

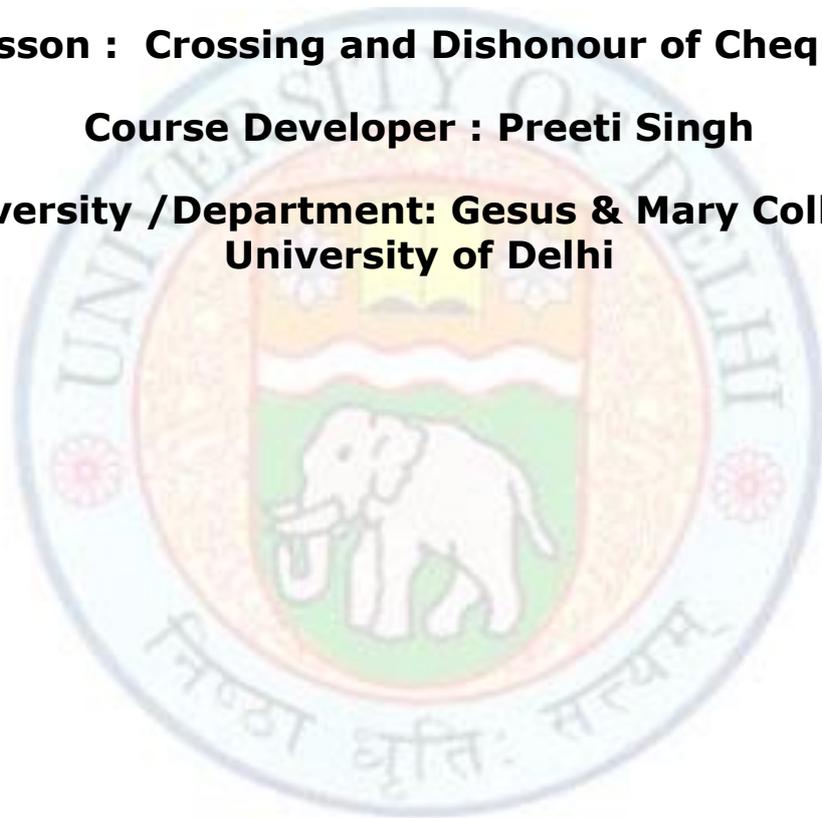
3 (D) Crossing and Dishonour of Cheques

Subject : Commerce

Lesson : Crossing and Dishonour of Cheques

Course Developer : Preeti Singh

**University /Department: Gesus & Mary College,
University of Delhi**



3 (D) Crossing and Dishonour of Cheques

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Chapter 3 (D) Crossing and Dishonour of Cheques

The scope of the Unit is given below:

- 23.1 Definition of banking, banker, customer
- 23.2 Crossing of cheques
- 23.3 Types of crossing
- 23.4 Refusal of payment by banker
- 23.5 Protection to paying banker
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23.1 Definition of Banking

Section 5B of the Banking Regulation Act defines the term banking “as accepting for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise and withdrawal by cheque, draft, order or otherwise.” A banking company is described by the Act as that company which is engaged in the business of banking in India. The banking company should accept deposits for further lending and investing the same to the public. If the company decides to accept the deposits for its own financing, it would not be called a banking company. The deposits have to be for the purpose of furthering the banking business. The banking company, in accordance with an agreement with the depositor, has to repay the money on demand to the depositor. The customer should make the demand through an order in writing by cheque or draft. The money cannot be withdrawn through orders given verbally.



Figure 23.1 Actual Performance

The relationship of banker and a customer is established through communication and interaction between the banker and the customer, involving primarily the activities of the business of banking with respect to depositing and withdrawing funds, and taking loans from the bank. Such a relationship is not established if the customer uses the services of a banker for transactions relating to en-cashing a cheque, transferring funds or using the facilities of a locker in a bank. The services are considered as additional services offered by the banker to create value to the main activity of the business of banking described above.

23.1.1 Definition of Banker

A banker is engaged in the business of banking. He accepts deposits from public and uses the funds of the public for further lending or investment. He has to honour the cheques drawn by his customer from whom he receives the money in a savings bank account, and for whom, he receives and pays money in a current account. Therefore by definition, a banker performs the functions of accepting deposits, lending and investment and repaying customers on demand or order through cheques. The banker has the following statutory obligations towards his customers:

1 Payment of cheques: Section 31 of the Negotiable Instruments Act states that if the customer has available cash balance the banker has to honour his payments. If the banker does not make the payment, the customer has the right to recover monetary loss and personal loss due to injury to his reputation.

2 Secrecy of customers accounts: A banker has to be responsible while dealing with his customer. He should not provide any information about the customer and his accounts to other people which will in any way harm his reputation. Utmost secrecy is required in maintaining the accounts of a customer.

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3 Following instructions of customer: The banker has to carry out the instructions given to him by his customer, as he is under a contractual relationship with him.

4 Record of accounts: A banker has to maintain a record of the transactions of a customer. An amount deposited or withdrawn has to be carefully recorded. Mistakes should be avoided by double checking to ensure that the customers do not suffer any losses.

23.1.2 Definition of Customer

A customer is a person, who has opened an account in a bank. He has agreed to abide the regulations and limitations of the bank. Although, there is no definition of a customer in the Act it is implied that a person, who has opened an account in a bank to engage in the business of banking is a customer. A customer can be an individual, a company, a society or a government department. A customer should have the following characteristics:

Opening an account: A person who has opened an account in his own name.

Business of banking: An individual / firm / company or association that has opened an account for carrying out the business of banking.

Relationship of banking: The relationship of the customer should be specifically towards banking business and not a personal relationship or any other social capacity.

Acceptance of services and facilities: The customer accepts the services and facilities provided to him by the banker in accordance with the banking provisions.

23.2 Crossing of Cheques

The bank allows a customer to withdraw his money from his account on demand. However, the customer has to give his order in writing through a printed cheque issued by the bank. Cheques may be open cheques or crossed cheques. The banker is obliged to pay depending on the type of cheque. Certain cheques can be handed over at the counter, and money can be received immediately. Other cheques can be more complex in nature. A cheque must be in writing with an express order to pay another party. It should be definite and unconditional order. It consists of three parties. The person, who makes the cheque, is called the drawer. The cheque is drawn on the banker, who is called the drawee, and the third party is the payee, in whose favour the cheque is drawn. The forms of different kinds of cheques are discussed below:

23.2.1. Open or Uncrossed Cheques

An open or uncrossed cheque is the one for which the banker has to pay cash across the counter, when it is presented by the customer. An open cheque is risky because, if the holder of the cheque loses it, any person, who is in possession of it, can take the payment from the bank. The payment of such cheques can be stopped by the drawer by writing a letter to the banker regarding loss of cheque. To make cheques secure and useful, crossing of cheques was adopted.

