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## ***ABOUT US***

WHITE BLACK LEGAL is an open access, peer-reviewed and refereed journal provide dedicated to express views on topical legal issues, thereby generating a cross current of ideas on emerging matters. This platform shall also ignite the initiative and desire of young law students to contribute in the field of law. The erudite response of legal luminaries shall be solicited to enable readers to explore challenges that lie before law makers, lawyers and the society at large, in the event of the ever changing social, economic and technological scenario.

With this thought, we hereby present to you

# **THE NEED TO REFORM PLEDGE LAWS IN INDIA**

AUTHORED BY: JEEYA VEDA TAMILARASI J<sup>1</sup>

## **1. INTRODUCTION:**

The law of pledge in India, as codified in Sections 172 to 179 of the Indian Contract Act, 1872,<sup>2</sup> is one of the foundational legal mechanisms governing secured transactions. It allows a borrower (pawnor) to offer movable property to a lender (pawnee) as security for a debt or obligation. However, this framework was conceived in a vastly different economic and technological environment when commerce was centred on tangible goods, physical possession and personal interactions. In contrast, the 21<sup>st</sup> century economy is increasingly defined by digital transactions, electronic records, dematerialized securities and non-traditional forms of movable assets.

Newer financial models such as invoice financing, warehouse receipts, peer-to-peer lending, digital tokens, dematerialized securities and receivables as security challenge traditional interpretations of possession and ownership. Furthermore, with the increasing role of fintech platforms and alternative credit models driven by algorithms, big data and credit scoring mechanisms like CIBIL, there is a pressing need to assess whether the current legal structure governing pledges remains adequate and inclusive.<sup>3</sup>

At present, Indian courts and financial institutions often face ambiguity in dealing with symbolic or constructive possession,<sup>4</sup> particularly when collateral is intangible or stored electronically. The absence of specific legal provisions or modernized definitions limits the ability of businesses and lenders to create enforceable security interests over many forms of valuable assets. This regulatory gap can hinder credit access, delay financing, and discourage innovation in secured lending.

Through this project, an attempt will be made to analyse the limitations of the existing law of

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<sup>2</sup> The Indian Contract Act, No. 9 of 1872, §§ 172–179 (India).

<sup>3</sup> Credit Information Companies (Regulation) Act, No. 30 of 2005, § 14 (India).

<sup>4</sup> R.K. Jain, Law of Bailment and Pledge 215–18 (5th ed. 2022).

pledge, understand how it impacts modern commerce, and evaluate how comparative jurisdictions have responded to similar challenges. The study will also suggest potential directions for reform, whether through legislative amendment, judicial innovation, or the development of model laws or regulatory frameworks, to ensure that Indian pledge law evolves in tandem with contemporary commercial practices.

## REVIEW OF LITERATURE:

1. Mulla, *The Indian Contract Act*, 15th ed. (LexisNexis 2022)  
*Review:* This authoritative commentary comprehensively covers Sections 172–179 of the Indian Contract Act, elaborating on the traditional understanding of pledge, including requirements of delivery and possession. The book also discusses key judicial interpretations that reinforce the idea of physical possession as a core feature of a valid pledge.  
*Gap:* While rich in doctrinal analysis, the commentary does not address the applicability of pledge law to digital assets, fintech innovations, or symbolic possession in the current economic landscape.
2. Basu, Aniruddha, “Reforming Security Interests in India: A Case for Harmonising with International Best Practices” (2020) 12 NUJS L. Rev. 103  
*Review:* This article critiques India’s fragmented approach to secured transactions and advocates for a unified legal framework akin to Article 9 of the UCC (US) or UNCITRAL’s model law. It examines the inefficiencies of existing laws in dealing with modern financing tools like receivables, warehouse receipts, and electronic records.  
*Gap:* Although it makes a broader case for reforming security law, it does not specifically analyse the pledge provisions under the Contract Act or their reform needs in light of symbolic and constructive possession.
3. World Bank, *Doing Business: Secured Transactions* (2020 Report)  
*Review:* The World Bank evaluates how various jurisdictions facilitate access to credit through effective movable asset frameworks. India scores low due to the lack of a comprehensive regime for non-possessory security interests and intangible assets.  
*Gap:* The report provides comparative data and macro-level insights but lacks a focused legal-analytical treatment of how the Indian pledge law could evolve to meet these needs.
4. Mansinghka, Sakshi, “Digital Gold and the Law: Possession in the Age of Dematerialisation” (2023) 5(2) NLS Bus. L. Rev. 67

*Review:* The article discusses the legal ambiguity surrounding ownership and possession of digital gold, a form of dematerialized asset increasingly used as collateral. It challenges traditional notions of delivery and pledging in the context of tech-based investment models.

