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**BENEFITS OF ENFORCEMENT OF SECURITY INTEREST UNDER  
SECURITISATION ACT**

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**ABSTRACT**

*Under the provisions of Section 69 of Transfer of Property Act a mortgage can take possession of the mortgaged property and sell the same without intervention of court only in case of English mortgage. In addition, mortgage can take possession of mortgaged property where there is specific provision in mortgage deed and the mortgaged property is specific provision in mortgaged deed and the mortgaged property is situated in towns of Kolkata, Chennai and Mumbai. In other cases possession of property can be taken only with the intervention of Court.*

*Presently, there is no specific provision in law in respect of hypothecation, though hypothecation is one of the major Security interests taken by bank and financial institution. The Bill proposed to empower banks and financial institutions to take possession of Securities and sell them in case of default. Another working group of RBI was working on Asset Securitisation and drafted a Bill on Asset Securitisation. The idea is to handover the work of assets reconstruction to a specialized agency. The draft Bill containing provisions for Securitisation was submitted to the Government. Government combined these two drafts and prepared a combined Bill. However, without waiting for parliament Approval, an Ordinance titled, Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Ordinance 2002 has been promulgated on 21.06.2002. The Ordinance has been converted into a full-fledged Act in November 2002. It is briefly and popularly called as Securitisation Act.*

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**SECURITISATION ACT**

One of the major problems being faced by banks and the financial institutions in India is that of bad debts, known in glorified phrase as 'Non-Performing Asset' (NPAs) in the official banking terminology. There are various claims on the amount of NPAs in Indian banks and financial institutions. The amount ranges between Rs. 70,000 and 1,00,000 crore and unofficial sources of a credit rating agency claims it too much higher than this estimate.

Fortunately, the government was and is aware of the problems. But as it believes and does "better late than never". It did also the same in this context. First of all Sickness of Industrial Companies Act was enacted in 1986 to solve the problem of the sick companies. It not only failed to solve the problem of sick companies, but in fact helped in aggravating the problem of NPAs as companies found safe heaven and unlimited protection in Section 22 of the Act. This Act is likely to repeal and most of its provisions are to be incorporated in the Companies Act, 1956. The SICA was followed by Board for Industrial and Financial Reconstruction (BIFR). What it is doing today is proposed to be done by Company Law Tribunal? What improvement it will bring is anybody's guess? The BIFR was followed by 'Recovery of Debts Due to Banks and Financial Institutions Act' in 1993 to expedite the recovery. After some false start the Act is stabilizing. Results achieved by the formation of DRTs (Debt Recovery Tribunals) and ATs (Appellate Tribunals) under the Act can be said as moderately encouraging.

The Reserve Bank of India (RBI) is also taking various policy decisions to control the problem of NPAs. A OTS (One Time Settlement) scheme for the settlement of NPAs for small borrowers was introduced in 1997. Under this scheme public Sector banks could recover a total sum of Rs. 2192 crore in respect of 5.23 lakh accounts as on 30<sup>th</sup> June 2001. The scheme has not been extended. However, banks are free to design and implement their own policy for recovery and write-offs incorporating compromises and negotiated settlements, based on broad framework provided for settlement in the guidelines of 1995.

A CDR (Corporate Debt Restructuring) Scheme was also announced by RBI in the year 2001 but this is applicable only to the multi banking accounts with outstanding exposure of Rs. 20 crore and above with the banks and financial institutions. Considering the gravity of the situation about NPAs and to develop Securitisation market, the Government of India promulgated the "Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Ordinance 2002" and made effective on 21<sup>st</sup> June 2002. It is one more step in the direction of improving the health of banks and financial institutions by reducing NPAs.

This ordinance was later on converted into a full-fledged Act by the both houses of Parliament in November 2002. This Act has come to known as Securitisation Act.