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Pay <u>Mr. Chand</u>		10-11-2008
Rupees <u>Fifty Thousand Only</u>		Or Bearer
AC No. 2010000390	LF No. 1/187	50,000/-
Syndicate Bank NFC, New Delhi		MCC 10
⑈121120⑈ 110017222		

Illustration

Sanjay gave a cheque to Mitra for Rs.12500/- on purchasing 50 metres of silk cloth. He did not cross the cheque. Mitra was traveling in a bus and a pick pocket took away his possessions and cashed the cheque over the counter at a bank. It was an open bearer cheque. Sanjay has suffered a loss. Can Sanjay recover the money?

Since the cheque was not crossed, he was not protected. He cannot recover the amount.

23.2.2. Meaning and Effect of Crossed Cheques

Crossed cheques were introduced to protect the owner of the cheque from losses due to theft of a cheque. A crossed cheque is one in which two parallel lines are drawn on the left hand top corner of a cheque. When a cheque is crossed, cash cannot be paid at the counter. It has to be paid only to the holder of the cheque who deposits it in his own account. Since a cheque is a negotiable instrument, a crossed cheque continues to be negotiable like an uncrossed cheque. The purpose of crossing a cheque is to give an order to the banker to pay the cheque only to the party, whose name has been provided in the cheque. The specimen of an uncrossed cheque is given above in figure

23.2.1. The different types of crossing and their effects on cheques is discussed in the next slide:

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Check your Progress

Cheque

**Rapid Fire
With
Multiple Choice Questions**

Start

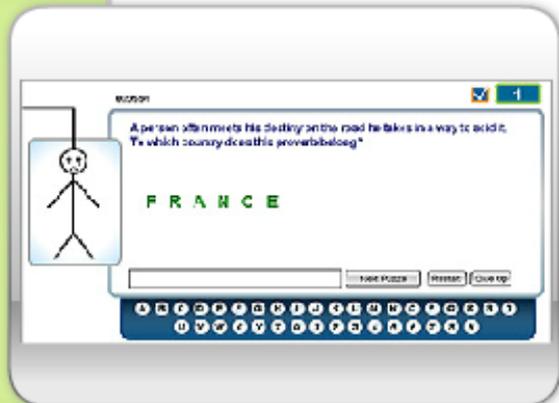


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Check your Progress

Crossing of Cheque

Welcome to Escape the Hangman. You will be given a question on-screen along with all the character spaces the answer will take. A panel at the bottom provides you with the letters of the English alphabet and numerals zero to nine. To fill in your answer, click all the alphabets or numerals in the answer, or alternatively type in the answer and click the Guess the Answer button. After your sixth incorrect entry, the hangman fills in the answer for you. If you get it right however, you're free of the noose and move on to the next question. Click Start to begin.



Start



3 (D) Crossing and Dishonour of Cheques

23.3 Types of Crossing

Crossing of cheques may be general, special or restrictive. These are explained below:

23.3.1 General Crossing

According to Section 123 of the Banking Regulation Act, 1949, a general crossing on a cheque can be made by inserting two parallel lines on the left hand top corner of a cheque. The two lines themselves show that the cheque has to be treated in a special way because something, in addition to an uncrossed cheque, has been inserted. Between the two parallel transverse lines the options are to add certain words like --- '**and company**', '**& company**' or '**not negotiable**'.

The holder of such a cheque has the right to the cheque through his own account. He can deposit the cheque, and when it is cleared, he will receive the money.

In a crossed cheque the banker, on whom the holder draws the cheque, has to pay the amount indicated on the cheque to the collecting banker. When the words 'not negotiable' are written on a crossed cheque, there is no restriction in transferring the cheque, but the rights of the transferee are acquired from the transferor. It takes the title from the endorser that may be good or defective. If the transferor has a good title, he will pass on the rights of a good title to the transferee, but if it is defective the transferee will only get a bad title. The reason for this is that the transferee cannot get a better title than the transferor of the cheque. Therefore, a non negotiable cheque is deprived of negotiability . In such a cheque, there cannot be a holder in due course. The effect of such a crossing is that there is a dilution of the essence of negotiability.

Illustration

Shivu draws a cheque of Rs. 9,500 in favour of Minu as full and final payment of his debt. He crosses the cheque by adding the words '**& company**'. Can Minu take the money from the counter in the bank by signing her name? This is a crossed cheque. Minu is required to deposit this cheque in her bank account to get the money. The amount will be credited in Minu's account.

Specimen of general crossing is depicted through a diagram:

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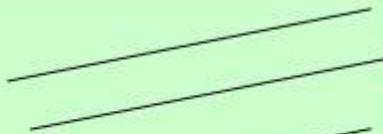
Types of General Crossing	Specimen
<ul style="list-style-type: none"> Two parallel transverse lines on cheque. 	
<ul style="list-style-type: none"> 'And company' between two parallel lines. 	
<ul style="list-style-type: none"> '& Co.' between two parallel lines. 	
<ul style="list-style-type: none"> 'Not Negotiable' between two transverse parallel lines. 	
<ul style="list-style-type: none"> 'and company Not Negotiable' crossing between two parallel lines. 	
<ul style="list-style-type: none"> '& Co. not Negotiable' written between two parallel lines. 	

Table 23.3.1 Specimen of types of general crossing of cheques

23.3.2 Special Crossing

A special crossing was introduced to provide greater protection to the drawer of the cheque. According to Section 124, "a cheque is deemed to be specially crossed when in the parallel transverse lines in a cheque the name of the banker is written with or without the words 'not negotiable'". Even two parallel transverse lines are not necessary for a special crossing. When a cheque is specially crossed, cash can be received only from the banker, whose name appears on the face of the cheque with or without the parallel lines (Section 126). The banker, collecting the cheque can authorize an agent bank to collect the funds on his behalf.

A cheque can be specially crossed in favour of more than one bank. However, Section 127 of the banking Act puts a restriction on it. In case it is necessary to put the name of two banks, the second bank should be an agent of the first bank.

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Types of Special Crossing	Specimen
Name of the bank without parallel lines.	<i>ZEE Bank</i>
Name of the bank between two parallel lines.	<i>ZEE Bank</i>
Name of the bank with the words 'not negotiable' between two parallel lines.	<i>ZEE Bank Not Negotiable</i>
Name of the bank with the words 'and Company' between two parallel lines.	<i>ZEE Bank and Company</i>
Name of a bank with the words 'not negotiable' as well as '& Co.' written between two parallel lines.	<i>ZEE Bank Not Negotiable & Co.</i>

Table 23.3.2 Specimen of types of special crossing of cheques

Illustration

Kaka draws a cheque of Rs 3500 in full and final payment of some money that of Bank Of Xena to get the money but the bank refused. Did the bank take the right action?

