

Insolvency and Bankruptcy Code overrides the Customs law – SC

30 August 2022



Summary

The Supreme Court (SC) has held that the Insolvency and Bankruptcy Code, 2016 (IBC) will prevail over the Customs Act, 1962 for recovery of dues once the moratorium under the IBC is declared. The Customs authority can only determine the quantum of duties and levies but cannot initiate recovery proceedings by means of sale/confiscation under the Customs law. Once the insolvency proceedings are initiated under the IBC, the Interim Resolution Professional (IRP) can immediately secure the goods from the Revenue authorities and take appropriate steps under the IBC. The SC stated that after such assessment, the customs authorities must submit their claims to the adjudicating authority, for claiming the customs dues as operational debt under the IBC.

Facts of the case

- The Corporate Debtor¹ was in the business of shipbuilding and imported various materials under the Export Promotion Capital Goods Scheme (EPCG) regularly and stored such imported goods in Custom Bonded Warehouses.
- The appellant² was appointed as the IRP by the National Company Law Tribunal (NCLT) to initiate the Corporate Insolvency Resolution Process (CIRP) against the Corporate Debtor. The appellant informed the Revenue of the initiation of CIRP and sought custody of the warehoused goods and requested the Revenue not to dispose off or auction the same.
- The Revenue demanded custom duties from the Corporate Debtor on non-fulfillment of export obligations under the different EPCG licences.
- After initiation of the liquidation process, the appellant sought a direction against the Revenue to release the warehoused goods belonging to the Corporate

Debtor by filing an appeal before the NCLT³. The NCLT allowed the appeal and directed the Revenue to allow the appellant to remove the goods from the warehouse without any payment of customs duty.

- The Revenue filed an appeal before the National Company Law Appellate Tribunal (NCLAT) challenging the order passed by the NCLT.
- The NCLAT allowed the appeal filed by the Revenue and held that the Corporate Debtor had relinquished his title to the imported goods because they were not claimed.
- Being aggrieved, the appellant filed an appeal before the SC challenging the order passed by the NCLAT.

SC observations and ruling⁴:

- **Recovery proceedings under the customs law:** The proper officer can initiate proceedings under the customs law only when the importer has not taken sufficient steps for clearance of goods⁵. Further, the Revenue has not

¹ ABG Shipyard

² Sundaresh Bhatt, Liquidator of ABG Shipyard

³ u/s 60(5) of the IBC

⁴ Civil Appeal No. 7667 of 2021 dated 26 August 2022

⁵ Section 72 of the Customs Act, 1962

issued notices against the corporate debtor prior to initiation of the CIRP.

- **Purpose of moratorium under the IBC:** During the insolvency process, the adjudicating authority is required to declare the moratorium on the continuation or initiation of proceedings against the Corporate Debtor. The purpose of the moratorium is to keep the assets of the Corporate Debtor together during the insolvency process and to facilitate orderly completion of the process. Such measures ensure the curtailing of parallel proceedings and reduce the possibility of conflicting outcomes in the process. The moratorium should be continued even when the company goes into liquidation⁶.
- **IBC overrides other laws:** The provisions of the IBC clearly state that the code overrides the other laws which are inconsistent with IBC provisions⁷. Even the Customs law provides that the customs authorities would have first charge on the assets of an assessee under the Customs Act except with respect to cases under the IBC⁸. Therefore, the IBC clearly overrides the Customs Act.
- **Issuance of demand notices violates the provision of the IBC:** The demand notices are an initiation of legal proceedings against the Corporate Debtor. Therefore, the issuance of demand notices to seek enforcement of the custom dues during the moratorium period violates the provision of the IBC⁹.
- **Limitation on powers of the Revenue during moratorium:** The Revenue can only take steps to determine the tax, interest, fines, or any penalty which is

due. However, it cannot enforce a claim for recovery or levy interest on the tax due during the period of moratorium. Therefore, demand notices issued by the Revenue was in clear breach of moratorium.

- **No abandonment of goods:** There was no 'abandonment of goods' which would authorise the Customs Authorities to initiate the adjudicatory process to transfer title to themselves. No such adjudication or notice has been placed on record to suggest that such abandonment of the warehoused goods had taken place prior to the imposition of the moratorium. Such fact has been ignored by the NCLAT and, therefore, has rendered the moratorium *otiose*.
- **Appeal allowed:** The SC allowed the appeal filed by the appellant and set aside the impugned order of the NCLAT.

⁶ Section 33(5) of the IBC

⁷ Section 238 of the IBC

⁸ Section 142A of the Customs Act, 1962

⁹ Section 14 or 33(5) of the IBC

Our comments:

Earlier, in the case of Gujarat Urja Vikas Nikam Ltd, the SC had held that a harmonious construction of two special laws containing non-obstante clauses can be undertaken by looking at the purpose of both the laws. A special law enacted later prevails over the earlier special law. Therefore, the non-obstante clause under Section 174 of the Electricity Act would be overridden by Section 238 of IBC in case of a conflict of jurisdiction to resolve a dispute.

This is a significant ruling and in line with the above ruling, wherein the SC has held that once insolvency process has been initiated the IBC shall override any other enactment giving priority to the charges on the property of the Corporate Debtor. Post initiation of the insolvency process, the Revenue authorities do not have first right of recovery from assets of the Corporate Debtor under the IBC. It has further reiterated that the customs authorities have the powers to assess the quantum of dues, however, it does not have powers to initiate the recovery of dues under the Customs law.

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