LEGALLY ENFORCEABLE DEBT OR OTHER LIABILITY UNDER SECTION 138 OF THE NEGOTIABLE INSTRUMENTS ACT: FROM STATUTORY TEXT TO JUDICIAL PRINCIPLE

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ABSTRACT

Section 138 of the Negotiable Instruments Act 1881 which is a penal provision was introduced by The Banking, Public Financial Institutions and Negotiable Instruments Law (Amendment) Act 1988, which makes the requirement of a "legally enforceable debt or other liability" an essential prerequisite to be fulfilled in case of dishonour of a cheque to attract criminal liability. This expression forms the very basis of attracting criminal liability under section 138 (subject to other conditions). Despite being the fundamental condition, it is nowhere defined in the statute to provide clarity on when a debt or liability can be said to be enforceable by law and it is because of this reason, the Judiciary takes the responsibility to construe the meaning of this abovementioned expression.

This article examines the decisions of the Supreme Court which collectively contributed to the development of this statutory expression and shows how an undefined statutory requirement changes into a well defined expression under Section 138 in a gradual manner.

The article demonstrates that the judicial interpretation of this expression resulted not only in identifying the debt which is legally enforceable and capable of attracting criminal liability but also in preserving the distinction between civil liability and criminal prosecution and finally concludes that the term legally enforceable debt or other liability is not merely an ingredient but is also the foundation upon which the entire doctrine of cheque dishonour has developed and still continues to determine the scope and limits of criminal liability under the provision.

Keywords: Section 138, Negotiable Instruments Act, Legally Enforceable Debt, Cheque Dishonour, Statutory Presumption, Criminal Liability.

1. Introduction

The legislature, by the 1988 Amendment, introduced section 138 of the Negotiable Instrument Act 1881 containing a penal provision in case of dishonour of cheques. The liability under the section does not arise immediately as dishonour of the cheque takes place but only after certain conditions are fulfilled. Out of such conditions, one is that the cheque which got dishonoured must be issued in discharge of only legally enforceable debt or liability. Though this expression "legally enforceable debt or other liability" forms the core foundation of every issue related to dishonour of cheque, the Parliament left it undefined, and therefore the responsibility shifts on the Judiciary to interpret such expression to give a practical meaning to an expression that the statute itself left undefined.

The development of this expression is not the result of a single decision of the Supreme Court but a series of them. In any case of dishonour of cheque where the issue with respect to security cheques, future and contingent liabilities, time barred debts, statutory presumptions and the burden of proof arise, the court in every such case examines different aspects of the legal enforceability of debt, clarifying the meaning and scope each time of the same statutory requirement, showing the gradual emergence of construction of a condition necessary for governing the operation of Section 138.

The article tries to map these judicial decisions that interpreted and refined this statutory requirement by first laying down the legislative foundation of Section 138, which is the purpose behind incorporating Section 138 and the significance of the initial mandatory requirement of legally enforceable debt or other liability, second by analysing the judicial decisions that shaped the meaning of the expression and third, by evaluating whether the construction of the expression legally enforceable debt and other liabilities is in line with the legislative purpose underlying Section 138.

2. Legislative Foundation

Cheques are an important payment mechanism that is used frequently for making payments especially in commercial transactions, as it provides both certainty and confidence in financial dealings. However, this certainty and confidence were diminishing due to the growing cases of dishonour of cheques. Absence of any deterrent mechanism against deliberate defaults further puts the credibility of this payment system in question. In order to prevent loss of such certainty and confidence, legislature incorporated criminal liability under Section 138 of the Negotiable Instruments Act 1881.

It was evident from the Statement of Objects and Reasons of the 1988 Amendment that the object was not merely to provide another remedy for recovering money but to ensure that the credibility of cheques and confidence in the banking system remains intact and to achieve this purpose the drawer will be made criminally liable in case of dishonour of cheques. Criminal liability was therefore introduced as a means of ensuring financial discipline. It is also important to know that Parliament did not criminalise every dishonour of a cheque but only those that fulfilled statutory conditions imposed under section 138. Among these conditions, the first requirement is that the cheque must have been issued in discharge of a legally enforceable debt or other liability.

