

22. The securities and Reconstruction of Finance Assets and enforcement of Security Assets Act, 2002

Definitions

- **Assets reconstruction:** means acquisition by any securitisation company or reconstruction company of any right interests of any bank of financial institution in any financial assistance for the purpose of realisation of such financial assistance.
- **Borrower:** means any person who has been granted financial assistance by any bank or FI or who has given any grantee or created any mortgage or pledged as security for the financial assistance granted by bank or FI and includes a person who becomes borrower of securitisation company or reconstruction company upon acquisition by it of any rights or interests of any bank or FI in relation to such financial assistance.
- **Default:** means non-payment of principal debt or interest thereon or any other amount payable by a borrower to any secured creditor consequent upon which the account of such borrower is classified as non-performing asset in the books of account of the secured creditor.
- **Financial assistance:** means any loan or advantage granted by any debentures or bonds subscribed or any guarantees given or letters of credit established or any other credit facility extended by any bank or FI.
- **Financial Assets:** means debt or receivable includes:
 - ✓ A claim to any debt or receivables or part thereof, whether secured or unsecured;
 - ✓ Any debt or receivables secured by, mortgage of, or charge on, immovable property;
 - ✓ A mortgage, charge, hypothecation or pledge of movable property; or
 - ✓ Any right or interest in the security, whether full or part underlying such debt or receivables, or
 - ✓ Any beneficial interest in property, whether movable or immovable, or in such debt, receivables, whether such interest is exiting, future, accruing, conditional or contingent;
 - ✓ Any financial assistance.
- **Non-performing Assets:** means an asset or account of a borrower, which has been classified by a bank or FI as sub-standard, doubtful or loss assets,-
 - ✓ In case such bank or FI is administrated or regulated by any authority or body established, constituted or appointed by any law for the time being in force, in accordance with the direction or guidelines relating to assets classification issued by such authority or body;
 - ✓ In any other case, in accordance with the directions or guidelines relating to assets classification issued by the RBI.
- **Reconstruction Company:** means a company formed and registered under the companies act, 1956 for the purpose of asset reconstruction.
- **Scheme:** means a scheme inviting subscription to security receipts proposed to be issued by Securitisation Company or Reconstruction Company under that scheme.

Registration of Securitisation Company (SC) or Reconstruction Company (RC) (section 3)

- **Conditions;** not commence business without-
 - ✓ Obtaining a certificate of registration granted under this section; and
 - ✓ Having the owned fund of not less than Rs. 2 crore or such other amount not exceeding 15% of total financial assets acquired or to be acquired by the SC or RC, as the reserve bank may, by notification, specify.
- Time limit for making application is within 6 month if company already engage in such business before commencement of said Act.
- **Form and manner**
 - ✓ In such form as specify by RBI
- Condition for grant of certificate of registration

The RBI may, by an inspection of records or books of such SC or RC, or otherwise, that the following condition are fulfilled, namely

 - ✓ That the SC or RC has not incurred losses in any of the 3 preceding FYs.
 - ✓ That such RC or SC has made adequate arrangements for realisation of the financial assets acquired for the purpose of securitisation or asset reconstruction and shall be able to pay periodical returns and redeem on respective due date on the investments made in the company by the qualified institutional buyers or other person.
 - ✓ That the directors of SC or RC have adequate professional experience in matters related to finance, securitisation or reconstructions.
 - ✓ That the BOD of such SC or RC does not consist of more than half of its total number of directors who are either nominees of any sponsor or associated in any manner with the sponsor or any of its subsidiaries.
 - ✓ That any of its director has not been convicted of any offence involving moral turpitude;
 - ✓ That a sponsor, is not a holding company of the SC or RC company, as the case may be, or does not otherwise hold any controlling interest in such company.
 - ✓ That SC or RC has complied with or is in positions to comply with prudential norms specified by the RB.
 - ✓ That SC or RC has complied with one or more conditions specified in the guidelines issued by the RB for the said purpose.
- Grant of certificate
 - ✓ After satisfying above conditions
- Rejection of application
 - ✓ The RB may reject the application if he believes than condition are not satisfied
 - ✓ Opportunity for being heard given
- Prior approval of RB for certain changes
 - ✓ For substantial change in its management or change in location of its RO or change in its name.
 - ✓ 'Substantial change in management' means by way of transfer of shares or amalgamation of the business.
- 'Sponsor' means any person holding not less than 10% of the paid-up capital of a SC or RC.

