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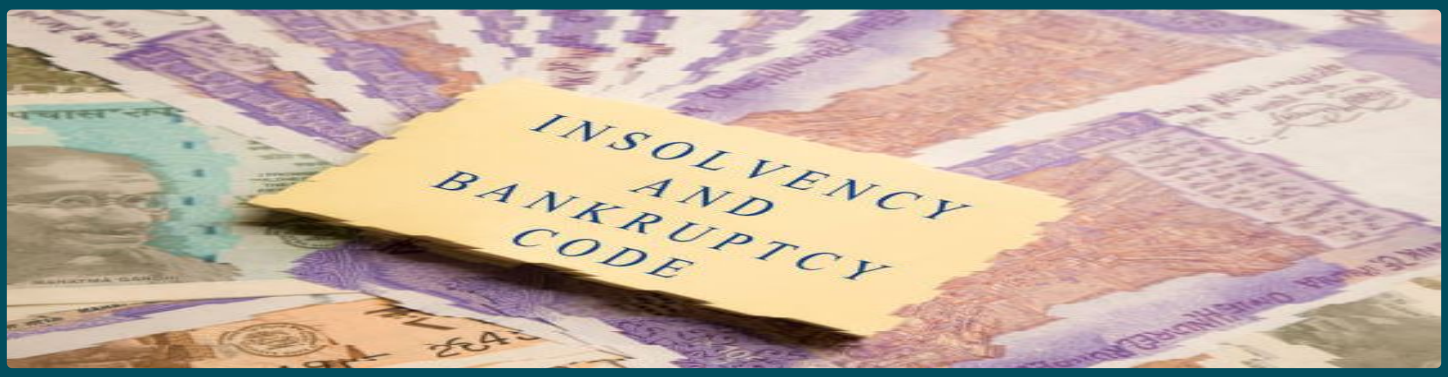

CIVIL

Abuse of Interim Moratorium Under Section 96 of the Insolvency and Bankruptcy Code, 2016: A Legal Perspective

AUTHOR Rahul Sundaram

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Introduction

The Insolvency and Bankruptcy Code, 2016 (“IBC”) was enacted to streamline insolvency proceedings and ensure timely resolution of distressed assets. However, certain provisions of the IBC, particularly Section 96, which provides for an interim moratorium upon the filing of an application under Section 94 or 95, have been exploited by unscrupulous borrowers. Many borrowers / Personal Guarantors to a corporate debtor invoke this provision not with the intent of genuine insolvency resolution but as a tactical move to delay recovery or security enforcement actions initiated by secured creditors under the provisions of the SARFAESI Act, 2002.

This article examines the misuse of interim moratoriums and discusses the Bombay High Court judgment in Bank of Baroda v. Union of India & Anr. (2024), which provides crucial guidelines to address this issue.

Table of contents

- Introduction
- Understanding Interim Moratorium Under Section 96
- Pattern of Abuse: How Borrowers Exploit Section 96, IBC, 2016
- Bombay High Court’s Intervention in Bank of Baroda v. Union of India (2024)
- Key Directions by the Bombay High Court
- Conclusion

Understanding Interim Moratorium Under Section 96

Section 96 of the IBC states that when an application under Section 94 (by the debtor) or Section 95 (by a creditor) is filed, an interim moratorium comes into effect immediately. This moratorium:

1. **Stays all legal actions** against the debtor concerning any debt.
2. **Prevents creditors from initiating any new proceedings** against the debtor.
3. **Remains in effect until the application is admitted or rejected.**

While the provision aims to provide relief to financially distressed individuals and ensure a fair resolution process, it is often misused by personal guarantors to a corporate debtor and borrowers who file applications without pursuing them seriously. This results in a stay on security enforcement actions for an “extremely unreasonable period of time”, stalling legitimate recovery proceedings by secured creditors under SARFAESI. It is interesting to note that unlike the moratorium u/s 14 of the Code post an order from the NCLT, the interim moratorium u/s 96 applies merely on filing of an application u/s 94 or 95 of the Code and does not require any order from the adjudicating authority.

