



**GYAANI
ACADEMY**

CMA FOUNDATION

NOTES

NEGOTIABLE

INSTRUMENTS ACT, 1881

NEW SYLLABUS 2022

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CHARACTERISTICS OF NEGOTIABLE INSTRUMENTS

INTRODUCTION

Negotiable Instrument Act, 1881 primarily contains the law relating to negotiable instruments of the commercial world which facilitates the activities of trade & commerce. The main objective of this Act is to legalize the system by which the instruments contemplated by it could freely pass from one hand to another like any other goods. **The term 'negotiable' means transferable and the term 'instrument' means 'any written document creating a right in favor of some person.'** Thus, by negotiable instrument we mean a written document by which a right is given to a person and which is transferable in accordance with provisions of Negotiable Instrument Act, 1881.

WHAT IS NEGOTIABLE INSTRUMENT?

In common parlance a negotiable instrument can be understood as a piece of paper which entitles to a sum of money and which is transferable from one person to another merely by delivery or by endorsement and delivery. The person to whom it is so transferred becomes entitled to the sum mentioned therein and also to the right to further transfer it. Though there is a general principle that no one can become owner of any property unless the person who sold the property to him is the true owner of the said property, yet this rule is not applicable in the case of Negotiable instrument. Now let us refer to the Act how the term Negotiable instrument is defined in the section.



Sec. 13 of the Act defines a negotiable instrument as 'a promissory note, bill of exchange or cheque payable either to order or to bearer.'

Thus, a Negotiable Instrument means an instrument, the property in which is acquired by anyone who takes a bona fide and for value, notwithstanding any defect in the title of the Transferor. It need not necessarily be a promissory note, bill of exchange or a cheque.

A negotiable instrument may be payable to two or more persons jointly or it may be made payable in the alternative to one of two or one or some of several payees.

CHARACTERISTICS OF A NEGOTIABLE INSTRUMENT

The term negotiability may also be extended to other instruments like Bill of Lading; Hundies, etc. provided it satisfies the following characteristics -

- 1. Free and Innumerable Transfers:** A Negotiable Instrument may be transferred by Delivery, or by Endorsement and Delivery. Also, a Negotiable Instrument can be transferred ad infinitum, i.e., transferred any number of times till its satisfaction on date of maturity.
- 2. Free From Defects:** The Holder in due course obtains the good title to the instrument, notwithstanding any defect in a previous holder's title. A Holder in due course is one who receives the instrument for Consideration, Before maturity, and without any notice as to the defect in title of the Transferor.
- 3. Holder to Sue in His Own Name:** The Holder in due course of a Negotiable Instrument can sue on the instrument in his own name.

4. **Presumptions:** A Negotiable Instrument is subject to certain presumptions listed u/s 118 and 119 as to consideration, date, time of acceptance and transfer, endorsements, etc.

Note: Share Certificates with Blank Transfer Deeds, Deposit Receipts and Mate's Receipts are not Negotiable Instruments.

PRESUMPTIONS

Until the contrary is provided, the following aspects are presumed in respect of Negotiable Instruments –

Presumptions a to..	Description
Consideration	Every Negotiable Instrument was made or drawn for consideration, and such Negotiable Instrument was accepted, Endorsed, negotiated or transferred for consideration.
Date	Every Negotiable Instrument bearing a date was made or drawn on that date.
Time of Acceptance	Every Bill of Exchange was accepted within a reasonable time after the date mentioned therein but before the date of its maturity.
Time of Transfer	Every transfer of a Negotiable Instrument was made before its maturity.
Order of Endorsements	Endorsements appearing on a Negotiable Instrument were made in the order in which they appear thereon.
Stamp	That a lost Promissory Note, Bill of Exchange or Cheque was duly stamped
Holder in Due Course	That the holder of a Negotiable Instruments is a holder in due course.
Fact of Dishonor [Sec.119]	In a suit for the dishonor of a Negotiable Instrument, the Court shall, on proof of protest, presume the fact of dishonor, unless and until it is disproved.

Note:

- ✓ Where the Negotiable Instruments has been obtained from its lawful owner/custodian by means of an offence/fraud or for unlawful consideration, the burden of proving that a Holder is a Holder in due course, lies upon him.
- ✓ The NI Act will not affect Sec.21 of the Indian Paper Currency Act, 1871, or any local usage relating to any instrument in a local language. [Sec. 1].

TYPES OF NEGOTIABLE INSTRUMENTS

Negotiable Instruments are of two types:

1. **Negotiable by Statute:** Section 13 of the Act, provides that a negotiable Instrument includes promissory note, bill of exchange and cheque, whether payable to bearer or order.
2. **Negotiable by Custom or Usage:** Though the Act speaks of only three types of Negotiable Instrument, **but it does consider other kinds of instruments from being treated as a negotiable**

instrument provided, they possess the characteristics of a negotiable instruments. Accordingly certain other instruments take the character of negotiable instruments by custom or usage. **Dividend warrant, circular notes, bearer debentures are some of them though they are not specifically mentioned in the Act as negotiable instrument.**

CLASSIFICATION OF NEGOTIABLE INSTRUMENTS

1. Bearer and Order Instruments

A negotiable instrument is said to be payable to **bearer** when

- ✓ It is expressed to be so payable
- ✓ Only or last endorsement is a blank endorsement.

A negotiable instrument is said to be payable to **order** when

- ✓ It is expressed to be so payable
- ✓ Expressed to be payable to a particular person with restricting its transferability.

2. Inland and Foreign Instruments: A bill, promissory note or cheque if both drawn and payable in India or drawn on a person resident in India is said to be an inland bill. A bill which is not an inland bill is deemed to be a foreign bill. Foreign bill must be protested for dishonor if such protest is required by the law of the place where it was drawn, this is not case with Inland bills where protest for non-payment is optional as per section 104 of the Act.

3. Demand and Time Instruments: An instrument is payable on demand when it is expressed to be so payable or when no time is specified on it. A cheque is always payable on demand. **A note or bill if payable after a specified period or happening of a specified event which is certain, it is a time instrument.** If a promissory note or bill of exchange bears the expression "at sight" and "on presentation" means on demand (section 21). The words "on demand" are usually found in a promissory note, whereas the words "at sight" are found in a bill of exchange.

