

IMPERFECTIONS OF LAW OF PERFECTION-OF-SECURITY SYSTEM IN INDIA

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Abstract

*It is well accepted that access to credit is crucial for economic growth. Intellectual Property is recognised as a valuable asset world over and it is considered that use of intellectual property as security asset can increase available credit. When a security** interest is created by borrower/other person interested in the borrower, in favour of lender, it becomes enforceable against the borrower/that other person who created security interest. But the existence of the security interest will not necessarily be known to third parties who propose to acquire an interest in the asset, or to other unsecured creditors. To safeguard such people law usually requires the secured party to give some form of public notice. This requirement of public notice is known as perfection requirement for third party effectiveness. The perfection systems presently existing in India are Registration/Filing/Noting with Authorities under Intellectual Property Statutes and Laws Other Than Intellectual Property Statutes; and Possession/deposit of title document based perfection systems. Attempt in the article is to survey the existing system(s) of perfection of security interest recognised in India to see its appropriateness to IP secured Financing and bring out imperfections thereof.*

PREFERRED CITATION

- Dr. Lawwellman P, Imperfections of law of perfection-of-security system in India, *The Lex-Warrier: Online Law Journal* (2018) 1, pp. 1 – 18, ISSN (O): 2319-8338

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** The term 'Security' means either the mode security or the asset in respect of which security right is created, depending on the context.

INTRODUCTION

Secured credit¹ is an efficient form of lending, which, when implemented in a proper legal and institutional framework, can reduce transaction costs associated with borrowing and thus stimulate economic activity. Historically, secured lending laws and institutions associated with specific type of property have been reformed as that type of property assumed increased economic importance².

'Intellectual Property' is subject matter protectable as copyright, patent, trademark including subject matter protectable under passing off, industrial designs, geographical indication of goods including subject matter protectable under passing off, plant varieties and farmers' rights and Layout-designs under respective law in India and includes trade secrets; and Intellectual property is being accepted as one of the most valuable commercial asset world over.³ It is

recognized that use of intellectual property as security asset can increase the amount of available credit⁴. In India, the National Intellectual Property Rights Policy, 2016 acknowledges possibility of using intellectual property as collateral for credit⁵.

CONTEXT

When a security interest is created by borrower/other person interested in the borrower, in favour of lender, it becomes enforceable against the borrower/that other person who created security interest. But the existence of the security interest will not necessarily be known to third parties who propose to acquire an interest in the asset, or to other unsecured creditors. To safeguard such people law usually requires the secured party to give some form of public notice. This requirement of public notice is known as perfection requirement for third party effectiveness⁶.

The law has long exhibited deep suspicion of secret liens that do not put third parties on reasonable notice of the financing. The fear is that such devices would allow a debtor to induce innocent persons to purchase the collateral or extend false credit

¹'Secured Credit' is a credit transaction where the borrower or other person interested in the borrower would create security interest in respect of his property in favour of lender so that in case of default on the part of borrower the lender can proceed against security property to realise the amount due.

²Norman Siebrasse and Catherine Walsh, *Leveraging Knowledge Assets*, RFP # LCC/CDC 00-226, 2002, p. v (Report of the Project Commissioned by Law Commission of Canada).

³The World Intellectual Property Organisation (WIPO) has estimated that intellectual property will account for six trillion dollars in global trade by 2020, see Xuan-Thao Nguyen, *Collateralizing Intellectual Property*, 42 Ga.L.Rev.1at p.3; WTO mandates norms for trade in intellectual property apart from trade in goods and services in World Trade, and protection of subject matters of intellectual property in TRIPs Agreement as compulsorily Protectable.

⁴*Intellectual Property Financing : An Introduction*, World Intellectual Property Organisation (WIPO) Magazine, Oct, 2008, No. 5, Geneva, p. 2.

⁵The National IPR Policy, 2016, Ministry of Commerce and Industry, Department of Industrial Policy and Promotion, Government of India, p.13.

⁶Professor Louise Guillifer (editor), *Goode on Legal Problems of Credit and Security*, 5th Edn, 2013, Sweet and Maxwell, London p. 77.

on the strength of the apparent ownership. The earliest personal property financing arrangements therefore required actual delivery of the collateral to the creditor. Gradually, various forms of non-possessory security devices were recognized. In those cases a public filing was required as a condition of protecting the creditor against fraudulent conveyance⁷.

The main purposes of perfection are;⁸

- **False wealth:** to publicise the security interest so that unsecured creditors are aware that the debtor's assets are allocated to a particular creditor, thereby reducing the assets available to unsecured creditors.
- **Priorities:** To protect the secured creditor's priority over subsequent purchasers, mortgagers and others dealing with the debtor in respect of the asset, and also to protect these other third parties against unpredictable upsets of their transactions by reason of a prior secret security interest. Priority by publicity therefore protects both secured creditors and market.

A system which is capable of providing information pertaining to prior security creation so as to ensure the priority (in case of enforcement) for prior security right holder, and which is adequate to provide all necessary information as to prior security or any other interest to a party who proposes to deal with the asset concerned, is the most appropriate perfection system. The Objective herein is to survey the existing system(s) of perfection of security interest recognised in India to see its appropriateness for IP secured Financing. The system for perfection of various securities in India is not an integrated single system. There are various arrangements available under different laws. The present system can be examined under the following headings.

