RITES had paid for the material supplied. It was submitted that the goods supplied by the Appellant had not been accepted by RITES since the material supplied was of poor quality and that only part of the supply had been completed. Since there was no provision for part payment in the business transaction between RITES and the Corporate Debtor, RITES refused to release payment to the Corporate Debtor as entire supply had not taken place. The Appellant was, therefore, not entitled to any payment as the Corporate Debtor had not received corresponding payment from RITES. It has also been the contention of the Corporate Debtor that the transaction carried out between the Appellant and the Corporate Debtor was in the nature of profit-sharing arrangement and not an operational debt.

6. We have duly considered the arguments advanced by the Learned Counsel for both the parties and perused the records carefully. The moot point for consideration is whether in the facts of the present case, there was an operational debt which was due and payable and whether there was a genuine and real pre-existing dispute in existence between the two parties.

7. We notice that the Adjudicating Authority has dwelled upon both the facts as to whether the debt claimed by the Appellant was in the nature of operational debt and whether there were pre-existing disputes between the parties.

8. On the issue of operational debt, it is the contention of the Respondent that the Appellant in their email dated 12.12.2021 addressed to the Respondent has adverted attention about talks with Mr. Sanjay Singh, the deceased Director of Respondent regarding their inter-se business dealings to supply electric equipment to Railways. In the said email, the Appellant had proposed equal

investment and equal sharing of profit and loss and that amount were not payable invoice-wise but only profits, if any, were to be shared. Calling their business relationship a profit-sharing arrangement, it is the contention of Corporate Debtor that the Appellant cannot term these transactions as operational debt. Further, the Appellant having acknowledged multiple transactions and businesses between parties, two invoices in isolation cannot form the basis of Section 9 Application disregarding other business transactions.

9. We have perused the impugned order and note that the Adjudicating Authority having considered at length the contentions of both the sides have relied on an email dated 12.12.2021 sent by the Appellant to the Corporate Debtor to come to the conclusion that there is a partnership business dealing between the parties in which supply of material by Corporate Debtor was one of the many transactions and compliances. It has therefore held at paragraph 7 of the impugned order that since the claim of the Appellant is arising out of a mutual business understanding of partnership business, the debt claimed by the Operational Creditor does not fall within the definition of operational debt.

10. For better appreciation of this issue, at the outset we may take notice of the relevant statutory provisions of IBC in the context of operational debt. Operational Creditor is defined in Section 5(20) while Operational Debt is defined in Section 5(21) as outlined below which is to the effect:

Section 5 (20) - "operational creditor" means a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred.

Section 5 (21) - "operational debt" means a claim in respect of the provision of goods or services including employment or a debt in respect of the repayment of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority.

11. From a plain reading of the above provisions, it is clear that the primary and operative requirement of Section 5(21) is that the claim must bear some nexus with a provision of goods or services irrespective of who is to be the supplier or receiver. The expression "operational debt" has been defined by Code and it must fulfil following substantive elements, namely: debt arising out of provisions of goods or services or out of employment or dues payable to Central Government, any State Government or any local authority. Further the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 under Rule 5(1) provides that any operational creditor can issue a notice in relation to an operational debt either through a demand notice or copy of invoices. Also, an operational creditor who is seeking to claim an operational debt in a CIRP can rely either on a contract or on an invoice for the supply of goods and services with the corporate debtor under Regulation 7(2)(b)(i) and (ii) of the Insolvency and Bankruptcy Board of India (Insolvency Resolution Process for Corporate Persons) Regulations 2016. Thus, all forms of contracts for the supply of goods or services between the operational creditor and the corporate debtor are included in this.

12. The Section 8 Demand Notice and Section 9 application in the present case are based on invoices dated 21.03.2021 and 27.03.2021 which have been placed on record at pages 76-77 of Appeal Paper Book ("**APB**" in short). The invoices have

been raised for supply of railway equipment by the Appellant to the Respondent for supplying to RITES. The purchase orders dated 02.03.2021 have also been placed on record at pages 64-67 of APB. Given the above factual matrix, it is an undisputed fact that the Appellant has submitted two invoices demanding payment for the goods and services supplied to the Corporate Debtor to prove the existence of the debt. At this stage we do not wish to enter into the contention of the Respondent/Corporate Debtor disputing the amount contained in the invoices or that the invoices flow from and are part of a larger transaction. All that we wish to take cognizance of, for the present, is whether the Appellant/Operational Creditor fulfilled the requirements of Rule 5(1) of the Insolvency and Bankruptcy (Application to Adjudicating Authority) Rules, 2016 or not. We clearly find that the Appellant having attached invoices claiming payment of goods supplied by them while furnishing the demand notice has conformed to the requirements of Form 3 appended with the aforesaid Rules to establish their operational claims. There is no denial by the Respondent either in respect of purchase order issued by them or the receipt of demand notice along with requisite invoices from the Operational Creditor. The operative and primary requirements of Section 5(21) having been met, we are therefore not convinced by the narrow and hyper-technical view taken by the Adjudicating Authority in not treating the above claim arising out of supply of goods as operational debt on the ground that the canvas of business dealing between the parties covers more than mere stand-alone transaction of supply of materials. It is also quizzical that the Adjudicating Authority on the one hand has held the transaction not to be an operational debt and on the other hand concurrently gone ahead to record its findings on the issue of pre-existing disputes surrounding the said debt.