4. Genuine, Accommodation and Fictitious Bill: When a bill is drawn, accepted, or endorsed for consideration it is a genuine bill. When it is drawn, accepted, or endorsed without consideration it is accommodation bill. When drawer or payee or both are fictitious the bill is called fictitious bill. If both drawer and payee of a bill are fictitious person, the acceptor is liable to a holder in due course, if the holder in due course can show that the signature of the supposed drawer and that of first payee are in the same handwriting.

5. Clean and Documentary Bill: When no documents relating to goods are annexed to the bill, it is clean bill. When documents of title or other documents relating to goods are attached, it is documentary bill.

6. Ambiguous Instrument: When an instrument due to faulty drafting may be interpreted either as bill or note, it is an ambiguous instrument. It is for holder to decide how he wants the bill to be treated. **Ambiguity may also arise when the amount is stated differently in words and figures. In such case the amount stated in words will be taken into account.**

7. Inchoate Instrument: An instrument incomplete in some respect is known as inchoate instrument. When a person signs and delivers to another a blank or incomplete stamped paper, he authorizes the other person to make or complete upon it a negotiable instrument for any amount not exceeding the amount covered by the stamp. The effect of such signing is that the person signing the instrument is liable upon such instrument in the capacity in which he signed it to holder in due course of the instrument.

8. Escrow Instrument: When an instrument is drawn conditionally or for a special purpose as a collateral security and not for the purpose of transferring property therein, it is called Escrow

instrument. The liability to pay in case of an Escrow instrument does not arise if the conditions agreed upon are not fulfilled or the purpose for which the instrument was delivered is not achieved.

PARTIES TO A NEGOTIABLE INSTRUMENT

Parties	Meaning
Drawer	The Maker of a Promissory Note, Bill of Exchange or Cheque.
Drawee	The person on whom the instrument is drawn and thereby directed to pay.
Drawee in case of need	The person whose name is given in the bill or on any Endorsement thereof, in addition to the name of the Drawee, who should be resorted to in case of need. Where a Drawee in case of need is named in a Bill of Exchange or any endorsement thereon, the Bill of Exchange is not dishonored, unless it has been dishonored by such Drawee [Sec.115] A Drawee in case of need may accept and pay the Bill of Exchange, without previous protest. [Sec.116]
Acceptor	When the Drawee signs his assent upon the Bill, and delivers the same to the holder or some other person on his behalf, he becomes the "Acceptor".
Acceptor for Honor	Person accepting a Bill of Exchange (which has been noted or protested for non-acceptance or for better security) supra protest for honor of the drawer or of any endorsers. Acceptor for Honor must specify as to whose honor he is accepting the Bill of Exchange. Otherwise, it shall be deemed to be made for the honor of the Drawer.
Payee	Payee is the person to whom the amount is payable, which may be the Drawer himself or any other person.
Holder	Any person entitled in his own name to the possession thereof and to receive or recover the amount due thereon from the parties thereto. Where the instrument is lost or destroyed, its holder is the person so entitled at the time of such loss or destruction. [Sec.8]

CAPACITY TO BECOME A PARTY

A person competent to contract can become a party to a negotiable instrument. If a party who makes, draws, endorses, or negotiates a negotiable instrument is incompetent to do so, the agreement is void as against him. But the contract is still valid against the other parties competent to contract. The conditions under which certain categories of person like a Minor, Corporate body, Agent and Legal representatives can be a party to a negotiable instrument are as under:

- 1. Minor:** A minor person is not competent to contract; therefore, he cannot bind himself by becoming a party to a negotiable instrument. But mere presence of a minor as one of the parties in a negotiable instrument does not make it invalid. **A minor can draw, indorse, deliver and negotiate an instrument so as to bind all parties except himself.**

Example: A, B and C, a minor executed a promissory note in favor of P. Held, C's immunity from liability did not absolve A and B, other joint promisors, from liability.

A minor is not personally liable on a bill or note given by him for necessities supplied to him. It is only his estate which is liable for such a bill or note.

2. Corporation: Corporation can be a party to a negotiable instrument if authorized by its Article of Association, otherwise it cannot.

3. Agent: As per section 27 an agent can bind his principal by acting on his behalf only in the manner in which he is duly authorized to become a party to a negotiable instrument. The agent is required to make it clear that he is acting in representative capacity which must be evidenced by the manner he signs such document. The form of signature must show that he does not intend to incur personal liability. **Otherwise, he becomes personally liable.**

Example 1: Arun a manager of ABC Ltd accepted a bill of exchange and signed as manager. It was held that Arun was personally liable.

Example 2: Arun a manager of ABC Ltd accepted a bill of exchange and signed as for ABC Ltd. It was held that Arun was not personally liable.

4. Legal Representative: As per section 30 a legal representative of a deceased person who signs his name to a negotiable instrument incurs personal liability unless by clear words, he limits his liability to the extent of the assets of the deceased received by him as legal representative.

GYAANI'S ONE LINERS

- ✓ Negotiable Instrument Act, 1881 primarily contains the law relating to negotiable instruments of the commercial world.
- ✓ The term 'negotiable' means transferable and the term 'instrument' means 'any written document creating a right in favor of some person.' Thus, by
- ✓ Negotiable instrument means a written document by which a right is given to a person and which is transferable in accordance with provisions of Negotiable Instrument Act, 1881.
- ✓ Sec. 13 of the Act defines a negotiable instrument as 'a promissory note, bill of exchange or cheque payable either to order or to bearer.'
- ✓ A negotiable instrument may be payable to two or more persons jointly or it may be made payable in the alternative to one of two or one or some of several payees.
- ✓ A Negotiable Instrument may be transferred by Delivery, or by Endorsement and Delivery.
- ✓ Also, a Negotiable Instrument can be transferred any number of times till its satisfaction on date of maturity.
- ✓ A Holder in due course is one who receives the instrument for Consideration, Before maturity, and without any notice as to the defect in title of the Transferor.
- ✓ The Holder in due course obtains the good title to the instrument, notwithstanding any defect in a previous holder's title.
- ✓ The Holder in due course of a Negotiable Instrument can sue on the instrument in his own name.
- ✓ A Negotiable Instrument is subject to certain presumptions listed u/s 118 and 119 as to consideration, date, time of acceptance and transfer, endorsements, etc.
- ✓ Share Certificates with Blank Transfer Deeds, Deposit Receipts and Mate's Receipts are not Negotiable Instruments.