- Registration/Filing/Noting with an Authorities under
 - Intellectual Property Statutes.
 - Laws Other Than Intellectual Property Statutes.
- Possession/Control based perfection systems.

PERFECTION OF SECURITY INTEREST UNDER INTELLECTUAL PROPERTY STATUTES

⁷Lorin Brennan, Financing Intellectual Property Under Federal Law: A National Imperative, 23 Hastings Comm. & Ent. L.J. 195, at p. 210.

⁸Philip R Wood, Comparative Law of Security Interests and Title Finance, (2nd ed. 2007), Sweet & Maxwell, London, p.141.

There are only two laws relating to intellectual property that recognise security creation and the consequent filing of security interest with IP authorities. Those are

- Patent Act, 1970
- Designs Act, 2000

Patent Act, 1970

Patent Law provides that there shall be kept at the patent office a register of patents, wherein shall be entered particulars of such other matters affecting the validity or proprietorship of patents as may be prescribed⁹. A mortgage of patent shall not be valid unless the same are in writing and the agreement between the parties concerned is reduced to the form of a document embodying all the terms and conditions governing their rights and obligations and duly executed¹⁰. Where any person becomes entitled as a mortgagee, he shall apply in writing in the prescribed manner to the Controller of Patents for the registration of notice of his interest in the Patent Register. Where an application is made for registration, upon proof of interest in the patent, controller shall enter in the register notice of interest, with particulars of the instrument, if any, creating it. The Controller shall be supplied with, in the prescribed manner, copies of all documents

authenticated to be filed in the patent office¹¹.

The Register of Patents shall at all convenient times be open to inspection by the public; and certified copies of any entry in the register shall be given to any person requiring them on payment of the prescribed fee¹².

Designs Act, 2000

Designs Act provides for compulsory registration of all transactions in designs. A mortgage shall not be valid unless the same are in writing and the agreement between the parties concerned is reduced to the form of an instrument embodying all the terms and conditions governing their rights and obligation and the application for registration under such instrument is filed in the prescribed manner with the Controller within six months from the execution of the instrument or within such further period not exceeding six months in the aggregate as the Controller on application made in the prescribed manner allows. On entry of its particulars in the register, it will have effect from the date of its execution¹³. Application for registration of mortgage is to be made to

⁹The Patent Act, 1970, Section 67(1)(c).

¹⁰*Id*, Section 68.

¹¹*Id*, Section 69; See The Patent Rules, 2003, Rules 90, 91 and 92; see also Form-16.

¹²*Id*, Section 72(1) and (2); If the record of particulars is kept in computer floppies or diskettes or in any other electronic form, public would be deemed to have given access to register if such computer floppies, diskettes or any other electronic form or printouts of such record of particulars is made available for inspection, see *Id*, Section 72(3).

¹³ The Designs Act, 2000, section 30 (3).

the Controller to register interest and the Controller shall, on receipt of such application and on proof to his satisfaction, cause notice of the interest to be entered in the prescribed manner in the register of designs, with particulars of the instrument, if any, creating such interest¹⁴. A document or instrument in respect of which no entry has been made in the register shall not be admitted in evidence in any court in proof of any interest therein, unless the court, for reasons to be recorded in writing, otherwise directs¹⁵. Every register kept under this Act shall at all convenient times be open to the inspection of the public; certified copies of any entry in any such register shall be given to any person requiring the same on payment of the prescribed fee¹⁶.

Both Patent and Designs statute contemplate similar system for perfection – Registration with Controller General. The system is not without drawbacks. The only kind of security interest registerable are ‘mortgage’; however, security interest in IP may not be confined mortgage alone. In addition, statutes relating to two categories of intellectual property only –patent and designs - provide for security interest perfection. It is a realistic possibility that intellectual property secured transactions

may be with respect to a group/cluster of intellectual property items which may include items other than patent and designs. In such a situation security interest in some category of IP alone would be ‘perfectible’. In addition, it is declared in the enactments that the entries in the register would only be prima facie evidence of the matters entered therein. However, it is advantages that as the laws require compulsory registration of all transactions relating to patent and design in that office itself, a person searching for encumbrances (security interest related or any other encumbrances arising out of other transactions like assignment, licensing etc) has the possibility of finding information at the same Office/Authority.

PERFECTION WITH AN AUTHORITY IN LAWS OTHER THAN INTELLECTUAL PROPERTY STATUTES

The registration/filing/noting with authorities as a means of public notice is provided as per the following enactments, which are in addition to IP statutes mentioned above.

- Registration Act, 1908
- The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
- Companies Act, 1956 (and Companies Act, 2013)

¹⁴*Id*, section 30 (2).

¹⁵*Id*, section 30 (5).

¹⁶*Id*, proviso to section 26. See also The Designs Rules, 2001, Rule 38 and 41; and also Rules 32, 33, 34, 35, 36, 37 Forms 10,12 and 13.