13. Now that we have arrived at the finding that the present set of transactions does fall within the scope and definition of operational debt, it would be in order to analyse whether Section 9 proceeding under IBC can be initiated at the instance of the Operational Creditor in the light of the issue of pre-existing disputes raised by the Corporate Debtor.

14. It is the contention of the Respondent/Corporate Debtor that prior to the Demand Notice, the Respondent had already disputed the above two invoices in their email dated 24.12.2021 as raised the need to determine the real intention of the parties and the real business agreement between them. It is also contended that the Corporate Debtor had made timely payments to the Appellant but the latter having failed to discharge the obligations on their part in failing to meet the quality standards of the goods is not entitled to get any further payment. Moreover, as per business understanding, payment was to be released to the Operational Creditor only after payment was released by RITES to the Corporate Debtor. However, since RITES had withheld payment over quality issues as well as incomplete supply hence the Appellant was not entitled for payment.

15. We notice that the Adjudicating Authority has carefully considered the relevant correspondence exchanged between both the parties with respect to their business relations and attendant transactions. The email from the Operational Creditor dated 12.12.2021 seeking payments has been reproduced at Para 5 of the impugned order in its entirety. Attention has also been adverted to the relevant paragraphs of the reply email thereto as sent by the Corporate Debtor on 24.12.2021 in which the invoices of the Operational Creditor have been disputed.

The relevant excerpts from the stated paragraph have been extracted at Para 8 of the impugned order which reads as follows:

“... Yes. Your This Invoice Itself is Marked Red by Our Auditor that (17611877 + 4436592 = 22048469/-) - The Actual Invoice amount is Raised as (19840834 + 5885660 = 25726294/-) is the Diff. of INR 36,77,825/- (There is No Funny Understanding as Mentioned Above that We Give You The Business and Turnover also and Share Profits Too with You - No Company Does This). Secondly. To Your Info and Records: Rs. 44,36,592/- Invoice has Not Been Accepted Even from Our Side by Railways and The Material Supplied to Them is as Good as Scrap and Was Needed Not Now. Another Interesting Thing You Forgot to Mention That REPL has Paid You 75.85 Lac. Till date Plus Many of Your EMIs to Help you out.”

16. A cursory reading of the above extracts clearly shows that the Corporate Debtor has not only disputed the invoices but also suggested that transaction between Appellant and Respondent cannot be closed merely by considering the two invoices but all the items have to be considered when accounts were required to be settled. From the tone and tenor of the said reply, we have no hesitation in recording our view that ingredients of dispute between the two parties are reasonably etched out therein. More significantly, as pointed out in the impugned order, this correspondence encapsulating ongoing disputes between the two parties predates the Demand Notice of 08.02.2022. It can thus be safely concluded that the disputes were pre-existing in nature.

17. Also, reference has been made at para 8 of the impugned order to a letter issued by RITES dated 17.02.2022. We notice that the Respondent in their email

dated 24.12.2021 had stated that the Railways had disputed the payments on grounds of quality. This dispute is indeed corroborated in the abovementioned letter dated 17.02.2022 issued by RITES. The letter clearly states that as certain vital parts of the Electronic Interlocking Systems had yet not been supplied and since there is no therefore provision for part-payment, RITES had intimated the Corporate Debtor that piece-meal bills cannot be processed. The Adjudicating Authority has inferred therefrom that there is a pre-existing dispute with regard to quality of material supplied by the Operational Creditor. We find no reasons to disagree with the findings of the Adjudicating Authority on this count. Having perused these communications, we are convinced that there were genuine pre-existing disputes between the parties which is more than a moonshine defence.

18. We have seen the impugned order and note that the Adjudicating Authority having considered at length the contentions of both the sides held that dispute was brought to the notice of the Operational Creditor prior to the issuance of the demand notice. In the present factual matrix, the defence raised by the Corporate Debtor therefore cannot be held to be moonshine, spurious, hypothetical or illusory. The Adjudicating Authority in abiding by the touch-stone laid down in terms of the judgement of the Hon'ble Supreme Court in **(2018) 1SCC 353 Mobilox Innovations Pvt Ltd vs Kirusa Software Pvt Ltd** has therefore not committed any error in holding that for such disputed operational debt, Section 9 proceeding under IBC cannot be initiated at the instance of the Operational Creditor.

19. For the foregoing reasons, we are of the view that the Adjudicating Authority has rightly dismissed the application of the Appellant filed under Section 9 of IBC.

We however make it clear that in the event the Appellant seeks remedy before any other appropriate forum, it shall be open for the Appellant to raise all pleas as permissible in law. There is no merit in the Appeal. The Appeal is dismissed. No order as to costs.

[Justice Ashok Bhushan]
Chairperson

[Barun Mitra]
Member (Technical)

Place: New Delhi

Date: 11.07.2023

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