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CENTRAL BANK OF INDIA

v.

SIRIGUPPA SUGARS & CHEMICALS LTD. & ORS.

AUGUST 7, 2007

B

[TARUN CHATTERJEE AND P.K. BALASUBRAMANYAN, JJ.]

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*Contract Act, 1872—Sections 173 and 176—Rights of pawnee on sale proceeds of pawned goods—Sugar Company obtained loan from Bank-pawnee by pledging stocks of sugar and loan not repaid—Interim order by High Court directing disbursal of certain amounts realised on sale proceeds for satisfying claim of cane growers and employees of the Company—Interference with—Held: Pawnee has right to retain goods pledged for payment of debt including interest on debt and all necessary expenses incurred by it—Rights of the bank as pawnee over pawned sugar prevailed over the claims of cane growers and workmen, who were only unsecured creditors since no liquidation of the Company had taken place—Thus, interim order set aside—Bank entitled to the amount in satisfaction of its debt and surplus, if any be disbursed to unsecured creditors.*

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*Interim order: Interim order by High Court—When final adjudication to be made in writ appeal pending before it—Interim order resulting in serious prejudice to the parties—Propriety of—Held: Not proper.*

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**First respondent-company secured loan from the appellant-bank by pledging its stock of sugar with the appellant-bank. The Company did not pay dues of the sugarcane growers who supplied them sugarcane and also of the workmen of the Company. Aggrieved, parties initiated recovery proceedings. Labour Commissioner passed an order against the respondent company in respect of dues to the workmen. Cane Commissioner passed orders against the respondent company in respect of dues to the sugarcane growers. Respondent company filed writ petition challenging the recovery proceedings. The first respondent company had not repaid the loan amount to the appellant-bank. During pendency of the writ petition, the Recovery Authority took possession of stock of sugar lying pledged to the appellant-bank and under its control, forcibly and without reference to the appellant-bank. Taking into consideration that the sugar stock was liable to lose its value by being stored**

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indefinitely, the court directed sale of sugar. Out of the sale price fetched, A  
part of the sum was paid towards excise duty and the balance was held under  
the orders of court. Writ petition was dismissed. First respondent Company  
then filed an appeal. High Court passed an interim order directing  
disbursement of certain amounts realized on sale of stocks of sugar, owned  
by respondent company under pledge by appellant-bank, to the employees of  
the company, to the sugarcane cultivators and to the appellant-bank. Hence B  
the present appeal.

Appellant-bank contended that the High Court erred in ignoring the  
rights of the appellant as a pawnee to the proceeds of the sale of the goods  
pledged to it to secure a debt due from the borrower; that the bank as pawnee C  
had the first charge on the stock of sugar over the debts due to other  
unsecured creditors and the charge crystallised when the stock of sugar  
pledged with it was sold; that in the absence of any winding up proceeding the  
workmen had no preferential rights and their status, was that of unsecured  
creditors; that neither the Cane growers nor the workmen were secured  
creditors; and that by passing such an interim order the Division Bench had D  
seriously prejudiced the rights of parties which remain to be determined in  
the writ appeal itself and such an interim order ought not to have been passed.

Respondent-Company contended that the amounts due to the sugarcane  
growers and to the workmen had to be provided for and as such there is no  
reason to interfere with the interim order passed by the Division Bench of E  
the High Court.

Allowing the appeals, the Court

HELD: 1.1. Under section 173 of the Contract Act, a pawnee has the  
right to retain the goods pledged for payment of the debt including interest F  
on the debt and all necessary expenses incurred by the pawnee in respect of  
the possession or for the preservation of the goods pledged.

[Para 6] [903-C-D]

1.2. The rights of the appellant-bank over the pawned sugar had  
precedence over the claims of the Cane Commissioner and that of the  
workmen. Therefore, the High Court was in error in passing an interim order  
to pay parts of the proceeds to the Cane Commissioner and to the Labour  
Commissioner for disbursal to the cane growers and to the employees. There  
is no dispute that the sugar was pledged with the appellant bank for securing  
a loan of the first respondent and the loan had not been repaid. The goods H

- A were forcibly taken possession of at the instance of the revenue recovery authority from the custody of the pawnee, the appellant-bank. In view of the fact that the goods were validly pawned to the appellant bank, the rights of the appellant-bank as pawnee cannot be affected by the orders of the Cane Commissioner or the demands made by him or the demands made on behalf of the workmen. Both the Cane Commissioner and the workmen in the absence of a liquidation, stand only as unsecured creditors and their rights cannot prevail over the rights of the pawnee of the goods.