This was a special crossing. Accordingly only National Bank was empowered to pay the money. The bank took the right action in not making a payment over the counter.



Figure 23.2 Restrictive Crossing

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23.3.3 Restrictive Crossing

Restrictive crossing involves the crossing of a cheque through two parallel lines on the left corner of a cheque. The words A/c payee are inserted inside the parallel lines. This restriction can be made through general or special crossing. It provides a higher protection to the drawer of the cheque, in case, a cheque is misplaced or lost. According to this crossing, the cheque can be collected by the bank only for the person, whose name is written on the cheque. This crossing restricts the negotiability of the cheque because the banker cannot collect cheques on behalf of any person who is not named in the cheque. If the banker makes the mistake of collecting the cheque on behalf of a person whose name is not written on the cheque, he will not be provided with any statutory protection under section 131 of the Banking Regulation Act.

An account payee not negotiable cheque is even more restrictive because as explained a not negotiable cheque cannot give a better title to the receiver than the transferor of the cheque. If a transferee is affected by a bad title given by the transferor, he will not be able to claim the rights of a holder in due course, even if, he has received the cheque for value as well as good faith.

Types of Restrictive Crossing	Specimen
<ul style="list-style-type: none">• When the words account payee is written in a crossed cheque. It is to be credited only to the account of the payee.• Between two parallel lines the words account payee and not negotiable are added. The cheque loses its negotiability.• Two parallel lines in which the bank's name is written indicates payment in that bank only and in the payee's account.	

Table 23.3.3 Specimen of types of restrictive crossing of cheques

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Illustration

Mr. Rawat draws a cheque of Rs. 1750 in favour of Mr. Rao for purchasing books from him. He writes the words A/c payee and crosses the cheque so that the cheque is protected and received by no one but Mr. Rao. On receipt of the cheque what should Mr. Rao do? He does not know how to get his money.

This is a restrictive crossed cheque and the amount can only be credited to Mr. Rao's account. His bank will send the cheque for clearing to the drawer's bank. When it is cleared Mr. Rao's bank account will be credited with the amount and Mr. Rawat's balance will be reduced from his account.

23.3.4 Not Negotiable Crossing

A not negotiable cheque has to be carefully taken by the transferee. He must analyze and enquire about the title of the transferor before accepting the cheque. Such a cheque cannot be accepted, either in good faith, or for the value that is written on it because it has some important implications for the transferee. The transferee, as explained above, is not capable of getting a better title than the transferor, even if, he can prove that he took the cheque in good faith.



Figure 23.3 Negotiable cheque

A not negotiable cheque has important implications for the transferor also. The transferor has a greater protection with the words not negotiable written on the cheque. In case of loss in transit or misplaced cheque, it cannot be cashed by any other person than that of the person, whose name is written on it.

The banker has a responsibility attached to a 'not negotiable' crossing. He has to be careful, while presenting such cheques. He is protected under Section 128 if he Acts in good faith, honestly and without negligence. The facts of a case determine, whether the banker has acted in good faith. Bankers have to be responsible, and use a high degree of care for protecting the interest of the true owner.

The banker has a responsibility attached to a 'not negotiable' crossing. He has to be careful, while presenting such cheques. He is protected under Section 128 if he Acts in good faith, honestly and without negligence. The facts of a case determine, whether the banker has acted in good faith. Bankers have to be responsible, and use a high degree of care for protecting the interest of the true owner.

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Check your Progress

Negotiable Cheque

1. Type the correct answer for the given question.

1. A not negotiable cheque has to be carefully taken by the

2. Answer the question by clicking the appropriate check boxes.

2. Anuj crosses a cheque and marks it with the words 'not negotiable'. The cheque is to be transferred to Anil. While the cheque is transported from Gurgaon to Wazirpur, it gets lost and Manish finds it. He gives value to

Yes

No

Attempt the questions and scroll down to click the Submit button for results.

Illustration

Atul crosses a cheque and marks it with the words 'not negotiable'. The cheque is to be transferred to Amul. While the cheque is transported from Dhaula Kuan to Connaught Place, it gets lost and Bali finds it. He gives value to the cheque, and endorses it in favour of Malti. She deposits the cheque in her own bank. Her banker presents it and gets a payment from the drawee bank. Is the banker protected?

Under Section 128 and 131, the collecting bank and the paying bank are protected, but Malti has to refund the money to the owner as such a cheque is not a negotiable instrument. She cannot get a better title than Bali who has stolen, or found the cheque that does not belong to him.

23.3.5 Double Crossed Cheque

In a cheque if two special crossings are made it is called a double crossed cheque. If a banker receives a double crossed cheque with two special crossings to more than one banker, he is not permitted to make a payment as specified under Section 127 of the Act.

However, there is an exception to it. If the cheque is crossed in favour of an agent for the purpose of collecting a cheque, it is acceptable and the bank cannot refuse its payments. When two special crossings are made, the second special crossing has to be specified by stating that the crossing of cheque is in favour of the banker who is an agent for collection of the cheque and the cheque is being collected on behalf of the first

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banker. Special double crossing is usually made when a particular bank is not situated in the city where the cheque is being collected. The agent bank collects the cheque on behalf of the prime bank. A specimen of double crossing is made in the following form:

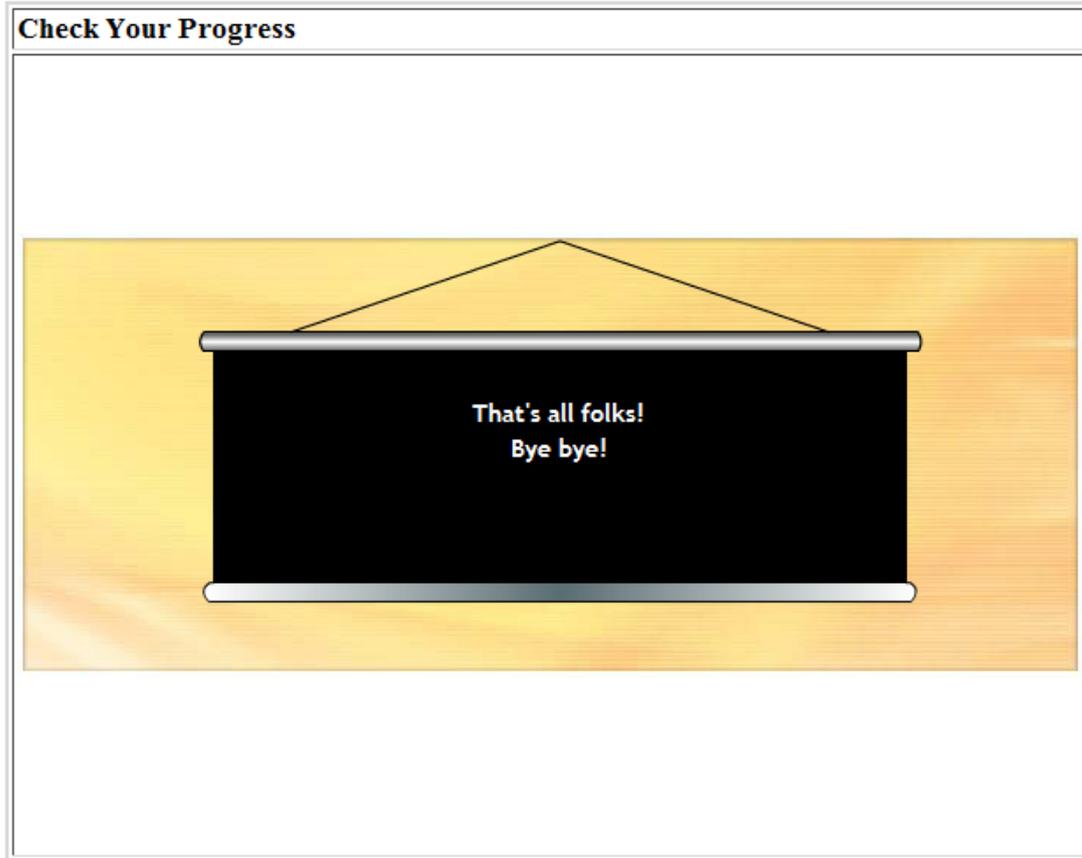
Zee Bank
To
Sonali Bank of Patiala
as agent for collection

23.3.6 Provisions for Crossing Cheques

The Negotiable Instruments Act is silent on the provision of crossing cheques. However, the prevailing practice is that the drawer of the cheque crosses it at the time of issuing it. Crossing of a cheque is considered to be a material part of a cheque, and it cannot be altered by any person except under Section 125 in the following cases:

- **Uncrossed into crossed cheques:** If the drawer omits to cross a cheque, it is possible for the holder to cross an open cheque.
- **General crossing into special crossing:** The holder has a right to make a change in the general crossing of a cheque and make it special crossing. He can also add the words not negotiable to either general or specially crossed cheques.
- **Banker can cross cheques:** The banker has a right to cross an open cheque. He can also make a generally cross cheque into a specially crossed one. He can cross the cheque specially in favour of himself or cross it specially in favour of another banker to whom he may send the cheque for collection.
- The act, however, does not permit the conversion of a special crossing into general crossing. It also does not allow any material changes on the cheque. The above explanation is illustrated in table 23.3.6

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Particulars	Right to cross a cheque.
Uncrossed cheque	The holder of the cheque can make a general or special crossing on an uncrossed cheque.
Generally crossed cheque	The holder can cross it into a specially crossed cheque. The name of the banker has to be added by him.
Cheques crossed generally or specially	The holder of the cheque can insert the words not negotiable.
Cheques crossed specially	The cheque crossed in favour of a particular banker can make another crossing in favour of another banker or his agent for collection of the amount.

Table 23.3.6 Conditions and the right to cross a cheque

23.3.7 Payment of Crossed Cheques

A crossed cheque cannot be paid over the counter. The cheque has to be collected. There is a procedure for making a payment and collecting the amount on a crossed cheque. The rules are different for payment of a crossed cheque generally and a crossed cheque specially. The procedures for the payment of different kinds of crossed cheques are explained according to the rules provided under Section 126 of the Act:

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- **Collection procedure for generally crossed cheques:** A 'generally crossed cheque' can be collected only through a banker. The paying banker does not have the right of making a payment directly over the counter. If the banker defaults in this procedure, he becomes liable to the owner of the cheque for any losses occurring to him because of the payment of the cheque to the wrong person. He cannot charge the customer with the amount paid to a person other than to whom the cheque has been given.

Illustration



Neeru draws a cheque of Rs 18000 and gives it to Ravi in full and final payment of his dues. The cheque is drawn on ICICI Bank. Ravi is the payee of the cheque. The cheque has been crossed generally. How should Ravi collect the money? In cheques crossed generally the amount cannot be paid over the counter. On receipt of the cheque Ravi must deposit the cheque in his bank. He may deposit it in his account in Punjab National Bank. The cheque will be collected and the amount will be credited to Ravi's account. At ICICI Neeru's account will be debited with the amount.

- **Collection procedure for specially crossed cheques:** The procedure for making a payment in a special crossing is that the person, who is the payee deposits the cheques in the bank. The banker requests the paying banker to make the payment. The paying banker should pay the cheque only to that banker, in whose name the cheque is crossed, or to his agent for collection of the same. Under Section 129, if the paying banker makes a default, and the payment is made by mistake to some other person, he will be liable for losses occurring out of such a transaction, and will have to make good the loss to the true owner of the cheque.

Illustration

Surya draws a cheque on State Bank of India. Nirmal is the payee of the cheque. Nirmal crosses the cheque generally to Syndicate Bank. How will the payment be collected? Surya's account in State bank will be debited only when it pays the cheque to Syndicate Bank. If Syndicate Bank cannot present the cheque to State Bank of India, because there is no branch in that area, it may cross it specially to its agent State Bank of Patiala to get the cheque collected through that bank.

3 (D) Crossing and Dishonour of Cheques

23.4 Refusal of Payment by Banker

A banker is responsible to his customers. It is necessary that he takes care to make the payments to honour the customer's account. In order to protect the customer there are certain special circumstances, where the customer is justified in not honouring the cheques of the customers. Refusal to pay cheques by the banker is in different types of circumstances. These are:

- **Conditions when banker 'may' refuse to honour cheques and**
- **Conditions when banker 'must' refuse to honour the cheques.**

23.4.1 Conditions When Banker 'may' refuse to Honour Cheques

A banker '**may**' refuse to make a payment of his customer's cheques. If he refuses a payment, he is actually making his position secure because if he pays these cheques the court has the right to determine the liability of the banker after considering the facts of the case. In the following conditions the banker has the right to 'refuse' cheques without incurring any liability:



Figure 23.4 Refusal of Payment

When cheque is post dated: In India a cheque is valid for six months from date of issue. If it is presented after the due date the banker 'may' refuse to honour the cheque.