- The Depositories Act, 1996
- Insurance Act, 1938

Registration Act, 1908

The purpose of the Registration Act, amongst other things, is to provide a method of public registration of documents so as to give information to people regarding legal rights and obligations arising or affecting property, and to perpetuate documents which may afterwards be of legal importance, and also to prevent fraud¹⁷. Registration Act classifies documents into two categories; compulsorily registerable documents and documents the registration of which is optional. Generally, documents for registration shall be presented for registration within four months from the date of registration¹⁸. A registered document shall operate from the time from which it would have commenced to operate if no registration thereof had been required or made, and not from the time of its registration¹⁹. “Books” of registration of documents and index are maintained at Offices of Registration²⁰. Index contains information relating the names and addresses of all persons executing and of all persons claiming under the document and description of such property sufficient to

identify the same²¹. Books relating to non-testamentary documents and the Indexes relating thereto shall be at all times open to inspection by any person; copies of entries in such books shall be given to all persons applying for such copies²².

A perusal of provisions indicates that the documents which are compulsorily registerable are documents pertaining to immovable property and no other²³. Provisions stipulating the registration of documents which are optional cover documents relating to immovable as well as movable property²⁴; A residual clause in the provision is likely to permit registering documents relating to intangible like intellectual property also²⁵. But, it is important to note that the residual clause provides for documents which are not compulsorily registerable.

²¹*Id*, section 55 read with sections 51 and 21.

²²*Id*, section 57.

²³ See *Id*, section 17. Documents compulsorily registerable are documents pertaining to gift of immovable property; lease of immovable property exceeding one year; non-testamentary instruments which purport or operate to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent, of the value of one hundred rupees and upwards, to or in immovable property or acknowledgement of the aforesaid; or, non-testamentary instruments transferring or assigning any decree or order of a Court or any award when such decree or order or award purports or operates to create, declare, assign, limit or extinguish, whether in present or in future, any right, title or interest, whether vested or contingent, of the value of one hundred rupees and upwards, to or in immovable property.

²⁴See *Id*, section 18.

²⁵See *Id*, clause (f) of section 18 which reads : (f) all other documents not required by section 17 to be registered.

¹⁷Jogi Das and Others v. Fakir Panda, AIR 1970 Ori 22, at pp. 24 and 25.

¹⁸Registration Act, 1908 section 32.

¹⁹*Id*, section 47.

²⁰*Id*, sections 51 and 55.

The Registration Law declares that if a document which is compulsorily registerable is not registered the transaction shall not be valid, and such documents shall not be received as evidence of any transaction affecting such property or conferring any power²⁶. Though system under Registration Act is a public filing system, the provision dealing with compulsory filing does not cover intellectual property²⁷. And so, it cannot be relied on as a public filing system which gives third party notice about the security interest in intellectual property secured transaction. A person is presumed to have notice only when the document relating to the same is compulsorily registerable²⁸. Hence, third party effectiveness and perfection of security right relating to intellectual property cannot be done under the system presently provided by Law relating to Registration.

However, a notable advantage of the system of under Registration Act that since any transaction relating to immovable property are compulsorily registerable, a person searching for encumbrance will be able to

²⁶*Id*, section 49.

²⁷*Id*, section 18 might be interpreted to include and permit intellectual property secured transactions. However, section 18 deals with registration of documents which are optional.

²⁸ See The Transfer of Property Act, 1882, Section 3, Explanation I - Where any transaction relating to immovable property is required by law to be and has been effected by a registered instrument, any person acquiring such property or any part of, or share or interest in, such property **shall be deemed to have notice of such instrument as from the date of registration...** (emphasis added).

get secured right as well as other encumbrances related information in any form (relating to the subject matter covered under Registration Act, i.e. immovable property) with the same authority; the same may be emulated.

The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002(SARFAESI Act)

Central Registry of Securitization Asset Reconstruction and Security Interest of India (CERSAI)²⁹ is to maintain and operate a Registration System for the purpose of registration of transactions of securitization, asset reconstruction of financial assets and creation of security interest over property, as contemplated under SARFAESI Act³⁰.

Following are the key Goals and Objectives of the Central Registry System³¹:

- To provide a mechanism for registration of transaction of securitization and reconstruction of financial Asset and security interest created under SARFAESI Act³².

²⁹Central Registry of Securitization Asset Reconstruction and Security Interest of India (CERSAI) is a company licensed under section 25 of the Companies Act, 1956.

³⁰ As per Chapter IV of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002

³¹See User Manual, CERSAI, Central Registry System, Version 1.2, 08th Jan 2012, Tata Consultancy Services Ltd., p. 5.

³² See SARFAESI Act, 2002,Section 22.

- Create a central data repository for collateral related information.
- To develop a web based system for financial institutions and general public to access this information.
- To enable lenders and other stake holders to get real time current information regarding the collateral being mortgage by borrower.
- To prevent fraudulent transactions arising out of same asset being mortgage with multiple lenders.
- To collect and decimate information regarding the priority and amount secured by the charge on collateral.
- Provide potential buyers of assets with information about any encumbrances on the assets.
- Maintaining history of charges created and satisfied on a particular asset.
- Lenders can access the data on this registry to ascertain whether the same asset has been mortgage with any other institutions.

