BEFORE THE NATIONAL COMPANY LAW TRIBUNAL
BENGALURU BENCH

COMPANY PETITION No. 10/2017

DATED: SUNDAY THE 19TH DAY OF FEBRUARY 2017

IN THE MATTER OF THE COMPANIES ACT, 1956
UNDER SECTIONS 433 AND 434
AND SECTIONS 327 READ WITH 326 OF THE
COMPANIES ACT, 2013
AND

IN THE MATTER OF STALWART ONLINE STORES PVT. LTD.

1. Global Office Suppliers Pvt. Ltd., Bengaluru……..Petitioner 1
2. Shareholders of Stalwart Online Stores Pvt. Ltd……..…Petitioner 2
3. Additional Commissioner of Income-tax, Bengaluru……...Petitioner 3
4. Deputy Commissioner of Commercial Tax, Bengaluru……..Petitioner 4

Versus

5. Stalwart Online Stores Pvt. Ltd., Bengaluru……Respondent

ORDER

1. These Petitions have been filed on behalf of Petitioners under Section 280 r/w Section 271 of the Companies Act, 2013. The Tribunal has been granted jurisdiction to hear such Petitions by virtue of the Notification released by the Ministry of Corporate Affairs bearing S.O. 3677(E), dated 7th December, 2016.
2. The averments in the Petitions are briefly described hereunder:-
   a. The Petitioner 1 filed the winding up Petition against the Respondent after serving a legal notice on the Respondent on December 31, 2016 to have failed to pay debts totaling to INR 13.92 crores. The Petition was filed after the expiry of the statutory period u/s 434 of the Companies Act, 1956.

b. The Respondent challenged the validity of the statutory notice stating the cause for non-payment of the pending amount to be due to deficiency of services by Petitioner 1 to Respondent's customers under its marketplace model further challenging the appropriation of payments to be bad in law. The Respondent has challenged the jurisdiction of this Tribunal to hear this Petition in view of an arbitration clause in the agreement between the parties and the recovery proceedings instituted by the Petitioner 1.

c. The Petitioner 2 filed the winding up Petition against the Respondent for the acts of oppression, mismanagement and siphoning of funds by its board of directors. They alleged the directors to have conducted a related party transaction and the loan advancement to be prohibited and against the spirit of the Companies Act, 2013.

d. The Respondent has challenged this Petition on the ground of *forum non conveniens* and also on merits, stating that the loan advancement was not prohibited by law. They further argued that the acts of the directors were not oppressive as they acted in accordance with the provisions of the Companies Act.

e. The Petitioner 3 and Petitioner 4 filed impleading petitions stating they have sizeable tax claims. The Income-tax Department levied tax on the loan advanced by Stalwart to Galileo as deemed dividend under the Income-tax Act ("IT Act"). The Sales Tax Department levied VAT and CST on the Respondent for not registering itself as a dealer with the Karnataka Sales Tax Department. ("KVAT Act")

3. The following issues have been considered by the Tribunal:-

I. Whether the Petition filed by Petitioner 1 is maintainable and whether their existed a *bonafide* dispute between the parties?

II. Whether the Petition filed by Petitioner 2 is maintainable and whether their existed just and equitable grounds to wind up the company?

III. Whether the loan advanced by the Respondent Company is a deemed dividend under the IT Act?

IV. Whether the Respondent should have registered itself as a dealer under the KVAT Act?

4. We have heard the learned Counsel for Petitioner 1 and also the learned Counsel for the Respondent. The contention of the learned Counsel for Petitioner 1 is that the recovery suit filed before the Civil Court will not affect the maintainability of the present petition as the suit for enforcing recovery and a petition seeking winding up being independent, are neither substitutes nor alternatives to each other. He referred to the judgment in the case of *Madhya Pradesh Iron and Steel Co. v. G.B. Springs Pvt. Ltd.,* (2003) 54 CLA 9 (Delhi). He argued that the legislature allows simultaneous existence of the two. Citing the judgment of the Apex Court in the case of *Haryana Telecom Ltd. v. Sterlite Industries (India) Ltd.,* A.I.R 1999 (SC) 2354 he argued that an arbitrator has no jurisdiction to entertain any winding up matter of a company. The Counsel further submitted that the arbitration clause can be invoked only when there exists a *bonafide* dispute.

