DECIPHERING "DISPUTE"

Mobilox Innovations Pvt. Ltd. v. Kirusa Software Pvt. Ltd.

- ***Richa Saraf***

Editor's Note: *A default in repaying debt is the fundamental requirement for initiating process under IBC.However, a debt, which itself is 'disputed', cannot form the basis of the process. In case of operational creditors, it is mandated that the operational creditor serves a demand notice to the corporate debtor. In response, the corporate debtor may either 'pay' the debt, or 'dispute' the debt. However, the dispute must be something which was 'pre-existing' – that is, the corporate debtor is not entitled to raise frivolous disputes only on receiving the demand notice. Where there exists a dispute, the operational creditor is not entitled to initiate application for corporate insolvency resolution process under IBC.*

There had been a lot of 'dispute' around the word 'dispute' – different benches of NCLTs interpreted the word differently – strictly or liberally. The debate was finally settled by the Apex Court in one of its landmark rulings, Mobilox Innovations Pvt. Ltd. v. Kirusa Software Pvt. Ltd. *The article, originally written in 2017, gives a threadbare analysis of the judgment and delves into the definition of 'dispute'.*

The Supreme Court of India has provided a much required clarity on the provisions of IBC vis-à-vis the existence of dispute. In this article, we broadly discuss the various issues that were dealt with in the judgment.

Brief facts of the case

Mobilox Innovations Pvt. Ltd. (hereinafter referred to as "Appellant" or "Corporate Debtor") was engaged by Star TV for conducting tele-voting for the "Nach Baliye" program on Star TV, who in turn subcontracted the work to the Kirusa Software Pvt. Ltd. (Respondent). A Non-Disclosure Agreement (NDA) was also executed between the parties in this regard.

The Respondent provided the requisite services and raised monthly invoices, which were payable within 30 (Thirty) days of receipt of the invoice. After several follow- ups, the Appellant wrote to the Respondent that the payments are being withhold on account of breach of NDA.

Finally, a demand notice was sent under Section 8 of IBC, to which the Appellant asserted that there exists serious and bona fide disputes between the parties, the notice issued was a pressure tactic and nothing was payable inasmuch as the Respondent had been told way back.

The Respondents then filed an application before the NCLT which was dismissed. Next, an appeal was filed before the National NCLAT, wherein it was held that the Hon'ble NCLT had acted mechanically by rejecting the application, without examining and discussing the issue in context and the case was remitted to AA. It was further held that the Corporate Debtor has failed to fulfil the condition stipulated in Section 8(2) IBC and thus the defence claiming dispute was vague and motivated to evade its liability. Thereafter, the matter came up for final determination by the Apex Court

Question of Admissibility of an Insolvency Application

The Hon'ble Supreme Court has laid down directions to the AA, wherein the NCLT will be required to determine certain questions, while examining the admissibility of an application under Section 9 IBC. The same are as follows-

(i) Whether there is an "operational debt" exceeding Rs.1 lakh and as defined in IBC?

(ii) Whether the documentary evidence furnished with the application shows that the aforesaid debt is due and payable and has not yet been paid?

(iii) Whether there is existence of a dispute between the parties or the record of the pendency of a suit or arbitration proceeding filed before the receipt of the demand notice of the unpaid operational debt in relation to such dispute?

It was held- "*If any one of the aforesaid conditions is lacking, the application would have to be rejected.*"

"And" or "Or"-

Samee Khan v. Bindu Khan

*"**The word 'and' need not necessarily be understood as denoting a conjunctive sense.** In Stroud's Judicial Dictionary, it is stated that the word 'and' has generally a cumulative sense, but sometimes it is by force of a context read as 'or'.*

Apart from the above, the Adjudicating Authority should consider the factors mentioned in IBC while deciding the admissibility of a case, i.e. the Adjudicating Authority **must follow** the mandate of Section 9 of IBC, more particularly Section 9(5), and only then admit or reject the application.

Conflict between "And" and "Or" resolved

Section 8(2)(a) of IBC provides that the corporate debtor shall, within a period of 10 (Ten) days of the receipt of the demand notice or copy of the invoice bring to the notice of the operational creditor- existence of a dispute, if any, **and** record of the pendency of the suit or arbitration proceedings filed before the receipt of such notice or invoice in relation to such dispute.