The Registration would be applicable to transactions of security interest over property (definition of which includes intangibles including intellectual property)³³ created to secure loans and

³³*Id*, Section 2 (1)(t) "property" means--

- (i) immovable property;
- (ii) movable property;
- (iii) any debt or any right to receive payment of money, whether secured or unsecured;

advances from the banks and financial institutions³⁴. As per the SARFAESI Act the particulars of creation of security interest shall be filed, with the Central Registrar, within thirty days of creation of security, by the secured creditor. The Central Registrar may allow the filing of the particulars of such transaction following the expiry of the said period of thirty days, on payment of such additional fee not exceeding ten times the amount of such fee³⁵. The power to condone delay, if the delay is more than 30 days (that is if filing is to be done after 60 days), is with the Central Government³⁶. Central Government is also vested with the power to extend time in respect of modification and satisfaction of security interest. It is further declared that where the Central Government extends time for registration, condoning the delay, such order shall not prejudice any rights acquired in respect of the property before the transaction is actually registered³⁷. Whenever the terms or conditions, or the extent of operation, of any security interest registered are/is modified, it shall be the duty of the secured creditor to send to the Central Registrar, the particulars of such

- (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;** (emphasis added).

³⁴*Id*, Section 2 (1)(m) (c) defines bank" and Section 2 (1)(m) defines "financial institution".

³⁵*Id*, s. 23. see section 26A.

³⁶*Id*, section 26A.

³⁷*Id*, proviso to section 26A.

modification³⁸. CERSAI is a public registry and any person can search and inspect the records maintained by the Registry on payment of fees prescribed³⁹.

It is notable that the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (Central Registry) Amendment Rules, 2016 provides for filing of particulars of creation, modification or satisfaction of security interest in intangible assets, being know how, patent, copyright, trade mark, license, franchise or any other business or commercial right of similar nature in the Central Registry⁴⁰. The same is an important development as far as perfection of security interest in intellectual property in India.

³⁸*Id.*, s. 24.

³⁹*Id.*, s. 26 : Right to inspect particulars of securitisation, reconstruction and security interest Transactions (1) The particulars of securitisation or reconstruction or security interest entered in the Central Register of such transactions kept under section 22 shall be open during the business hours for inspection by any person on payment of such fee as may be prescribed.(2) The Central Register, referred to in sub-section (1) maintained in electronic form, shall also be open during the business hours for the inspection of any person through electronic media on payment of such fee as may be prescribed. Fees are prescribed in the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (Central Registry) Rules, 2011 and the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (Central Registry) (Amendment) Rules, 2013.

⁴⁰The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (Central Registry) Amendment Rules, 2016, Rule 2 C provides that *Particulars of creation, modification or satisfaction of security interest in intangible assets, being knowhow, patent, copyright, trade mark, licence, franchise or any other business or commercial right of similar nature, shall be filed in Form I or Form II, as the case may be, and shall be authenticated by a person specified in the Form for such purpose by use of a valid digital signature.*

However, the following are remarkable in this respect

- CERSAI provides for filing of security interest by Banks and Financial institutions only as applicability of SARFAESI Act is confined to the same. It is not applicable to all the category of lenders⁴¹.
- The issue of multiple filing and related uncertainty is likely to arise. For example a security interest created in respect of patent and design would have to be filed under IP statues (Patent Act and Designs Act), companies Act and CERSAI also. The multiple procedures would create trouble for the subsequent parties as searching with different authorities would be expensive, time consuming and cumbersome.
- It is also remarkable that IP laws (except patent and design law) do not provide for creation of security interest. However, a system for the

⁴¹SARFAESI Act, 2002, Section 2(1)(zd) "secured creditor" means 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, in whose favour security interest is created for due repayment by any borrower of any financial assistance;

perfection is laid in place under SARFAESI Act (CERSAI).

- Issues regarding priority may also arise as SARFAESI Act provides that The provisions of this Act pertaining to the Central Registry (CERSAI) shall be in addition to and not in derogation of any of the provisions contained in the Registration Act, the Companies Act, the Patents Act and the Designs Act or any other law requiring registration of charges and shall not affect the priority of charges or validity thereof under those Acts or laws⁴².
- Further, the consequence of non-filing of a secured transaction with CERSAI is not provided, which may result in non-filing of secured interest under the system.
- A remarkable advantage with the system is that, CERSAI is established to record not only secured transactions, but not transactions other than secured transactions (which a third party

⁴²*Id*, section 20 (4) provides that (4) 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.

who propose to deal with the asset would be interest to know)⁴³.

Companies Act, 2013 (and Companies Act, 1956)

Provisions relating to registration of security/charge in both the above enactments are discussed herein⁴⁴. Under the **Companies Act, 1956** Particulars of the 'charge' ('charge' includes a mortgage⁴⁵) together with the instrument, if any, by which the charge is created or evidenced, or a copy thereof verified in the prescribed manner are to be filed with the Registrar within thirty days after the date of its creation⁴⁶. The law provides for filing of

⁴³*Id*, Section 22 (1)(1) provides: For the purposes of this Act, a record called the Central Register shall be kept at the head office of the Central Registry for entering the particulars of the transactions relating to--

- (a) securitisation of financial assets;
- (b) reconstruction of financial assets; and
- (c) creation of security interest.