*Gap:* The discussion is specific to digital gold and does not extend the analysis to broader categories like peer-to-peer lending, fintech credit models, or invoice financing under pledge law.

## **RESEARCH OBJECTIVES:**

1. To examine the adequacy of existing pledge laws under the Indian Contract Act, 1872, in addressing modern commercial transactions involving digital and intangible assets.
2. To identify and analyse the limitations in the current legal framework that hinder the use of alternative financing mechanisms such as invoice financing, peer-to-peer lending, and warehouse receipts.
3. To propose legal reforms that align Indian pledge law with global best practices and accommodate fintech innovations, thereby enhancing credit access and financial inclusion.

## **RESEARCH QUESTIONS:**

1. To what extent are the existing pledge provisions under the Indian Contract Act, 1872, adequate to govern pledges involving digital and intangible assets in contemporary commercial transactions?
2. What are the key legal and structural limitations of the current pledge framework that restrict the effective use of alternative financing mechanisms such as invoice financing, peer-to-peer lending, and electronic warehouse receipts?
3. How can Indian pledge law be reformed to align with international best practices and evolving fintech innovations to improve credit access and financial inclusion?

## **STATEMENT OF THE PROBLEM:**

The current Indian law of pledge, rooted in traditional notions of possession, fails to address the complexities of modern digital and intangible assets. This legal gap hampers emerging credit practices and necessitates urgent reform to align with contemporary commercial realities.

## **HYPOTHESIS:**

The existing legal framework governing pledge under the Indian Contract Act, 1872, is insufficient to address the complexities of emerging commercial practices involving intangible assets, digital financial instruments, and technology-driven credit models, thereby necessitating targeted legal reforms to ensure effectiveness, inclusivity, and economic adaptability.

## **2. EVOLUTION AND LIMITATIONS OF THE LAW OF PLEDGE IN INDIA:**

The law of pledge in India, codified under Sections 172 to 179 of the Indian Contract Act, 1872 (ICA), represents one of the earliest formalized frameworks of secured credit in colonial India. Its introduction was an outcome of the British colonial government's desire to transplant English mercantile law into India, ensuring predictability in commercial transactions at a time when credit markets were rudimentary and largely informal. The framers of the ICA drew heavily from English common law principles, particularly those related to pawn and pledge under English bailment law, to create a statutory mechanism for lending secured by movable property. While this legislative framework served the needs of the late 19th-century economy, it has increasingly struggled to cope with the complexity of 21st-century financial systems, especially in the context of digital and intangible assets.

### **2.1 Historical Evolution:**

The historical evolution of pledge law can be traced to the English common law doctrine of bailment, where delivery of goods was central to the creation of a pledge. A pledge was essentially a special kind of bailment in which goods were delivered by the debtor (pawnee) to the creditor (pawnee) as security for repayment of a debt. When codified in 1872, Indian law preserved this emphasis on delivery of possession as the foundational requirement of a pledge. Section 172 of the ICA defines a pledge as 'the bailment of goods as security for payment of a debt or performance of a promise', thereby cementing physical transfer as an essential condition.

This statutory design reflected the economic context of colonial India, where commerce was based largely on agricultural produce, precious metals, and tangible goods. Scholars note that the ICA's drafters sought to create certainty and reduce disputes in a fragmented credit market

dominated by moneylenders.<sup>5</sup> By providing legal recognition to possession-based security, the pledge enabled creditors to enforce debts with minimal resources, without lengthy litigation, a pressing concern in the colonial economy.

Over time, however, the Indian economy underwent structural transformations. The emergence of banking institutions in the 20<sup>th</sup> century, the growth of corporate finance, and most recently the rise of fintech have fundamentally altered how assets are held and unchanged since 1872, save for judicial interpretations. This static framework, rooted in tangible property transactions, has been critiqued as being anachronistic in addressing the realities of a modern digital economy.<sup>6</sup>

## **2.2 STRUCTURAL LIMITATIONS OF THE LAW OF PLEDGE:**

While historically significant, the Indian pledge framework suffers from several enduring limitations that undermine its efficacy in contemporary financial markets.