[Para 18] [907-G-H; 908-A-B]

- C 1.3. Pending the writ appeals, the High Court ought not to have passed such an interim order of consequence. Therefore, the order of the High Court cannot be sustained and calls for interference. [Para 19] [908-C-D]

- D 1.4. The impugned order of High Court directing payment out of parts of the sale proceeds to the Labour Commissioner and to the Cane Commissioner is set aside. Appellant as the pawnee is entitled to the amount in satisfaction of its debt to secure which, the goods had been pawned and to appropriate the sale proceeds towards the debt due and only if there is surplus, to make it available for disbursement to the Cane Commissioner and to the Labour Commissioner. [Para 20] [908-D-E]

- E *Workers of M/s Rohtas Industries Ltd. v. M/s Rohtas Industries Ltd.*, [1987] 2 SCC 588; *State of M.P. v. Jaura Sugar Mills Ltd. and Ors.*, [1997] 9 SCC 207; *Textile Labour Association and Anr. v. Official Liquidator and Anr.*, [2004] 9 SCC 741 and *Rajasthan State Financial Corporation and Anr. v. Official Liquidator and Anr.*, [2005] 8 SCC 190, distinguished.

- F *Lallan Prasad v. Rahmat Ali and Anr.*, [1967] 2 SCR 233; *Bank of Bihar v. State of Bihar and Ors.*, [1971] Suppl. SCR 299; *Karnataka Pawnbroker's Association and Ors. v. State of Karnataka and Ors.*, [1998] 7 SCC 707; *Dena Bank v. Bhikhabhai Prabhudas Parekh and Co. and Ors.*, [2000] 5 SCC 694; *O. Konavalov v. Commander, Coast Guard Region and Ors.*, [2006] 4 SCC 620 and *Workers of M/s Rohtas Industries Ltd. v. M/s Rohtas Industries Ltd.*, [1987] Suppl. SCC 462, referred to.

*The Law of Mortgages by Edward F. Cousins*, referred to.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 3499-3500 of 2007.

From the Judgment & Order dated 3.12.2003 of the High Court of A  
Karnataka at Bangalore in Writ Appeal No. 7746 of 2001 and Writ Appeal No.  
1722 of 2003.

Jaideep Gupta, Dinesh Mathur, Gopa Talukdar and Rameshwar Prasad  
Goyal for the Appellant.

R. Mohan, ASG Sanjay R. Hegde, P. Narasimhan, B.K. Prasad, P.  
Parmeswaran and Vipin Gupta for the Respondents. B

The Judgment of the Court was delivered by

**P.K. BALASUBRAMANYAN, J.** Leave granted. C

1. These appeals challenge the interim order passed by the Division  
Bench of the High Court in a pending writ appeal, directing disbursement of  
certain amounts realised on sale of stocks of sugar, owned by the first  
respondent - company held under pledge by the appellant--bank. The Labour  
Commissioner had passed an order under Section 33(c) of the Industrial D  
Disputes Act against the first respondent company in respect of the dues to  
the workmen. The same was challenged by the first respondent in the writ  
petition as also by others. Similarly the Cane Commissioner had passed  
orders for recovery of amounts due from the first respondent-company for  
being paid to the sugarcane growers for the cane supplied by them to the first  
respondent-company. During the pendency of the writ petition, the recovery E  
authority had taken possession of stock of sugar lying pledged to the  
appellant-bank and under its control, forcibly and without reference to the  
appellant-bank. The appellant-bank had got itself impleaded in the writ  
petition. Considering that the sugar stock was liable to lose its value by  
being stored indefinitely, the court had directed sale of the sugar. The sale F  
fetched a price of Rs.1,53,50,400/-. Out of the same, a sum of Rs.10,60,800/  
- was paid towards excise duty and the balance was held under orders of  
court.

2. The writ petition filed by the first respondent challenging the recovery  
proceedings, both at the instance of the Labour Commissioner and the Cane G  
Commissioner was dismissed by the learned Single Judge. The decision of  
the learned Single Judge was challenged in appeal. In the appeal filed by the  
company, the impugned interim order was made directing that a sum of  
Rs.43,00,000/- be made available to the Labour Commissioner for disbursement  
to the employees of the company, a sum of Rs.60,00,000/- be made available H

A to the Cane Commissioner for disbursal to the sugarcane cultivators who had supplied sugarcane and a sum of Rs.20,00,000/- be paid to the appellant--bank, subject to the bank obtaining sanction from the Board for Industrial and Financial Reconstruction (for short "BIFR") and that the balance shall be kept in a fixed deposit subject to final orders. The appellant bank has challenged this order on the ground that its right as a pawnee, well recognised by law, had been totally ignored by the Division Bench of the High Court. Consequently, the order is clearly illegal and that such an interim order ought not to have been passed when the final adjudication had to be made in the appeals that were pending before the High Court.