⁴⁴The Companies Act, 2013 passed by the Parliament has received the assent of the President of India on 29th August, 2013. The Act consolidates and amends the law relating to companies. The Companies Act, 2013 has been notified in the Official Gazette on 30th August, 2013. Some of the provisions of the Act have been implemented by a notification published on 12th September, 2013. The provisions of Companies Act, 1956 is still in force, See information at <http://www.mca.gov.in/MinistryV2/companiesact.html>.

⁴⁵ Companies Act, 1956, Section 124.

⁴⁶*Id*, Section 125 (1). It is also provided that Registrar may allow registration of charge within thirty days next following the expiry of the initial period of thirty days on payment of such additional fee not exceeding ten times the amount of fee specified in Schedule X as the Registrar may determine, if the company satisfies the Registrar that it had sufficient cause for not filing the particulars and instrument or copy within that period, see proviso to section 125. Central Government is vested with the power to condone delay in filing charge beyond 60 days, see section 141.

charge created in India or outside India of property situated in or outside India⁴⁷.

The following particulars are entered in the register by the Registrar of Companies (ROC)⁴⁸:

- a. the date of creation of charge, and if the charge was a charge existing or property acquired by the company, the date of the acquisition of the property;
- b. the amount secured by the charge ;
- c. short particulars of the property charged ; and
- d. the persons entitled to the charge.

Failure to register will make the charge void against the liquidator and any creditor of the company⁴⁹. Where any charge on any property of a company required to be registered under Act is so registered, any person acquiring such property or any part thereof, or any share or interest therein, shall be deemed to have notice of the charge as from the date of such registration⁵⁰. Nevertheless, it is declared that failure to register charge shall not prejudice any contract or obligation for the repayment of

the money secured by the charge⁵¹. That is to say, failure to register charge will not affect the rights and obligations between the parties to the transaction. Charge registerable with ROC, inter alia, includes a charge on goodwill, on a patent or a licence under a patent, on a trade mark, or on a copyright or a licence under a copyright⁵². The register of companies maintained is open to inspection by any person.

In addition to the above, Companies Act, 1956 provides for Company's Register of Charges⁵³. It is provided that every company shall keep at its registered office, a 'register of charges' and enter therein all charges specifically affecting property of the company, and all floating charges on the undertaking or on any property of the company, giving in each case (i) a short description of the property charged; (ii) the amount of the charge; and (iii) except in the case of securities of bearer, the names of the persons entitled to the charge⁵⁴. The copies of instruments creating charges kept as

⁵¹ See *Id*, Section 125 (2).

⁵² See *Id*, Section 125 (4).

⁵³ See *Id*, Section 130(c).

'Register of Companies' is maintained in Form III prescribed in Companies Regulations, 1956.

Companies Act, 1956 declares that the provisions relating to creation of charge applies to modification of charge also, see See Companies Act, 1956, Section 135. In addition, the Act provides for satisfaction of charge, see, Companies Act, 1956, Section 138, 139 and 141.

⁵⁴See *Id*, Section 143(1). If any officer of the company knowingly omits, or wilfully authorises or permits the omission of, any entry required to be made in Company's Register, he shall be punishable with fine which may extend to five thousand rupees, See Companies Act, 1956, Section 143(2).

⁴⁷*Id*, Section 125(5) and (6).

⁴⁸*Id*, Section 130(1B)(b).

⁴⁹ See *Id*, Section 125 (1).

⁵⁰*Id*, Section 126.

aforementioned, and the register of charges thereof, shall be open during business hours (subject to such reasonable restrictions as the company in general meeting may impose) for inspection by any person at the registered office of the company⁵⁵.

Under the **Companies Act, 2013**⁵⁶, 'charge' is defined to mean an interest or lien created on the property or assets of a company or any of its undertakings or both, as security and includes a mortgage⁵⁷. Though intellectual property has not been expressly mentioned in Companies Act, 2013, it is to be understood to include intellectual property asset also⁵⁸. It is the duty of every company creating a charge within or outside India, on its property or assets or any of its undertakings, whether tangible or otherwise, and situated in or outside India, to register the particulars of the charge signed by the company and the charge-holder together with the instruments, if any, creating such charge in such form, on payment of such

⁵⁵*Id*, Section 144(1) and (2). If inspection of the said copies or register is refused, the company, and every officer of the company who is in default, shall be punishable with fine which may extend to five hundred rupees and with a further fine which may extend to two hundred rupees for every day during which the refusal continues. The *Central Government* may also by order compel an immediate inspection of the said copies or register, See *Id*, Section 144(3) and (4).

⁵⁶Companies Act, 2013, Chapter VI deals with registration of charge and related matters.

⁵⁷*Id*, Section 2 (16).

⁵⁸Companies (Registration of Charges) Rules, 2014, Form No. CHG 1 (entry/column 8), which requires the kind of asset in respect of which charge is created to be mentioned, includes in the list patent, patent licence, copyright, trademark, goodwill and a residuary item to include any other property/asset.

fees and in such manner as may be prescribed, with the Registrar within thirty days of its creation⁵⁹.