### **A) Over-Reliance on Possession:**

The main issue here is the requirement for physical delivery of goods before a pledge can be established. While this made sense in the past, especially in agricultural and trade settings, it creates real problems today with modern assets like dematerialized shares, electronic securities, and digital currencies. Courts have been trying to figure out if electronic entries in a depository account can count as delivery for pledging, but the results have been all over the place<sup>7</sup>. Unlike the Uniform Commercial Code (UCC) article 9 in the United States,<sup>8</sup> which recognizes ‘control’ over intangibles as equivalent to possession, Indian law remains tethered to an outdated physicalist conception of property.

### **B) Fragmentation of Security Law:**

One more limitation is the overlap and fragmentation between the pledge provisions in the ICA

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<sup>5</sup> Banerjee, R. (2014). “Colonial Codification and Commercial Law in India.” *Indian Economic and Social History Review*, JSTOR.

<sup>6</sup> Ravi, P. (2020). “Revisiting the Indian Contract Act: Outdated or Enduring?” *Journal of Business Law*, ResearchGate.

<sup>7</sup> Singh, A. (2019). “Pledge of Dematerialized Securities: The Indian Experience.” *National Law School Journal*, ResearchGate.

<sup>8</sup> U.C.C. § 9-101 et seq. (Am. Law Inst. & Unif. Law Comm’n 2010).

and sector-specific legislations, especially the Depositories Act, 1996<sup>9</sup>, SARFAESI Act, 2002<sup>10</sup> and the Companies Act, 2013<sup>11</sup>. For instance, while deposit accounts allow for pledging of dematerialized shares through electronic instructions, those pledges exist in a parallel regime where there is no clear statutory integration with the ICA. This multiplicity creates uncertainty for creditors, as the enforceability of security interests depends on which statute governs this transaction.<sup>12</sup>

In the case of *JRY Investments Pvt. Ltd. vs Deccan Leafline Services Ltd & Ors.*, on the 11<sup>th</sup> of March 2003,<sup>13</sup> Hon'ble Justice SA Bobde emphasized the importance of modernising the existing pledge laws. The Plaintiff in this case pledged 15 lakh shares to Deccan Leafline as security for a loan of Rs. 1.12 Crore. The loan was not even sanctioned in the first place, and before that, the securities were transferred as shares to other parties without notice. This is because the pledge law just because it is not inclusive of demat shares and hence gives broader powers to the pawnee to sell shares without notice. This case exposes the fragility of borrower protections under old laws. The plaintiffs lost their ownership; the law didn't protect electronic pledges unless all formalities were followed. This judgment exposed how borrowers can lose ownership if lenders misuse pledged demat shares and the pledge is not registered properly under the pledge laws.

### C) Lack of Adaptivity to Fintech Innovations:

The current pledge law doesn't really address the rise of fintech assets like peer-to-peer lending platforms, tokenized securities, and blockchain-based assets. While other regions have updated their secured transactions laws to include digital assets, India is still relying on a 19th-century legal framework, which creates some significant gaps in enforceability. For instance, it's unclear whether a crypto-asset can be considered 'delivered' under Section 172<sup>14</sup>, which makes it a bit risky for creditors to accept these assets as collateral.<sup>15</sup>

In the case of *PTC India Financial Services Ltd v. Venkateshwara Kari*<sup>16</sup>, in the year 2002, it

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<sup>9</sup> The Depositories Act, No. 22 of 1996, INDIA CODE (1996).

<sup>10</sup> The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, No. 54 of 2002, INDIA CODE (2002).

<sup>11</sup> The Companies Act, No. 18 of 2013, INDIA CODE (2013).

<sup>12</sup> Sharma, N. (2021). "Security Interests in Indian Law: Fragmentation and Reform." *Indian Journal of Legal Studies*, JSTOR.

<sup>13</sup> *JRY Investments Pvt. Ltd. v. Deccan Leafline Services Ltd. & Ors.*, 2004 (121) Comp Cas 12 (Bom HC)

<sup>14</sup> The Indian Contract Act, No. 9 of 1872, § 172, INDIA CODE (1872).

<sup>15</sup> Menon, A. (2022). "Fintech, Cryptocurrencies, and Secured Transactions: Lessons for India." *Asian Journal of Comparative Law*, Cambridge Journals.

