



LIVE VIRTUAL CLASSES

BOARD OF STUDIES, ICAI

CA FOUNDATION

TOPIC NAME – THE NEGOTIABLE INSTRUMENT ACT 1881

CHAPTER - 7

PAPER 2: BUSINESS LAWS

Faculty Name: CA Sudeep Kumar Jain

**“Our greatest
weakness lies in
giving up. The most
certain way to
succeed is always
to try just one
more time.”**

Thomas Edison





Negotiable Instruments Act

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

3



COMMENCEMENT

The Negotiable Instruments Act, 1881

- came into force on first day of March 1882.

Recent developments

The Act was amended several times by:

- The Negotiable Instruments (Amendment and Miscellaneous Provisions) Act, 2002;
- The Negotiable Instruments (Amendment) Act, 2015, and
- The Negotiable Instruments (Amendment) Act, 2018.

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

4

Negotiable Instruments

Definition

The Act does not define the term 'NI'.

However, Section 13 provides for only 3

- Promissory notes
- Bills of exchange
- Cheques

-payable either to order or bearer

NEGOTIABLE INSTRUMENT



Negotiable Instruments

Meaning

Every document

- which entitles a person
- to a sum of money and
- which is transferable
- by delivery or
- by endorsement & delivery.

NEGOTIABLE INSTRUMENT



Negotiable Instruments

To Sum up

Therefore, an instrument may be negotiable either by:-

Statute (Law)

- PN,
- BOE,
- Cheque

Usage (In India)

- Hundi,
- Bearer debentures,
- Share warrants,
- Dividend warrants,
- Delivery orders
- Railway receipts

NEGOTIABLE INSTRUMENT



Order Instrument v/s Bearer Instrument

Order Instrument

- It is expressed to be so payable
- When it is expressed to be payable to a specified person and does not contain words prohibiting its transfer. (i.e. it is transferrable by endorsement and delivery)



Bearer Instrument

- A negotiable instrument which is expressed to be payable to bearer.
- A negotiable instrument on which the last endorsement is in blank.



Order Instrument v/s Bearer Instrument

Rs.10,000

Lucknow

April 10, 2022

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)

Back Side

Endorsement of NI

Meaning

Endorsement means

- **Signing** – on the face or back of NI; or
– on a slip of paper annexed to NI
- **by** – the holder of negotiable instrument
- **for the purpose of** negotiating such NI.

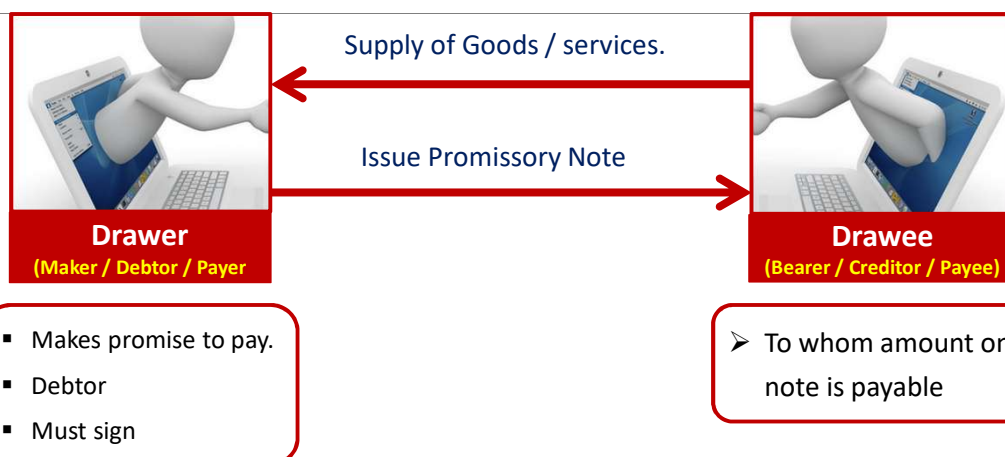
Essential requirements of a valid endorsement

(a) Writing	The endorsement must be in writing.
(b) Signed	The endorsement shall not be valid unless it is signed.
(c) By holder	The endorsement shall be valid only if the NI is signed by holder

Essential Characteristics of NI

- In writing.
- Signed.
- Freely transferable from one person to another.
- Holder's title is free from defects.
- Can be transferred any number of times till its satisfaction.
- Contain an unconditional promise or order to pay some money only.
- The sum payable, the time of payment, the payee, must be certain.
- Delivery is must.

