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The Limits to a Moratorium: Interplay Between the Indian Insolvency and Bankruptcy Code and Defensive Proceedings

Author(s)

Abhijnan Jha
Partner at
AZB &
Partners

Chetan Chawla
Associate
at AZB &
Partners

Posted

1 February 2023

Time to read

4 Minutes

OBLB categories [Commercial Law](#)

OBLB types [Opinion](#)

OBLB keywords [Insolvency and Bankruptcy Code](#), [Bankruptcy](#), [Corporate insolvency](#), [Moratorium](#)

Jurisdiction [India](#)

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Section 14 of the Indian Insolvency and Bankruptcy Code, 2016 ('IBC') imposes a moratorium on the initiation and continuation of legal proceedings against a corporate debtor during the Corporate Insolvency Resolution Process ('CIRP'). It states that the adjudicating authority shall declare a moratorium for prohibiting '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'.

There is no quarrel about the need for and objective of a moratorium on legal proceedings and recovery actions against a corporate debtor during the CIRP. Courts have repeatedly affirmed the principle behind the imposition of a moratorium, ie to shield the corporate debtor from pecuniary attacks and to ensure the maximization of the assets of the corporate debtor.

At the same time, section 14(1)(a) of the IBC does not create any fetter on the right of the corporate debtor to initiate or continue litigation. This has been recognized recently by the Supreme Court of India in the case of *NDMC v. Minosha India Ltd.*, [2022 SCC OnLine SC 546] This interpretation is further bolstered when the construction of section 14(1)(a) of the IBC is contrasted with that of section 33(5) of the IBC, which relates to a moratorium on legal proceedings during liquidation (ie when CIRP has failed to revive the corporate debtor). Section 33(5) states: 'when a liquidation order has been passed, no suit or other legal proceeding shall be instituted by or against the corporate debtor'. This illustrates the legislative intent to restrict the scope and sweep of section 14 of the IBC, which restricts the bar of

the moratorium to proceedings ‘against the corporate debtor’, as opposed to section 33 where proceedings ‘by or against the corporate debtor’ are stalled.

Therefore, a blanket construction of section 14 of the IBC creates a piquant situation where some proceedings may be initiated by a corporate debtor, but the opposing party loses the right to defend itself (by way of an appeal or revision) against an order which may be passed in such proceedings. Consider a corporate debtor that initiates a suit before a High Court. If the High Court passes a judgment in favour of the corporate debtor, after which CIRP is commenced, the corporate debtor may seek the advantage of section 14 of the IBC to stall hearings in any appeal which may be filed by the defendant in the suit.

In this post, we argue that the interpretation of section 14 ought not to be so all-encompassing and necessary guardrails need to be recognized to prevent abuse. We analyse the prior regime relating to winding up of companies and explain that there is existing judicial authority for such limitations to be read into section 14.

The question which arises is whether a defensive proceeding can be said to be a proceeding ‘against the corporate debtor’. If the answer is no, the consequence would necessarily be that a moratorium under section 14(1)(a), IBC would not hit an appeal by a party against an order passed in a suit instituted by a corporate debtor.

This position becomes unequivocally clear when the words ‘against the company’ are read in light of the interpretation of the phrase in section 171 of the Companies Act, 1913 and section 446 of the Companies Act, 1956.

Section 171 of the Companies Act, 1913 states: ‘When a winding up order has been made, no suit or other legal proceeding shall be proceeded with or commenced against the Company except by leave of the Court, and subject to such terms, as the Court may impose.’

A full bench of the Lahore High Court interpreted ‘against the Company’ in section 171 in *Kishen Singh v. Industrial Bank of India* [1918 SCC OnLine Lah 2] and held that an appeal or an application for revision arising out of an action brought by a company does not come within the purview of section 171, and that it can be initiated or continued without the leave of the court. As regards defensive proceedings, the Court observed that a person instituting a defensive proceeding could legitimately contend that it did not take the initiative in setting the machinery of the court into motion, and that consequently its failure in the court of

first instance should not debar it from going up to the higher court and satisfying such a court that its defence was correct.

The interpretation of the Lahore High Court was in line with the position taken by the House of Lords in the case of *Humber & Co. v. John Griffiths Cycle Company* [(1901) 85 LT 141]. Lord Davey held that once an action by the company itself has been proceeded with, there is no necessity for the defendants in the action to obtain leave for any defensive proceeding on their part.

The same position was reiterated by a full bench of the Allahabad High Court in the case of *Rahmat Ali Fateh Ullah v. Calcutta National Bank Limited* [1954 SCC OnLine All 176]. The High Court held that if a company had instituted a suit or other proceeding to enforce a claim, any action taken by the defendant or the opposite party by way of defence, or if the company has obtained a decree or order, any defensive action by way of appeal, revision, review or setting aside of an ex-parte decree or order should not require the permission of the Company Judge. Thus, appeals and defensive actions were excluded from the ambit of actions 'against the company' within the terms of section 171 of the Companies Act, 1913. This principle has been reiterated over the years by various High Courts in relation to the Companies Act, 1956.

Principles of natural justice and statutory interpretation would also lend credence to the interpretation that appeals/defensive proceedings should not be hit by the moratorium under section 14 of the IBC. It is trite law that in the legal pursuit of a remedy, the suit, appeal and second appeal are steps in a series of proceedings, are connected by an intrinsic unity, and are to be regarded as a composite legal proceeding (see *Garikapati Veeraya v N. Subbiah Choudhry & Ors* [1957 SCR 488]). Thus, if a suit instituted by the corporate debtor is not hit by the moratorium, an appeal arising from such a suit should also not be barred due to a moratorium on the corporate debtor's affairs. The right of the corporate debtor to proceed with a suit is naturally intermingled with the right of the defendant therein to contest the suit by means of an appeal, since the right of appeal is not a mere matter of procedure but is a substantive right. Moreover, an interpretation which leaves the appellant remediless defeats the doctrine embodied in the legal maxim *ubi jus ibi remedium* since every person who has a right must have a means to vindicate it.

This interpretation of section 14 is in line with the principle that the interpretation of a statute ought not foreclose a forum for enforcement of a remedy, and the forum ought to be revealed where it does not exist clearly. Any statutory interpretation should avoid absurdity and inconsistency. Allowing a corporate

debtor to institute and pursue proceedings against another party, while at the same time tying the hands of the other party to defend itself is exactly the kind of absurdity which needs to be avoided while interpreting section 14 of the IBC.

Abhijnan Jha is a Partner at AZB & Partners.

Chetan Chawla is an Associate at AZB & Partners.

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