<sup>16</sup> *PTC India Financial Services Ltd. v. Venkateswarlu Kari*, (Civil Appeal No. 5443 of 2019) (S.C. May 12, 2022) – 2022 INSC 562 – [2022] 9 S.C.R. 1063.

was clarified that the Depositories Act of 1996 very clearly overrides the ICA of 1872, when it comes to pledging demat shares. The facts of this case are that PTC's the plaintiff, gave a loan of rupees 125 Crore to NSL Nagapatnam Power. In order to secure this loan, they pledged demat shares of 31.8 loans. When the borrower defaulted, PIFSL invoked the pledge and became the 'beneficial owner' of the shares via the depository system. The key question that arose is whether the Depositories Act, 1996, overrides the ICA, 1872, when it comes to pledging demat shares. It is a clear dispute between two legislations. This gives a very clear aspect of the fact that modernisation is required in the ICA's pledge laws. It should include mandatory safeguards like notice before sales, even if the contract says otherwise. And before that, include the electronic assets in the sections of the pledge laws of ICA, 1872.

#### D) Enforcement Mechanism and Judicial Delays.

Even though the ICA allows the pawnee to keep the goods and even sell them in case of default (Section 176),<sup>17</sup> it is usually unattractive due to procedural inefficiencies and judicial backlog, which means that enforcement ends up being a painful exercise. This gets in the way of the most fundamental mandate of a pledge: to serve as both a fast and burden-shifting solution, if it no longer accomplishes this goal, its utility decreases compared to a newer framework that permits extra-judicial enforcement.<sup>18</sup>

#### e) Limited Scope of Property:

The pledge law under the Ica restricts its application to movable property, excluding immovable property and several categories of intangibles. While mortgages and hypothecation fill some gaps, the narrow statutory scope of pledge renders it an inflexible toll in a financial system while intangibles and mixed asset classes dominate.<sup>19</sup>

### **2.3. THE CONTINUING RELEVANCE OF PLEDGE:**

Despite its limitations, pledge law retains continuing relevance, especially in informal and small-scale credit markets where physical goods are still being exchanged as collateral. Studies have shown that in rural credit markets, pledging of agricultural produce or gold remains a

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<sup>17</sup> The Indian Contract Act, 1872, § 176, No. 9 of 1872, INDIA CODE (1872).

<sup>18</sup> Sudipta De Sarkar & N. L. Mitra, Secured Lending on Intellectual Property Rights in India: Issues on Valuation, 10 Asian J. Legal Educ. 1 (2023).

<sup>19</sup> Manupatra Articles, Transfer of Actionable Claims under the Transfer of Property Act, 1882

common and trusted method of securing loans.<sup>20</sup> Thus, while outdated in fintech contexts, the ICA framework still provides functional security for a significant portion of India's population. The evolution of pledge law in India reflects the trajectory of colonial codification, where English doctrines were transplanted into a vastly different socio-economic context. While it offered certainty in the 19th century, the static nature of the ICA's pledge provisions has become a constraint in a digitalized, fintech-driven economy.<sup>21</sup> The law's reliance on possession, its failure to adapt to intangible assets, and its fragmented coexistence with sectoral laws underscore the urgent need for reform. As comparative frameworks like the UCC demonstrate, modernization requires moving from a possession-based model to a control-based model that can accommodate both tangible and intangible assets.<sup>22</sup> For India, reforming the pledge law is not merely about modernizing commercial legislation, but about aligning its secured credit system with the realities of a digital economy.<sup>23</sup>

Since the Depositories Act, 1996, Indian capital markets have transitioned to dematerialized securities. The evolving pledge mechanism today looks antiquated. Shares, as they exist today, are not in the form of physical certificates in storage but are entries in electronic ledgers, which are maintained by depositories, NSDL and CDSL.<sup>24</sup> These depositories have established their own schemes for the establishment and enforcement of pledges electronically; however, these systems function primarily outside of the terms of the Indian Contract Act, and instead rely on agreement amongst the parties through innovation. The result is an inconsistent regime whereby the statutory law deviates from the existing market construct.<sup>25</sup> Scholars and practitioners have pointed out that this gap creates a level of legal uncertainty for investors, and especially for lenders or other counterparties in cross-border financing where counterparties expect agree on contractual terms but want statutory clarity.<sup>26</sup>

Since the ICA was introduced a nearly 100 years ago, and hence its application on the contemporary situations are becoming extremely difficult. The ICA does address the bailment of goods part but the advent of technology raises issues about how it can be applied. Section

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<sup>20</sup> Chaudhuri, S. (2018). "Collateral in Rural Credit Markets: The Role of Pledge." *Economic and Political Weekly*, JSTOR.

