

The Cheque & its Dishonor Section 138 of Negotiable Instrument Act, 1881

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Abstract: The advent of cheques in the market have given a new dimension to the commercial and corporate world, its time when people have preferred to carry and execute a small piece of paper called cheque than carrying the currency worth the value of cheque. In place of bundle of notes a piece of cheque is much easier to carry. It facilitated trade and commerce tremendously. But at the same time with the arrival of cheque system the problem of its dishonoring was also started.

Keywords: Cheque, Section 138 of Negotiable Instrument Act, 1881, Banking system, Dishonor

I. INTRODUCTION

People started to issue cheques in order to commit fraud and without intention of honoring them. When a cheque is issued by a person in liquidation of his debt or liability and the same get dishonored by the payee bank for whatsoever reason then it only creates a bad taste and also results in damage and mental harassment to its holder. Since business activities have increased, the attempt to commit economic crimes and to indulge in activities for making easy money have also increased.¹ Thus every bank has its own printed cheque forms / books which are supplied to the account holders at the time of opening the accounts. These cheques are printed by expert printers on special security paper which is sensitive to chemicals. This is done in order to make chemical alterations, if any, noticeable.² The customers may obtain a new cheque book when the old one is finished or is about to finish, by signing the requisition slip provided in the cheque book towards the end. If a customer desire to have more than one cheque book, one to draw cash and another to be issued to his suppliers, the bank may have such cheque leaves printed with the crossing as well as superscripts like Account payee and Not - Negotiable thereon. Therefore besides civil law, an important development both in internal and external trade is the growth of crimes and it has been founded that the banking transaction and banking business is every day being confronted with the criminal actions and this had led to an increase in number of criminal cases relating to or concerned with the banking transaction. In India cheques are governed by the Negotiable Instrument Act, 1881, which is largely a codification of the English law on the subject. Before this there was no effective legal provision to restrain people from issuing cheques without having sufficient funds in their account or any stringent provision to punish them in the event of such cheque not being honoured by their banker and returned unpaid. Although upon dishonor of cheque there is a

civil liability accrued, however in reality the process to seek civil justice becomes notoriously dilatory and recovery by way of a civil suit takes an inordinate long time. The Negotiable Instrument Act, 1881 was amended by the Banking public financial Institution and Negotiable Instrument Laws (Amendment) Act, 1988 wherein a new chapter XVII was incorporated for penalties in case of dishonor of cheque due to insufficiency in funds in the account of drawer of the cheque. The Act was further amended in year 2002 in relation to section 138 of the said Act. Not only this it went through a major change on 1st August 2014 when a three-judge bench of the Honourable Supreme Court overturned many of the Court's previous decisions. In **Dashrath Rupsingh Rathod vs. State of Maharashtra**,³ Before this judgment the legal position was as follows – Let us say a party X based in Mumbai issued a cheque to a party Y of Kolkata. The cheque was drawn on a bank of Mumbai. The cheque was presented by Y to his bank in Kolkata. The cheque bounced. Y issued a notice to X demanding payment for the bounced cheque. X did not pay. Y would file a complaint with the Magistrate at Kolkata. After the judgment dated 1st August 2014, Y had to necessarily come to Mumbai to file the complaint. The Honourable Supreme Court had made it mandatory that the complaint related to cheque bouncing must be filed only where the drawee bank is located. This surely made life difficult for anyone who received a cheque, while simultaneously making it easy for the accused or the person whose cheque bounced. However Supreme Court's judgment has been overturned by the Government of India by getting the President of India to promulgate on 15th June 2015 an Ordinance, The Negotiable Instruments (Amendment) Ordinance, 2015, No. 6 of 2015. The Ordinance has introduced a new sub-section to section 142 of The Negotiable Instruments Act. Also until 1st April 2012, cheques in India were valid for a period of 6 months from the date of their issue, before the

¹ Somashekar N.T, Banking, NAIP, 2009, p 222., Available at [www. Worldpress. com](http://www.Worldpress.com)

² Shaw Patrick Dunlop, NIA, R.C & OB, 1936, Available at www.books.google.co.in

³ (2014) 9 SCC 129

reserve bank of India issued a notification reducing their validity to 03 months from the date of issue.

