

## CRITICAL ANALYSIS OF RDDBFI AND SARFAESI ACT

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### ABSTRACT

*Debt recovery has been a huge issue in India for decades. Prior to 1993, there was no effective legal mechanism for debt recovery, which forced the banks to take the long route of civil procedure to recover their dues, which caused a lot of procedural delays and further hampered the economic growth of the country. Later in 1993, the RDDBFI Act was enacted to provide an effective legal mechanism for banks to recover debt, and in 2002, the SARFAESI Act came into force, enabling banks to recover debt without the intervention of the court. The article tends to critically analyse the two acts with reference to case laws and find out whether they have been effective in the recovery of debt, followed by a conclusion and suggestions.*

**Keywords :** *Banks, Court, Debt Recovery, Economic Growth, Legal Mechanism.*

## 1. INTRODUCTION

In 1993, the RDDBFI (Recovery of Debt Due to Banks and Financial Institutions) Act<sup>1</sup> was enacted with the purpose of providing an effective legal mechanism for banks and financial institutions to recover their debts. This article tends to analyse the effectiveness of RDDBFI Act and SARFAESI Act with a critical approach.

Certain implications of the RDDBFI Act:

- DRT (Debt Recovery Tribunal) is to be constituted as per the Act as a statutory body for debt recovery.
- The DRTs must consist of a 'Presiding Officer' who must be qualified to be a district judge and whose tenure must be 5 years or till the age of 62 years. DRT also consists of a 'Recovery Officer' who works on the basis of a 'Recovery Certificate' issued by the Presiding Officer.
- The applications made to DRTs must be decided within 180 days of such applications.
- The minimum amount of debt due should be at least 20 lakh rupees in order to approach DRT.
- A DRAT (Debt Recovery Appellate Tribunal) appeal can be filed against the order of DRT in DRAT within 30 days of such an order.
- The applicant has to deposit 50% of the order amount to the DRAT.

DRT has the exclusive power to deal with debt recovery cases, but the Supreme Court and the High Court have the power to deal with such cases in cases of writ petitions under Articles 32<sup>2</sup> and 226 of the Indian Constitution<sup>3</sup>.

In *Union of India & Anr v. Delhi High Court Bar Association & Ors*<sup>4</sup>, the question was raised: Is the said act valid on constitutional grounds? The act was struck down by the Delhi High Court, stating that it violated the independence of the judiciary. The Supreme Court stated in the case that the manner in which the proceedings were conducted prior to the passing of the act was according to civil procedure, but the said act states that to constitute a tribunal for the recovery of debt, parliament under Articles 323A and 323B of the Indian

<sup>1</sup> Recovery of Debt Due to Banks and Financial Institutions, 1993, No. 51, Acts of Parliament, 1993 (India)

<sup>2</sup> INDIA CONST. art. 32

<sup>3</sup> INDIA CONST. art. 226

<sup>4</sup> *Delhi High Court Bar Association & Ors v. Union of India & Anr*, 2002 (4) SCC 275

Constitution is empowered to constitute tribunals<sup>5</sup>. Thus, the Supreme Court was of the opinion that the disputed act does not hinder the independence of the judiciary, and the act was held constitutionally valid.

Even after the commencement of the act, there were major procedural delays in disposing of the suits. Later in 2002, the SARFAESI [Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest] Act came into force with the main objective of dealing with the NPAs [Non Performing Assets]. The act empowered secured creditors to acquire the asset held as security in case of default in repayment of the loan without the intervention of any court. However, an appeal can be filed against the action of the secured creditors in DRT within 45 days of such notice.

Implications of the Act:

- The amount of the loan should be 1 lakh rupees and above. The loan must be secured.
- The creditor must auction the acquired asset to the Asset Reconstruction Company to recover the due amount.
- The act is not applicable if 80% of the due amount has been recovered.
- The banks and financial institutions must serve notice to the borrower classified as an NPA and give 60 days to settle the dues. If dues are not settled within the given time period, the bank is entitled to acquire the security.

In *Mardia Chemicals v. Union of India*<sup>6</sup>, the Supreme Court dealt with the issue of whether sections 13 and 17 were arbitrary in nature. The court held that the very purpose of the act was the quick recovery of the debt. The sections cannot be held unconstitutional for the reason that they are harsh on borrowers. Thus, the act was held valid, and an appeal can be made in DRT without deposition of any amount.