Illustration

Meera made a cheque of Rs. 50,000 in favour of Moti on 26th March, 2008. Moti presented the cheque to his bank on October 10th, 2008. The banker refused to pay the amount because the validity of the cheque ended on 26th October, 2008 and it was considered as a stale cheque by the banker. What is the position of the banker? Since the cheque was presented after the validity date, the banker has a right to refuse payment of such a cheque.

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Check your Progress

Bankers Right

1. Ankit made a cheque of Rs. 45,000 in favour of Manoj on 26th Feb, 2009. Manoj presented the cheque to his bank on August 10th, 2009. The banker refused to pay the amount because the validity of the cheque ended and it was considered as a stale cheque by the banker.

Yes

No

Select your answers to the questions from the choices provided. Pay special attention to the feedback you receive on the right. Good luck!

Feedback:

When balance is insufficient: If a customer has an insufficient balance, and he gives a cheque to another, his banker has a right to refuse the payment if the customer does not have any overdraft facility.

Illustration

Arti gave a cheque to Shyama for Rs. 8,500. When Shyama tried to en-cash it with the banker, she was refused payment. On the cheque the bank stamped cheque returned due to insufficiency of funds. Arti had in fact, only Rs. 3,000 in her bank. Can the bank refuse payment?

The bank in such a case was perfectly justified in not honouring the cheque of the customer.

When customer has notified other commitments: If a customer of a bank has committed the funds in his account for some specific purpose and the funds are not available for honouring a new cheque, the banker may refuse to pay another cheque.

Illustration

Mona had Rs. 75,000 in her bank account. She had authorized the bank to pay Rs. 55,000 as her quarterly EMI for the house that she was purchasing. She wrote a cheque in favour of Neetu for Rs. 35,000. The banker refused to pay the amount because Mona

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had a assigned her funds for some specific purpose and the bank did not have enough funds to honour a cheque of 35,000. Should the banker have paid the amount of the cheque?

The banker has acted appropriately in not paying the amount because Mona's amount in her account had already been assigned.

When cheque is not properly presented: If a person has presented a cheque to a bank in which he does not have an account, or he presents a cheque after banking hours, it means that the cheque is not properly presented. The banker has a right to dishonour the cheque.

Illustration

Mishra presented his cheque of Rs. 15,000 to a bank at 6:30 PM in the evening. The bank manager and some staff were working on their annual reports but bank time for customers was upto 4'O clock. Mishra pleaded with the bank manager to give him money because he had to catch a train. The bank manager refused to honour the cheque because it was presented after working hours. Does he have the right to refuse payment?

The banker has a right to refuse payment on the grounds that the cheque was not properly presented.

When validity is doubtful: When a customer presents a cheque in which the amount does not match in figures and words the banker has the benefit of doubt. He may not honour the cheque.

Illustration

Mona had Rs. 75,000 in her bank account. She had authorized the bank to pay Rs. 55,000 as her quarterly EMI for the house that she was purchasing. She wrote a cheque in favour of Neetu for Rs. 35,000. The banker refused to pay the amount because Mona had a assigned her funds for some specific purpose and the bank did not have enough funds to honour a cheque of 35,000. Should the banker have paid the amount of the cheque?

The banker has acted appropriately in not paying the amount because Mona's amount in her account had already been assigned.

23.4.2 When Banker 'Must' Refuse Payment of Cheque

In the following cases the banker 'must' refuse the payment of a cheque. If the banker makes a payment he will have to bear the loss himself. If he does not honour the cheque of the customer he will have no liability against him.

Stop Payment: A customer has the right to ask the banker not to pay the cheque that he has issued in favour of another person. There may be many reasons for it. The cheque issued to another may have been misplaced or lost or stolen. In these circumstances the banker has to protect his customer. He must immediately on receiving the written instructions from his customer stop payment of the cheque. Stopping payment of cheque is also called 'countermanding the payment' by the customer or in other words issuing instructions to stop payment.

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Illustration



Neelu gave a cheque to Geeta for Rs. 8,500. She lost the cheque while going from her work place to her house and she notified Neelu. Her immediate reaction was to write to the bank to 'stop payment' of the cheque so that some person who finds the cheque does not take the cash from the bank. What should the banker do? The banker must refuse to pay as he has received 'stop payment' orders from his customer.

Death or insanity of the customer: If a customer of the bank dies and notice is given to the bank in writing, the banker should not pay any cheques. This rule is relevant even when a customer becomes insane because when he is in that state of mind he is incapable of taking any decisions. Therefore on the death or insanity of a customer the banker must refuse payment of the cheque.

Illustration

Ramu died on 21st October, 2008. Although the bank was not officially informed in writing by his family members, the bank manager saw a big advertisement stating a pooja ceremony and uthala of the person and he visited the family. When some cheques came to the bank for clearing after his death the banker refused. In this case the banker protected himself from any losses. Is the procedure correct? The banker must refuse payment of the cheques and hand over the money only to the legal nominee of his customer.

Notice of assignment: If a customer assigns his account in favour of another person and sends a notice to the banker in writing, the banker must refuse payment of the cheques from this account.

Illustration

Piya assigned her account in favour of her daughter Riya. The assignment to the account was sent in writing to the banker. When some cheques came for clearing the banker refused stating that the account had already been assigned in favour of another person. Is the banker justified in his actions?

The banker is justified. He must not honour the cheque of the customer.

Garnishee order: This is a court order to attach the balance of a customer's account. When a banker receives this notice he has to honour it. He cannot pay any cheques issued by the customer. In case he disobeys this order and makes a payment, he will not be entitled to recover that amount. He must bear any losses associated with such payments made by him.

Illustration

Ravi had a dispute with Subi regarding a property matter. The court attached the balance in Ravi's account until the dispute was cleared by the court. The balance was attached according to a 'garnishee order'. What should the banker do? The banker must

3 (D) Crossing and Dishonour of Cheques

refuse to honour the cheques of his customer because the court has issued a garnishee order.

Defective title of the holder: When a banker receives a cheque, and finds it in order, but has the knowledge that the person presenting the cheque has a defective title because he has obtained a stolen or forged cheque, he must refuse to make the payment on the cheque.

Illustration

Amit stole a cheque of Rs. 22,000 made in favour of his roommate Atul. When he presented to cheque to the bank he was refused payment because the banker knew that it was a stolen cheque. Is the banker authorized to refuse payment? The banker was authorized to refuse payment of the cheque as it had a defective title and he knew that the cheque had been stolen.