The Hon'ble Supreme Court noted that in the Insolvency and Bankruptcy Bill, 2015, only '**existence of dispute**' was mentioned. Elaborating on the intent here, it held-

> *"29. ** Even otherwise, the word **'and'occurring in Section 8(2)(a) must be read as 'or'** keeping in mind the legislative intent and the fact that an anomalous situation would arise if it is not read as 'or'. If read as 'and', disputes would only stave off the bankruptcy process if they are already pending in a suit or arbitration proceedings and not otherwise. This would lead to great hardship; in that a dispute may arise a few days before triggering of the insolvency process, in which case, though a dispute may exist, there is no time to approach either an arbitral tribunal or a court. Further, given the fact that long limitation periods are allowed, where disputes may arise and do not reach an arbitral tribunal or a court for upto three years, such persons would be outside the purview of Section 8(2) leading to bankruptcy proceedings commencing against them. Such an anomaly cannot possibly have been intended by the legislature nor has it so been intended. We have also seen that one of*

> *the objects of the Code qua operational debts is to ensure that the amount of such debts, which is usually smaller than that of financial debts, does not enable operational creditors to put the corporate debtor into the insolvency resolution process prematurely or initiate the process for extraneous considerations. It is for this reason that it is enough that a dispute exists between the parties.*

It is settled law that the expression 'and' may be read as 'or' in order to further the object of the statute and/or to avoid an anomalous situation. In this regard, it is quintessential to cite the case of*Samee Khan v. Bindu Khan*[5], it was held-

> *"**The word 'and' need not necessarily be understood as denoting a conjunctive sense.** In Stroud's Judicial Dictionary, it is stated that the word 'and' has generally a cumulative sense, but sometimes it is by force of a context read as 'or'. Maxwell on Interpretation of Statutes has recognised the above use to carry out the interpretation of the legislature. This has been approved by this Court in* Ishwar Singh Bindra v. State of U.P. [AIR 1968 SC 1450: 1969 Cri LJ 19]*."*

The Hon'ble Supreme Court, agreeing with the aforesaid view, also referred to the case of *Maharishi Mahesh Yogi Vedic Vishwavidyalaya v. State of M.P.*[6] and *Director of Mines Safety v. Tandur and Nayandgi Stone Quarries (P) Ltd.*[7].

A probe into the intricacies of Existence of Dispute

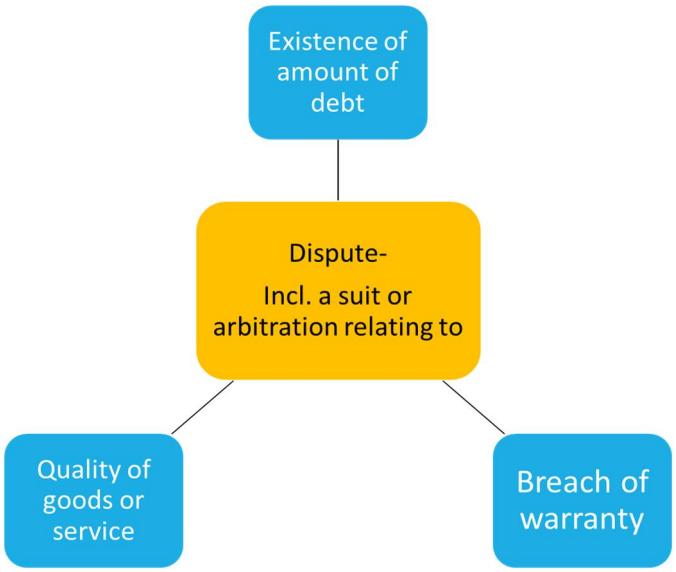

Figure 6: Elements of "Dispute"

It is pertinent to note that '**dispute**' as envisaged by BLRC and as postulated in the Bill meant "**bona fide suit or arbitration proceedings**", contrary to the present version of 'dispute', as retained in Section 5(6) of IBC, which excludes the expression 'bona fide'. The Hon'ble Supreme Court was pleased to construe the purport behind such exclusion and held-

> *"It is difficult to import the expression "bona fide" into Section 8(2)(a) in order to judge whether a dispute exists or not."*

Section 5(6) of IBC which defines the term '**dispute**' is reproduced herein below-

> *"dispute **includes** a suit or arbitration proceedings relating to-*
>
> *(a) the existence of the amount of debt;*
> *(b) the quality of goods or service; or*
> *(c) the breach of a representation or warranty."*

[5](1998) 7 SCC 59
[6](2013) 15 SCC 677
[7] [(1987) 3 SCC 208]

Earlier, in the present case, while interpreting the term 'dispute', the Hon'ble NCLAT pointed out that the intent of the Legislature, as evident from the definition of the term 'dispute', is that it wanted the same to be illustrative and not exhaustive. If the intent was to define 'dispute' as only a suit or arbitration proceedings then the word '**include**' would not have been used, it would have simply said 'dispute **means** a suit or arbitration proceedings'. Agreeing with the aforesaid view, the Hon'ble Supreme Court also held-