The legislature build the section in such a manner that it not only restricts its ambit to cases where dishonour of cheque takes place with respect to debt or liability which is legally enforceable but by further use of the words ‘other liability’ along with ‘debt’ it also expanded the applicability of the section to not only with respect to discharge of monetary liability but also any other liability, whether arising from a loan, sale of goods, provision of services, hire purchase transactions, guarantees or other contractual relationships which can be legally enforceable.

From the expression “legally enforceable debt or other liability” it is clear that the legislature requires debt or other liability to be legally enforceable in order to attract criminal liability (subject to other requirements). However, it provides no information regarding the meaning or scope of it and therefore the Supreme Court takes this responsibility in hand to find out the meaning and scope of such expression which forms the subject matter of the whole discussion.

3. Judicial Development of the Expression "Legally Enforceable Debt or Other Liability"

3.1 Guarantor Cheque Case

The first important case where the court attempts to explain the meaning of the expression "legally enforceable debt or other liability" is found in ICDS Ltd. v. Beena Shabeer & Anr. In this case the principal issue before the Supreme Court was whether criminal liability under section 138 could arise where the cheque had been issued by the guarantor and not by the principal debtor.

The court observed the two expressions used under section 138 that is ‘where any cheque’ and ‘any debt or other liability’. Both expressions used the word ‘any’ which shows first that the section attracts criminal liability not only in case where dishonoured cheque was issued by the principal debtor but liability may also arise in cases where it was issued by person other than principal debtor. Thus the word any cheque means any cheque including one issued by guarantor. Second, the section is not only limited to liability of principal debtor but also of a guarantor which he undertook to fulfill in case of default by the principal debtor, provided such obligation is enforceable by law that is it must be in existence at the time of presentation of cheque.

This interpretation expanded the scope of the section beyond the identity of the principal debtor and also shifted the emphasis to the existence of a legally enforceable debt.

3.2 Security Cheque Case

The next issue before the Supreme Court was whether the mere description of a cheque as a 'security cheque' excludes the application of section 138. This issue was resolved in “Sampelly Satyanarayana Rao v. IREDA, where several post dated cheques issued as security cheques under a loan agreement got dishonoured.

The court observed that the label attached to a cheque as ‘security’ is not a decisive factor in attracting liability under Section 138 of the Act. In this case the loan amount was already given and repayment had become due. Therefore, the cheques represent an outstanding liability and would come within the scope of Section 138. The real test here is not the name attached to a cheque but the existence of a debt or other liability at the time when such cheque was presented for payment. If such cheque was presented before the due date, it cannot be said to be one legally enforceable by law.

The issue of security cheque again came before the Supreme Court in Sunil Todi v. State of Gujarat where the court reiterated what was discussed in the Sampelly case ensuring judicial consistency, and observed that the description of a cheque is not the conclusive factor in deciding liability under section 138 of the Act. There must be the existence of a legally enforceable debt or liability when the cheque was presented.

3.3 Part Payment Case

Another issue arose in Dashrathbhai Trikambhai Patel v. Hitesh Mahendrabhai Patel, where the drawer made some payment of the debt after the cheque was drawn but before it was presented. The Supreme Court held that in such a case where part payment has been made but the cheque has not been amended accordingly and represents the previous debt amount will not be considered as a legally enforceable debt. On the date of presentation of the cheque, it must represent the actual amount that remains as debt, that is the difference between original debt taken and the part payment made.

3.4 Statutory Presumption and Rebuttal of such presumption

The abovementioned cases clarified the circumstances in which a cheque could be regarded as having been issued in discharge of a legally enforceable debt or other liability. Once these principles were established, another important question arose before the Supreme Court. Since the existence of a legally enforceable debt is an essential ingredient of an offence under Section 138, how is this requirement to be proved during trial?