II. WHAT IS A CHEQUE?

A Cheque is a Negotiable Instrument⁴ and in order to understand a cheque, firstly one has to know that what a bill of Exchange is. Section 5 of the Act defines a Bill of Exchange as an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument. Section 6 of the Act now define Cheque as a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand and it includes the electronic image of a truncated cheque and a cheque in the electronic form. a cheque in the electronic form means a cheque drawn in electronic form by using any computer resource and signed in a secure system with digital signature (with or without biometrics signature) and asymmetric crypto system or with electronic signature, as the case may be; A truncated cheque means a cheque which is truncated during the course of a clearing cycle, either by the clearing house or by the bank whether paying or receiving payment, immediately on generation of an electronic image for transmission, substituting the further physical movement of the cheque in writing.

III. FORMS OF CHEQUES

The Negotiable Instrument Act does not specify any type or form of a cheque. Section 13 of the Act defines a negotiable instrument as a promissory note, bill of exchange or Cheque payable either to order or to bearer. Thus a Cheque can be an **order Cheque** or a **bearer Cheque** not only this, a cheque can be following:⁵

1. **Blank Cheque:** a cheque on which the drawer put his signature and leaves all other columns blank is called a blank cheque.
2. **Stale Cheque:** a cheque which is more than 6 months old is a stale cheque
3. **Mutilated Cheque:** if a cheque is torn in to two or more pieces, it is termed as mutilated cheque.
4. **Post dated Cheque:** if a Cheque bears a date later than the date of issue, it is termed as post dated cheque
5. **Open Cheque:** a Cheque which is not been crossed is called a open cheque. Even if a cheque is crossed and subsequently the drawer has cancelled the crossing at the request of the payee and affixes his full signature with the words "Crossing cancelled pay cash", it became an open cheque
6. **Crossed Cheque:** a cheque which carries too parallel transverse lines across the face of the cheque with or without the words "I and co", is said to be crossed.

7. **Gift Cheque:** gift cheques are used for offering presentations on occasions like birthday, weddings and such other situations.

8. **Traveller's Cheque:** it is an instrument issued by bank for remittance of money from one place to another.

IV. DISHONOUR OF CHEQUE

A cheque is said to be dishonor when the payment is not made on its presentation to the bank. Earlier before 1988, there was no liability provided in case of dishonor of a cheque but after the insertion of Section 138 in the Negotiable Instrument Act, 1881 criminal as well civil liability were imposed by way of short term imprisonment and fine on the dishonor of the cheque. It is done to develop and create the faith of the cheque among the people.⁶ Section 6 of the Negotiable Act, 1881, defines a cheque as a bill of exchange drawn on a specified banker and not expressed that to be payable otherwise on demand. Thus "Dishonour" means to refuse or neglect to accept or pay when duly presented for payment of a bill of exchange or a promissory note or draft on a banker.⁷ Black's Law Dictionary defines the term "Dishonor" as to refuse to accept or pay a draft or to pay a promissory note when duly presented. An Instrument is dishonoured when a necessary or optional presentment is duly made and due acceptance or payment is refused, or cannot be obtain within the prescribed time, or in case of bank collections, the instrument is reasonably returned by midnight deadline.⁸ Reference to the term dishonour has been made in Sec 91 & Sec 92 of the Negotiable Instrument Act, 1881. Sec - 91 Dishonor by Non- acceptance: a bill of exchange is said to be dishonored by Non-acceptance when the drawee, or one of several drawees not being partners, makes default in acceptance upon being duly required to accept the bill, or where presentment is excused and the bill is not accepted. Where the drawee is incompetent to contract, or the acceptance is qualified the bill may be treated as dishonored. Sec 92, Dishonour by Non - Payment: A promissory note, bill or exchange or cheque is said to be dishonored by Non-payment when the maker or the note, acceptor or the bill or drawee or the cheque makes default in payment upon being duly required to pay the same. A cheque is said in be bounced or dishonoured when it is refused to accept or pay when presented to the bank. It refers to a cheque that is drawn by a bank customer on his bank. Which cheque has been dishonored by the *bank* upon presentation by the payee of the cheque or the payee's authorized agent, ostensibly, because there was either outright lack of funds or insufficiency of funds in the account on which the cheque was drawn.⁹ Further sec- 92 of the Act defines, a cheque is said to be dishonored by Non-payment when the maker or the note, acceptor of the bill or drawee of the cheque makes default in payment upon being duly required to pay the same. In the case of *K. Venkatasubbaya v.*

