

Criminalizing Cheque Bounce Cases – An effective remedy?

Centre for Civil Society

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The criminalization of writing cheques without sufficient balance was introduced in India in 1988. It was an addition to a much older British law called the Negotiable Instruments Act, 1881. The reason for the amendment was the endemic problem of cheques being dishonored. This had made it difficult to do transactions where payment and delivery didn't happen instantaneously. Mistrust of cheques was encouraging cash transactions with consequent problems of counterfeiting, costs of storing and moving cash, and the law enforcement problems of an underground economy (Shubho Roy a). It was based on the report of the committee on banking laws by Dr. Rajamannar, submitted in 1975, which suggested, inter alia, penalizing the issuance of cheque without sufficient funds (Sandeep Jalan a).

Usually the time prescribed by the Act for fast disposal in Section 138 matters is 6 months (S. 143 N.I. Act, 1881) but unfortunately the matters are not disposed within the said timeframe as the courts are flooded with matters. The minimum time period for a trial to end in a cheque bounce case is 2-3 years. The other side-effect of the amendment has been the flooding of the courts with cheque bounce cases. There are an estimated 4-5 million pending cases involving the offence of cheque bounce in the country (Dhananjay Mahapatra). The report of the first phase of work done on judicial reform by Aman Satya Kachroo Trust highlights that 55 per cent of all cases registered in the Delhi High Court between 2005 and 2010 are cheque bounce cases and further that 50 per cent of the 13 lakh cases pending in the High Court are Cheque Bounce Cases. Also, the report of National Mission for Delivery of Justice and Legal Reform titled "Towards Timely Delivery of Justice to All" cites cases under Section 138 of the Negotiable Instruments Act, 1881 as one of the top bottlenecks clogging the judicial system of India (Raj Kachroo). To say that the criminalizing of cheque bounce has been successful in acting as a deterrent for future dishonoring of cheques would be an overstatement. But it has proved to be partly successful in that at least. The criminalizing of cheque bounce cases have at least deterred some to only give cheques that they are in a position to honour.

Let's first have a look at the Sections 138-142 that criminalize cheque bouncing-

Section 138

In order to draw out and say that an offence has been committed under Section 138 of the Negotiable Instruments Act, the following conditions must be fulfilled:

- Existence of a 'live account' is a necessary prerequisite, which should be in existence at the time at which the cheque is issued, in order to attract the provisions of Section 138.
- The cheque should have been given by the drawer in discharge of a legally enforceable debt or legal liability, whether in whole or in part.
- The cheque should be presented to the bank by the holder of such cheque within six months from the date mentioned on the same. The latest directive of the Reserve Bank of India provides that the validity of a cheque has been reduced to three months.
- The bank should have returned the cheque unpaid on the ground that the money in the account of the drawer is insufficient, or exceeds the credit arrangement so extended by

the bank to the drawer. The Supreme Court has given an extended meaning to this in the broadest possible sense.

- The payee or the holder in due course, as the case may be, must within thirty days from the date on which the bank has returned the cheque unpaid, make a demand on the drawer for the amount of the cheque in writing.
- The drawer thereafter should fail to make the payment of the amount of the cheque to the payee or the holder in due course, within a period of 15 days from the receipt of the above mentioned demand.
- The payee or holder in due course is mandated to file a criminal complaint in writing within a period of one month from the expiry of the above mentioned period of 15 days (Legal Era).

The insertion of the provisions criminalizing the cases of cheque bouncing was done with intent to deter people from dishonoring cheques and to ensure credibility of cheques. But with backlog of an estimated 4 million cases and minimum time frame for disposal of these cases being 2-3 years, the endeavor is fast turning to be a failure.

So, in hindsight criminalizing the practice of cheque bounce has not proved to be successful when it comes to our legal system. Obviously the lawmakers did not take into account the legal costs involved in the whole exercise. However, by this legislative fiction, the Magistrate Courts were now called upon to adjudicate private and more so plentiful and complicated commercial disputes. Therefore, the Magistrate Courts which were collapsing with over burdened cases of cheating, criminal breach of trust, theft, robbery etc. are now called upon to decide private disputes which are purely contractual in nature (Sandeep Jalan).