Irregularity in the cheque: The banker has a right to dishonour a cheque if any material facts on a cheque are not entered, like date, signature of the customer not tallying with the specimen signature with the bank.

Illustration

Anuj gave a cheque to Dhanur for Rs. 19,000 but the bank refused to honour the cheque because it gave the reason that it was not a valid cheque since Anuj's signature, which was given as specimen to the bank, did not match the signature on the cheque. Does the banker have the right to take such a decision?

The bank took the right decision to refuse payment on the basis of irregularity of the cheque.

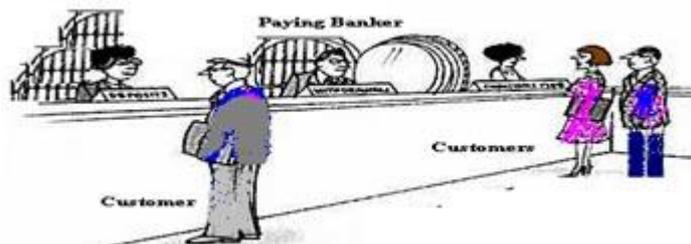
Closing of account: If a customer closes his account with a bank, the banker has a right not to honour any further cheques issued by the customer.

Illustration

After closing his account with his banker in Orissa Munish issued several cheques. The banker refused to pay the cheques issued after his customer had closed his account with them. Is the bank liable for this decision?

He stated that Munish was no longer their customer and therefore it was not his responsibility to pay any more cheques that were issued after closing his account.

3 (D) Crossing and Dishonour of Cheques



23.5 Protection to the Paying Banker

Bankers are offered special protection under the Negotiable Instruments Act for honouring the cheques of their customers in good faith and without negligence. This protection is required because the banker has a connection only with the drawer of the cheque and not the payee or other parties who are called holders of the instrument. If the banker acts in good faith, and takes special care to discharge his responsibility, he will be absolved of making a payment to a receiver of a defective title.



Figure 23.5 Protection

Protection to Banker in Case of Order Cheques Under Section 85 (1), a banker is protected against payments made by him in good faith and with responsibility, even though later on it is found that the indorsement on the cheque was forged and did not belong to the payee.

Protection in Case of Bearer Cheques Under Section 85 (2) the provision regarding protection of paying banker of bearer cheques is that he does not have to verify regularity of endorsement on the bearer cheque. The banker is discharged of his responsibility, if he makes a payment of an uncrossed cheque to a bearer in due course. The cheque may be a stolen one, but the banker will be protected because a bearer cheque always remains the same, and it does not change its legality with the number of new endorsements. Therefore, the banker is absolved of his responsibility, if he has made a payment in good faith, after taking into account all necessary precautions.

Protection in case of Forged Signature of the Drawer

The banker is not protected, if he has made a payment in due course, and the signature of the drawer is forged, and the banker makes a payment on the basis of a forged signature. In such circumstances, the banker will have to bear the losses incurred on the payment of such a cheque. However, if the banker can prove to his customer that he has not been negligent, yet he could not detect the forged signature, and made a wrong payment, he will be absolved of his responsibility. A customer should stop payment, if it comes to his knowledge that the cheque issued has been forged by entering his signature. If he does not take this important step, after coming to know of forgery, then, the banker cannot be made responsible for payment made by him.

3 (D) Crossing and Dishonour of Cheques

Protection to Collecting Banker

The banker, who makes the collection of payment on a crossed cheque, is called the collecting banker. Under Section 131, protection is granted to a collecting banker, who has carried out his work in good faith and without negligence. If a customer has collected a payment of a cheque, which is crossed generally or specially, and the cheque is found to be defective, he will be protected, if he has used full precautions, while clearing the cheque. The cheque should be crossed, when the banker receives it, and he should have collected it on behalf of his customer, or acted as an agent for another banker for collecting the payment. However the banker is not protected, if an account payee crossed cheque is credited to incorrect account, and the payee on it is forged.

Negligence of Collecting Bank

A bank has to prove that it is not negligent in order to be protected, and absolved of his liability, while collecting a cheque. In some of the following conditions, the bank will be guilty of negligence, and will not be able to get protection under Section 131.

- If a banker collects a cheque that is payable to order, but does not make enquiries, or verify the endorsements or the cheque.
- When a banker collects a cheque that is crossed account payee, and deposits it into an account, which is not that of a payee.
- If a banker collects a large amount for a customer who has a very low balance. The banker, from the very nature of his duty, should become suspicious in such cases, and verify that the cheque is not stolen or forged.
- If the cheque that is payable is collected for the private account of an official of the bank, it must be verified, otherwise the bank will be guilty.
- The collecting banker should only receive payment for his customer. He cannot get protection, if he collects a payment for an individual, who is not his customer.

3 (D) Crossing and Dishonour of Cheques

23.6 Right of Holder against Banker

If a banker refuses to pay his customer a cheque wrongfully, damaging the reputation of his customer, he will be liable to his customer, but not to the payee or holder of the cheque. Therefore, the holder is not protected against the banker because there is no privity in the contract between the banker and the holder for wrongful refusal to pay a cheque. However, there are two exceptions to this case.

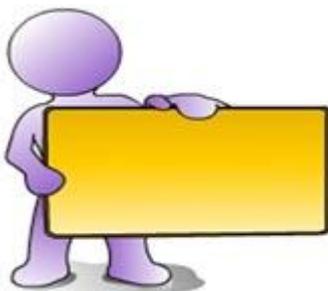


Figure 23.6 Rights of holder

Delay in presenting cheque: If a bank becomes insolvent, and the holder had delayed presenting the cheque due to which, the banker had losses, the holder becomes a creditor of the banker in its insolvency proceedings, and is able to recover the amount from the banker under Section 84.

Illustration

Manu draws a cheque of Rs. 7,500, and gives it to Sonu, who delays in presenting cheque to the bank. In the time gap the banker becomes insolvent. Manu, the drawer of the cheque is discharged from making a payment but Sonu, the holder has a right against the banker as a creditor.

Sonu should be able to prove that the bank was financially stable, when he received the cheque from Monu.

Liability for incorrect procedure in cheque payment: The banker is liable to the holder, who is the true owner of the cheque, if he pays a cheque crossed generally over the counter, or a cheque crossed specially to a banker, whose name is not written on the cheque. The banker, under Section 129 is liable for J, and he can recover the amount from the payee, if he is able to identify him.

Illustration

Reena draws a cheque in favour of Chinu. The cheque is crossed generally. The banker pays the cheque over the counter. Can the banker make a payment over the counter? The banker is liable for any losses occurring to Reena on account of making a payment over the counter instead of making the payment through the bank in a cheque crossed generally.

