Unit – V

Chapter - IX

CHEQUE

OBJECTIVES

- To know the meaning and definition of a cheque
- To learn about requisites of a cheque and how to draw it
- To learn about various types of cheques
- To know the effects of alteration, marking and crossing of cheques
- To learn about various types of crossing and their implications on payment of cheques
- Endorsement of cheques and their kinds
- Legal effect of loss of cheques in transit

1. INTRODUCTION

1.1 Meaning of the term "Cheque"

Normally ***'Cheque' is a paper printed and issued by a banker*** (normally issued in the form of booklets containing 10 leaves, 20 leaves etc – called "cheque book") either ***used to withdraw money for personal use or to make trade payments or otherwise in favour of another person.***

In legal terms, cheque is a negotiable instrument. "Negotiable" means transferable. A cheque given in the name of one person can be transferred to the ownership of another person, by merely putting a signature on the backside of the cheque. The second owner can also transfer it to a third person, by putting his signature below the signature of the first owner. This process is called "Negotiation" and the instrument is called "Negotiable Instrument". A cheque is a negotiable instrument which is supplied by a banker to the customer who opens a savings or current account in a bank.

1.2 Definition of a cheque

According to section 6 of the Negotiable Instruments Act, 1881, "a cheque is a bill of exchange, drawn on a specified banker and not expressed to be payable, otherwise than on demand".

From the above definition; we come to know that,

- ***A cheque is always drawn upon a banker***
- ***It is always payable on demand***

Another definition of a Cheque

"Cheque is an instrument in writing containing an unconditional order, addressed to a banker, signed by the person who has deposited money with the banker, requiring him to pay on demand a certain sum of money only to or to the order of certain person or to the bearer of instrument."

1.3 ESSENTIAL ELEMENTS / CHARACTERISTICS OF CHEQUE

Essential characteristics of a cheque

If we take a close look at the definition of a cheque, it becomes clear that a cheque has the following 10 essential elements or characteristics.

1. ***It must be in writing:*** A cheque must be in writing. An oral order to pay does not constitute a cheque.
2. ***It should be drawn on a banker:*** It is always drawn on a specified banker. A cheque can be drawn on a bank where the drawer has an account (saving bank or current account).
3. ***It contains an unconditional order to pay:*** A cheque cannot be drawn so as to be payable conditionally. The drawer's order to the drawee bank must be unconditional and should not make the cheque payable dependent on a contingency. A conditional cheque shall be invalid. (Example: Pay only if presented by Ram in person) This is conditional. So the cheque become not valid for payment, though presented properly.
4. ***The cheque must have an order to pay a certain sum:*** The cheque should contain an order to pay a certain sum of money only. If a cheque is drawn to do something in addition to, or other than to pay money, it cannot be a cheque. For example, if a cheque contains 'Pay USD 500 and a TV worth USD 500 to A' it is not a cheque.
5. ***It should be signed by the drawer and should be dated:*** A cheque does not carry any validity unless signed by the original drawer. It should be dated as well.
6. ***It is payable on demand:*** A cheque is always payable on demand.

7. ***Validity:*** A cheque is normally valid for three months from the date it bears. Thereafter it is termed as stale cheque. A post-dated cheque will not be valid. In both cases, the validity of the cheque is presumed to commence from the date mentioned on it.
8. ***It may be payable to the drawer himself:*** Cheques may be payable to the drawer himself/herself. It may be drawn payable to bearer on demand unlike a bill or a pro-note.
9. ***Banker is liable only to the drawer:*** The banker on whom the cheque is drawn shall be liable only to the drawer. A holder or bearer has no remedy against the banker if a cheque is dishonoured.
10. ***It does not require acceptance and stamp:*** Unlike a bill of exchange, a cheque does not require acceptance on part of the drawee. There is, however, a custom among banks to mark cheques as 'good' for the purpose of clearance. But this marking is not an acceptance. Similarly no revenue stamp is required to be affixed on cheques.

1.4 More about the Cheque

A savings bank account holder may have an account "with cheque" or "without cheque" facility. But all the current account holders will be provided with a cheque book. The cheque book may consist of 10, 20, 50 or 100 printed leaves.