## 2. CRITICAL ANALYSIS WITH CASE LAWS

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<sup>5</sup> INDIA CONST. art. 323

<sup>6</sup> *Mardia chemicals v. Union of India*, AIR ONLINE 2004 SC 948

Though both acts appear to be without any ambiguity theoretically, that is not the case when dealing with the practical aspect. Section 34 of SARFAESI was questioned in<sup>7</sup>:

*Leelamma Mathew v. Indian Overseas Bank*<sup>8</sup>: The bank auctioned property to the auction purchaser it was a dispute regarding the area of the property the court ordered the Bank to pay compensation to petitioner but the Bank challenged the maintainability of the suit as per section 34. The Supreme Court interpreted that the suit was for ‘damages and compensation’ in accordance with the property, which could not have been decided by the DRT or DRAT as the auction purchaser did not challenge the sale certificate, which does not fall within the purview of the tribunal.

There is an ambiguity between the RDB Act<sup>9</sup> and the Civil Procedure Code, as seen in the case *Bank of Rajasthan Ltd. v. VCK Shares & Stock Broking*<sup>10</sup>. The bank initiated a proceeding against the borrowers under Section 19 of the RDB Act. The borrower filed a civil suit in the Calcutta High Court seeking a decree for the sale of pledged shares and recovery of the proceeds. The Supreme Court was of the opinion that a borrower can initiate a civil proceeding as there is no bar against such a proceeding in the RDB Act. No power is inferred from the courts to transfer such proceedings to the DRTs; now that there is no power to transfer the suit, the consent of the borrower to transfer the case does not come into question.

Section 13(8) of SARFAESI<sup>11</sup> came into question in *Moonlight Poultry Farm v. Union of India*<sup>12</sup>. The main question was, to what extent does the right to exercise the right to redemption of the mortgage exist? The High Court found that 13(8) merely deals with the date at which the secured creditor’s right to transfer commences; the right to redeem does not expire on the date fixed for sale. This section is silent on when the right of redemption is exhausted. The court further stated that the right is not exhausted immediately upon the highest bid made by the auction purchaser; it is subsequent to the deposit of outstanding dues

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<sup>7</sup> Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, § 34, No. 54, Acts of Parliament, 2002 (India)

<sup>8</sup> *Leelamma Mathew v. Indian Overseas Bank*, 2022 SCC Online SC 1601

<sup>9</sup> The RDDBFI Act is now called the Recovery of Debts and Bankruptcy Act (RDB Act, 1993)

<sup>10</sup> *Bank of Rajasthan v. VCK Shares & Stock Broking*, 2022 SCC Online SC 1557

<sup>11</sup> Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, § 13(8), No. 54, Acts of Parliament, 2002 (India)

<sup>12</sup> *Moonlight poultry farm v. Union of India*, 2022 SCC Online AP 2424

by the borrower. Thus, it was held that the borrower had exercised the right of redemption timely; subsequently, the sale certificate was nullified.

Presently, there are 39 DRTs and 5 DRATs for dealing with debt recovery matters. As per the reports, there are about 15,8000 pending cases with the tribunals as of February 2023, which nearly amounts to total dues of 4.43 lakh crore rupees. The purpose of both acts was to ensure speedy recovery and, secondly, reduce the burden of the civil courts. As far as speedy recovery is concerned, a time of 180 days is given to the tribunal for the disposal of suits under the act, but when the real scenario is concerned, there are procedural delays from the parties to the suit that cause delays. When the suit has been decided by the tribunal, the aggrieved parties have the right to file a writ petition. There is no doubt that it is a fundamental right, but the principle of speedy recovery is sacrificed. One case takes years to reach the final judgement, leaving behind a huge backlog of cases.

SARFAESI Act was introduced to provide an effective mechanism to deal with NPAs. The procedures appear to be straight in the act, but firstly, unsecured creditors are exempt. The term 'wilful defaulter' has not been very clearly stated, leaving huge scope for the banks to misuse it. In some cases, banks tend to take possession even if the borrower is not a wilful defaulter, and banks even tend to make misrepresentations of documents to take possession.

Once possession of the secured asset is taken, an auction is held in which ARCs bid to acquire the asset, which is again a complex procedure. Usually, banks discharge those assets at a much lower value, and even the issued sale certificate can be challenged by the borrower, which marks further delay.

One of the major issues with the act is that it has highly ignored the interests of the buyers; it has provided much greater autonomy to the banks and financial institutions; in a way, it has acted as a tool of harassment to borrowers.

### **3. CONCLUSION & SUGGESTIONS**

In my opinion, both RDB Act and SARFAESI Act have been successful to some extent when it comes to debt recovery. However, there is a strict need to work on the loopholes as far as

efficiency is concerned. A major shortcoming is ambiguity in interpretations, as seen in the case where there is a tussle between the DRT and civil court regarding the filing of a counterclaim. The auction purchaser has moved to DRT to claim compensation, where the civil court is empowered to hold a proceeding. To avoid procedural delays, ambiguous sections should be amended concerning the present issues. Clarity in interpretation will save much of the time, which will serve the primary purpose of both acts, which is the speedy recovery of debts. The number of total DRTs and DRATs should be increased to enhance procedural efficiency.

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