

Central Registry



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CENTRAL REGISTRY

Introduction

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (hereinafter referred to as "SARFAESI Act") was enacted to enable banks and financial institutions to take possession of securities and sell them. The SARFAESI Act was put in place with a view to provide the Banking Sector with an organised platform; thereby empowering them to manage their mounting non-performing assets (NPA) stocks and to keep pace with international financial institutions. In consonance with the above, the object of the SARFAESI Act has been stated in the Act as, "An Act to regulate securitisation and reconstruction of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto."

Central Registry is defined by Section 2 (g) of the SARFAESI Act. Under s.20 of the said Act, The Central Government is empowered to set up a Central Registry for the purposes of registration of transaction of securitisation and reconstruction of financial assets and creation of security interest. The particulars of the transaction need to be filed and modified (whenever necessary) by the securitisation company or reconstruction company or the secured creditor. They are also under a duty to report satisfaction of the security interest. The particulars of the transaction may be inspected by any person during business hours on payment of a particular amount of fee.

The Reserve Bank of India (RBI) by a notification announced the operationalization of Central Registry from the 31st March, 2011, that will have details of all properties against which loans have been taken, to prevent frauds in loan cases involving multiple lending from different banks on the same immovable property.

Moreover, a Government Company, licensed under Section 25 of the Companies Act, 1956, has been incorporated to operate and maintain the Central Registry under the provisions of the SARFAESI Act, 2002. It is called the Central Registry of Securitisation Asset Reconstruction and Security Interest of India (hereinafter referred to as CERSAI). The Government of India has 51 per cent stake in it while the remaining 49 per cent is with the National Housing Bank and 10 other banks.

CERSAI would be under the superintendence and direction of the Central Registrar. Mr. RV Verma, Chairman and Managing Director, National Housing Bank, has been given additional charge as the Registrar of the Central Registry for three months, and he will also be the Managing Director and CEO of CERSAI. The office of the Central Registrar would be situated in the local chapter of Indian Banks' Association. It would have jurisdiction over the whole of India.

Features of the Registration System under the SARFAESI Act

1. Effective date of the Registry System:

The Government notifications of establishing the Central Registry, prescribing the Central Registry Rules and appointing the Central Registrar, are all dated 31st March 2011. The Registration System has therefore become effective from 31st March 2011 and all security interests by way of creation of mortgage by deposit of title deeds as also transactions of securitisation and asset reconstruction on and after 31st March 2011 are required to be registered. The relevant Rules have not been given retrospective effect and hence transactions of mortgages or securitisation or asset reconstruction undertaken prior to 31st March 2011 are not required to be registered. If in any loan accounts there is a release and re-deposit of title deeds on or after 31st March 2011 amounting to creation of mortgage, such transaction will require registration.

2. Applicability of the Registration System:

The provisions of the SARFAESI Act are applicable to secured creditor, defined under s. 2(1)(zd) of the Act. According to the definition, following categories of secured creditors are governed by the SARFAESI Act:

- i) Banks
- ii) Financial Institutions
- iii) Debenture Trustee appointed by any bank or financial institution
- iv) Securitisation Company (SC) or Reconstruction Company (RC)
- v) Any other trustee holding securities on behalf of a bank or financial institution

In terms of the definition of bank and financial institution contained in section 2(1)(c) and (m), the Central Government has powers to declare any other bank or financial institution as a bank

or financial institution for the purposes of the provisions of the SARFAESI Act. In exercise of the above powers the Central Government has declared certain banks and housing finance companies as financial institutions for the purposes of the SARFAESI Act, by issue of Notifications as under:

- a. Declared Co-operative Bank as defined in clause (cci) of section 5 of the Banking regulation Act, 1949 as 'bank'.
- b. Declared certain Housing Finance Companies registered under section 29A of the National Housing Bank Act, 1987, as 'financial institutions'.
- c. Declared Asian Development Bank as 'financial institution'.
- d. Declared Regional Rural Banks as defined in clause (f) of section 2 of the Regional Rural Banks Act, 1976 as 'bank'.

All such entities are secured creditors for the purposes of SARFAESI Act and are required to register security interest by way of mortgage by deposit of title deeds with CERSAI. In addition to debenture trustees referred to in the definition of secured creditors there are certain trustee companies holding securities on behalf of banks and financial institutions. Such trustee companies are also secured creditors for the purposes of the SARFAESI Act and are governed by the requirements of the Registration System.

