

Exceptions to Moratorium Under Section 14(1) of the Insolvency and Bankruptcy Code, 2016



*The moratorium is a crucial provision of the Insolvency and Bankruptcy Code, 2016 (IBC) for successful resolution of the Corporate Debtor. As per Section 14 (1) of the IBC, the Adjudicating Authority is empowered to declare the moratorium for the Corporate Debtor that shall have effect from the Insolvency Commencement Date (ICD) till the approval of the Resolution Plan or Liquidation as the case may be. As the order of the moratorium prohibits any kind of recovery action by any creditor including taxation agencies against the Corporate Debtor and ensures maintenance of the supply of essential goods and/or services, it greatly helps in running the Corporate Debtor as a Going Concern which is crucial for the value maximization. In the present article, the author presents a thorough analysis of the various aspects of the moratorium under the IBC and related jurisprudence. **Read on to know more...***



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1. Declaration of Moratorium

Once the application for the initiation of Corporate Insolvency Resolution Process (CIRP) filed by either Financial Creditor or Operational Creditor, against a Corporate Debtor is admitted by the Adjudicating Authority (AA), the AA declares a moratorium under Section 14 of the Insolvency and Bankruptcy Code, 2016 (IBC). The term 'moratorium' has not been defined in the IBC. In Cambridge Dictionary the expression 'moratorium' has been defined to mean 'the stopping of an activity for an agreed amount of time'. In Merriam Webster Dictionary it means 'legally authorized period of delay in the performance of a legal obligation or the payment of a debt; a waiting period set by an authority; or a suspension of activity.

The moratorium begins from the commencement of CIRP and ceased to have effect on the approval of Resolution Plan by the AA or on Liquidation. In between period the bar available in Section 14 will have effect.

2. Prohibitions Imposed by Moratorium

The moratorium prohibits the following activities after commencement of CIRP under Section 14(1) of the IBC:

- (a) the institution of suits or continuation of pending suits or proceedings against the Corporate Debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
- (b) transferring, encumbering, alienating or disposing of by the Corporate Debtor any of its assets or any legal right or beneficial interest therein;
- (c) any action to foreclose, recover or enforce any security interest created by the Corporate Debtor in respect of its property including any action under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
- (d) the recovery of any property by an owner or lessor where such property is occupied by or in the possession of the corporate debtor.

Thus, any legal proceedings during the moratorium period are prohibited under Section 14(1) of the IBC. However, there are exceptions to Section 14(1). While Section 14(1)(a) refers to monetary liabilities of the Corporate Debtor, Section 14(1)(b) refers to the Corporate Debtor's assets, and together, these two clauses form a scheme which shields the Corporate Debtor from pecuniary attacks against it in the moratorium period so that the Corporate Debtor gets breathing space to continue as a going concern in order to ultimately rehabilitate itself.

Section 14(1)(a) refers to monetary liabilities of the CD while Section 14(1)(b) refers to the CD's assets, and together, these two clauses form a scheme which shields the CD from pecuniary attacks against it in the moratorium period.

There are many case laws where the proceedings against the Corporate Debtor have been barred by National Company Law Tribunal (NCLT), National Company Law Appellate Tribunal (NCLAT), High Courts and the Supreme Court.

3. License, Quota etc.

The explanation to Section 14(1) provides that a license, permit, registration, quota, concession, clearances or a similar grant or right given by the Central Government, state governments, local authorities, sectoral regulator or any other authority constituted under any other law for the time being in force, shall not be suspended or terminated on the grounds of insolvency, subject to the condition that

there is no default in payment of current dues arising for the use or continuation of the license, permit, registration, quota, concession, clearances or a similar grant or right during the moratorium period.

4. Supply of Essential Goods

Section 14(2) of the IBC provides that the supply of essential goods or services to the Corporate Debtor as may be specified shall not be terminated or suspended or interrupted during moratorium period.

Section 14(2A) of the IBC provides that where the Interim Resolution Professional and/or Resolution Professional (RP) considers the supply of goods or services critical to protect and preserve the value of the Corporate Debtor and manage the operations of such Corporate Debtor as a going concern, then the supply of such goods or services shall not be terminated, suspended or interrupted during the period of moratorium, except where such corporate debtor has not paid dues arising from such supply during the moratorium period or in such circumstances as may be specified.

However, Section 14(3) of the IBC, as amended from time to time, provides that the restrictions during moratorium shall not apply to:

- (a) such transactions, agreements or other arrangements may be notified by the Central Government in consultation with any financial sector regulator or any other authority.
- (b) surety in a contract of guarantee to a Corporate Debtor.

5. Corporate Guarantee

As per Section 14(3)(b) of the IBC the guarantee can be revoked during CIRP. The same has been confirmed by the NCLAT in the matter of *National Small Industries Corporation Limited, Delhi v. Prabhakara Kumar and Canara bank¹* (2023). The NCLAT held that the 'Bank Guarantee' provided by the Respondent No. 2/Bank is held to be covered by the exception provided in provisions of Section 14(3)(b) of the IBC and the moratorium prescribed under Section 14(1) of the IBC, shall not apply to its 'encashment'. The NCLAT set aside the order of the AA and allowed the appeal.

¹ *Company Appeal (AT) (Insolvency) No. 841 of 201 in IA No. 3139/ND/2020 in CP (IB) No. 364(ND)/2019- NCLT, Principal Bench, New Delhi, decided on October 10, 2023.*

6. Arbitration proceedings

In the matter of *Alchemist Asset Reconstruction Company Limited v. Hotel Gaudayan Private Limited*² (2017) the Supreme Court held that arbitration proceedings initiated after implementation of CIRP is *non est* in the law. However, Courts have created certain exceptions where arbitration may be allowed to continue, if, it was filed before the order of moratorium or invoked during moratorium in cases where the claims are for the benefit of Corporate Debtor.

