
THE BANKING REGULATION ACT, 1949

1. Introduction

The Banking Companies Act, presently known as Banking Regulation Act was enacted owing to safeguard the interest of the depositors, control abuse of powers by some bank personnel controlling the banks in particular and to the interest of Indian economy in general. However, it should be remembered that this Act is in addition to, and not, except as otherwise provided, in derogation of the Companies Act, 1956 and any other law for the time being in force. Since, some historic events took place in Indian Banking System, detailed discussion on the various provisions of the Act would leave some scope of incompleteness without mentioning those developments. The Social Control Act of 1968 under the leadership of the then Deputy Prime Minister, Mr. Morarji Desai was an amending act of the Banking Regulation Act. The followings were the main provisions of this amending Act:-

- Bigger banks have to be managed by whole time chairman possessing special knowledge and practical experience of the working of a banking company or of finance, economics or business administration.

- The majority of the directors had to be persons with special knowledge or practical experience in any of the areas such as accountancy, agriculture, rural economy, banking, co-operative, economics, finance, law, small scale industries.

- At least two directors had to possess special knowledge and practical experience in respect of agriculture, rural economy and co-operation.
The banks were also prohibited from making any loans or advances, secured or unsecured to their directors or to any companies in which they have substantial interest.

But, considering the social control measure as inadequate one, the Government of India took another historic decision of Nationalization of 14 Indian banks through an ordinance under the leadership of the then Prime Minister Mrs. Indira Gandhi and, accordingly, with effect from 19th July, 1969 those 14 banks were taken over by the Govt. of India under the Banking Companies (Acquisition & Transfer of Undertakings) Act of 1969. Again in 1980 another six banks were taken over on 14th March, 1980 under the Banking Companies (Acquisition and Transfer of Undertakings Act) 1980. No foreign banks were nationalized.

On the other hand, well before nationalization, State Bank of India Act, 1955 was enacted to convert Imperial bank of India to SBI and in 1959 “State Bank of India(Subsidiary) Act was passed and eight Indian banks were made subsidiaries to State Bank of India. As a result in the Indian Banking System, the number of public sector banks figured to 29(20 nationalized & 9 banks comprising SBI & 8 subsidiaries). However, at present number of public sector banks is 27 after merging of nationalized bank “New Bank of India” with “Punjab National Bank” in 1993 and amalgamation of two subsidiaries of SBI viz. State Bank of Bikaner and State Bank of Jaipur into one as “State Bank of Bikaner & Jaipur”. Besides these, in Indian banking system there are indigenous old private banks, new generation private banks and foreign banks. Moreover, Regional Rural Banks, Co-operative banks, Land Development Banks are in existence besides a few industrial or Development Banks.

2. Different Provisions of Banking Regulation Act, 1949

The Banking Regulation Act, 1949 has ten parts, each dealing with a specific topic. The following is the at a glance picture of the same.

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The Act as it stands now provides for the following controls:

1. Minimum Paid-up Capital
2. Classification of Companies into Banking and Non-Banking Companies
3. Licensing of Banking Companies
4. Restriction on Branch Banking
5. Maintenance of Cash Reserves
6. Maintenance of Assets in India
7. Minimum Liquid Asset Ratio
8. Prohibition of Common Directors
9. Restriction on Payment of Dividend and Transfer of a certain percentage of profit to the Reserve Fund
10. Restriction on Nature of Subsidiary Company
11. Accounts and Balance Sheet
12. Inspection of Banking Companies
13. Suspension of Business and Winding up
14. Schemes for Arrangement and Amalgamation
15. Compulsory Amalgamation of Banking Company

3. Applicability of the Banking Regulation Act, 1949

This Act applies to following categories of Banks:

1. Nationalized Banks
2. Non-Nationalized Banks
3. Co-operative Banks in the manner and to the extent specified in Part V

4. Business of Banking Companies

Section 6 of the Banking Regulation Act, 1949 states the Forms of business in which banking companies may engage.

(1) In addition to the business of banking, a banking company may engage in any one or more of the following forms of business, namely:

(a) the borrowing, raising, or taking up of money; the lending or advancing of money either upon or without security; the drawing, making, accepting, discounting, buying, selling, collecting and dealing in bills of exchange, hundies, promissory notes, coupons, drafts, bills of lading, railway receipts, warrants, debentures, certificates, scrips and other instruments, and securities whether transferable or negotiable or not; the granting and issuing of letters of credit, traveller's cheques and circular notes; the
buying, selling and dealing in bullion and specie; the buying and selling of foreign exchange including foreign bank notes; the acquiring, holding, issuing on commission, underwriting and dealing in stock, funds, shares, debentures, debenture stock, bonds, obligations, securities and investments of all kinds; the purchasing and selling of bonds, scrips or other forms of securities on behalf of constituents or others, the negotiating of loans and advances; the receiving of all kinds of bonds, scrips or valuables on deposit or for safe custody or otherwise; the providing of safe deposit vaults; the collecting and transmitting of money and securities;

(b) acting as agents for any Government or local authority or any other person or persons; the carrying on of agency business of any description including the clearing and forwarding of goods, giving of receipts and discharges and otherwise acting as an attorney on behalf of customers, but excluding the business of a managing agent or secretary and treasurer of a company;

(c) contracting for public and private loans and negotiating and issuing the same;

(d) the effecting, insuring, guaranteeing, underwriting, participating in managing and carrying out of any issue, public or private, of State, municipal or other loans or of shares, stock, debentures, or debenture stock of any company, corporation or association and the lending of money for the purpose of any such issue;

(e) carrying on and transacting every kind of guarantee and indemnity business;

(f) managing, selling and realising any property which may come into the possession of the company in satisfaction or part satisfaction of any of its claims;

(g) acquiring and holding and generally dealing with any property or any right, title or interest in any such property which may form the security or part of the security for any loans or advances or which may be connected with any such security;

(h) undertaking and executing trusts;

(i) undertaking the administration of estates as executor, trustee or otherwise;

(j) establishing and supporting or aiding in the establishment and support of associations, institutions, funds, trusts and conveniences calculated to benefit employees or ex-employees of the company or the dependents or connections of such persons; granting pensions and allowances and making payments towards insurance; subscribing to or guaranteeing moneys for charitable or benevolent objects or for any exhibition or for any public, general or useful object;

(k) the acquisition, construction, maintenance and alteration of any building or works necessary or convenient for the purposes of the company;

(l) selling, improving, managing, developing, exchanging, leasing, mortgaging, disposing of or turning into account or otherwise dealing with all or any part of the property and rights of the company;

(m) acquiring and undertaking the whole or any part of the business of any person or company, when such business is of a nature enumerated or described in this sub-section;
(n) doing all such other things as are incidental or conducive to the promotion or advancement of the business of the company;

(o) any other form of business which the Central Government may, by notification in the Official Gazette, specify as a form of business in which it is lawful for a banking company to engage.

(2) No banking company shall engage in any form of business other than those referred to in sub-section (1).

Agency Services:-
Carrying on and transacting guarantee or indemnity business on behalf of its clients, collection of bills, pro-notes, hundies, cheques, cheques, securities etc, issuing on commission and underwriting of stocks, shares, funds etc, purchasing and selling of shares, G.P.Notes, bonds, debenture, etc. on behalf of constituents, negotiating of loans and advances, remittance of money by drafts, mail transfer, telegraphic transfer, electronic fund transfer (EFT) etc, granting and issuing letter of credit / letter of guarantee, buying and selling of foreign exchanges including foreign bank notes under Forex business, acting as an agent for any Govt. local authority etc. contracting for private and public notes, undertaking or executing trusts, undertaking the administration of estates as executor, trustees, or otherwise. The above mentioned agency services can be grouped as under:-

1. Non-fund Business (issuing Letter of Credit/ Letter of Guarantee)
2. Collection of instruments and securities on behalf of customers
3. Portfolio Management or Merchant Banking (Acting as Issue manager, lead manager, underwriting of any issue etc)
4. Facility of remittance of funds
5. Money Exchange business as Authorized Dealer under Foreign Exchange Business
6. Other Agency Business on behalf of Govt. / Local Body etc.
7. Factoring Services (Indigenous Receivable Administration on behalf of clients)
8. Forfeiting Services (Export Receivable Administration on behalf of clients)
9. Special Purpose Vehicle (SPV) services for securitization of assets under Securitization & Reconstruction of Financial Assets and Enforcement of Security Interest Act
10. Collection of taxes on behalf of the people
11. collection of different dues/ cess/ duty of the people say, telephone/ electricity, municipal taxes etc.

General Utility Services:-
1. Providing Safe-custody facility to its customers for keeping their valuables
2. Providing the facility of Safe Deposit Vault (Locker) under lease agreement to its customers for keeping their valuables
3. Technology based general utility services like Tele-banking, phone-banking, on-line banking, Home Banking, Single window banking, Demat Services for securities trading, ATM services, Credit Card services etc

4. Consultancy Services

5. ECS services for payment of different dues of the people

6. Payment of pension

7. Payment of salaries of employees of schools etc.

8. Payment of salaries etc.

9. Many others

Note:- Some of the activities mentioned both under agency services & general utility services are of new generation activities particularly after reforms measures in financial sector and growing adoption of technology based banking.

5. Prohibition of trading (Section 8)

Notwithstanding anything contained in section 6 or in any contract, no banking company shall directly or indirectly deal in the buying or selling or bartering of goods, except in connection with the realisation of security given to or held by it, or engage in any trade, or buy, sell or barter goods for others otherwise than in connection with bills of exchange received for collection or negotiation or with such of its business as is referred to in clause (i) of sub-section (1) of section 6:

Provided that this section shall not apply to any such business as is specified in pursuance of clause (a) of sub-section (1) of section 6.

Explanation.—For the purposes of this section, "goods" means every kind of movable property, other than actionable claims, stocks, shares, moneys, bullion and specie, and all instruments referred to in clause (a) of sub-section (1) of section 6.

6. Disposal of non-banking assets (Section 9)

Notwithstanding anything contained in section 6, no banking company shall hold any immovable property howsoever acquired, except such as is required for its own use, for any period exceeding seven years from the acquisition thereof or from the commencement of this Act, whichever is later or any extension of such period as in this section provided, and such property shall be disposed of within such period or extended period, as the case may be:

Provided that the banking company may, within the period of seven years as aforesaid, deal or trade in any such property for the purpose of facilitating the disposal thereof:

Provided further that the Reserve Bank may in any particular case extend the aforesaid period of seven years by such period not exceeding five years where it is satisfied that such extension would be in the interests of the depositors of the banking company.
7. Reserve Fund (Section 17)

Every Banking Company incorporated in India must create a Reserve Fund and transfer a sum equal to not less than 20% of its net profits. However, the Central Government is empowered to exempt from this requirement on the recommendation of the RBI. Such exemption will be allowed only:

- When the amounts in the reserve fund and the share premium account are not less than the paid-up capital of the banking company.
- When the Central Govt. feel that its paid-up capital and reserves are adequate to safeguard the interest of the depositors.

If a banking company appropriates any sum from the Reserve fund or the share premium account, it must be reported to RBI within 21 days from the date of such appropriation explaining the circumstances leading to such appropriation.

Provided that the Reserve Bank may, in any particular case, extend the said period of twenty-one days by such period as it thinks fit or condone any delay in the making of such report.

8. Restrictions on Loans & Advances (Section 20)

No banking company shall

(a) grant any loans or advances on the security of its own shares, or

(b) enter into any commitment for granting any loan or advance to or on behalf of

   (i) any of its Directors, or

   (ii) any firm in which any of its Directors is interested as Partner, Manager, Employee or Guarantor, or

   (iii) any company (not being a subsidiary of the banking company or a company registered under section 25 of the Companies Act, 1956 or a Government company or the subsidiary or the holding company of which any of the Directors of the banking company is a Director, Managing Agent, Manager, Employee or Guarantor or in which he holds substantial interest, or

   (iv) any individual in respect of whom any of its Directors is a partner or guarantor.

Where any loan or advance granted by a banking company is such that a commitment for granting it could not have been made on the date on which the loan or advance was made, or is granted by a banking company after the commencement of section 5 of the Banking Laws (Amendment) Act, 1968 but in pursuance of a commitment entered into before such commencement, steps shall be taken to recover the amounts due to the banking company on account of the loan or advance together with interest, if any, due thereon within the period stipulated at the time of the grant of the loan or advance, or where no such period has been stipulated, before the expiry of one year from the commencement of the said section 5:
Provided that the Reserve Bank may, in any case, on an application in writing made to it by the banking company in this behalf, extend the period for the recovery of the loan or advance until such date, not being a date beyond the period of three years from the commencement of the said section 5, and subject to such terms and conditions, as the Reserve Bank may deem fit provided further that this sub-section shall not apply if and when the Director concerned vacates the office of the Director of the banking company, whether by death, retirement, resignation or otherwise.

No loan or advance or any part thereof shall be remitted without the previous approval of the Reserve Bank, and any remission without such approval shall be void and of no effect.

Where any loan or advance payable by any person, has not been repaid to the banking company within the period specified in that sub-section, then, such person shall, if he is a Director of such banking company on the date of the expiry of the said period, be deemed to have vacated his office as such on the said date.

RBI is empowered to issue directives to a banking company to determine the policy in relation to loans and advances.

Section 21A:- Rate of interest charged by banking company on the basis of loan contract between the bank and debtor is not to be subject to scrutiny by the court on the ground that the rate of interest charged in respect to such transaction is excessive.

9. Accounts and Balance Sheet (Section 29)

Every Banking Company incorporated in India, in respect of all business transacted by it and through its branches in India, shall prepare a balance sheet and profit & loss account as on the last working day of the Accounting year (which was earlier calendar year, now April to March i.e. 31st March) in the Form “A” and “B” given in the third schedule of the Act. The amalgamated Balance Sheet and Profit Loss should be signed by the CMD and at least three Directors where there are more than three directors or where there are not more than three directors, by all the directors. In case of banking companies incorporated outside India by the principal officer of the company in India.

The provisions of the Companies Act, 1956,(Presently the Companies Act, 2013) relating to the balance sheet and profit and loss account of a company shall also be applicable to the profit and loss account and balance sheet of a banking company, in so far as they are not inconsistent with the provision of the Act.

10. Audit (Section 30)

Balance sheet & profit & loss account as prepared in terms of sec 29 are subject to audit by a person duly qualified under any law for the time being in force to be an auditor for auditing such balance sheet and profit & loss accounts. (These Auditors are known as Statutory Auditors for the said purpose and appointment /reappointment or removal is subject to prior approval of the RBI. Under these Statutory Auditors there are numbers of External Auditors who conduct audit operation of the branch accounts)
Further Reserve Bank can by order, direct for special Audit of Banking Company, if it is of the opinion that it is in the public interest or in the interest of the depositors. The auditors shall comply with the directions given by the RBI and shall submit a report of the audit to RBI and also to the bank. The auditor shall have the powers and exercise the functions as specified in section 227 of the Companies Act, 1956.

Apart from the above, the auditor is required to state in his report:

- Whether or not the information and explanation required by him have been found to be satisfactory;
- The transactions of the bank which have come to his notice have been within the powers of the bank or not;
- The return received from branch offices have been found adequate for the purpose of his audit;
- Whether the profit and loss account shows a true balance of profit or loss for the period covered by such account; and
- Any other matter which he considers should be brought to the notice of the share holders of the company;

**Section 31:** Submission of Balance Sheet & P&L: - The accounts and balance sheet along with auditors report shall be published in prescribed manner and three copies thereof shall be furnished as returns to RBI within three months from the end of the period to which they refer. The RBI may extend the period by a further period of not exceeding three months.

**Section 32:** Three copies of such accounts and balance sheet along with auditor’s report shall be sent by the banking company to the Registrar of Companies, at the same time while sending the same to RBI.

**Section 35:** Power of RBI to inspect banks: - RBI is empowered to conduct inspection of any bank and to give them direction as it deems fit. All banks are bound to comply with such directions. Every director or other officer of the bank shall produce all such books, documents as required by the inspector. The inspector may examine on oath any director or other officers.

RBI shall supply the bank a copy of such inspection. The RBI shall, if it has been directed by the Central Government to cause an inspection to be made, and may, in other cases, report to the Central Government on any inspection and the latter, on scrutiny, if is of the opinion that the affairs of the bank are being conducted detrimental to the interest of its depositors, it may, after giving an opportunity of being heard, to the bank, may order in writing prohibiting the bank from receiving fresh deposits and direct the RBI to apply section 38 for winding up of the bank.