C 3. We may notice here that there are no proceedings for winding up of the first respondent-company under the Companies Act. The first respondent-company has only approached BIFR by way of reference under Section 15(1) of the Sick Industrial Companies (Special Provisions) Act.

D 4. Learned counsel for the appellant--bank submitted that the High Court was clearly in error in ignoring the rights of the appellant as a pawnee and in ignoring the binding decisions of this Court on the rights of the pawnee to the proceeds of the sale of the goods pledged to it to secure a debt due from the borrower. According to him, the bank as pawnee has the first charge on the stock of sugar and the charge crystallised when the stock of sugar pledged with it was sold. When it has thus crystallised, the bank had a priority over the debts due to other unsecured creditors. Neither the Cane Commissioner, nor the Labour Commissioner, in this case or the workmen, on whose behalf he was acting, were secured creditors. Consequently, the right of the appellant as the pawnee must prevail. Counsel submitted that the workmen become secured creditors only when there is a winding up and it is Section 529 of the Companies Act that made them secured creditors, entitled to disbursement *pari passu* with other secured creditors. In the absence of any winding up proceeding the workmen had no preferential rights and their status, at best, was that of unsecured creditors. Counsel further submitted that by passing such an interim order the Division Bench had seriously prejudiced the rights of parties which remain to be determined in the appeal itself and such an interim order ought not to have been passed.

H 5. On behalf of the respondents, it was contended that the amounts due to the sugarcane growers and to the workmen had to be provided for and going by some of the decisions of this Court, the workmen's dues could not be ignored and under the circumstances, there is no reason to interfere with

the interim order passed by the Division Bench of the High Court. Additional A  
Solicitor General also submitted that the question whether sales tax dues or  
the dues under a certificate issued by the Debt Recovery Tribunal had  
priority, had been referred to a larger Bench for a decision. It was submitted  
that the decision in *State of M.P. v. Jaura Sugar Mills Ltd. And Ors.*, [1997]  
9 SCC 207 will apply here. On behalf of the State it was submitted that the B  
decision in *State of M.P.'s case (supra)* held the field and the order of the  
Division Bench was supportable in the light of that decision.

6. The right of the lender, or pledgee, is to retain the chattle until a  
proper tender of the amount due is made. (See The Law of Mortgages by  
Edward F. Cousins) Under Section 173 of the Contract Act, a pawnee has C  
the right to retain the goods pledged for payment of the debt including  
interest on the debt and all necessary expenses incurred by the pawnee in  
respect of the possession or for the preservation of the goods pledged. The  
rights of the pawnee were summed up by this Court in *Lallan Prasad v.*  
*Rahmat Ali and Anr.*, [1967] 2 SCR 233 at 239 thus:

“There is no difference between the common law of England and the D  
law with regard to pledge as codified in sections 172 to 176 of the  
Contract Act. Under Section 172 a pledge is a bailment of the goods  
as security for payment of a debt or performance of a promise. Section  
173 entitles a pawnee to retain the goods pledged as security for E  
payment of a debt and under Section 175 he is entitled to receive from  
the pawner any extraordinary expenses he incurs for the preservation  
of the goods pledged with him. Section 176 deals with the rights of  
a pawnee and provides that in case of default by the pawner the  
pawnee has (1) the right to sue upon the debt and to retain the goods  
as collateral security and (2) to sell the goods after reasonable notice F  
of the intended sale to the pawner. Once the pawnee by virtue of his  
right under Section 176 sells the goods the right of the pawner to  
redeem them is of course extinguished. But as aforesaid the pawnee  
is bound to apply the sale proceeds towards satisfaction of the debt  
and pay the surplus, if any, to the pawner.”

7. In the *Bank of Bihar v. State of Bihar and Ors.*, [1971] Suppl. SCR G  
299 the law is set down thus:

“According to the Statement in Halsbury's Laws of England "pawn"  
has been described as a security where by contract a deposit of  
goods is made a security for a debt and the right to the property vests H