Pattern of Abuse: How Borrowers Exploit Section 96, IBC, 2016

The following are common tactics employed by borrowers to misuse the interim moratorium:

1. **Filing of application by individuals other than “Personal Guarantors to a Corporate Debtor** (PGTCD). Part III of the IBC has been notified by the central government qua PGTCD , and it is seen that individuals who are not PGTCD or under a misconception of being a PGTCD file such application to abuse the process and protract and delay security enforcement action initiated by creditors.
2. **Filing an Application with Defects**: Borrowers file an application under Section 94 but fail to remove procedural defects pointed out by the National Company Law Tribunal (NCLT) Registry. Since the interim moratorium starts from the date of filing, the debtor enjoys protection indefinitely.
3. **Failure to Pursue the Application**: After filing, borrowers deliberately do not prosecute their cases or comply with procedural requirements, ensuring that their applications remain in limbo.
4. **Deliberate Delay in Compliance**: Many borrowers take no steps to get their applications registered and numbered at NCLT , allowing the interim moratorium to continue indefinitely without judicial scrutiny.
5. **Re-filing to Restart the Moratorium**: If an application is rejected due to non-compliance, borrowers refile the same application to restart the interim moratorium, further delaying enforcement actions.

The Bank of Baroda v. Union of India & Anr. (2024) case highlighted this issue where multiple borrowers used these tactics to stall SARFAESI proceedings indefinitely.

Bombay High Court's Intervention in Bank of Baroda v. Union of India (2024)

In this case, Bank of Baroda filed a writ petition before the Bombay High Court, arguing that:

- Borrowers were misusing Section 96 by filing applications under Section 94, only to delay security enforcement under SARFAESI.
- NCLT Mumbai was not enforcing Rule 28 of the NCLT Rules, 2016, leading to long-pending defective applications and "extremely unreasonable" extended interim moratoriums.
- The legislative intent of the IBC was not to provide an indefinite shield to defaulters against their creditors.

The Bombay High Court recognized the systemic abuse of interim moratoriums and directed NCLT Mumbai to enforce strict procedural timelines under Rule 28 of the NCLT Rules (Rule 28 /Rules).

Key Directions by the Bombay High Court

To curb the misuse of interim moratoriums, the Court established **strict timelines for NCLT Mumbai** to process applications under Sections 94 and 95 of the IBC, 2016 read with the said Rule 28:

1. **Objection Notification (Within 7 Days):**
   - NCLT must notify defects in applications within 7 days of filing as per Rule 28(2) from filing of the application u/s94 or 95 of the IBC, 2016 .
2. **Compliance Deadline (7 Days from Notification):**
   - Applicants must rectify defects within **7 days**.
3. **Monthly Scrutiny Notices:**
   - NCLT will issue a monthly list of defective applications where compliance has not been completed within the stipulated 7 days.
4. Within a period of 15 days from the issuance of the monthly list as above a notice under Rules 28(3) and 28(4) stating that matters where compliance is not carried out will be proceeded to be dealt with in accordance with Rule 28(4) within in 30 days.
5. **Final Warning & Rejection (After 30 Days of Non-Compliance):**
   - If objections are not cleared within **30 days**, the application will be **declined** within a Period of 7 days and marked online as " dismissed as declined by register"
6. **No Automatic Moratorium on Re-filed Applications:**
   - If an application is rejected due to non-compliance, merely re-filing it will not restart the interim moratorium unless an appeal under Rule 63 of the NCLT Rules is pursued.

By enforcing these rules, the Court aimed to ensure that borrowers cannot misuse the IBC to indefinitely stall security enforcement proceedings under the SARFAESI Act, 2002.

Conclusion

The interim moratorium under Section 96, while well-intended, has been widely misused by borrowers to indefinitely delay creditor enforcement actions. The Bombay High Court's ruling in Bank of Baroda v. Union of India (2024) has set a strong precedent by ensuring that procedural timelines under Rule 28 of the NCLT Rules are strictly enforced. Legislative amendments and stricter compliance mechanisms will be essential to prevent abuse and restore balance between borrower protection and creditor rights under the IBC.

For further details write to contact@indialaw.in