Apart from inspection under section 35, RBI is empowered to undertake inspection of a bank in terms/ for the purposes of the following sections:

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Section 38: Winding up by High Court

Section 44: Power of High Court in voluntary winding-up

Section 44A: Procedure for Amalgamation of banking companies

Section 45: Power of RBI to apply to Central Govt. for suspension of business by a bank and prepare scheme of reconstitution or amalgamation

Section 35A: Power of RBI to give directions:

1. Where the RBI is satisfied that in the public interest or in the interest of banking policy or to prevent the affairs of any bank being conducted in a manner detrimental to the interest of the depositors or in a manner prejudicial to the interest of the bank or to secure the proper management of the bank generally, it is necessary to issue directions to banking companies generally or to any banking company in particular, it may, from time to time, issue such directions as it deems fit, and the banks or bank, as the case may be, shall be bound to comply with such directions.

2. RBI may, on representation made to it or on its own motion, modify or cancel any direction issued under sub-section (1), and in so modifying or canceling any direction may impose such condition as it thinks fit, subject to which the modification or cancellation shall have effect.

Section 35B: Amendments of provisions relating to appointments of Managing Directors, etc., to be subject to prior approval of the RBI:

Amendments relating to no. of directors, remuneration, appointment, reappointment, removal etc, of chairman, managing director or any other director or any other chief executive shall not have effect unless approved by RBI. Similarly, appointment, re-appointment, removal of any such officials shall have effect only with prior approval of RBI.

Section 35AA. Power of Central Government to authorise Reserve Bank for issuing directions to banking companies to initiate insolvency resolution process: The Central Government may, by order, authorise the Reserve Bank to issue directions to any banking company or banking companies to initiate insolvency resolution process in respect of a default, under the provisions of the Insolvency and Bankruptcy Code, 2016.

Explanation.—For the purposes of this section, “default” has the same meaning assigned to it in clause (12) of section 3 of the Insolvency and Bankruptcy Code, 2016.

Section 35AB. Power of Reserve Bank to issue directions in respect of stressed assets: (1) Without prejudice to the provisions of section 35A, the Reserve Bank may, from time to time, issue directions to any banking company or banking companies for resolution of stressed assets. (2) The Reserve Bank may specify one or more authorities or committees with such members as the Reserve Bank may appoint or approve for appointment to advise any banking company or banking companies on resolution of stressed assets.
Section 36:- Further powers and function of RBI:- The RBI may-

(i) caution or prohibit banks generally or any bank(s) in particular against entering into any particular transaction or class of transactions and generally give advice to any bank

(ii) may assist, subject to provision of this Act, on a written request of a bank, in proposal for amalgamation of such bank

(iii) give assistance to any bank by means of grant of loan or advances (known as Refinance/ rediscounting of bills), in terms of the provision of RBI Act, 1934.

(iv) in case where it is satisfied that in the public interest or in the interest of banking policy or preventing the affairs of the banking company, being conducted in a manner detrimental to the interest of the bank or its depositors, it is necessary to do so, by order in writing and on such terms and conditions as may be specified, require the banking company:-

(a) to call a meeting of its directors for the purpose of considering any matter

(b) to require an officer to discuss any matter with an officer of RBI

(c) to depute one or more of its officers to watch the proceedings of any meeting of the Board of directors or of any committee or of any other body constituted by it. The officers so deputed shall have to be given an opportunity to be heard at such meeting, and they shall send a report to the RBI (Generally, RBI nominated director looks after these things);

(d) to depute officer to observe the affairs of even the branches and make a report thereon; and

(e) to require the bank to make such changes in the management and within such time as RBI deem fit.

The RBI shall make an Annual Report and submit the same to Govt. of India on the trend and progress of banking in the country with particular reference to activities under clause (2) of section 17 of RBI Act, 1934. The RBI may appoint such persons at such places as it may feel necessary, to scrutinize the statements and information furnished by the banking company and also to ensure efficient performance of its function under the Act. (As a requirement of banking Sector Reforms for better supervision on banks by RBI, besides on-site inspection a system of off-site surveillance has been introduced where RBI officials scrutinize the DSB returns submitted by banks and if necessary, percolates down to on-site supervision.)

Section 36AA:- Power of Reserve Bank to remove managerial and other persons from office:- RBI can terminate any chairman, Director, Chief Executive, other officials or any employee of the bank where it considers desirable to do so particularly when RBI is of the opinion that conduct of such person is detrimental to the interest of the depositors or for securing proper management of the banking company. Before such termination concerned person should be given opportunity to be heard of. Such terminated officials can make appeal to the Central Govt. within 30 days from the date of communication of such termination order. The decision of the Central Govt. on such appeal can not be called into question in any court. In case an order is issued pursuant to this section, the concerned person shall cease to hold his office and shall
not in any way be concerned with or take part in the management of any bank for a period of not exceeding 5 years as may be specified in the order. Contravention of the above provision shall be punishable with a fine, which may extend to Rs 250 per day.

The Reserve Bank may by order, appoint a suitable person in place of the Chairman or director or Chief executive officer or employee who has been removed.

Any such order shall be valid for a period not exceeding three years or such further periods of not exceeding three years at a time as RBI may specify.

Section 36AB: RBI is empowered to appoint additional Directors for the banking company with effect from the date to be specified in the order, in the interest of the bank or that of depositors. Such additional directors shall hold office for a period not exceeding three years or such further periods not exceeding three years at a time.

Section 36AE: Power of Central Govt. to acquire the undertaking of Banking Companies in certain cases: If Central Govt. is of the opinion that the Banking Co has failed to comply with the direction given to it by RBI relating to policy matters under section 21 and 35A and/or the bank is being managed in a manner detrimental to the interest of the depositors or that of to the banking policy, or for better provision of credit generally or of credit to any particular section of the community or in any particular area; it is necessary to acquire the undertaking of such banking company, it (Central Govt.) may after consultation with RBI as it thinks fit, by notified order, acquire the undertaking of such banking company with effect from such date as may be specified in this behalf by the Central Govt. In case of such a notification, on the specified date the undertaking of the acquired bank and its assets & liabilities shall stand transferred to, and vest in Central Govt. Before acquiring the undertaking of any banking company, the Central Govt. shall give a reasonable opportunity to the banking company proposed to be acquired of showing cause against the proposed action.

Section 36AF: Power of Central Govt. to make a scheme for the acquired bank in consultation with RBI: The scheme may provide for transfer of assets & liabilities of the acquired bank, constitution of the first Board of Management and incidental matters, the service condition of the employees, compensation payable to the shareholders of the acquired bank and such other incidental, consequential and supplemental matters as may be necessary to complete the transfer.

Section 36AG: Compensation to shareholders of the acquired bank: Compensation to be paid to the registered shareholders in accordance with the principle provided in Fifth Schedule of the Act. Any shareholder aggrieved with the amount of compensation may request the Central Govt. to refer the matter to Tribunal to be constituted under section 36 AH. If the no. of representation received is not less than one-fourth of the no of shareholders holding not less than one-fourth of the paid-up share capital of the acquired bank, the Central Govt. shall constitute a Tribunal for the purpose.

Section 36AH: Constitution of the Tribunal: The Tribunal shall consist of a Chairman and two other members. Chairman shall be a person who is or has been a judge of the High Court or the Supreme Court. Of the two other members, one shall be a person, who in the opinion of
the Central Govt. has had commercial banking experience and the other shall be a person who is a Chartered Accountant

**Section 36 Ai:** - **Tribunal to have power of a civil court:**- The Tribunal shall enjoy the power of a civil court, while trying a suit, under CPC 1908, in respect of the following matters:-

(i) Summoning and enforcing attendance of any person and examining him on oath. (ii) discovery & production of documents, (iii) receiving evidence on affidavits, (iv) issuing commission for examination of witnesses or documents. However, Tribunal can not compel Central Govt. or RBI to produce any books or documents which the latter(s) consider confidential, to make any such documents part of the records of the proceedings, to give inspection of any such books to any party before it or to any other person.

**Section 36AJ:** - **procedure of the Tribunal:**- The Tribunal enjoys the power to regulate its own procedure, may hold the whole or any part of its inquiry in camera. Any mistake arising out of accidental slip or omission may, at any time, be corrected by the Tribunal either of its own motion or at the request of any other parties.

**11. Some Important Recent Changes**

- Foreign direct investment in private sector banks will be 74% (automatic route upto 49%)
- In terms of sec 17(1) and 11 (1) (b) (ii) transfer of balance of profit to reserve fund which was earlier 20% but w.e.f., 31-03-2001 advised to 25 % for all scheduled commercial banks including foreign banks operating in India
- Any appreciation from reserve fund or the share premium account has to be reported within 21 days along with explanation
- Cabinet gave its ex-post facto approval for modifying the banking companies Bill 2005 to allow the RBI to recommend a person other than an officer of RBI for appointment as a director in the Board of PSB.

**12. Conclusion**

Any attempt to cover all the aspects of regulatory measures in banking within the limited scope of this write-up is not possible but an effort has been made to narrate all the important provisions of Banking Regulation Act 1949. Moreover, Banking in India is a perfect mixture of Law and Practices since legislation of banking activities has an age old practices. During post reforms era, banking in India has got a paradigm shift to make it viable in the present competition particularly where the existence of private banks, foreign banks, and new generation private banks have parallel existence with the public sector banks. A number of policy measures have been implemented as part of the first generation and second generation reforms and all attempts are being made to make the Indian Banking System a Global Standard. The profitability is the sole criteria for sustainable solvency of any Industry and the banking industry is not an exception to it. But, on the contrary, banking industry being the backbone of the financial system, public sector banks are to play an important role for the development of the rural economy. The prudential accounting norms, capital adequacy norms, disclosure norms etc have become the
yardstick of the banks’ performance vis-à-vis its survival. The challenge which the Indian banking system in general and public sector banks particular is facing is the forthcoming bussel accord II for which all banks have to be ready for arranging capital either making more and more profits or by raising capital from the market. A many of the banks have already gone to the market since 1994 when banking laws were amended allowing the public sector bank to dilute govt. stake to the extent of 49 %. But in terms of the recommendation of Narashimam Committee, 67 % of the govt. stake is supposed to be diluted to accept the future challenge which could not be implemented due to strong opposition from the trade union as well as leftists. As a result Govt. is planning and framing come out with suitable alternatives to face the challenge of Bussel II. Govt has allowed banks to raise capital through innovative perpetual debt which would be eligible for inclusion as capital for the purpose of capital adequacy. On the other hand, corporate Governance is revamped in banks through changes in the composition of boards through inclusion of shareholder directors, increasing whole time director from 2 to 4 through amending Banking Companies (Acquisition & Transfer of Undertaking) Act 1970, & 1980. Moreover, attempt of merger and amalgamation of the banks to tap wide market vis-a-vis increase volume of business is the headline of the dailies. Last but not least removal of minimum & maximum range in CRR & SLR maintenance will make provide a level playing field to classes of the banks.

All these initiatives are effected through amendments of relevant acts pertaining to banking industry that may be Banking Regulation Act or SBI Act or SBI Subsidiary Act ir Banking Company (Transfer & Acquisition of Undertakings) Act, through which greater functional autonomy is provided to the banks and road maps are prepared to make the industry a global standard.

THE INSURANCE ACT, 1938

1. Introduction

Under British dominion, the first Act on Insurance was enacted in 1912, which was called Act 5 of 1912 which regulated Provident Insurance Societies Act 6 of 1912 and Act 20 of 1928. The former being related to Life Insurance business and the later being dealt with statistical matters concerning non-life Insurance business by the external entities. With the increase in the volume of insurance business in India, a need arose for more exhaustive legislation. As a result, a Bill was prepared on 1925. The Act 6 of 1912 was based on Insurance Company Act 1909. The amending of the 1909 Act became imperative and Government of India was awaiting the result of the amendment of 1909 Act. But such wait became too long. In the meantime, another legislation was passed in 1928. The Government of India in 1935 took the initiative to reform Insurance business and deputed Mr. S.C. Sen to look into the probable deficiencies and lacunnaes in the insurance industry. In 1936, the Companies Act, 1913 was amended. Mr. Sen recommendations regarding insurance business were submitted to the Government. The recommendations among other things stressed overall supervision of the insurance industry with special emphasis on operations conducted by indigenous entities as well as foreign companies. The deposit money for Life Insurance business was increased to the net sum of
Corporate and Allied Laws

र 50,000 so as to discourage financially weak companies to enter into the insurance business. Restrictions and controls were imposed on external companies. The process of winding up of insurance companies along with amalgamation and transfer of business schemes were revamped. Managing agents are prohibited to do any business in future, in the insurance sector. Insurance agents were provided with licences. The post of Superintendent of Insurance was established under whose control and direction the business was conducted, who was normally the Government Actuary.

It was decided that effective supervision of Insurance industry is necessary to see whether they operate under sound business principle. The schemes proposed by any company were expected to be transparent and unsound schemes were not accepted. The books of accounts and documents were thoroughly scrutinized. Investment policies on assets of the companies were changed for better protection of the interests of the insured. The Insurance Bill was passed on 26th February, 1938 and came into effect on 1st July, 1938 vide Notification No. 589 – 1 (4) / 38 as The Insurance Act 1938 (4of 1938). Till 2005, 25 amendments regarding this Act has been made.


Highlights of the amended Act: The amendment Act paved way for removing archaic and redundant provisions in the legislations and incorporates certain provisions to provide Insurance Regulatory and Development Authority of India (IRDAI) with the flexibility to discharge its functions more effectively and efficiently. It also provides for enhancement of the foreign investment cap in an Indian Insurance Company from 26% to an explicitly composite limit of 49% with the safeguard of Indian ownership and control.

In addition to the provisions for enhanced foreign equity, the amended law will enable capital raising through new and innovative instruments under the regulatory supervision of IRDAI. Greater availability of capital for the capital intensive insurance sector would lead to greater distribution reach to under / un-served areas, more innovative product formulations to meet diverse insurance needs of citizens, efficient service delivery through improved distribution technology and enhanced customer service standards. The Rules to operationalize the new provisions in the Law related to foreign equity investors have already been notified on 19th February 2015 under powers accorded by the Ordinance.

The four public sector general insurance companies, presently required as per the General Insurance Business (Nationalisation) Act, 1972 (GIBNA, 1972) to be 100% government owned, are now allowed to raise capital, keeping in view the need for expansion of the business in the rural and social sectors, meeting the solvency margin for this purpose and achieving enhanced competitiveness subject to the Government equity not being less than 51% at any point of time.

Further, the amendments to the laws will enable the interests of consumers to be better served through provisions like those enabling penalties on intermediaries / insurance companies for misconduct and disallowing multilevel marketing of insurance products in order to curtail the practice of mis-selling. The amended Law has several provisions for levying higher penalties
ranging from up to ₹1 Crore to ₹25 Crore for various violations including mis-selling and misrepresentation by agents / insurance companies. With a view to serve the interest of the policy holders better, the period during which a policy can be repudiated on any ground, including mis-statement of facts etc., will be confined to three years from the commencement of the policy and no policy would be called in question on any ground after three years. The amendments provide for an easier process for payment to the nominee of the policy holder, as the insurer would be discharged of its legal liabilities once the payment is made to the nominee. It is now obligatory in the law for insurance companies to underwrite third party motor vehicle insurance as per IRDAI regulations. Rural and Social sector obligations for insurers are retained in the amended laws.

The Act will entrust responsibility of appointing insurance agents to insurers and provides for IRDAI to regulate their eligibility, qualifications and other aspects. It enables agents to work more broadly across companies in various business categories; with the safeguard that conflict of interest would not be allowed by IRDAI through suitable regulations. IRDAI is empowered to regulate key aspects of Insurance Company operations in areas like solvency, investments, expenses and commissions and to formulate regulations for payment of commission and control of management expenses. It empowers the Authority to regulate the functions, code of conduct, etc., of surveyors and loss assessors. It also expands the scope of insurance intermediaries to include insurance brokers, re-insurance brokers, insurance consultants, corporate agents, third party administrators, surveyors and loss assessors and such other entities, as may be notified by the Authority from time to time. Further, properties in India can now be insured with a foreign insurer with prior permission of IRDAI; which was earlier to be done with the approval of the Central Government.

The amendment Act defines ‘health insurance business’ inclusive of travel and personal accident cover and discourages non-serious players by retaining capital requirements for health insurers at the level of ₹100 Crore, thereby paving the way for promotion of health insurance as a separate vertical.