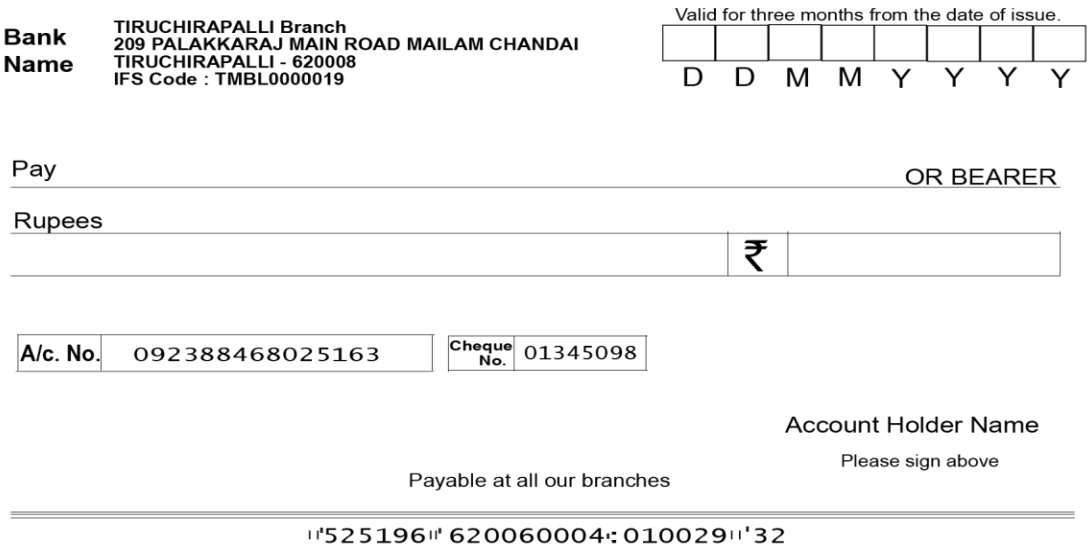
1.4.1 MICR Cheques

Now-a-days, banks supply to their customer, MICR (Magnetic Ink Character Recognition) Cheques. This means that ***cheque contains white patch at the bottom, in which numbers are given in magnetic form.*** The given numbers represent the number of the cheque, the code number of the concerned branch and the bank.

This MICR code has been given to enable mechanical sorting. Normally the MICR code line is framed in such a manner, containing the following numbers.

- The first 6 numbers signify the cheque number
- The second 3 numbers signify the city code
- The third 3 numbers signify bank code
- The fourth 3 numbers signify the branch code of the bank

1.4.2 Specimen of a Cheque



1.4.3 A Cheque payment involves three parties:

- ***The drawer of the cheque*** – Bank Account Holder
- ***Drawee of the cheque*** – on whom the cheque is drawn. It is the bank branch which has issued the cheque book. That bank branch, ultimately pays the cheque.
- ***Payee of the cheque*** /
  Beneficiary of the cheque - The person to whom the amount of cheque is paid.

2. REQUISITES OF A CHEQUE:

Form of the Cheque: A cheque can take the form of an order written on an ordinary piece of paper. But generally the banks will supply printed cheque forms to the customer while opening the account and the customers as a rule must use only the printed cheque forms supplied only as that rule, if the order is made on piece of paper the bank will refuse payment.

Issue of Cheque: A cheque is said to be issued when the drawer parts it to another person. The issue of cheque is very important because the drawer is not liable on a cheque until he has issued it. Even if drawer is induced by fraud, it is deemed to be duly issued.

Dating of Cheque: A cheque is not invalid simply because it is not dated. But dating of a cheque is essential to find whether it is stale cheque or not. A stale cheque is one which is not presented for payment before three months from the date of issue of cheque.

2.1 Drawing of a Cheque

If the drawer makes the cheque properly and if the balance of the drawer at the bank permits, the bank must pay the amount of cheque as soon as it is presented. If the drawer does not make the cheque properly, the bank rejects payment. Hence, to make the cheque properly, the following points or rules must be considered.

1. ***Date:*** Date should be mentioned on the cheque properly. If the cheque is more than three months old or contains future date then the bank will not pay the amount.
2. ***Name of the Payee:*** The name of the payee should be mentioned on the cheque.
3. ***Amount of the Cheque:*** The amount of the cheque should be mentioned both in words and figures clearly. The amount written in the word should tally with the amount written in figures.
4. ***Signature:*** The drawer should sign the cheque properly. The signature given on the cheque should tally with the signature given on the signature specification card. The signature specification card is kept by the bank.
5. ***Account Number:*** The drawer should mention his account number clearly and correctly.
6. ***Minimum Balance:*** The amount mentioned on the cheque should not be more than the amount deposited in the bank. Beside it, a certain amount of minimum balance should always be there in the account as per the rule of the bank.
7. ***Overwriting:*** There should not be any overwriting in the cheque.
8. ***Condition of the Cheque:*** Cheque should be in proper condition. If the cheque is torn, wet and spotted, it will not be acceptable to the bank.
9. ***Endorsement:*** The ordered and crossed cheques should be transferred by proper endorsement and delivery. Otherwise, the amount of cheque will not be paid by the bank

