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The Liability of a Director in a Cheque Bounce Case: Reading in the Light of recent Supreme Court Judgment

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In India, mere dishonor or bouncing of a cheque is sufficient ground to initiate criminal proceedings against a defaulter according to relevant existing laws. The bouncing of a cheque is an often instance of default arising from financial obligation between individuals or business entities including incorporated companies. According to section 138 of the Negotiable Instruments Act, 1881, the cheque bounced due to insufficient funds in the bank account is a punishable offense and the act further provides provisions for extending the criminal liability against the company and its directors in case of their involvement in such offences. While observing several erstwhile cheque bounce cases where companies were involved as offenders, a persistent trend was visible, that mere invoking of the relevant sections was considered sufficient to trigger and attribute criminal liability against all the existing directors of such offender companies regardless of their role in the offence. However, in recent times, several judgements from various High courts and Hon'ble supreme court itself have retracted from such blanket attribution of criminal liability against directors in cheque bounce cases and in fact reiterated to decide their liability only according to their role in the offence not by their mere involvement by virtue of an office. More relevantly, courts are duly considering strictly construe such age-old statutes while deciding disputes involving companies to reduce impact over the ease of doing business in our country due to relentless litigations.

Keywords: *cheque bounce, director, liability.*

INTRODUCTION

In the recently adjudicated case of Ashutosh Ashok Parasrampuriya and anr v. M/s Gharrkul Industries Pvt. Ltd. and ors¹, Supreme Court has once again reaffirmed the grounds on which a Director of a company can be summoned and prosecuted for a criminal case under Section 141 read with Section 138 of the Negotiable Instruments Act, 1881. Cheque bounce is an often seen instance during the financial transactions between the parties through banks. Banks rejecting admission of cheque due to varied reasons including mismatch of signature or overwriting, and Insufficient funds, out of which cheque bounce due to the insufficient fund has been prevalent and also a grave concern of public interest. Considering the need to deter such dishonest practices, the Negotiable Instruments, 1881(hereinafter referred to as "NI Act") has made the dishonor of Cheque a punishable criminal offense (Imprisonment up to 2 years).

CHEQUE AND DISHONOR OF CHEQUE

From the layman's understanding, a cheque can be conceived as an order to the bank to pay a fixed sum to the person to whom the cheque is issued. According to NI Act, *Cheque is a bill of exchange drawn on a banker and to be payable only when demanded by the payee and also includes the electronic image of a truncated cheque and a cheque in the electronic form.*² Dishonor of a cheque is an instance when it is rejected by the Drawee bank upon which the Cheque has been submitted by the beneficiary to whom the amount is to be paid by the bank on the order of Drawer. There can be several reasons which may trigger the dishonor of a cheque by the bank considering some of the relevant reasons as follows:

- The Cheque is not duly filled or overwritten
- The Cheque is not duly signed by the Drawer
- Incomplete details of the payee/ Beneficiary
- The Insufficient fund in the Bank account of the payer

¹ *Ashutosh Ashok Parasrampuriya & Anr v M/s Gharrkul Industries Pvt Ltd & Ors*

² Negotiable Instruments Act 1881, s 6

Section 138, NI Act, 1881, dealt in detail on the matter of the Dishonor of Cheque triggered due to the lack of required funds in the bank account of the person who issues the cheque. The section stipulates certain conditions under which the triggering of an offense will be convened as follows³ :

- The cheque should be used by the beneficiary on an account of the payment in discharging of a legally enforceable debt or liability and a section specifically excludes the liability of this act over the dishonor of cheque given for the matter of gift or charity etc.
- The cheque should be presented to the bank within 6 months from the date on which it is drawn or within its validity whichever is earlier
- Upon receiving the Cheque return memo sent by the concerned bank, the Payee is required to send a legal notice to the drawer intimating the Cheque return due to insufficient funds and to pay the due amount within the stipulated time.
- And, the Drawer is failed to pay the required fund even after 15 days of the receipt of a notice from the payee.

An Incorporated company being the creation of law is a juridical person and a separate legal entity, however, the affairs of the company are attributed to a human agency. Such humans who manage the affairs of the company are referred to as the Directors and the collective management of the company by such human agency is referred to as the “Board of Directors”. Directors are the key managerial persons who manage the business and affairs on behalf of the company and they can be said to be acting alter ego of the company. According to the principle of attribution, any wrongful act done by such alter egos can be attributed towards

³ Krrishan Singhania, ‘Section 138 of Negotiable Instruments Act: Overview’ (*mondaq*, 2021) <<https://www.mondaq.com/india/financial-services/812822/section-138-of-negotiable-instruments-act-overview>> accessed 15 October 2021

the company and such company can be prosecuted for such wrongful act committed by the Directors.⁴

However, the reverse application of the principle is not permissible in general and the Supreme Court has specifically answered the question of the reverse application of the attribution of the offense by the company to its directors through the case, *Sunil Bharti Mittal vs Central Bureau of Investigation*⁵ The court has reiterated that the reverse application of the principle of the Attribution is not permissible and when the company is accused of any offence, its directors cannot be held liable except in the following two situations:-

- a) if there is sufficient incriminating evidence against their relevant role in the wrong done on behalf of the company artificial personality
- b) The statutes specifically provide for the vicarious liability of the Directors with regard to any act done on behalf of the company.

Section 141, of the NI Act, 1881, is one such statute that comes under the aforementioned exception.