The amended law enables foreign reinsurers to set up branches in India and defines ‘re-insurance’ to mean “the insurance of part of one insurer’s risk by another insurer who accepts the risk for a mutually acceptable premium”, and thereby excludes the possibility of 100% ceding of risk to a re-insurer, which could lead to companies acting as front companies for other insurers. Further, it enables Lloyds and its members to operate in India through setting up of branches for the purpose of reinsurance business or as investors in an Indian Insurance Company within the 49% cap.

The Life Insurance Council and General Insurance Council have now been made self-regulating bodies by empowering them to frame bye-laws for elections, meetings and levy and collect fees etc. from its members. Inclusion of representatives of self-help groups and insurance cooperative societies in insurance councils has also been enabled to broad base the representation on these Councils.

Appeals against the orders of IRDAI are to be preferred to SAT as the amended Law provides for any insurer or insurance intermediary aggrieved by any order made by IRDAI to prefer an appeal to the Securities Appellate Tribunal (SAT).
2. Important Definitions

Actuary: Section 2(1): “Actuary” means an actuary as defined in clause (a) of sub-section (1) of section 2 of the Actuaries Act, 2006.

Authority: Section 2(1A): Authority means the Insurance Regulatory and Development Authority of India established under sub-section (1) of section 3 of the Insurance Regulatory and Development Authority Act, 1999.

Policy Holder: Section 2 (2): “Policy holder” includes a person to whom the whole of the interest of policy holder in the policy is assigned once and for all, but does not include an assignee thereof whose interest in the policy is defeasible or is for the time being subject to any condition.

Banking Company: Section 2 (4A): “Banking Company” and “Company” shall have the meanings respectively assigned to them in clauses (c) and (d) of subsection (1) of section of the Banking Companies Act, 1949 (10 of 1949).

Controller of Insurance: Section 2 (5B): “Controller of Insurance”, means the officer appointed by the Central Government under section 2B to exercise all the powers, discharge the functions and perform the duties of the Authority under this Act or the Life Insurance Corporation Act, 1956 (31 of 1956) or the General Insurance Business (Nationalisation) Act 1972 (57 of 1972) or the Insurance Regulatory and Development Authority Act 1999.

Court: Section 2 (6): “Court” means the Principal Civil court of original jurisdiction in a district, and includes the High Court in exercise of its ordinary original civil jurisdiction.

General Insurance Business: Section2 (6B): “General insurance business” means fine, marine or miscellaneous insurance business, whether carried on singly or in combination with one or more of them.

Health Insurance Business: Section 2(6C): “Health Insurance Business” means the effecting of contracts which provide for sickness benefits or medical, surgical or hospital expense benefits, whether in-patient or out-patient travel cover and personal accident cover.


Indian Insurance Company: Section 2(7A): “Indian insurance company” means any insurer, being a company which is limited by shares, and,—

(a) which is formed and registered under the Companies Act, 2013 as a public company or is converted into such a company within one year of the commencement of the Insurance Laws (Amendment) Act, 2015;

(b) in which the aggregate holdings of equity shares by foreign investors, including portfolio investors, do not exceed forty-nine per cent. of the paid up equity capital of such Indian insurance company, which is Indian owned and controlled, in such manner as may be prescribed.
Explanation.—For the purposes of this sub-clause, the expression "control" shall include the right to appoint a majority of the directors or to control the management or policy decisions including by virtue of their shareholding or management rights or shareholders agreements or voting agreements;

(c) whose sole purpose is to carry on life insurance business or general insurance business or re-insurance business or health insurance business.

Insurer: Section 2(9): "Insurer" means (a) an Indian Insurance Company, or (b) a statutory body established by an Act of Parliament to carry on insurance business, or (c) an insurance co-operative society, or (d) a foreign company engaged in re-insurance business through a branch established in India. The expression "foreign company" shall mean a company or body established or incorporated under a law of any country outside India and includes Lloyd's established under the Lloyd's Act, 1871 (United Kingdom) or any of its Members.

Insurance Agent: Section 2(10): "insurance agent" means an insurance agent who receives agrees to receive payment by way of commission or other remuneration in consideration of his soliciting or procuring insurance business including business relating to the continuance, renewal or revival of policies of insurance;

Investment Company: Section 2 (10A): "Investment Company" means a company whose principal business is the acquisition of shares, stocks, debentures or other securities.

Life Insurance Business: Section 2(11): "life insurance business" means the business of effecting contracts of insurance upon human life, including any contract whereby the payment of money is assured on death (except death by accident only) or the happening of any contingency dependent on human life, and any contract which is subject to payment of premiums for a term dependent on human life and shall be deemed to include—

(a) the granting of disability and double or triple indemnity accident benefits, if so provided in the contract of insurance;

(b) the granting of annuities upon human life; and

(c) the granting of superannuation allowances and benefits payable out of any fund applicable solely to the relief and maintenance of persons engaged or who have been engaged in any particular profession, trade or employment or of the dependents of such persons;

Explanation. —For the removal of doubts, it is hereby declared that "life insurance business" shall include any unit linked insurance policy or scrips or any such instrument or unit, by whatever name called, which provides a component of investment and a component of insurance issued by an insurer referred to in clause (9) of this section.

Re-insurance: Section 2(16B): "Re-insurance" means the insurance of part of one insurer's risk by another insurer who accepts the risk for a mutually acceptable premium.

3. Provisions Related to Insurance
(a) Indian properties not to be insured with foreign insurers (section 2CB)
Without the permission of the IRDAI, no person shall take out or renew any policy of insurance in respect of any property in India or any ship or other vessel or aircraft registered in India with an insurer whose principal place of business is outside India.

(b) Requirements as to Capital (Section 6)
No insurer (not being an insurer as defined in sub-clause (d) of clause (9) of section 2) carrying on the business of life insurance, general insurance, health insurance or re-insurance in India or after the commencement of the Insurance Regulatory and Development Authority Act, 1999, shall be registered unless he has minimum paid up capital as prescribed below:

<table>
<thead>
<tr>
<th>Type of Insurance Business</th>
<th>Minimum Paid-up equity capital required (with a provision for further enhancement &amp; Paid-up equity excludes preliminary expenses incurred during formation and registration)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Life insurance or general insurance</td>
<td>₹ 100 crore</td>
</tr>
<tr>
<td>Health insurance (exclusively)</td>
<td>₹ 100 crore</td>
</tr>
<tr>
<td>Re-insurer (exclusively)</td>
<td>₹ 200 crore (besides re-insurer shall not be registered unless he has net owned funds of not less than ₹ 5,000 crore)</td>
</tr>
</tbody>
</table>

Provided that the insurer, may enhance the paid-up equity capital, as provided in this section in accordance with the provisions of the Companies Act, 2013, the Securities and Exchange Board of India Act, 1992 and the rules, regulations or directions issued thereunder or any other law for the time being in force:

Provided further that in determining the paid-up equity capital, any preliminary expenses incurred in the formation and registration of any insurer as may be specified by the regulations made under this Act, shall be excluded.

No insurer, as defined in sub-clause (d) of clause (9) of section 2, shall be registered unless he has net owned funds of not less than rupees five thousand crore.

(c) Further Conditions (Section 6A)
To carry on the business of life or general or health or re-insurance the following further requirements are to be satisfied by such companies:

- that the capital of the company shall consist of equity shares each having a single face value and such other form of capital, as may be specified by the regulations;
- that the voting rights of shareholders are restricted to equity shares;
that, except during any period not exceeding one year allowed by the company for
payment of calls on shares, the paid-up amount is the same for all shares, whether
existing or new.

- The aforesaid conditions shall not apply to a public company which before the
commencement of the Insurance (Amendment) Act, 1950, has issued any shares
other than ordinary shares each of which has a single face value or shares, the paid-
up amount whereof is not the same for all them for a period of three years from such
commencement.

(d) Audit of accounts of insurance companies (Section 12) & Submission of returns
(Section 15)

Unless subject to audit under the Companies Act, 2013, the balance sheet, profit and loss
account, revenue account and profit and loss appropriation account of every insurer, in
respect of all insurance business transacted by him, shall be audited annually by an
auditor, and the auditor shall in the audit of all such accounts have the powers of, exercise
the functions vested in, and discharge the duties and be subject to the liabilities and
penalties imposed on, auditors of companies by section 147 of the Companies Act, 2013.

The audited accounts and statements and the abstract and statement referred to in section
13 shall be printed, and four copies thereof shall be furnished as returns to the Authority
within six months from the end of the period to which they refer. Of the four copies so
furnished, one shall be signed in the case of a company by the chairman and two directors
and by the principal officer of the company and, if the company has a managing director
by that managing director and one shall be signed by the auditor who made the audit or
the actuary who made the valuation, as the case may be.

(e) Actuarial Valuation/Report (section 13)

At least once a year, every insurer carrying on life insurance business shall cause an
investigation of the life insurance business carried on by him including a valuation of his
liabilities in respect thereto and shall cause an abstract of the report of such actuary to
made in accordance with the regulations. The Authority may, having regard to the
circumstances of any particular insurer, allow him to have the investigation made as at a
date not later than two years from the date as at which the previous investigation was
made. If the investigation is made annually by any insurer, the statement need not be
appended every year but shall be appended at least once in every three years.

(f) Record of Policies and claims (Section 14)

Every insurer, in respect of all business transacted by him, shall maintain

1. a record of policies, in which shall be entered, in respect of every policy issued by the
insurer, the name and address of the policyholder, the date when the policy was
effectected and a record of any transfer, assignment or nomination of which the insurer
has notice;

2. a record of claims, every claim made together with the date of the claim, the name
and address of the claimant and the date on which the claim was discharged, or, in
the case of a claim which is rejected, the date of rejection and
the grounds thereof;
3. a record of policies and claims may be maintained in any such form, including
electronic mode, as may be specified by the regulations made under this Act;
4. Every insurer shall, in respect of all business transacted by him, endeavour to issue
policies above a specified threshold in terms of sum assured and premium in
electronic form, in the manner and form to be specified by the regulations made under
this Act.

(g) Investment of Assets (Section 27)
Every insurer shall invest and at all times keep invested assets equivalent to not less than
the sum of the amount of his liabilities to holders of life insurance policies in India on
account of matured claims, and the amount required to meet the liability on policies of life
insurance maturing for payment in India, less the amount of premiums which have fallen
due to the insurer on such policies but have not been paid and the days of grace for
payment of which have not expired, and any amount due to the insurer for loans granted
on and within the surrender values of policies of life insurance maturing for payment in
India issued by him or by an insurer whose business he has acquired and in respect of
which he has assumed liability in the following manner namely:-

1. 25% of the said sum in Government securities, a further sum equal to not less than
twenty-five per cent of the said sum in Government securities or other approved
securities; and
2. the balance in any of the approved investments as may be specified by the regulations
subject to the limitations, conditions and restrictions specified therein.

In the case of an insurer carrying on general insurance business, 25% of the assets in
Government Securities, a further sum equal to not less than ten per cent of the assets in
Government Securities or other approved securities and the balance in any other
investment in accordance with the regulations of the Authority and subject to such
limitations, conditions and restrictions as may be specified by the Authority in this regard.

No insurer carrying on life insurance business shall invest or keep invested any part of his
controlled fund and no insurer carrying on general business shall invest or keep invested
any part of his assets otherwise than in any of the approved investments as may be
specified by the regulations subject to such limitations, conditions and restrictions therein.
(Section 27A)

All assets of an insurer carrying on general insurance business shall subject to such
conditions, if any, as may be prescribed, be deemed to be assets invested or kept invested
in approved investments specified in section 27. (Section 27B)

An insurer may invest not more than five per cent in aggregate of his controlled fund or
assets in the companies belonging to the promoters, subject to such conditions as may be
specified by the regulations. (Section 27C)
(h) **Prohibition of loans (Section 29)**

No insurer shall grant loans or temporary advances either on hypothecation of property or on personal security or otherwise, except loans on life insurance policies issued by him within their surrender value, to any director, manager, actuary, auditor or officer of the insurer, if a company or to any other company or firm in which any such director, manager, actuary or officer holds the position of a director, manager, actuary, officer or partner. This shall not apply to such loans made by an insurer to a banking company, as may be specified by the Authority. Further this shall not be applicable from granting such loans or advances to a subsidiary company or to any other company of which the company granting the loan or advance is a subsidiary company if the previous approval of the Authority is obtained for such loan or advance. The provisions of section 185 of the Companies Act, 2013 shall not apply to a loan granted to a director of an insurer being a company, if the loan is one granted on the security of a policy on which the insurer bears the risk and the policy was issued to the director on his own life, and the loan is within the surrender value of the policy.

(i) **Liability of directors for contravention (Section 30)**

If by reason of a contravention of any of the provisions of section 27, 27A, 27B, 27C, 27D or section 29, any loss is sustained by the insurer or by the policyholders, every director, manager or officer who is knowingly a party to such contravention shall, without prejudice to any other penalty to which he may be liable under this Act, be jointly and severally liable to make good the amount of such loss.

(j) **Obligations of Insurers in respect of third party risks of motor vehicles (Section 32D)**

Every insurer carrying on general insurance business shall, after the commencement of the Insurance Laws (Amendment) Act, 2015, underwrite such minimum percentage of insurance business in third party risks of motor vehicles as may be specified by the regulations: The Authority may, by regulations, exempt any insurer who is primarily engaged in the business of health, re-insurance, agriculture, export credit guarantee, from the application of this section. If an insurer fails to comply with the provisions of section 32B, section 32C and section 32D, he shall be liable to a penalty not exceeding twenty-five crore rupees. (Section 105B)

(k) **Power of investigation and inspection by authority (Section 33)**

The Authority may, at any time, if it considers expedient to do so by order in writing, direct any person ("Investigating Officer") specified in the order to investigate the affairs of any insurer or intermediary or insurance intermediary, as the case may be, and to report to the Authority on any investigation made by such Investigating Officer: The Investigating Officer may, wherever necessary, employ any auditor or actuary or both for the purpose of assisting him in any investigation under this section. Notwithstanding anything to the contrary contained in section 210 of the Companies Act, 2013, the Investigating Officer may, at any time, and shall, on being directed so to do by the Authority, cause an inspection to be made by one or more of his officers of the books of account of any insurer or intermediary or insurance intermediary, as the case may be, and the Investigating Officer
shall supply to the insurer or intermediary or insurance intermediary, as the case may be, a copy of the report on such inspection.

It shall be the duty of every manager, managing director or other officer of the insurer including a service provider, contractor of an insurer where services are outsourced by the insurer, or intermediary or insurance intermediary, as the case may be, to produce before the Investigating Officer directed to make the investigation or inspection, all such books of account, registers, other documents and the database in his custody or power and to furnish him with any statement and information relating to the affairs of the insurer or intermediary or insurance intermediary, as the case may be, as the Investigating Officer may require of him within such time as the said Investigating Officer may specify. The Investigating officer shall make a report to the Authority on such inspection and the Authority may after giving such opportunity to the insurer or intermediary to make a representation. All expenses incidental to any investigation shall be defrayed by the insurer or intermediary or insurance intermediary and shall have priority over the debts due from the insurer and shall be recoverable as an arrear of land revenue.

(l) **Prohibition of payment by way of commission or otherwise for procuring business (Section 40)**

No person shall, pay or contract to pay any remuneration or reward whether by way of commission or otherwise for soliciting or procuring insurance business in India to any person except an insurance agent or an intermediary or insurance intermediary in such manner as may be specified by the regulations. No insurance agent or intermediary or insurance intermediary shall receive or contract to receive commission or remuneration in any form in respect of policies issued in India, by an insurer in any form in respect of policies issued in India, by an insurer except in accordance with the regulations specified in this regard.

(m) **Appointment of insurance agents (Section 42)**

An insurer may appoint any person to act as insurance agent for the purpose of soliciting and procuring insurance business. Such person should not suffer from any of the disqualifications. Further no person shall act as an insurance agent for more than one life insurer, one general insurer, one health insurer and one of each of the other mono-line insurers: The Authority shall, while framing regulations, ensure that no conflict of interest is allowed to arise for any agent in representing two or more insurers for whom he may be an agent.

