

**Course Name – B.A.LL.B 6<sup>th</sup> Sem**

**Subject – Competition Law**

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**Concept Covered - SARFAESI ACT, 2002**

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# Introduction

- The *Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act*, of 2002, allows banks and financial institutions to auction properties (residential and commercial) when borrowers fail to repay their loans.
- Was amended in 2004.
- It enables banks to reduce their non-performing assets (NPAs) by adopting measures for recovery or reconstruction.

- Upon loan default, banks can seize the securities (except agricultural land) without intervention of the court.
- SARFAESI is effective only for secured loans where bank can enforce the underlying security (eg. hypothecation, pledge and mortgages.)
- In such cases, court intervention is not necessary, unless the security is invalid or fraudulent.
- However, if the asset in question is an unsecured asset, the bank would have to move the court to file civil case against the defaulters.

# History

- ❖ Before SARFAESI Act, **RECOVERY OF DEBTS DUE TO BANKS AND FINANCIAL INSTITUTIONS ACT** of 1993, was used for recovery of default loans.
- ❖ It had various features such as Debt Recovery Tribunals and Debt Recovery Appellate Tribunals.
- ❖ However there were several loopholes, that were misused by the borrowers as well as the lawyers.
- ❖ This led to the Govt to introspect the act and to reform it. Hence another committee led by Mr. Andhyarujina was appointed.
- ❖ This committee recommended various new legislations to empower banks and other financial institutions to take possession of the NPAs.

# How it works?

- The SARFAESI Act, 2002 gives powers of "seize and desist" to banks.
- Banks can give a notice in writing to the defaulting borrower requiring it to discharge its liabilities within 60 days.
- If the borrower fails to comply with the notice, the Bank may take recourse to one or more of the following measures:
  - Take possession of the security for the loan
  - Sale or lease or assign the right over the security
  - Manage the same or appoint any person to manage the same.

The SARFAESI Act also provides for the establishment of Asset Reconstruction Companies (ARCs) regulated by RBI to acquire assets from banks and financial institutions.

The Act provides for sale of financial assets by banks and financial institutions to asset reconstruction companies (ARCs). RBI has issued guidelines to banks on the process to be followed for sales of financial assets to ARCs.

# Pre-conditions

The Act stipulates four conditions for enforcing the rights by a creditor:

- The debt is secured
- The debt has been classified as an NPA by the banks
- The outstanding dues are one lakh and above and more than 20% of the principal loan amount and interest there on.
- The security to be enforced is not an Agricultural land.

# Rights of the Borrower

- The borrowers can at any time before the sale is concluded, remit the dues and avoid losing the security.
- In case any unhealthy/illegal act is done by the Authorised Officer, he will be liable for penal consequences.
- The borrowers will be entitled to get compensation for such acts.
- For redressing the grievances, the borrowers can approach firstly the DRT and thereafter the DRAT in appeal. The limitation period is 45 days and 30 days respectively



# Methods of Recovery

This act makes provisions for two main methods of recovery of the NPAs as follows:

- **Securitisation:** the process of issuing marketable securities, backed by a pool of existing assets such as auto or home loans. After an asset is converted into a marketable security, it is sold. A securitization company or reconstruction company may raise funds from only the QIB (Qualified Institutional Buyers) by forming schemes for acquiring financial assets.
- **Asset Reconstruction:** Enacting SARFAESI Act has given birth to the Asset Reconstruction Companies in India. It can be done by either proper management of the business of the borrower, or by taking over it or by selling a part or whole of the business or by rescheduling of payment of debts payable by the borrower enforcement of security interest in accordance with the provisions of this Act.

# Resolution of Disputes

Where any dispute relating to securitisation or reconstruction or non-payment of any amount, arises amongst any of the parties:

Such dispute shall be settled by conciliation or arbitration as provided in the Arbitration and Conciliation Act, 1996 (26 of 1996), as if the parties to the dispute have consented in writing for determination of such dispute by conciliation or arbitration and the provisions of that Act shall apply accordingly.

# Special Situations

Provisions of this Act not to apply in certain cases:

- Any security interest for securing repayment of any financial asset not exceeding one lakh rupees.
- Any security interest created in agricultural land.
- Any case in which the amount due is less than twenty per cent of the principal amount.
- The SARFAESI Act is not applicable to NBFCs, however it is applicable to PFIs.

# CONCLUSION

- The high level of NPAs has led to lower interest income and loan loss provisioning requirements which reduced the profitability of the banks.
- The Act is intended to strengthen Banks and FIs to recover NPAs faster.
- The Act empowers banks and FIs to seize charged assets without Court's intervention and sell them off.



THANK YOU