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Penalties in Case of Dishonour of Cheques for Insufficiency of Funds in the Account

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ABSTRACT

Sections 138 to 148 of the Negotiable Instruments Act deal with the dishonour of cheques and the compensation that would be awarded to the payee. The researcher is interested in researching the penalties in case of dishonour of cheques for insufficiency of funds in the account. Negotiable instruments have been used since the evolution of the transfer of money. When cheques were issued as negotiable instruments, they would sometimes bounce due to insufficiency of funds. To make the drawer liable for bouncing of cheques and to ensure they pay adequate compensation, Sections 138 to 148 of the Banking, Public Financial Institutions and Negotiable Instruments Laws (Amendment) Act, 1988 were inserted. The researcher seeks to enlighten the significance of these sections by elaborating them with case laws and amendments briefly.

Keywords: *Dishonour, Cheque, Interim Compensation, Summon, Affidavit, Prima Facie Evidence.*

I. INTRODUCTION

A negotiable instrument is a transferable instrument by mere endorsement and delivery. The word negotiable is derived from the French term "negoce," which means business, trade, or management of affairs. Black's Law Dictionary defines a negotiable instrument as "legally capable of being transferred from one person to another by mere delivery and endorsement." Both endorsement and delivery are essential in the case of the transfer of a negotiable instrument.

Section 13 of the Negotiable Instruments Act, 1882, states that a "negotiable instrument" means a promissory note, bill of exchange, or cheque payable either to the order or bearer. A negotiable instrument is said to be payable to order when it is specified to be paid to a particular person and does not prohibit transfer. A negotiable instrument is payable to bearer when it is expressed to be so payable, and the only or last endorsement is an endorsement in blank.

A negotiable instrument must be in writing, signed by the drawer, drawee, or payee, whomever is necessary, and must be capable of transferring from one person to another. Transfer can be

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made any number of times. The holder must be free from all defects, except in the case of a holder in due course holding the instrument. The instrument must be an unconditional order and must pay a certain sum of money only. The sum payable must be certain. The date and signature of the drawer, drawee, or payee are essential.

Section 138 deals with the dishonour of cheques alone and not any other negotiable instrument.

II. DISHONOUR OF CHEQUE FOR INSUFFICIENCY OF FUNDS

1. Punishment and compensation in case of dishonour or bouncing of a cheque is mentioned in Section 138 of the Negotiable Instruments Act.
2. When a person draws an amount by cheque from an account maintained by him with a banker for payment of a certain sum of money either wholly or in part for the discharge of debt or liability, and
3. The cheque is returned unpaid due to insufficiency of funds or it exceeds the amount arranged to be paid from the account by agreement with the bank.
4. When the cheque is bounced due to these reasons, it is an offence punishable with imprisonment of up to two years or with a fine that may extend to twice the amount of the cheque.

(A) Conditions to be fulfilled before filing a suit under section 138:

1. The cheque must be drawn within six months from the date it was issued or within its period of validity.
2. The payee or holder in due course should inform the drawer of the dishonour within 30 days by issuing a notice after the cheque is returned unpaid.
3. The drawer should have failed to pay the money within 15 days of receiving such notice.

(B) Protection of holders' rights:

1. Presumption in favour of the payee or holder in due course is mentioned under Section 139 of the Negotiable Instruments Act.
2. It is presumed, unless proven otherwise, that the payee or holder in due course received the cheque as provided under Section 136.
3. The burden of proof lies on the drawer to prove that the dishonour was unintentional.

(C) Defence of drawer:

1. The drawer cannot claim defence under Section 138 by stating that he had no knowledge

or reason to believe that the cheque would be dishonoured.

2. Section 140 of the Negotiable Instruments Act does not provide any defence for the drawer to withhold liability for an offence punishable under Section 138.

(D) Offences by companies:

1. Offences committed by companies under Section 138 are dealt with in Section 141 of the Negotiable Instruments Act.
2. Every person in charge of and responsible for the conduct of business at the time the offence was committed shall be found guilty and liable to be punished accordingly.
3. A person who took due diligence to prevent the offence or had no knowledge of the offence will be excluded from liability.
4. A director nominated by virtue of holding office in the central or state government or a financial corporation owned or governed by the central or state government will not be liable for an offence committed under this Act.
5. Section 141(2) states that if the offence under Section 138 is committed with the consent or connivance of or is attributable to the negligence of any director, manager, secretary, or officer of the company, they shall be guilty and punished accordingly.