(n) **Prohibition of insurance business through principal agent, special agent and multilevel marketing (Section 42A)**

No insurer shall, on or after the commencement of the Insurance Laws (Amendment) Act, 2015, appoint any principal agent, chief agent, and special agent and transact any insurance business in India through them. No person shall allow or offer to allow, either directly or indirectly, as an inducement to any person to take out or renew or continue an insurance policy through multilevel marketing scheme. The Authority may, through an officer authorised in this behalf, make a complaint to the appropriate police authorities against the entity or persons involved in the multilevel marketing scheme. *multilevel
marketing scheme" means any scheme or programme or arrangement or plan (by whatever name called) for the purpose of soliciting and procuring insurance business through persons not authorised for the said purpose with or without consideration of whole or part of commission or remuneration earned through such solicitation and procurement and includes enrolment of persons into a multilevel chain for the said purpose either directly or indirectly.

(o) **Policy not to be called in question after three years (Section 45)**

No policy of life insurance shall be called in question on any ground whatsoever after the expiry of three years from the date of the policy, i.e., from the date of issuance of the policy or the date of commencement of risk or the date of revival of the policy or the date of the rider to the policy, whichever is later. A policy of life insurance may be called in question at any time within three years from the date of issuance of the policy or the date of commencement of risk or the date of revival of the policy or the date of the rider to the policy, whichever is later, on the ground of fraud. The insurer shall have to communicate in writing to the insured or the legal representatives or nominees or assignees of the insured the grounds and materials on which such decision is based.

A policy of life insurance may be called in question at any time within three years from the date of issuance of the policy or the date of commencement of risk or the date of revival of the policy or the date of the rider to the policy, whichever is later, on the ground that any statement of or suppression of a fact material to the expectancy of the life of the insured was incorrectly made in the proposal or other document on the basis of which the policy was issued or revived or rider issued:

Provided that the insurer shall have to communicate in writing to the insured or the legal representatives or nominees or assignees of the insured the grounds and materials on which such decision to repudiate the policy of life insurance is based:

Provided further that in case of repudiation of the policy on the ground of misstatement or suppression of a material fact, and not on the ground of fraud, the premiums collected on the policy till the date of repudiation shall be paid to the insured or the legal representatives or nominees or assignees of the insured within a period of ninety days from the date of such repudiation.

Explanation.—For the purposes of this sub-section, the misstatement of or suppression of fact shall not be considered material unless it has a direct bearing on the risk undertaken by the insurer, the onus is on the insurer to show that had the insurer been aware of the said fact no life insurance policy would have been issued to the insured.

Nothing in this section shall prevent the insurer from calling for proof of age at any time if he is entitled to do so, and no policy shall be deemed to be called in question merely because the terms of the policy are adjusted on subsequent proof that the age of the life insured was incorrectly stated in the proposal.

(p) **Agent/intermediary not to be a director (Section 48A)**
No insurance agent or intermediary or insurance intermediary shall be eligible to be or remain a director in insurance company. Any director holding office at the commencement of the Insurance Laws (Amendment) Act, 2015 shall not become ineligible to remain a director by reason of this section until the expiry of six months from the date of commencement of the said Act. The Authority may permit an agent or intermediary or insurance intermediary to be on the Board of an insurance company subject to such conditions or restrictions as it may impose to protect the interest of policyholders or to avoid conflict of interest.

(q) **Prohibition of business on dividing business (Section 52)**

No insurer shall commence any business upon the dividing principle, that is to say, on the principle that the benefit secured by a policy is not fixed but depends either wholly or partly on the result of a distribution of certain sums amongst policies becoming claims within certain time-limits, or on the principle that the premiums payable by a policyholder depend wholly or partly on the number of policies becoming claims within certain time-limits: This does not deemed to prevent an insurer from allocating bonuses to holders of policies of life insurance as a result of a periodical actuarial valuation either as reversionary additions to the sums insured or as immediate cash bonuses or otherwise.

(r) **Councils of Life and General Insurance (Section 64C)**

On and from the date of commencement of this Act, the existing Life Insurance Council, a representative body of the insurers, who carry on the life insurance business in India; and the existing General Insurance Council, a representative body of insurers, who carry on general, health insurance business and re-insurance in India, shall be deemed to have been constituted as the respective Councils under this Act.

(s) **Surveyors or loss assessors (Section 64UM)**

No person shall act as a surveyor or loss assessor in respect of general insurance business after the expiry of a period of one year from the commencement of the Insurance Laws (Amendment) Act, 2015, unless he possesses such academic qualifications as may be specified by the regulations made under this Act; and is a member of a professional body of surveyors and loss assessors, namely, the Indian Institute of Insurance Surveyors and Loss Assessors. In the case of a firm or company, all the partners or directors or other persons, who may be called upon to make a survey or assess a loss reported, as the case may be, shall fulfil the same requirements. Every surveyor and loss assessor shall comply with the code of conduct in respect of his duties, responsibilities and other professional requirements, as may be specified by the regulations made under the Act.

(t) **Assets and liabilities how to be valued (Section 64V)**

Assets shall be valued at value not exceeding their market or realisable value and certain assets may be excluded by the Authority in the manner as may be specified by the regulations made in this behalf. A proper value shall be placed on every item of liability of the insurer in the manner as may be specified by the regulations made in this behalf. Every insurer shall furnish to the Authority along with the returns required to be filed under this Act, a statement, certified by an Auditor, approved by the Authority in respect of general
overview of banking & insurance laws

insurance business or an actuary approved by the Authority in respect of life insurance business, as the case may be, of his assets and liabilities assessed in the manner required by this section as on the 31st day of March of each year within such time as may be specified by the regulations.

(u) **Sufficiency of assets (Section 64VA)**

Every insurer and re-insurer shall at all times maintain an excess of value of assets over the amount of liabilities of, not less than fifty per cent of the amount of minimum capital as stated under section 6 and arrived at in the manner specified by the regulations. An insurer or re-insurer, as the case may be, who does not comply with shall be deemed to be insolvent and may be wound-up by the court on an application made by the Authority. The Authority shall by way of regulation made for the purpose, specify a level of solvency margin known as control level of solvency on the breach of which the Authority shall act in accordance with without prejudice to taking of any other remedial measures as deemed fit.

Thus, the amendment Act incorporate enhancements in the Insurance Laws in keeping with the evolving insurance sector scenario and regulatory practices across the globe. The amendments will enable the Regulator to create an operational framework for greater innovation, competition and transparency, to meet the insurance needs of citizens in a more complete and subscriber friendly manner. The amendments are expected to enable the sector to achieve its full growth potential and contribute towards the overall growth of the economy and job creation.

**THE INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY ACT, 1999**

1. **Introduction**

Before the IRDA Act 1999, came into being, Controller of Insurance appointed under section 2B of Insurance Act 1938 performs the function of superintendence, control and management of all kinds of Insurance companies. But after nationalisation of Life Insurance in 1956 and General Insurance in 1972, the role of the Controller became dormant, until 1999. After Indian economy got liberalised during early 1990's, competitions from private Indian companies became imperative. As a result a high powered committee was set up under the chairmanship of former R.B.I. Governor, Shri R.N. Malhotra, examine the current status of Indian Insurance Industry and recommend changes, if any for efficient and economical functioning of it, keeping in view the Indian financial system. The Committee later recommended establishment of a regulatory framework to oversee the proper functioning of the Indian Insurance Industry. The importance of such a framework was highlighted by the former Finance Minister Shri Yaswant Sinha while moving the Finance Bill of 1998 – 99. Later the Insurance Regulatory and Development Authority Act 1999 (Act No. 41 of 1999) became operative from 29th December, 1999 after receiving Presidential assent.

2. **Important Definitions**
Appointed Day: Sec – 2 (a): Appointed day means the date on which the Authority is established under sub – section (1) of Sec – 3.

Authority: Sec 2 (b): “Authority” means the Insurance Regulatory and Development Authority of India established under Sub – section (1) of Sec – 3.

Chairperson: Sec – 2 (c): “Chairperson” means the Chairperson of the Authority.

Fund: Sec – 2 (d): “Fund” means the Insurance Regulatory and Development Authority Fund constituted under Sub – Section (1) of Section 16.

Interim Insurance Regulatory Authority: Sec – 2 (e): “Interim Insurance Regulatory Authority” means that Insurance Regulatory Authority set up by the Central Government through Resolution No. 17 (2) /94 Ins – V, dated, the 23rd January, 1996.

Intermediary or Insurance Intermediary: Sec 2 (f): “Intermediary or Insurance Intermediary” includes insurance brokers, reinsurance brokers, Insurance Consultants, corporate agents, third party administrator, surveyors and loss assessors and such other entities, as may be notified by the Authority from time to time.

Members: Sec – 2 (g) “Member” means a whole time or part-time member of the “Authority” and includes the Chairperson.

3. Insurance Regulatory and Development Authority of India: (Sections 3-12)

The Central Government by notification appoint such ‘Authority’ in the nature of body corporate enjoying all the characteristics of such entity along with contractual powers.

The Head Office of such ‘Authority’ is to be decided by the Central Government.

The members of such ‘Authority appointed by the Central Government depending upon their expertise and experience in the field of Insurance, Law, Economic Accountancy, etc.

The member consists of: (a) Chairman.

(b) Five Whole Time members (maximum)

(c) Four Part – Time members (maximum)

One of these members should have knowledge in Life Insurance, General Insurance and Actuarial Science.

The Chairperson shall hold office for a term of five years until he reaches sixty five years. And he is eligible for re–appointment. A whole time member however can hold office for up to sixty-two years.

Moreover a member can relinquish his membership by giving three month prior notice to the Central Government or he can be removed from office under provision of Sec – 6. A member may be removed from office if he became insolvent or insane or convicted for offence involving moral turpitude or illegally established financial interest in the ‘Authority’ or acting contrary to public interest.

The remuneration for each member shall be as per prescribed Law.
The chairperson and the Whole – time member shall within two years from the date of appointment, cannot hold office under Central Government or State Government or any Insurance Sector.

All decisions regarding administrative matters are taken by the Chairperson.

The procedural aspect of the meetings of the ‘Authority’ may be determined by regulations. Resolutions are passed by simple majority and chairperson may use casting vote in case of a tie. In case, chairperson unable to attend any meeting then members attending may appoint chairperson among themselves. Any act of the ‘Authority’ cannot be invalidated simply because of any defect in appointing a member or procedural irregularity.

From time to time, authority may appoint employees and officers for efficiency in their work.

4. Transfer of Assets, liabilities, etc. of Indian Insurance Regulatory Authority (IIRA) to Insurance Regulatory Development Authority (IRDA) (Section 13)

On any appointed day, all assets and liabilities shall stand transferred from IIRA to IRDA. Here, the assets may be movable or immovable. Along with it also includes attached rights and powers. Before this, books of accounts, documents and other papers are also included.

All contractual obligations entered by IIRA with third parties till before the appointed day shall automatically transferred to IRDA.

Similarly all debts owed to IIRA also stands transferred to IRDA.

Also, legal proceedings including suits whether instituted by or against IIRA shall stand transferred to IRDA.

5. Duties, Powers and Functions of Authority: (Sec – 14)

The Authority shall have the duty to regulate, control, promote and ensure healthy development of insurance and re – insurance business. The powers and functions of the Authority includes inter-alia:

(i) Issue, modify, cancel, etc, of Registration certificate to the applicant.

(ii) Safeguarding the interests of the policyholders like insurable interests, settlement of claim, surrender value of the policy, etc.

(iii) Specifying code of conduct of the Surveyors.

(iv) Determining qualifications and training aspect of agents and intermediary.

(v) Levying fees and charges for their work.

(vi) Conducting investigations and enquiries relating to issues concerning insurance business.

(vii) Regulating and controlling business not controlled by Tariff Advisory committee under section 64 of Insurance Act 1938.
(viii) Regulatory investment funds by the Insurance Companies.
(ix) Regulating maintenance of margin of solvency.
(x) Adjudicating and settling disputes between intermediaries and insurers.
(xi) Supervising the functioning of Tariff Advisory Committee.

6. Finance, Accounts and Audit: (Sections 15 – 17)

The Central Government grants funds necessary for such Authority.
The fund shall be called as “IRDA of India Fund”. And it includes:

(i) Governmental Grants, fees and charges.
(ii) Money received by the ‘Authority’ from other sources specified by the Central Government.

The above funds shall be applied for:

(a) meeting salaries and allowances of members, officers and employees of the authority.
(b) meeting other legitimate expenses of the authority.

The ‘Authority’ has to maintain Books of Accounts and prepare Annual Financial Statements as per norms prescribed by Central Government in consultation with CAG.

The accounts of the ‘Authority’ shall be audited by the CAG according to their schedule and the expenditure required for such audit has to be borne by the ‘Authority’.

Any other person appointed by CAG may enjoy same privileges and have access to books, documents and other relevant papers.

The certified accounts of the ‘Authority’ whether audited by CAG or person appointed by CAG, to be put forward to the Central Government and the same be laid before the Parliament by such Union Government.

7. Other Matters: (Sections 18 – 32)

The ‘Authority’ is bound by the action of the Central Government regarding policy matters. However, the Authority has the leverage of operating independently relating to technical and administrative matters.

The Central Government may if situation warrants like, the Authority persistently defaulting directions of them or in public interest, may supersede the Authority for not more than six month duration, through notification and appointing a person as controller of Insurance under section 2B of the Insurance Act 1938. However, while prior to such notification, doctrine of Natural Justice has to be observed.

From the date of publication of the notification, the chairperson and other members cease to hold office and all powers, functions and duties vests on the Central Government. And also all properties shall vest on the Central Government.
The Central Government may then appoint fresh chairperson and other members before the expiration of the term of the super session. The notification and the Action Taken Report has to be placed before the Parliament at the earlier possible opportunity.

From time to time the Authority has to furnish returns, statements and other particulars regarding to any existing or proposed programme, to the Central Government.

The members and employees of the Authority shall be deemed to be public servants under section 21 of IPC while discharging their official duties. And their actions while performing their official duties are insulated from any legal proceedings, provided they have acted in good faith.

The Authority may by prior notification, establish Insurance Advisory Committee. This Committee consists of twenty-five members (maximum) excluding existing members.

The chairperson shall be the ex-officio chairperson and other existing members shall be ex-officio members of Insurance Advisory Committee. The Committee advises the Authority on various matters, including under Section 26.

The ‘Authority’ may by general or special order delegate powers and functions to any of its members or officers or employees.

The Central Government may by notification make rules relating to salary and allowances of the members, Annual Statements of Accounts, matters relating to furnishing of documents under Section 20 (1) and also matters relating to Insurance Advisory Committee under Section 25 (1).

The Authority may after consulting the committee by notification, make regulations particularly addressing the procedural aspect in conducting meetings, determining terms and conditions of the services of the officers and employees, delegating powers to the committee and other miscellaneous matters.

Each rule and regulation made under this Act to be placed before Upper House and Lower House of Parliament for thirty days, while the Parliament is in session.

Each rule or regulation shall be subjected to any modification or amendment within such period.

This Act supplements all existing Acts made with relation to Insurance Business.

The Central Government has right to remove any difficulties or impediments by making notification in the Official Gazette within two years from the appointed day.

Section 30 deals with various amendments made with respect to Insurance Act 1938 stated in the First Schedule.

Section 31 deals with amendments made with respect to Life Corporation of India Act 1956 and which is specified in the Second Schedule.

Section 32 deals with various amendments made in General Insurance Business (Nationalisation) Act 1972 which were specified in the Third Schedule.
1. Introduction

The financial sector has been one of the key drivers in India's efforts to achieve success in rapidly developing its economy. Since our existing legal framework relating to commercial transactions has not kept pace with the changing commercial practices and financial sector reforms. This has resulted in slow pace of recovery of defaulting loans and mounting levels of nonperforming assets of banks and financial institutions.

Narasimham Committee I and II and Andhyarujina Committee was constituted by the Central Government for the purpose of examining banking sector reforms have considered the need for changes in the legal system in respect of these areas. These Committees, among others, have suggested enactment of a new legislation for securitisation and empowering banks and financial institutions to take possession of the securities and to sell them without the intervention of the court. Acting on these suggestions, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 was promulgated on the 21st June, 2002 to regulate securitisation and reconstruction of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto. It extended to the whole of India.


It is an Act further to amend four laws:

(i) Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI),

(ii) Recovery of Debts due to Banks and Financial Institutions Act, 1993 (RDBDFI),

(iii) Indian Stamp Act, 1899 and

(iv) Depositories Act, 1996, and for matters connected therewith or incidental thereto.

Chapter II, of this amendment Act deals with the amendments to the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.
This amendment Act is "an act to regulate securitisation and reconstruction of financial assets and enforcement of security interest and to provide for a central database of security interests created on property rights, and for matters connected therewith or incidental thereto."