According to Section 141, if the person committing the offence under section 138 is a company, every person, at the time of the commission of offence, who was in charge or was responsible to run the day to day business of the company along with any other person who is the director or secretary or other key managerial persons of the company and the Company itself will be liable for punishment.⁶ The provision relating to the Directors liability in the aforementioned situation when Company indulged in the check bounce cases has been contested in the court of law severally, to decide the circumstances in which a director is vicariously liable for such offenses.

⁴ KSR & CO, 'Vicarious Liability of Directors in Criminal Offences-When Applicable' (*ksrandco*, 2021) <<https://ksrandco.in/publications/vicarious-liability-of-directors-in-criminal-offences-when-applicable/>> accessed 14 October 2021

⁵ *Sunil Bharti Mittal v Central Bureau of Investigation* (2015) 4 SCC 609

⁶ Negotiable Instruments Act 1881, s 141

THE JUDGEMENT

On 08/10/2021, the Supreme court through its judgment on the case of Ashutosh Ashok Parasrampuriya and anr v M/s Gharrkul Industries Pvt. Ltd. and Ors, provided more clarity in the matter of Directors liability in cheque bounce cases under Section 141, read with section 138 of the NI Act. The facts of the case were that a private company incorporated under Companies Act, 1956, named Ameya Paper Mills Pvt Ltd. has borrowed an amount of Rs. 1,50,19,831 from another private company M/s. Gharkul Industries Pvt. Ltd, upon agreeing to pay back the borrowed money in a span of one or two years. Later on when the borrowed money was demanded the appellant company has issued a Cheque with a stated amount of Rs 100000, dated 2/6/2012 in favor of as part payment of the borrowed amount. However, the issued cheque has been bounced due to the lack of required funds in the account and subsequently, the respondent intimated and also demanded the cheque amount through a legal notice which the appellant didn't even consider receiving and acknowledging.

On the background of the aforesaid facts, the respondent company has initiated a criminal proceeding under section 141 read with section 138 of the NI Act, and held in the plea that the Directors of the appellant company are equally liable and responsible for the offense committed by the company. Subsequently, summon has been issued to the Directors of the company.

The two-Judge comprising Justice Ajay Rastogi and Justice Abhay S oka was dealing with the appeal against the High court order which refuses to quash the aforesaid summons. While deciding the appeal bench relied on the ratio it's judgment in the MS Pharmaceuticals Ltd. v Neeta Bhalla and Another and held that in order to assert a valid claim under Section 141, during the time when the offence was committed, the accused person by virtue of their office, needs to be in charge of the office and also responsible for the management of the business of the company. The concurrence of the commission of the offence with the accused people's

active role in the management of the company during such an event is an essential requirement to bring the matter under the ambit of Section 141.⁷

Further held that All the ex officio Directors of a company cannot be dragged into the matter under section 141, whereas the Director who sought to be liable must be in charge of the Management and responsible for the conduct of the company at the relevant time and this has to be conclusively proved since there is no such presumption for deemed liability prescribed in this statute.⁸

The Court also noted that the question of law has considered only those Directors who are not among the signatories to cheque in issue and also who is not an Executive director who would be acting on behalf of the company as a person in charge during such event. If such conditions are proved as concurrently existing, then such Directors will be liable under section 141 of the act. The court, in this case, has conclusively decided that it is necessary to state in the complaint filed under Section 141 of the NI Act, at the relevant time when the offense was committed, either Director were signatories or Director were responsible for the conduct of the business of the company.⁹

CONCLUSION

Considering the recent judgment *Ashutosh Ashok Parasrampuriya and anr vs M/s Gharrkul Industries Pvt. Ltd. and ors*, with various erstwhile relevant judgments and the relevant statutory sections, it can be summed up that, In order to attract the criminal liability over a director of a Company in a cheque bounce case arising from Section 141 of the NI Act, following conditions must be satisfied undisputedly:

- To attract the vicarious liability under the act, Director must be at the time of the offense committed, was in charge of, and was responsible to the company for the conduct of the business of the company.

⁷ *MS Pharmaceuticals Ltd v Neeta Bhalla & Anr* (2005) 8 SCC 89

⁸ *Ibid*

⁹ *Ashutosh Ashok Parasrampuriya* (n 1)

- The Director who is a signatory of the cheque or the managing director or joint managing director who are in charge of and responsible for the conduct of the business of the company, by virtue of the office they hold is undoubtedly covered as officers who are liable for punishment under the Section 138¹⁰ read with 141 of the NI Act.

The Beneficial construction of such often contested sections will not only clears ambiguities within statutes but also clears the room from unwanted attribution of criminal liability towards any innocent individuals who merely act by virtue of their office (if and only if acts in good faith).

Moreover, such reaffirmations have more relevance on the ground when the Apex court has recently expressed its grave concern over the pendency of Cheque bounce cases arising out of Section 138, NI Act and specifically noted the persistence of a worrying trend with regards to this relevant statute which is burdening the criminal justice system of our Country.¹¹ The court also observed that the unfortunate trend of a criminal complaint filed out of a Cheque bouncing instance involving business entities and it is unreasonable pending within various courts around the country have been inflicting severe blow over the ease of doing business in India.

Reading the relevant observation from the Supreme Court on the overburdening by such sections and along with recent judgements affirming the grounds on which a director of any business entity can be held liable under this act, It can be concluded that such timely interventions and beneficial constructions are the need of the hour to set the sail of such often misinterpreted criminal jurisprudences impacting the current business environment of our Country towards a shore of a business-friendly jurisprudence.

¹⁰ Negotiable Instruments Act 1881, s 138

¹¹ *M/s Gimpex Private Limited v Manoj Goel* Criminal Appeal Nos 1069-1075/2021