### **OVERALL SCHEME OF THE ACT**

The Act is really 'two in one' Act. One aspect is in respect of enforcement of Security interest by Secured creditors (Banks and Financial Institutions) without intervention of court. Another aspect is transfer of the non-performing assets to Securitisation or reconstruction company, which will then dispose off those assets and realise the proceeds. These two aspects are almost independent of each other. Thus, it is possible for a Secured Creditor to take possession of assets and dispose off it himself, without handing it over to Securitisation or reconstruction company is at the option of the bank or financial institution

### **ENFORCEMENT OF SECURITY INTEREST**

The bank and financial institution always grant loans on the basis of Security. The Security may be in the form of mortgage, hypothecation, pledge, etc. In addition, personal guarantees of the directors, partners or group companies are obtained. Thus on paper, the lending by banks and financial institution appears to be very Secured. However, when the time comes, it is found that Security for loan is only on paper and is of no use in recovering the bad debts.

The Security, which the bank and financial institution has, is required to be enforced only through courts and now debt recovery tribunal also. Unfortunately, the experience is no satisfactory and must admit that judiciary, for whatever reasons, has not been able to meet the requirements of commerce and business where speed and prompt action is of utmost importance. NPAs are increasing to alarming levels. Some NPAs are because of business failures due to conditions beyond the control of management. In such cases entrepreneurs cannot be blamed much for defaults. However, some NPAs are because of unscrupulous management who misuse the funds or divert the funds elsewhere.

#### **When Security Can Be Enforced**

Section 13 (1) provides that notwithstanding anything contain in Section. 69 or Section 69A of Transfer of Property Act any Security interest can be enforced by Secured creditor without intervention of Court or Tribunal in accordance with provision of the Act. Section 13 (2) states that action can be taken only if there is default in repayment of installment of debt and the account is classified as NPA by the Secured creditor.

No action can be taken in case of (i) agricultural land, (ii) when amount due is less than Rs. 1,00,0000 (iii) when the amount due is less than 20 percent of the principal amount and

interest thereon. Similarly, no action can be taken if the debt is time barred u/s 36 under Limitation Act.

### **Initiation of Action for Enforcement of Security**

The action for enforcement of Security interest can be initiated u/s 13 (2) when a borrower, who is under liability of Secured creditor under a Security agreement, makes any default in repayment of Secured debt or any instalment thereof and his account is classified by the Secured creditor as non-performing asset, the Secured creditor may require the borrower by notice in writing to discharge the liability in full within 60 days from the date of notice failing which the Secured shall be entitled to exercise all or any of the rights specified in Section 3 (4) of the Act which are as follows:

- Take possession of the Secured asset of the borrower including the right to transfer by way of lease, assignment or sale for realising the Secured asset;
- Take over the management of Secured asset of the borrower including the right to transfer by way of lease, assignment or sale and realise the Secured asset;
- Appoint any person as manager who manage the Secured asset, the possession of which has been taken over by the Secured creditor; and
- Require at any time by notice in writing, any person who has acquired any of the Secured asset from the borrower and from whom any money is due or may become due to the borrower, to pay the Secured creditors, so much of the money as is sufficient to pay the Secured debt.

Thus, action for enforcement can be initiated only when following conditions are fulfilled :

(i) Borrower (ii) who is under a liability of Secured creditor (iii) under a Security agreement, (iv) makes default, (v) in repayment of Secured debt or instalment, and (vi) his account is classified by the Secured creditor as NPA. Unless all these conditions are fulfilled, no action can be initiated. Further as per Section 31, no action can be initiated if Security interest is less than Rs. 100,000 or when the amount due is less than 20 percent of the principal amount and interest thereon.

### **BENEFITS OF ENFORCEMENT OF SECURITY INTEREST –**

The query to the respondents was about the benefits brought by the enforcement of security interest in the legislation. The banks and financial institutions always grant loan on the basis of security. Security may be in the form of mortgage, hypothecation, pledge, etc. In addition, personal guarantees of the directors, partners, or group companies are obtained. Thus on paper, the lending by the banks and financial institutions appears to be very secured.

However, when the time comes, it is found that security for the loan is only on the paper and is of no use in recovering of the debts.