Cancellation of certificate (Section 4)

➤ Circumstances

- ✓ Cease to carry on the business of securitisation or reconstruction;
- ✓ Ceases to receive or hold any investment from a qualified institute of buyer;
- ✓ Has failed to comply with any conditions subject to which the ROC has been granted to it; or
- ✓ At any time fails to fulfil any of the conditions referred at registration time;
- ✓ Fails to-
 - Company with any directions issued by RB;
 - Maintain accounts in accordance with the requirements of any law or any directions or order issued by the RB;
 - Submit or offer for inspection of BOA or other relevant documents when so determined by the RB; or
 - Obtain prior approval of the RB required under section 6
- A SC or RC can appeal against cancelation of registration to CG within 30 days.
- A SC or RC which s holding investment of qualified institutional buyers and whose application for registration has been rejected or COR has been cancelled shall, notwithstanding such rejection or cancellation, be deemed to be a SC or RC until it repays the entire investments held by it, within such period as the RB may direct.

Acquisition of rights or interest in financial assets (FA) (section 5)

- 1. Acquisition of FA:** notwithstanding anything contained in any law or agreement, any SC or RC may acquire FA of any bank or FI-
 - ✓ By issuing a debenture bond or any other security in the nature of the debenture, for consideration agreed upon between such company and the bank or FI, incorporating therein such terms and conditions as may be agreed upon between them; or
 - ✓ By entering into an agreement with such bank or FI for the transfer of such FA to such company on such terms and conditions as may be agreed upon between them.
- 2. Acquisition of rights**
 - a. If the bank or FI is a lender in relation to any FA acquired under sub section (1) by the SC or RC, such SC or RC shall, on such acquisition, be deemed to be the lender and all the rights of such bank or FI shall vest in such company in relation to such FA.
- 3. Enforcement**
 - ✓ After satisfying condition in an agreement or in any other manner after fulfil of condition SC or RC can use or acted as upon as fully and effectually as if, in the place of said bank or FI as the case may be.
- 4. Continuation of legal proceedings**
 - ✓ On the name of SC or RC if pending at the time of acquisition.

Measure for assets reconstruction (Section 9)

- The proper management of the business of the borrower, by change in, or take over of, the management of the business of the borrower;
- The sale or lease of a part or whole of the business of the borrower;
- Rescheduling of payment of debts payable by the borrower;
- Enforcement of security interests in accordance with the provisions of the act;

- Settlement of dues payable by the borrower;
- Taking possession of secured assets in accordance with the provisions of the act.

Other function of SC or RC (Section 10)

1. To act as agent, manager and receiver

- ✓ Act as an agent for any bank or FI for the purposes of recovering their dues from the borrower on payment of such fees or charges as may be mutually agreed upon between the parties;
- ✓ Act as a manager referred in clause (c) of the sub section (4) of section 13 on such fees as may be mutually agreed upon between the parties;
- ✓ Act as receiver if appointed by any court or tribunal.

2. No SC or RC shall act as a manager if acting as such gives rise to any pecuniary liability.

3. No business other than securitisation or reconstruction business

- ✓ Except as otherwise provide in section (1), no SC or RC which has been registered, shall commence carry on, without prior approval of the reserve bank, any business other than securitisation or asset reconstruction.

Provided that SC or RC which is carrying on, on or before the commencement of the act, any business other than, securitisation or assets reconstruction shall cease to carry on any business within 1 year from the date of enforcement of act.

