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Interim moratorium under the Insolvency and Bankruptcy Code, 2016 does not bar execution of regulatory penalties against the personal guarantor

The Supreme Court of India ("**Supreme Court**") recently in the case of ***Saranga Anilkumar Aggarwal vs. Bhavesh Dhirajlal Sheth and Ors.***[1], held that the interim moratorium on personal guarantors under Section 96 of the Insolvency and Bankruptcy Code, 2016 ("**IBC**") does not extend to regulatory penalties (such as those imposed under consumer protection laws). This judgment reaffirms that such penalties remain enforceable despite the ongoing insolvency process.

Brief facts

Several homebuyers ("**Respondent Nos. 1 and 2**") filed consumer complaints before the National Consumer Disputes Redressal Commission ("**NCDRC**") against East & West Builders (RNA Corp. Group Co.) ("**Appellant**"), a real estate developer. The complaints were arising out of the Appellant's failure to deliver possession of residential units within the agreed timeline. By final judgment and order dated August 10, 2018, the NCDRC imposed 27 (twenty-seven) penalties on the Appellant for deficiency in service and directed the Appellant to complete construction, obtain occupancy certificates, and hand over possession of residential units to the homebuyers.

Respondent Nos. 1 and 2, as decree holders, filed execution applications before the NCDRC, seeking enforcement of the penalty orders, since the Appellant failed to comply with the NCDRC's directions.

Subsequently, an application under Section 95 of the IBC was filed against the Appellant, triggering an interim moratorium under Section 96 of the IBC.

Accordingly, the Appellant filed an application before the NCDRC seeking a stay of the execution proceedings, on the grounds that the interim moratorium barred further legal actions. By order dated February 7, 2024, the NCDRC rejected the Appellant's application, holding that consumer claims and penalties did not fall within the scope of the moratorium under the IBC.

Aggrieved, the Appellant challenged the NCDRC's decision by filing a civil appeal before the Supreme Court.

Issue

Does the interim moratorium under Section 96 of the IBC extend to regulatory penalties imposed by bodies like the NCDRC?

[1] Civil Appeal No. 4048 of 2024, Supreme Court

Findings and analysis

The Supreme Court upheld the NCDRC's order dated February 7, 2024, and dismissed the Civil Appeal. It ruled that the interim moratorium under the IBC does not bar regulatory penalties imposed under the Consumer Protection Act, 2019. The Supreme Court reasoned as follows:

1. **Moratorium under IBC does not preclude the imposition of regulatory penalties**: The Supreme Court distinguished financial liabilities from regulatory penalties, holding that the moratorium provisions under IBC are intended to safeguard the financial viability of the debtors, but do not to exempt them from the legal consequences of statutory violations.

   The Supreme Court clarified that the penalties imposed by the NCDRC do not constitute recovery proceedings for financial debt by a creditor. Instead, these penalties serve as a punitive function to enforce statutory compliance and uphold public interest.

2. **Scope of moratorium under the IBC**: The Supreme Court clarified that Section 96 of the IBC imposes an interim moratorium only on legal proceedings concerning 'debt' when insolvency proceedings commence against individuals and personal guarantors. It was held that consumer protection penalties fall outside this definition, as they function to penalise unfair trade practices rather than enforce financial obligations.

   Similarly, the Supreme Court affirmed that the moratorium under Section 14, which applies to corporate debtors, does not cover criminal or regulatory penalties aimed at ensuring compliance with statutory mandates.

3. **IBC cannot serve as a shield against consumer protection laws**: The Supreme Court noted that staying regulatory penalties would establish a dangerous precedent, enabling insolvent entities to evade liability for consumer rights violations solely by invoking insolvency proceedings.

   The Supreme Court further clarified that the IBC seeks to only facilitate financial resolution. It does not absolve corporate debtors or individuals of their statutory obligations under consumer protection laws or other regulatory frameworks.

   Lastly, it was held that granting a moratorium on such penalties would undermine the consumer protection laws and diminish the accountability of developers towards homebuyers.

Conclusion

The Supreme Court ruled that the interim moratorium under Section 96 of the IBC does not protect regulatory penalties imposed under consumer protection laws. The Appellant was ordered to comply with the penalties within 8 (eight) weeks, reinforcing the principle that insolvency proceedings cannot be used as a mechanism to avoid statutory duties.

This judgment clarifies the boundaries of the IBC's moratorium provisions, ensuring that entities cannot exploit insolvency proceedings to avoid regulatory penalties. It upholds the integrity of consumer protection laws by affirming that penalties serving public interest are not to be stayed under the IBC moratorium. The decision also highlights the judiciary's commitment to preventing the misuse of legal frameworks, ensuring that insolvency mechanisms are not abused to circumvent statutory duties. Overall, the ruling reinforces the balance between facilitating corporate debt resolution and protecting consumer rights.

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