**MODULE III**

**NEGOTIABLE INSTRUMENTS**

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**LIABILITY OF COLLECTING AND PAYING BANKERS**

**COLLECTING BANKERS RESPONSIBILITY**

*Section 131 in The Negotiable Instrument Acts, 1881 provides that.*

*“A banker who has in good faith and without negligence received payment for a customer of a cheque crossed generally or especially to him shall not, in case the title to the cheque proves defective, incur any liability to the true owner of the cheque by reason only of having received such payment.”*

The protection available to the collecting bankers under Section 131of NI Acts 1881 only when following conditions are satisfied by the collecting banker.

1. The check should have been crossed generally or especially to the bank.
2. The bank should have collected such cheque for a customer as an agent for collection and not as a holder for a value.
3. The proceeds of the collected cheque are credited to only to the account of the payee or to the account of  endorsee if endorsement on the instrument is regular.
4. The collecting banker must have acted in good faith. Here ’good faith’ means banker had no reasonable ground to believe that the customer is not entitled to receive payment of the amount therein mentioned.
5. The collecting banker should have acted without negligence. ’Without negligence’ means the account of the customer on whose behalf cheque is collected, is opened with proper compliance of KYC norms such as verification of identity proof and address proof before opening the account.
6. The collecting banker who received payment based on the electronic image of truncated cheque should have verified the apparent genuineness of the cheque in his possession with due diligence and ordinary care to ensure the prima facie genuineness of the instrument.

***PAYING BANKER’S RESPONSIBILITIES***

The section 85(1), 85(2), 128 of negotiable instrument acts provide statutory protection to paying banker for making payments of order cheque, bearer cheque or crossed cheque in that order.

***Payment of order cheque***

Section -85(1) of N.I.Acts 1881 provides that

“Where a cheque payable to order purports to be endorsed by or on behalf of the payee, the drawee is discharged by payment in due course”

The above section provides protection to paying banker if he has made payment of an order cheque in due course (within the meaning of sec.10 of N.I.Act.) and if the proceeds credited to the account of an endorsee if and only if the endorsement is regular.

***Payment of bearer cheque***

Section -85(2) of N.I.Acts provides that

*“Where a cheque is originally expressed to be payable to bearer, the drawee is discharged by payment in due course to the bearer thereof, notwithstanding any endorsement whether in full or blank appearing thereon and notwithstanding that any such endorsement purports to restrict or exclude further negotiation”.*

The above section specifies that a cheque which is ‘once a bearer is always bearer’ (which means if a cheque is originally drawn as a bearer cheque remains always bearer irrespective of any endorsements on the back of the instrument). Therefore banks are not required to verify the regularity of the endorsement on the back of the cheque if any and they are protected from liability if they have made payment of an uncrossed bearer cheque to a bearer in due course.

***Payment of ‘Crossed cheque’***

Section -128.of N.I.Acts 1881 provides that

*“Where the banker on whom a crossed cheque is drawn has paid the same in due course, the banker paying the cheque and (in case such cheque has come to the hands of the payee) the drawer thereof shall respectively be entitled to the same rights, and be placed in if the amount of the cheque had been paid to and received by the true owner thereof”.*

*The paying banker of a crossed cheque shall satisfy the following condition to be eligible for protection under related NI acts.*

1. *Payment shall be made in due course.*
2. *Where a cheque is crossed generally, the banker on whom it is drawn shall not pay it otherwise than to a banker.*
3. *Where a cheque is crossed specially, the banker on whom it is drawn shall not pay it otherwise than to the banker to whom it is crossed or his agent for collection.*

*In following cases paying banker does not get statutory protections if he makes the payment of a cheque;*

*a) Materially altered or signature of the drawer is forged or payment made of a crossed cheque with an irregular endorsement.
b) Makes payment of a crossed cheque to a person otherwise than to the banker then he is liable for the loss to the true owner of the cheque.*

***Collecting Banker***

Collecting Banker is the one who accumulates the proceeds of a cheque for the customer. Even though a banker gathers the proceeds of a cheque for the customer solely as a matter of service, hitherto the Negotiable Instruments Act, 1881 ultimately inflicts obligation, statutory in nature.

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As per Section 131 of Negotiable Instruments Act 1881, "A banker who has in good faith and without negligence received payment for a customer of a cheque crossed generally or specifically to himself -shall not, in case the title to the cheque proves defective, incur any liability to the true owner of the cheque by reason of only having received such payment.

Explanation: A banker receives payment of a crossed cheque for a customer within the meaning of this section notwithstanding that he credits his customer's account with the amount of-the cheque before receiving payment thereof."