Enforcement of Security interest (Section 13)

- No intervention of court or tribunal in enforcement of security (1)
 - ✓ SC or RC can create enforcement against any secured creditor without intervention of court or tribunal
- Notice to secured creditor to borrower to discharge liability within 60 days (2)
 - ✓ If secured creditor become NPA than they can give notice in writing for fulfilment of liability within 60 days
- Discoursed required in notice (3)
 - ✓ Amount payable by the borrower
 - ✓ Secured assets intended to be enforced by the secured creditor
- Secured creditor to consider the representation or objection of the borrower (3A)
 - ✓ After receiving notice he can make representation or object on notice
 - ✓ Provided that the reasons so communicated or the likely action of the secured creditor at the stage of communication reasons shall not confer any right upon the borrower to prefer an application to the debts recovery Tribunal under section 17
- Measure for secured creditor in case of default by the borrower (4)
 - 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 assets.
 - b. Take over the management of the business of the borrower including the right to transfer by way of lease, assignment or sale for realising the secured assets;
 - c. Appoint any person, 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.
- Any payment made by any person referred in (d) to the secured creditor shall give such a person valid discharge as if he has made payment to the borrower (5)
- Any transfer of secured assets to any other person is deemed to be transfer by its original owner (6)
- If any costs, or expenses incurred for action taken against borrower than all the expenses are reimbursed by borrower.
- No sale of secured asset if all dues paid to secured creditor before the date fixed for sale (8)
- In the case of financing if a FA by a more than one secured creditors or joint financing of a FA by a secured creditors, no secured creditor shall be entitled to exercise any or all of the rights conferred on him under or pursuant to this section unless exercise of such right is agreed upon by the secured creditors representing not less than 3.4th in value of the amount outstanding as on a record date and such action shall be binding on all the secured creditors. (9)
- In case if a company in liquidation, the amount realised on the sale of secured assets shall be distributed in accordance with the provisions of companies Act.
- 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 prescribed by Debts recovery Tribunal for balance amount.
- Without prejudice to the rights conferred on the secured creditor under or by this section, secured creditor shall be entitled to proceed against the guarantors or sell the pledged assets without first taking any of the measures specified in clause (a) to (d) of s/s 4 in relation to the secured assets under this act. (11)
- 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 (12)
- No borrower shall, after receipt of notice, transfer by way of sale, lease or otherwise any of his secured assets referred to in the notice.

Manner and effect of takeover of management (section 15)

- Notices in newspaper on takeover of management (1)
 - ✓ English and Indian language newspaper where principal office
- Consequences of publication of notice (2)
 - ✓ In the companies – all the person who has power related to control of the business are deemed to vacate their office after notice published.
 - ✓ Any contract of management shall be deemed to be terminated.
 - ✓ A person appointed for such administration is deemed to be a director, administrators of business, as the case may be from date of publication of notice
 - ✓ The directors appointed under this section shall, for all purposes, be the directors of the company of the borrower and he can alone exercise all the powers which referred in memorandum or AOA or not.

- Certain rights of shareholders suspended in case takeover of management (3): notwithstanding anything contained in the act or in AOA or memorandum of such borrower-
 - ✓ It shall not be lawful for the shareholders of such company or any other person to nominate or appoint any person to be a director of the company.
 - ✓ No resolution passed at any meeting of the shareholders of such company shall be given effect to unless approved by the secured creditor.
 - ✓ No proceedings for the winding up of such company or for the appointment of a receiver in respect thereof shall lie in any court, except with the consent of the secured creditor.
- Where the management of business is taken over by creditor, secured creditor shall, on realisation of debt in full, restore the management of the business of the borrower to him.

No compensation (Section 16)

- Notwithstanding anything contained in law or act or contract no director, manager or person is liable to claim for compensation for loss of office in case of takeover of management.
- Nothing contained in this section shall apply to any other sum other than remuneration to claim from borrower by manager, director or any other person.

Right to appeal (Section 17)

- Any person including borrower, aggrieved by any of the measures taken in s/s 4 of the section 13 taken by secured creditor or his authorised officer under this chapter, may prefer an appeal to the DRT having jurisdiction in the matter within 45 days from the date on which such measures had been taken.
- If the appeal is preferred by a borrower, such appeal is not entertained by the DRT unless the borrower has deposited with the DRT 75% of the amount claimed in the notice.
- However, the DRT may, waive or reduce the amount to be deposited, for reasons to be recorded in writing.

