

## **NCLAT: Bank guarantees (including advance bank guarantees) can be invoked even during the period of moratorium under Section 14 of the IBC**

In the recent decision of *IDBI Bank v. Indian Oil Corporation Limited*<sup>1</sup>, the National Company Law Appellate Tribunal (“NCLAT”) has held that an irrevocable and unconditional bank guarantee can be invoked even during moratorium period in view of the amended provision under Section 14 (3) (b) of the Insolvency and Bankruptcy Code, 2016 (“IBC”).

### **Brief Facts**

In the Corporate Insolvency Resolution Process (“CIRP”) of Punj Llyod Limited (“Corporate Debtor”), the resolution professional filed an application under Section 60(5) of the IBC before National Company Law Tribunal (“NCLT”), Delhi seeking a restrain on encashment of the bank guarantees by IDBI Bank and the Central Bank of India. The bank guarantees were issued on behalf of the Corporate Debtor under the terms of the Indian Oil Corporation Limited (“IOCL”) package for the Aishwarya Project at its Haldia Refinery in West Bengal. IOCL invoked the bank guarantee for breach of the contract.

The NCLT dismissed the application holding that the bank guarantees constitute an independent contract between the banks and the applicant, and if the transaction is not hit by Section 14 of the IBC, the banks are obligated to honour IOCL’s request for invocation.

Aggrieved, IDBI Bank filed the appeal before the NCLAT on the grounds that (a) advance bank guarantees are not the same as performance bank guarantees and hence, cannot be invoked during moratorium; (b) the advance bank guarantee had been wrongly utilized by IOCL (contrary to the terms of the guarantee); and (c) IOCL and the Corporate Debtor had fraudulently misused the advance bank guarantees in contravention of the terms of bank guarantee, as well as the terms of their own inter-se contract.

### **Issue**

Whether bank guarantees can be invoked/ encashed during moratorium under Section 14 of the IBC?

---

<sup>1</sup> IDBI Bank v. Indian Oil Corporation Ltd. & Anr., judgement dated January 10, 2023 in Company Appeal (AT) (Insol.) No.543 of 2021, NCLAT, New Delhi

## Findings and Rationale

The NCLAT dismissed the appeal challenging NCLT's decision not to interfere with the encashment/ invocation of the bank guarantees.

The NCLAT held that an irrevocable and unconditional bank guarantee can be invoked even during moratorium period in view of the amended provision under Section 14 (3) (b) of the IBC<sup>2</sup>, for the following reasons:

1. Bank guarantees are outside the scope of the moratorium under Section 14 of the IBC and Section 3 (31)<sup>3</sup> of the IBC specifically excludes performance bank guarantees, hence, the encashment of the bank guarantee was legal and valid.
2. Whenever a bank guarantee is sought to be encashed, the bank is bound to honour the bank guarantee irrespective of any dispute raised by the customer (at whose instance the guarantee was issued) against the beneficiary<sup>4</sup>.
3. There was no reason to interfere with the encashment of advance bank guarantees by IOCL as there was no injustice or harm caused to it by the encashment. Hence, there is also no reason to delve into the objections regarding breach and fraud, particularly since IDBI Bank had itself had not taken any action with respect to the issue of fraud raised by it. Even otherwise, it is settled law that the NCLT has no jurisdiction to decide the question of disputes and claims/ counter claims<sup>5</sup>.
4. Moreover, the same bank guarantees were also subject matter of dispute in the arbitration proceedings between IOCL and the Corporate Debtor, where also the Arbitral Tribunal had dismissed the Section 17 application seeking stay on encashment (which order had attained finality) while specifically dismissing the Section 14 moratorium objection raised in those proceedings also.

## JSA Comment

5. In 2018, the amendment to Section 14 made the moratorium under IBC inapplicable to contracts of surety, and being a clarificatory amendment, it is applied retrospectively<sup>6</sup> by courts<sup>7</sup>.
6. This decision clarifies (though not explicitly) that the inapplicability of moratorium also extends to advance bank guarantees also since the provision excludes the broad category of 'contracts of surety'.
7. This position originates from the contract law principles of co-extensive liabilities of guarantees which is applied under the IBC to prevent guarantors (personal and corporate) from escaping their independent repayment liabilities. Marrying this with the concept of the IBC moratorium, i.e., to safeguard the dissipation of the Corporate Debtor's assets during the CIRP, the rationale to exclude guarantees from the purview of the moratorium is that the guarantees are issued by independent third parties, which are outside the purview of the IBC regime and therefore, the IBC proceedings against the Corporate Debtor will not be affected by action of third-party sureties.