In the matter of Alchemist Asset Reconstruction Company Limited v. Hotel Gaudayan Private Limited (2017) the Supreme Court held that arbitration proceedings initiated after implementation of CIRP is non-est in the law.

In *Power Grid Corporation of India Limited v. Jyoti Structures Limited*³ (2017), it was held that a case was initiated under Section 34 of the Arbitration Act to set aside the arbitral award which was passed in the favor of the Corporate Debtor. The nature of the arbitral award was that of a pure money decree. When the proceedings were pending, an application for insolvency of the Corporate Debtor was filed and a moratorium was imposed under Section 14. The question before the Court was whether, after the imposition of the moratorium, the arbitral proceedings ought to be stayed or not.

The Court held that the term 'proceedings' mentioned in Section 14 is limited to the debt recovery actions against the assets of the Corporate Debtor and not any type of proceedings. Moreover, there is no burden created on the assets of the Corporate Debtor when the proceedings are continued. Hence, there is no bar on such proceedings under the provisions of moratorium. Moreover, a distinction is made between usage of the term 'against the Corporate Debtor' in Section 14(1)(a) of the IBC in comparison with 'by or against the Corporate Debtor' in Section 33(5). It makes it clear that the latter encompasses a wider meaning.

Furthermore, only the enforceability of the arbitral award is subjected to the moratorium provision and not the proceedings, execution of the award and the objections.

Subsequently, the proceedings can be continued by the Interim Resolution Professional.

7. Negotiable Instruments Act

Section 138 of the Negotiable Instruments Act (NI Act) deals with cheque bouncing; if an amount falls due in this respect, the same can be recovered by filing a complaint under this provision. The NCLAT, in *Shah Brothers Ispat Pvt. Ltd. v. P. Mohanraj & others*⁴ (2018) held that a moratorium would not be extended to proceedings filed under the NI Act. The reasoning adopted by the NCLAT was that the proceedings under the NI Act are criminal in nature and that Section 138 is a penal provision. The NCLAT took the view that the action taken under the section is not a proceeding or a judgment or a decree of a money claim.

The NCLAT in Shah Brothers Ispat Pvt. Ltd. v. P. Mohanraj ((2018), on the grounds that the Negotiable Instruments (NI) Act is criminal in nature and that Section 138 is a penal provision, held that a moratorium would not be extended to proceedings filed under the NI Act.

8. Proceedings under Articles 32 and 136 of the Constitution of India

An exception was created by the NCLAT in *Canara Bank v. Deccan Chronicle Holdings Limited*⁵ (2017) in which it was held that the imposition of the moratorium will not restrict any proceedings to be initiated or pending before the Supreme Court under Article 32 or Article 136 of the Constitution of India wherein an order is passed. Moreover, the power of any High Court under Article 226 of the Constitution of India will not be affected by such imposition of a moratorium.

9. Property not owned by Corporate Debtor

In *Alpha & Omega Diagnostics (India) Limited v. Asset Reconstruction Company of India Limited and others*⁶ (2023), the appellant filed an application under Section 10 of the IBC for initiation of CIRP. For the question whether a property which is not owned by a Corporate Debtor shall come within the ambits of the moratorium, the Adjudicating Authority held that the word 'its' denotes the property owned by the Corporate Debtor. The property not

² The Supreme Court, Civil Appeal No. 16929 of 2017 decided on October 23, 2017.

³ Delhi High Court, OMP (Comm) 397 of 2016, decided on December 11, 2017.

owned by the Corporate Debtor does not fall within the ambits of the moratorium.

10. Circulars

Exceptions to Section 14 of the IBC are given by the Insolvency and Bankruptcy Board of India (IBBI) through its circulars.

- (a) The Central Government vide Notification No. S.O. 2660(E), dated June 14, 2023, notified that the provisions of sub section (1) of Section 24 of the IBC, 2016 shall not apply where the Corporate Debtor has entered into any of the following transactions, arrangements or agreements, namely: -
- (i) the Production Sharing Contracts, Revenue Sharing Contracts, Exploration Licenses and Mining Leases made under the Oilfields (Regulation and Development) Act, 1948 and rules made there under; and
 - (ii) any transactions, arrangements, or agreements, including Joint Operating Agreement, connected or ancillary to the transactions, arrangements or agreements referred to in clause (i).
- (b) The Central Government vide Notification No. SO 4321(E), dated October 03, 2023, notified that the provisions of sub-section (1) of Section 14 of the IBBI

not apply to transactions, arrangements or agreements, under the Convention and the Protocol, relating to aircraft, aircraft engines, airframes and helicopters.

Moratorium is applicable to all proceedings which have a civil nature or seem to enforce a civil remedy. The basis for the application of moratorium is the nature of such proceedings and the object and purpose of such enactment.

11. Conclusion

Moratorium is applicable to all proceedings which have a civil nature or seem to enforce a civil remedy. The basis for the application of moratorium is the nature of such proceedings and the object and purpose of such enactment. It is now clear that once a moratorium has been declared, any proceeding which may affect the liquidity or assets of the company cannot be permitted to continue in the event moratorium has been declared. While the Supreme Court has clearly laid down the effects of moratorium on proceedings instituted to recover a civil debt, question marks remain over the effects of moratorium for recovery of 'proceeds of a crime' once moratorium has been declared. While such criminal proceedings are likely to be unaffected, question marks may arise as to how such criminal proceedings may affect parties whose dues are not recoverable owing to the effects of moratorium.