Parties to Promissory Note





Essential Characteristics of Promissory Note

a. **In writing:** An oral promise to pay is not sufficient.

b. There must be **an express promise to pay**. Mere acknowledgment of debt is insufficient.

Get it in WRITING!



Example 1: *"I acknowledge myself to be indebted to B in Rs.1,000, to be paid on demand, for value received."*

(Valid PN as the promise to pay is definite).

Example 2: *"Mr. B, I.O.U Rs.1,000."*

(Invalid PN as there is no promise to pay. It is just an acknowledgement of debt.)



Essential Characteristics of Promissory Note

c. **Definite & Unconditional Promise.**

Example 3: *"I promise to pay B Rs.500 seven days after my marriage with C."*

(Invalid PN as marriage with C may or may not happen.).

Exceptions : An instrument is made payable on the happening of a **certain event** which is **bound to happen**, it is valid promissory note.

Example 4: *"I promise to pay B Rs.500 on D's death"*

(as death of D is certain, promise is unconditional. Thus, the promissory note is valid.)

Example 5: *"I promise to pay B Rs.500 on D's death, provided D leaves me enough to pay that sum."* Invalid PN as promise is dependent on D's leaving behind money which is not certain.



Essential Characteristics of Promissory Note

d. **signed by the maker** otherwise it is incomplete and ineffective.

e. **Promise to pay money only**

Example 6: *"I promise to pay B Rs.500 and to deliver to him my black horse on 1st January next."*

Invalid PN, as the promisor needs to deliver its black horse which is not money.

Example 6a: *"I promise to pay B in 30 shares and 20 bonds of a company."*

Invalid PN



Essential Characteristics of Promissory Note

f. **Promise to pay a certain sum**

Example 7: *"I promise to pay B Rs.500 and all other sums which shall be due to him."*

Invalid PN as the amount payable is not certain.

But sometimes, the language of a promissory note is such that the amount payable can be easily ascertained. In such cases, the promissory note will be **valid**.

Example 8: *"I promise to pay B Rs.500 alongwith simple interest at the rate of 12% p.a."*



Essential Characteristics of Promissory Note

g. Maker & payee must be certain, definite and different persons:

A PN cannot be made payable to the bearer.

Only RBI or CG can make or issue a promissory note 'payable to bearer'. [Section 31 of the Bank of India Act, 1934 (RBI Act)].

Sometimes party may be described by designation. E.g. Branch Manager of State Bank of India, Kamla Nagar, Agra.

h. Stamped: A promissory note must be stamped.

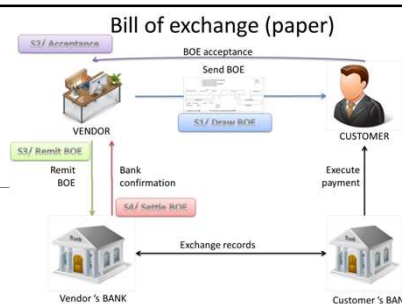
Bills of Exchange (Sec. 5)


Meaning

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.

E.g. A wrote and signed an instrument ordering B to pay Rs. 500 to C. This is a bill of exchange. In this instrument B has been ordered to pay Rs. 500 to C.





Parties to Bills of Exchange

Drawer

- Who draws or makes the bill.
- His liability is secondary and conditional.
- His liability is primary and conditional until the bill is accepted.


Drawee

- On whom the bill is drawn
- On acceptance of the bill -
 - (a) he is called as acceptor'
 - (b) he becomes liable for the payment of the bill;
 - (c) his liability is primary and unconditional.