<sup>21</sup> Manupatra Articles, Transfer of Actionable Claims under the Transfer of Property Act, 1882.

<sup>22</sup> Motika, "Pledge over Digital Assets".

<sup>23</sup> EY, "Modernization of the Legislative Framework for Pledges and Unified Electronic Registry," Oct. 30, 2024,

<sup>24</sup> Chambers and Partners, "India's Supreme Court clarifies the law on pledge of dematerialised shares," Feb. 14, 2024.

<sup>25</sup> Mondaq, "Recent Developments in India's Corporate & Commercial Laws," Feb. 25, 2025.

<sup>26</sup> EnterSlice, "Role of NSDL and CDSL in the Process of Dematerialisation," Aug. 13, 2024.

148 of the ICA<sup>27</sup> mentions that bailment as delivery of goods and subsequently section 2(7) in the Sale of Goods Act,1930 defines goods as every kind of movable property, excluding actionable claims and money,<sup>28</sup> because the digital data does not qualify as tangible movable property, it falls outside the circumvent of the definition of goods. And as a consequence, data cannot be the subject of bailment under the current framework. Hence the act of transferring and registering data to a cloud service provider for storage closely resembles the legal structure of pledges.<sup>29</sup>

### **3. CONTEMPORARY CHALLENGES AND THE NEED FOR MODERNIZATION OF PLEDGE LAWS IN INDIA**

Though its values and conceptions have continued to serve traditional commerce, tectonic shifts in global financial systems, the emergence of fintech driven lending, and the dematerialization of assets, have exposed serious gaps in the prevailing framework. This chapter details contemporary challenges like technological innovation and global financial sophistication and stresses the need to modernize pledge laws in India.

In the past ten years or so, few developments are as significant as the emergence of fintech platforms, which have transformed credit intermediation. Increasingly digital lenders, P2P lending platforms and NBFCs, have also focused on intangible or dematerialized assets as collateral. However, India's pledge law is poorly adapted to this context, as it requires physical delivery of goods for a pledge to be valid.

For instance, while dematerialized shares in a Depository Participants (DP) account, or digital payment receivables cannot be "physically delivered," they are an essential part of modern collateral structures.<sup>30</sup> Fintech companies often wish to avail of substantial credit models, while control over such electronic assets is provided by way of an escrow, control over a digital account, or even algorithmic monitoring of the asset.

The absence of specific statutory acknowledgment or acceptance of informal customs creates

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<sup>27</sup> Indian Contract Act, No. 9 of 1872, § 148 (India), INDIA CODE (1872).

<sup>28</sup> Sale of Goods Act, No. 3 of 1930, § 2(7) (India), INDIA CODE (1930).

<sup>29</sup> Ramanujan, P. "Legal Challenges of Digital Data and Bailment in India," *Journal of Indian Law and Technology*, vol. 15, no. 2 (2024).

<sup>30</sup> World Bank. "Credit Scoring Approaches Guidelines." World Bank Group, 2020.

legal ambiguity and uncertainty around enforceability. Such delimitation between adequate statutory recognition and real-life situations of technological reality not only exposes lenders to credit risks but holds back the scale-up of creative and innovative credit models<sup>31</sup>. It is occupied with limitations that prevent it from a standard, more simplistic possession approach, such as within circuits in the area of UCC Article 9,<sup>32</sup> whereby “control” over the electronic securities and accounts is sufficient to perfect a security interest in the transaction.<sup>33</sup>

The evolution of Indian capital markets towards dematerialized securities since the Depositors Act, 1996,<sup>34</sup> has made the traditional pledge arrangement somewhat redundant. Shares today do not exist with the status of physical certificates but rather are recorded in electronic ledger kept by depositories like NDSL and CDSL.<sup>35</sup>

While these depositories have developed their own means to create and enforce pledges electronically, the depositories create pledges, and only via contractual innovation and these don't sit squarely within the statutory framework of the ICA, 1872, this is a piecemeal arrangements system whereby statutory law hasn't caught up with market practice.<sup>36</sup> Scholars suggest this is troubling for legal certainty and investor confidence, particularly in cross border financing transactions where counterparties have different expectations around statutory clarity.<sup>37</sup>

Additionally, the emergence of some new asset classes, cryptocurrencies, tokenized assets, and intellectual property rights, creates another complication.<sup>38</sup> Because there are no ‘delivered’ items comprising such intangibles, the pledge law is in danger of becoming antiquated without reform in a non-physical asset economy.<sup>39</sup>

The inadequacies of Indian pledge law become more apparent when we compare it to

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<sup>31</sup> Routh, Supriya. "Examining the Legal Legitimacy of Informal Economic Activities." *Social & Legal Studies* 31, no. 2 (2021): 282-308.

