

LEGAL ACCOUNTABILITY FOR DISHONOURING POST-DATED CHEQUE WITHOUT SUFFICIENT BALANCE

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Abstract

Issuing a post-dated check without sufficient balance in the bank account at its presentation can lead to serious legal consequences. Although post-dated cheques are widely used due to their reliability, low risk, and security, they can create difficulties when there aren't enough funds in the account when presented. To protect the interests of the payee, Sections 138 to 142 of the Negotiable Instruments Act cover the dishonour of such checks. This research paper examines the legal responsibility of dishonouring post-dated checks due to insufficient funds, analyses the relevant legal framework, discusses potential consequences, and proposes preventive measures to reduce associated risks.

Keywords: Negotiable Instruments, Banking, Cheque Dishonour, Bank Account, .

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INTRODUCTION

The term “thing” in jurisprudence refers to an object of rights, such as a negotiable instrument. It is considered a “thing” because it not only represents money but also embodies rights. When a person lawfully obtains possession of such an instrument, they acquire legal title to it. Additionally, the instrument is not affected by any defects or fraud in its source as long as its acquisition is genuine and of value.¹

Cheques are important not only for corporate entities but also for ordinary people when they receive payments such as their salaries, rent in advance, finalising business deals, or securing home loans in the form of cheques. In routine commercial dealings, transactions are not always conducted in cash. As commerce and trade continue to expand, the increasing demand for money cannot always be met with immediate cash exchange. Often, a business may not have ready cash available or may prefer not to carry large amounts of money. To address these challenges, businesses have adopted the use of negotiable instruments (NI) as substitutes for money. These instruments facilitate transactions and represent a written, unconditional order or promise to pay a specific sum of money, negotiable from one party to another by delivery or endorsement. The legal framework governing NIs in India is primarily contained in the Negotiable Instruments Act 1881², along with its subsequent amendments in 1988, 2002, 2015, and 2018. The origins of this law can be traced back to personal laws, as well as the customs and usages of merchants and traders long before the Act was passed. This framework is crucial in regulating the issuance and dishonour of post-dated cheques, particularly when there are insufficient funds in the issuer’s account, highlighting the importance of legal provisions under Section 138 of the Act.

In this context, understanding the rights and obligations of parties to a cheque is essential. The drawer of the cheque is obligated to ensure that there are sufficient funds in the account to cover the amount. The payee, on the other hand, has the right to expect payment upon presentation of the cheque. If the cheque is dishonoured, the payee can initiate legal action under Section 138 of the NIA.

Precautions while drawing a cheque include ensuring the accuracy of the date, the amount in words and figures, and the signature. It is also important to avoid any alterations or overwriting, as these can lead to the cheque being dishonoured. Similarly, precautions while receiving a

¹ LSD Law, “Things in Action.” available at: <https://www.lsd.law/define/things-in-action> (last visited on: July 15, 2024).

² Hereinafter referred as NIA

cheque involve verifying the details such as the date, the amount, the drawer's signature, and the validity of the cheque. Additionally, it is prudent to confirm that the drawer has a history of sufficient funds and to present the cheque for payment within the stipulated time frame to avoid issues related to the validity period.³

What is a post-dated check, and how does the specified date impact its validity and acceptance by the bank?

A post-dated cheque is a standard or regular cheque with a future date written on it instead of the date on which the cheque is written. The bank can only honour the cheque on or after the specified date, which can be in the future. The specified date determines the validity of the post-dated cheque.⁴

Suppose Raj has to pay a supplier INR 5,000 on 10th August for transactions he made 60 days ago. Since Raj lacks the funds to pay the supplier, he agrees to send the supplier two INR 2,500 cheques, one dated 10th September and the other dated 10th October. The supplier undertakes to hold and deposit the cheques as specified. In addition, Raj ensures the supplier that his bank will pay the cheques on the specified dates.

When Raj's PDC cheques arrive on 20th August, the supplier must not debit cash or credit accounts receivables because the dates on the cheques state that the cheques cannot be encashed before those dates. This feature allows Raj to issue a cheque but has control over when the supplier gets paid.

Validity of a post-dated cheque

Post-dated cheques, like regular cheques, are valid for three months from the date of issuance. The Reserve Bank of India reduced the validity period of all cheques from six months to three months, effective April 1, 2012. It's important to note that the three-month period is calculated based on the date of issuance, not the number of days. For example, if a cheque is issued or payable on January 1, 2024, it will be valid until March 31, 2024, regardless of the number of days in between.⁵

³ Avtar Singh, *Negotiable Instrument* (Eastern Book Company, New Delhi, 3rd Ed., 2016).

⁴ Khatabook, "All You Need to Know About Post-dated Cheques" *available at*: <https://khatabook.com/blog/what-is-post-dated-cheque-and-how-to-write-it/> (last visited on July 18, 2024).

⁵ *Ibid.*

What is a bank cheque, and how is it used in financial transactions?

