

(2016) 04 AHC CK 0245
In the Allahabad High Court
Case No : Writ C No. 14923 of 2016.

Asset Reconstruction Company (India) Ltd. - Petitioner @HASH State of U.P. and Another

Date of Decision : 05-04-2016

Acts Referred:

Enforcement of Security Interest Act, 2002 — Section 13, Section 13, Section 14, Section 2, Section 3, Section 5

Citation : (2017) ACD 282 : (2017) 2 ADJ 211 : (2016) AIR(Allahabad) 200 : (2017) 1 AILLJ 595 : (2016) 119 ALR 372 : (2017) 1 DRTC 198 : (2017) 134 RD 102 : (2016) 2 RJ 1623

Hon'ble Judges : Krishna Murari and Vinod Kumar Misra, JJ.

Bench : Division Bench

Advocate : Ashutosh Kumar Pandey, Advocate, for the Petitioner; C.S.C, for the Respondent

Final Decision : Allowed

Judgement

1. Petitioner is a company incorporated under the Companies Act, 1956 and registered with the Reserve Bank of India under Section 3 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (for short the "SARFAESI Act, 2002") and thus is covered under the definition of Reconstruction Company and Securitisation Company as defined under the provisions of the SARFAESI Act.

2. Application made by the petitioner company under Section 14 of the SARFAESI Act seeking assistance from the District Magistrate in taking over possession of the secured asset was not being entertained and thus a representation was made pointing out that since the petitioner being a Securitisation and Assets Reconstruction Company, on being assigned rights and interest, created in favour of any bank or financial institution in any loan or advance granted or created, steps into the shoe of the lender and is entitled to make application under Section 14. On the said representation, the Additional District Magistrate (Finance & Revenue) submitted a report dated 18.6.2014 to the effect that since the petitioner company is not covered under the definition of "Financial

Institution" as defined under Section 2(m)(iv) of the SARFAESI Act, 2002 as it has not been notified as Financial Institution by the Central government, as such, it is not entitled to maintain a claim for enforcement of security interest provided by Section 13 of the SARFAESI Act as the said power can only be exercised by a secured creditor and for the said reason, the application made by the petitioner under Section 14 is not maintainable and not liable to be entertained. The District Magistrate vide order dated 23.8.2014 approved the report of the Additional District Magistrate.

3. Learned counsel for the petitioner contends that the petitioner being a registered Securitisation and Assets Reconstruction Company is entitled to acquire rights and interest any financial assets of the bank and financial institution under the provisions of the SARFAESI Act, 2002 and can enforce the same under Section 13 of the said Act and thus is entitled to maintain the application under Section 14 and the view of the respondents that application on behalf of the petitioner is not maintainable is per se illegal and without jurisdiction and against the provisions of the SARFAESI Act, 2002.

4. Question which arises for our consideration is whether a company which is registered as Securitisation and Assets Reconstruction Company with the Reserve Bank of India under the provisions of the SARFAESI Act, 2002 and not notified as financial institution by the Central Government is entitled to acquisition of the rights or interest in financial assets and under Section 5 of the SARFAESI Act, 2002 and to enforce the security interest under section 13 after acquiring the rights or interest in the financial assets of the bank or financial institution.

5. In order to derive an answer to the question posed before us, it becomes necessary to analyse the Scheme of the Act.

6. SARFAESI Act, 2002 was enacted to regulate securitisation and reconstruction of financial assets and enforcement of security interest. The Act enables the banks and financial institution to realise the long term assets and to improve recovery of debts by exercising powers to take possession of securities, sell them and reduce the non-performing assets by adopting measures for recovery and reconstruction. The Act provides for setting up of Assets Reconstruction Company empowered to take possession of secured assets of the borrower with the right to transfer the same by way of lease assignment or sale. The Act also empowers the Assets Reconstruction Company to take over the management of the business of the borrower.

7. It is stated in the statement of object and reasons that existing legal framework relating to commercial transaction was not in consonance with the changing commercial transaction and could not keep pace with the changing commercial practise and financial sector reforms resulting in slow pace of recovery of defaulting loans and mounting levels of non-performing assets of banks and financial institutions. Based on the reports of the Narasimham Committee I & II and Andhyarujina Committee constituted by the Central

Government for the purpose of examining banking sector reforms suggested enactment of a new legislation for securitisation and empowering the banks and financial institutions to take possession of the securities and to sell them without intervention of the court, the Act was promulgated and enforced. The enactment provides for cumulative remedies to secured creditors and the object is recovery of debts by non-adjudicatory process.