3 (D) Crossing and Dishonour of Cheques

23.7 Bouncing Of Cheques and Penalties to the Drawer

Bouncing of cheques is a serious offence under section 138 to 142 of the amended Banking, Public Financial Institutions and Negotiable Instruments Laws Act, 1988. This amendment was brought about to make the drawer of the cheque consider that a promise to pay a cheque is serious business. If the amount on it is not paid by the banker due to insufficiency of funds in the drawer's account, he would be penalized. This offence is punishable with imprisonment of one year and/or a fine or both extending to more than one year and up to a maximum two years with a fine of twice the amount of the cheque. Therefore when a person draws a cheque, he should keep sufficient amounts for clearing the cheque to avoid being penalized. If a person has committed an offence, he will be liable to be proceeded against and punished accordingly. However, if the drawer can prove that he did not commit the offence knowingly, and he has tried in every possible way not to inconvenience the payee, then, he will not be liable. To summarize, the following holds good if a person is found guilty of dishonouring a cheque:

Imprisonment for dishonouring cheque: Imprisonment of the drawer for a period that may extend up-to two years.

Fine for default in payment: The drawer can be fined. The fine may extend to be double the amount of the cheque.

Imprisonment and fine to drawer: The penalty to a drawer can include imprisonment and also fine that extends to double the amount of the cheque.

23.7.1 Conditions for Applicability of Section 138

The following conditions should be identified to prove that the drawer committed an offence and should be penalized:

Insufficient funds: When a banker receives a cheque, he should compare the amount drawn on the cheque with the customers credit balance and the amounts assigned by him for his various other activities. If the amount is less than the required funds, he has a right to dishonour the cheques of the drawer. When the cheque is dishonoured, the drawer will be penalized.

Insufficiency of funds is thus, recognized in the following two cases:

- The funds in the drawer's account are not sufficient for honouring the cheque, Or, if the amount is greater than the amount of balance left in the drawer's account, after paying the funds assigned by him for other purposes.

Case law1

Modi Cements Ltd. V K. K. Nandi JT 1998 (2) SC 198

In Modi Cements Ltd. V K. K. Nandi , it was held that the drawer of the dishonoured cheque had committed an offence, and shall be punished with imprisonment, which may extend upto two years, he may have to pay a fine for twice the amount to cheque or both imprisonment and fine.

3 (D) Crossing and Dishonour of Cheques

Case law 2

**KPO Moideenkutty Hajee V Pappu Manjooran
JT 1996 (3) SC 329**

In KPO Moideenkutty Hajee V Pappu Manjooran , it was held that if a cheque is dishonoured because of insufficiency of funds to the credit of the drawer. The drawer will be held responsible as a person committing an offence under Section 138.

Case law 3

**Micon Ltd. V Magma Leasing Ltd.
JT 1999 (3) SC 374**

In Micon Ltd. V Magma Leasing Ltd. , it was decided that if a cheque has been drawn, and on presenting the cheque it has been returned on the grounds of account closed it amounts to dishonour of a cheque under Section 138, making the drawer liable under an offence.

However, if the amount is dishonoured because of some technical reasons such as words in the cheque not matching the figures it will not be applicable under section.

Check your Progress

Conditions for Applicability

1. If a bank becomes insolvent, and the holder had delayed presenting the cheque due to which, the banker had losses, the holder becomes a creditor of the banker in its insolvency proceedings, and is able to recover the amount from the banker under

Submit

Next

Type the appropriate letters in the spaces with asterisks and click the Submit button to view the feedback.

3 (D) Crossing and Dishonour of Cheques

Case law 4

MMTC Ltd. V Medchl Chemicals and Pharma (P) Ltd (2002) 1 SCC 234

In MMTC Ltd. V Medchl Chemicals and Pharma (P) Ltd , it was held that if there were sufficient funds in the customer's account, but he had given a 'stop payment notice' for some important and valid reasons including that there were no existing liabilities when the cheque was presented, section 138 will not be applicable upon the drawer.

Presentation of cheque beyond validity period: A cheque should be presented within 6 months of the issue. If the date of drawing the cheque or the validity period has expired, the cheque will be dishonoured.

Discharge of legally enforced debt or liability: The drawer should have made the cheque in favour of the payee as a payment for discharge of a legally enforceable debt or liability wholly or a part of it.

Case law 5

C.V.Alexander V Joseph Chako 1995 82 comp cas 368

In C.V.Alexander V Joseph Chako , it was decided that the debt or liability to discharge a cheque that has been issued may not be only the liability as a drawer, but also as a surety of another person.

Under Section 138 of the Act, if the cheque was drawn in favour of the payee by way of

- Gift or donation, or
- Unlawful or illegal consideration, or
- Moral obligation, and it gets dishonoured, it will not be considered as an offence.

Dishonour notice to the drawer: The payee or the holder of the cheque must send a written notice to the drawer within 30 days of receiving a notice from the banker of the dishonour of the cheque, and demand the amount on the cheque from the drawer. A notice must preclude a complaint



3 (D) Crossing and Dishonour of Cheques

Case law 6

Suman Sethi v Ajay K Kejriwal 2002 (2) SCC 380

In *Suman Sethi v Ajay K Kejriwal*, it was held that a notice is legal, even though, other claims for interest, damages and other charges are inserted in it, and the drawer must adhere to it otherwise he will be considered as an offence.

Demand of Payee within 30 days of notice: Notice to a drawer is given so that he gets a chance to rectify his mistake. If the drawer fails to pay within 30 days of the notice given to the drawer that the cheque has been dishonoured, it will be considered as an offence. However, if the drawer makes the payment within the time limit, he will be absolved of his liability.

Case law 7

Paramjith Singh V N.C. job (1990) B.C. 177 Ker

In *Paramjith Singh V N.C. job*, it was held that the action should be taken only on the failure to pay the amount to the payee within 30 days of giving the notice of dishonour. Offence arises not on the date of issue of cheque, but on failure to make payment within 30 days of notice period.

Payee should give a written complaint within one month: The payee should make a written complaint within one month after the expiry of the notice period to the court under section 138 to a first class magistrate or metropolitan magistrate. A court inferior to this court cannot be allowed to try the offence. The complaint has to be filed in the place, where the cheque was presented for collection or near the business house of the payee a holder in due course. The complaint must also be forwarded with details regarding the bank and its branch on which the cheque was issued and the date and the number of the cheque when it was drawn and the reasons given by the bank for not honouring the cheque. The court also requires the date, when the payee sent a notice demanding his payment from the drawer, and if there were any replies to the demand they were to be attached.