3. VARIOUS TYPES OF CHEQUES

A cheque is an unconditional order addressed to a banker, signed by the person who has deposited money with a banker, requesting him to pay on demand a certain sum of money only to the order of the certain person or to the bearer of the instrument.

Types of Cheques:- Bearer Cheque

Bearer cheques are the cheques which are used to withdraw money by the cheque's owner. These types of cheques normally used for a cash transaction.

Order Cheque

Order cheque are the cheques which are withdrawn for the payee (the cheque withdrawn for another person). Before paying the amount to that payee, banks cross check the identity of the payee.

Crossed Cheque

Crossed cheques are cheques which bear, two parallel line made on the left top part of the cheques. Then that cheques formed to crossed cheques. In this type of cheques, payment is not made in cash while the payment of that type of cheque transferred to the payee's account or to the person's account recommended by the holder of the cheque.

Account Payee Cheque

When two parallel lines along with a crossing made on the cheque and the word 'Account Payee' written between these lines, then that types of cheques are called account payee cheque. The payment of the account payee cheque should be made to the person, firm or company on whose name the cheque was issued.

Company Crossed Cheque

When two parallel lines along with a cross made on the cheque and the word 'Company' written between these lines, then that types of cheques are called company crossed cheques. Normally crossed cheque and company crossed cheque are same.

Stale Cheque

If any cheque issued by a holder does not get withdrawn from the bank till three months, then that type of cheques are called stale cheque.

Post Dated Cheque

If any cheque issued by a holder to the payee given with a later date, then that type of cheques are called post-dated cheque.

Anti-Dated Cheque

If a cheque contains a date, prior to the date of presentation it is called Ante-Dated cheque Banker will honour this cheque till the completion of 3 months from the date of the cheque.

4. EFFECTS OF ALTERATION, MARKING AND CROSSING OF CHEQUES

4.1 RBI Guidelines on Alteration of Cheques

As per RBI guidelines on Alterations/ Corrections on cheques, effective from l December 2010, no changes/ corrections would be allowed on cheque forms (with exception of date). For any changes in the cheque, a fresh cheque form needs to be issued. This will be applicable only for cheques cleared under the image based cheque truncation system (CTS) . This is not applicable to cheques cleared under other clearing arrangements such as MICR clearing, non-MICR clearing, over the counter collection (for cash payment) or direct collection of cheques outside the Clearing House arrangement.

4.2 Marking of a cheque

Marking of a cheque is writing on a cheque by the drawee banker that it would be honoured when it is duly presented for payment. Marked cheque can not be countermanded (i.e Stop payment) by the drawer. Payee is certain of getting money.

4.3 Crossing of a Cheque

4.3.1 The usage of crossing cheques:

- Cheques are usually crossed as a measure of safety Crossing is made by drawing two parallel transverse lines across the left top corner of the cheque with or without the addition of certain words.
- The usage of crossing distinguishes cheques from other bills of exchange.

- The object of general crossing is to direct the drawee banker to pay the amount of the cheque only to a banker, to prevent the payment of the cheque being made to wrong person.

4.3.2 Definition of Crossing

Sections 123 to 131 (A) of the Negotiable Instruments Act deal about crossing of a cheque. There are two types of crossing. They are (1) General crossing, and (2) Special crossing. Section 123 defines general crossing of cheque while section 124 defines special crossing.

General Crossing: According to section 123 "where a cheque bears across its face an addition of the words 'And Company' or any abbreviation thereof, between two parallel transverse lines, or two parallel transverse lines simply, either with or without the words "Not negotiable" that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed generally".

Special Crossing: According to section 124 "where a cheque bears across its face an addition of the name of the banker, either with or without the words 'Not negotiable', that addition shall be deemed a crossing and the cheque shall be deemed to be crossed specially and to be crossed to that banker".

4.3.3 What Constitutes crossing of a cheque:

When a cheque is crossed across the face with two transverse parallel lines, it is said to be crossed. In between the two parallel lines, the cheque will contain words such as "And Company' or an abbreviation as '& Co.', such cheque is said to be crossed generally.