Appeal to AT (Section 18)

- If aggrieved from order of DRT, then make appeal to AT within 30 days from the receipt of the order of DRT.
- No appeals shall be entertained unless 50% of amount from him, as claimed by the secured creditors or determined by the DRT whichever is less to be deposited by borrower to the AT.
- The AT may, for the reasons to be recorded in writing reduce the amount to not less than 25%.
- AT may dispose the appeal in accordance with the provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 and rules there under.
- If the DRT on an application made under 17 or the AT on an appeal referred in section 18, holds that the possession of the secured assets by the secured creditor is not in accordance with the provisions of the act and rules there, then such borrower shall be entitled to payment of such compensation and costs may be determined by such DRT or AT. (Section 19)

Central registry (Section 20)

- HO and other office (2)
 - ✓ As specified by the CG

- Jurisdiction (3)
 - ✓ CG, by notification
- Provisions applicable to central registry in addition to other provisions (4)
 - ✓ Registration Act, 1908
 - ✓ The companies Act, 1956
 - ✓ The merchant shipping Act, 1958
 - ✓ The Patents Act, 1970
 - ✓ The Motor vehicles Act. 1988; and
 - ✓ The Designs Act, 2000
 - ✓ Or any other law requiring registration of charges and shall not affect the priority of charges or validity thereof under those acts or laws.

Central registrar (Section 21)

- Appointment of Central registrar by CG (1)
 - ✓ Appoint a person, for the purpose of registration of transaction relating to securitisation, reconstruction of assets and security interest created over properties, to be known as the central registrar.
- Appointment of other officers (2)
 - ✓ The CG may appoint such other officer with such designation as he thinks fit for discharge work of Central registrar.

Register of Securitisation, reconstruction and security interests, transaction (Section 22)

- Central register to be kept at HO (1)

Transaction relating to –

 - ✓ Securitisation of FA;
 - ✓ Reconstruction of FA; and
 - ✓ Creation of security assets.
- Notwithstanding anything contained in any law, it shall be lawful for the central registrar to keep the records wholly or partly in computer floppies, disk or in any other electronic form subject to such safeguards as may be prescribed.(2)
- The register shall be kept under the control and management of central registrar (4)

Offences and penalties

- **Penalties (Section 27):** if default is made –
 - ✓ In filing under section 23, the particulars of every transaction, or
 - ✓ In sending under section 24, the particulars of the modification referred to in that section; or
 - ✓ In giving intimation under section 25,

Than, every company and every officer of the company or the secured creditors and every officer of the secured creditor who is in default shall be punishable with fine which may extend to 5,000 rupees for every day during which the default continues.
- If any SC or RC fails to comply with any direction issued by RB u/s 12, shall be punishable with fine which may extend to 5,00,000 Rs. In the case of a continuing offence, with an additional fine which may extend to 10,000 for every day during the default continues. (section 28)

- If any person contravenes or attempts to contravene or abets the contravention of the provisions of this act, shall be punishable with imprisonment for a term which may extend to 1 year, or with fine, or with both. (section 29)
- No court inferior to that of a metropolitan magistrate or judicial magistrate of the first call shall try any offence punishable under this act. (section 30)

Provisions of this Act not to apply in certain cases (section 31)

- a. A lien on goods, money or security given by or under the Indian Contract Act, 1872 or the sale of Goods Act, 1930 or any other law for the time being in force;
- b. A pledge of movables within the meaning of the ICA, 1872;
- c. Creation of any security in any aircraft as defined in Aircraft Act, 1934;
- d. Creation of security interest in any vessel as defined in the Merchant Shipping Act, 1958;
- e. Any conditional sale, hire-purchase or lease or any other contract in which no security interest has been created;
- f. Any rights of unpaid seller under Sale of Goods Act, 1930;
- g. Any properties not liable to attachment or sale under the first proviso of CPC, 1908;
- h. Any security interest for securing repayment of any loan not exceeding Rs. 1 Lakh;
- i. Any security interest created in agricultural land;
- j. Any case in which the amount due is less than 25% of the principal amount and interest thereon.