3. **Equitable mortgages in favour of trusts/trustee companies**

As mentioned above, the definition of 'secured creditor' under the SARFAESI Act includes trustees acting on behalf of any bank or financial. In cases where equitable mortgages are created in favour of a trustee or a trustee company, Form-I should be filed by such trustee and in para 7 of Form-I, name of the charge holder may be stated as under:

'..... Trustee Company acting on behalf of Bank andFinancial Institution'. (The names of the Banks and Financial Institutions on whose behalf the trustee is holding the securities may be indicated after the name of the trustee / trustee company).

4. **Types of Security Interests required to be registered with CERSAI**

The Central Government has notified the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (Central Registry) Rules, 2011 (Central Registry Rules)

with effect from 31st March 2011. In terms of the provisions of the said Rules, the Forms have been prescribed for the purposes of registration of following transactions with CERSAI:

- (i) Creation of mortgage by deposit of title deeds in favour of secured creditors: Form-I
- (ii) Satisfaction of Charge : Form-II
- (iii) Securitisation or Reconstruction of Financial Assets: Form-III
- (iv) Satisfaction of Securitisation or Reconstruction of Financial Assets : Form-IV

It can be seen from the provisions of the Central Registry Rules that no Forms have been prescribed for registration of charges other than mortgage by deposit of title deeds. Hence for the present, the secured creditors are required to file particulars of only equitable mortgages with CERSAI.

Initially, transactions relating to securitisation and reconstruction of financial assets and those relating to mortgage by deposit of title deeds to secure any loan or advances granted by banks and financial institutions, as defined under the SARFAESI Act, are to be registered in the Central Registry. To begin with, only mortgages would be registered and not hypothecation or other charges. The records maintained by the Central Registry will be available for search by any lender or any other person desirous of dealing with the property.

The forms for registration and the fees for filing registration particulars as well as for taking a search in the Central Registry have been prescribed by Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (Central Registry) Rules, 2011.

There are plans to extend the Central Registry to an online platform. In the future, the Registry will also record security over movable and intangible property.

5. Registration of Securitisation and Reconstruction Transactions:

Banks and financial institutions undertake securitisation of healthy assets, but such securitisation may not be under the provisions of the SARFAESI Act. The assignment of loan receivables with or without the benefit of underlying securities is done in favour of a Special Purpose Vehicle (SPV), using the provisions of the Indian Trust Act, 1882. Such assignment of loan receivables may not be in favour of any SC or RC registered under the provisions of section 3 of the

SARFAESI Act. Such securitisation transactions are therefore not required to be registered with CERSAI.

If any SC or RC registered under the SARFAESI Act is acquiring loan receivables for securitisation or asset reconstruction, such transactions are required to be registered in Form-III prescribed under the Central Registry Rules. It needs to be noted that registration of transactions of securitisation or reconstruction has no relevance with creation of mortgage by deposit of title deeds.

There could be cases where securitisation or reconstruction is undertaken in respect of loan receivables which are unsecured or secured by security interest other than mortgage by deposit of title deeds. All such transactions of securitisation or reconstruction are required to be registered with CERSAI. In many cases, such securitisation or reconstruction transactions would relate to a bundle of loans consisting of many loan accounts acquired from any bank or financial institution. In such cases, satisfaction of the securitisation / reconstruction transaction will have to be filed with CERSAI after all the accounts contained in such bundle of loans are satisfied or otherwise closed. It is not necessary to file any Form for Satisfaction, if only part of such loan portfolio acquired by SC/RC is settled and recovered.

It is not necessary that the loans acquired by SC/RC for the purpose of securitisation or reconstruction or secured by mortgage by deposit of title deeds. However, any SC/RC registered with RBI is also a secured creditor for the purposes of SARFAESI Act. Hence, if in the process of reconstruction of any loans acquired by SC/RC, a mortgage is created in favour of SC/RC to secure the reconstructed loans or any further finance granted to the borrower, such mortgage created in favour of SC/RC will have to be registered by filing Form-I with the CERSAI.