8. Section 2(b) of the SARFAESI Act, 2002 defines asset reconstruction as under :

"Reconstruction" means acquisition of any securitisation company or reconstruction company of any right or interest of any bank or financial institution in any financial assistance for the purpose of realisation of such financial assistance.

9. Section 2(v) defines reconstruction company as under :

"reconstruction company" means a company formed and registered under the Companies Act, 1956 for the purpose of asset reconstruction.

10. "Securitisation Company" is defined under Section 2(za) as under :

"securitisation company" means any company formed and registered under the Companies Act, 1956 for the purpose of securitisation.

11. Section 2(ze) defines secured debt as a debt which is secured by any security interest.

12. Section 2(zf) defines security interest as right, title and interest of any kind whatsoever upon property, created in favour of any secured creditor and includes any mortgage, charge, hypothecation, assignment other than those specified in Section 31.

13. Section 2(z) defines securitisation to mean acquisition of financial assets by any securitisation company or reconstruction company from any originator, whether by raising of funds by such securitisation company or reconstruction company from qualified institutional buyers by issue of security receipts representing undivided interest in such financial assets or otherwise.

14. Section 2(f) defines word "borrower" to mean the principal borrower who is granted financial assistance by any bank or financial institution and includes a guarantor or a mortgagor as well as a pledger. It also includes a person who becomes a borrower of asset reconstruction company consequent upon acquisition by it of the rights or interest of any bank or financial institution in relation to financial assistance.

15. Section 2(l) defines financial asset to mean any debt or receivables. It includes a claim to any debt or receivables which may be secured or unsecured. It includes a mortgage, charge, hypothecation or pledge, as also any right or interest in the security underlying such debt or such receivables as well as any beneficial interest in the property. It also includes any financial assistance.

16. Section 5 of the SARFAESI Act, 2002 deals with the acquisition of rights or interest in the financial assistance by securitisation company or reconstruction company. The said Section reads as under :

"5. Acquisition of rights or interest in financial assets. - (1) Notwithstanding anything contained in any agreement or any other law for the time being in force, any securitisation company and reconstruction company may acquire financial assets of any bank or financial institution -

(a) by issuing a debenture or bond or any other security in the nature of debenture, for consideration agreed upon between such company and the bank or financial institution, incorporating therein such terms and conditions as may be agreed upon between them; or

(b) by entering into an agreement with such bank or financial institution for the transfer of such financial assets to such company on such terms and conditions as may be agreed upon between them.

(2) If the bank or financial institution is a lender in relation to any financial assets acquired under sub-section (1) by the securitisation company or the reconstruction company, such securitisation company or reconstruction company shall, on such acquisition, be deemed to be the lender and all the rights of such bank or financial institution shall vest in such company in relation to such financial assets.

(3) Unless otherwise expressly provided by this Act, all contracts, deeds, bonds, agreements, powers-of-attorney, grants of legal representation, permissions, approvals, consents or no-objections under any law or otherwise and other instruments of whatever nature which relate to the said financial asset and which are subsisting or having effect immediately before the acquisition of financial asset under sub-section (1) and to which the concerned bank or financial institution is a party or which are in favour of such bank or financial institution shall, after the acquisition of the financial assets, be of as full force and effect against or in favour of the securitisation company or reconstruction company, as the case may be, and may be enforced or acted upon as fully effectually as if, in the place of the said bank or financial institution, securitisation company or reconstruction company, as the case may be, had been a party thereto or as if they had been issued in favour of securitisation company or reconstruction company, as the case may be.

(4) If, on the date of acquisition of financial asset under sub-section (1), any suit, appeal or other proceedings of whatever nature relating to the said financial asset is pending by or against the bank or financial institution, save as provided in the third proviso to sub-section (1) of Section 15 of the Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986) the same shall not abate, or be discontinued or be, in any way, pre-judicially affected by reason of the acquisition of financial asset by the securitisation company or reconstruction company, as the case may be, but the suit, appeal or other proceeding may be

continued, prosecuted and enforced by or against the securitisation company or reconstruction company, as the case may be.

(5) On acquisition of financial assets under sub-section (1), the securitization company or reconstruction company, may with the consent of the originator, file an application before the Debts Recovery Tribunal or the Appellate Tribunal or any court or other Authority for the purpose of substitution of its name in any pending suit, appeal or other proceedings and on receipt of such application, such Debts Recovery Tribunal or the Appellate Tribunal or court or Authority shall pass orders for the substitution of the securitization company or reconstruction company in such pending suit, appeal or other proceedings."