- A in the pledgee so far as is necessary to secure the debt; in this sense it is intermediate between a simple lien and a mortgage which wholly passed the property in the things conveyed. "The pawnee has a special property or special interest in the thing pledged, while the general property therein continues in the owner. That special property or interest exists so that the pawnee can compel payment of the debt or can sell the goods when the right to do so arises. This special property or interest is to be distinguished from the mere right of detention which the holder of a lien possesses, in that it is transferable in the sense that a pawnee may assign or pledge his special property or interest in the goods." "Where judgment has been obtained against the pawnor of goods and execution has issued thereon, the sheriff cannot seize the goods pawned unless he satisfied the claim of the panwee". (based mainly on *Rogers v. Kennay* (1846 (9) Q.B. 592). "On the bankruptcy of the pawnor the pawnee is a secured creditor in the bankruptcy with respect to things pledged before the date of the receiving order and without notice of a prior available act of bankruptcy". (Halsbury's Laws of England 3rd Edn. Vol.29 p.222) It has not been shown how the law in India is in any way different from the English law relating to the rights of the pawnee vis-à-vis other unsecured creditors of the pawnor."
- B
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- D
- E In our judgment the High Court is in error in considering that the rights of the pawnee who had parted with money in favour of the pawnor on the security of the goods can be defeated by the goods being lawfully seized by the Government and the money being made available to other creditors of the pawnor without the claim of the pawnee being fully satisfied. The pawnee has special property and a lien which is not of ordinary nature on the goods and so long as his claim is not satisfied no other creditor of the pawnor has any right to take away the goods or its price. After the goods had been seized by the Government it was bound to pay the amount due to the plaintiff and the balance could have been made available to satisfy the claim of other creditors of the pawnor. But by a mere act of lawful seizure the Government could not deprive the plaintiff of the amount which was secured by the pledge of the goods to it. As the act of the Govenrment resulted in deprivation of the amount to which the plaintiff was entitled it was bound to reimburse the plaintiff for such amount which the plaintiff in ordinary course would have realized by sale of goods pledged with it on the pawnor making a default in
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payment of debt.

The approach of the trial court was unexceptionable. The plaintiff's right as a pawnee could not be extinguished by the seizure of the goods in its possession inasmuch as the pledge of the goods was not meant to replace the liability under the cash credit agreement. It was intended to give the plaintiff a primary right to sell the goods in satisfaction of the liability of the pawnor. *The Cane Commissioner who was an unsecured creditor could not have any higher rights than the pawnor and was entitled only to the surplus money after satisfaction of the plaintiff's dues.*" (emphasis supplied)

8. It has to be noticed that the Cane Commissioner was held to be an unsecured creditor, he could not have any higher right than the pawnor and was entitled only to the surplus money after satisfaction of the pawnee's dues.

9. In *Karnataka Pawnbroker's Association and Ors. v. State of Karnataka and Ors.*, [1998] 7 SCC 707 this Court summed up the position as under:

"It cannot be and it is not disputed that the pawnbroker has special property rights in the goods pledged, a right higher than a mere right of detention of goods but a right lesser than general property right in the goods. To put it differently, the pawnor at the time of the pledge not only transfers to the pawnee, the special right in the pledge but also passes on his right to transfer the general property right in the pledge in the event of the pledge remaining unredeemed resulting in the sale of the pledge by public auction through an approved auctioneer. The position being what is stated above, the natural consequence will be that it is the pawnee who holds not only the absolute special property right in the pledge but also the conditional general property interest in the pledge, the condition being that he can pass on that general property only in the event of the pledge being brought to sale by public auction in accordance with the Act and the Rules framed thereunder."

10. The Act there referred was the Karnataka Sales Tax Act and the question that fell for decision was whether the pawnee, the pawnbroker, on sale could be considered to be a dealer, liable to pay sales tax under the Sales Tax Act.



- A 11. In *Dena Bank v. Bhikhabhai Prabhudas Parekh & Co. and Ors.*, [2000] 5 SCC 694 the position was reiterated in the following words:

B “However, the Crown's preferential right to recovery of debt over  
C other creditors is confined to ordinary or unsecured creditors. The  
common law of England or the principles of equity and good conscience  
(as applicable to India) do not accord the Crown a preferential right  
D for recovery of its debts over a mortgagee or pledgee of goods or a  
secured creditor. It is only in cases where the Crown's right and that  
of the subject meet at one and the same time that the Crown is in  
general preferred. Where the right of the subject is complete and  
perfect before that of the King commences, the rule does not apply,  
E for there is no point of time at which the two rights are at conflict,  
nor can there be a question which of the two ought to prevail in a  
case where one, that of the subject, has prevailed already. In *Giles  
v. Grover*, (1832 (131) ER 563 : 9 Bing 128) it has been held that the  
Crown has no precedence over a pledgee of goods. In *Bank of Bihar  
v. State of Bihar* (supra) the principle has been recognised by this  
Court holding that the rights of the pawnee who has parted with  
money in favour of the pawnor on the security of the goods cannot  
be extinguished even by lawful seizure of goods by making money  
available to other creditors of the pawnor without the claim of the  
pawnee being first fully satisfied. Rashbehary Ghose states in *Law  
of Mortgages* (Tagore Law Lectures, 7th Edn. P. 386) - “It seems a  
government debt in India is not entitled to precedence over a prior  
secured debt.”