⁴ Section 13, Negotiable Instrument Act, 1881

⁵ Somashekar. N. T, *Banking*, 2009, available at www.wordpress.com

⁶ The Hindu Business Line, Dated 29th July 2001

⁷ Wharton's Law Lexicon, 1978, p 335

⁸ Rakesh Porwal v. Narayan Joglekar, 1993 Cr.LJ at p 680

⁹ Grner A Bryen, Black's Law Dictionary, 7th Edn (West Group), 1999

*P.R Rao Tobacco Co.*¹⁰ The court held that a promissory note, bill of exchange or cheque is said to be dishonoured by Non - payment when the maker or the note, acceptor or the Bill or drawee or the cheque makes default In payment upon being duly required to pay the same *as* against Section - 92 applied to all the three types or instruments like promissory notes, cheque and bills of exchange.

V. SECTION 138 OF THE NEGOTIABLE INSTRUMENT ACT, 1881

Section 138 of the Act only prescribe penalties in case of dishonor of cheques for insufficiency of funds in the accounts and provides that where any cheque drawn by a person on an account maintained by him with a banker for payment of any amount of money to another person from out of that account for the discharge, in whole or in part, of any debt or other liability, is returned by the bank unpaid, either because of the amount of money standing to the credit of that account is insufficient to honour the cheque or that it exceeds the amount arranged to be paid from that account by an agreement made with that bank, such person shall be deemed to have committed an offence and shall, without prejudice to any other provision of this Act, be punished with imprisonment for [a term which may be extended to two years¹¹], or with fine which may extend to twice the amount of the cheque, or with both. Provided that nothing contained in this section shall apply unless:-

- a. the cheque has been presented to the tank within a period of six months from the date on which it is drawn or within the period of its validity, whichever is earlier;
- b. the payee or the holder in due course of the cheque, as the case may be, makes a demand for the payment of the said amount of money by giving a notice; in writing, to the drawer of the cheque, [within thirty days] of the receipt of information by him from the bank regarding the return of the cheque as unpaid; and
- c. the drawer of such cheque fails to make the payment of the said amount of money to the payee or, as the case may be, to the holder in due course of the cheque, within fifteen days of the receipt of the said notice.

The section further explains "debt of other liability" means a legally enforceable debt or other liability. Thus the section postulates the essential ingredients an offence under the section 138 that can be summed up as follows:-

1. A person must have drawn a cheque on a bank account maintained by him.
2. The cheque should have been issued in discharge, in whole or in part, of any debt or other liability.
3. The cheque has been presented to the bank within the period of its validity.

4. The cheque is returned by the bank unpaid, either because of funds insufficient or it exceeds the amount arranged to be paid.
5. The payee makes a demand for the payment by giving a notice in writing, within 30 days of the receipt of information by him from the bank.
6. The drawer fails to make payment of the said amount of money within 15 days of the receipt of the said notice.
7. Complaint is made within one month of the date on which the cause – of -- action arises.¹¹

Cognizance and Trial of the Offence of dishonour of Cheque

The Act provides that no court inferior that of a metropolitan Magistrate or a Judicial Magistrate of 1st Class shall try or take Cognizance of the offence under section 138 of the Act. It further provides that cognizance of the offence is to be taken upon a written Complaint by the payee or by the holder of due course of cheque within one month from the date on which the cheque is returned unpaid by the bank. The procedure that is followed by the concerned magistrate is that of provisions of section 262 to 265 (both Inclusive) of Code of Criminal procedure, 1973.¹² Also the offence is compoundable at any stage; the matter can be settled at any time between the parties. In case of any such settlement, an application should be moved before the court to compound and close the case.¹³