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- ✓ Negotiable Instruments are of two types i.e., Negotiable by Statute and Negotiable by Custom or Usage
- ✓ Dividend warrant, circular notes, bearer debentures are negotiable by custom though they are not specifically mentioned in the Act as negotiable instrument.
- ✓ A negotiable instrument is said to be payable to bearer when it is expressed to be so payable and only or last endorsement is a blank endorsement.
- ✓ A negotiable instrument is said to be payable to order when it is expressed to be so payable and expressed to be payable to a particular person with restricting its transferability.
- ✓ A bill, promissory note or cheque if both drawn and payable in India or drawn on a person resident in India is said to be an inland bill.
- ✓ A bill which is not an inland bill is deemed to be a foreign bill.
- ✓ An instrument is payable on demand when it is expressed to be so payable or when no time is specified on it. A cheque is always payable on demand.
- ✓ A note or bill if payable after a specified period or happening of a specified event which is certain, it is a time instrument.
- ✓ When a bill is drawn, accepted, or endorsed for consideration it is a genuine bill. When it is drawn, accepted, or endorsed without consideration it is accommodation bill.
- ✓ When drawer or payee or both are fictitious the bill is called fictitious bill.
- ✓ When no documents relating to goods are annexed to the bill, it is clean bill.
- ✓ When documents of title or other documents relating to goods are attached, it is documentary bill.
- ✓ When an instrument due to faulty drafting may be interpreted either as bill or note, it is an ambiguous instrument.
- ✓ Ambiguity may also arise when the amount is stated differently in words and figures. In such case the amount stated in words will be taken into account.
- ✓ An instrument incomplete in some respect is known as inchoate instrument.
- ✓ When an instrument is drawn conditionally or for a special purpose as a collateral security and not for the purpose of transferring property therein, it is called Escrow instrument.
- ✓ The liability to pay in case of an Escrow instrument does not arise if the conditions agreed upon are not fulfilled or the purpose for which the instrument was delivered is not achieved.
- ✓ The maker of the negotiable instrument is known as Drawer.
- ✓ The person on whom the instrument is drawn and thereby directed to pay is known as Drawee.
- ✓ The person whose name is given in the bill or on any endorsement thereof, in addition to the name of the drawee, who should be resorted to in case of need is known as Drawee in case of need.
- ✓ Where a drawee in case of need is named in a Bill of Exchange or any endorsement thereon, the Bill of Exchange is not dishonored, unless it has been dishonored by such drawee.
- ✓ When the drawee signs his assent upon the bill and delivers the same to the holder on his behalf, he becomes the Acceptor.
- ✓ Acceptor for honor is a person accepting a bill of exchange which has been noted or protested for non-acceptance or for better security supra protest for honor of the drawer of any one of endorsers.

- ✓ Payee is the person to whom the amount is payable, which may be the drawer himself or any other person.
- ✓ Holder is the person entitled in his own name the possession to receive or recover the amount due thereon from the parties thereto.
- ✓ A person competent to contract can become a party to a negotiable instrument.
- ✓ If a party who makes, draws, endorses, or negotiates a negotiable instrument is incompetent to do so, the agreement is void as against him. But the contract is still valid against the other parties competent to contract.
- ✓ A minor can draw, indorse, deliver and negotiate an instrument so as to bind all parties except himself.
- ✓ A minor is not personally liable on a bill or note given by him for necessaries supplied to him. It is only his estate which is liable for such a bill or note.
- ✓ Corporation can be a party to a negotiable instrument if authorized by its Article of Association, otherwise it cannot.
- ✓ An agent can bind his principal by acting on his behalf only in the manner in which he is duly authorized to be become a party to a negotiable instrument. The agent is required to make it clear that he is acting in representative capacity which must be evidenced by the manner he signs such document. Otherwise, he becomes personally liable.
- ✓ A legal representative of a deceased person who signs his name to a negotiable instrument incurs personal liability unless by clear words, he limits his liability to the extent of the assets of the deceased received by him as legal representative.

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PROMISSORY NOTE, BILL OF EXCHANGE AND CHEQUE

INTRODUCTION

A promissory note, bill of exchange or cheque is payable to order which is expressed to be so payable or which is expressed to be payable to a particular person, and does not contain words prohibiting transfer or indicating an intention that it shall not be transferable.

PROMISSORY NOTE

According to Section 4 of the Negotiable Instruments Act, 1881, "A Promissory note is an instrument in writing (not being a bank note or a currency note) containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument."

PARTIES TO A PROMISSORY NOTE

1. **Maker:** The person who makes the promissory note and promises to pay is called the maker.
2. **Payee:** The person to whom the payment is to be made is called the payee.

FUNDAMENTALS OF A PROMISSORY NOTE

- ✓ It must contain date.
- ✓ The sum payable must be certain.
- ✓ The maker and payee must be certain.
- ✓ The promissory note must be in writing.
- ✓ The promise to pay should be unconditional.
- ✓ The promissory note must be signed by the maker.
- ✓ The instrument must contain a promise to pay money only.
- ✓ It must contain an undertaking to pay. There must be an express promise to pay.
- ✓ **Stamping of Promissory Note is essential.** An unstamped promissory note is not admissible in evidence and no suit can be maintained.
- ✓ The limitation period for a promissory note to file a suit is **three years** from the date of execution or from the date of acknowledgement.

₹ 10,000	Lucknow April 10, 2020
Three months after date, I promise to pay Shri Ramesh (Payee) or to his order the sum of Rupees Ten Thousand, for value received.	
	Stamp Sd/- Ram
To, Shri Ramesh, B-20, Green Park, Mumbai. (Maker)	

BILL OF EXCHANGE

According to Section 5 of the Negotiable Instruments Act, 1881, "A bill of exchange is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument".

PARTIES TO A BILL OF EXCHANGE

There are **three parties** to bill of exchange:

1. **The drawer:** The person who gives the order to pay or who makes the bill is called the drawer.
2. **The drawee:** The person who is directed to pay is called the drawee. When the drawee accepts the bill, he is called the acceptor.

3. **The Payee:** The person to whom the payment is to be made is called the payee.

FUNDAMENTALS OF A BILL OF EXCHANGE

- ✓ It must be in writing.
- ✓ The drawer must sign the instrument.
- ✓ The amount to be paid should be certain.
- ✓ Every Bill of Exchange must be stamped.
- ✓ The order to pay must be definite and unconditional.
- ✓ The time of payment must be indicated in the bill with certainty.
- ✓ The consideration of a bill of exchange should be paid only by way of money only.
- ✓ All the parties i.e., Drawer, Drawee and Payee of a bills of exchange must be certain.