The Act deals with the following:

(a) Registration and regulation of Asset Reconstruction Companies (ARCs) by the Reserve Bank of India;

(b) Facilitating securitisation of financial assets of banks and financial institutions with or without the benefit of underlying securities;

(c) Facilitating easy transferability of financial assets by the ARC to acquire financial assets of banks and financial institutions by issue of debentures or bonds or any other security in the nature of a debenture;

(d) Empowering ARCs to raise funds by issue of security receipts to qualified buyers

(e) 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

(f) Declaration of any securitisation company or reconstruction company registered with the Reserve Bank of India as a public financial institution for the purpose of section 4A of the Companies Act, 1956

(g) Defining 'security interest' as any type of security including mortgage and change on immovable properties given for due repayment of any financial assistance given by any bank or financial institution;

(h) Empowering banks and financial institutions to take possession of securities given for financial assistance and sell or lease the same or take over management in the event of default, i.e. classification of the borrower's account as non-performing asset in accordance with the directions given or under guidelines issued by the Reserve Bank of India from time to time

(i) The rights of a secured creditor to be exercised by one or more of its officers authorised in this behalf in accordance with the rules made by the Central Government;

(j) An appeal against the action of any bank or financial institution to the concerned Debts Recovery Tribunal and a second appeal to the Appellate Debts Recovery Tribunal;

(k) Setting up or causing to be set up a Central Registry by the Central Government for the purpose of registration of transactions relating to securitisation, asset reconstruction and creation of security interest;
(l) Application of the proposed legislation initially to banks and financial institutions and empowerment of the Central Government to extend the application of the proposed legislation to non-banking financial companies and other entities.

(m) Non-application of the proposed legislation to security interests in agricultural lands, loans not exceeding rupees one lakh and cases where eighty per cent, of the loans are repaid by the borrower.
2. Structure

The Act is divided into six chapters and 42 sections:

- **Chapter I- Preliminary (Section 1-2)**
- **Chapter II- Regulation of securitisation and reconstruction of financial assets of banks and financial institutions (Section 3-12A)**
- **Chapter III- Enforcement of security interest (Section 13-19)**
- **Chapter IV- Central registry (Section 20-26A)**
- **Chapter IVA- Registration by secured creditors and other creditors (Section 26B-26E)**
- **Chapter V- Offences and penalties (Section 27-30)**
- **Chapter VI- Miscellaneous (Section 37-42)**

3. Important Concepts

The Act introduced multiple new concepts and infrastructures to support ease of recovery actions such as:

- Formation of Securitisation or reconstruction companies
- Recovery without interference of courts
- Framework for revival or reconstruction of the borrowers' business
- Central registry
- Qualified buyers
- Security receipts
4. Role of the Act

**Alternative presentation (simpler version):**

1. Proper management of the borrower's business
2. Sale or lease of business
3. Rescheduling of debts
4. Enforcement of security interest
5. Settlement of dues
6. Possession of secured assets

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5. Definitions

Some key definitions are explained below:

- **"Asset reconstruction"** means acquisition by any securitisation company (SC) or reconstruction company (RC) of any right or interest of any bank or financial institution in any financial assistance for the purpose of realisation of such financial assistance [Section 2(b)]

  The term "financial assistance" means any loan or advance granted or any debentures or bonds subscribed or any guarantees given or letters of credit established or any other credit facility extended by any bank or financial institution; [Section 2(k)]

  The purpose of acquisition by securitisation company (SC) or reconstruction company (RC) is to realise such assets and not to stay invested by becoming the shareholders of the company. However it has the right to take over the management of the business, subject to RBI's guidelines from time to time. Such realised amount should be held and applied towards redemption of investments and payment of returns assured to the QIBs

- **"Asset reconstruction company (ARC)"** means a company registered with Reserve Bank under section 3 for the purposes of carrying on the business of asset reconstruction or securitisation, or both. [Section 2(ba)]

  An ARC is not a banking company although it is regulated by RBI. Such company cannot carry out any other business other than securitisation or reconstruction.

- **"Borrower"** means any person who has been granted financial assistance by any bank or financial institution or who has given any guarantee or created any mortgage or pledge as security for the financial assistance granted by any bank or financial institution and includes a person who becomes borrower of a securitisation company or reconstruction company consequent upon acquisition by it of any rights or interest of any bank or financial institution in relation to such financial assistance or who has raised funds through issue of debt securities. [Section 2(f)]
"Default" means:
(a) non-payment of any debt or any other amount payable by the 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; or
(b) non-payment of any debt or any other amount payable by the borrower with respect to debt securities after notice of ninety days demanding payment of dues served upon such borrower by the debenture trustee or any other authority in whose favour security interest is created for the benefit of holders of such debt securities. [Section 2(j)]

Conditions for calling default under this act is:
- debt or any other amount- The amount due should be in the nature of debt.
- Secured creditor- An unsecured creditor doesn’t have recourse to this act
- Classification of NPA- A stressed asset which is yet to be classified as NPA cannot be resolved through this act.
- For non-payment of debenture or bonds to be called default, a notice of 90 days is a pre-requisite by the debenture trustee or beneficiary of the security

"Debt" shall have the meaning assigned to it in clause (g) of section 2 of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 and includes—
(a) unpaid portion of the purchase price of any tangible asset given on hire or financial lease or conditional sale or under any other contract;
(b) any right, title or interest on any intangible asset or licence or assignment of such intangible asset, which secures the obligation to pay any unpaid portion of the purchase price of such intangible asset or an obligation incurred or credit otherwise extended to enable any borrower to acquire the intangible asset or obtain licence of such asset; [Section 2(ha)]

"Financial asset" means debt or receivables and includes-
(i) a claim to any debt or receivables or part thereof, whether secured or unsecured; or
(ii) any debt or receivables secured by, mortgage of, or charge on, immovable property; or
(iii) a mortgage, charge, hypothecation or pledge of movable property; or
(iv) any right or interest in the security, whether full or part underlying such debt or receivables; or
(v) any beneficial interest in property, whether movable or immovable, or in such debt, receivables, whether such interest is existing, future, accruing, conditional or contingent; or
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(va) any beneficial right, title or interest in any tangible asset given on hire or financial lease or conditional sale or under any other contract which secures the obligation to pay any unpaid portion of the purchase price of such asset or an obligation incurred or credit otherwise provided to enable the borrower to acquire such tangible asset; or

(vb) any right, title or interest on any intangible asset or licence or assignment of such intangible asset, which secures the obligation to pay any unpaid portion of the purchase price of such intangible asset or an obligation incurred or credit otherwise extended to enable the borrower to acquire such intangible asset or obtain licence of the intangible asset;

(vi) any financial assistance; [Section 2(l)]

An asset which is not a financial asset cannot be securitised, acquired or transferred under this Act.

Example: Value of an unsecured land in the balance sheet of the borrower cannot be acquired by an ARC by way of issuing security receipts.

• "Non-performing asset (NPA)" means an asset or account of a borrower, which has been classified by a bank or financial institution as sub-standard, doubtful or loss asset,

(a) in case such bank or financial institution is administered or regulated by an authority or body established, constituted or appointed by any law for the time being in force, in accordance with the directions or guidelines relating to assets classifications issued by such authority or body;

(b) in any other case, in accordance with the directions or guidelines relating to assets classifications issued by the Reserve Bank. [Section 2(o)]

• "Qualified buyer" means a financial institution, insurance company, bank, state financial corporation, state industrial development corporation, trustee or asset reconstruction company which has been granted a certificate of registration under sub-section (4) of section 3 or any asset management company making investment on behalf of mutual fund or pension fund or a foreign institutional investor registered under the Securities and Exchange Board of India Act, 1992 (15 of 1992) or regulations made thereunder, any category of non-institutional investors as may be specified by the Reserve Bank under sub-section (1) of section 7 or any other body corporate as may be specified by the Board; [Section 2(u)]

An ARC cannot raise funds from investors which is not a qualified buyer (QB) as defined above.

For example, a manufacturing company looking to invest surplus cash by investing in the ARC, or a Public sector unit, or a strategic investor who wish to acquire the assets of the borrower company etc.

• "Securitisation" means acquisition of financial assets by any asset reconstruction company from any originator, whether by raising of funds by such asset reconstruction
company from qualified buyers by issue of security receipts representing undivided interest in such financial assets or otherwise \[\text{Section 2(z)}\];

The process of securitisation helps the ARC to acquire financial assets like Loans from banks due to which the ARC shall 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.

- **“Secured creditor”** means-
  
  (a) any bank or financial institution or any consortium or group of banks or financial institutions holding any right, title or interest upon any tangible asset or intangible asset as specified in clause (i);
  
  (b) debenture trustee appointed by any bank or financial institution; or
  
  (c) an asset reconstruction company whether acting as such or managing a trust set up by such asset reconstruction company for the securitisation or reconstruction, as the case may be; or
  
  (d) debenture trustee registered with the Board appointed by any company for secured debt securities; or
  
  (e) any other trustee holding securities on behalf of a bank or financial institution, in whose favour security interest is created by any borrower for due repayment of any financial assistance \[\text{section 2 (zd)}\]

- **“Security interest”** means right, title and interest of any kind, other than those specified in section 31, upon property created in favour of any secured creditor and includes—
  
  (a) any mortgage, charge, hypothecation, assignment or any right, title or interest of any kind, on tangible asset, retained by the secured creditor as an owner of the property, given on hire or financial lease or conditional sale or under any other contract which secures the obligation to pay any unpaid portion of the purchase price of the asset or an obligation incurred or credit provided to enable the borrower to acquire the tangible asset; or
  
  (b) such right, title or interest in any intangible asset or assignment or licence of such intangible asset which secures the obligation to pay any unpaid portion of the purchase price of the intangible asset or the obligation incurred or any credit provided to enable the borrower to acquire the intangible asset or licence of intangible asset \[\text{Section 2(zf)}\];

A creditor shall not be called as secured creditor unless its interest over the assets of the debtor or borrower is covered under the above definition. Refer section 31 (Provisions of this Act not to apply in certain cases) for specific exclusions of rights that shall not be treated as security interest.
6. Regulation of securitisation and reconstruction of financial assets of banks and financial institutions

This part of the Act is covered in chapter II of the Act, comprising of Sections 3 – 12. This chapter provides for regulation of securitisation and reconstruction of financial assets of banks and financial institutions.

(I) Registration of ARCs (Section 3)

• Commencement of business of securitisation or asset reconstruction: Such a company can commence or carry on the business of securitisation or asset reconstruction only after obtaining a certificate of registration granted under this section and having the net owned fund of not less than 'one hundred crore rupees or such other higher amount as the Reserve Bank, may, by notification, specify.

However, the term “net owned fund” is not defined in the Act and hence we have to refer to the definition of “net owned fund” as mentioned in the explanation to Section 45I of the Reserve Bank of India Act.

• Conditions: The Reserve Bank may, for the purpose of considering to grant its approval for the application for registration of an ARC to commence or carry on the business of securitisation or asset reconstruction, as the case may be, require to be satisfied, by an inspection of records or books of such ARC, or otherwise, that the following conditions are fulfilled, namely:

  (a) that the ARC has not incurred losses in any of the three preceding financial years;

  (b) that such ARC 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 dates on the investments made in the company by the qualified buyers or other persons;

  (c) that the directors of ARC have adequate professional experience in matters related to finance, securitisation and reconstruction;

  (d) that any of its directors has not been convicted of any offence involving moral turpitude;

  (e) that a sponsor of an ARC is a fit and proper person in accordance with the criteria as may be specified in the guidelines issued by the Reserve Bank for such persons;

  (f) that ARC has complied with or is in a position to comply with prudential norms specified by the Reserve Bank.

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1 Vide RBI Notification dated 28th April, 2017, in exercise of the powers conferred by clause (b) of subsection (1) of section 3 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002, Reserve Bank of India hereby specifies that the Net Owned Fund (NOF) for Asset Reconstruction Companies (ARCs) shall be minimum Rupees One Hundred Crore (in place of 2 Crore rupees ) on an ongoing basis with effect from the date of this Notification.
(g) that ARC has complied with one or more conditions specified in the guidelines issued by the Reserve Bank for the said purpose.

- **Issue of certificate of registration to ARC:** A certificate of registration is thereafter granted to the ARC to commence or carry on business of securitisation or asset reconstruction, and it must be noted that the Reserve Bank may also prescribe any other conditions, which it may consider, fit to impose. In case the Reserve Bank is of the opinion that the above conditions are not satisfied then it may reject the application, after the applicant is given a reasonable opportunity of being heard.

- **Requirement of prior approval of RBI:** Once a company is registered as an ARC, it must obtain prior approval of the Reserve Bank for the following purposes:-
  (a) any substantial change in its management, including appointment of any director managing director or chief executive officer
  (b) change of location of its registered office
  (c) change in its name

- **Decision of RBI shall be final & binding:** The decision of the Reserve Bank, whether the change in management of an ARC is a substantial change in its management or not, shall be final and binding. The expression "substantial change in management" means the change in the management by way of transfer of shares or change affecting the sponsorship in the company by way of transfer of shares or amalgamation or transfer of the business of the company.

(II) **Cancellation of certificate of registration (Section 4)**

- The Reserve Bank may cancel a certificate of registration granted to an ARC, if such company-
  (i) ceases to carry on the business of securitisation or asset reconstruction; or
  (ii) ceases to receive or hold any investment from a qualified buyer; or
  (iii) has failed to comply with any conditions subject to which the certificate of registration has been granted to it; or
  (iv) at any time fails to fulfil any of the conditions referred to in clauses (a) to (g) of subsection (3) of section 3; or
  (v) fails to-
    (a) comply with any direction issued by the Reserve Bank under the provisions of this Act; or
    (b) maintain accounts in accordance with the requirements of any law or any direction or order issued by the Reserve Bank under the provisions of this Act; or
    (c) submit or offer for inspection its books of account or other relevant documents when so demanded by the Reserve Bank; or
(d) obtain prior approval of the Reserve Bank required under sub-section (6) of section 3:

- Before cancelling a certificate of registration on the ground that the ARC has failed to comply with the provisions of clause (c) or has failed to fulfil any of the conditions referred to in clause (d) or sub-clause (iv) of clause (e), the Reserve Bank, unless it is of the opinion that the delay in cancelling the certificate of registration granted under sub-section (4) of section 3 shall be prejudicial to the public interest or the interests of the investors or the ARC, shall give an opportunity to such company on such terms as the Reserve Bank may specify for taking necessary steps to comply with such provisions or fulfilment of such conditions.

- **Appeal to an order of cancellation:** In case the ARC is aggrieved by the order of cancellation of certificate of registration by the Reserve Bank, then it may prefer an appeal, within a period of thirty days from the date on which such order of cancellation is communicated to it, to the Central Government (Secretary, Ministry of Finance, and Government of India). The Central Government must also give such company a reasonable opportunity of being heard before rejecting the appeal.

- It must be noted that an ARC, which is holding investments of qualified buyers and whose application for grant of certificate of registration has been rejected or certificate of registration has been cancelled shall, notwithstanding such rejection or cancellation be deemed to be an ARC until it repays the entire investments held by it (together with interest, if any) within such period as specified by the Reserve Bank.

(III) **Acquisition of rights or interest in financial assets (Section 5)**

- **Acquiring of financial assets of any bank or financial institution:** Notwithstanding anything contained in any agreement or any other law for the time being in force, any ARC may acquire financial assets of any bank or financial institution-
  
  (i) 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

  (ii) 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.

- Any document executed by any bank or financial institution as mentioned above, in favour of the ARC acquiring financial assets for the purposes of asset reconstruction or securitisation shall be exempted from stamp duty in accordance with the provisions of section 8F of the Indian Stamp Act, 1899

  Provided that the provisions of this sub-section shall not apply where the acquisition of the financial assets by the asset reconstruction company is for the purposes other than asset reconstruction or securitisation.
Such exemption is provided in order to encourage banks or FIs to resolve non performing assets (NPA) issues by offloading it to ARCs.

- **Debenture**: As we commonly known, is an acknowledgement of debt. Bond also refers to the same nature of instrument as a debenture. Both of them acknowledge a debt and hence an obligation to pay.

- **In case where bank or financial institution is a lender in relation to any financial assets acquired by the ARC**: Then such ARC 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 the subject financial assets.