Registrar is vested with the power to condone the delay in filing charge. Registrar may, on an application by the company, allow such registration to be made within a period of three hundred days of such creation⁶⁰. Central Government is the authority to consider, if there is a delay to file charge is beyond three hundred days⁶¹. Where any charge on any property or assets of a company or any of its undertakings is registered, any person acquiring such property, assets, undertakings or part thereof or any share or interest therein shall be deemed to have notice of the charge from the date of such registration⁶². It is declared that any subsequent registration of a charge shall not prejudice any right

⁵⁹See *Id*, section 77(1).

Where a company fails to register the charge within the period specified, the person in whose favour the charge is created may apply to the Registrar for registration of the charge along with the instrument created for the charge, within such time and in such form and manner as may be prescribed and the Registrar may, on such application, within a period of fourteen days after giving notice to the company, unless the company itself registers the charge or shows sufficient cause why such charge should not be registered, see Companies Act, 2013, section 78.

The provisions relating to registration of charges shall, so far as may be, apply to (a) a company acquiring any property subject to a charge within the meaning of that section; or (b) any modification in the terms or conditions or the extent or operation of any charge registered under that section, see Companies Act, 2013, sections 82, 83 and 87 deal with satisfaction and registration of satisfaction of charge.

⁶⁰See *Id*, section 77(1).

⁶¹See *Id*, section 87.

⁶²See *Id*, section 80.

acquired in respect of any property before the charge is actually registered⁶³.

Similar to Companies Act, 1956 if a charge created in is not registered with the Registrar, such charge shall not be taken into account by the liquidator or any other creditor⁶⁴. However, failure to register shall not prejudice any contract or obligation for the repayment of the money secured by a charge and valid between the parties thereof⁶⁵. Register maintained by the registrar of Companies shall be open to inspection by any person on payment of such fees as may be prescribed for each inspection⁶⁶.

In addition to the registration if charge with the Registrar of Companies, Companies Act, 2013 provides that every company shall keep at its registered office a Register of Charges and entered therein all charges and floating charges affecting any property or assets of the company or any of its undertakings. Copy of the instrument creating the charge is kept at the registered office of the company along with the register of charges⁶⁷. The register of charges and instrument of charges kept by company

⁶³See *Id*, section 77(1)(third proviso)

⁶⁴See *Id*, section 77(3).

⁶⁵See *Id*, section 77(4).

⁶⁶See *Id*, section 81.

The particulars of charges maintained on the Ministry of Corporate Affairs portal www.mca.gov.in/MCA21 are deemed to be the register of charges for the purposes of the Act, see Companies (Registration of Charges) Rules, 2014, Rule 7.

⁶⁷See *Id*, section 85(1).

is open for inspection during business hours by any member or creditor without any payment of fees; or by any other person on payment of such fees as may be prescribed, subject to such reasonable restrictions as the company may, by its articles, impose⁶⁸.

In addition to companies' Charge, charges created by Limited Liability partnerships (LLPs) can also be filed with Registrar of Companies. Among the assets in respect which charge can be created and filed include Patent, License under Patent, Copyright, License under Copyright, Trademark, Goodwill and any other property⁶⁹. However, notably, it is not mandatory to file the charge details with the office of Registrar, but the stakeholders can voluntarily file the same⁷⁰.

A critical view at the system of registration of charge under Company Statutes indicate that the system is not adequate to operate as a public filing mechanism to ensure third party effectiveness or perfection in the case

⁶⁸See *Id*, section 85(2).

If any company contravenes the provisions relating to maintenance of company's register of charges, the company shall be punishable with fine which shall not be less than one lakh rupees but which may extend to ten lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to six months or with fine which shall not be less than twenty-five thousand rupees but which may extend to one lakh rupees, or with both, see Companies Act, 2013, section 86.s

⁶⁹See the Limited Liability Partnership Rules, 2009, Form 8, column/entry 3. The same is part of a statement of Accounts and Solvency as per Rule 24.

⁷⁰See the website of Ministry of Corporate Affairs http://www.mca.gov.in/LLP/llp_eFiling_faq_02.html.

of IP secured transactions. The most important drawback is that the system under the Company Statutes, apparently, limited to filing of charge in respect of two sets of potential borrowers (charge creators) only. That is, against company and LLPs only; charge created in respect of other parties like individuals, sole proprietorships, partnerships and Hindu Undivided Families (Joint Families) cannot be filed with ROC. The Register Companies maintained at the Registered Office of the companies also has the same drawback that only company charges are entered therein.

Even in respect of those borrowers covered, the system is not found to be without drawbacks. Even though in respect of companies, it is an effective system, in the case of Limited Liability Partnerships (LLPs) filing of charge is optional, and for the very reason cannot be relied on as a perfection system giving notice to the third parties.