***The fundamentals of claiming protection under Section 131 of Negotiable Instruments Act 1881 are as follows:***

***(***i) The collecting banker should have acted in good faith & without negligence. Acted in good faith refers that the act that is done honestly. The plea of good faith can be refuted on the ground of unruliness indicative of want of proper care & attention.

(ii) The banker should have accumulated a crossed cheque

(iii) The proceeds should have been gathered for a customer, i.e., a person who has an account with him.

(iv) That the collecting banker has acted as an agent of the customer. If he had developed into the holder for value, the protection available in Section 131 of Negotiable Instruments Act 1881 is forfeited

# Protection of Paying Banker (Sections 10, 85 and 128)

A cheque initially articulated by the drawer himself to be payable to bearer, the banker may disregard any endorsement on cheque. He will be released by payment in due course.

Section 85 of the Negotiable Instruments Act states that “where a cheque payable to order purports to be endorsed by or on behalf -of the payee the banker is discharged by payment in due course. He can debit the account of the customer with the amount even though the endorsement turns out subsequently to have been forged, or the agent of the payee without authority endorsed it on behalf of the payee”. It would be observed that the payee comprises of endorsee. This protection is approved for the reason that a banker cannot be anticipated to know the signatures of all persons in the world. He is only entitled to know the signatures of his own customers.

Consequently, the forgery of drawer's signature will not usually defend the banker but even in this case, the banker may debit the account of customer, if it can illustrate that the forgery was familiarly connected with the laxity of the customer & was the adjacent cause of loss.

***The duties and responsibilities of a collecting banker are discussed below:***

1. Due care and diligence in the collection of cheque.

2. Serving notice of dishonour.

3. Agent for collection.

4. Remittance of proceeds to the customer.

5. Collection of bills of exchange.

***1. Due Care and Diligence in the Collection of Cheques:***

The collecting banker is bound to show due care and diligence in the collection of cheques presented to him. In case a cheque is entrusted with the banker for collection, he is expected to show it to the drawee banker within a reasonable time. According to Section 84 of the Negotiable Instruments Act, 1881, “Whereas a cheque is not presented for payment within a reasonable time of its issue, and the drawer or person in whose account it is drawn had the right, at the time when presentment ought to have been made, as between himself and the banker, to have the cheque paid and suffers actual damage, through the delay, he is discharged to the extent of such damage, that is to say, to the extent to which such drawer or person is a creditor of the banker to a large amount than he would have been if such cheque had been paid.”
In case a collecting banker does not present the cheque for collection through proper channel within a reasonable time, the customer may suffer loss. In case the collecting banker and the paying banker are in the same bank or where the collecting branch is also the drawee branch, in such a case the collecting banker should present the cheque by the next day. In case the cheque is drawn on a bank in another place, it should be presented on the day after receipt.

***2. Serving Notice of Dishonour:***

When the cheque is dishonoured, the collecting banker is bound to give notice of the same to his customer within a reasonable time.

It may be noted here, when a cheque is returned for confirmation of endorsement, notice must be sent to his customer. If he fails to give such a notice, the collecting banker will be liable to the customer for any loss that the customer may have suffered on account of such failure.

Whereas a cheque is returned by the drawee banker for confirmation of endorsement, it is not called dishonour. But in such a case, notice must be given to the customer. In the absence of such a notice, if the cheque is returned for the second time and the customer suffers a loss, the collecting banker will be liable for the loss.

***3. Agent for Collection:***

In case a cheque is drawn on a place where the banker is not a member of the ‘clearing-house’, he may employ another banker who is a member of the clearing-house for the purpose of collecting the cheque. In such a case the banker becomes a substituted agent. According to Section 194 of the Indian Contract Act, 1872, “Whereas an agent, holding an express or implied authority to name another person to act in the business of the agency has accordingly named another person, such a person is a substituted agent. Such an agent shall be taken as the agent of a principal for such part of the work as is entrusted to him.”

***4. Remittance of Proceeds to the Customer:***

In case a collecting banker has realised the cheque, he should pay the proceeds to the customer as per his (customer’s) direction. Generally, the amount is credited to the account of the customer on the customer’s request in writing, the proceeds may be remitted to him by a demand draft. In such circumstances, if the customer gives instructions to his banker, the draft may be forwarded. By doing so, the relationship between principal and agent comes to an end and the new relationship between debtor and creditor will begin.

***5. Collection of Bills of Exchange:***

There is no legal obligation for a banker to collect the bills of exchange for its customer. But, generally, bank gives such facility to its customers. In collection of bills, a banker should examine the title of the depositor as the statutory protection under Section 131 of the Negotiable Instruments Act, 1881.

Thus, the collecting banker must examine very carefully the title of his customer towards the bill. In case a new customer comes, the banker should extend this facility to him with a trusted reference.