STAMP	Mr. Alpha (Drawer) 576, Gurugram Feb 17, 2018
₹ 1,00,000	
Three months after date, pay to Mr. Beta (payee) a sum of rupees one lakh, for the value received.	
To, Mr. Gamma (drawee) 268, Noida	Mr. Alpha Sd/-

CHEQUE

According to Section 6 of the Negotiable Instruments Act, 1881, "A cheque is a bill of exchange drawn upon a specified banker and payable on demand and it includes the electronic image of a truncated cheque and a cheque in the electronic form."

A cheque in the electronic form means "cheque which contains the exact mirror image of a proper cheque, and is generated, written and signed in a secure system ensuring the minimum safety standards with the use of digital signature and asymmetric crypto system."

A truncated cheque means a cheque which is truncated during the course of a clearing cycle, either by the clearing house or by the bank whether paying or receiving payment, immediately on generation of an electronic image for transmission, substituting the further physical movement of the cheque in writing.

'Clearing House' means the clearing house managed by the Reserve Bank of India or a clearing house recognized as such by the Reserve Bank of India [Sec. 6 as substituted by the Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002].

A cheque is a specie of a bill of exchange; but it has the following two additional qualifications:

- ✓ It is always drawn on a specified banker, and
- ✓ It is always payable on demand.

PARTIES TO A CHEQUE

There are **three parties** to bill of exchange:

1. **The Drawer:** The customer who signs the cheque is called "drawer".
2. **The Drawee:** The bank on whom the cheque is drawn is called "drawee".
3. **The Payee:** The person to whom the payment is to be made is called the payee.

FUNDAMENTALS OF A CHEQUE

- ✓ Payee to be certain.
- ✓ The cheque must contain the date.
- ✓ A cheque must be an order in writing.
- ✓ It must contain an unconditional order.
- ✓ A cheque must be signed by the maker.
- ✓ A cheque may be drawn payable to order or bearer.

भारतीय स्टेट बैंक
State Bank Of India
New Delhi
Kapli Bazar NH, 65 Ram Ghat
Mahadev Road - 110025
IFC CODE - SBIN0011256
01012020
D D M M Y Y Y Y

PAY Teach Lane को या उसके आदेश पर OR ORDER
₹ पाके RUPEES Five Thousand Only अंश कर ₹ 5000/-

8563261452630 VALID FOR ₹ 100000/- & UNDER
Prefix: 1519000002
Here Signature Dipak Das
MULTI-CITY CHEQUE Payable at Par at All Branches of SBI
Please sign above

9500 20 69500 203 20 00 2860 3 1
Cheque No MICR Code RBI A/C NO Transaction Code

- ✓ **The amount must be specifically mentioned in figures and words.**

WHO CAN CROSS A CHEQUE ?

By crossing the cheque, the drawer instructs the banker to not to pay it over the counter but only credit to the account of the person named therein. It adds to the security and thus ensures payment to the payee or to his order. A cheque may be crossed by any of the following persons:

- ✓ **The drawer of a cheque.**
- ✓ **The holder of a cheque.** Where a cheque is issued uncrossed, it may be crossed by the holder generally or specially.
- ✓ **The banker** in whose favor the cheque has been crossed specially may again cross it specially in favor of another banker.

DUE DATE OF A BILL OR NOTE

Every instrument payable, otherwise, then on demand is entitled to **three days of grace.**

Instruments **not entitled** to 'period of grace' are:

- ✓ a cheque
- ✓ a bill or note payable on demand,
- ✓ a bill or note in which no time is mentioned.

Instruments **entitled** to 'period of grace' are:

- ✓ a bill or note payable on a specified day,
- ✓ a bill or note payable 'after sight',
- ✓ a bill or note payable at a certain period on happening of a certain event.

So, in case of time bill or note, it becomes due on the last day of grace period. Where an instrument is payable by installments, each installment is due 3 days after the date fixed for payment of the installment. **If the due date falls on a public holiday, the bill becomes due on immediately preceding business day. If the month in which the period is to terminate has no corresponding day, the period will terminate on the last day of the month.**

PAYMENT IN DUE COURSE

Payment in due course means payment in accordance with the apparent tenor of the instrument in good faith and without negligence to any person in possession thereof. The payment to the person in possession of the instrument must be under circumstances which do not afford a reasonable ground for believing that he is not entitled to receive payment of the amount mentioned in the instrument.

Payment in due course results in discharge of the instrument. A payment is said to be 'payment in due course' if it satisfies the following conditions:

- ✓ It is in accordance with apparent tenor of the instrument. This means that **payment must be made according to the period mentioned on the face of the instrument.** A payment before the maturity date of an instrument will not be considered as a payment in due course.
- ✓ **It is made on behalf of drawee or acceptor.**
- ✓ **It must be made in money term only which includes cheque and currency notes.** The holder of a negotiable instrument cannot be forced to accept payment in any other mode except with his consent.

- ✓ Payment must be **made to the person in possession** of the instrument i.e., the lawful holder of the instrument and also entitled to payment.
- ✓ **Payment must be made in good faith, without negligence and under bona fide circumstances.** If a cheque bears forged signature of the drawer, the payment will not be payment in due course if the banker fails to exercise the necessary care. For example, if a bill payable to bearer (Naman) has been lost or stolen and a finder of the bill (Aman) presents it for the payment, a payment to the finder i.e., Aman would not be a payment in due course, if the person paying (Chaman) knows that the bill is a stolen bill and the person demanding payment i.e., Aman is not entitled to be paid. But if Chaman has no idea and makes the payment to Aman in good faith, it would be a payment in due course.
- ✓ **There is no ground for believing that possessor is not entitled to receive payment.**