---

### <sup>2</sup> "Section 14. Moratorium

(1) Subject to provisions of sub-sections (2) and (3), on the insolvency commencement date, the Adjudicating Authority shall by order declare moratorium for prohibiting all of the following, namely: -

... (c) any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (54 of 2002);

... (3) The provisions of sub-section (1) shall not apply to —

... (b) a surety in a contract of guarantee to a corporate debtor."

<sup>3</sup> 3 (31) "security interest" means right, title or interest or a claim to property, created in favour of, or provided for a secured creditor by a transaction which secures payment or performance of an obligation and includes mortgage, charge, hypothecation, assignment and encumbrance or any other agreement or arrangement securing payment or performance of any obligation of any person:

Provided that security interest shall not include a performance guarantee;

<sup>4</sup> U.P. Cooperative Federation Ltd. vs. Singh Consultants and Engineers Pvt. Ltd., [(1988 1 SCC 174]

<sup>5</sup> Dynepro Pvt. Ltd. vs. V. Nagarajan, CA (AT) (Insol.) No.229 of 2018 dated January 30, 2019, NCLAT, New Delhi; affirmed by Supreme Court in Civil Appeal No.2391 of 2019

<sup>6</sup> State Bank of India v. V. Ramakrishnan, (2018) 17 SCC 394

<sup>7</sup> Bharat Aluminium Co. Ltd. v. JP Engineers Pvt. Ltd., CA (AT) (Insol.) No.759 of 2020 dated February 26, 2021, NCLAT, New Delhi

## Insolvency and Debt Restructuring Practice

JSA is recognized as one of the market leaders in India in the field of insolvency and debt restructuring. Our practice comprises legal professionals from the banking & finance, corporate and dispute resolution practices serving clients pan India on insolvency and debt restructuring assignments. We advise both lenders and borrowers in restructuring and refinancing their debt including through an out-of-court restructuring as per the guidelines issued by the Reserve Bank of India, asset reconstruction, one-time settlements as well as other modes of restructuring. We also regularly advise creditors, bidders (resolution applicants), resolution professionals as well as promoters in connection with corporate insolvencies and liquidation under the IBC. We have been involved in some of the largest insolvency and debt restructuring assignments in the country. Our scope of work includes formulating a strategy for debt restructuring, evaluating various options available to different stakeholders, preparing and reviewing restructuring agreements and resolution plans, advising on implementation of resolution plans and representing diverse stakeholders before various courts and tribunals. JSA's immense experience in capital markets & securities, M&A, projects & infrastructure and real estate law, combined with the requisite sectoral expertise, enables the firm to provide seamless service and in-depth legal advice and solutions on complex insolvency and restructuring matters.

This Prism has been prepared by:



**Dheeraj Nair**  
Partner



**Vishrutyi Sahni**  
Partner

For more details, please contact [km@jsalaw.com](mailto:km@jsalaw.com)

---

[www.jsalaw.com](http://www.jsalaw.com)



17 Practices and  
24 Ranked Lawyers



16 Practices and  
11 Ranked Lawyers



7 Practices and  
2 Ranked Lawyers



11 Practices and  
39 Ranked Partners  
**IFLR1000 APAC Rankings 2022**

-----  
Banking & Finance Team  
of the Year

-----  
Fintech Team of the Year

-----  
Restructuring & Insolvency  
Team of the Year



Among Top 7 Best Overall  
Law Firms in India and  
10 Ranked Practices

-----  
13 winning Deals in  
IBLJ Deals of the Year

-----  
10 A List Lawyers in  
IBLJ Top 100 Lawyer List



Banking & Financial Services  
Law Firm of the Year 2022

-----  
Dispute Resolution Law  
Firm of the Year 2022

-----  
Equity Market Deal of the  
Year (Premium) 2022

-----  
Energy Law Firm of the Year 2021



**Ranked #1**  
**The Vahura Best Law Firms to**  
**Work Report, 2022**

-----  
Top 10 Best Law Firms for  
Women in 2022



Ahmedabad | Bengaluru | Chennai | Gurugram | Hyderabad | Mumbai | New Delhi



This prism is not an advertisement or any form of solicitation and should not be construed as such. This prism has been prepared for general information purposes only. Nothing in this prism constitutes professional advice or a legal opinion. You should obtain appropriate professional advice before making any business, legal or other decisions. JSA and the authors of this prism disclaim all and any liability to any person who takes any decision based on this publication.