5. The Counsel for Petitioner 1 submitted that the Sales-cum-Service agreement entered into between the parties was a single instrument embodying two separate contracts with distinct sets of reciprocal promises, one under the inventory model and the other under the marketplace model. He further argued that the two contracts being separate, non-performance of one will not affect the performance of the other. Therefore, the deficiency under the marketplace model will not affect the payments under the inventory model eliminating any scope of dispute.

6. He submitted that as the debtor while making the six intermittent payments failed on providing the creditor with any instructions whatsoever, the right to appropriate devolved on the creditor by virtue of Section 60 of the Indian Contract Act, 1872. The appropriation of payments, the Counsel argued was therefore good in law.

7. The Counsel citing the judgment of the Apex Court in the case of *Madhusudan Gordhandas and Co. v. Madhu Wollen Industries Pvt. Ltd.*, A.I.R. 1971 SC 2600 submitted in *arguendo*

that even if the exact amount of debt was under dispute, but as the Respondent has accepted its liability, the Respondent Company is liable to be wound up.

8. The last submission of the Counsel for Petitioner 1 was that the Respondent Company was unable to pay its debts. He submitted taking aid of the judgment in the case of *Life Insurance Corporation of India v. Gadadhar De,* A.I.R. 1978 Cal. 419, that where all the cheques were being dishonored, an inference is drawn that the company was unable to pay its debts. He argued that clause (a) of sub-section (1) of Section 434 of the Companies Act, 1956 gives a statutory right to the creditor to have the company wound up, in cases of non-payment of debts after the service of the legal notice, even if the company is solvent.
9. The Counsel for the Respondent on the other hand vehemently argued against the maintainability of the present petition. He submitted that the Petitioner 1 having already filed a civil suit for recovering the same debt for which the winding up petition has been filed, it is not proper and legitimate for Petitioner 1 to seek admission of the present Petition. The Counsel took aid of the judgment of the Apex Court in the case of *Hind Overseas Pvt. Ltd. v. Raghunath Prasad Jhunjhunwala,* (1976) 2 SCR 226.
10. He further argued the existence of a *bonafide* dispute and submitted, calling reference to the judgment in the case of *Lloyds Metals and Engineering Ltd. v. Neelachal Ispat Nigam Ltd.*, (2010) 155 Comp Cases 600, that with the availability of an arbitration clause in the agreement between the parties, the proper remedy would be for the parties to refer to arbitration.
11. The Counsel for the Respondent further submitted that the Sales-cum-Service agreement entered into between the parties was an entire and an indivisible contract. He submitted that the performance of the contract under the inventory model was made incidental to the performance under the marketplace model. Therefore, the deficiency and delay of services by Petitioner 1 under the marketplace model which led to the Respondent's decline in profits laid grounds for a *bonafide* dispute. He further submitted that by virtue of Clayton's rule, in

cases of current account, the right of appropriation never devolves on the creditor and the appropriation has to be first towards the principal amount and that too in the order of the debt. He relied on the judgments in the cases of *Cory Bros & Co. Ltd. v. Owners of Turkish Steamship (Mecca)*, (1897) AC 286 and *Sarab Dial v. Nanda Mal Wazir Chand*, A.I.R. 1936 Pesh 143.

