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Analysing developments impacting business

A BORROWER CAN NOW CHALLENGE SYMBOLIC POSSESSION UNDER THE SARFAESI ACT

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Introduction

The Hon'ble Supreme Court (SC), in its recent decision in the matter of *M/s Hindon Forge Pvt. Ltd. & Anr. v State of Uttar Pradesh* [(Civil Appeal No 10873 of 2018 along with Civil Appeal No 10874 of 2018)] (Appeals) held that a borrower can prefer an application under Section 17(1) of the Securitization and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002 (Act) even before physical or actual possession of secured assets is taken over by banks/financial institutions in exercise of their powers under Section 13(4) of the Act read with Rule 8 of the Security Interest (Enforcement) Rules, 2002 (Rules).

Background

A full bench of the Hon'ble Allahabad High Court held that under the scheme of Section 13(4) and Sections 14 and 17 of the Act read with Rules 8 and 9 of the Rules, unless physical or actual possession of the secured asset was taken over by the banks/financial institutions, as contemplated under Section 13(4) of the Act, the borrower cannot not file an application before the debt recovery tribunal (DRT) under Section 17(1) of the Act for challenging the action of such banks/financial institutions. (Allahabad HC Order)

Issue before the Supreme Court

The SC was asked to decide on whether an application under Section 17 (1) of the Act is maintainable before physical or actual possession of secured assets is taken by the secured creditor under Section 13(4) of the Act read with Rule 8 of the Rules.

Analysis of law and decision by the Hon'ble Supreme Court: -

The SC observed that the decision in *Mardia Chemicals Ltd. v. Union of India* [(2004)4 SCC 311], clarified that after all measures have been taken under Section 13(4) prior to the sale auction, the borrower may file an application under Section 17 of the Act.

Section 13(4)(a) provides for mode of taking possession of secured assets in accordance with Rule 8 of the Rules, which stipulates that the authorised officer shall take or cause to be taken possession of the secured asset by delivering a possession notice prepared in accordance with the form provided in Appendix IV of the Rules and affixing such possession notice to the door or other conspicuous place of the property. Rule 8(2) provides that the possession notice should be published in 2 leading newspapers within 7 days of taking possession. From this stage, the secured asset is

liable to be sold to realise the secured debt and the title then transfers from the borrower to the purchaser as provided in Section 13(6) of the Act.

The SC observed that after the issuance of possession notice under Rule 8(1) and, 8(2) of the Rules, the borrower explicitly cannot deal with the secured asset at all as any further steps to realize the debt will then be taken by the secured creditor.

The scheme of Section 13(4) of the Act read with Rule 8(1) of the Rules makes it clear that the delivery of a possession notice together with affixation on the property and publication is one mode of taking "possession" under Section 13(4) of the Act, and as such Section 17 of the Act is attracted once possession is taken under Rule 8(1) and Rule 8(2) of the Rules read with Section 13 (4)(a) of the Act.

The SC observed that the object of the Act stipulates that if a secured creditor does not act in conformity with the Act to realise the secured debt, the borrower may take recourse to seeking appropriate relief from the DRT. Thus, the object of the Act would be stultified if the borrower must wait for sale notice to be issued or for the actual sale to take place before taking recourse to Section 17 of the Act.

Thus, the SC set aside the Allahabad HC Order and held that a borrower is entitled to approach the DRT under Section 17 of the Act at the stage of possession notice under Rule 8(1) and Rule 8(2) of the Rules.

Comment:

Earlier, a borrower could seek recourse under the Act against measures taken by the bank/financial institution only when steps for actual physical possession of the secured asset were taken by the bank/financial institution. After this decision, the borrower need not wait till the bank/financial institution takes such steps, but may now, under Section 17(1) of the Act, prefer an application to challenge these measures even at the stage of constructive possession by the bank/financial institution.

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