

Extinguishment of prior criminal liabilities of a Corporate Debtor: A safety armour for Resolution Applicants

The jurisprudence developing around the Insolvency & Bankruptcy Code, 2016 (hereinafter referred to as 'I & B Code') is, nowadays, focused on affording protection to resolution applicants from the criminal liabilities of corporate debtor in order to promote resolution of such distressed companies. The I & B Code has been subjected to several course corrections from the judiciary as well as the legislature. While the former is intervening in the form of landmark decisions such as in the case of *Venus Recruiters Private Limited v. Union of India & Ors.*¹, the latter has been actively remodelling the I & B Code in order to boost the confidence of the stakeholders as well as investors. One such amendment has come in the form of introduction of Section 32-A² into the I & B Code. The insertion of Section 32-A emanated came after several that are vying for assets being auctioned under the I & B Code expressed concern regarding getting into legal trouble over the cases against previous promoters, a concern which substantially surfaced in the light of *Bhushan Power and Steel Limited v. Mahendra Kumar Khandelwal*³. In fact, the Insolvency Law Committee descried the issue of prospective resolution applicants getting disincentivised on account of such impending legal scuffles and observed that if the cloud of suspicion shadows properties that are tainted as 'proceeds of crime', the object of value maximisation of the assets of the corporate debtor will be rendered a mirage.⁴

Chronology of Events

Since the inception of the I & B Code, the norm that has been persisting is that the initiation of insolvency has no affect on parallel criminal proceedings against the insolvent corporate person. Such a course had been carved by courts in catena of judgements qua Prevention of Money Laundering Act, 2002 (hereinafter referred to as 'PMLA') and the Negotiable Instruments Act, 1881 (hereinafter referred to as 'NIA'), wherein it has been consistently held that there is no conflict between the Code and criminal statutes. It was in the case of *Varrsana*

¹ 2020 SCC OnLine Del 1479

² Inserted vide Insolvency and Bankruptcy Code (Amendment) Act, 2020 dated 13th March, 2020.

³ 2019 SCC OnLine NCLAT 201

⁴ Para 17.9, Insolvency Law Committee Report (February, 2020)

*Ispat Limited v. Directorate of Enforcement*⁵ wherein the issue regarding interface between the I & B Code and PMLA arose before the Hon'ble NCLAT, where it was held that since the order of attachment was prior to the order of moratorium, the Enforcement Directorate could not be directed to release the properties so attached. Further, the NCLAT reiterated that Section 14 of the I & B Code does not apply to criminal proceedings, including acts having essence of a crime. The same position of law was reiterated in the cases of *Rotomac Global (P) Ltd. v. Directorate of Enforcement*⁶ and *Shweta Vishwanath Shirke v. Committee of Creditors*⁷, wherein the NCLAT recapitulated that if the assets of the Corporate Debtor are based on the proceeds of crime, then it is always open to Enforcement Directorate to seize the same and initiate action against PMLA. While the observation of the court seems to be sagacious, but in the process the Court overlooked that fact that mere attachment of property does not amount to conclusive finding that the assets so attached are 'proceeds of crime'.⁸ Having said that, if the court, at the time of conclusion of insolvency proceedings finds that the assets were not proceeds of crime, then it would taint the objective of maximisation of assets of the corporate debtor. In order to avoid such a situation, Section 32-A was inserted giving an overriding effect to the Code with respect to the criminal liabilities of the Corporate Debtor prior to commencement of insolvency proceedings. However, this provision only applies where there is a change in management and control of the Corporate Debtor. It further grants immunity against attachment of assets under PMLA, which are retained as 'proceeds of crime'. Seemingly, the amendment was made in light of the fact that a criminal case outlasts the time frame of 330 days envisaged under the I & B Code, and it may prove to be counter-productive and in effect, impose a practical problem in securing a time-bound and efficient insolvency resolution in absence of such immunity.

IBC and PMLA: CONFLICT or NO CONFLICT?