6. Filing of EM with Central Registry vis a vis Filing of Form 8 under the Companies Act for creation or modification of charge u/s. 125-128 and registration under the Registration Act, 1918

The Central Registration system established under the SARFAESI act is in addition to and supplemental to other registration system already in operation under other laws such as the Companies Act 1956 or Registration Act, 1918. The registration under the SARFAESI Act does not in any way affect or change the requirement of registration under other laws. As given under s.20(4)

of the SARFAESI Act, "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 (16 of 1908), the Companies Act, 1956 (1 of 1956), the Merchant Shipping Act, 1958 (44 of 1958), the Patents Act, 1970 (39 of 1970), the Motor Vehicles Act, 1988 (59 of 1988) and the Designs Act, 2000 (16 of 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.

Therefore, the above provision makes it clear that registration of documents under the various prevailing acts shall continue to exist in addition to the registration system of the Central registry under the SARFAESI Act.

7. Registration fees attract Service Tax and TDS required to be deducted from the advance remittance by the HFCs.

The registration fees are payable as required under the Central Registry Rules 2011 framed in exercise of powers conferred on the Central Government under Section 23 read with Section 38(2)(d) of the SARFAESI Act, 2002. The fees which is being collected by the Central Registry from the banks and financial institutions is an advance towards the fees to be paid to the Government for registration. When the particulars of mortgages are filed with the registry the fees will be debited to the advance already collected. In our views no TDS/ST is payable in respect of such payments which are charges payable to the Govt. The amount of advance is linked to registrations required to be filed by the Bank or Financial Institution. Once the Central Registry installs the Payment Gateway for payment of fees for registration there will be no requirement of payment of advance.

Multiple advantages of the Registration System

Availability of such records would prevent frauds involving multiple lending against the security of same property as well as fraudulent sale of property without disclosing the security interest over such property. With the existence of Central Registry, it would be virtually impossible for a borrower to raise loans twice against the same property or raise loans using forged documents. In the past, there have been instances where borrowers have forged the title deed and borrowed money from multiple banks by giving duplicate documents (title deed) as security for home loan. As a result, when the borrower defaults on the loan, many banks would make claim for the same house.

Besides being beneficial to the lenders and innocent third parties, the establishment of the Central Registry would result in advantages given below:

- a single source to verify charges, if any, on any asset created by any entity,
- charges/encumbrances created on the asset of an unregistered entity including individuals, HUF, Association of Persons can be easily traced and the information be readily available,
- chances of use of false title deeds or false representations on the title of the assets can be eliminated. Accordingly, fraud on title of properties can be controlled, minimised and eliminated,
- due diligence on portfolio securitisation can be eased out,
- due diligence on sale and purchase of assets/properties would become easy and transparent,
- gullible public and innocent buyers who are generally left in the hands of unscrupulous real estate brokers and builders can be saved and their interests protected,
- data on charged and encumbered properties can be made available in a transparent manner giving the industry reflection and exposure of the lenders on such assets, and
- once such Central Registry is established, the possibility of protecting the property by insuring the title deed of real estate properties may emerge in a big way.
- Since the land records are not computerised in all the states and tracing the title of properties is still a complex problem, the Central Registry would better equip the lender to make a fair assessment of risk undertaken while providing finance against the property, thus making lending more easy and safe.
- Bureaucratic delays and fleecing which happens on account of lack of transparency and procedure to determine the encumbrances would be reduced or eliminated, restoring faith in the land record system as well in respect of assets other than real estate. It is said that this will enthuse secured creditors to provide credit to productive sectors to help sustain the growth momentum of the economy.
- If there is a security interest being created in favour of two or more lenders, the details of inter se priority among them and whether they hold it on a paripassu or subordinate basis is to be specified. All details of transactions maintained in the Central Registry are open for inspection through its website, and during business hours at the Central Registry on payment of a fee.

Impact of Central Registry on Banks

There is a provision under Section 27 of the SARFAESI Act with regard to Central Registry that affects the bankers. This pertains to the penalty for not reporting the transactions in time. It is provided that every bank and its officers, who are in default, shall be punishable with a fine up to a maximum of Rs.5,000 per day for delay.

If the bank is in default, there may be a case for the Government to penalise the bank, but to penalise the officers of the bank as well, is felt to be a draconian measure. If penalty is to be levied on individual bank officers in addition to the banks, many officers could go bankrupt in case the authorities were to seriously enforce the law. Bank, a corporate entity, is a legal person and by fining both bank and officer, does it not amount to fining a person and also a limb of the person? It must be admitted that a similar provision exists in the Companies Act in regard to filing of particulars of charges created on the company's property and assets, but the authorities do not appear to have levied any fine on any officer of a company in default.