GYAANI'S ONE LINERS

- ✓ According to Section 4 of the Negotiable Instruments Act, 1881, "A Promissory note is an instrument in writing (not being a bank note or a currency note) containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument."
- ✓ There are 2 parties to a promissory note i.e., Maker and Payee
- ✓ The person who makes the promissory note and promises to pay is called the maker.
- ✓ The person to whom the payment is to be made is called the payee.
- ✓ According to Section 5 of the Negotiable Instruments Act, 1881, "A bill of exchange is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument".
- ✓ There are three parties to bill of exchange i.e., Drawer, Drawee and Payee
- ✓ The person who gives the order to pay or who makes the bill is called the drawer.
- ✓ The person who is directed to pay is called the drawee. When the drawee accepts the bill, he is called the acceptor.
- ✓ The person to whom the payment is to be made is called the payee.
- ✓ According to Section 6 of the Negotiable Instruments Act, 1881, "A cheque is a bill of exchange drawn upon a specified banker and payable on demand and it includes the electronic image of a truncated cheque and a cheque in the electronic form."
- ✓ A cheque in the electronic form means "cheque which contains the exact mirror image of a proper cheque, and is generated, written and signed in a secure system ensuring the minimum safety standards with the use of digital signature and asymmetric crypto system."
- ✓ A truncated cheque means a cheque which is truncated during the course of a clearing cycle, either by the clearing house or by the bank whether paying or receiving payment, immediately on generation of an electronic image for transmission, substituting the further physical movement of the cheque in writing.
- ✓ A cheque is a specie of a bill of exchange; but it has the following two additional qualifications i.e., it is always drawn on a specified banker and it is always payable on demand.
- ✓ There are 3 parties to a cheque i.e., Drawer, Drawee and Payee
- ✓ The customer who signs the cheque is called "drawer".
- ✓ The bank on whom the cheque is drawn is called "drawee".

- ✓ The person to whom the payment is to be made is called the payee.
- ✓ By crossing the cheque, the drawer instructs the banker to not to pay it over the counter but only credit to the account of the person named therein. It adds to the security and thus ensures payment to the payee or to his order.
- ✓ A cheque may be crossed by the drawer of a cheque, the holder of a cheque and the banker.
- ✓ Every instrument payable, otherwise, then on demand is entitled to three days of grace.
- ✓ Instruments which are not entitled to 'period of grace' are cheque, a bill or note payable on demand and a bill or note in which no time is mentioned.
- ✓ If the due date falls on a public holiday, the bill becomes due on immediately preceding business day. If the month in which the period is to terminate has no corresponding day, the period will terminate on the last day of the month.
- ✓ Payment in due course means payment in accordance with the apparent tenor of the instrument in good faith and without negligence to any person in possession thereof.
- ✓ Payment in due course results in discharge of the instrument.

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DIFFERENCE BETWEEN VARIOUS NI

Difference	Promissory Note	Bills of Exchange	Cheque
Parties	2 Parties - Maker & Payee	3 parties – Drawer, Drawee and Payee	3 parties - Drawer, Banker and Payee
Nature	Contains an unconditional promise by maker to pay the payee	Contains an unconditional order to the drawee to pay the payee	Drawn on specified Banker to pay on demand.
Acceptance	Not necessary	Necessary if the bill is payable after sight.	Not necessary.
Liability	Liability of maker is primary and absolute.	Liability of drawer is conditional and secondary upon non payment by drawee.	Liability of drawer is conditional and secondary upon non payment by banker
Notice of Dishonor	Not necessary	Necessary	Not necessary
Payable	On demand or after a specified time. Cannot be made payable to bearer on demand or even after certain period.	On demand or after a specified time. Cannot be made payable to bearer on demand.	On demand even to bearer if so made.
Crossing	Not possible	Not possible	Can be crossed.
Noting and protesting In case of dishonor	Not required	Required to Establish the fact of dishonor.	Not required
Grace Period	Available if payable after specified time	Available if payable after specified time	Not available.
Stamping	Must be stamped.	Must be stamped.	Need not be stamped.

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CROSSING OF CHEQUES

INTRODUCTION

Section 123 to 131-A of the Negotiable Instruments Act, 1881 explains about “Crossing”. A cheque may be an ‘open cheque’ or a ‘crossed cheque’. The former may be presented across the counter for payment; the latter will have to be presented through another banker. While, in the case of an open cheque, payment may be obtained in cash, in the case of a crossed cheque, the amount will be credited to the account of the customer of a bank.

MEANING OF CROSSING

The act of drawing two diagonal or transverse parallel lines on the face of a cheque is called “crossing of the cheque”. In other words, a crossed cheque is one which has two transverse parallel lines. Crossing is a direction to the banker not to pay the money across the counter. It means the banker should pay the money only through banker.

OBJECTIVE OF CROSSING

The main object of crossing is to give protection and safeguard to the owner of the cheque. The crossed cheque cannot be paid across the counter but it should be paid only through an account with a bank, who may be either the drawee banker or a different one. If it is mis-utilized, it can be traced very easily and the fraudulent person can easily be detected.

TYPES OF CROSSING

There are different kinds of crossing: General crossing and Special crossing.

GENERAL CROSSING (SECTION 123)

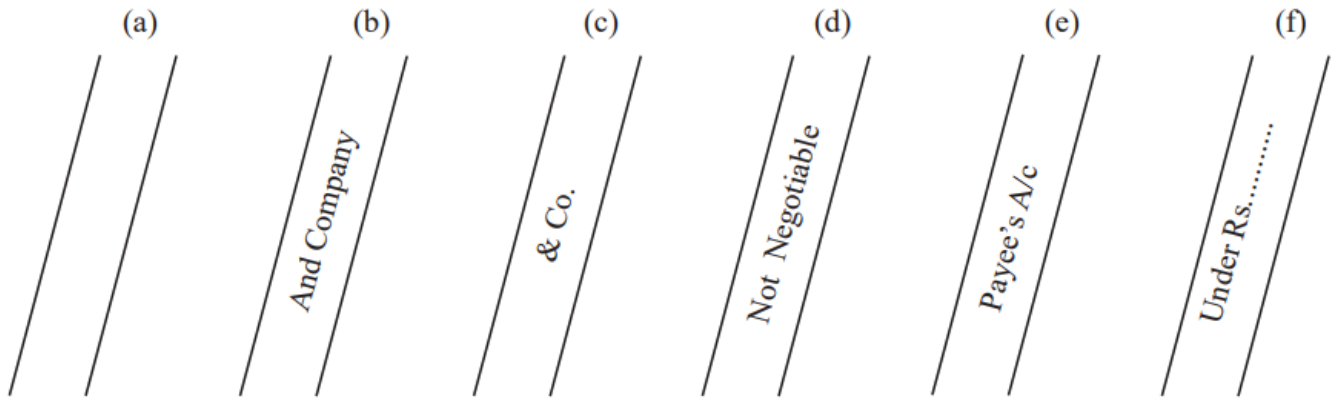
Where a cheque bears across its face an addition of the words “and company” or any abbreviation thereof, between two parallel transverse lines, or of two parallel transverse lines simply, either with or without the words “Not negotiable” that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed generally.

