FACULTY OF JURIDICAL SCIENCES

COURSE NAME : BALLB/BBALLB

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Banking hypothecation

Hypothecation Meaning

Hypothecation means offering an asset as collateral security to the lender. Herein, the ownership lies with a lender and the borrower enjoys the possession. In the case of default by the borrower, the lender can exercise his ownership rights to seize the asset.

It is usually done in a case of movable assets, for creating the charge against collateral for the loan given. Under hypothecation, the possession of the security remains with the borrower itself. Hence, if the borrower defaults on payments, the lender would have to first take possession of the security (asset under hypothecation) and then sell the asset to recover dues.

Example of Hypothecation

In the case of vehicle loans, the vehicle remains with the borrower but the same is hypothecated to the bank/ financer. If there is any default by the borrower, the bank takes possession of the vehicle after giving notice and then sells the same. The loan account is credited with the sales proceeds of the asset to recover the dues towards the principal amount and interest amount. Any balance left thereafter shall be given back to the borrower. Apart from vehicles, hypothecation can be done for stocks and bills receivables.

Though pledge seems similar to hypothecation as both are types of charge created on movable assets; there lie some differences between pledge, hypothecation, and mortgage. Let us look at the differences to get a better idea of these terms.

Pledge V/s Hypothecation

The possession of the asset remains with the lender in case of a pledge; while it remains with the borrower in case of hypothecation. Common examples include the gold loan in case of pledge and vehicle loan in case of hypothecation.

Alternate Asset for Hypothecation

It can also be done for investments/stocks. This is a common practice in stock trading, better known as, margin lending. In such a case, the buyer, buying shares on margin, places his existing shares as collateral with the brokerage firm. These shares can be sold by the brokerage firm if the buyer faces the margin call. A margin call is received when the value of securities bought decreases more than a certain limit or the account value reduces beyond a certain limit.

Documentation

This activity usually requires an agreement to be made and is known as the hypothecation deed.

The hypothecation deed is an agreement which contains standard features and rules; which usually cover the following points: Definitions, Insurance [to ensure good condition of the asset], Inspection rules [giving lender the right to inspect the asset as per agreed terms], rights and remedies of each party [in case of any default], security details marked for hypothecation, sale realizations, insurance proceeds, liability of each party, jurisdiction prevailing, marking of the assets etc. This deed protects the rights of both the parties to the contract.[adsense_bottom]

MCQs

1. We should keep our savings with banks because

a) It is safe

b) Earns interest

c) Can be withdrawn anytime

d) All of above

2. Bank does not give loan against

a) Gold Ornaments

b) LIC policy

c) Lottery ticket

d) NSC

3. Bank having maximum number of branches in India

a) Reserve Bank of India

b) State Bank of India

c) Punjab National Bank

d) Bank of Baroda

4. 100/- Rupee note is signed by

a) Prime Minister

b) Finance Minister

c) RBI Governor

d) None of above

5. ATM password should be kept in

a) Personal diary

b) Office diary

c) Memory

d) All of above