

THE TRUE PURPOSE OF SECTION 138 OF THE NEGOTIABLE INSTRUMENTS ACT, 1881, WOULD NOT BE FULFILLED, IF THE TERM 'DEBT OR OTHER LIABILITY' IS INTERPRETED TO INCLUDE ONLY A DEBT THAT EXISTS AS ON THE DATE OF DRAWING OF THE CHEQUE

INTRODUCTION:

*The Apex Court in its recent decision in **Sunil Todi and Ors. vs State of Gujarat and Anr.**¹ held that merely labelling a cheque as a security would not obviate its character as an instrument designed to meet a legally enforceable debt or liability.*

FACTS:

The Appellants are four Directors and the Managing Director of the company, R.L. Steels and Energy Limited ("**Company**").

On 19th December, 2015, a Letter of Intent was issued by the Company in favour of the Respondent No. 2 for providing uninterrupted power supply at the plant of the Company situated at Aurangabad, Maharashtra.

The Company issued a post dated cheque dated 28th August, 2017, for an amount of Rs. 2,67,84,000/- with an endorsement "*to be deposited after confirmation only for security purpose*" ("**said Cheque**").

On 24th July, 2016, the Company and Respondent No. 2 executed a Power Supply Agreement ("**said Agreement**"). The said Agreement stated that the Company would make payments to the Respondent No. 2 on the tenth day of every calendar month by way of a Letter of Credit ("**LC**").

On 10th August, 2016, 12th September, 2016, and 27th September, 2016 respectively, a total of three LCs' favouring the Respondent No. 2 were issued by the Punjab National Bank at the request of the Company.

The LCs' provided by the Company were not in the required format as sought by the bankers of the Respondent No. 2. The Company was informed of this position in an exchange of emails wherein the Respondent No. 2 alleged that the Company had failed to provide LCs in the required format. However, in spite of the correspondences exchanged, it was alleged by the Respondent No. 2 that the Company failed to provide LCs in the correct format.

On 20th October, 2016, the Company terminated the said Agreement. Thereafter, the Respondent No. 2 deposited the said Cheque on 28th August, 2017. The same was dishonoured.

On 18th September, 2017, the Respondent No. 2 issued a legal notice to the Appellants, alleging that they had committed offences under Section 138 of the Negotiable Instruments Act, 1881 ("**said Act**"). The notice stated that the Appellants had issued the said Cheque drawn on Karur Vysya Bank, Aurangabad, which had been dishonoured for the reason of '*payment stopped by drawer*'.

Thereafter, the Appellants addressed a reply dated 5th October, 2017, in response to the legal notice, stating *inter alia* that the said Cheque issued was only for the purpose of security and

¹ Criminal Appeal No. 1446 of 2021 and Criminal Appeal No. 1447 of 2021

not for encashment and therefore the same could not have been deposited in the first place.

On 2nd November, 2017, a criminal complaint was filed by the Respondent No. 2 before the Additional Chief Judicial Magistrate, Mundra, against the Appellants seeking issuance of summons and imposition of fine of Rs. 5,35,68,000/-.

The Appellants approached the High Court by filing petitions under Section 482 of the Code of Criminal Procedure, 1973 ("**the CrPC**"), for quashing of the criminal complaint.

The High Court, by its order dated 24th June, 2019, dismissed the aforesaid petitions. This order was challenged before the Apex Court.

ISSUES FOR CONSIDERATION:

The main issue for consideration before the Apex Court *inter alia* was:

Whether the dishonour of a cheque furnished as a 'security' was covered under the provisions of Section 138 of the said Act?

SUBMISSIONS ON BEHALF OF THE APPELLANTS:

The Appellant submitted that the said Cheque issued in favour of the Respondent No. 2 was intended to be a security towards payment, at all material times. This was evident from the endorsement made on the reverse of the said Cheque, and was further buttressed by the provisions of the said Agreement, that the payment was to take place by means of a LC.

It was submitted that since the said Cheque was issued by way of a security, it was never the intention for the said Cheque to be deposited.

The Appellants further submitted that recourse to the filing of a complaint under Section 138 of the said Act was an abuse of the process of law and that a clear case for invocation of the jurisdiction under Section 482 of the CrPC was justified.

SUBMISSIONS ON BEHALF OF THE RESPONDENTS:

The Respondent No. 2 *inter alia* submitted that the High Court in its impugned order dated 24th June, 2019, opined that there was no dispute to the liability of the Company, for the electricity supplied under the said Agreement during the months of August, September and October, 2016.

It was submitted that the law did not prohibit the invocation of section 138 of the said Act in a situation where cheques were issued as a security.

Therefore, there was no reason to interfere with the impugned order of the High Court.

JUDGMENT:

The Apex Court observed that the said Agreement between the parties provided that the Respondent No. 2 would supply power to the Company. The Appellants did not dispute that the power was supplied for a period of three months to the Company. Accordingly, the said Agreement was acted upon and power was supplied by the Respondent No. 2 and consumed by the Company.

The Apex Court observed that the explanation to Section 138 of the Act provided that '*debt or any*

other liability' would mean a legally enforceable debt or other liability.

Relying on a full bench judgment of the Calcutta High Court in *Banchharam Majumdar vs. Adyanath Bhattacharjee*², the Apex Court observed that the term debt included a sum of money promised to be paid at a future date by reason of a present obligation. A post-dated cheque issued after the debt had been incurred would be covered by the definition of 'debt'. However, if the sum payable depended on a contingent event, then it would take the colour of a debt only after the contingency had occurred. In the present case, a debt was incurred after the Respondent No. 2 began the supply of power for which payments were not made because of the non-acceptance of the LCs.

The Apex Court further observed that the object of the Act was to enhance the acceptability of cheques and inculcate faith in the efficiency of negotiable instruments for transaction of business. The purpose of the provision of the said Act would become otiose if the provision of the said Act was interpreted to exclude cases where debt was incurred after the drawing of the cheque but before its encashment.

The Apex Court observed that the said Cheque was issued in close proximity with the

commencement of power supply. To hold that the said Cheque was not issued in the context of a liability, as assumed by the Company, to pay the dues towards power supplied would be to produce an outcome at odds with the business dealings. If the Company failed to provide a satisfactory LC and yet consumed power, the said Cheque would be capable of being presented for the purpose of meeting outstanding dues.

The Apex Court held that once the payments for electricity supply became due in terms of the said Agreement, and the Company failed to discharge its dues, the Respondent No. 2 was entitled to present the said Cheque for payment. The Apex Court further held that merely labelling the said Cheque as a security would not obviate its character as an instrument designed to meet a legally enforceable debt or liability, i.e., once the supply of power had been provided for which there were monies due and payable.

The Apex Court dismissed the appeals holding that the same had no merits.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

² (1909) ILR 36 Cal 936