<sup>32</sup> Uniform Commercial Code § 9-314. Perfection by Control.

<sup>33</sup> City of London Law Society. "Digital Assets, The Limits of the Concept of Possession".

<sup>34</sup> Depositories Act, 1996, Act No. 22 of 1996, India Code (Aug. 10, 1996)

<sup>35</sup> Rajeev Singh Rathi, Dematerialization, *Law eJournal* (2020).

<sup>36</sup> Bhatt and Joshi Associates, *The Depositories Act 1996: India's Transition to Electronic Securities* (May 21, 2025)

<sup>37</sup> MISM, *Dematerialization in Indian Securities Market* (Nov. 12, 2024),

<sup>38</sup> Nishith Desai Associates, *Dematerialization of Securities by Private Companies* (Nov. 10, 2023)

<sup>39</sup> Wyczik, Jakub. "The Property Law of Crypto Tokens." *SSRN*, Nov. 1, 2023.

international frameworks. UCC Article 9 in the United States and the UNCITRAL Model Law<sup>40</sup> on Secured Transactions both embrace the principle of functional equivalence, allowing security interests to be created, perfected, and enforced over both tangible and intangible assets.<sup>41</sup>

Under UCC Article 9, a lender may secure rights over electronic securities, receivables, or even future intangibles by establishing “control” rather than physical possession. Similarly, the UK’s Financial Collateral Arrangements (No.2) Regulations, 2003, permit legal recognition of pledges over book-entry securities.<sup>42</sup> These frameworks prioritize flexibility, recognizing that security law must evolve with financial practices.

India’s adherence to colonial-era provisions contrasts sharply with these modern frameworks, and as a result, Indian businesses face disadvantages in accessing global credit markets. Indian courts have occasionally attempted to reconcile pledge laws with modern commercial realities. In cases involving dematerialized shares, courts have accepted depository pledges as valid despite the absence of physical delivery. However, such judicial innovation is piecemeal and cannot substitute for legislative clarity.<sup>43</sup>

Moreover, courts remain constrained by the text of the Indian Contract Act, which explicitly ties pledge to “delivery of goods.” Expansive interpretation risks doctrinal inconsistency, undermining the predictability of commercial law.<sup>44</sup>

The pressing need for modernization stems from three interrelated imperatives. First, credit markets today rely heavily on intangible assets, and a law centred on physical delivery is inherently inadequate.<sup>45</sup> Second, the fintech ecosystem in India, driven by government initiatives such as the Digital India program and the proliferation of Unified Payments Interface (UPI), requires a legal framework that recognizes digital collateral.<sup>46</sup> Third, international competitiveness demands alignment with global practices to attract cross-border investments

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<sup>40</sup> iPleaders. "All about UNCITRAL Model Laws," Aug. 3, 2024.

<sup>41</sup> UNCITRAL. "Model Law on Secured Transactions," Guide to Enactment (2017).

<sup>42</sup> City of London Law Society, "Digital Assets: The Limits of the Concept of Possession" (2021).

<sup>43</sup> Macdonald, Roderick, et al. "A Model Law on Secured Transactions." *McGill Law Journal* 56, no. 3 (2011): 567-663

<sup>44</sup> Indian Contract Act, No. 9 of 1872, §§ 172–179 (India), INDIA CODE (1872)

<sup>45</sup> Vidhi Centre for Legal Policy, *Modernising the Law for Payment Services in India: Preparing for the Future of Retail Payments* 6 (2021).

