HOMEBUYERS VS SECURED CREDITORS: ANALYSIS OF SUPREME COURT'S 2022 RULING AND ITS IMPACT ON HOUSING FINANCE NPA

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ABSTRACT

The landmark judgment of the Supreme Court in the case of Union Bank of India vs Rajasthan RERA [1]shows the attempt of the judiciary to balance the protection of homebuyers and the rights of creditors in India's real estate sector. This article aims to examine the judicial precedent that has established the supremacy of RERA over the SARFAESI Act, and to analyse the immediate and long-term implications of these changes for housing finance Non-Performing Assets (NPAs). The article also delves into the question of whether these consumer-centric changes brought by this ruling would create new challenges for the financial sector stability in real estate housing finance.

Keywords: Rera, Sarfaesi, Mortgage, Secured Creditors, Financial Institutions, Banking Sector.

[1] *Union Bank of India v. Rajasthan Real Estate Regulatory Authority*, (2022) SCC Online SC 123 (India).

INTRODUCTION:

The real estate sector in India has seen unprecedented judicial intervention in recent years, and this has caused changes in the relationship between homebuyers, developers, and financial institutions. The Real Estate (Regulations and Development) Act, 2016 [2]was introduced in 2016 with an aim of resolving issues such as delays in the completion of projects, escalations in the costs due to default of the parties, and malpractices of developers, which have always been the constant cause of worry for homebuyers. The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI)[3] provides the powers to the banks and the financial institutions to recover the secured debts without the intervention of the courts. The tussle between these two legislations was addressed by the Supreme Court in the case of Union Bank of India vs Rajasthan RERA, which held that provisions of RERA take precedence over SARFAESI in matters of the protection of rights of homebuyers.

RERA's Consumer Centric Approach:

Section 11(4)(a) of RERA requires that 70% of the project fund received from allottees should be deposited in a separate escrow account. This provision aims to address the issue of diversion of funds where developers utilize the proceeds from one project and finance other projects, which results in leaving the initial project underfunded. This provision permits the withdrawal of the funds from this account only for the land acquisition and the construction costs. These withdrawals by the developer depend on the certifications from engineers, architects, and chartered accountants. The homebuyers can also track the utilization of these funds through the periodic updates on the RERA portal. Section 18 of RERA provides both compensatory and punitive measures against defaulting developers. This section requires the payment of interest at the State Bank of India's highest marginal cost of lending rate plus 2% for delayed possession, which creates the financial incentives for the timely completion of the projects.

RERA introduces the state legal regulatory bodies, which have quasi-judicial powers. There is also a divergence in the dispute resolution process; the civil remedies before RERA required lengthy court proceedings. The RERA authorities have the powers and jurisdiction to conduct

[2] The Real Estate (Regulation and Development) Act, No. 16 of 2016, Acts of Parliament, 2016 (India).
[3] The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, No. 54 of 2002, Acts of Parliament, 2002 (India).

the summary proceedings and adjudicate the disputes within the time duration provided in the statute.

SARFAESI's Creditor Centric Approach

There is a revolution in the debt recovery process after the introduction of the SARFAESI Act, 2002, because this act allows the secured creditors to enforce security interests without the intervention of the court. Section 13(2) allows the banks to take possession of the secured assets, and Section 13(4) provides the powers to the bank to sell the asset without the need for the involvement of the judiciary. This legislation was introduced with the purpose of addressing the crisis of NPA and to fast-track the process of recovery of the debts.

Judicial Trends Prior to 2022

Before the ruling in Union Bank of India v Rajasthan RERA, the judiciary had given priority to the rights of secured creditors under the SARFAESI Act over the protections to the homebuyers. This approach of the judiciary has been to ensure the stability of the banking sector at the expense of the interests of the consumers. This approach has created a hierarchical approach and has placed secure financial institutions over the individual homebuyers.

Mardia Chemicals Ltd v Union of India (2004): This case challenges the constitutional validity of the SARFAESI Act, especially sections 13, 15,17, and 34. The petitioners argued that the act conferred unchecked powers on banks and financial institutions, and borrowers are provided no adequate forum to challenge the correctness or validity of the lender's claims before action is taken. Under Section 17, borrowers are allowed to appeal to the Debt Recovery Tribunal only after the lender has taken possession or sold the asset. The borrowers are also required to deposit 75% of the claimed amount to entertain the appeal, which seems to be a barrier to justice for the borrowers. The Supreme Court in this case upheld the constitutional validity of the SARFAESI Act and recognized the requirement of a swift way to address NPAs and the need for effective recovery of debt by financial institutions for the economy[4].