17. An analysis of the definition of asset reconstruction, financial assistance, securitisation, reconstruction company and securitisation company, secured creditor and borrower contained in Section 2 of the SARFAESI Act, 2002 and provisions of Section 5 of the SARFAESI Act, 2002 clearly goes to show that an asset created in favour of the bank or financial institution by a borrower could be assigned to the asset management company or asset reconstruction company, which, in turn, steps into the shoes of the secured creditor namely; bank and financial institution.

18. Section 6 of the SARFAESI Act, 2002 provides for a notice to be given by the bank or financial institution of acquisition of the financial assets by securitisation company or reconstruction company to the concerned obligor and other concerned persons and also the concerned registering authority. Sub-section (2) of Section 6 provides that where such a notice of acquisition of financial assets under sub-section (1) is given by a bank or financial institution, the obligor on receipt of such notice is to make payment to the concerned securitisation company or reconstruction company and the same shall be in full discharge to the obligor from all liabilities in respect of such payment. It may be pertinent to notice at this stage that obligor has been defined under Section 2(q) to mean a person liable to the originator whether under a contract or otherwise, to pay a financial asset or to discharge any obligation in respect of a financial asset, whether existing, future, conditional or contingent and includes the borrower. The originator has been defined as the owner of the financial asset itself acquired by a securitisation company or reconstruction company for the purpose of securitisation and asset reconstruction.

19. Chapter III of SARFAESI Act, 2002 deals with the enforcement of security interest. Section 13 of the Act falling under the said Chapter begins with a non obstante clause. The said Section reads as under :

"13. Enforcement of security interest.-

(1). Notwithstanding anything contained in section 69 or section 69A of the Transfer of Property Act, 1882 (4 of 1882), any security interest created in favour of any secured creditor may be enforced, without the intervention of the court or tribunal, by such creditor in accordance with the provisions of this Act.

(2). Where any borrower, who is under a liability to a secured creditor under a security agreement, makes any default in repayment of secured debt or any instalment thereof, and his account in respect of such debt is classified by the secured creditor as non-performing asset, then, the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within sixty days from the date of notice failing which the secured creditor shall be entitled to exercise all or any of the rights under sub-section (4).

(3) The notice referred to in sub-section (2) shall give details of the amount payable by the borrower and the secured assets intended to be enforced by the secured creditor in the event of non-payment of secured debts by the borrower.

(3A) If, on receipt of the notice under sub-section (2), the borrower makes any representation or raises any objection, the secured creditor shall consider such representation or objection and if the secured creditor comes to the conclusion that such representation or objection is not acceptable or tenable, he shall communicate (within fifteen days) of receipt of such representation or objection the reasons for non-acceptance of the representation or objection to the borrower.

Provided that the reasons so communicated or the likely action of the secured creditor at the stage of communication of reasons shall not confer any right upon the borrower to prefer an application to the Debts Recovery Tribunal under section 17 or the Court of District Judge under section 17A.

(4) In case the borrower fails to discharge his liability in full within the period specified in sub-section (2), the secured creditor may take recourse to one or more of the following measures to recover his secured debt, namely:-

(a) take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realising the secured asset;

(b) take over the management of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realising the secured asset;

Provided that the right to transfer by way of lease, assignment or sale shall be exercised only where the substantial part of the business of the borrower is held as security for the debt:

Provided further that where the management of whole, of the business or part of the business is severable, the secured creditor shall take over the management of such business of the borrower which is relatable to the security or the debt;

(c) appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;

(d) require at any time by notice in writing, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may

become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

(5) Any payment made by any person referred to in clause (d) of sub-section (4) to the secured creditor shall give such person a valid discharge as if he has made payment to the borrower.

(5A) Where the sale of an immovable property, for which a reserve price has been specified, has been postponed for want of a bid of an amount not less than such reserve price, it shall be lawful for any officer of the secured creditor, if so authorised by the secured creditor in this behalf, to bid for the immovable property on behalf of the secured creditor at any subsequent sale.

(5B) Where the secured creditor, referred to in sub-section (5A), is declared to be the purchaser of the immovable property at any subsequent sale, the amount of the purchase price shall be adjusted towards the amount of the claim of the secured creditor for which the auction or enforcement of secured interest is taken by the secured creditor, under sub-section (4) of section 13.

(5C) The provisions of section 9 of the Banking Regulation Act, 1949 (10 of 1949) shall, as far as may be, apply to the immovable property acquired by secured creditor under sub-section (5A).

(6) Any transfer of secured asset after taking possession thereof or take over of management under sub-section (4), by the secured creditor or by the manager on behalf of the secured creditor shall vest in the transferee all rights in, or in relation to, the secured asset transferred as if the transfer had been made by the owner of such secured asset.