There is another anomaly. The mortgage or other charges, under Section 23 of the Act, are required to be filed/ registered within 30 days from the date of their creation. An extension of further 30 days alone is available after the initial period of 30 days on payment of 10 times the fee prescribed for the initial registration.

The objection is to the inherent time involved in submitting the transaction details to the Central Registry for registration. Obviously, the Central Registry cannot get the data from the 70,000 bank branches. It has to ask banks to identify nodal offices – say, regional or zonal offices, not exceeding 30 for big banks, 20 for medium-sized and 10 for small banks – which should be authorised to submit the information to the Central Registry. Nodal offices would, in turn, be fed by a large number of branches. Inevitably, 30 days (including bank holidays) would be insufficient for the banks to register all the transaction. This needs to be reviewed by the authorities.

There should be at least a few lakh mortgages created in favour of banks and financial institutions. And, after the first creation, every change, whether it be an increase or reduction in the loan amount, has to be

recorded. Recording all of this would be a gigantic task for the banks, in terms of their duty to register it, as well as the Central Registry.

Under the Companies Act, the obligation is on the borrower to register a charge whereas under Section 23 of the SARFAESI Act, the obligation lies on the secured creditor that is the bank. So, overall the setting up of the Central Registry creates an additional procedural burden on the banks as well as the bankers.

Position as regards under-construction property

As defined under the section 2 (1)(zc), secured asset means the property on which security interest is created; Now, property is defined under s 2 (t) of the same act as under:

"property" means--

- (i) immovable property;
- (ii) movable property;
- (iii) any debt or any right to receive payment of money, whether secured or unsecured;
- (iv) receivables, whether existing or future;
- (v) intangible assets, being know-how, patent, copyright, trade mark, licence, franchise or any other business or commercial right of similar nature.

The Transfer of Property Act states that assignment of a debt should be in whole and not apart assignment. Further, both the Transfer of Property Act and the Sale of Goods Act hold that only a property currently in existence is capable of being transferred.

These laws impede the development of securitisation of future receivables, as transfer of a future property does not fall under the definition of debt.

Below mentioned is an example of a case in which reference was made to the SARFAESI Act – the secured assets included 39 flats ‘under construction’ – therefore, can it be said that SARFAESI Act includes property under construction within its purview:-

ICICI Bank Ltd - Rs.1359.91 lacs: The loan outstanding as per book of account as at 31.03.2010 is Rs.1359.91 lacs after payments amounting to Rs.531 lacs by Land Marvel Homes (LMH) to whom the Company had transferred Project Paramount Gardens (Saligramam) development rights with related liabilities vide agreement dated 31.03.2005. **The bank has issued notice under the Securitization and Reconstruction of Financial Assets & Enforcement of Securities Interest Act 2002 (SARFAESI)** dated 10.07.2008 to recover an amount of Rs.4070.12 lacs including interest up to 22nd May 2008. The claim of the Bank towards interest, penalties and other charges is disputed by the Company and no provision made there against. The properties held by ICICI Bank as collateral security are i) Property in Perambur ii) **55.52% undivided share in the 129 grounds at West Mogappair and 39 flats under construction (from which the Bank ceded 11.84% undivided share to State Bank of Indore).**

In the light of priority over charges vis-à-vis the bank and statutory authorities like income tax as well as sales tax, custom and such fiscals - Whether secured creditors and really secured?

The Supreme Court has held that the DRT Act and SARFAESI Act do not per se create preceding charge in favour of banks, financial institutions and other secured creditors, while, a specific statutory charge will prevail over rights of any other secured creditor.

The 'doctrine of priority of state debts' is a settled principle under common law, as per which the government ('State') has first charge over the priority of debts. However, in the recent past there have been conflicts between secured creditors who have initiated credit recovery proceedings under the provisions of the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 ("DRT Act") or the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interests Act, 2002 ("SARFAESI Act") and the State, with respect to priority of claim on the debts due to them.

It has been contended by the State that by virtue of the doctrine of priority of state debt, they have priority over the claim of secured creditors. While, banks, financial institutions and other secured creditors, who have initiated proceedings under the SARFAESI Act or DRT Act have maintained that the non-obstante clause contained under the SARFAESI Act and DRT Act has an overriding effect on the provisions of any other legislation providing for recovery of dues, including the debts due to the State.