Before this legislation the security was required to be enforced only through courts and debt recovery tribunals. Unfortunately, the experience was not satisfactory and judiciary was not able to meet the requirements of commerce and business where speed and prompt action was of utmost importance. With the promulgation of this Act secured creditors can enforce the security directly, without the intervention of the court or tribunal, after giving 60 days notice under Section 13(1). If borrower doesn't pay the principal and interest as specified in the notice within 60 days the secured creditor can take possession of asset, takeover the management of asset and appoint any person to manage the asset, etc. under Section 13(4).

**TABLE**  
**Benefits of Enforcement of Security Interest**

Benefits	Status			
	Yes	No	Can't say	Total
(a) Removal of roads blocks and delays in recovery	45 (83.33)	6 (11.11)	3 (5.56)	54 (100)
(b) Creation of better understanding between lenders and Borrowers	33 (61.11)	12 (22.22)	9 (16.67)	54 (100)
(c) Lenders have an upper hand	29 (53.70)	18 (33.33)	7 (12.97)	54 (100)
(d) Seized assets will be productively utilized for stock holders	32 (59.26)	10 (18.52)	12 (22.22)	54 (100)
(e) Act is a deterrent to recalcitrant borrowers	37 (68.52)	12 (22.22)	5 (9.26)	54 (100)
(f) Lenders' right has recognised by the borrowers	43 (79.63)	3 (5.56)	8 (14.81)	54 (100)
(g) Improved value for both stockholders and depositors	30 (55.56)	12 (22.22)	12 (22.22)	54 (100)
(h) Financial resources of lenders have been enhanced	45 (83.33)	3 (5.56)	6 (11.11)	54 (100)
(i) Minimised cost for funding for borrowers	23 (42.59)	25 (46.30)	6 (11.11)	54 (100)
(j) Distressed credit problem is resolved	39 (72.22)	8 (14.81)	7 (12.97)	54 (100)
(k) Improved flow of capital	42 (77.78)	7 (12.96)	5 (9.26)	54 (100)
(l) Greater flexibility and efficiency in the system	45 (83.33)	3 (5.56)	6 (11.11)	54 (100)

Source: Sample Survey

Figures given in parentheses represent percentages

The introduction of this clause resulted into number of benefits listed in Table. The responses to these benefits have been summarised in the above said table. The Enforcement of Security Interest has resulted into benefits of 'removal of road blocks and delays in the recovery of loans', 'financial resources of the lenders enhanced' and 'greater flexibility and efficiency in the system' as 'affirmatively' admitted by highest percentage of respondents (83.33percent) for each benefit. 79.63 percent respondents felt that 'borrowers have recognised the lenders' right' followed by 'improved flow of capital' by 77.78 percent and 'problem of distressed credit has resolved' by 72.22 percent respondents and so on. The benefit 'cost of funding has been minimised for borrowers' was denied by 46.33 percent respondents. It shows that this benefit has not been approved by the respondents. 22.22 percent respondents preferred 'can't say' option for the benefit of 'improved value for both stock holders and depositors' and 'seized assets will be productively utilized for stockholders'.

On the basis of analysis, it may be concluded that Enforcement of Security Interest has resulted into various benefits to the lenders in varying degrees.

### **RESEARCH DESIGN**

The present study was undertaken for knowing the impact of Securitisation Legislation in the management of NPAs in selected financial institutions. To attain this target following banking institutions operating at their local, regional and zonal levels have been approached to provide the requisite data and information. Banks operating at all the three levels include State Bank of India, Oriental Bank of Commerce, Union Bank of India, Allahabad Bank, Bank of Baroda, Canara Bank and Punjab National Bank. Banks operating at two levels include Bank of India, Central Bank of India, Dena Bank, Punjab & Sind Bank, State Bank of Patiala, Syndicate Bank and Vijaya Bank. Banks operating at only one level include Andhra Bank, Bank of Maharashtra, Corporation Bank, Indian Bank, Indian Overseas Bank, United Bank of India and UCO Bank.

In all 54 bank branches of 21 public sector banks have been included in the study. The performance at national level of the banks under study has been already discussed in previous chapter while various aspects of NPAs and Securitisation Legislation have been enquired from the respondent banks situated in Haryana, Punjab, Delhi, U.P. and Chandigarh.



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