When a cheque is crossed it implies two things:

- Payment will not be made across the counter by a bank when a crossed cheque is presented.
- The crossed cheque will have to be presented in an account through a pay-in-slip.

If a banker makes payment on a crossed cheque across the counter, it is a gross violation of payment in due course. When the cheque goes to an account, it will be credited and the amount can be withdrawn only by a separate cheque.

4.3.4 Who can cross a cheque

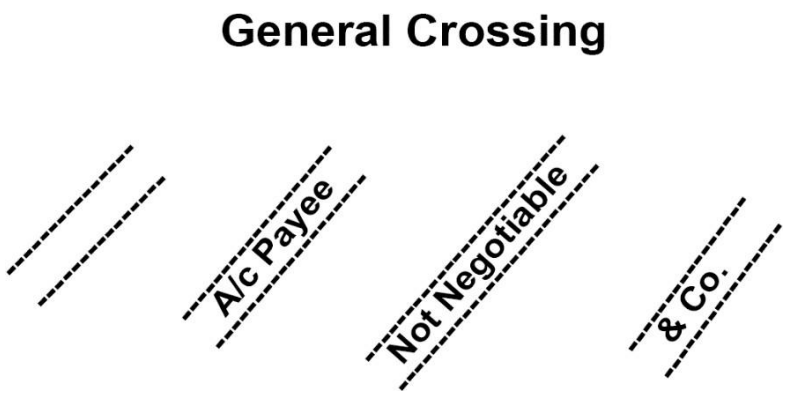
A cheque can be crossed by four persons:

- ***Drawer:*** When a drawer issues a cheque to a party, he can cross the cheque either generally or specially.
- ***Holder:*** When a cheque is given to the holder by the drawer without crossing, the holder can cross the cheque.
- ***Holder in due course:*** When a holder in due course receives an open cheque, he can cross the cheque generally, or when the cheque is already crossed generally, it can be converted into special crossing.
- ***Banker:*** When the collecting banker receives an open cheque without any crossing, the banker himself can cross the cheque before sending it for collection.

5. TYPES OF CROSSING

5.1 General Crossing

In General crossing, two transverse parallel lines are drawn by the drawer of the Cheque with or without words "Not Negotiable" in between parallel lines. Such a crossing is called General Crossing.



Words Such as 'and Company' or '& Co' may be written between two parallel lines. "Account Payee" or "A/c Payee" is written between two parallel lines.

5.1.1 Effect of General Crossing

Cheques which are generally crossed by the drawer can only be paid into a bank account of the payee whose name written on the cheque.

They cannot be encashed over the counter by bearer or payee.

Both bearer and order cheques can be crossed. However, drawer can make it bearer cheque by cancelling the crossing, writing that CROSSING IS CANCELLED and Putting full signature verifying the crossing cancellation.

5.2 Special Crossing

When drawer imposes restrictions on collecting or paying banker by writing particular bank's name between two parallel lines.

5.2.1 Effect of Special Crossing

The bank makes payment only to banker whose name is written in special crossing. There can be two special crossing. In this collecting banker add an additional crossing and write the name of other bank who act as their agent in collection of cheque. It allow other bank to collect the amount on their behalf.

5.3 Restrictive Crossing / Account Payee Crossing

Drawer write the word such as "Account payee only" or "A/c Payee" in between the parallel lines.

5.3.1 Effect of Restrictive Crossing

This crossing restrict the collecting banker to make the payment in account of payee named in the cheque. If collecting banker credit the amount to any third person other than payee, he will be liable for any loss arising to drawer or payee.

5.4 Not Negotiable Crossing

Drawer writes the word "Not Negotiable" in between the transverse lines of crossing.

5.4.1 Effect of Not Negotiable Crossing

The effect of "Not Negotiable Crossing" is that cheque lost its essential feature of "a Negotiable Instrument". The Transferee of such crossed cheque cannot get a better title than that of the transferor (cannot become holder in due course).

5.5 Banker do not comply with crossing

A banker can't debit its customer's account without complying with the crossing on cheque. If a banker fails to comply with instructions or crossing marked by the drawer of the cheque, it amounts to breach of contract of the bank with its customer.

Banker will be liable to pay any losses arising out to the drawer or payee.