Bikram Chatterji vs Union of India (2019): In this case, the Court held that RERA is a special legislation which is intended to protect the homebuyers from project delays, frauds, and builder malpractices. In situations involving the rights of homebuyers, such as delayed possession,

[4] *Mardia Chemicals Ltd. v. Union of India*, (2004) 4 SCC 311 (India).

fund diversions, RERA prevails over SARFAESI, but SARFAESI proceedings would receive priority in disputes that are unrelated to homebuyers, such as debt recovery[5].

M/S New Tech Promoters and Developers Pvt Ltd vs State of UP & Ors (2021): In this case, Uttar Pradesh RERA directed the promoter to refund buyers with interest. This order was challenged by the developer on the grounds that RERA lacks jurisdiction over disputes that involve secured creditors. The key questions were whether RERA has the power to issue directions against banks and financial institutions who has taken control over the project as secured creditors under SARFAESI and whether RERA's jurisdiction shows a conflict with the debt recovery process under the SARFAESI Act. The Supreme Court held that under Section 13(4) of SARFAESI, banks take possession of a project and step into the shoes of the promoter and become an "assignee" under Section 2(zk)(i) of RERA. As an assignee, banks assume the responsibilities of a promoter, which include the responsibilities towards homebuyers, such as ensuring the completion of the project and refunds. The Court held that RERA is not ultra vires when applied to secured creditors, and RERA has the power to entertain complaints against the banks if the enforcement of the SARFAESI Act has an impact on the rights of homebuyers[6].

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In this case, the developer defaulted on a loan taken from Andhra Bank (later merged with Union Bank of India), which led to the initiation of recovery proceedings by the bank under the SARFAESI Act through the auctioning of the mortgaged real estate project. The homebuyers challenged it by filing complaints before the Rajasthan RERA and contended that banks should be treated as promoters or assignees under RERA and they should be subjected to the obligations of RERA. The moot question before the court in this case was whether RERA has the jurisdiction to entertain complaints against banks or financial institutions that act as secured creditors under the SARFAESI Act. The second question was which legislation should prevail in cases of conflict between RERA and SARFAESI.

The Rajasthan High Court analysed the issues and held that RERA has jurisdiction over the banks and financial institutions who has taken possession of the project under SARFAESI, and they can be treated as "assignees" of the promoter under Section 2(zk) of RERA. It was also

[5] *Bikram Chatterji v. Union of India*, (2019) SCC Online SC 1509 (India).
[6] *M/s New Tech Promoters and Developers Pvt Ltd v. State of UP & Ors*, (2021) SCC Online SC 789 (India).

held that RERA has the power to issue directions to the banks if there is initiation of proceedings by homebuyers to protect their rights, and in circumstances of conflict between RERA and SARFAESI, RERA provisions would be given precedence.

The judgment of the Rajasthan High Court was upheld by the Supreme Court, and confirmed that banks, after taking possession of the mortgaged property, step into the shoes of the promoter and become liable to follow the obligations created by RERA. RERA has the jurisdiction to adjudicate the complaints filed by the homebuyers if the bank takes possession of the project and starts proceedings under Section 13(4) of SARFAESI.

ANALYSIS OF SUPREME COURT JUDGMENT:

The Supreme Court, through this decision, has established the primacy of RERA proceedings over SARFAESI when the rights of homebuyers are concerned. The decision of the court to provide authority to RERA to entertain complaints by homebuyers against banks who has taken possession of the projects as secured creditors extends the reach of RERA beyond the developers of real estate projects, but also to the financial institutions that function as third parties as secured creditors. This judgment can have a far-reaching impact because of the involvement of various stakeholders in these real estate projects. This judgment benefits the homebuyers because they can now take recourse to the RERA authorities when the possession of projects is taken over by secured creditors in cases of default[7]. This would ensure the protection of the rights of consumers despite the change in the ownership of the projects. This judgment has clarified that homebuyers can file complaints before RERA immediately if the banks and financial institutions start the proceedings under Section 13(4) of the SARFAESI Act after taking possession due to the default of the promoter in paying dues.

However, this decision can create legal challenges for the banking sector. This decision introduces additional regulations for banks and financial institutions, which make the process of debt recovery more difficult and time-consuming. The process to realize their interests in the distressed real estate projects would become more complicated and prolonged.