So we come to the basic question- what is the way forward? Should we go back to the civil suits for enforcing post-dated cheques and to the Indian Penal Code for penalizing the drawer of a dishonored Cheque? Do we really need provisions in the Negotiable Instruments Act to criminalize cheque- bouncing?

Here is a look at the other options which a holder of a dishonored cheque due to insufficient balance has against the drawer-

Arbitration

The government is mulling an amendment to the Negotiable Instruments Act that aims to make it compulsory for the disputing parties to resolve the matter through alternative dispute resolution mechanism. The use of alternative dispute resolution mechanism along the lines of Section 89 of the Code of Civil Procedure; through arbitration; conciliation; judicial settlement including settlement through Lok Adalat of mediation may be made compulsory in cheque bounce cases by making suitable amendments to the Negotiable Instruments Act (Cheque Bounce offence likely to go).

This means that the government is planning to decriminalize cases of cheque bounce and is going to make it compulsory that they be dissolved by way of alternative dispute redressal mechanism. But the fact remains that considering the huge number of pendency of cases, arbitration of cheque bounce cases won't be a mean task either.

There are very few arbitrators in India, and there is no institutional system of providing arbitration services outside larger cities. The costs of arbitration are very high in India. There is no standardized procedure in the arbitration system in India for cheque bounce cases. Evidentiary and procedural variety will lead to more challenges in appeal and increase the burden of the judiciary where every appeal will have to be checked for procedural propriety. The authority of the arbitration system is based on the efficiency of the court system. The rational violator knows that the arbitral award will go to the same over-burdened judiciary where penal costs are rarely imposed, so there will be little incentive to honour arbitration awards. So, arbitration does not come across as the most effective alternative to deal with the cases of bounced cheques unless the legislature frames rules for effective arbitration in cases involving cheque bounce (Shubho Roy).

Civil remedies

Now coming onto the civil remedies, as were present before the amendment criminalizing the cases of cheque bounce was enacted by the legislature. It means going back to the same legal system to enforce the contract. Enforcing a contract through the judiciary is a painstaking effort as it involves at an average 1420 days for resolving a contract dispute (Enforcing Contracts). The process to seek civil justice has become notoriously dilatory and recovery by way of a civil suit takes an inordinately long time. This would also mean that the deterrent effect created by the amendment would wear off and the whole purpose of the amendment would be defeated. Legal certainty regarding the costs that can be imposed on the defaulter would also be eliminated. The negotiable instruments provides for imprisonment up to two years and fine extending to double the amount mentioned in the cheque. This provides certainty to the holder of the cheque and at the same time proves to be a deterrent for the drawer. The civil remedies and criminal liability are co-extensive and not mutually exclusive. Aggrieved party can institute a civil suit along with filing of a criminal complaint against the defaulter. Hence, section 138 does not preclude the institution of a civil suit and civil remedy is always available to the aggrieved party. Therefore making the cases of cheque bounce a civil liability won't be much of a help considering the agonizing pile of cases already pending.

Criminal Penalty

Indian Penal Code contains two sections under which the holder of a dishonored cheque can prosecute the drawer. The aggrieved party can initiate proceedings under section 406 (Criminal Breach of Trust) and Section 420 (Cheating). The Supreme Court in the case of *Sangeetaben Mahendrabhai Patel Vs. State of Gujarat* (Criminal Appeal no. 645 of 2012) held that the proceedings can be initiated under both the IPC as well as the Negotiable Instruments Act. The Court said there is no double jeopardy as envisaged in Article 20(2) of the Constitution of India as the ingredients of offences in both the acts are different and hence a drawer of a dishonored cheque can be prosecuted under both the Acts (Double Jeopardy in India). This means that the criminal liability of the drawer of a dishonored Cheque exists regardless of the amendment made in the Negotiable Instruments Act criminalizing dishonored cheques. Section 138 of the Negotiable Instruments Act proves to be a boon for the holders of dishonored cheques as