> *"First and foremost, the definition is an inclusive one, and we have seen that the word 'includes' substituted the word 'means' which occurred in the first Insolvency and Bankruptcy Bill. Secondly, the present is not a case of a suit or arbitration proceeding filed before receipt of notice – Section 5(6) only deals with suits or arbitration proceedings which must 'relate to' one of the three sub- clauses, either directly or indirectly. We have seen that a 'dispute' is said to exist, so long as there is a real dispute as to payment between the parties that would fall within the inclusive definition contained in Section 5(6)."*

Further, the Hon'ble Supreme Court accepted the dictionary meaning of the term '**existence**' and also went on to discuss the judgments of the Australian and UK Courts for the purpose of determining the dispute. The Oxford English Dictionary stipulates the meaning of the word '**existence**' viz., a) reality, as opposed to appearance; b)the fact or state of existing; actual possession of being. Continued being as a living creature, life, especially under adverse conditions; Something that exists; an entity, a being. All that exists.

Further, a **'genuine'** dispute requires that:

- the dispute be bona fide and truly exist in fact;
- the grounds for alleging the existence of a dispute are real and not spurious, hypothetical, illusory or misconceived.

The Australian High Courtin *Spencer Constructions Pty Ltd. v. G & M Aldridge Pty Ltd.*[8]while construing the term 'genuine dispute', relied on *Eyota Pty Ltd. v. Hanave Pty Ltd.*[9]**,** where his Honour said-

> *"In my opinion [the] expression connotes a plausible contention requiring investigation, and raises much the same sort of considerations as the 'serious question to be tried' criterion which arises on an application for an interlocutory injunction or for the extension or removal of a caveat. This does not mean that the court must accept uncritically as giving rise to a genuine dispute, every statement in an affidavit 'however equivocal, lacking in precision, inconsistent with undisputed contemporary documents or other statements by the same deponent, or inherently and probable in itself, it may be not having 'sufficient prima facie plausibility to merit further investigation as to [its] truth'* (cf Eng Mee Yong v. Letchumanan [1980] AC 331 at 341)*, or 'a patently feeble legal argument or an assertion of facts unsupported by evidence':* cf South Australia v. Wall (1980) 24 SASR 189 at 194.*"*

[8] [1997] FCA 681
[9] (1994) 12 ACSR 785

Deciphering Dispute

It is not expected that the court will embark upon any extended enquiry in order to determine whether there is a genuine dispute between the parties and certainly will not attempt to weigh the merits of that dispute. All that the legislation requires is that the court concludes that there is a dispute and that it is a genuine dispute[10]. It is clear that what is required in all cases is something between mere assertion and the proof that would be necessary in a court of law. Something more than mere assertion is required because if that were not so then anyone could merely say it did not owe a debt.[11]

In the case of *Re Morris Catering (Australia) Pty Ltd.*[12], it was held-

> *"That is not to say that the court will examine the merits or settle the dispute. The specified limits of the court's examination are the ascertainment of whether there is a 'genuine dispute' and whether there is a 'genuine claim'.*
>
> *It is often possible to discern the spurious, and to identify mere bluster or assertion. But beyond a perception of genuineness (or the lack of it) the court has no function. It is not helpful to perceive that one party is more likely than the other to succeed, or that the eventual state of the account between the parties is more likely to be one result than another.*
>
> *The essential task is relatively simple- to identify the genuine level of a claim (not the likely result of it) and to identify the genuine level of an offsetting claim (not the likely result of it)."*

Chadwick Industries v. Condensing Vaporisers

The notion of a 'genuine dispute' in this context suggests to me that the court must be satisfied that there is a dispute that is not plainly vexatious or frivolous. It must be satisfied that there is a claim that may have some substance.

In *Chadwick Industries (South Coast) Pty Ltd. v. Condensing Vaporisers Pty Ltd.*[13], it was held-

> *"Certainly the court will not examine the merits of the dispute other than to see if there is in fact a genuine dispute. The notion of a 'genuine dispute' in this context suggests to me that the court must be satisfied that there is a dispute that is not plainly vexatious or frivolous. It must be satisfied that there is a claim that may have some substance".*

In *Greenwood Manor Pty Ltd. v. Woodlock*[14]the formulations in*Re Morris Catering (Australia) Pty Ltd.*[15] and *Mibor Investments Pty Ltd. v. Commonwealth Bank of Australia*[16] where referred to,wherein the dictionary definition of 'genuine' as being in this context 'not spurious- real or true' was noted and the following was concluded:

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[10] See *Mibor Investments Pty Ltd v Commonwealth Bank of Australia (1993) 11 ACSR 362*; *Moyall Investments Services Pty Ltd v White (1993) 12 ACSR 320.*

[11] See *John Holland Construction and Engineering Pty Ltd v Kilpatrick Green Pty Ltd (1994) 12 ACLC 716*; *Aquatown Pty Ltd v Holder Stroud Pty Ltd (Federal Court of Australia, 25 June 1996, unreported)*.