- ✓ **Two transverse lines** are the essentials of general crossing.
- ✓ The **lines should not occupy printed letters or numbers** or any such written matters.
- ✓ The lines are generally **drawn on the left-hand side**.
- ✓ **The words ‘and company’ / ‘& co.’ may be written between transverse lines**. But these words are not compulsory. The crossing itself is sufficient. However, it is the practice of the people to write those words.
- ✓ **The words ‘Not negotiable’ may be added** to a crossing. But they themselves do not constitute crossing.

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Forms of General Crossing

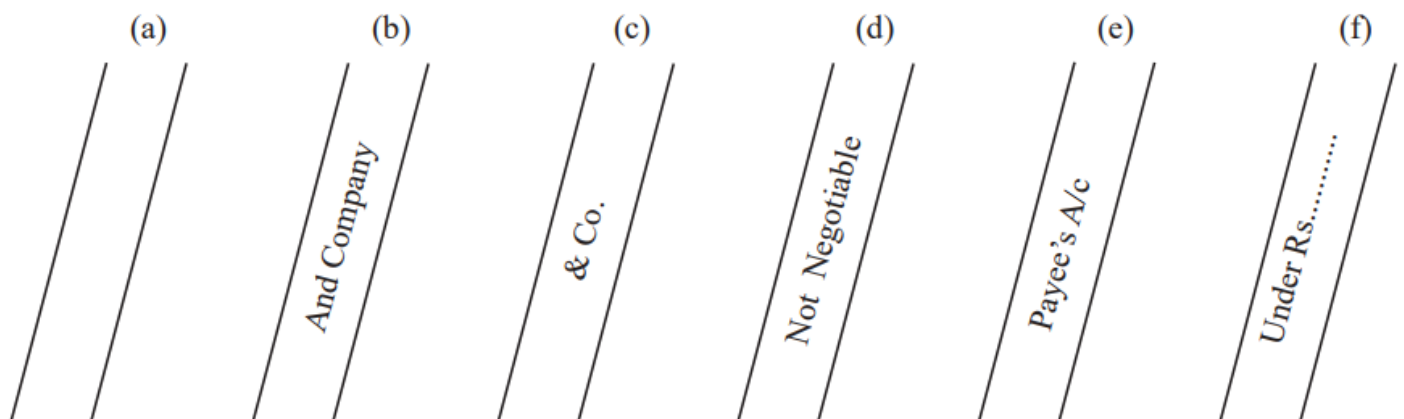


Effects of General Crossing

- ✓ **It gives a direction to the paying banker.**
- ✓ Sec. 126 of the NI Act, 1881 lays down that when a cheque is crossed generally, the banker on whom it is drawn shall not pay it otherwise than to a banker. Therefore, this type of cheque cannot be paid at counter. The payment should be made through an account only. Thus, the **General crossing gives protection and avoids fraudulent withdrawals.**
- ✓ It is the liability of the paying banker to verify proper payment in proper account. **The payment does not constitute "Payment in due course". The banker is answerable to his customer, if he pays the money to a third person without the direction of his customer.** He should not make any contract with third party concerning the cheque generally crossed.

SPECIAL CROSSING (SECTION 124)

Where a cheque bears across its face an addition of the name of a 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.



- ✓ **Two parallel transverse lines** are not essential.
- ✓ The **name of the bank should be mentioned** with or without crossing. **The name of the bank itself constitutes special crossing.**
- ✓ The name of the bank should be written on the **left side** of cheque.
- ✓ The name of the bank and **the words "Not Negotiable" or "A/c Payee" or "Not Negotiable" or "A/c Payee Only", may also be mentioned.**

Effects of Special Crossing

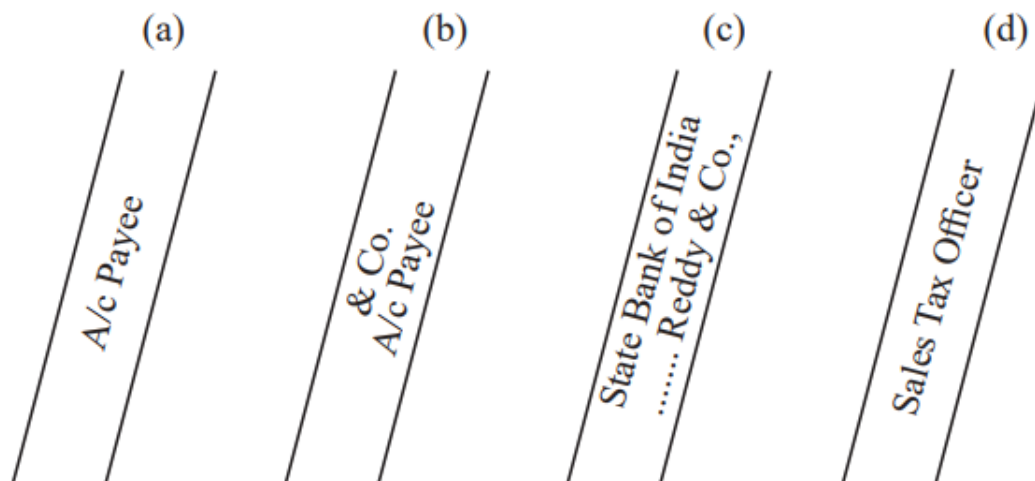
- ✓ It **prevents the fraudulent transactions** and misappropriation.

- ✓ It is **direction to the paying banker** to pay the amount to the account holder of that bank, but not to others.
- ✓ **If a cheque is specially crossed on a particular bank, and if such cheque is presented in another bank, the paying bank should refuse the payment.**
- ✓ **Special crossing gives more protection than general crossing.** In the case of special crossing, the banker's name and payee's name are mentioned, and the banker is well acquainted with the payee's name and signature. **If there is any forgery, he can easily detect it.**

Another type of crossing which is not defined in the Act but presents in usage is Restrictive Crossing or Account Payee Crossing.