  If the bank or financial institution is holding any right, title or interest upon any tangible asset or intangible asset to secure payment of any unpaid portion of the purchase price of such asset or an obligation incurred or credit otherwise provided to enable the borrower to acquire the tangible asset or assignment or licence of intangible asset, such right, title or interest shall vest in the asset reconstruction company on acquisition of such assets.

- **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 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 ARC, as the case may be, and may be enforced or acted upon as fully and 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 ARC, as the case may be.

- **If**, on the date of acquisition of financial asset, any suit, appeal or other proceeding 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 the same shall not abate, or be discontinued or be, in any way, prejudicially affected by reason of the acquisition of financial asset by the ARC, as the case may be, but the suit, appeal or other proceeding may be continued, prosecuted and enforced by or against the ARC, as the case may be.

- **On acquisition of financial assets**, the ARC, 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 ARC in such pending suit, appeal or other proceedings.
(IV) Transfer of pending applications to any one of Debts Recovery Tribunals in certain cases (Section 5A)

- If any financial asset, of a borrower acquired by an ARC, comprise of secured debts or more than one bank or financial institution for recovery of which such banks or financial institutions has filed applications before two or more Debts Recovery Tribunals, the ARC may file an application to the Appellate Tribunal having jurisdiction over any of such Tribunals in which such applications are pending for transfer of all pending applications to any one of the Debts Recovery Tribunals as it deems fit.

- On receipt of such application for transfer of all pending applications under sub-section (1), the Appellate Tribunal may, after giving the parties to the application an opportunity of being heard, pass an order for transfer of the pending applications to any one of the Debts Recovery Tribunals.

- Notwithstanding anything contained in the Recovery of Debts Due to Banks and Financial Institutions Act, 1993, any order passed by the Appellate Tribunal under sub-section (2) shall be binding on all the Debts Recovery Tribunals referred to in sub-section (1) as if such order had been passed by the Appellate Tribunal having jurisdiction on each such Debts Recovery Tribunal.

- Any recovery certificate, issued by the Debts Recovery Tribunal to which all the pending applications are transferred under sub-section (2), shall be executed in accordance with the provisions contained in sub-section (23) of section 19 and other provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 shall, accordingly, apply to such execution.

(V) Notice to obligor and discharge of obligation of such obligor (Section 6)

- The bank or financial institution may give a notice of acquisition of financial assets by any ARC to the concerned obligor and any other concerned person and to the concerned registering authority.

- The obligor shall make payment to the concerned ARC in discharge of any of the obligations in relation to the financial asset specified in the notice

(VI) Issue of security by raising of receipts or funds by ARC (Section 7)

- Any ARC, may, after acquisition of any financial asset under section 5(1), offer security receipts to qualified buyers (or such other category of investors including non-institutional investors as may be specified by the Reserve Bank in consultation with the Board, from time to time) for subscription in accordance with the provisions of those Acts.

- An ARC may raise funds from the qualified buyers by formulating schemes for acquiring financial assets and shall keep and maintain separate and distinct accounts in respect of each such scheme for every financial asset acquired out of investments made by a qualified buyer and ensure that realisations of such financial asset is held and applied towards redemption of investments and payment of returns assured on such investments under the relevant scheme.
(VII) Exemption from registration of security receipt (Section 8)

- any security receipt issued by the ARC and not creating, declaring, assigning, limiting or extinguishing any right, title or interest, to or in immovable property except in so far as it entitles the holder of the security receipt to an undivided interest afforded by a registered instrument, or any transfer of security receipts, shall not require compulsory registration under section 17 of the Registration Act, 1908.

(VIII) Measures for assets reconstruction (Section 9)

- AN ARC may, provide for any one or more of the following measures, for the purposes of asset reconstruction:
  
  (a) the proper management of the business of the borrower, by change in, or takeover of, the management of the business of the borrower;
  
  (b) the sale or lease of a part or whole of the business of the borrower;
  
  (c) rescheduling of payment of debts payable by the borrower;
  
  (d) enforcement of security interest in accordance with the provisions of this Act;
  
  (e) settlement of dues payable by the borrower;
  
  (f) taking possession of secured assets in accordance with the provisions of this Act;
  
  (g) conversion of any portion of debt into shares of a borrower company:

Provided that conversion of any part of debt into shares of a borrower company shall be deemed always to have been valid, as if the provisions of this clause were in force at all material times.

- The Reserve Bank shall, for the purposes as given above, determine the policy and issue necessary directions including the direction for regulation of management of the business of the borrower and fees to be charged.

- The asset reconstruction company shall take measures in accordance with policies and directions of the Reserve Bank determined under section 9(2).
(IX) Other functions of ARC (Section 10)

- Any ARC may-
  1. act as an agent for any bank or financial institution for the purpose of recovering their dues from the borrower on payment of such fees or charges as may be mutually agreed upon between the parties;
  2. act as a manager referred to section 13(4)(c) on such fee as may be mutually agreed upon between the parties;
  3. act as receiver if appointed by any court or tribunal

Provided that no ARC shall act as a manager if acting as such gives rise to any pecuniary liability.

- No ARC which has been granted a certificate of registration section 3(4), shall commence or carry on, without prior approval of the Reserve Bank, any business other than that of securitisation or asset reconstruction.

Provided that an ARC which is carrying on, on or before the commencement of this Act, any business other than the business of securitisation or asset reconstruction or business referred to in sub-section (1), shall cease to carry on any such business within one year from the date of commencement of this Act.

- For the purposes of this section, ARC does not include its subsidiary.

(X) Resolution of disputes (Section 11)

Where any dispute relating to securitisation or reconstruction or non-payment of any amount due including interest arises amongst any of the parties, namely,

1. the bank, or
2. financial institution, or
3. ARC or
4. qualified buyer,

Such dispute shall be settled by conciliation or arbitration as provided in the Arbitration and Conciliation Act, 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.

(XI) Power of Reserve Bank to determine policy and issue directions (Section 12)

- In the public interest, Reserve bank may determine the policy and give directions to any ARC in matters relating to income recognition, accounting standards, making provisions for bad and doubtful debts, capital adequacy based on risk weights for assets and also relating to deployment of funds by the ARC.

- Without prejudice to the generality as above, the Reserve bank may give directions to any ARC in particular as to:
(a) the type of financial asset of a bank or Financial institution which can be acquired and procedure for acquisition of such assets and valuation thereof;

(b) the aggregate value of financial assets which may be acquired by any securitisation company or reconstruction company.

(c) the fee and other charges which may be charged or incurred for management of financial assets acquired by any asset reconstruction company;

(d) transfer of security receipts issued to qualified buyers

(XII) Power of Reserve Bank to Call for Statements and information (Section 12 A)

The Reserve Bank may direct ARC to furnish it within such time as may be specified by the Reserve Bank, with such statements and information relating to the business or affairs of such securitisation company or reconstruction company (including any business or affairs with which such company is concerned) as the Reserve Bank may consider necessary or expedient to obtain for the purpose of this Act.

(XIII) Power of Reserve Bank to carry out audit and inspection (Section 12 B)

• The Reserve Bank may, for the purposes of this Act, carry out or caused to be carried out audit and inspection of an asset reconstruction company from time to time.

• It shall be the duty of an asset reconstruction company and its officers to provide assistance and cooperation to the Reserve Bank to carry out audit or inspection.

• Where on audit or inspection or otherwise, the Reserve Bank is satisfied that business of an asset reconstruction company is being conducted in a manner detrimental to public interest or to the interests of investors in security receipts issued by such asset reconstruction company, the Reserve Bank may, for securing proper management of an asset reconstruction company, by an order—
  
  (a) remove the Chairman or any director or appoint additional directors on the board of directors of the asset reconstruction company; or

  (b) appoint any of its officers as an observer to observe the working of the board of directors of such asset reconstruction company:

  Provided that no order for removal of Chairman or director under clause (a) shall be made except after giving him an opportunity of being heard.

• It shall be the duty of every director or other officer or employee of the asset reconstruction company to produce before the person, conducting an audit or inspection under sub-section (1), all such books, accounts and other documents in his custody or control and to provide him such statements and information relating to the affairs of the asset reconstruction company as may be required by such person within the stipulated time specified by him.
7. **Enforcement of security interest**

Provisions dealing with enforcement of security interest are contained in Chapter III of the Act, comprising of Sections 13 – 19.

(I) **Enforcement of security interest (Section 13)**

- Notwithstanding anything contained in section 69 or section 69A of the Transfer of Property Act, 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.

- **Where borrower makes a default payment of debt**: 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) of Section 13.

Provided that—

(i) the requirement of classification of secured debt as non-performing asset under this sub-section shall not apply to a borrower who has raised funds through issue of debt securities; and

(ii) in the event of default, the debenture trustee shall be entitled to enforce security interest in the same manner as provided under this section with such modifications as may be necessary and in accordance with the terms and conditions of security documents executed in favour of the debenture trustee;

- **Notice prescribing the details of the debts**: This notice 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. The procedure for the service of the notice is prescribed in the Security Interests (Enforcement) Rules.

- **Objection or rejection to the borrower on the notice**: If, on receipt of the notice, 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 15 days of receipt of such representation or objection the reasons for non-acceptance of the representation or objection to the borrower:

- **No right to borrower to prefer an application**: 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.
• **Borrower fails to discharge his liability:** if the borrower fails to discharge his liability in full within the above specified period, the secured creditor may take recourse to one or more of the following measures to recover his secured debt:

(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 business 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 for 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.

• **Modes of enforcement of security**

- take possession of the secured assets
- take over the management (which is relatable to secured debt)
- appoint any person as the manager, to manage the secured assets
- Demand notice to the person who has acquired the secured assets

• **Discharge from payment:** Any payment made by any person referred to in section 5(4)(d) to the secured creditor shall give such person a valid discharge as if he has made payment to the borrower.
- **Right with respect to the immovable property**: 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. [Sub-section (5A)]

  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 of enforcement of security interest is taken by the secured creditor, under sub-section (4) of section 13. [Sub-section (5B)]

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

- **Right related to transfer of secured assets by the secured creditor**: Any transfer of secured asset after taking possession thereof or takeover 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.

- **Recovery of expenses from the borrower**: Where any action has been taken against a borrower, 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—
  
  (a) firstly, in payment of such costs, charges and expenses and

  (b) 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.

- **Payment of dues of the secured creditors**: Where the amount of dues of the secured creditor together with all costs, charges and expenses incurred by him is tendered to the secured creditor at any time before the date of publication of notice for public auction or inviting quotations or tender from public or private treaty for transfer by way of lease, assignment or sale of the secured assets,—

  (a) the secured assets shall not be transferred by way of lease assignment or sale by the secured creditor; and

  (b) in case, any step has been taken by the secured creditor for transfer by way of lease or assignment or sale of the assets before tendering of such amount under this subsection, no further step shall be taken by such secured creditor for transfer by way of lease or assignment or sale of such secured assets.
• **Joint Financing:** Subject to the provisions of the Insolvency and Bankruptcy Code, 2016, 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. [Section 13(9)]. But in 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 (Corresponding section 326 of the Companies Act, 2013).

• **Secured creditors may retain the sale proceeds of his secured assets:** 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 (Corresponding section 325 of the Companies Act, 2013), 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 (Corresponding section 326 of the Companies Act, 2013) of that Act:

• **Role of liquidator with respect to workmen dues:** Provided also that liquidator referred to in the second proviso shall intimate the secured creditor the workmen's dues in accordance with the provisions of section 529A of the Companies Act, 1956 (Corresponding section 326 of the Companies Act, 2013) 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 estimate dues with the liquidator:

• **In case of deposits of amount of workmen dues by secured creditor:** 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:

• **Furnishing of undertaking by secured creditor:** 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 three-fourth 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.

• **Filing of an application by secured creditor:** 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.

- **Rights of secured creditors in relation to secured assets**: 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 measured specifies in clause (a) to (d) of sub-section (4) in relation to the secured assets under this Act.

- 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.

- **No transfer of secured assets by borrower**: No borrower shall, after receipt of notice, 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.

(II) **Chief Metropolitan Magistrate or District Magistrate to assist secured creditor in taking possession of secured asset (Section 14)**

The secured creditor may, for the purpose of taking possession or control of secured asset, request, in writing, the Chief Metropolitan Magistrate or the District Magistrate within whose jurisdiction any such secured asset or other documents relating thereto may be situated or found, to take possession thereof, and the Chief Metropolitan Magistrate or, as the case may be, the District Magistrate shall, on such request being made to him--

(a) take possession of such asset and documents relating thereto; and

(b) forward such asset and documents to the secured creditor

within a period of thirty days from the date of application.

Provided further that if no order is passed by the Chief Metropolitan Magistrate or District Magistrate within the said period of thirty days for reasons beyond his control, he may, after recording reasons in writing for the same, pass the order within such further period but not exceeding in aggregate sixty days.

(III) **Manner and effect of takeover of management (Section 15)**

- **Appointment of persons by secured creditors**: When the management of business of a borrower is taken over by an ARC under section 9(a) or, by a secured creditor under section 13(4)(b) as the case may be, the secured creditor may, by publishing a notice in a newspaper published in English language and in a newspaper published in an Indian language in circulation in the place where the principal office of the borrower is situated, appoint as many persons as it thinks fit-
(a) in a case in which the borrower is a company under the Companies Act, 1956, to be the directors of that borrower in accordance with the provisions of that Act; or

(b) in any other case, to be the administrator of the business of the borrower

**Manner and effect of takeover of management**

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<th>In case where borrower is a:</th>
<th>Appoint persons as:</th>
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<td>Company under Companies Act, 1956 (i.e., the Companies Act, 2013)</td>
<td>Directors of the borrower</td>
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<tr>
<td>Any other cases</td>
<td>Administrator of the business of the borrower</td>
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- **On publication notice**: All persons holding office as directors of the company (if the borrower is a company) and in any other case, all persons holding any office having power of superintendence, direction and control of the business of the borrower immediately before the publication of the above notice, shall be deemed to have vacated their offices.

- **When any contract of management shall be deemed to be terminated**: Any contract of management between the borrower and any director or manager thereof holding office as such immediately before publication of the above notice, shall be deemed to be terminated. The directors or the administrators appointed under this section shall take such steps as may be necessary to take into their custody or under their control all the property, effects and actionable claims to which the business of the borrower is, or appears to be, entitled and all the property and effects of the business of the borrower shall be deemed to be in the custody of the directors or administrators, as the case may be, as from the date of the publication of the above notice.

- **Exercise of the powers of the person so appointed for the borrowers**: All directors appointed in accordance with the above notice shall, for all purposes, be the directors of the company of the borrower and such directors or the administrators (if the borrower is other than a company) appointed under section 15, shall only be entitled to exercise all the powers of the directors or as the case may be, of the persons exercising powers of superintendence, direction and control, of the business of the borrower whether such powers are derived from the memorandum or articles of association of the company of the borrower or from any other source.

- **Management of borrower taken by the secured creditor**: Where the management of the business of a borrower, being a company as defined in the Companies Act, 1956 (i.e., the Companies Act, 2013), is taken over by the secured creditor, then, notwithstanding anything contained, such borrower- in the said Act or in the memorandum or articles of association of such company -
(a) 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;

(b) no resolution passed at any meeting of the shareholders of such company shall be given effect to unless approved by the secured creditor;

(c) no proceeding 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.

- **Obligation of secured creditor:** The secured creditor is under an obligation to restore the management of the business of the borrower, on realisation of his debt in full, in case of takeover of the management of the business of a borrower by such secured creditor.

- Provided that if any secured creditor jointly with other secured creditors or any asset reconstruction company or financial institution or any other assignee has converted part of its debt into shares of a borrower company and thereby acquired controlling interest in the borrower company, such secured creditors shall not be liable to restore the management of the business to such borrower.

(IV) **No compensation to directors for loss of office (Section 16)**

Irrespective of anything contained in any contract or in any other law for the time being in force, no managing director or any other director or a manager or any person in charge of management of the business of the borrower shall be entitled to any compensation for the loss of office or for the premature termination under this Act. However any such managing director or any other director or manager or any such person in charge of management has the right to recover from the business of the borrower, moneys recoverable otherwise than by way of such compensation.

(V) **Application against measures to recover secured debts (Section 17)**

- **Filing of an application:** Any person (including borrower), aggrieved by any of the measures given in section 13(4) taken by the secured creditor or his authorised officer under this Chapter, may make an application along with such fee, as may be prescribed to the Debts Recovery Tribunal having jurisdiction in the matter within forty-five days from the date on which such measure had been taken.

Provided that different fees may be prescribed for making the application by the borrower and the person other than the borrower.