Security in Securities⁷¹ Held in Depository

⁷¹The Securities Contract (Contracts) Regulation Act, 1956, Section 2 (h) 'securities' include—

(i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable

securities of a like nature in or of any incorporated company or other body corporate;

(ia) derivative

(ib) units or any other instrument issued by any collective investment scheme to the investors in such schemes;

(ic) security receipt as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;

The Depositories Act, 1996 provides for pledge or hypothecation of securities held in Depository. The same is discussed herein considering the fact that securities in demat form has similarities with IP assets; notably it is in an intangible form. The Securities held in a depository account can be pledged/hypothecated to avail loan/credit facility. Pledge of securities in NSDL depository requires that both the borrower (pledgor) and the lender (pledgee) should have account in NSDL depository. A beneficial owner of a securities held in a depository may with the previous approval of the depository create a pledge or hypothecation in respect of a security owned by him through a depository⁷². Every beneficial owner shall give intimation of such pledge or hypothecation to the depository and such depository shall thereupon make entries in its records accordingly⁷³. Any entry in the records of a depository shall be evidence of a pledge or hypothecation⁷⁴.

(id) units or any other such instrument issued to the investors under any mutual fund scheme;

(ii) Government securities;

(iia) such other instruments as may be declared by the Central Government to be securities; and

(iii) rights or interest in securities.

⁷²The Depositories Act, 1996, section 12 (1). The Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996, Regulation 58 deals with pledge/hypothecation of shares. Bye-Law 9.9 deals with Pledge and hypothecation; Business Rule 12.9 deals with Pledge; and Business Rule 12.10 deals with Hypothecation of securities.

⁷³The Depositories Act, 1996, section 12 (2).

⁷⁴*Id*, section 12 (3).

The pledgor would submit an instruction to its DP (Depository Participant) to initiate a pledge/hypothecation request in the DPM (software provided by NSDL to the DP). The pledgor will indicate therein, the agreement number, closure date of the pledge/hypothecation (this date is indicative of the duration of pledge/hypothecation), pledgee's details, and the details of securities to be pledged. The DP will enter the details of the request in the DPM, generate a pledge/hypothecation instruction number for the request and release the request to NSDL. The securities pledged are moved from 'Free Balances' to 'Pledged Balances' account. Thus the securities pledged will not be available to pledgor for any other purpose. The details of the pledge/hypothecation are electronically communicated to the DPM of pledgee's DP through the DM for confirmation⁷⁵.

Procedure for confirmation of creation of pledge/hypothecation by the pledgor is that the pledge/hypothecation request will be displayed on the DPM of pledgee's DP. The pledgee's DP will furnish the details of the pledge/hypothecation requests received for confirmation to the pledgor through the report generated by the DPM. The acceptance/rejection of pledge/hypothecation confirmation is electronically communicated to the DPM of

the pledgor's DP through DM. Acceptance of the creation of pledge/hypothecation will appear in the DPM of the pledgor's DP and pledgee's DP as a status change. Status of the pledge/hypothecation instruction will change as 'Pledged'⁷⁶.

Apparently, the security interest covered under the Depositories Act, 1996 is only securities and not Intellectual Property. However, subject matter therein has similarity with IP (intangible nature). Therefore, such system and its working might throw light on a system that is appropriate for IP. It can also be seen that the system is structured keeping in view the nature of asset and the needs of the parties and commerce, which indicates an appropriate system for IP should consider the nature of IP assets and needs of parties thereto. Further, it is to be found that when the importance of the asset is recognised in a jurisdiction/industry and the commerce reckons the value thereof (be it securities/share etc or intellectual property), there needs to be a system put in place to track the transactions (including security transactions) relating to the same.

Security Right in Insurance Policy

A security right is created in insurance policy by way of assignment as per the provisions of the Insurance Act, 1938. The notable

⁷⁵ See information at website of National Securities Depository Limited (NSDL) <https://nsdl.co.in/value/pledge.php>.

⁷⁶ See information at website of National Securities Depository Limited (NSDL) <https://nsdl.co.in/value/pledge.php>.

feature of insurance transaction, i.e., intangible form, prompted discussion of such transaction herein. A transfer or assignment of a policy of life insurance, whether with or without consideration, may be made only by an endorsement upon the policy itself or by a separate instrument, signed in either case by the transferor or by the assignor or his duly authorised agent and attested by at least one witness, specifically setting forth the fact of transfer or assignment⁷⁷. The transfer or assignment in favour of the insurer shall not be operative as against an Insurer and shall not confer upon the transferee or assignee, or his legal representative, any right to sue for the amount of such policy or the moneys secured thereby until a notice in writing of the transfer or assignment if and either the said endorsement or instrument itself or a copy thereof certified to be correct by both transferor and transferee or their duly authorised agents have been delivered to the insurer⁷⁸. Subject to the terms and conditions of the transfer or assignment, the insurer shall, from the date of the receipt of the aforementioned notice, recognise the transferee or assignee named in the notice as the only person entitled to benefit under the policy, and such person shall subject to all

liabilities and equities to which the transferor or assignor was subject at the date of the transfer or assignment and may institute any proceedings in relation to the policy without obtaining the consent of the transferor or assignor or making him a party to such proceedings⁷⁹.