(E) Cognizance of offences:

1. **Cognizance of an offence under Section 138** is dealt with in Section 142 of the Negotiable Instruments Act.
2. In spite of the provisions contained in the Criminal Procedure Code, 1973:
 - (a) A court shall take cognizance of an offence punishable under Section 138 only when the payee or holder in due course has made a complaint in writing.
 - (b) The complaint should be made within 1 month from when the cause of action arises, as provided under Section 138(c).
 - (c) Any court inferior to the position of a Judicial Magistrate or Metropolitan Magistrate shall not deal with dishonour of cheque cases, an offence punishable under Section 138.
3. **Under Section 142(2)**, the offence under Section 138 will be investigated and tried only by a court within the jurisdiction of the area where:
 - (a) The cheque is deposited through an account in the branch of the bank where the payee or holder in due course maintains an account.
 - (b) If the cheque is presented for payment in any other way, the court with jurisdiction is where

the bank branch of the person who wrote the cheque is located.

Section 142 as amended by the Amendment Act of 2015:

1. Where the cheque is delivered for collection through an account — the court where the payee maintains the account will have jurisdiction.
2. Where the cheque is presented for payment by the payee otherwise through an account — the court where the drawer maintains the account will have jurisdiction.

(F) Validation of transfer of pending cases:

1. According to **Section 142A(1)**, in spite of any provisions contained in the Criminal Procedure Code, judgments, orders, or directions from any court, all cases that have been transferred to the appropriate court under **Section 142(a)** of the **NI Act, 2015** are considered to have been transferred according to the **NI Act, 1881** as though this amendment has always been in effect.
2. **Section 142A(2)** states that irrespective of **Section 142(2)/(1)**, where the payee or holder in due course filed a complaint against the drawer for an offence committed under **Section 138** in the court having jurisdiction under **Section 142(2)**, and the case was transferred under **sub-section 1** and such complaint is pending before the court, all the subsequent complaints shall be filed before the same court, irrespective of whether the cheques were delivered for collection or presented for payment within the jurisdiction of the court.
3. **Section 142(3)** states that after the commencement of the **NI Act, 2015**, if more than one case has been filed by the payee or holder in due course against the drawer in multiple courts regarding the same issue and this has been brought to the knowledge of the court, the court shall issue a notice to transfer all the cases to the court where the first case was filed, or under **Section 142(2)** as amended by the **NI Ordinance Act, 2015**.

(G) Power of courts to handle cases by summary trial:

1. **Section 143(1)** states that irrespective of the Criminal Procedure Code, every offence committed under **Section 138** shall be dealt with by the first judicial magistrate or metropolitan magistrate, provided that:
 - The magistrate, in a summary trial, cannot pass a sentence of imprisonment exceeding 1 year or a fine of more than five thousand rupees.
 - If the magistrate in a summary trial feels that imprisonment of 1 year or a fine

of up to five thousand rupees is not sufficient, the magistrate shall hear the parties, record an order, recall any witness, and proceed to hear or rehear the case as per the said code.

2. **Section 143(2)** states that the case shall proceed on a day-to-day basis until the court finds it necessary to adjourn the trial beyond the following day, with the reason for adjournment recorded in writing.
3. **Section 143(3)** states that every trial should be disposed of within 6 months from the date of filing of the complaint.

(H) Power of court to direct interim compensation:

1. According to **Section 143A(1)**, irrespective of the provisions contained in the Criminal Procedure Code, the court may direct the drawer to pay interim compensation to the complainant:
 - In a summary trial or summons case, if the accused pleads not guilty of the offence, and
 - In any other type of case when formal charges are framed against the accused.
2. **Section 143A(2)**: The interim compensation should not exceed 20% of the amount of the cheque.
3. **Section 143A(3)**: The interim compensation should be paid within 60 days of the order, with an extension of not exceeding 30 days if directed by the court for sufficient cause shown by the drawer.
4. **Section 143A(4)**: If the drawer is acquitted, the complainant should repay the interim compensation, including interest at the bank rate set by the RBI at the start of the financial year. Repayment must be made within 60 days of the order. If the complainant shows valid reason, an extension of 30 days may be granted.
5. **Section 143A(5)**: The interim compensation may be recovered as a fine under **Section 421** of the Criminal Procedure Code.
6. **Section 143A(6)**: The amount of fine imposed under **Section 138** of the **NI Act** or compensation provided under **Section 357** of the **CrPC** shall be reduced from the amount paid or recovered as interim compensation under the Act.

(I) Mode of service of summons:

1. According to **Section 144** of the Negotiable Instruments Act, irrespective of the

provisions contained in the Criminal Procedure Code, the magistrate must issue a summons to the accused or witness at their place of residence, place of business, or where they personally work for gain. The summons shall be sent by speed post or by courier services approved by the court.

2. If the court receives proof from either the accused, a witness, or someone authorized by the postal or courier service that the accused or witness refused to accept the summons, the court may consider that the summons has been duly served.

(J) Evidence on affidavit:

1. According to **Section 145(1)**, irrespective of the provisions contained in the Criminal Procedure Code, the complainant may submit evidence through an affidavit, and subject to certain exceptions, this shall be used during inquiry, trial, or other proceedings under the said code.
2. According to **Section 145(2)**, the court has the authority to examine the prosecution or the accused and call or inquire into the facts mentioned in any written statement by anyone who has provided evidence.

