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Petition under Section 95 of Insolvency and Bankruptcy Code, 2016 is not maintainable against a partnership firm or its partners

On March 6, 2024, the Hon'ble High Court of Karnataka ("Karnataka HC"), in the case of *M/S Manyata Realty vs. The Registrar and Ors*¹, held that the National Company Law Tribunal ("NCLT") does not have jurisdiction to entertain a petition filed under Section 95 of the Insolvency and Bankruptcy Code, 2016 ("IBC") against a partnership firm or its partners. The Karnataka HC declared the filing of the petition as *non-est* and illegal.

Brief facts

1. M/s Manyata Realty, a partnership firm ("**Firm**"), had entered into distinct joint development agreements with Buoyant Technology Constellation Private Limited ("**Company**" and together with the Firm referred to as the "**Parties**") between 2010 and 2015. Subsequently, a dispute arose between the Parties, leading to the Firm issuing a notice to: (a) terminate the joint development agreement; and (b) claiming damages on account of breach of the agreement. In order to resolve the dispute between the Parties, arbitration proceedings were initiated in 2022.
2. Thereafter, the Company issued a legal notice, invoking Section 95 of the IBC, against the Firm and its partners, demanding the Firm to repay its dues. Even though the Firm denied the claim made by the Company, a petition was filed before the NCLT.
3. Aggrieved by the filing before NCLT, the Firm and its partners filed separate writ petitions, under Articles 226 and 227 of the Constitution of India, before the Karnataka HC ("**Writ Petitions**"), challenging the jurisdiction of NCLT to entertain/ even number the Petition filed by the Company.
4. The Firm argued that the IBC does not cover insolvency resolution for individuals and partnership firms, and that jurisdiction should lie with the Debts Recovery Tribunal ("**DRT**") or Debts Recovery Appellate Tribunal. It contended that only personal guarantors to corporate debtors can be brought under Section 90 of the IBC, and since the firm and its partners are neither a personal guarantor nor a corporate debtor, the petition filed under Section 95 of the IBC is outside the NCLT's jurisdiction and should be dismissed, allowing arbitration proceedings to continue.

Issues

¹ Writ Petition No. 26977 of 2023

Whether a petition under Section 95 of the IBC can be numbered and maintainable against a partnership firm or its partners?

Analysis and findings

The Karnataka HC, after appreciating the submissions advanced by the Parties and having regard to settled law, held as follows:

1. the Karnataka HC after analysing the definitions of 'corporate person' and 'corporate debtor' under Section 3(7) and 3(8) of the IBC, held that: (a) IBC is applicable when a corporate person owes debt to any person; (b) except as provided in Part-III of IBC, partnership firm and/or its partners are not covered within the ambit of IBC. Further, the DRT is the adjudicating authority for the partnership firm and/or its partners;
2. the Karnataka HC observed that filing a petition under Sections 94 or 95 of the IBC triggers Section 96 of IBC immediately, leading to significant consequences. An interim moratorium is automatically imposed, freezing the corporate debtor's activities. This moratorium also affects all partners of a firm as of the application date. Additionally, a resolution professional is appointed to handle the proceedings and must submit a report within 10 (ten) days. These consequences occur upon filing the application, not when the application is entertained by the NCLT. The DRT is the authority to entertain such applications under Part III of the IBC. Once a petition is registered under Section 95 of the IBC before the NCLT (even before it is entertained by NCLT), interim moratorium and appointment of a Resolution Professional is axiomatic. Thus, the consequence of filing such petition is dire on the Corporate Debtor as there is no requirement under the IBC for NCLT to entertain the petition in order for other provisions under the IBC to come into effect;
3. NCLT cannot decide the issue of its jurisdiction to entertain the petition under Section 95 of the IBC since the filing of the Petition itself leads to dire consequences. Further, the petition is not eligible for submission before the NCLT and cannot be allowed to be proceeded up to the stage of determining whether such filings are entertainable; and
4. the Karnataka HC held that the maintainability of the petition before the DRT is crucial, as it pertains to the NCLT's jurisdiction to entertain the petition, which IBC does not permit. Even the acceptance of filing by the NCLT is contrary to law. As a result, the Writ Petitions were allowed by the Karnataka HC, and the e-filing of petitions by the Company under Section 95 of the IBC, was declared illegal and non-est. All proceedings before the NCLT were quashed, and the Firm was entitled to all consequential benefits from the setting aside of these proceedings. The Karnataka HC also directed that any action taken on the registration of the proceedings also stood obliterated.

Conclusion

This judgment clarifies the jurisdictional scope of the NCLT under the IBC. It underscores the principle that the jurisdiction of a tribunal is determined by the statute that governs it. The decision is significant as it protects partnership firms and their partners from insolvency proceedings under Section 95 of the IBC before the NCLT. It also highlights the importance of correctly identifying the appropriate forum for legal proceedings.

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