12. The Counsel for the Respondent also took the plea of the Respondent being a growth oriented company and submitted that it is commercially solvent. He submitted citing the case of *Reliance Infocomm Ltd. v. Sheetal Refineries Pvt. Ltd*., (2008) 142 Comp Cases 170, that the court will never wind up a company if it is commercially solvent.
13. The Counsel for Petitioner 2 argued that winding up petitions are maintainable on the grounds of oppression, mismanagement and siphoning of funds. The Counsel submitted that it was just and equitable to have the Respondent Company wound up as the Respondent has conducted a related party transaction without seeking shareholders' approval.
14. The counsel argued that the Respondent and Galileo, its private equity investor, being related parties had by virtue of Section 188(1)(d) of the Companies Act, 2013 entered into a related party transaction. By virtue of the 2nd proviso to the said Section r/w Rule 15(3) of the Companies (Meeting of Board and its Powers) Rules, 2004, prior approval of shareholders was mandatory.
15. The Counsel for Petitioner 2 lastly submitted that such a transaction is strictly prohibited by the RBI. Such loan advancements by an Indian entity are permitted only to an overseas JV/WOS in which the entity has some equity participation. The remittance of such a loan nonetheless was only possible by way of misrepresenting before the banks, making a clear case of siphoning of funds.
16. The Counsel for the Respondent on the other hand vehemently opposed the maintainability of this impleading Petition as Petitioner 2 had an alternative remedy by virtue of Section 241 of the Companies Act, 2013 to complain of oppression and mismanagement. The Petitioner 2

having not exhausted all the alternate remedies cannot seek winding up of the Respondent Company. Reference was made to the case of *K. Mohan Babu v. Heritage Foods India Ltd.*, (2002) 108 Comp Cases 793.

17. The Counsel further submitted that the meaning of the term person u/s 2(76)(vii) of the Companies Act, 2013 has to be harmoniously read with Sections 161 and 149 of the said Act, thereby showing it to mean an individual. Galileo therefore is not a related party to the Respondent. The question of a related party transaction being conducted cannot arise.
18. The Counsel made his submissions that the said loan advancement will never require shareholders approval, as the threshold provided under Section 186(2) is far from the amount of the loan. He argued that the notice was not served on Petitioner 2 because the Respondent was not mandated to do so. The power to sanction such a loan advancement has been granted to the board of directors by virtue of Section 186 of the Companies Act, 2013. The directors when acting in accordance with law cannot be said to be oppressing the shareholders.
19. After having considered the arguments of both the sides, we conclude that the Petitions filed by Petitioner 1 and Petitioner 2 are not maintainable taking aid of the judgment of the Apex Court in the case of Amalgamated Commercial Traders (supra), as the bench believes in the existence of a *bonafide* dispute between the parties. We disagree with the Counsel for Petitioner 1 and hold keeping in mind the intention of the parties, that the SSA was an entire and an indivisible contract thereby making the deficiency under the marketplace model to affect the payments under the inventory model. The Petitioner 1 has also failed to establish any commercial insolvency or inability to pay on the part of the Respondent Company.
20. The bench also has failed to understand the reason why Petitioner 2 did not approach this Tribunal under Section 241 of the Companies Act, 2013 which has been incorporated solely to address cases relating to oppression and mismanagement. We are in agreement with the Counsel for Respondents when they say that Galileo is not a related party to the Respondent Company and that the alleged transaction was not a related party transaction but merely a

loan advancement permissible u/s 186 of the Companies Act, 2013. Having said that, the bench finds no reason whatsoever why shareholders approval should be required, thereby eliminating all questions of oppression.

21. We have heard the learned Additional Advocate General of Karnataka ("AAG") for Petitioner 3 and also the learned Counsel for the Respondent. The AAG contended that the loan advanced by Stalwart to Galileo is a deemed dividend under Section 2(22)(e) of the IT Act. He argued that Stalwart possessed accumulated profits at the time of this loan advancement. In order to substantiate the same, he inferred that Stalwart could not have advanced a loan of Rs. 50 crores considering it had insufficient funds to pay Petitioner 1 and made payments to it as and when it received sale proceeds. Therefore, it's impossible for Stalwart to have advanced a loan from its current years sale proceeds.

