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Section 138 NI Act and IBC Moratorium: Supreme Court Defines the Boundaries

AUTHOR Rahul Sundaram

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The Supreme Court of India recently delivered a significant judgment in the case of Vishnoo Mittal versus M/S Shakti Trading Company, addressing the interplay between insolvency proceedings and criminal prosecutions under the Negotiable Instruments Act.

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Background of the Case

This legal battle arose from a business relationship between Vishnoo Mittal, director of Xalta Food and Beverages Private Limited, and M/S Shakti Trading Company, which was a super stockist for the corporate entity. The respondent had issued eleven cheques totalling Rs.11,17,326/- to M/S Shakti Trading Company, which were subsequently dishonoured by the bank on 07.07.2018.

Key Facts

Following the dishonour of these cheques, M/S Shakti Trading Company issued a legal notice under Section 138 of the Negotiable Instruments Act on 06.08.2018. Importantly, insolvency proceedings against Xalta Food and Beverages Private Limited had commenced on 25.07.2018, with a moratorium imposed under Section 14 of the Insolvency and Bankruptcy Code (IBC). This moratorium typically restricts various legal actions against the corporate debtor during insolvency proceedings.

Submissions by the Parties

The appellant argued that since the moratorium was imposed before the cause of action under Section 138 of the NI Act had fully matured, the proceedings against him should be quashed. He contended that after the appointment of the Interim Resolution Professional (IRP), he no longer had control over the corporate debtor's assets or bank accounts, making it impossible to fulfil the demand notice requirements.

The respondent relied on the High Court's previous decision, which had dismissed the appellant's petition, primarily based on the Supreme Court's judgment in P. Mohan Raj v. M/S Shah Brothers Ispat Pvt. Ltd. That case had held that the moratorium under Section 14 of the IBC applies only to corporate debtors and not to natural persons like the appellant.

High Court's Decision

The High Court had dismissed the appellant's petition under Section 482 of the CrPC, relying on P. Mohan Raj. The court held that since the moratorium under Section 14 of the IBC only protected the corporate debtor and not its directors or other natural persons, the proceedings under Section 138 of the NI Act could continue against the appellant.

Legal Provisions and Case Laws Discussed

The Supreme Court examined several key legal provisions:

Section 14 of the IBC: Which imposes a moratorium preventing various legal actions against the corporate debtor during insolvency proceedings

Section 138 of the NI Act: Which criminalizes dishonouring cheques for insufficiency of funds

Section 482 of the CrPC: Which grants High Courts inherent powers to quash proceedings in appropriate cases

Section 17 of the IBC: Which transfers management of the corporate debtor to the Interim Resolution Professional upon appointment

The Court also discussed relevant case law, including:

P. Mohan Raj v. M/S Shah Brothers Ispat Pvt. Ltd. (2021) 6 SCC 258: Which held that the moratorium under Section 14 of the IBC applies only to corporate debtors

Jugesh Sehgal v. Shamsher Singh Gogi (2009) 14 SCC 683: Which explained the ingredients required to establish an offence under Section 138 of the NI Act

Supreme Court's Analysis and Final Decision

The Supreme Court carefully distinguished this case from P. Mohan Raj, noting that in the present matter, the cause of action under Section 138 of the NI Act had not fully matured before the moratorium was imposed. The Court emphasized that the appellant, as director, had been suspended from his position upon the appointment of the IRP and thus lacked the capacity to fulfill the demand notice requirements under Section 138 of the NI Act.

The Court held that since the appellant could not have complied with the demand notice due to the moratorium and transfer of control to the IRP, the proceedings under Section 138 should be quashed.

Conclusion and Implications

This judgment clarifies the relationship between corporate insolvency proceedings and criminal prosecutions against company directors. It establishes that when a moratorium is imposed under the IBC before the cause of action under Section 138 of the NI Act has fully matured, and the director has been suspended from his position, criminal proceedings under the NI Act should be quashed.

The decision has important implications for corporate insolvency proceedings, balancing the rights of creditors with the need for fair treatment of directors during corporate restructuring processes.

For further details write to contact@indialaw.in