Figure 23.7 Agreement

- Section 139 also states that the court will presume that the cheque was given for discharge of debt or liability, unless the drawer proves that it is not so. Section 140 states that a drawer will not be able to take any defence under the fact that he issued the cheque, but did not expect it to be honoured.

3 (D) Crossing and Dishonour of Cheques

Case law 8

S. Ramaswamy v K. Sudarshan Rao (1995) 83 Comp Cas 673 Mad

In S. Ramaswamy v K. Sudarshan Rao , it was held that the complaint should be within the time limit prescribed and if it is delayed, there should be a sufficient reason to explain, why the complaint was delayed in the judicial magistrate (or metropolitan magistrate) court. Further, it stated that the complaint should normally be filed by the payee, but it can also be filed by his authorized agent or power of attorney holder.

23.7.2 Documents Required For Complaint

To file a criminal complaint in the court, the applicant has to file certain documents with the complaint. The holder should attach the following documents to prove that he has not received payment:

Bounced cheque attached: The complaint sent to the court should be attached with the bounced cheque.

Bank refusal statement: The document received by the payee from the banker refusing payment of the cheque.

Legal notice: A copy of the legal notice sent to the drawer notifying him of the dishonour of the cheque requesting the amount stated in the cheque.

Receipt of notice: The registered post receipt taken from the post office for sending the legal notice of dishonour of cheque to the drawer.

Signed acknowledgement: Acknowledgement card of the legal notice signed by the drawer.

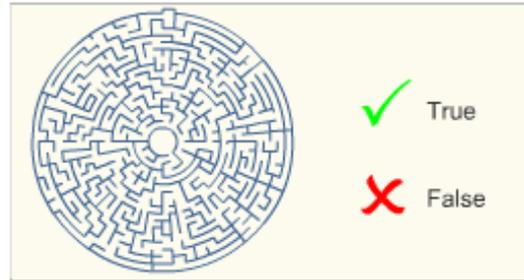
Thus the relationship of a banker and his customer is of trust and confidence. The customer and banker interaction is very important, while cheques are being issued in the course of business dealings. The banker has to create confidence in his customer and act in good faith and without negligence and protect his customer's interests.

Check Your Progress

3 (D) Crossing and Dishonour of Cheques

True or False

Start the movement of the maze object by pressing the down arrow key on your keyboard. At given intervals, barriers will block your path. They can be removed by correctly answering the given questions. Press T key if you wish to select the True option and the F key to select the False option. Click the Start button to proceed.



Start

Use the keyboard arrow keys to move in the maze and press T or F to answer the questions.



3 (D) Crossing and Dishonour of Cheques

Practical Problems

1. Ankita draws a cheque and crosses it with the words not negotiable before he gives it to Subu. The cheque is stolen and Saurab finds it and in good faith he gives value for it. He deposits the cheque in his own bank and receives the payment from the drawee - bank. What is the

Yes

No

Feedback:

Select your answers to the questions from the choices provided. Pay special attention to the feedback you receive on the right. Good luck!



3 (D) Crossing and Dishonour of Cheques

Summary

Definition Of Banking according to section 5B of the Banking Regulation Act.

- Banking means accepting for the purpose of lending or investment, of deposits of money from the public.
- They are repayable on demand or otherwise and withdrawal is by cheque, draft, order or otherwise.

Definition of Banker

- A banker is engaged in payment of cheques.
- Maintaining secrecy of accounts of their customers.
- Following customer's instructions.
- Keeping a record of customers accounts.

Definition of Customer

- A person who has opened an account in his own name.
- An individual / firm / company or association that has opened an account for carrying out the business of banking.
- The relationship of the customer should be specifically towards banking business.
- The customer accepts the services and facilities provided to him by the banker.

Crossing of Cheques- Types

- Open or uncrossed cheques
- Cheques crossed generally
- Cheques crossed specially
- Restrictive crossing
- Not Negotiable crossing
- Double crossing

Payment of Crossed Cheques

- A 'generally crossed cheque' can be collected only through a banker
- A 'specially crossed cheque' can be collected only through the banker whose name has been written in the cheque.

Refusal of Payment By Banker

Banker may refuse payment

- When cheque is post dated
- When balance is insufficient
- When customer has notified other commitments
- When cheque is not properly presented
- When validity is doubtful Banker must refuse payment
- When payment is countermanded / stop payment notice is given by the customer
- In the case of death or insanity of the customer
- When there is notice of assignment
- When Garnishee order is issued by court order to attach the balance in the customer account.
- When title of holder is defective.
- If the loss of cheque is reported.
- If there are irregularities in the cheque
- When account of customer is closed.

Protection to the Paying Banker

3 (D) Crossing and Dishonour of Cheques

- Protection is given to banker in case of order cheques if he acted in good faith and made a payment on which the indorsement was forged.
- Protection in case of bearer cheques is given to the banker if he made the cheque in good faith.
- No protection is given to the banker when drawer's signature is forged unless he can prove that he has not been negligent in his duty.

Protection to Collecting Banker

- Under Section 131 protection is granted to a collecting banker who has carried out his work in good faith and without negligence.
- Banker is not protected if an account payee crossed cheque is credited to incorrect account and the payee's signature on it is forged.

Right of Holder against Banker

- If holder delays in presenting cheque and subsequently bank becomes insolvent.
- Holder can become a creditor of the banker in the insolvency proceedings.
- Banker is liable to the holder of the cheque if he pays a crossed cheque over the counter.

Bouncing of Cheques attracts the following penalties for the drawer.

- Imprisonment for dishonouring cheque up to a maximum of two years.
- Fine for default in payment
- Imprisonment and fine to drawer

Conditions For Penalties to the Drawer (Section 138)

- Insufficient funds in the drawer's account.
- Presentation of cheque beyond validity period.
- The cheque has been drawn for discharge of legally enforced debt or liability
- Payee should make a demand within 15 days of notice.
- Payee should give a written complaint within one month

The Following Documents Required For Complaint should be attached.

- The complaint should be attached with the bounced cheque.
- The document received by the payee from the banker refusing payment of the cheque.
- A copy of the legal notice sent to the drawer notifying him of the dishonour of the cheque requesting the amount stated in the cheque.
- The registered post receipt taken from the post office for sending the legal notice of dishonour of cheque to the drawer.
- Acknowledgement card of the legal notice signed by the drawer.

3 (D) Crossing and Dishonour of Cheques

Glossary

Glossary of Legal Terms

Type the keyword to view the glossary terms.

3 (D) Crossing and Dishonour of Cheques

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