**Explanation:** For the removal of doubts, it is hereby declared that the communication of the reasons to the borrower by the secured creditor for not having accepted his representation or objection or the likely action of the secured creditor at the stage of communication of reasons to the borrower shall not entitle the person (including borrower) to make an application to the Debts Recovery Tribunal under this sub-section.

- **Jurisdiction:** An application under sub-section (1) shall be filed before the Debts Recovery Tribunal within the local limits of whose jurisdiction—

  (a) the cause of action, wholly or in part, arises;
(b) where the secured asset is located; or
(c) the branch or any other office of a bank or financial institution is maintaining an account in which debt claimed is outstanding for the time being.

- **Measures taken shall be in compliance**: The Debts Recovery Tribunal shall consider whether any of the measures referred to in section 13(4) taken by the secured creditor for enforcement of security are in accordance with the provisions of this Act and the rules made thereunder.

- If, the Debts Recovery Tribunal, after examining the facts and circumstances of the case and evidence produced by the parties, comes to the conclusion that any of the measures referred to in section 13(4), taken by the secured creditor are not in accordance with the provisions of this Act and the rules made thereunder, and require restoration of the management or restoration of possession, of the secured assets to the borrower or other aggrieved person, it may, by order,—
  (a) declare the recourse to any one or more measures referred to in section 13(4) taken by the secured creditor as invalid; and
  (b) restore the possession of secured assets or management of secured assets to the borrower or such other aggrieved person, who has made an application under sub-section (1), as the case may be; and
  (c) pass such other direction as it may consider appropriate and necessary in relation to any of the recourse taken by the secured creditor under sub-section (4) of section 13.

- **Remedies opted by the securities creditor**: If, the Debts Recovery Tribunal declares the recourse taken by a secured creditor under sub-section (4) of section 13, is in accordance with the provisions of this Act and the rules made thereunder, then, notwithstanding anything contained in any other law for the time being in force, the secured creditor shall be entitled to take recourse to one or more of the measures specified under sub-section (4) of section 13 to recover his secured debt.

Where—

i. any person, in an application under sub-section (1), claims any tenancy or leasehold rights upon the secured asset, the Debt Recovery Tribunal, after examining the facts of the case and evidence produced by the parties in relation to such claims shall, for the purposes of enforcement of security interest, have the jurisdiction to examine whether lease or tenancy,—
  a. has expired or stood determined; or
  b. is contrary to section 65A of the Transfer of Property Act, 1882; or
  c. is contrary to terms of mortgage; or
  d. is created after the issuance of notice of default and demand by the Bank under sub-section (2) of section 13 of the Act; and

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ii. the Debt Recovery Tribunal is satisfied that tenancy right or leasehold rights claimed in secured asset falls under the sub-clause (a) or sub-clause (b) or sub-clause (c) or sub-clause (d) of clause (i), then notwithstanding anything to the contrary contained in any other law for the time being in force, the Debt Recovery Tribunal may pass such order as it deems fit in accordance with the provisions of this Act.

- **Time limit for disposal of an application:** Any application made under sub-section (1) shall be dealt with by the Debts Recovery Tribunal as expeditiously as possible and disposed of within sixty days from the date of such application:

  Provided that the Debts Recovery Tribunal may, from time to time, extend the said period for reasons to be recorded in writing, so, however, that the total period of pendency of the application with the Debts Recovery Tribunal, shall not exceed four months from the date of making of such application made under sub-section (1).

- **Order by the appellate tribunal for expeditious disposal of the pending application:**

  If the application is not disposed of by the Debts Recovery Tribunal within the period of four months as specified in sub-section (5), any party to the application may make an application, in such form as may be prescribed, to the Appellate Tribunal for directing the Debts Recovery Tribunal for expeditious disposal of the application pending before the Debts Recovery Tribunal and the Appellate Tribunal may, on such application, make an order for expeditious disposal of the pending application by the Debts Recovery Tribunal.

- **Save as otherwise provided in this Act,** the Debts Recovery Tribunal shall, as far as may be, dispose of the application in accordance with the provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 and the rules made thereunder.

(VI) **Making of application to Court of District Judge in certain cases (Section 17A)**

  In the case of a borrower residing in the State of Jammu and Kashmir, the application under section 17 shall be made to the Court of District Judge in that State having jurisdiction over the borrower which shall pass an order on such application.

  **Explanation:** It is hereby declared that the communication of the reasons to the borrower by the secured creditor for not having accepted his representation or objection or the likely action of the secured creditor at the stage of communication of reasons shall not entitle the person (including borrower) to make an application to the Court of District Judge under this section.

(VII) **Appeal to Appellate Tribunal (Section 18)**

- **Appeal to an order of DRT:** Any person aggrieved, by any order made by the Debts Recovery Tribunal under section 17, may prefer an appeal along with such fee, as may be prescribed to the Appellate Tribunal within thirty days from the date of receipt of the order of Debts Recovery Tribunal.

  Provided that different fees may be prescribed for filing an appeal by the borrower or by the person other than the borrower;
• **Condition for the appeal:** Provided further that no appeal shall be entertained unless the borrower has deposited with the Appellate Tribunal fifty per cent. of the amount of debt due from him, as claimed by the secured creditors or determined by the Debts Recovery Tribunal, whichever is less. Provided also that the Appellate Tribunal may, for the reasons to be recorded in writing, reduce the amount to not less than twenty-five per cent of debt referred above.

• **Dispose of appeal as per the RDDBFI Act, 1993:** Save as otherwise provided in this Act, the Debts Recovery Tribunal under section 17 or the Appellate Tribunal under section 18 shall, as far as may be, dispose of the appeal in accordance with the provisions of the Recovery of Debts Due to Banks and Financial Institutions Act(RDDBFI), 1993 and rules made thereunder.

(VIII) **Validation of fees levied (Section 18A)**
Any fee levied and collected for preferring an appeal to the Debts Recovery Tribunal or the Appellate Tribunal under this Act, before the commencement of the Enforcement of Security Interest and Recovery of Debts Laws (Amendment) Act, 2004, shall be deemed always to have been levied and collected in accordance with law as if the amendments made to sections 17 and 18 of this Act by sections 10 and 12 of the said Act were in force at all material times.

(IX) **Appeal to High Court in certain cases (Section 18B)**

• Any borrower residing in the State of Jammu and Kashmir and aggrieved by any order made by the Court of District Judge under section 17A-✓ may prefer an appeal, to the High Court having jurisdiction over such Court, within thirty days from the date of receipt of the order of the Court of District Judge.

• **Requirement for preferring an appeal:** No appeal shall be preferred unless the borrower has deposited, with the Jammu and Kashmir High Court, fifty per cent. of the amount of the debt due from him as claimed by the secured creditor or determined by the Court of District Judge, whichever is less. Provided further that the High Court may, for the reasons to be recorded in writing, reduce the amount to not less than twenty-five per cent. of the debt referred here.

(X) **Right to lodge a caveat (Section 18C)**

• **Filing of a caveat:** Where an application or an appeal is expected to be made or has been made under section 17(1) or section 17A or section 18(1) or section 18B, (a) the secured creditor, or (b) any person claiming a right to appear before the Tribunal or the Court of District Judge or the Appellate Tribunal or the High Court, as the case may be, on the hearing of such application or appeal, may lodge a caveat in respect thereof.
- **Notice of caveat**: Where a caveat has been lodged -
  (a) the secured creditor by whom the caveat has been lodged (hereafter in this section referred to as the caveator) shall serve notice of the caveat by registered post, acknowledgement due, on the person by whom the application has been or is expected to be made.
  (b) any person by whom the caveat has been lodged (hereafter in this section referred to as the caveator) shall serve notice of the caveat by registered post, acknowledgement due, on the person by whom the application has been or is expected to be made.

- **Notice on the caveator by adjudicating authority**: Where after a caveat has been lodged, any application or appeal is filed before the Tribunal or the court of District Judge or the Appellate Tribunal or the High Court, as the case may be, the Tribunal or the District Judge or the Appellate Tribunal or the High Court, as the case may be, shall serve a notice of application or appeal filed by the applicant or the appellant on the caveator.

- **Furnishing of copy of application and documents**: Where a notice of any caveat has been served on the applicant or the Appellant, he shall periodically furnish the caveator with a copy of the application or the appeal made by him and also with copies of any paper or document which has been or may be filed by him in support of the application or the appeal.

- **Validity of period of caveat**: Where a caveat has been lodged, such caveat shall not remain in force after the expiry of the period of ninety days from the date on which it was lodged unless the application or appeal has been made before the expiry of the period.

(XI) **Right of borrower to receive compensation and costs in certain cases (Section 19)**

- If the Debts Recovery Tribunal or the Court of District Judge, on an application made under section 17 or section 17A or the Appellate Tribunal or the High Court on an appeal preferred under section 18 or section 18A, holds that the possession of secured assets by the secured creditor is not in accordance with the provisions of this Act and rules made thereunder, and
  - directs the secured creditors to return such secured assets to concerned borrowers or any other aggrieved person, who has filed the application under section 17 or section 17A or appeal under section 18 or section 18A, as the case may be,
  - the borrower or such other person shall be entitled to the payment of such compensation and costs as may be determined by such Tribunal or Court of District Judge or Appellate Tribunal or the High Court referred to in section 18B.

8. **Central Registry**

The provisions related to Central Registry is contained in chapter IV of the Act. It covers sections 20 to 26 of the Act.

(I) **Central Registry (Section 20)**
• **Setup of Central Registry**: The Central Government may, by notification, set up or cause to be set up from such date as it may specify in such notification, a registry to be known as the Central Registry with its own seal for the purposes of registration of transactions of securitisation and reconstruction of financial assets and creation of security interest under this Act.

The head office of the Central Registry shall be at such place as the Central Government may specify and for the purpose of facilitating registration of transactions referred above, there may be established at such other places as the Central Government may think fit, branch offices of the Central Registry.

• **Central Government notifies territorial jurisdiction of the Central Registry**: The Central Government may, by notification, define the territorial limits within which an office of the Central Registry may exercise its functions. The provisions of this Act pertaining to the Central Registry shall be in addition to and not in derogation of any of the provisions contained in the Registration Act, 1908, the Companies Act, 1956 (i.e. Companies Act, 2013), 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 Registry of Securitisation Asset Reconstruction and Security Interest of India (CERSAI) is a Government of India Company licensed under section 8 of the Companies Act, 2013 with Govt. of India having a shareholding of 51% by the Central Government and select Public Sector Banks and the National Housing Bank also being shareholders of the Company.

The object of the company is to maintain and operate a Registration System for the purpose of registration of transactions of securitisation, asset reconstruction of financial assets and creation of security interest over property, as envisaged in the SARFAESI Act.

**(II) Integration of registration systems with Central Registry (Section 20A)**

• The Central Government may, for the purpose of providing a Central database, in consultation with State Governments or other authorities operating registration system for recording rights over any property or creation, modification or satisfaction of any security interest on such property, integrate the registration records of such registration systems with the records of Central Registry established under section 20, in such manner as may be prescribed.

• The Central Government shall after integration of records of various registration systems referred with the Central Registry, by notification, declare the date of integration of registration systems and the date from which such integrated records shall be available; and with effect from such date, security interests over properties which are registered under any registration system referred shall be deemed to be registered with the Central Registry for the purposes of this Act.
(III) Delegation of powers (Section 20B)

The Central Government may, by notification, delegate its powers and functions under this Chapter, in relation to establishment, operations and regulation of the Central Registry to the Reserve Bank, subject to such terms and conditions as may be prescribed.

(IV) Central Registrar (Section 21)

- The Central Government may, by notification, appoint a person for the purpose of registration of transactions relating to securitisation, reconstruction of financial assets and security interest created over properties, who shall be known as the Central Registrar.

- The Central Government may appoint such other officers with such designations as it thinks fit for the purpose of discharging, under the superintendence and direction of the Central Registrar, such functions of the Central Registrar under this Act as he may, from time to time, authorise them to discharge.

(V) Register of securitisation, reconstruction and security interest transactions (Section 22)

- A record called the Central Register shall be kept at the head office of the Central Registry for entering the particulars of the transactions relating to-
  
  (a) securitisation of financial assets;
  
  (b) reconstruction of financial assets;
  
  (c) creation of security interest

- The Central Registrar can keep the records wholly or partly in computer, floppies, diskettes or in any other electronic form subject to the prescribed safeguards. Records kept in these form shall also form a part of the Central Register. The register shall be kept under the control and management of the Central Registrar.

(VI) Filing of transactions of securitisation, reconstruction and creation of security Interest (Section 23)

- The particulars of every transaction of securitisation, reconstruction or creation of security interest shall be filed, with the Central Registrar in the prescribed manner and on payment of the prescribed fees. [Section 23(1)]

  Provided that the Central Government may, by notification, require registration of all transactions of securitisation, or asset reconstruction or creation of security interest which are subsisting on or before the date of establishment of the Central Registry under section 20(1) within such period and on payment of such fees as may be prescribed.

- The Central Government may, by notification, require the registration of transaction relating to different types of security interest created on different kinds of property with the Central Registry [Section 23(2)]
The Central Government may, by rules, prescribe forms for registration for different types of security interest under this section and fee to be charged for such registration.

(VII) Modification of security interest registered under this Act (Section 24)

Whenever the terms or conditions, or the extent or operation, of any security interest registered under this Chapter, are, or is, modified it shall be the duty of the ARC to send to the Central Registrar, the particulars of such modification.

(VIII) ARC or secured creditor to report satisfaction of security interest (Section 25)

- The ARC or the secured creditor as the case may be, shall give intimation to the Central Registrar of the payment or satisfaction in full, of any security interest relating to the ARC or the secured creditor and requiring registration under this Chapter, within thirty days from the date of such payment or satisfaction.
- On receipt on intimation, the Central Government shall order that a memorandum of satisfaction shall be entered in the Central Registry.

(IX) Right to inspect particulars of securitisation, reconstruction and security interest transactions (Section 26)

The particulars of securitisation or reconstruction or security interest entered in the Central Register of such transactions kept under section 22 shall be open during the business hours for inspection by any person on payment of such fee as may be prescribed.

9. Rectification by Central Government in matters of registration, modification and satisfaction etc. (Section 26A)

- The Central Government, on being satisfied-
  
  (a) that the omission to file with the Registrar the particulars of any transaction of securitisation, asset reconstruction or security interest or modification or satisfaction of such transaction or; the omission or mis-statement of any particular with respect to any such transaction or modification or with respect to any satisfaction or other entry made in pursuance of section 23 or section 24 or section 25 of the principal Act was accidental or due to inadvertence or some other sufficient cause or it is not of a nature to prejudice the position of creditors; or
  
  (b) that on other grounds, it is just and equitable to grant relief, may, on the application of a secured creditor or securitisation company or reconstruction company or any other person interested on such terms and conditions as it may seem to the Central Government just and expedient, direct that the time for filing of the particulars of the transaction for registration or modification or satisfaction shall be extended or, as the case may require, the omission or mis-statement shall be rectified.
Where the Central Government extends the time for the registration of transaction of security interest or securitisation or asset reconstruction or modification or satisfaction thereof, the order shall not prejudice any rights acquired in respect of the property concerned or financial asset before the transaction is actually registered.

10. Registration by secured creditors and other creditors

The government has introduced new provisions in the form of Chapter IVA in order to encourage registration of security interest by the secured creditors, which shall facilitate uniformity, completeness and transparency in the status of security interest of the creditors over the borrower's assets.

(I) Registration by secured creditors and other creditors (Section 26B)

- The Central Government may by notification, extend the provisions of Chapter IV relating to Central Registry to all creditors other than secured creditors as defined in clause (zd) of section 2(1), for creation, modification or satisfaction of any security interest over any property of the borrower for the purpose of securing due repayment of any financial assistance granted by such creditor to the borrower.
- From the date of notification, any creditor including the secured creditor may file particulars of transactions of creation, modification or satisfaction of any security interest with the Central Registry in such form and manner as may be prescribed.
- However, a creditor other than the secured creditor filing particulars of transactions of creation, modification and satisfaction of security interest over properties created in its favour shall not be entitled to exercise any right of enforcement of securities under this Act.
- Every authority or officer of the Central Government or any State Government or local authority, entrusted with the function of recovery of tax or other Government dues and for issuing any order for attachment of any property of any person liable to pay the tax or Government dues, shall file with the Central Registry such attachment order with particulars of the assessee and details of tax or other Government dues from such date as may be notified by the Central Government, in such form and manner as may be prescribed.
- Also, if any person, having any claim against any borrower, obtains orders for attachment of property from any court or other authority empowered to issue attachment order, such person may file particulars of such attachment orders with Central Registry in such form and manner on payment of such fee as may be prescribed.