A non-obstante clause is a legislative device, which is usually employed to give overriding effect to certain provisions over some contrary provisions that may be found either in the same legislation or in some other legislation.

In the recent judgment of the Supreme Court of India ("Supreme Court") dated February 27, 2009, in the matter of Central Bank of India v. State of Kerala and Ors, the Supreme Court tagged various appeals involving interpretation non-obstante clauses contained in the SARFAESI Act and the DRT Act in light of the specific clauses contained under the State Government revenue legislations, including the Bombay Sales Act, 1959 ("Bombay Act") and Kerala General Sales Tax Act, 1963 ("Kerala Act"), which provides for creation of first charge in favour of State Government over the property of the assessee who has defaulted in payment of State Government dues.

The Supreme Court noted that the non-obstante provisions contained under the SARFAESI Act and DRT Act merely gives an overriding effect to the credit recovery proceedings initiated under the said two legislations. Further, the said Acts regulate the distribution of money received by the secured creditor, and do not per se create a preceding charge in favour of the secured creditor.

The Supreme Court also clarified that the DRT Act and SARFAESI Act and the State revenue legislations are within respective competent legislative power of Central and State legislatures and there is no ostensible overlapping between two sets of legislations.

The Supreme Court further remarked that, it could have given effect to the non-obstante clauses contained in DRT Act and SARFAESI Act, only if there was a specific provision in creating first charge in favour of the banks, financial institutions and other secured creditors. For the same, the Supreme Court cited the non-obstante provisions of the Companies Act, 1956 and the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 recognizing the priority of workers dues over other debts.

Similarly, in the year 2008, in Krishna Lifestyle Technologies Ltd v. Union of India, the Bombay High Court while considering the non-obstante provision of Central Excise Act, 1944 held that in absence of any specific provision creating first charge in favour of the State, the provisions of SARFAESI Act would override the provisions of the Central Excise Act, 1944 and the sale of the assets would be distributed in the order of priority of the creditor as provided under SARFAESI Act.

However, the Bombay High Court observed that, it is open to the State, to provide that its dues have priority of claims over the dues of a secured creditor(s). This understanding has been affirmed in the present case, where the Supreme Court has affirmed the provisions of the Bombay Act and Kerala Act, which provides for creation of first charge in favour of State.

Though, the Supreme Court has recognized the fact that the DRT Act and SARFAESI Act have been created for benefit of a banks, financial institutions and other secured creditors, it has been clarified that these two Central legislations do not per se create first charge in favour of the banks, financial institutions and other secured creditors. Thus, it can be concluded that the State would have priority of claim, if there is a specific provision giving priority to the State dues. However, if the dues are recoverable merely as arrears of land revenue, those debts cannot have priority of claim over the dues of a secured creditor.

Future Suggestions

The objective of setting up the Central Registry – to prevent frauds in loan cases involving multiple lending from different banks on the same immovable property – could be defeated by huge procedural lapses and problems.

Notifications in the Central Government Gazette – be they ordinary, extraordinary, special, and so on – are elusive to even government departments and the RBI, not to speak of banks and the common man. The May 26, 2011, notification/circular issued by the RBI, which is supposed to contain the entire rules published in the Government of India Gazette of March 31, 2011, does not contain Forms I to IV, said to have been appended to the said rules.

Further, the SARFAESI Act needs to be amended to provide that registration could be done at the head-office or at designated branches of the Central Registry. Otherwise, the Central Registry would be bogged down with massive work, which it will find extremely difficult, if not impossible, to do.

This benefit of searching and drawing a presumption about the existence or otherwise of a security interest, does not apply to India. Indian law, exactly contrary to the very spirit of international laws, says that the non-

filing of security interest will not affect priority. This would mean, a lender may have obtained security interest, and not filed it, and yet claim priority over a second lender who would have searched the Central Registry, not found the charge, and hence, went ahead and sanctioned a loan on the same asset. If the fact of non-registration does not affect the validity or priority of a security interest, then the very reliability of the searching process gets negated. And if the search of the Central Registry does not have an unquestionable reliability, one wonders why it exists at all? After all, the Central Registry is not a library of security interests, displaying its proud possessions!

Some provision must be brought into existence which makes filing of security interest mandatory. Only then will non-filing of security interest affect priority. This enabling provision will ensure that the purpose of a Central Registry is efficiently solved.

