



BANKING AND FINANCE

THE PRINCIPLE OF “AS IS WHERE IS” AND “AS IS WHAT IS BASIS” IN RELATION TO SECURED ASSETS PURCHASED IN PUBLIC AUCTION UNDER SARFAESI ACT, 2002

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INTRODUCTION

As the Legal frame work and mechanism for curtailing and controlling mounting Non- Performing Assets (“**NPA**”) has become inadequate and outdated which resulted in tardy recovery of defaulting loans by the Financial Institutions arising out of such NPAs, the Central Government of India constituted Narasimhan Committee I and II and Andhyarujina Committee (“**Committees**”) for the purpose of examining banking sector reforms. The Committees inter-alia, have suggested enactment of a new legislation for securitisation and empowering banks and financial institutions to take possession of the securities and sell them without the intervention of the Courts. Based on the recommendations of the Committees, Central Government has enacted [Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002](#) (“**SARFAESI Act**”) which came into force on 21st June 2002.

FUNDAMENTAL OBJECTIVE OF THE SARFAESI ACT

The fundamental objective of the [SARFAESI Act](#) is to entitle a Secured Creditor^[1] to enforce Security Interest^[2] created in its favour in a time bound manner, decrease asset liability mismatches, transfer of NPA accounts to Asset Reconstruction Companies, provide a legal framework for Securitisation of Assets and providing speedy adjudicating mechanism for addressing the grievances of the aggrieved parties.

IMPORTANT PROVISIONS UNDER SARFAESI ACT FOR ENFORCING SECURITY INTEREST CREATED BY THE BORROWER

Subsequent to availing financial assistance from a Secured Creditor, if a borrower defaults in repaying the secured debt, the loan account of the borrower will be classified as NPA. Thereafter, a Secured Creditor enforces its rights under SARFAESI Act by issuing a notice under Section 13(2) to the borrower calling upon it to pay the outstanding/defaulted amount within a period of sixty (60) days from the date of notice, failing which Secured Creditor shall be entitled to exercise all or any of its rights under Section 13(4) of the SARFAESI Act.

If a borrower fails to discharge its liability subsequent to receipt of notice under Section 13(2) of the SARFAESI Act, a Secured Creditor can take one or more recourses contemplated under Section 13(4) of the SARFAESI Act. Further, where a borrower creates a Security Interest in favour of a Secured Creditor, securing repayment of loan amount and in case of default by a borrower, Secured Creditor can take recourse under Section 13(4)(a)^[3] of the SARFAESI Act in compliance with rules stipulated under Security Interest (Enforcement) Rule, 2002 (“**Rules**”).

A Secured Creditor can proceed with the sale of Secured Immovable Asset only in accordance with the procedure contemplated under the Rules. If the sale of Secured Asset is being effected either by inviting tenders from the public or by holding public auction, a Secured Creditor shall cause a public notice as per Rule 8(6)^[4] a to Rule 8(6) f of the Rules.

SALE OF SECURED ASSET BY PUBLIC AUCTION

As a general practice, in most of the public auction notice, in addition to other conditions mentioned therein, Secured Creditor incorporates a condition that, Secured Asset is auctioned on “as is where is” and “as is what is basis” unless specified otherwise. This means a successful bidder of the Secured Asset will inherit all the physical and legal conditions of the Secured Asset and the Secured Creditor shall not be responsible for any charge, lien and encumbrance etc., with respect of auctioned Secured Asset.

A successful bidder of the Secured Asset under the public auction has to pay the sale consideration as per the timelines provided under Rule 9(3)^[5] and 9(4)^[6] of the Rules and if the same is not complied by the auction purchaser the amount already paid shall be forfeited by the Secured Creditor under Rule 9(5)^[7]

Pursuant to purchasing the auctioned property and before paying balance sale consideration, there may be several instances wherein an auction purchaser may either demand for refund of the amount already paid or request for cancellation of sale if sale certificate is already issued, inter-alia on the ground that there exists an encumbrance on the auctioned property by litigation, defect in title or on the apprehension that title may not be proper and that the Secured Creditor may not be in possession to deliver physical and vacant possession of the Auctioned Property.

When such claims are raised by the auction purchaser, a Secured Creditor generally rejects such claims on the ground that Secured Asset was sold on “as is where is” and “as is what is basis” and Secured Creditor asserts that the rule of caveat emptor would apply and the auction purchaser ought to have undertaken proper due diligence before purchasing the Secured Asset.

The author’s humble endeavor through this article is to summarize the legal position on the concept of as is where is” and “as is what is basis vis-a-vis Secured Assets purchased in public auction in light of various landmark judgments passed by Hon’ble High Court (“**HC**”).

In matter of Rekha Sahu [\[8\]](#) the Hon’ble HC of Allahabad has observed that under Section 55(1) of the Transfer of Property Act, 1882, a seller is bound to disclose to the buyer any material defect in the property or title thereto. The Court further observed that a duty is cast upon the authorized officer of the Secured Creditor to disclose to the auction purchaser any material defect in the title, failing which it could be construed that the purchaser was misled. The Bench further observed that it is evident that the immunity claimed by the bank on the pretext of as is where is and as is what is basis was dying a slow death and the secured creditor has to make due diligence/thorough search of the property before proposing its sale.