[12](1993) 11 ACSR 601

[13](1994) 13 ACSR 37

[14](1994) 48 FCR 229

[15](1993) 11 ACLC 919

[16][1994] 2 VR 290

> *"Although it is true that the Court, on an application under ss 459G and 459H is not entitled to decide a question as to whether a claim will succeed or not, it must be satisfied that there is a genuine dispute between the company and the respondent about the existence of the debt. If it can be shown that the argument in support of the existence of a genuine dispute can have no possible basis whatsoever, in my view, it cannot be said that there is a genuine dispute. This does not involve, in itself, a determination of whether the claim will succeed or not, but it does go to the reality of the dispute, to show that it is real or true and not merely spurious".*

TheChancery Division in*Hayes v. Hayes*[17]under the U.K. Insolvency Rules held-

> *"I do not think it necessary, for the purposes of this appeal, to embark on a survey of the authorities as to precisely what is involved in a genuine and substantial cross-claim. It is clear that on the one hand, the court does not need to be satisfied that there is a good claim or even that it is a claim which is prima facie likely to succeed.*
>
> *On the other hand, the court should be alert to detect wholly spurious claims merely being put forward by an unwilling debtor to raise what has been called 'a cloud of objections' as I referred to earlier."*

Similar view was upheld by the Hon'ble Supreme Court in the instant case-

> *"40. It is clear, therefore, that once the operational creditor has filed an application, which is otherwise complete, the adjudicating authority must reject the application under Section 9(5)(2)(d) if notice of dispute has been received by the operational creditor or there is a record of dispute in the information utility. It is clear that such notice must bring to the notice of the operational creditor the "existence" of a dispute or the fact that a suit or arbitration proceeding relating to a dispute is pending between the parties. Therefore, all that the adjudicating authority is to see at this stage is whether there is a plausible contention which requires further investigation and that the "dispute" is not a patently feeble legal argument or an assertion of fact unsupported by evidence. It is important to separate the grain from the chaff and to reject a spurious defence which is mere bluster. However, in doing so, the Court does not need to be satisfied that the defence is likely to succeed. The Court does not at this stage examine the merits of the dispute except to the extent indicated above. So long as a dispute truly exists in fact and is not spurious, hypothetical or illusory, the adjudicating authority has to reject the application."*

It is relevant to note here, that a confirmation from a financial institution that there is no payment of an unpaid operational debt by the corporate debtor is an important piece of information that needs to be placed before the adjudicating authority.

Concluding Remarks

The judgment in *Mobilox Innovations Pvt. Ltd. v. Kirusa Software Pvt. Ltd* is substantially significant as by providing such a liberal construction of the term 'dispute', the Apex Court has provided an end to all the doubts and clarified the scope of dispute, contradictory to the judgment in *Essar*

[17](2014) EWHC 2694 (Ch)

ProjectsIndia Ltd. v. MCL Global Steel Pvt. Ltd.[18], wherein the Mumbai NCLT, while interpreting the definition of dispute under IBC, held that dispute in existence means only when the same is raised before a court or an arbitral tribunal prior to the date of receipt of a demand notice and in several other cases, where a very rigid view was taken.

Know more . . .

The Insolvency and Bankruptcy Code (Second Amendment) Act, 2018 was later enacted, and eliminated the confusion of "and" and "or". Section 8 was amended to replace "and" by "or".

The ruling in *Mobilox* was cited in another landmark ruling of the Supreme Court, namely, *K. Kishan v. Vijay Nirman Company Pvt. Ltd.* wherein the Apex Court, in the context of arbitration proceedings, held that a challenge to an arbitral award under section 34 of the Arbitration Act shows a pre-existing dispute and continues '*at least till the final adjudicatory process under Sections 34 & 37 has taken place*." As such, a debt which is under challenge in arbitral proceedings would be a disputed debt.

The idea behind creating this bar for operational creditors was thus stated in the above case –"*that operational creditors cannot use the Insolvency Code either prematurely or for extraneous considerations or as a substitute for debt enforcement procedures*".

Notably, there is no provision pertaining to dispute in case of financial debts. BLRC opined that the chances of dispute in operational debts are much higher than those in financial debts. However, it does not imply that financial debts cannot be disputed. As is known, existence of 'default' is *sine qua non* for initiation of corporate insolvency resolution process. If prior to admission of application by the adjudicating authority, the corporate debtor can show that no default exists, *in the sense that a debt, which may also include a disputed claim, is not due i.e. it is not payable in law or in fact,* then also application by the financial creditor would not be maintainable. See the ruling in *Mobilox*.

[18] 2017 (4) TMI 1156