(7) Where any action has been taken against a borrower under the provisions of sub-section (4), all costs, charges and expenses which, in the opinion of the secured creditor, have been properly incurred by him or any expenses incidental thereto, shall be recoverable from the borrower and the money which is received by the secured creditor shall, in the absence of any contract to the contrary, be held by him in trust, to be applied, firstly, in payment of such costs, charges and expenses and secondly, in discharge of the dues of the secured creditor and the residue of the money so received shall be paid to the person entitled thereto in accordance with his rights and interests.

(8) If the dues of the secured creditor together with all costs, charges and expenses incurred by him are tendered to the secured creditor at any time before the date fixed for sale or transfer, the secured asset shall not be sold or transferred by the secured creditor, and no further step shall be taken by him for transfer or sale of that secured asset.

(9) In the case of financing of a financial asset by more than one secured creditors or joint financing of a financial asset by secured creditors, no secured creditor shall be entitled to exercise any or all of the rights conferred on him under or pursuant to sub-section (4) unless exercise of such right is agreed upon

by the secured creditors representing not less than [sixty per cent] in value of the amount outstanding as on a record date and such action shall be binding on all the secured creditors:

Provided that in the case of a company in liquidation, the amount realised from the sale of secured assets shall be distributed in accordance with the provisions of section 529A of the Companies Act, 1956 (1 of 1956):

Provided further that in the case of a company being wound up on or after the commencement of this Act, the secured creditor of such company, who opts to realise his security instead of relinquishing his security and proving his debt under proviso to sub-section (1) of section 529 of the Companies Act, 1956 (1 of 1956), may retain the sale proceeds of his secured assets after depositing the workmen's dues with the liquidator in accordance with the provisions of section 529A of that Act:

Provided also that the liquidator referred to in the second proviso shall intimate the secured creditors the workmen's dues in accordance with the provisions of section 529A of the Companies Act, 1956 (1 of 1956) and in case such workmen's dues cannot be ascertained, the liquidator shall intimate the estimated amount of workmen's dues under that section to the secured creditor and in such case the secured creditor may retain the sale proceeds of the secured assets after depositing the amount of such estimated dues with the liquidator:

Provided also that in case the secured creditor deposits the estimated amount of workmen's dues, such creditor shall be liable to pay the balance of the workmen's dues or entitled to receive the excess amount, if any, deposited by the secured creditor with the liquidator:

Provided also that the secured creditor shall furnish an undertaking to the liquidator to pay the balance of the workmen's dues, if any.

Explanation.-For the purposes of this sub-section,-

(a) "record date" means the date agreed upon by the secured creditors representing not less than [sixty per cent] in value of the amount outstanding on such date;

(b) "amount outstanding" shall include principal, interest and any other dues payable by the borrower to the secured creditor in respect of secured asset as per the books of account of the secured creditor.

(10) Where dues of the secured creditor are not fully satisfied with the sale proceeds of the secured assets, the secured creditor may file an application in the form and manner as may be prescribed to the Debts Recovery Tribunal having jurisdiction or a competent court, as the case may be, for recovery of the balance amount from the borrower.

(11) Without prejudice to the rights conferred on the secured creditor under or

by this section the secured creditor shall be entitled to proceed against the guarantors or sell the pledged assets without first taking any of the measures specified in clauses (a) to (d) of sub-section (4) in relation to the secured assets under this Act.

(12) The rights of a secured creditor under this Act may be exercised by one or more of his officers authorised in this behalf in such manner as may be prescribed.

(13) No borrower shall, after receipt of notice referred to in sub-section (2), transfer by way of sale, lease or otherwise (other than in the ordinary course of his business) any of his secured assets referred to in the notice, without prior written consent of the secured creditor.

20. Section 14 of the Act empowers the secured creditor to take assistance from the District Magistrate of the District where the secured asset is situate and also of Chief Metropolitan Magistrate in case of a Metropolitan area in taking possession of the same.

21. The object and reason of enactment of SARFAESI Act, 2002 is to enforce the interest in the financial asset belonging to the bank or the financial institution by virtue of contract between the parties. An analysis of Section 13 quoted above when read with object and reasons makes it clear that the object of SARFAESI Act, 2002 is recovery by non adjudicatory process. A secured asset as defined under the Act is an asset in which interest is created by the borrower in favour of the bank or financial institution on the basis of which they can enforce the security interest for realisation of their outstanding by non adjudicatory process. Essentially, the SARFAESI Act, 2002 deals with the rights of the secured creditor and proceeds on the premises that debtor has not only failed to repay the debt but also to maintain the level of margin.