22. The Counsel for the Respondent on the other hand contended that the loan advanced by Stalwart is not a deemed dividend under the IT Act. He argued that Section 2(22)(e) ought to receive a strict interpretation as laid down in *Tarulata Shyam v. CIT*, (1977) 108 ITR 345 (SC). If the Department is to tax a loan as dividend, there must be a definite finding of accumulated profits and not mere presumption as held in *CIT v. Nagindas M. Kapadia*, (1989) 177 ITR 393 (Bom). At the time of this loan advancement, there was no definite finding if Stalwart possessed accumulated profits. Therefore, the Counsel established that the onus is on the Petitioner to prove the existence of accumulated profits and not assume the same through mere presumption. He also argued that Article 10 of the India-Singapore Double Taxation Avoidance Agreement ("DTAA") does not include Section 2(22)(e) of the IT Act, as a loan does not amount to a corporate right. He cited the case of *Rajeev Makhija v. Dy. Director of Income Tax*, where the ITAT held that nowhere deemed income in the form of deemed dividend has been brought to tax under Article 10. The Counsel contended that in *P.V.A.L Kulandagan Chettiar*, 267 ITR 654, the Apex Court held in case of a conflict between the IT Act and the DTAA, the DTAA shall prevail. The AAG argued that Article 10

fails to include deemed dividend not being a real dividend under the IT Act. The provision has been incorporated to cure the mischief by private companies to evade tax by paying accumulated profits in the form of a loan. Therefore, the Counsel argued that Article 23 and Article 25 of the DTAA, which stipulate enforcing domestic tax laws in case express provision to the contrary is not provided under the DTAA.

23. We agree with the contention of the Counsel for the Respondent that dividend under DTAA does not provide for deemed dividend and therefore we cannot bring to tax a deemed provision not provided for under the tax treaty.

24. We have heard the learned AAG for Petitioner 4 and also the learned Counsel for the Respondent. The AAG contended that Stalwart is a dealer under the Karnataka Value Added Tax Act, 2003 (hereinafter referred to as "KVAT Act") and therefore, should have discharged its VAT and CST liability. He argued that clause (c) of Section 2(12) of the KVAT Act includes a commission agent within the definition of the creditor. He further argued that Stalwart in a way sold the goods on behalf of the sellers to the retailers and received the amount from the buyers, took its commission and remitted the remaining amount to the sellers. Therefore, the Respondent effected the sale on behalf of the sellers. The commission that was charged by it was a fixed charge payable to an agent or broker for providing services for facilitating a transaction as laid down in the case of *Bangalore Turf Club v. Regional Director, ESIC,* (2014) 9 SCC 657. The AAG also argued that Stalwart having its registered office in Bangalore, it had a "place of business" in Bangalore, Karnataka. Therefore, it was required to register itself as a dealer with the Karnataka Sales Tax Department.

25. The Counsel for the Respondent on the other hand, argued that the Respondent Company was not a dealer under the KVAT Act, as it did not effect any sale on behalf of the seller but merely provided an online portal to connect the seller and buyer. In this manner, the Respondent Company was not a dealer but a service provider and the commission charged by it was a service fee. The Counsel cited the judgment of the Apex Court in the case of *Bhopal*

Sugar Industries Ltd. v. STO, (1977) 40 STC 42 (SC) which held that payment of commission by itself is not conclusive to show that the agreement was one of agency. The question whether contract is for agency or sale will have to be determined having regard to terms and recital of agreement, intention of parties as spelt out in agreement, surrounding circumstances and having regard to course of dealings between the parties. Therefore, the Counsel for the Respondent contended that Respondent Company was a service provider as the nature of the commission was in the form of a service fee and not agency. He cited the case of *Amazon Seller Services Pvt. Ltd.* v. *The Commissioner of Central Excise,* wherein the AAR held Amazon to be a service provider considering its marketplace model.

26. We agree with the Counsel for the Respondent that the sale transactions were effected by sellers who were registered on the online portal of Stalwart and therefore VAT or CST was leviable on the seller. The indirect tax system in India still needs to adapt itself for the e-commerce industry. Therefore, we conclude that the Respondent is not a dealer under the KVAT Act.

27. In the light of the above conclusions, all the impleading Petitions along with the main winding up Petition stand dismissed.