there is no need to prove mens rea or intention of the holder for deciding his criminal liability under the Act. The provision also provides a fair chance to drawer by making him liable only if the cheque is for the discharge of a debt or liability. Section 138 helps to quicken the pace of criminal trial of the drawer by dishing out a summary procedure for his prosecution. The Negotiable Instruments Act in fact provides an effective and quick remedy to the holder of a dishonored cheque against the drawer. The deletion of Section 138 would either result in same workload being thrust on the criminal justice system or that the holders would no longer file a criminal complaint because of tedious and long drawn criminal proceedings. What Negotiable Instruments Act does is that it provides an alternative recourse to the aggrieved party that is both effective as well as quick. The party is free to prosecute the defaulter under IPC as well. Both the remedies are extensive and not mutually exclusive.

Practices in Other Countries

It is important to study the penalties imposed in other countries against cheque bounce offenders and analyze their effective implementation in India.

Australia

Where a cheque is dishonored, the holder may recover as damages from any person liable on the cheque, and an indorser who has been compelled to pay the cheque may recover as damages from the drawer or prior endorser:

- (a) If the cheque is dishonored in Australia:
 - (i) The sum ordered to be paid by the cheque and
 - (ii) The amount of any interest that, in accordance with the regulations, is payable in respect of that sum (Section 76, Cheques Act 1986).

Australian Legal System basically prescribes civil remedy in case of a cheque being dishonored and the person can file a civil suit to claim the damages.

United Kingdom

In United Kingdom, there is civil remedy available to the holder and he can bring in a civil suit to get the damages.

The holder may recover from any party liable on the bill, and the drawer who has been compelled to pay the bill may recover from the acceptor, and an indorser who has been compelled to pay the bill may recover from the acceptor or from the drawer, or from a prior indorser:

- (a) The amount of the bill;
- (b) Interest thereon from the time of presentment for payment if the bill is payable on demand, and from the maturity of the bill in any other case;
- (c) The expenses of noting, or, when protest is necessary, and the protest has been extended, the expenses of protest (Bills of Exchange Act, 1882).

Singapore

Singapore is the top rated country in the Doing Business Report by the World Bank when it comes to enforcing contracts. It also imposes a civil liability on the defaulting party and there is no criminal liability.

Where a bill is dishonored, the measure of damages, which shall be deemed to be a liquidated amount, shall be as follows:

- (a) the holder may recover from any party liable on the bill, and the drawer who has been compelled to pay the bill may recover from the acceptor, and an indorser who has been compelled to pay the bill may recover from the acceptor or from the drawer, or from a prior indorser:
 1. the amount of the bill;
 2. interest thereon from the time of presentment for payment if the bill is payable on demand, and from the maturity of the bill in any other case;
 3. the expenses of noting, or, when protest is necessary, and the protest has been extended, the expenses of protest.

France

France also imposes civil liability when it comes to cases involving dishonor of cheques and has a unique feature of registering prolonged and frequent offenders to a master database and banning them from issuing a cheque for 5 years. This policy has obviously shown good results as France is placed at tenth spot in the report.

The bearer may claim the following from the person against whom he exercises his right of recourse:

1. The amount of the unpaid cheque
2. Interest with effect from the day of presentment at the legal rate applicable in France
3. The costs of the protest and notices given, as well as other costs.

Within certain limits banks are free to charge their own fees for unpaid cheques. The law limits to €30 the fee for an unpaid cheque under €50 and a limit of €50 is set for an unpaid cheque over €50. There may well be other penalties in the event of further breaches.

If you fail to regularise the situation, you face the prospect of harsher treatment as your name will be added to a central register called the *Fichier Central de Chèque*(FCC) and you will then be banned from issuing cheques for 5 years. There will also be bank charges and you may be liable to a fine from the *Trésor Public* (Payment of Cheques in France).