(K) Prima Facie Evidence:

1. According to **Section 146**, the court shall assume, upon the production of a bank slip or memo with an official mark denoting the cheque dishonoured, that the cheque is dishonoured unless the fact is disproved.
2. According to **Section 147**, irrespective of the provisions contained in the Criminal Procedure Code, every offence committed under **Section 138** shall be considered a compoundable offence.

(L) Appellate court's authority to order payment of fine or compensation while an appeal against conviction is in process:

1. According to **Section 147** of the Negotiable Instruments Act, irrespective of the provisions in the Criminal Procedure Code, in an appeal by a person convicted under **Section 138**, the appellate court has the authority to order the deposit of at least 20% of the fine or compensation imposed by the trial court. The amount payable shall be in addition to the interim compensation paid by the appellant under **Section 143A**.
2. According to **Section 147(2)**, the compensation amount should be paid within 60 days. In exceptional cases, a further extension of 30 days may be granted to the appellant.
3. According to **Section 147(3)**, the appellate court may withdraw the liability of the

complainant while the appeal is still ongoing. If the appellant is acquitted, the complainant must repay the interim compensation, which includes interest at the bank rate set by the RBI at the start of every financial year. This must be done within 60 days of the order. If the complainant shows a valid reason, an extension of 30 days may be granted.

(M) Reasons for dishonour:

1. Insufficiency of funds
2. Amount exceeds the amount mentioned in the agreement
3. Refer to drawer
4. Funds expected
5. Account closed
6. Stop payment

(N) Reasons which do not attract section 138:

1. Technical reasons such as irregularity in endorsement or structural discrepancy in the cheque
2. Signature variation/incomplete signature
3. When the cheque is found mutilated, torn, or pasted
4. A stale cheque that can be returned unpaid by the banker
5. Postdated cheques that are returned
6. Where the banker has received a garnishee or other legal order attaching or otherwise dealing with such money, the cheque may be returned unpaid

III. CASE LAWS

1. **K. Bhaskaran v. Shankaran:** Offences related to dishonour of cheque cases can be filed in the following places:
 1. Where the cheque is drawn
 2. Where payment had to be made
 3. Where the cheque is presented for payment
 4. Where the cheque is dishonoured
 5. Where notice is served to the drawer

2. **Dalmia Cement Ltd. v. Galaxy Traders and Agencies Ltd.:** The case involved a bounced cheque, and the complainant issued a notice to inform the accused. However, by the time the notice was received, the deadline for filing a complaint had passed. This situation occurred twice, with the accused failing to pay the required amount both times. The Court ruled that **Section 138** was created to protect the legal rights of individuals who are not paid on time. If someone cannot receive payment due to such issues, the section must be enforced to ensure the law's purpose is upheld. As a result, the Court ordered actions against the accused, as per the provisions of the Act.
3. **Vinod Tanna:** This case ruled that a cheque returned unpaid by a bank due to a missing signature from the drawer is not an offence under **Section 138**.
4. **Dashrath Rupsingh Rathod v. State of Maharashtra (2014):** The Supreme Court interpreted **Section 138** of the Negotiable Instruments Act regarding cheque dishonour and laid down the following points:
 1. The offence punishable under **Section 138** should have occurred.
 2. A written complaint should be filed by the payee or holder within one month from the date the cause of action arises under **Section 138**.
 3. **When the Cause of Action Arises:** (a) The cheque must be presented to the bank within three months of its issue.
(b) The complainant must demand payment within 30 days of receiving notice of the cheque's dishonour.
(c) The drawer must fail to pay the cheque amount within 15 days of receiving the notice.
 4. The events that trigger the cause of action (dishonour, demand, non-payment) do not, by themselves, constitute the offence under **Section 138**.
 5. Criminal proceedings and court action are delayed until the cause of action fully arises as defined.

IV. CONCLUSION

Sections 138 to 148 of the *Negotiable Instruments Act, 1881* form the backbone of legal provisions dealing with the dishonour of cheques. **Section 138**, in particular, has revolutionized the commercial world by embedding a sense of accountability in financial transactions, ensuring the integrity of cheques as a mode of payment. **Sections 139 to 148** provide necessary procedural safeguards, presumptions, and defenses for both the payee and the drawer. These

sections collectively establish a balance between ensuring the smooth flow of commerce and protecting individuals from wrongful criminal liability.

In essence, these provisions not only act as a deterrent to financial malpractice but also reinforce confidence in using cheques as a secure form of payment. The inclusion of both civil and criminal consequences ensures a robust framework, while recent amendments have sought to streamline processes and reduce delays, reflecting the dynamic nature of commercial law.