(II) Effect of the registration of transactions, etc. (Section 26C)

- any registration of transactions of creation, modification or satisfaction of security interest by a secured creditor or other creditor or filing of attachment orders under this Chapter shall be deemed to constitute a public notice from the date and time of filing of particulars of such transaction with the Central Registry.
Where security interest or attachment order upon any property in favour of the secured creditor or any other creditor are filed for the purpose of registration, the claim of such secured creditor or other creditor holding attachment order shall have priority over any subsequent security interest created upon such property and any transfer by way of sale, lease or assignment or licence of such property or attachment order subsequent to such registration, shall be subject to such claim:

Provided that nothing contained in this sub-section shall apply to transactions carried on by the borrower in the ordinary course of business.

(III) Right of enforcement of securities (Section 26D)

No secured creditor shall be entitled to exercise the rights of enforcement of securities under Chapter III unless the security interest created in its favour by the borrower has been registered with the Central Registry.

(IV) Priority to secured creditors (Section 26E)

After the registration of security interest, the debts due to any secured creditor shall be paid in priority over all other debts and all revenues, taxes, cesses and other rates payable to the Central Government or State Government or local authority.

However such priority shall be subject to the provisions of the Insolvency and Bankruptcy Code, 2016, where insolvency or bankruptcy proceedings are pending in respect of secured assets of the borrower.

11. Offences and Penalties

This chapter V of the Act provides for the offences and the penalties for the commission of default in filing of particulars of every transaction of securitisation, asset reconstruction or creation of security interest with Central registry. This chapter covers section 27 to 30 of the Act.

(I) Penalties (Section 27)

If a default is made-

(a) in filing under section 23, the particulars of every transaction of any securitisation or asset reconstruction or security interest created by an ARC or secured creditors; or
(b) in sending under section 24, the particulars of the modification referred to in that section; or
(c) in giving intimation under section 25,

then, 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 five thousand rupees for every day during which the default continues.

Provided that provisions of this section shall be deemed to have been omitted from the date of coming into force of the provisions of this Chapter and section 23 as amended by

(II) Offences (Section 29)

- If any person-
  ✓ contravenes or
  ✓ attempts to contravene or
  ✓ abets the contravention of the provisions of this Act or of any rules made thereunder,

he shall be punishable with imprisonment for a term which may extend to one year, or with fine, or with both.

(III) Cognizance of offence (Section 30)

- No court shall take cognizance of any offence punishable under section 27 in relation to non-compliance with the provisions of section 23, section 24 or section 25 or under section 28 or section 29 or any other provisions of the Act, except upon a complaint in writing made by an officer of the Central Registry or an officer of the Reserve Bank, generally or specially authorised in writing in this behalf by the Central Registrar or, as the case may be, the Reserve Bank.

- No court inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of the first class shall try any offence punishable under this Act.

(IV) Power of adjudicating authority to impose penalty (Section 30A)

- Where any asset reconstruction company or any person fails to comply with any direction issued by the Reserve Bank under this Act, the adjudicating authority may, by an order, impose on such company or person in default, a penalty not exceeding one crore rupees or twice the amount involved in such failure where such amount is quantifiable, whichever is more, and where such failure is a continuing one, a further penalty which may extend to one lakh rupees for every day, after the first, during which such failure continues.

- The adjudicating authority shall serve a notice on the asset reconstruction company or the person in default requiring such company or person to show cause why the amount specified in the notice should not be imposed as a penalty and a reasonable opportunity of being heard shall be given to such person.

- Any penalty imposed under this section shall be payable within a period of thirty days from the date of issue of notice, failure of which adjudicating authority shall cancel its registration.

- No complaint shall be filed against any person in default in any court pertaining to any failure under sub-section (1) in respect of which any penalty has been imposed and recovered by the Reserve Bank under this section.

- Where any complaint has been filed against a person in default in the court having jurisdiction no proceeding for imposition of penalty against that person shall be taken under this section.
• "Adjudicating authority" means such officer or a committee of officers of the Reserve Bank, designated as such from time to time, by notification, by the Central Board of Reserve Bank.

• "person in default" means the asset reconstruction company or any person which has committed any failure, contravention or default under this Act and any person incharge of such company or such other person, as the case may be, shall be liable to be proceeded against and punished under section 33 for such failure or contravention or default committed by such company or person.

(V) Appeal against penalties (Section 30B)

• A person in default, aggrieved by an order passed in section 30A(4), may, within a period of thirty days from the date on which such order is passed, prefer an appeal to the Appellate Authority.

• Appellate Authority may entertain an appeal after the expiry of the said period of thirty days, if it is satisfied that there was sufficient cause for not filing it within such period.

(VI) Appellate Authority (Section 30C)

• The Central Board of Reserve Bank may designate such officer or committee of officers as it deems fit to exercise the power of Appellate Authority.

• The Appellate Authority shall have power to pass such order as it deems fit after providing a reasonable opportunity of being heard to the person in default.

• The Appellate Authority may, by an order stay the enforcement of the order passed by the adjudicating authority under section 30A, subject to such terms and conditions, as it deems fit.

• Where the person in default fails to comply with the terms and conditions imposed by order without reasonable cause, the Appellate Authority may dismiss the appeal.

(VII) Recovery of penalties (Section 30D)

Any penalty imposed under section 30A shall be recovered as a "recoverable sum" and shall be payable within a period of thirty days from the date on which notice demanding payment of the recoverable sum is served upon the person in default and, in the case of failure of payment by such person within such period, the Reserve Bank may recover the sum as per the section.

12. Miscellaneous

Chapter VI of the Act comprises of miscellaneous provisions dealt under sections 31-42 of the Act.

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

• The situations in which the provisions of this Act do not apply are as follows:-

  (a) a lien on any 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 section 172 of the Indian Contract Act, 1872;

(c) creation of any security in any aircraft as defined in clause (1) of section 2 of the Aircraft Act, 1934;

(d) creation of security interest in any vessel as defined in clause (55) of section 3 of the Merchant Shipping Act, 1958;

(e) any rights of unpaid seller under section 47 of the Sale of Goods Act, 1930;

(f) any properties not liable to attachment (excluding the properties specifically charged with the debt recoverable under this Act) or sale under the first proviso to sub-section (1) of section 60 of the Code of Civil Procedure, 1908;

(g) any security interest for securing repayment of any financial asset not exceeding one lakh rupees;

(h) any security interest created in agricultural land;

(i) any case in which the amount due is less than twenty per cent of the principal amount and interest thereon

(II) Provisions of the Act not to apply in some cases (Section 31A)

- The Central Government may, by notification in the public interest, direct that any of the provisions of this Act,
  a. shall not apply to such class or classes of banks or financial institutions; or
  b. shall apply to the class or classes of banks or financial institutions with such exceptions, modifications and adaptations, as may be specified in the notification.

- A copy of every notification proposed to be issued under sub-section (1), shall be laid in draft before each House of Parliament, while it is in session, for a total period of thirty days, and if, both Houses agree in disapproving the issue of notification or both Houses agree in making any modification in the notification, the notification shall not be issued or, as the case may be, shall be issued only in such modified form as may be agreed upon by both the Houses.

- In reckoning any such period of thirty days as is referred to in sub-section (2), no account shall be taken of any period during which the House referred to in sub-section (2) is prorogued or adjourned for more than four consecutive days.

- The copies of every notification issued under this section shall, as soon as may be after it has been issued, be laid before each House of Parliament.

(III) Protection of action taken in good faith (Section 32)

- No suit, prosecution or other legal proceedings shall lie against the Reserve Bank or the Central Registry or any secured creditor or any of its officers for anything done or omitted to be done in good faith under this Act.
Offences by companies (Section 33)

- Where an offence under this Act has been committed by a company, every person who at the time the offence was committed was in charge of, and was responsible to, the company, for the conduct of the business of the company, as well as the company, shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished in accordance with the provisions of the Act.

- But if such person is able to prove that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence, then section 33 does not apply to such person.

- It must also be noted that, where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any director, manager, secretary or other officer of the company, such director, manager, secretary or other officer shall also be deemed to be guilty of the offence and shall be liable to be proceeded against and punished in accordance with the provisions of the Act.

- For the purposes of section 33:
  (a) "company" means any body corporate and includes a firm or other association of individuals; and
  (b) "director", in relation to a firm, means a partner in the firm.

Civil Court not to have jurisdiction (Section 34)

- No civil court shall have jurisdiction to entertain any suit or proceeding in respect of any matter which a Debts Recovery Tribunal or the Appellate Tribunal is empowered by or under this Act to determine and no injunction shall be granted by any court or other authority in respect of any action taken or to be taken in pursuance of any power conferred by or under this Act or under the Recovery of Debts Due to Banks and Financial Institutions Act, 1993.

The provisions of this Act to override other laws (Section 35)

- The provisions of this Act shall have effect, notwithstanding anything inconsistent therewith contained in any other law for the time being in force or any instrument having effect by virtue of any such law.

Limitation (Section 36)

- No secured creditor shall be entitled to take all or any of the measures under sub-section (4) of section 13, unless his claim in respect of the financial asset is made within the period of limitation prescribed under the Limitation Act, 1963.
(VIII) Application of other laws not barred (Section 37)

- The provisions of this Act or the rules made thereunder shall be in addition to, and not in derogation of, the Companies Act, 2013, the Securities Exchange Board of India Act, 1992, the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 or any other law for the time being in force.

(IX) Application of other laws not barred (Section 38)

- The Central Government may, by notification and in the Electronic Gazette make rules for carrying out the provisions of this Act. In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:-

  (a) other business or commercial rights of similar nature under clause (t) of section 2;

  aa. the form and manner in which an application may be filed under sub-section (10) of section 13;

  (b) the manner in which the rights of a secured creditor may be exercised by one or more of his officers under section 13(12);

  ba. the fee for making an application to the Debts Recovery Tribunal under section 17(1);

  bb. the form of making an application to the Appellate Tribunal under section 17(6);

  bc. the fee for preferring an appeal to the Appellate Tribunal under section 18(1);

  bca. the manner of integration of records of various registration systems with the records of Central Registry under sub-section (1) of section 20A;

  bcb. the terms and conditions of delegation of powers by the Central Government to the Reserve Bank under section 20B;"

  (c) the safeguards subject to which the records may be kept under sub-section (2) of section 22;

  (d) the manner in which the particulars of every transaction of securitisation shall be filed under section 23 and fee for filing such transaction;

  da. the form for registration of different types of security interests and fee thereof under sub-section (3) of section 23;"

  (e) the fee for inspecting the particulars of transactions kept under section 22 and entered in the Central Register under sub-section (1) of section 26;

  (f) the fee for inspecting the Central Register maintained in electronic form under sub-section (2) of section 26;
fa. the form and the manner for filing particulars of transactions under sub-section (2) of section 26B;

fb. the form and manner of filing attachment orders with the Central Registry and the date under sub-section (4) of section 26B;

c. the form and manner of filing particulars of attachment order with the Central Registry and the fee under sub-section (5) of section 26B.

(g) any other matter which is required to be, or may be, prescribed, in respect of which provision is to be, or may be, made by rules.

- **Power of Central Government to make rules** Every rule made under this Act shall be laid, as soon as may be after it is made, before each House of Parliament, while it is in session, for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or both Houses agree that the rule should not be made, the rule shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule.

**Examples**

1. **Facts**
   - ABC Bank has provided term loan of 10 crores to XYZ Ltd., a steel manufacturing company at an interest rate of 10% p.a. and principal amount is to be payable in equal quarterly instalments within 5 years from the date of disbursement of loan.
   - The loan is fully secured against plant & machinery.
   - The company successfully repaid 4 instalments along with interest during the first year. From the start of second year, the EBITDA of the company fell drastically due to multiple factors including crash in steel prices, rise of coal and iron ore prices, and plant shut down. The company therefore couldn’t repay the 5th instalment but it paid the interest amount as and when due.
   - After the end of 60 days from the due date of the 5th instalment the credit manager of the bank decided to sell the loan to LMN Ltd., an asset reconstruction company, along with the overdue loan of 2 crore to another textile company, which was classified as NPA six months ago, and a loan of ₹ 2 crore to a farmer Mr JKL, secured against agriculture land.
   - Please analyse and advise the manager whether he can do so?
Analysis:

- The balance amount is 8 crore (i.e. 80% of the total loan value), which is more than 20% of the total principal and interest amount (s. 31(j)). The loan is a financial asset and the bank has security interest as defined in the act.

- For enforcement of security under this act, there has to be a default as defined u/s 2(1)(j), which requires the classification of the asset as NPA. In the immediate case of steel company, the debts are overdue by only 60 days, and is therefore still not classified as NPA (NPA classification shall happen after 90 days), unlike the loan of textile company.

- In absence of the other facts of the case of the textile company, we cannot comment if 'default' exists and it can be sold to LMN ltd.

- Further the loan given to Mr. JKL being secured against agricultural land, cannot be sold as the provisions of SARFAESI act is not applicable to such assets (s. 31(j)).

2. Facts

- XYZ Finance Ltd. is an NBFC company with total assets of 550 crore, and an NPA of 50 crore in its balance sheet.

- The 50 crore loan consists of 9 cases of 5 crore each and 10 cases of 50 lakhs each.

- The management of the company wants to sell bad loans worth 50 crore to an ARC. Of the ₹ 50 crore, 45 crore is secured against various properties, while one case of 5 crore is unsecured.

- During detailed discussion with the in-house legal counsel, it came to light that 2 crore of the secured bad loan has not been registered with the central registry CERSAI, however this was not informed to the buyer in the preliminary discussion.

- Please analyse and advise the CEO of XYZ finance Ltd. how much bad loan can he sell to the ARC?

Analysis:

- Sarfaesi is applicable to only those notified NBFC which has an asset base of 500 crore or above, hence in this case the XYZ finance Ltd. shall be able to sell the bad loans to ARCs through Sarfaesi.

- Further SARFAESI is applicable to secured loans only, therefore only 45 crore of bad loans can be sold to ARC under SARFAESI.

- As per section 26D no secured creditor shall be entitled to exercise the rights of enforcement of securities under Chapter III unless the security interest created in its favour by the borrower has been registered with the Central Registry, therefore the buyer may not be keen to take over the unregistered loan of 5 crore.
Further NBFCs can invoke SARFAESI for only those cases which are over 1 crore, therefore the 10 cases of 50 lacs each cannot be sold to ARC under SARFAESI.

Therefore, we are left with 8 cases of 5 crore each which can be sold to ARC subject to meeting all other conditions of the law.

3. Facts

A newly formed ARC has acquired secured interest on few assets in steel sector. The sector is undergoing cyclical recession due to global meltdown and increase in raw material price.

The management is now contemplating various options through which it can realise its assets.

What are the measures with the ARC management under the SARFAESI law?

Analysis:

Section 9 deals with measures for asset reconstruction which provides for the following measures:

- 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 interest in accordance with the provisions of this Act;
- settlement of dues payable by the borrower;
- taking possession of secured assets in accordance with the provisions of this Act;
- conversion of any portion of debt into shares of a borrower company: Provided that conversion of any part of debt into shares of a borrower company shall be deemed always to have been valid, as if the provisions of this clause were in force at all material times.

Further Chapter III deals with the enforcement of security interest, which provides for the following modes of security enforcement:

- 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;
- 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 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 for the debt;

- 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;

- 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.

4. Facts

- ABC limited has issued listed bonds five years ago, which is due to be redeemed in the current year worth 50 crore. Market analyst feels that the projected cash flows and profitability seems inadequate to repay the bond value.

- The single largest bond holder BH Ltd. holds bonds worth 20 crore, and wants to explore its options under SARFAESI law, in case ABC limited fails to repay the debt.

- Please advise whether BH ltd. can have recourse to the SARFAESI Act.

Analysis:

The definition of secured creditor under section 2(zd) of SARFAESI act has been amended so as to include debenture trustee appointed in respect of debt securities, and corresponding changes have also been made in SARFAESI Act and RDDBFI Act. Hence it shall have recourse to all options available to any secured creditor under the law such as enforcement of security, sale of loans to ARC etc. Unlike NBFC for which a threshold of assets of 500 crore is put for applicability of the SARFAESI act, there is no such limit for debenture holders.