<sup>46</sup> Nishith Desai Associates, *Fintech Report: India’s Flourishing Fintech* (2025)

and ensure enforceability of Indian security interests abroad.<sup>47</sup>

Legal reform could take multiple forms: Amending the Contract Act to expand the definition of pledge to include “control” over electronic and intangible assets, adopting a separate legislation modelled on UNCITRAL<sup>48</sup> recommendations, harmonizing secured transactions across asset types, integrating depository practices within statutory law to provide clarity on dematerialized pledges.<sup>49</sup> Such reforms would ensure that Indian law keeps pace with technological and financial innovation, while preserving the core principle of security for creditors and redemption for debtors.<sup>50</sup>

The law of pledge under the Indian Contract Act, 1872, while historically significant, is no longer equipped to meet the demands of modern financial systems.<sup>51</sup> Fintech innovation, the rise of dematerialized securities, and the growing prominence of intangible assets expose the limitations of a possession-based framework. Comparative jurisdictions have already embraced broader, more flexible approaches, enabling secured credit over digital and intangible assets.

For India, modernization of pledge laws is not merely a legal necessity but an economic imperative to foster innovation, deepen credit markets, and enhance global integration. As addressed in the previous chapter about the case of PTC India Financial Service Ltd. v. Mr. Venkateswarlu Kari,<sup>52</sup> the Sc did recognize the validity of pledges that were created over demat securities. The court clarifies that the section 12 of Depositories Act, 1996,<sup>53</sup> mere entry in the records of the depository serves as clear evidence of a pledge, hence enforcing the idea of constructive possession of digital goods. This recognition by the Supreme Court clearly illustrates that the existing legal frameworks can adapt existing legal concepts like bailment or pledge which is a subset of bailment to technological realities.<sup>54</sup>

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<sup>47</sup> Pradip Bhuyan et al., Retail Payment Habits in India: Evidence from a Pilot Survey, RBI Bulletin, Apr. 2021,

<sup>48</sup> United Nations Commission on International Trade Law (UNCITRAL), Legislative Guide on Secured Transactions (2017).

<sup>49</sup> Khaitan & Co., “Enforcement of pledge over dematerialised shares — Supreme Court provides much needed clarity,” (May 26, 2022).

<sup>50</sup> EY, “Modernization of the legislative framework for pledges and the establishment of a Unified Electronic Registry of Pledges on movables, claims, and other rights” (Oct. 30, 2024).

<sup>51</sup> Indian Contract Act, No. 9 of 1872, § 172 (India), INDIA CODE (1872).

<sup>52</sup> PTC India Financial Services Ltd. v. Venkateswarlu Kari, Civil Appeal No. 5443 of 2019, Supreme Court of India (May 12, 2022).

<sup>53</sup> Arora, Nidhi, Binny Chopra, and Amiya Krishna Upadhyay. "Enforcing Pledge of Dematerialized Shares: Insights from the PTC India Decision." EVA Law, Oct. 4, 2023.

<sup>54</sup> Cyril Amarchand Mangaldas. "Reinforcement of pledge over dematerialised shares: A fillip for financial markets." Mar. 2023.

But then the question is if this case can be a blueprint for the other succeeding cases. Firstly, pledge is a subset of bailment and does not extend for broader range of digital goods. Secondly the court's holding was limited to a confined scope of the Depositories Act,<sup>55</sup> while section 172 of the ICA defines a pledge to be a contract of bailment that has a special right for the pawnee only upon a delivery of possession, if its actual or constructive, the Court's interpretation in this particular case extended the concept of pledge to demat securities by recommending the reading of ICA with Depositories Act.<sup>56</sup> Still, the limitations mentioned before are not addressed because this decision offers only a minor part statutory solution.<sup>57</sup> Therefore, the need to redefining goods, and introducing a legal code, is essential to sort this rapidly evolving landscape of technology.

#### **4. CONCLUSION**

The law of pledges, as articulated in Section 172-179 of the Indian Contract Act, 1872, was one of the first statutory avenues for regulating secured transactions in India. Given its origin in the colonial period, it offered a statutory expression of a commercial world emphasizing physical goods, possession and direct lending between parties. Possession was an appropriate basis in a trade-based economy that materially depended on actual movables. However, pledge's reliance on possession pattern and principles as a central mechanism of security demonstrates structural limitations in a trading world that must also grapple with the realities of 21<sup>st</sup> century financial markets.

In this dissertation, it has been demonstrated that the development of pledge law has been uneven. However, judicial interpretation has consistently focused on the notion that physical delivery is a sine qua non, thus creating certainty but at the cost of flexibility. Conversely, global regimes, particularly the Uniform Commercial Code (UCC) in the US, are moving towards security interest in intangibles, electronic assets, and dematerialized securities based on the doctrine of 'control' rather than possession. These innovations are sadly lacking in India law.