A cheque is a written instruction to the bank requesting the payment of a specified sum from the account holder to the payee. Cheques are designed with specific security features to prevent forgery, and they are often customised by the respective banks with the account holder's name or number to ensure uniqueness and traceability.

Cheques are used in financial transactions:

1. Payment for Goods and Services,
2. Salary Payments,
3. Rent and Utilities bills,
4. Loan Repayments,
5. Clearing Debts,
6. Security Deposits,
7. Gifts and Donations.

OBJECTIVES

To examine the legal accountability for dishonouring post-dated cheques due to insufficient balance under Section 138 of the NIA and to propose improvements to the legal framework and preventive measures to enhance enforcement and reduce incidences of cheque dishonour.

This paper aims to investigate the legal responsibility for bouncing post-dated checks due to insufficient funds under the NIA. This study will analyse Section 138 and relevant case laws, identify challenges faced by recipients of this cheque, and propose practical precautions. Additionally, it seeks to provide policy recommendations to enhance the legal framework, ensuring better protection for recipients and creating a more secure financial transaction environment.

LEGAL FRAMEWORK: DISHONOR OF POST-DATED CHEQUES

When a bank refuses to process a cheque you have submitted, it is known as a dishonoured cheque. This rejection can occur for reasons such as insufficient balance in the account, a signature mismatch, a post-dated cheque, and several other reasons like overwriting, stale cheques, or stopping payment.

The NIA regulates post-dated cheques; according to this Act, if a post-dated check is dishonoured, it could lead to the following legal consequences:

- A fine of up to twice the amount specified on the check,
- Imprisonment for up to one year,
- And, or both of the above.

The NIA was created to define and amend the laws regarding Promissory Notes, Bills of Exchange, and Cheques. This act has been periodically amended to ensure quick resolution of cases involving the offence of cheque dishonour.

The ingredients of the offence as contemplated under the Act are as under⁶

1. The cheque must have been written to settle an existing debt or obligation. Legally enforceable debt:
2. The cheque must be presented within 3 months or before the validity period ends, whichever comes first
3. A cheque will be returned unpaid if there are insufficient funds or if it exceeds the arranged amount.
4. The fact that the cheque has been dishonoured must be communicated to the drawer within 30 days.
5. The drawer of the cheque must fail to make payment within 15 days of receiving the notice.⁷

Classification of offence

A violation under Section 138 is considered a non-cognizable offence, which means a police officer cannot arrest the accused without an arrest warrant. It is also a bailable offence. In the case of *Dasbrath Rupsingh Rathod v. State of Maharashtra*⁸, it was held that an offence under Section 138 is considered complete upon the dishonour of a cheque. However, no court can take cognisance of the offence until the complainant has a cause of action under clause (c) of the proviso, read in conjunction with Section 142.

⁶ Tejaswi Pandit “Dishonour of Cheque [S. 138 NI Act and allied sections]” available at: <https://www.sconline.com/blog/post/2019/05/07/dishonour-of-cheque-s-138-ni-act-and-allied-sections/> (last visited on July 20, 2024).

⁷ The Negotiable Instruments Act, 1881, sec. 138

⁸ 2014 (9) SCC 129

Liabilities on Dishonour of Cheques

Civil Liability: According to Section 138 of the NI Act, civil liability is imposed by requiring a fine of twice the amount of the dishonoured cheque. If the payee files a suit under Order 37 of the Code of Civil Procedure, 1908, and the judgment favours the payee, the drawer must pay the amount specified in the court order.

Criminal Liability: Section 138 prescribes punishment of imprisonment for up to two years, or a fine, or both. Additionally, the drawer of the cheque can be prosecuted under Sections 417 and 420 of the Indian Penal Code (IPC), 1860.

Judicial Interpretations and Case Law

*ICDS Ltd. v. Beena Shabeer*⁹

The Supreme Court has clarified Section 138 of the NIA, emphasising its broad scope and intent. The Court noted that the section's language is specific, beginning with the phrase "Where any cheque," and the term "any" is important, indicating that regardless of the reason, if a cheque is drawn on an account with a banker to discharge a debt or other liability, the liability under this provision cannot be avoided if the cheque is returned unpaid by the banker. The Court stressed that the clear language of Section 138 leaves no doubt that if a cheque is issued to settle a debt or liability and is dishonoured, the provisions of Section 138 apply.

*Sampelly Satyanarayan Rao v. Indian Renewable Energy Development*¹⁰

On March 15, 2001, Sampelly Satyanarayana Rao, a director of a power generation company and Indian Renewable Energy Development Agency Limited, entered into a loan agreement for Rs. 11.50 crores for a Biomass Power Project. According to clause 3.1(iii) of the agreement, the appellant was required to issue post-dated cheques as security for the repayment of loan instalments, including both principal and interest. However, the post-dated cheques were dishonoured, leading to a complaint filed by the respondent.

The main legal question was whether the dishonour of post-dated cheques issued as security for a loan would fall under the provisions of Section 138 of the NIA.