In Rangappa v. Sri Mohan the issue before the court was whether the presumption under section 139 of the Negotiable Instruments Act 1881 extends merely to the issuance of cheque or also to the existence of a legally enforceable debt or other liability. The court here interpreted sections 118(a), 138 and 139 together and held that once the execution or signature on the cheque is admitted or proved, the court is bound to presume that the cheque was issued for the discharge of legally enforceable debt or liability. The court further provided that section 139 raises a reverse burden of proof and once a presumption arises under it the evidentiary burden shifts to the accused. However, this reverse burden does not compel the accused rebut the prosecution case beyond reasonable doubt, but by a probable defence on the standard of preponderance of probabilities.

The court also provided that a mere denial of liability or an unsupported explanation would not be sufficient to rebut such presumption. It can be done by relying upon the evidence already produced by the complainant, by exposing inconsistencies during cross examination or by drawing reasonable inferences from surrounding circumstances.

This decision significantly strengthened the effectiveness of Section 138 by protecting the credibility of cheque transactions and preventing unnecessary obstacles for a genuine holder of the cheque.

Building upon Rangappa, the Supreme Court in Basalingappa v. Mudibasappa, summarised the principles with respect to sections 118(a) and 139 of the Negotiable Instruments Act and held that a rebuttable presumption is raised under section 139 as soon as the accused admits the execution of the cheque. This presumption does not require proof beyond reasonable doubt for its rebuttal but only needs probable defence based on preponderance of probabilities. Further when the accused raises a probable defence by questioning the financial capacity of the complainant and the surrounding circumstances make that challenge credible, the burden shifts back to the complainant to prove his financial capacity and the existence of the debt or liability.

This decision did not alter the principles laid down in Rangappa. Rather, it explained the practical operation of the statutory presumption in proceedings under Section 138. Together, they make it clear that although the law initially presumes the existence of a legally enforceable debt, that presumption remains open to challenge. Ultimately, the existence of a legally enforceable debt or other liability continues to be the foundation on which liability under Section 138 rests.

After going through various case laws, it can be said that although each case arose from different factual circumstances, the Court maintained a common approach by treating the existence of a legally enforceable liability as the primary condition to be fulfilled before attracting criminal liability under Section 138. The decisions discussed in this chapter have clarified the meaning, scope and evidentiary treatment of the expression, providing a settled legal framework for its application.

4. Contemporary Challenges in determining legally enforceable debt under section 138

4.1 Emerging Commercial Transactions

Cheques are used too frequently in commercial transactions and because of the changing nature of the commercial transaction, new challenges are emerging. Modern business involves frequent use of digital lending platforms, electronic payment systems, complex financial dealings, and hybrid contractual obligations making it difficult to determine whether a cheque was issued in discharging legally enforceable debt or not. For example, digital loan apps where repayment terms are disputed or online financing arrangements with changing repayment schedules, etc. In many cases the legal character of the transaction itself is in issue resulting in prolonged litigation before the applicability of section 138 can be determined.

4.2 Balancing Criminal Liability with Civil Disputes

Another challenge lies in maintaining a balance between preserving the credibility of cheque transactions and the need to ensure that criminal liability remains confined to cases involving genuine legally enforceable law. Section 138 was enacted to ensure that the credibility of cheques is maintained by discouraging people from issuing cheques where they lack the intention to honour them. However, it is not necessary that the accused carries this intention in every case. Sometimes parties genuinely disagree about whether any legally enforceable debt or liability actually exists or not. For example, in a case where a contract has been cancelled or amended or a debt amount has already been paid or non existence of legally enforceable liability. In such a case civil court is a more appropriate option for resolving a dispute than for criminal prosecution.

Conclusion

The continuing evolution of commercial transactions demonstrates that the concept of legally enforceable debt cannot remain static and will further evolve in future cases. While the judicial principles developed under section 138 provide a stable legal framework, their application must continue to adapt to changing commercial practices without departing from the statutory requirement that criminal liability can arise in case of dishonour of legally enforceable debt or other liability, thus preserving both the credibility of the cheque and the fairness of criminal justice system.

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