Judicial View of dishonor of Cheque

In *Lalit Kumar Sharma & Anr v State of Uttar Pradesh & Anr*,¹⁴ Two cheques were issued by the directors of a company and they were prosecuted. Meanwhile, there was a settlement under which Rs 5 lakh was to be paid to the creditor. However, this cheque also bounced, leading to another prosecution. The Allahabad High Court rejected their plea to quash the proceedings. But on appeal, the Supreme Court stated that the latter cheque was issued in terms of a compromise agreement and not to satisfy any debt or payment due. Therefore, the second instance would not invite prosecution under Section 138. The High Court judgment was set aside. In *Lakshmi Dyechem vs. State of Gujarat*,¹⁵ it was held by the court that Signature on cheque not matching with the signature in the record of the bank is treated as no different from "insufficient funds". It was observed that the expression "amount of money is insufficient" appearing in Section 138 of the Act is a genus and dishonour for reasons such "as account closed", "payment stopped", "referred to the drawer" are only species of that genus. Just as dishonour of a cheque on the ground that the account has been closed is a dishonour falling in the first contingency referred to in Section 138, so also dishonour on the ground that the "signatures do not match" or that the "image is not found", which too implies that

¹⁰ AIR 1972 (AP) 72

¹¹ Section 142, N.I Act, 1881

¹² Section 143, N.I Act, 1881

¹³ Section 147, N.I Act, 1881

¹⁴ (2008) 5 SCC 638

¹⁵ (2012) 13 SCC 375

the specimen signatures do not match the signatures on the cheque would constitute a dishonour within the meaning of Section 138 of the Act. In **MSR Leathers vs. S. Palaniappan and Anr.**¹⁶ The Supreme Court has reversed the legal principle that it had laid down in **Sadanandan Bhadran v. Madhavan Sunil Kuma**,¹⁷ that a cheque could only be presented once and the underlying principle was that a single instrument cannot lead to multiple causes of action. It was held and observed that so long as the cheque remains unpaid it is the continuing obligation of the drawer to make good the same by either arranging the funds in the account on which the cheque is drawn or liquidating the liability otherwise. It is true that a dishonour of the cheque can be made a basis for prosecution of the offender but once, but that is far from saying that the holder of the cheque does not have the discretion to choose out of several such defaults, one default, on which to launch such a prosecution. The omission or the failure of the holder to institute prosecution does not, therefore, give any immunity to the drawer so long as the cheque is dishonoured within its validity period and the conditions precedent for prosecution in terms of the proviso to Section 138 are satisfied. Reversing the decision in **Sadanandan Bhadran's** case the court stated that we have no hesitation in holding that a prosecution based on a second or successive default in payment of the cheque amount should not be impermissible simply because no prosecution based on the first default which was followed by a statutory notice and a failure to pay had not been launched. If the entire purpose underlying Section 138 of the Negotiable Instruments Act is to compel the drawers to honour their commitments made in the course of their business or other affairs, there is no reason why a person who has issued a cheque which is dishonoured and who fails to make payment despite statutory notice served upon him should be immune to prosecution simply because the holder of the cheque has not rushed to the court with a complaint based on such default or simply because the drawer has made the holder defer prosecution promising to make arrangements for funds or for any other similar reason. There is in our opinion no real or qualitative difference between a case where default is committed and prosecution immediately launched and another where the prosecution is deferred till the cheque presented again gets dishonoured for the second or successive time. In the result, we overrule the decision in **Sadanandan Bhadran's** case and hold that prosecution based upon second or successive dishonour of the cheque is also permissible so long as the same satisfies the requirements stipulated in the proviso to Section 138 of the Negotiable Instruments Act.

VI. CONCLUSION

The system of Cheques is a matter of concern for everybody whether one is a layman, a business magnate, an industrialist, a banker or a member of the bench or bar. The offence under section 138 of the Act could be visited with imprisonment up to two years and with a fine up to twice the amount of the cheque

¹⁶ (2013) 10 SCC 568

¹⁷ 1998 (6) SCC 514