Account Payee Crossing

In the present-day transactions, we find the terms "A/c Payee", "Account Payee", "Account Payee Only", on the cheques. It has developed in the trade and in common to use these terms on the left side of the cheque between the two transverse lines. But **there is no law mentioned about this type of crossing either in "The Bills of Exchange Act" of Great Britain or in "The Negotiable Instruments Act, 1881" of India. The terms mean that the amount should not be paid at counter, but should be credited into the account of the payee only.** However, the meaning of other crossings is also the same. This type of crossing only gives additional protection to the cheque.



Effects of Account Payee Crossing

- ✓ It is **merely in the form of direction** to the receiving bank that the drawer desires to pay the particular cheque into bank which keeps the account of the payee.
- ✓ A/c Payee crossing cheque **can also be transferable** like other cheques.
- ✓ It gives **further protection to the payee.** The collecting banker should credit the cheque only to the mentioned account of the payee.
- ✓ **If the banker credits the cheque to another's account and not to the account of the payee, the banker shall be held responsible for his negligence, and shall be held liable to pay the compensation.**
- ✓ The **safest method is to cross the cheque** with the terms of 'Not Negotiable' and 'A/c Payee only'.

Not Negotiable Crossing (Section 130)

Sections 123 and 124 of the Act permit the use of the words "Not Negotiable" in the crossing. Section 130 of the Act clarifies the position.

Section 130: A person taking a cheque crossed generally or specially, bearing in either case the words not negotiable shall not have, and shall not be capable of giving, a better title to the cheque than that which the person from whom he took it had.

The words “Not Negotiable” do not mean “not transferable”. If it is so, the very meaning and purpose of the cheque and its character of “Bill of Exchange” will die. “Transferability” is a narrower term than the word ‘negotiability’. The cheque “not transferable” crossed can also be transferred like any other cheque. But it gives more protection than General Crossing and Special Crossing. It is a warning to the paying and collecting bankers. Both of them should be very careful in the transaction of this type of cheques.

Object of Not Negotiable Crossing

The true owner is protected by this type of crossing more perfectly. If it is stolen, the finder cannot cash it so easily. The good title cannot be passed to him. He will be compelled to return it to the true owner. The owner’s right is preserved safely against any subsequent holder.

(a)
State Bank of Hyderabad
to Andhra Bank
(as agent for collection)

(b)
Pay to Andhra Bank as agent
for collection for State Bank
of Hyderabad.
(Sd) XXXXX
Manager.

Effects of Not Negotiable Crossing

- ✓ It gives more protection and safe to the holder of the cheque.
- ✓ A third person cannot cash it so easily.
- ✓ It can be transferred like any other cheque.
- ✓ If the banker is negligent and transfers the amount of that cheque to another account, he will be held responsible and he will be liable to make the compensation to the sufferer.

Double Crossing / Second Special Crossing (Section 125)

“Where a cheque is crossed specially, the banker to whom it is crossed may again cross it specially to another banker, his agent for collection” is called Double Crossing. This is the only case where a second special crossing is allowed by the Act, and that can be done only for the purpose of collection and that too by a banker. Therefore, it is called “Double Crossing” or “Second Special Crossing”. The private parties are not allowed to utilize double crossing.

Effects of Second special Crossing

- ✓ Double crossing is not permitted to general public. It is practiced only in case of transactions between the bankers. Others are not allowed to use double crossing.
- ✓ In case of Double crossing, it is the regular practice to cross at the back side of the cheque, where sufficient space is available.
- ✓ Sec. 127 lays down that where a cheque is crossed specially to more than one banker except when crossed to an agent for the purpose of collection, the banker on whom it is drawn shall refuse payment thereof.

- ✓ According to Sec. 127, it is necessary, in all cases, to specify in the second special crossing that the banker in whose favor it is made is an agent of the first banker for collection.

WHO CAN CROSS A CHEQUE

Generally, the maker of the cheque makes the crossing. If he does not cross, the holder of the cheque can cross it, or in certain occasions the banker may also cross it. Sec. 125 states about crossing after issue. According to Sec. 125 where a cheque is uncrossed, the holder may cross it generally or specially.

- ✓ Where a cheque is crossed generally, the holder may cross it specially.
- ✓ Where a cheque is crossed generally or specially, the holder may add the words “not negotiable”.
- ✓ Where a cheque is crossed specially, the banker to whom it is crossed may again cross it specially to another banker, his agent, for collection.

GYAANI'S ONE LINERS

- ✓ Section 123 to 131-A of the Negotiable Instruments Act, 1881 explains about “Crossing”.
- ✓ A cheque may be an ‘open cheque’ or a ‘crossed cheque’.
- ✓ The act of drawing two diagonal or transverse parallel lines on the face of a cheque is called “crossing of the cheque”.
- ✓ Crossing is a direction to the banker not to pay the money across the counter. It means the banker should pay the money only through banker.
- ✓ The main object of crossing is to give protection and safeguard to the owner of the cheque.
- ✓ Where a cheque bears across its face an addition of the words “and company” or any abbreviation thereof, between two parallel transverse lines, or of 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.
- ✓ Where a cheque bears across its face an addition of the name of a 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.
- ✓ If a cheque is specially crossed on a particular bank, and if such cheque is presented in another bank, the paying bank should refuse the payment.
- ✓ Special crossing gives more protection than general crossing.
- ✓ Sections 123 and 124 of the Act permit the use of the words “Not Negotiable” in the crossing.
- ✓ The words “Not Negotiable” do not mean “not transferable”. If it is so, the very meaning and purpose of the cheque and its character of “Bill of Exchange” will die. “Transferability” is a narrower term than the word ‘negotiability’. The cheque “not transferable” crossed can also be transferred like any other cheque. But it gives more protection than General Crossing and Special Crossing. It is a warning to the paying and collecting bankers. Both of them should be very careful in the transaction of this type of cheques.
- ✓ “Where a cheque is crossed specially, the banker to whom it is crossed may again cross it specially to another banker, his agent for collection” is called Double Crossing.
- ✓ Double crossing is not permitted to general public. It is practiced only in case of transactions between the bankers.