- *Non-Obstante Clauses in Both Statutes*

⁵ 2019 SCC OnLine NCLAT 236

⁶ 2019 SCC OnLine NCLAT 961

⁷ 2019 SCC OnLine NCLAT 1049

Since both the statutes encompass overriding clauses,⁹ any conflict arising between operation of the two leads to the question of supremacy between them. As a the principle of law endorsed by the doctrine of *lex posterior*, laws enacted later in time prevail over earlier laws, a stance that has been reiterated by the Hon'ble Supreme Court in the matter of ***Maruti Udyog v. Ram Lal & Ors.***¹⁰, wherein it was held that where two statutes contain non-obstante clause, the statute enacted later in time shall prevail over the earlier one. The NCLAT in the case of ***JSW Steel Ltd. v. Mahender Kumar Khandelwal & Ors.***¹¹ held that the insertion of Section 32A provides blanket immunity in respect of criminal liabilities of the corporate debtor, thereby extinguishing criminal prosecution under PMLA in respect of Corporate Debtor. The NCLAT in ***Directorate of Enforcement v. Manoj Kumar Agarwal & Ors.***¹² has upheld the primacy of the I & B Code over PMLA by virtue of Section 238 of the I & B Code, and it being a subsequent special legislation. Therefore, it is not *res integra* that the Code will prevail over the PMLA.

- ***'Appropriate Authority' to Decide the Matters Arising Out of Attachment of Assets of an Insolvent Company***

While the PMLA itself constitutes adjudicatory and appellate bodies, the contentions of the Enforcement Directorate that the such bodies are the 'appropriate authorities' for the purpose of adjudicating upon the matters relating to attachment of assets of an insolvent company has met with reluctance by the NCLAT in the matter of ***Directorate of Enforcement v. Manoj Kumar Agarwal & Ors.***¹³. Such contention is legally untenable as the I & B Code itself debars jurisdiction of other judicial bodies under Section 63 and bestows upon itself the ultimate jurisdiction with respect to any question of law or fact arising out of the insolvency proceedings of the Corporate Debtor under section 60(5) of the I & B Code.

- ***Proceedings Under PMLA: Criminal or Civil in Nature?***

⁹ Section 71 of PMLA and Section 238 of I & B Code.

¹⁰ (2005) 2 SCC 638

¹¹ Company Appeal (AT) (Insolvency) No. 957 of 2019

¹² MANU/NL/0144/2021

¹³ *Ibid*

As stated hereinbefore, the earlier position of non-applicability of the Code on PMLA emanated from proceedings under PMLA being criminal in nature. However, the NCLAT has substantially diverged from its earlier stance and observed the proceedings of attachment of assets as civil in nature.¹⁴ The NCLAT relied upon the ruling in the matter of *Pareena Swarup v. Union of India*¹⁵ wherein the Hon'ble Supreme Court, while deciding upon the nature of proceedings of attachment of assets involved in money laundering, held that “*the functions of Adjudicating Authority are civil in nature to the extent that it does not decide on the criminality of the offence nor does it have power to levy penalties or impose punishment.*” This decision of NCLAT is a milestone in resolving the conflict arising in, and from, intersection of both the statutes. In fact, as a corollary to this decision, it can be confidently said that there is no conflict between both the statutes.

- ***Applicability of Moratorium on Proceedings Under PMLA***

As a rule of interpretation of statutes, the bare wording of the legislation must be construed in tandem with the intention of the legislature. Section 14 of the I & B Code, imposing moratorium on suits and proceedings against the corporate debtor, is inserted with an intent to protect and preserve the assets of the corporate debtor to ensure its status as a going concern. Coherently interpreted, the attachment of assets by the Enforcement Directorate is, resultantly, barred by Section 14 read with Section 238 of the I & B Code. Any other construction of law shall be detrimental to the assets of the Corporate Debtor. Further, as stated above, the proceedings of attachment of assets under PMLA are civil in nature, which directly come under the moratorium envisaged under the I & B Code.

Conclusion

While Section 32-A of the I & B Code lucidly extinguishes criminal liability of corporate debtor on approval of resolution plan, the judgements put forth have resolved the conundrum with respect to interface between PMLA and the I & B Code before such resolution plan kicks in. The sanctity of the I & B Code has been upheld in primacy to other legislations,

¹⁴ *Ibid*

¹⁵ (2008) 14 SCC 107

and such steps are salutary, laying down stepping stones for achieving the ultimate objective of the I & B Code, that is, resolution of the insolvent and maximisation of its assets.