USA

There are different laws in different states. The states impose civil as well as criminal liability. Civil liability ranges from double to treble the amount and criminal liability ranges from 1-10 years. There are different laws in different states and the laws within states also vary depending on the amount of cheque involved. Also, there is increased punishment for frequent offenders.

Criminal Penalties

Alaska- Issuing a cheque for \$25,000 or more, maximum fine of \$50,000, imprisonment up to 10 years, or both; issuing a check for \$500 or more, up to \$25,000, maximum fine of \$50,000, imprisonment up to 5 years, or both; issuing a cheque for \$50 or more, up to \$500, maximum of \$5000, imprisonment up to one year, or both; issuing a cheque under \$50, maximum fine of \$1000, imprisonment up to 90 days, or both.

Arkansas- Issuing a cheque of \$200 or less, for 1st conviction fine of not less than \$50 nor more than \$500 or imprisonment up to 30 days or both; 2nd offense fine of not less than \$100 nor more than \$1000 or imprisonment up to 90 days or both; 3rd and subsequent offenses fine of not less than \$200 nor more than \$2000 or imprisonment up to one year or both.

Georgia- Issuing a cheque for less than \$100, fine of not more than \$500 or imprisonment not to exceed 12 months or both; issuing a cheque for \$100 or more but less than \$300, fine of not more than \$1,000 or imprisonment not to exceed 12 months or both. Upon conviction, defendant is required to make restitution of the amount of the cheque together with all the costs, which are presumed to be \$20 (Bad Check Laws by States).

Best Practices- What can be the most ideal option in the Indian Context?

One of the best practices followed around the world and which can act as an effective remedy is the one followed in France. Banks usually charge a service charge when a cheque bounces but the amount is usually small and is not an effective deterrent. In France, in addition to the service charge, the banks can add a person to the central register called the Fichier Central de Chèque which is a central database of drawers who default frequently when it comes to cheques. There is also a prospect of being banned from issuing cheques for five years. This can be an effective deterrent outside law and would considerably help to reduce defaults when it comes to cheques. This can easily be replicated in India and considering the huge number of cases would prove to be quite useful. In India, the penalty that is charged by the banks is too less to be of any significance. Sample this, in State Bank of India, in case of a bounced cheque whose value is less than INR 1 Lakh, the penalty charges are a measly INR 102 and if the value is more than INR 1 Lakh, then the penalty is INR 204. Increasing the penalty along with reporting a defaulter's name to a database would prove to be an effective deterrent. This is a good alternative for an extra-legal deterrent.

Another option is to make an amendment in the law and provide for increased penalty for subsequent default by a drawer resulting in cheque bounce. In some of the states in United States of America like Arkansas, there is an increased penalty for subsequent cheque bounce by a person. The incorporation of this feature can prove to be an effective deterrent and at least would be more effective than the present penalty.

Another option that we can suggest to the government is to give powers to the banks to freeze the account of the person who has dishonored a cheque on that account. The account would be made operational only when it has enough money to pay the debt or liability of the holder

of the cheque and the debt or liability would be discharged first and only then would the account be made operational for transactions.

Another issue which needs to be resolved is that according to the guidelines of RBI, in the event of dishonor of a cheque valued at INR 1 crore and above drawn on a particular account of a drawer on four occasions during the financial year for want of sufficient funds in the account, no fresh cheque book would be issued. This needs to be changed and the banning of issuance of cheques should not be linked to amount of the cheque. The drawer should be banned from issuing a cheque regardless of the amount mentioned in the cheque.

The last and the most effective option is to replace cheques by electronic transfer of funds. The electronic transfer of funds is the most effective and efficient way of transfer of funds and the biggest plus point is that the transfer happens within seconds and the creditor does not need to go to a bank to encash a cheque to get the money. The whole exercise of issuing a cheque can be done away with by resorting to a more viable and effective mode that is electronic transfer of funds.

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