The overall legal and policy implications of this judgement are the attempt of the judiciary to establish the relationship between commercial efficiency and consumer protection in India's

[7] **Partha N. Mansukhani**, *Supreme Court Rules on Mandatory Procedure under the SARFAESI Act*, IndiaCorpLaw (Apr. 1, 2025), https://indiacorplaw.in/2018/04/supreme-court-rules-mandatory-procedure-sarfaesi-act.html.

developing market economy. This decision shows that commercial law principles, which stress the preservation of the economy, cannot be given priority over the protection of the rights of consumers whose financial commitments are at stake[8].

IMPLICATIONS OF JUDGMENT OVER THE SECURED CREDITORS AND FINANCIAL INSTITUTIONS:

The banks and financial institutions are now required to abide by not only the existing laws of SARDAESI proceedings, but also to comply with RERA complaints when they take possession of the real estate project. There is expansion in the liability of banks and financial institutions that invoke Section 13(4) of SARFAESI because now they would be considered as "assignees" of the original promoters under RERA Section 2(zk). This means banks and financial institutions are now subject to RERA's promoter obligations, such as ensuring the completion of the project and refunds. This creates additional compliance burdens for these financial institutions and extends the usual time frame that is required to recover the distressed assets by banks. These changes hold huge significance in the banking sector because real estate loans constitute a substantial portion of the loans given by the banks. The potential implication of this judgment can be a reduction in the grant of loans for real estate projects because banks would now consider factors such as additional costs, risk assessment, and delays associated with the recovery of distressed real estate projects. Real estate financing would take a dip in the economy, and hence, there would be a slump in the availability of credit in this sector[9].

RECOMMENDATIONS:

There is a need to bring the changes in the RERA and SARFAESI provisions to make them more harmonized. The current interpretation of the provisions is creating challenges in the enforcement of the rights of homebuyers and financial institutions. There is a need for amendments in existing laws which can help to delineate the scope and jurisdiction of each authority while also keeping in mind the objective of protecting of rights of consumers. There is a need for consultation between the Ministry of Housing and Urban Affairs, the Reserve

[8] **Navya Shekhar**, *Resolving Real Estate Insolvency: Safeguarding Homebuyers' Interests While Ensuring Project Completion*, IBC Law (Apr. 24, 2025), https://ibclaw.in/resolving-real-estate-insolvency-safeguarding-homebuyers-interests-while-ensuring-project-completion-by-adv-navya-shekhar/.

[9] **Aryaditya Chatterjee**, *The Compromised Position of "Secured Creditors" under The Real Estate Regulatory Authority Act, 2016*, IBC Law Blog (Aug. 1, 2023), https://ibclaw.blog/the-compromised-position-of-secured-creditors-under-the-real-estate-regulatory-authority-act-2016-aryaditya-chatterjee/.

Bank of India, and state RERA authorities for the creation of a standard procedure to be followed in housing finance default cases. This would help to provide certainty and clarity to all the stakeholders. Secondly, the effective implementation of the directions of the Supreme Court in this case requires the initiatives to build the capacity of the RERA authorities to handle the cases of debt recovery, housing finance, and banking transactions. There should be a development of alternative dispute resolution to resolve disputes that involve homebuyers, developers, and secured creditors. This system would help to resolve disputes through mediation and conciliation procedures and provide resolution in a more efficient and cost-effective way. There is a need for regulatory reforms to address the conflict between RERA and SARFAESI and to establish clear jurisdictional boundaries for handling complex cases that involve secured creditors.

CONCLUSION:

The case of Union Bank of India vs Rajasthan RERA shows the conflict between RERA and SARFAESI, the two important legislations that govern the Indian housing finance. Before this judgment, primacy was given to SARFAESI proceedings, considering the mounting non-performing assets in the Indian banking sector. RERA is based on the protection of consumers and on addressing the power imbalances faced by disadvantaged individual consumers in complex commercial transactions. The legal conflict starts due to the intersection of both these legislations in the real estate sector, where homebuyers provide the advance funds to the developers, and banks provide the secured finance for the construction of the projects to the developers. The tussle begins when there is a default on bank loans and banks exercise their SARFAESI rights to take possession of the project, but the rights of homebuyers used to not get protection. The analysis of this judgment shows the attempt of the judiciary to reconcile the competing demands of commercial efficiency and protection of consumers. It can have far-reaching implications, and its ultimate success will depend on its implementation effectiveness and its fulfillment of the objective of consumer protection without causing negative consequences on the functioning of the financial sector[10].

[10] **Shardul Amarchand Mangaldas & Co**, *RERA vs. SARFAESI: Supreme Court Clarifies Jurisdictional Overlap*, SAM & Co. Insights (Feb. 14, 2022), https://www.amsshardul.com/insight/rera-vs-sarfaesi/.