6. ENDORSEMENT OF A CHEQUE

6.1 Meaning of Endorsement

In legal terms, cheque is a negotiable instrument. "Negotiable" means transferable. A cheque given in the name of the person can be transferred to the ownership of another person, by merely putting a signature on the backside of the cheque. The second owner can also transfer it to a third person, by putting his signature below the signature of the first owner. This process is called "Endorsement".

6.2 Definition of Endorsement

Endorsement has been defined in sec 15 of the Negotiable Instruments Act, 1881 as follows:-

Where the maker or holder of a negotiable instrument signs the same otherwise than as such maker, for the purpose of negotiation on the bank or face thereof or on a slip of paper annexed there to ------he is said to have endorsed the same and is called endorser.

In practice, an endorsement is made, always on the back of the instrument. If there is no space for further endorsement, a slip of paper (slip of paper is called as "Allonge") can be attached to the cheque and the endorsement can be continued.

6.3 Rules Regarding Endorsement

1. All Endorsements should be made in ink only (pencil endorsements are not objected in law, but as they may be altered, such practice should be discouraged)
2. An endorsement should not be in block letters. The endorsement should be made by signature and not by writing name in Block Letters.
3. A type written endorsement is also valid.
4. A rubber stamp endorsement is as valid as written endorsement
5. An endorsement in the form of facsimile, (signature made on a stamp) of payee's signature is also legally valid. But endorsement types from point 3 to 5 are normally discouraged in practice, as there are chances of fraud, to take place.
6. When endorsement is in a language which a banker is not expected to know the paying banker can refuse payment for its confirmation. But he should give valid reason for it.

6.4 Kinds of Endorsements:

1. ***Endorsement in blank:***

   If the endorser signs his name only, endorsement is said to be in blank. The endorser does not specify the name of the endorsee with the effect that an instrument endorsed in blank becomes payable to bearer, even though originally payable to order and no further endorsement is required for negotiation.

2. ***Endorsement in full:***

   If in addition to signature, the endorser adds a direction to pay the amount mentioned in the instrument to or to the order of a specified person, the endorsement is said to be endorsement in full.

3. ***Conditional Endorsement:***

   If the endorser of a negotiable instrument puts some conditions through explicit words in the endorsement to make his liability or the right of the endorsee to receive the amount due thereon is called a conditional endorsement.

4. ***Restrictive Endorsement***:

   Example: Pay the contents to 'C' only

   Pay to 'C' for my use

5. ***Endorsement Sans Recourse:***

Sans-Recourse means stop taking actions. Here the endorser informs the endorsee that in case of the dishonor of the instrument, the endorsee cannot make the endorser liable.

Example:

i. Pay to 'A' or order at his own risk
Sd/-R

ii. Pay to 'B' without recourse to me
Sd/-C

7. LEGAL EFFECT OF LOSS OF CHEQUE IN TRANSIT:-

When cheque are sent for collection to another branch or bank, there are chances of missing them in **transit** (i.e in the **travel from collecting banker to the paying banker**).

In such situation, "what should the banker do" – guidelines have been given in a circular issued by IBA (Indian Banks Association). IBA issued the circular on the orders of Reserve bank of India.

The circular says "In respect of cheques lost in transit or at the paying banks branch, banks should immediately bring it to the notice of the Account holder so that he can issue a stop payment instruction".

Customer can stop payment of the cheque either through net banking or by visiting the bank. He can also take care that other cheques issued by him are not dishonoured due to the non- credit of the amount of lost cheque.

Since the reason for such loss is on the collecting banker, customer are expected to be reimbursed for any ensuing expenses. They are also entitled to interest for the time taken to obtain the duplicate cheque. A photocopy of the deposited cheque is enough to prove a deficiency in service.

CONCLUSION

In this lesson, we have learnt about a cheque, its negotiability, requisites of a cheque and how it can be drawn. The purpose of various types of cheque is made known we have also learnt how effectively a cheque can be handled using various types of crossing and the significance of

Endorsements. We also know the steps of action to be followed, in case the cheque is lost in transit or at the place of the paying banker.

So, now effective usage of cheque book has been made possible for the learners.

EXERCISES

Short Answers Questions

1. Define a cheque.
2. What is a stale cheque?
3. What do you mean by crossing of cheque?
4. Can a cheque be altered?
5. Write the significance of Special Crossing.

Big Answers Questions

1. Enumerate the types of cheque that can be issued legally.
2. Bring out the significance of General Crossing and Special Crossing.
3. Write short notes on Endorsements on cheque.
4. You are a Bank customer. How will you protect yourself on experiencing a “loss of cheque in transit”?