



Interaction of Moratorium under IBC with SARFAESI Act- Unambiguous

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LEGAL FRAMEWORK

Moratorium signifies an authorized postponement, usually a lengthy one, in the deadline for paying a debt or performing an obligation.¹ The Banking Regulation Act, 1949 permitted the issuance of such orders against banking companies only by the Reserve Bank of India or the Central Government.² The Apex court issues a moratorium order to be a pre-emptive act in order to protect the bank and the associated stakeholder, whenever the banks are in precarious financial position.³ However, the new insolvency law in the country has extended the power of issuing moratorium in the hands of a quasi-judicial body i.e. National Company Law Tribunal (“NCLT”).⁴ Interestingly, the scope of moratorium passed by NCLT under the Insolvency and Bankruptcy Code, 2016 (“IBC”) shall not have any effect on the proceeding pending under Article 226

before the High Court and under Article 32 before the Supreme Court, respectively.⁵

Section 14 of the IBC is the enabling provision whereby the NCLT shall issue a moratorium in order to prohibit certain acts subject to a few exceptions like supply of essential commodities and others as specified by the Central Government. The basic intent behind a moratorium as identified by the Bankruptcy Laws Reform Committee⁶ is value maximising for the entity to continue operations even as viability is being assessed during the insolvency resolution process (“IRP”) and eliminating any additional stress on the business after the public announcement of the IRP. Maintaining consistency with the abovementioned intent, the Apex court held that the purpose behind a moratorium is “to provide the debtors a breathing spell in which he is to seek to reorganize his business.”⁷

FACTUAL MATRIX

In the case of *Indus Finance Limited v. Quantum Limited*⁸, the Petitioner had provided Quantum with an unsecured term loan amounting to INR 2 crore in the year 2011. The corporate debtor was highly irregular in paying interest in the year 2012, which consecutively, turned into a non-

¹ Bryan A. Garner, *Black’s Law Dictionary*, (West Group, United State of America, 5th Reprint, 2002).

² Section 45, The Banking Regulation Act, 1949 [Act 10 of 1949].

³ *Ganesh Bank, Kurundwad Ltd. v. The Union Of India And Ors.*, Civil Appeal No. 3698 of 2006 arising out of SLP (C) No. 7188 of 2006.

⁴ Section 5, Insolvency and Bankruptcy Code, 2016 [Act 31 of 2016].

⁵ *Canara Bank v. Deccan Chronicle Holdings*, Company Appeal (AT) (Insolvency) No. 147 of 2017.

⁶ The report of the Bankruptcy Law Reforms Committee Volume I: Rationale and Design, (November, 2015) available at:

<http://www.ibbi.gov.in/Reports.html>

⁷ *Innoventive Industries Ltd v. ICICI Bank Ltd*, CIVIL APPEAL NOS. 8337-8338 OF 2017.

⁸ C.P. No.10431 I & BP /NCLT/ MB/MAH/2017.



performing asset (“NPA”) by March, 2013 and credit options of the corporate debtor with a bank also tuned into an NPA. This led to sale of the liabilities upon Quantum to J M Finance Asset Reconstruction Company Private Limited, by the bank. Whereas, J M Finance Asset Reconstruction Company Private Limited, adopting its due legal recourse filed claims before the DRT under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interests Act, 2002 (“SARFAESI Act”) and got an order of recovery. The said recovery was to be realised by disposing of the properties hypothecated, leaving the Petitioner in the present matter, remediless. Therefore, in light of the aforesaid facts and aggrieved by the default in payment, the Petitioner initiated corporate IRP against Quantum under Section 7 of the IBC.

JUDGEMENT

- The NCLT applying the literal rule of interpretation admitted the application allowing the moratorium to sustain during the insolvency resolution process. The reason accorded by the tribunal was the difference in the time taken to adjudicate a dispute under SARFAESI vis-a-vis that of an IRP under IBC. IRP’s inherent feature of being a fast track procedure (maximum up to 180 days) shall not create an eclipse on the proceedings before Debt Recovery Tribunal (“DRT”).
- The adjudicating authority understood the position of the petitioner as an unsecured creditor who was unable to join the proceedings before the under the SARFAESI Act. Thus, it accepted the separate application under IBC, despite, it

being a parallel matter arising out of the same of facts and same transaction.

- Further, the NCLT unambiguously held that there is no overstepping of jurisdiction as both the statutes have separate objectives. Thus, by virtue of Section 14 (1)(c), there is no contradiction or overlapping between the two statutes and the powers conferred by them

IMPACT ANALYSIS

The order shall have an overall positive impact as it sets up a precedent negating the overlap. It upholds the law given under IBC and clearly demarcates the universe in which IBC and SARFAESI will operate and not coincide or disturb each other with respect to the moratorium. The SARFAESI Act is known to come to aid for the secured creditors by speedy enforcements⁹ and even reconstruction of assets subject to the economic viability of the same. Whereas, IBC is understood to strictly focus on decreasing the quantum of losses or speedy recovery of losses, already incurred, so as to encourage and facilitate an economically conducive environment for debt financing.¹⁰

The order takes into consideration the defects under SARFAESI Act which were subsequently, cured by IBC by providing adequate remedies to other class of creditors. Further, one of the objectives of IBC *inter alia*s prevent a tilt in balance of power in favour of the creditor¹¹. This objective is achieved by a moratorium and

⁹Sagar Innovative Pvt.Ltd.v. Punjab National Bank, 2017 (0) AIJEL-HC 237272, (para 15), available at: <http://aijel.com/80/JY7/237272.jdf>

¹⁰Supra note 6

¹¹Ibid



this order brings into effect a ‘calm period’ for negotiations given to a debtor by removing all encumbrances on assets till the conclusion of IRP.

CONCLUSION

A moratorium shall subsist during the pendency of proceedings before DRT and the rights of secured creditors shall not override those of the unsecured ones. Merely because a proceeding is pending before the DRT, shall not dissolve the claims of the unsecured creditors. Any class of creditor, who cannot seek a remedy under the SARFAESI Act, can approach the NCLT under IBC and the tribunal shall address the cause of their grievance, once the tribunal is satisfied on the occurrence of a ‘default’¹². NCLT Mumbai had also dismissed the application for sale of a property in favour of JM Finance Limited filed under Section 65 of the IBC, as the moratorium stood valid and an order of disposing off of a property to settle claims under SARFAESI cannot intervene in IRP without complying with the mandatory conditions¹³ specified under Rule 9 of the Security Enforcement Rules, 2002.¹⁴

¹²"default" means non-payment of debt when whole or any part or instalment of the amount of debt has become due and payable and is not repaid by the debtor or the corporate debtor, as the case may be. Section 12(2), Insolvency and Bankruptcy Code, 2016 [Act 31 of 2016].

¹³Mathew Varghese v. M. Amritha Kumar , (2014)5 SCC 610

¹⁴Varun Marwah, “Sale initiated under SARFAESI hit by moratorium under IBC? NCLT answers” barandbench.com, Oct 9th, 2017, available at: <https://barandbench.com/sale-sarfaesi-ibc-moratorium/>