- ✓ Sec. 127 lays down that where a cheque is crossed specially to more than one banker except when crossed to an agent for the purpose of collection, the banker on whom it is drawn shall refuse payment thereof.
- ✓ According to Sec. 127, it is necessary, in all cases, to specify in the second special crossing that the banker in whose favor it is made is an agent of the first banker for collection.
- ✓ Where a cheque is crossed generally, the holder may cross it specially.
- ✓ Where a cheque is crossed generally or specially, the holder may add the words “not negotiable”.
- ✓ Where a cheque is crossed specially, the banker to whom it is crossed may again cross it specially to another banker, his agent, for collection.

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DISHONOUR OF CHEQUES

INTRODUCTION

A cheque is said to be honored if the banks give the amount to the payee. While, if the bank refuses to pay the amount to the payee, the cheque is said to be dishonored. In other words, dishonor of cheque is a condition in which the bank refuses to pay the amount of the cheque to the payee. **Whenever the cheque is dishonored, the drawee bank instantly issues a 'Cheque Return Memo' to the payee banker specifying the reasons for dishonor. The payee banker provides the memo and the dishonored cheque to the payee.**

FIVE INGREDIENTS OF THE OFFENCE UNDER SEC. 138

The offence under Sec. 138 of the Act can be attracted, given sufficient components of the said offence;

1. Drawing of the cheque,
2. Presentation of the cheque to the bank,
3. Returning the cheque unpaid by the drawee bank,
4. Giving notice in writing to the drawer of the cheque demanding payment of the cheque amount.
5. Failure of the drawer to make payment within 15 days of the receipt of the notice.

Upon such dishonor of an issued cheque, the payee can initiate legal proceedings under Section 138 of Negotiable Instruments Act, 1881.

SECTION 138 OF THE ACT

Dishonor of cheque for insufficiency of funds in the account. —Where any cheque drawn by a person on an account maintained by him with a banker for payment of any amount of money to another person from out of that account for the discharge, in whole or in part, of any debt or other liability, is returned by the bank unpaid, either because of the amount of money standing to the credit of that account is insufficient to honor the cheque or that it exceeds the amount arranged to be paid from that account by an agreement made with that bank, such person shall be deemed to have committed an offence and shall, without prejudice to any other provisions of this Act, **be punished with imprisonment for a term which may be extended to 2 years, or with fine which may extend to twice the amount of the cheque, or with both.** Provided that nothing contained in this section shall apply unless—

(a) the cheque has been presented to the bank within a period of 6 months (reduced to 3 months after RBI circular dated 04,11.2011, effective from 01/04/2012) from the date on which it is drawn or within the period of its validity, whichever is earlier;

(b) the payee or the holder in due course of the cheque, as the case may be, makes a demand for the payment of the said amount of money by giving a notice in writing, to the drawer of the cheque, within 30 days of the receipt of information by him from the bank regarding the return of the cheque as unpaid; and

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(c) the drawer of such cheque fails to make the payment of the said amount of money to the payee or, as the case may be, to the holder in due course of the cheque, within 15 days of the receipt of the said notice.

EXPLANATION

For the purposes of this section, “debt or other liability” means a legally enforceable debt or other liability. Section 138 of the NI Act Marginal Note stating “Dishonor of cheque for insufficiency etc. of funds in accounts” addition of word “etc.” cannot be considered to be an accident.”

In short, upon dishonor of cheque a payee can, in exercise of his dues, initiate a legal notice for demand of the same within 30 days of receipt of the cheque dishonor memo. The said drawer of the cheque is bound to pay within 15 days of the receipt of the said notice, or the right to sue, for the payee arises from the same.

SECTION 143A OF THE ACT

Section 143A of the Act states that :-

(1) Notwithstanding anything contained in the Code of Criminal Procedure, 1973, **the Court trying an offence under section 138 may order the drawer of the cheque to pay interim compensation to the complainant—**

(a) in a summary trial or a summons case, where he pleads not guilty to the accusation made in the complaint; and

(b) in any other case, upon framing of charge.

(2) The **interim compensation** under sub-section (1) **shall not exceed 20% of the amount** of the cheque.

(3) The interim compensation **shall be paid within 60 days from the date of the order** under sub-section (1), or within such **further period not exceeding 30 days as may be directed by the Court** on sufficient cause being shown by the drawer of the cheque.

(4) **If the drawer of the cheque is innocent, the Court shall direct the complainant to repay to the drawer the amount of interim compensation, with interest at the bank rate as published by the Reserve Bank of India, prevalent at the beginning of the relevant financial year, within 60 days from the date of the order, or within such further period not exceeding 30 days as may be directed by the Court** on sufficient cause being shown by the complainant.

In Rakesh Nemkumar Porwal vs. Narayan Dhondu Joglekar - Citation-(1993), the Honorable Bombay High Court held that **“Any reason for dishonor is an offence.”**

GYAANI'S ONE LINERS

- ✓ A cheque is said to be honored if the banks give the amount to the payee.
- ✓ If the bank refuses to pay the amount to the payee, the cheque is said to be dishonored.
- ✓ Whenever the cheque is dishonored, the drawee bank instantly issues a ‘Cheque Return Memo’ to the payee banker specifying the reasons for dishonor.
- ✓ When a cheque is dishonor of cheque for insufficiency of funds in the account the person shall be punished with imprisonment for a term which may be extended to 2 years, or with fine which may extend to twice the amount of the cheque, or with both.

- ✓ Upon dishonor of cheque a payee can, in exercise of his dues, initiate a legal notice for demand of the same within 30 days of receipt of the cheque dishonor memo. The said drawer of the cheque is bound to pay within 15 days of the receipt of the said notice, or the right to sue, for the payee arises from the same.
- ✓ Section 143A of the Act states that the Court trying an offence under section 138 may order the drawer of the cheque to pay interim compensation to the complainant which shall not exceed 20% of the amount of the cheque.
- ✓ The interim compensation shall be paid within 60 days from the date of the order or within such further period not exceeding 30 days as may be directed by the Court on sufficient cause being shown by the drawer of the cheque.
- ✓ If the drawer of the cheque is innocent, the Court shall direct the complainant to repay to the drawer the amount of interim compensation, with interest at the bank rate as published by the RBI, prevalent at the beginning of the relevant financial year, within 60 days from the date of the order, or within such further period not exceeding 30 days as may be directed by the Court on sufficient cause being shown by the complainant.
- ✓ In *Rakesh Nemkumar Porwal vs. Narayan Dhondu Joglekar* - Citation-(1993), the Honorable Bombay High Court held that “Any reason for dishonor is an offence. ”

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