22. Section 13(1) and (2) of the SARFAESI Act, 2002 quoted above proceeds on the basis that security interest needs to be enforced expeditiously without intervention of the court or any tribunal. The legislative purpose for conferring the power on the secured creditor to enforce its security interest by taking recourse to Section 13(4) of the SARFAESI Act, 2002 without intervention of the court is to free the secured creditor of the impediment contained in Section 69 of the Transfer of Property Act. Under the provisions of the SARFAESI Act, 2002, a secured creditor is empowered by virtue of section 13 of the said Act to take any of the measure including the sale of secured assets without intervention of the court and notwithstanding the limitation of Section 69 of the Transfer of Property Act. As would be evident from perusal of statement of object and reasons of the Act, one of them is facilitating reconstruction of financial assets acquired by exercising powers of enforcement of securities or change of management or other powers which are proposed to be conferred on the banks and financial institutions. The scheme of the SARFAESI Act, 2002 makes it clear that it does not deal with the dispute between the secured creditors and the borrower and on

the contrary, it deals with the rights of the secured creditors. The Act proceeds on the basis that the liability of the borrower has crystallised and his account stands classified as non performing asset in the hands of bank or financial institution. Non performing account is an account which becomes nonviable and non performing in terms of the guidelines issued by the Reserve Bank of India. Such account is an asset available with the bank and financial institution as it represents a sum receivables and realisation by the bank or financial institution and in that sense it is an asset in the hands of the secured creditors. SARFAESI Act, 2002 was primarily enacted to reduce the non performing assets by adopting such measures for recovery which was fast and uninterrupted by any intervention of the court or tribunal but also for reconstruction. The Act clearly provides for setting up Assets Reconstruction Company, Securitisation Company etc. which are empowered to take possession of secured assets of the borrowers including the rights or transfer by way of lease, assignment and sale. It also provides for realisation of the amount due by sale of secured asset.

23. Under the provisions of the SARFAESI Act, 2002, all the rights vested in the secured creditors in respect of a non performing account which is a crystallised liability could be assigned to the Asset Management Company and Asset Reconstruction Company, which, in turn, steps into the shoe of the secured creditor namely, the bank or the financial institution. The same is clearly reflected from a bare reading of Section 5(2) of the SARFAESI Act, 2002 as well as the definition of the asset reconstruction contained in Section 2(b) and securitisation in Section 2(z) and Section 10 of the Act which prescribes the function of securitisation company and the reconstruction company under which it can act as an agent of any bank or financial institution for the purpose of recovering dues from the borrower on payment of such fee and charges as may be mutually agreed upon between the parties.

24. Aforesaid analysis of the scheme of the SARFAESI Act, 2002 clearly goes to show that all the rights which could be exercised by the secured creditor namely, the bank or financial institution can also be exercised by the securitisation or reconstruction company, once it acquires financial asset of any bank or financial institution, for the purpose of recovering their dues from the borrower.

25. In view of the aforesaid discussions, the only irresistible conclusion is that the rights of the secured creditor to take assistance either from the District Magistrate or the Chief Metropolitan Magistrate conferred by Section 14 of the Act could also be exercised by any securitisation or reconstruction company once it acquires the rights or interest in the financial assets of such bank or financial institution in accordance with the provisions of the SARFAESI Act, 2002 and there is no requirement for a securitisation or reconstruction company to be notified as a financial institution to exercise the rights.

26. Thus, the view taken by the Additional District Magistrate that since the petitioner company has not been notified as a financial institution by the Central Government, as such, it cannot maintain an application under Section 14 of the

SARFAESI Act is patently erroneous and cannot be sustained.

27. We are constrained to observe that the concerned authority failed to apply its mind to the various provisions of the SARFAESI Act, 2002 which have been discussed herein above. The asset reconstruction and securitisation is entirely different from a financial institution as defined under Section 2(m) of the Act. To function as Reconstruction and Securitisation Company, it only needs to be incorporated under the Companies Act, 1956 and obtain a certificate of registration as provided under Section 3 of the Act. There is no requirement for the Asset Reconstruction or Securitisation Company for declaration as financial institution to function under the provisions of the SARFAESI Act.

28. In view of above, the report of the Additional District Magistrate dated 18.6.2014 as well as the approval of the District Magistrate dated 21.6.2014 is not liable to be sustained and are hereby quashed.

29. Writ petition stands allowed.

30. A mandamus is issued commanding the District Magistrate, Agra to entertain the application made by the petitioner under Section 14 of the SARFAESI Act, 2002 and to decide the same in accordance with law expeditiously.