The accelerating development of fintech in India has continued to highlight the gap between

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<sup>55</sup> Depositories Act, No. 22 of 1996, INDIA CODE (1996).

<sup>56</sup> Asian Journal of Legal Education, Sudipta De Sarkar & N. L. Mitra, "Secured Lending on Intellectual Property Rights in India: Issues on Valuation," 2023.

<sup>57</sup> Taxmann. "Bailment and Pledge under the Indian Contract Act—FAQs," Jun. 19, 2025.

law and practice. Innovations such as peer-to-peer lending platforms, digital gold schemes, and tokenized assets, operates in a space where physical delivery of security is either impractical or impossible. In this case, lenders fintech companies and even regulators are forced to rely on contractual innovations or informal arrangements to get terms to override the constraint imposed by the Contract Act provisions. This presents uncertainty in enforcement, increases transaction costs and ultimately leads to inefficiencies in secured credit markets.

The constraints of the pledge law are also echoing in the broader policy space. While India has made progressive moves with measures such as the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002, and the Insolvency and Bankruptcy Code, 2016, those laws primarily respond to the context of large institutional credit, and large-scale defaults. Small borrowers and the fintech-based credit ecosystem remain bound by the outdated framework of the 1872 law. Thus, millions of transactions involving micro-credit, consumer loans, and digital collateral, remain caught in a legal grey zone of enforceability.

Therefore, pledge law reform is not only a doctrinal solution, but an urgent economic imperative. Reforms should seek to (i) broaden the definition of “goods” to include electronic and dematerialized assets, (ii) allow security interests to be established with reference to “control” or registration rather than possession, and (iii) harmonise Indian law with international best practice to facilitate interoperability with cross-border financial transactions. A shift toward a unified code for secured transactions, modelled on Article 9 of the UCC, is discussed by scholars and policymakers, and would bring much needed consistency and modernity into Indian law.

In conclusion, the pledge law, although historically great, is less and less useful in present financial realities. The pledge law has transpired through colonial importation and judicial rigidity, and its shortcomings are now acutely felt in the age of the fintech. To reconcile traditional legal techniques with new technological ecosystems, India needs to conceptualise the law of pledge, not as an artifact of nineteenth century commerce, but as a malleable legal concept capable of backing twenty-first century's innovations. This re-conceptualisation is crucial, not only for legal accuracy, but also for the burgeoning of India's digital economy, financial inclusion, and competitiveness on the world stage.

## **SUGGESTIONS AND RECOMMENDATIONS:**

1. Amend the Indian Contract Act, 1872: There is a necessity to revise the section 172-179 i.e., the definition of ‘goods’ and ‘pledge’ to explicitly include intangible assets, electronic records, dematerialized securities, digital tokens and intellectual property. There is also a need to legally recognize constructive and symbolic possession for non-physical assets, enabling pledges without physical delivery, aligned with modern commercial relations. Introduction of provisions which clarify the concepts of ‘control’ or ‘registration’ and to substitute for physical possession as a valid method to perfect security interests.
2. Enact a Unified Secured Transactions Code or Law: As referred from the global best practices such as the UCC (Article 9) and the UNICITRAL Model law on Secured Transactions, we need to draft, enact and implement a Secured Transactions Law. This law should be consolidating and harmonizing scattered provisions from the ICA, Depositories Act, SARFAESI Act, Companies Act, etc., into one coherent framework which will cover all the movable and intangible assets. This should also provide a modern regime for pledges and security interests, promoting transparency and legal certainty.
3. Integrate Depository Laws with Statutory Pledge Framework: The Depositories Act, 1996, should be amended or explicitly aligned with the pledge provisions in the Indian Contract Act to ensure coherence and reduce legal ambiguity. Providing statutory backing for depository-based electronic pledges will grant these arrangements clear legal enforceability beyond mere contractual innovations. This would reinforce that entries in electronic ledger accounts maintained by depositories like NSDL and CDSL constitute prima facie evidence of pledge or control, thus formally recognizing electronic pledges as valid and enforceable within India’s statutory framework.
4. Introduce Digital Asset-Specific Provisions: There is a need to craft specific regulations clarifying the legal status and treatment of emerging digital asset classes, including tokenized assets, digital securities, cryptocurrencies, and smart contracts, especially in the context of pledges. These regulations should allow pledges on digital assets subject to escrow or electronic control mechanisms, structured with enforceability safeguards and transparency rules to protect all parties involved while fostering innovation and legal certainty in digital collateral arrangements.

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