In the matter of Atishaya Construction Pvt. Ltd [\[9\]](#) the Petitioner has filed the case for refund the sale consideration of the property purchased on auction conducted by the Respondent on the ground that it was unable to hand over the possession of the property in question as an application was pending with the Chief Metropolitan Magistrate and that possession could be given only after obtaining necessary orders from the learned Chief Metropolitan Magistrate and this vital information was not brought to knowledge of the Petitioner in the Public Auction Notice. The Respondent claimed that the property was auctioned on as is where basis is.

The Hon’ble Gujarat HC has held that the Respondent cannot be permitted to, on the one hand, retain the sale consideration and on the other hand, not hand over the possession of the property in question to the Petitioner. The action of the Respondent in not handing over the property in question to the Petitioner despite the total sale consideration having been deposited in terms of sub-rule (6) of Rule 9 of the rules, is clearly contrary to Rule 9 of the Rules. Under these circumstances, the court was of the view that the Petitioner was entitled to refund of the amount

In the matter of Jai Logistic [\[10\]](#) the Hon’ble Madras HC has held that Rule 8(6)(f) mandates the Secured Creditors to set out in the terms of sale notice any other thing which the authorised officer considers it material for a purchaser to know to judge the nature and value of the property. A reading of the said rule, in our opinion, would also include the encumbrance relating to the property. We are inclined to read the rule in that way keeping in mind the interest of the intending purchaser to be put on notice as to the encumbrance, as otherwise he/she will be purchasing the property and simultaneously buying the litigation as well and an intending purchaser may not bid in the event he/she came to know of any encumbrance over the property.

That is why the rule specifically contemplates a provision for the authorised officer, while notifying the sale, to specifically state as to the encumbrance. The Hon’ble HC further held that, in the event the auction notice indicated that it is the duty of the intending purchaser to verify not only the encumbrance by way of alienation of the property, but also the other statutory liabilities and in that case, the intending purchaser cannot later on turn around and seek for either the refund of the earnest money deposited or insist the bank to clear the encumbrance.

In the matter of Mandava Krishna Chaitanya [\[11\]](#) the Hon’ble HC of Hyderabad for the State of Telangana and Andhra Pradesh has held that the concept of ‘as is where is’ and ‘as is what is’ basis has lost its significance in the current commercial milieu and the principle of caveat venditor is more on the rise as compared to the outdated principle of caveat emptor.

CONCLUSION

In view of the judicial precedents explained hereinabove, it can be concluded that, a duty is cast upon the Secured Creditor to disclose all encumbrances relating to the auctioned property in the public notice. If a Secured Creditor fails to disclose encumbrances relating to the auctioned property, it cannot later claim protection on the pretext of “as is where is” and as is what is’ basis for the fact that the same has lost its significance in the current commercial set-up and the principle of caveat emptor cannot be made applicable to the properties purchased in auction conducted under SARFAESI Act.

Disclaimer:

The article merely constitutes the views presented by the author on the various judgments pronounced in the above article by the various law courts on the subject matter and should not be considered as recommendations or opinion. The author relies on the facts and the ratio opined by the law courts. The author disclaims and shall not be liable for any direct, indirect, special or

incidental damages resulting from or arising out of or in connection with the use of the information by any person, entity, association or institution.

[1] “secured creditor” as per Section 2 (1) (zd) of SARFAESI Act:- any bank or financial institution or any consortium or group of banks or financial institutions and includes— (i) debenture trustee appointed by any bank or financial institution; or (ii) securitisation company or reconstruction company, whether acting as such or managing a trust set up by such securitisation company or reconstruction company for the securitisation or reconstruction, as the case may be; or (iii) any other trustee holding securities on behalf of a bank or financial institution,

[2] “security interest” as per Section 2 (1) (zf) of SARFAESI Act:- means right, title and interest of any kind whatsoever upon property, created in favour of any secured creditor and includes any mortgage, charge, hypothecation, assignment other than those specified in section 31;

[3] Section 13(4)(a) of Sarfaesi Act 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;

[4] Rule 8(6)[4] (a) The description of the immovable property to be sold, including the details of the encumbrances known to the secured creditor; (b) the secured debt for recovery of which the property is to be sold; (c) reserve price, below which the property may not be sold; (d) time and place of public auction or the time after which sale by any other mode shall be completed; (e) depositing earnest money as may be stipulated by the secured creditor; (f) any other thing which the authorised officer considers it material for a purchaser to know in order to judge the nature and value of the property.

[5] Rule 9 (3) on every sale of immovable property, the purchaser shall immediately pay a deposit of twenty-five per cent. of the amount of the sale price, to the authorised officer conducting the sale and in default of such deposit, the property shall forthwith be sold again.

[6] Rule 9 (4) The balance amount of purchase price payable shall be paid by the purchaser to the authorised officer on or before the fifteenth day of confirmation of sale of the immovable property or such extended period as may be agreed upon in writing between the parties.

[7] Rule 9(5) (5) In default of payment within the period mentioned in sub-rule (4), the deposit shall be forfeited and the property shall be resold and the defaulting purchaser shall forfeit all claim to the property or to any part of the sum for which it may be subsequently sold.

[8] Rekha Sahu v. UCO Bank MANU/UP/1191/2013: (2014) BC 221 (DB) (ALL),

[9] Atishaya Construction Pvt. Ltd. v. Central Bank of India MANU/GJ/1517/2014

[10] Jai Logistic v. The Authorised Officer, Syndicate Bank MANU/TN/1161/2010

[11] Mandava Krishna Chaitanya Vs.: UCO Bank, Asset Management Branch MANU/AP/0087/2018