- F 12. It may be noted that even the Crown's preferential right or a Crown  
debt was held to be subservient to the rights of a pawnee.

13. In *O. Konavalov v. Commander, Coast Guard Region and Ors.*, [2006] 4 SCC 620 this Court held that the lien of a pawnee traceable to Sections 172, 173 and 176 of the Contract Act is capable of satisfaction from property in the hands of the Government obtained even by lawful seizure.  
G This Court followed the views expressed in the decision in *Bank of Bihar v. State of Bihar*, (supra).

14. In *Workers of M/s Rohtas Industries Ltd. v. M/s Rohtas Industries Ltd.*, [1987] 2 SCC 588 a direction was made for payment of the workers dues by stating that such dues will have priority over other banks and financial  
H institutions. On going through the facts, it is seen that it was a case where

proceeding for liquidation of the company was going on and obviously Section 529 of the Companies Act was attracted. Moreover, it is not seen that the rights of a pawnee vis-à-vis the rights of the workmen is discussed. Since a liquidation had intervened there, which is not the case here, the said decision cannot be of any assistance to support the order passed by the High Court. In fact, in *Workers of M/s Rohtas Industries Ltd. v. M/s Rohtas Industries Ltd.*, [1987] Suppl. SCC 462 rendered while clarifying the earlier order, it was stated that the earlier order of the Court was made under peculiar circumstances obtaining in the case and was not to be taken as a precedent. Hence, even apart from the distinction, no value as a precedent can be attached to that decision. A B

15. In *State of M.P. v. Jaura Sugar Mills Ltd. And Ors.*, (supra) dealing with the Madhya Pradesh Sugar Cane (Regulation and Supply) Act, it was only held that the Cane Commissioner having power to compel the cane growers to supply cane to the factory, has incidental power and is duty bound to ensure payment of the price of the sugarcane supplied by the sugarcane growers. With respect, this decision does not enable us to adjudge the rights of a pawnee on the sale of the pawned goods or alter the status of the Cane Commissioner or the cane grower from only that of an unsecured creditor as recognised in *Bank of Bihar* (supra). C D

16. The decision in *Textile Labour Association and Anr. v. Official Liquidator and Anr.*, [2004] 9 SCC 741 was a case of liquidation and was a case to which Section 529 and 529A of the Companies Act were attracted. The said decision is also of no help in the case on hand since a liquidation has not intervened in the present case. E

17. The decision in *Rajasthan State Financial Corporation and Anr. v. Official Liquidator and Anr.*, [2005] 8 SCC 190 is also of no help since that was also a case where the question was the effect of Section 529 and 529A of the Companies Act on the power of the Debt Recovery Tribunal to sell the assets of the entity under winding up. F

18. Thus, going by the principles governing the matter, propounded by this Court there cannot be any doubt that the rights of the appellant-bank over the pawned sugar had precedence over the claims of the Cane Commissioner and that of the workmen. The High Court was, therefore, in error in passing an interim order to pay parts of the proceeds to the Cane Commissioner and to the Labour Commissioner for disbursal to the cane G H

A growers and to the employees. There is no dispute that the sugar was pledged with the appellant bank for securing a loan of the first respondent and the loan had not been repaid. The goods were forcibly taken possession of at the instance of the revenue recovery authority from the custody of the pawnee, the appellant-bank. In view of the fact that the goods were validly pawned to the appellant bank, the rights of the appellant-bank as pawnee cannot be affected by the orders of the Cane Commissioner or the demands made by him or the demands made on behalf of the workmen. Both the Cane Commissioner and the workmen in the absence of a liquidation, stand only as unsecured creditors and their rights cannot prevail over the rights of the pawnee of the goods.

C 19. We are also of the view that pending the writ appeals, the High Court ought not to have passed such an interim order of consequence especially in the light of the legal principles settled by this Court. The order of the High Court, therefore, cannot be sustained and calls for interference.

D 20. We, therefore, allow these appeals and set aside the impugned order of the High Court, directing payment out of parts of the sale proceeds to the Labour Commissioner and to the Cane Commissioner. We hold that the appellant as the pawnee, is entitled to the amount in satisfaction of its debt to secure which, the goods had been pawned and to appropriate the sale proceeds towards the debt due and only if there is surplus, to make it available for disbursal to the Cane Commissioner and to the Labour Commissioner. In the circumstances, we direct the parties to suffer their respective costs.

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N.J.

Appeals allowed.