The date on which aforementioned notice is delivered to the insurer shall regulate the priority of all claims under a transfer or assignment as between persons interested in the policy: and where there is more than one instrument of transfer or assignment, the priority of the claims under such instruments shall be governed by the order in which the notices are delivered⁸⁰. Upon the receipt of the notice, the insurer shall record the fact of such transfer or assignment together with the date thereof and the name of the transferee or the assignee and shall, on the request of the person by whom the notice was given, or of the transferee or assignee, on payment of a fee not exceeding one rupee, grant a written acknowledgment of the receipt of such notice; and any such acknowledgment shall be conclusive evidence against the insurer that he has duly received the notice to which such acknowledgment relates⁸¹. Once the

⁷⁷The Insurance Act, 1938, section 38 (1).

⁷⁸The Insurance Act, 1938, section 38 (2); Where the insurer maintains one or more places of business in India, such notice shall be delivered only at the place in India mentioned in the policy for the purpose or at his principal place of business in India, see proviso to section 38 (2).

⁷⁹*Id*, section 38 (5).

⁸⁰*Id*, section 38 (3).

⁸¹*Id*, section 38 (4); Notwithstanding any law or custom having the force of law to the contrary, and assignment in favour of a person made with the condition that it shall be inoperative or that the interest shall pass to some other person on the

credit amount is repaid the assignment is cancelled.

Apparently, the security interest covered under the Insurance Act, 1938 is only security in respect of an insurance claim and not Intellectual Property. However, the subject matter covered by the system has similarity with IP; that is, subject matter of security is a claim for a benefit under insurance policy is intangible. Such system and its working might throw light on a system that is appropriate for IP. The noting system with the insurer is wrought keeping in sight the nature of asset and the needs of the parties to the transaction and the interest of person who might deal with it, which throws useful light when considering a system for IP assets.

PERFECTION BY POSSESSION/DEPOSIT OF DOCUMENTS OF TITLE

In addition to the system of registration/filing/noting with an authority to perfect security interest, the laws in India also provide for possession/control method of perfection of security interest. Such a mode of perfection are recognised in The Indian Contract Act, 1872; The Negotiable Instrument Act, 1881; The

happening of a specified event during the lifetime of the person whose life is insured, and an assignment in favour of the survivor or survivors of a number of persons shall be valid, The Insurance Act, 1938, section 38 (7).

Transfer of Property Act, 1882; Deposit of Document of Title to Goods; and Deposit of Securities Certificates.

It can be found that under the Indian Contract, 1872 (pledge of goods) and under the Negotiable Instruments Act, 1881 (security of Negotiable Instruments) security of those subject matters are perfected by (transfer of) possession; therefore the same cannot be appropriate for IP.

Deposit of title deed/document is the mode of perfection for Equitable Mortgage under the Transfer of Property Act, 1882; for creating security by deposit of document of title to goods; and when share certificate can pledged. System based on deposit of title deeds/documents are not appropriate to intellectual property perfection since some of the major intellectual property assets are not compulsorily registerable; moreover, even though they are registerable, the certificates of registration cannot be equated with title deeds⁸².

⁸²Copyright is not compulsorily registerable; There can be unregistered Trademarks and Geographical Indications as common law remedy of passing off for the protection unregistered subject matters therein legally recognised; There is no statutory law for trade secrets in India; there are no adequate and comprehensive case laws so as to constitute common law regarding trade secrets. Hence, no title deeds nor even certificates of registration may not be available in the case of copyright, trademark, geographical indications and trade secrets.

Though, Patent, Designs, Plant Varieties and Semiconductor Integrated Layout Designs are compulsorily registerable, certificates of registration are (only) prima facie evidence of the

As far as the system of perfection based on possession and control are concerned, intellectual property has fundamental difficulty to be covered by such systems. Intellectual property, being intangible in nature cannot be physically possessed. Similarly, as intellectual property does not have title document system, such a system is also not appropriate in secured transactions in IP. Hence, third party effectiveness in intellectual property secured transaction cannot be done under a system based on deposit of title deeds also.

CONCLUSION

On consideration of various systems for perfection of security interest presently available in India, it can be found that these systems are not enough to cover perfection in intellectual property secured transaction. Registration system under Registration Act, 1908 does not provide for compulsory registration of secured transaction in intellectual property. The CERSAI system put in place as per the provisions of The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 provides for filing of security interest in IP. However, issues of coverage of certain categories lenders, multiple filing and priority, arise.

ownership/proprietorship and not equivalent of title deeds; see The Patent Act, 1970, s. 72; The Designs Act, 2000, s. 10; The Plant Varieties and Farmers' Rights Act, 2001, s. 82; The Semiconductor Integrated Layout Designs Act, 2000, s. 19.

Even though the provisions of Company statutes provides for registration of charge including charge in respect of intellectual property, it has in its ambit the companies and LLPs only; it does not have a system for filing when the borrower is other than company and LLP- like individual, sole proprietor, partnership or Hindu Joint Family. Remarkably, the registration of charge of LLPs is only optional and hence cannot act as system for third party effectiveness. The systems for noting pledge/hypothecation of shares etc. and Insurance policy under the relevant laws cover only those subject matters, though it conveys the important idea that the nature of asset to be covered and the needs of parties shall be guiding factors while structuring a system for regulating transactions in a particular category of assets. Therefore, there is need for reform of present law on perfection of security interest in India to do away the imperfections of perfection system, so as to facilitate IP secured financing.