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## Supreme Court clarifies non-applicability of moratorium under the Insolvency and Bankruptcy Code, 2016 to proceedings under the Negotiable Instruments Act, 1881

In a landmark ruling, a 2 (two) judge bench of the Hon'ble Supreme Court of India ("**Supreme Court**") in the case of *Rakesh Bhanot vs. M/s. Gurdas Agro Private Limited*<sup>1</sup> held that proceedings under Section 138 of the Negotiable Instruments Act, 1881 ("**NI Act**") cannot be stayed merely because a personal guarantor initiates insolvency resolution under Section 94 of the Insolvency and Bankruptcy Code, 2016 ("**IBC**"). The Supreme Court emphasised that the interim moratorium under Section 96 of the IBC applies only to civil debt recovery, not criminal liability arising from cheque dishonour.

### Brief facts

1. M/s Gurdas Agro Private Limited ("**Respondent**") filed a complaint under Section 138 of NI Act, against M/s Arjun Mall Retail Holdings Private Limited through its directors, Rakesh Bhanot ("**Appellant**") and others before the Judicial Magistrate First Class, Bathinda, ("**Trial Court**") for dishonour of cheques for insufficiency of funds.
2. During the pendency of the aforesaid proceedings, the Appellant filed an application under Section 94 of the IBC before the Hon'ble National Company Law Tribunal, Chandigarh Bench ("**NCLT**") seeking initiation of personal insolvency proceedings.
3. In view of the pending Section 94 application and the operation of interim moratorium under Section 96 of the IBC, the Appellant moved an application before the Trial Court seeking adjournment of the Section 138 proceedings *sine die*. The said application was rejected by the Trial Court.
4. Aggrieved by the rejection, the Appellant preferred a criminal petition under Section 482 of the Code of Criminal Procedure, 1973, before the High Court of Punjab and Haryana, which was also dismissed. Challenging the same, the lead criminal appeal was filed by the Appellant before the Supreme Court.
5. Notably, the Appellant contended that the moratorium under Section 96 of the IBC should be interpreted broadly to encompass criminal proceedings under Section 138 of the NI Act, as these arise from non-payment of a debt. The Respondent argued that the moratorium was intended only for civil recovery actions and not for penal proceedings, which serve a public interest by upholding the integrity of negotiable instruments.

<sup>1</sup> Criminal Appeal No.1607 of 2025; (2025 INSC 445)

## Issue

Whether the interim moratorium under Section 96 of the IBC automatically stays criminal proceedings under Section 138 read with Section 141 of the NI Act against personal guarantors/directors?

## Findings and analysis

### Re: Moratorium cannot be misconstrued as a means to avoid criminal accountability

1. The Supreme Court examined the statutory language and legislative intent of Sections 94, 96, and 101 of the IBC. Briefly, Section 94 of the IBC provides for a situation wherein a debtor may approach the Adjudicating Authority for initiation of personal insolvency resolution process. Section 96 of the IBC deals with the commencement of interim moratorium from the date of application filed under Section 94 of the IBC in relation to all debts, i.e., deemed stay on any legal proceeding pending against the debtor concerning any debt. It held that the interim moratorium under Section 96 is designed to provide debtors with a temporary shield from civil recovery actions during the pendency of insolvency resolution, not to insulate them from criminal liability for statutory offences like dishonour of cheque.
2. The Supreme Court also held that the object of moratorium or the right of a debtor to approach the NCLT under Section 94 of the IBC is not to stall criminal prosecution or any proceedings unrelated to the recovery of the debt. The term “*any legal action or proceedings*” does not mean “*every legal action or proceedings*”. It must be interpreted to mean only proceedings concerning recovery of debt by invoking the principles of *noscitur a sociis*.

### Re: The statutory liability against the directors under Section 138 of the NI Act continues to bind natural persons irrespective of any moratorium

1. The Supreme Court distinguished between actions for debt recovery (civil in nature) and prosecutions under Section 138 of the NI Act (criminal in nature). It observed that while the former may be stayed during the moratorium under the IBC, the latter are penal proceedings aimed at maintaining commercial discipline and trust in negotiable instruments.
2. The Supreme Court relying on *P. Mohanraj vs. Shah Brothers Ispat Private Limited*<sup>2</sup> and *Ajay Kumar Radheyshyam Goenka vs. Tourism Finance Corporation of India Limited*<sup>3</sup> reaffirmed that the moratorium under the IBC does not extend to criminal prosecutions. The Supreme Court emphasised that the object of the IBC is to facilitate resolution of financial distress, not to provide a refuge from personal criminal liability.
3. The Supreme Court further clarified that even if the underlying debt is extinguished or restructured through insolvency proceedings, the personal criminal liability of signatories or directors under Section 138 of the NI Act persists. The acceptance of a resolution plan under Section 31 of the IBC or the operation of a moratorium does not absolve individuals from prosecution for dishonour of cheque.

## Conclusion

1. The Supreme Court’s judgment provides much needed clarity on the interplay between insolvency proceedings and prosecutions for dishonour of cheques. The interim moratorium under Section 96 of the IBC is limited to civil actions for recovery of debt and does not shield individuals from criminal liability under Section 138 of the NI Act. This ensures that the statutory deterrence against dishonour of cheques remains robust, and the integrity of commercial transactions is preserved.

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<sup>2</sup> (2021) 6 SCC 258

<sup>3</sup> (2023) 10 SCC 545

2. The judgment also comes down heavily on attempts to misuse insolvency mechanisms as a shield against criminal accountability, reinforcing the principle that insolvency is a process for resolution, not a refuge from liability.
3. The Supreme Court emphasised that the object of the IBC is to facilitate the resolution of genuine financial distress and not to provide a refuge for individuals seeking to evade statutory penal consequences. The ruling demonstrates that the phrase “*legal action or proceeding in respect of any debt*” in Section 96 of the IBC must be interpreted in the context of civil proceedings for debt recovery and cannot be stretched to include criminal prosecutions which are fundamentally punitive and serve public interest.
4. The Supreme Court has further highlighted that the provisions for moratorium under the IBC are designed to offer a breathing space to enable reorganisation of financial affairs without the immediate threat of creditor actions. The provisions of moratorium flow with the overall scheme of a complete resolution such that the business of the debtor or corporate debtor can be started with a fresh slate or can be liquidated if resolution is not a viable option. Thus, in no way can a moratorium be interpreted to mean that it absolves an individual from criminal liability.
5. The Supreme Court has further clarified that the proceedings under Section 138 of the NI Act are not primarily for recovery of debt but rather for initiating criminal action against issuer of dishonoured cheque.
6. This judgment therefore ensures that creditors retain the ability to pursue both insolvency remedies and criminal prosecutions against defaulting companies and its directors, in turn maintaining the integrity of the financial system. It prevents the misuse of insolvency proceedings as a tool for delaying or avoiding criminal accountability and reinforces the legislative intent behind both the IBC and the NI Act.

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