⁹ (2002) 6 SCC 426

¹⁰ (2016) 10 SCC 458

The Supreme Court ruled that the applicability of Section 138 of the Act depends on whether the post-dated cheques were issued for the discharge of a legally recoverable debt or liability on the specified date. The Court clarified that even though the cheques were described as “security” under the loan agreement, they were actually issued to cover the repayment of the outstanding loan instalments.

The Court stated that once the loan was disbursed and instalments became due on the specified dates, the dishonour of such cheques falls under Section 138 of the Act as they represent the outstanding liability.

*Indus Airways (P) Ltd. v. Magnum Aviation (P) Ltd.*¹¹

In the *Indus Airways* case, it was determined that the dishonour of a post-dated cheque did not fall under Section 138 of the NIA. This was because the purchase order for which the cheque was issued had been cancelled, and therefore, the cheque did not represent any existing outstanding liability or debt. In this context, a post-dated cheque is not considered an offence under Section 138 if it does not correspond to a legally enforceable liability or debt.

In contrast, the present case involves post-dated cheques issued as “security” for a loan. Despite being termed as security in the loan agreement, the primary purpose of these cheques was to repay the loan instalments, thereby satisfying the outstanding liability. The Court distinguished between a cancelled purchase order transaction and a valid loan transaction where the loan was disbursed, and repayment was due on the date of the cheque. The Court held that Section 138 is applicable in the latter scenario because the dishonoured cheques were intended to discharge a legally enforceable debt.

Precautions to take while writing a Cheque

1. Upon receiving your chequebook, verify the number of cheque leaves. If there is any discrepancy, inform the bank immediately.
2. Always keep your chequebook secure and never leave it unattended. Store it in a safe, locked place.
3. Never sign blank checks. Ensure you fill in the date, recipient’s name, and amount before signing.
4. When appropriate, cross your check to prevent misuse.

¹¹ (2014) 12 SCC 539

5. Never issue blank cheques under any circumstances to prevent the risk of cheque bounce.
6. After filling in the recipient's name, amount, and any other open spaces, draw a horizontal line to prevent unauthorised alterations.
7. If corrections are needed, clearly cross out the error and sign the correction. However, it is better to use a new cheque instead of making multiple changes on one.
8. When cancelling a cheque, invalidate it by drawing a line across the face and writing "CANCEL" on it.
9. Always store your chequebook and bank cards separately to improve security.
10. Properly destroy all cancelled cheques.
11. Avoid issuing a post-dated cheque.

Precautions to take when receiving a cheque

1. Only accept a cheque or banker's draft from someone you know and trust, especially for high-value transactions.
2. Do not accept cheques written in pencil.
3. Ensure that the cheque is accurately dated and fully completed.
4. Do not accept cheques that show any signs of alteration.
5. Avoid accepting post-dated cheques or agreeing to hold a cheque for future deposit.
6. Be cautious with single or loose cheques that are not part of a complete cheque book.
7. . Store received cheques in a safe place and deposit them into your account as soon as possible.
8. Deposit your cheque within six months of its date, as it becomes stale and may not be honoured by the bank after that period.
9. If you receive a cheque for more than the agreed amount when selling an item, do not transfer the excess amount to the buyer or release goods until you are sure the cheque or draft is genuine and has been cleared.

Implications of the New Law

The new law introduces several significant changes for both businesses and individuals in India:

1. Accelerated Case Resolution: Cases will now be resolved within six months, providing quicker relief for cheque bounce disputes.

2. Enhanced Flexibility: Filing cases can now be done at either the place where the cheque was issued or where the complainant's bank branch is located, offering greater convenience.
3. Compounding of Offenses: This provision aims to ease the court's workload and expedite resolutions through settlement options.
4. Tougher Penalties for Repeat Offenders: Stricter penalties for repeat offenders deter future cheque bounce incidents and reduce their overall frequency.

CONCLUSION

The dishonouring of cheques is a significant issue in financial transactions involving negotiable instruments. As this problem has become more prevalent in legal settings, the law has evolved rapidly to address various aspects of cheque dishonour. According to the NIA, the drawer of a cheque can be held liable for dishonouring it, even if they were initially unaware of insufficient funds in their account. The law outlines a reasonable timeframe for repayment to the payee, and failure to rectify the situation within this period is considered a criminal act, reflecting an unlawful intention to withhold payment from the rightful party.

Post-dated cheques, while useful for scheduling or deferring payments, must be issued with full awareness of the account balance to avoid legal repercussions. Recent developments in the law offer faster resolution and stricter penalties for repeat offenders, aiming to enhance accountability and reduce the frequency of such cases.

To mitigate the risks associated with cheque dishonour, both businesses and individuals should take proactive measures. Maintaining a sufficient balance, carefully verifying cheque details, keeping track of issued cheques, and considering alternative payment methods, such as online transactions, can significantly reduce the likelihood of cheque bounce incidents. By adhering to these precautions, parties can ensure smoother and more reliable financial transactions while aligning with the legal expectations set forth by the NIA.

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