Payee

- To whom or to whose order the money is, by the instrument, directed to be paid

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
19




Parties to Bills of Exchange



Drawer

(Maker / Creditor / Payee)



Drawee

(Debtor / Payer / Acceptor)

←

Supply of Goods / services.

→

←

Drawing BOE

→

←

Accepting BOE

→

Note: Drawer or payee may be different person.

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
20



Essential Characteristics of Bills of Exchange

- a. **In writing:** An oral promise to pay is not sufficient.
- b. There must be **an express order to pay**.
- c. **Definite & Unconditional Order.**
- d. **signed by the maker** otherwise it is incomplete and ineffective.

Get it in WRITING!



Essential Characteristics of Bills of Exchange

e. **Drawer, drawee, and payee must be certain.** All these three parties may not necessarily be three different persons. One can play the role of two. But there must be two distinct persons in any case.

As per S. 31 of RBI Act, 1934, a BOE **cannot be** made **"payable to bearer on demand"**.

Example 9: *"On demand pay to the bearer the sum of Rs.500, for value received."*

It is **invalid BOE**.

However, a BOE payable on demand, in which name of the payee is mentioned, is valid.

Example 10: *"On demand pay to A or order Rs.500 for value received."*

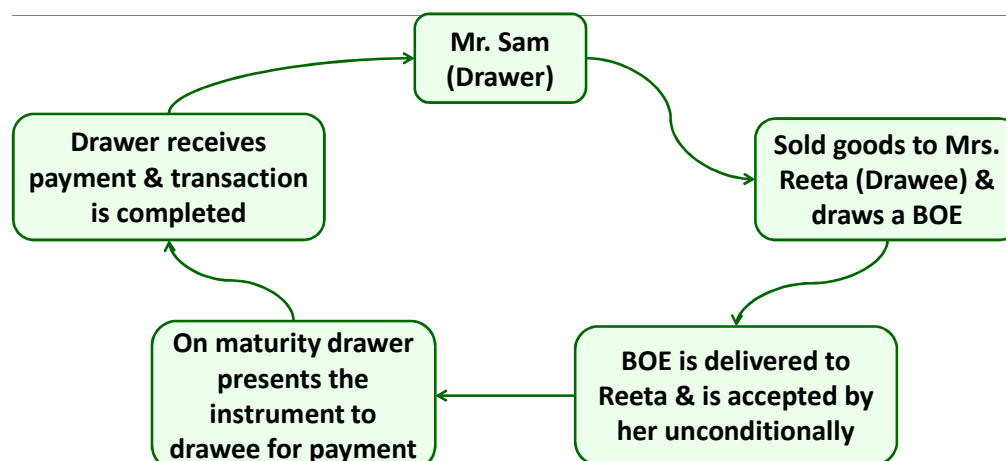
It is **valid BOE**.

Essential Characteristics of Bills of Exchange



- f. Order to pay a certain sum
- g. Order to pay money only
- h. **Stamped**: A BOE must be stamped.

Process of Bills of Exchange





Difference b/w PN & BOE

Basis	Promissory Note	Bills of Exchange
1. Definition	An instrument in writing (not being a banknote 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.	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.
2. Nature of Instrument	A promise to pay money.	An order for making payment.
3. Parties	2 parties - maker & payee	3 parties – drawer, drawee & payee
4. Acceptance	Does not require any acceptance	Needs acceptance from the drawee
5. Payable to bearer	Cannot be made payable to bearer.	Can be drawn payable to bearer. However, it cannot be payable to bearer on demand.

Let's Revise

REVISION TIME



NEGOIABLE INSTRUMENT	<p>Every document which entitles a person to a sum of money and which is transferable by delivery or by endorsement and delivery, is entitled to be called a negotiable instrument.</p> <p>Therefore, an instrument may be negotiable either by (i) Statute (Promissory notes, bills of exchange and cheques) (ii) Usage (Hundi, bearer debentures, share warrants, dividend warrants, delivery orders and railway receipts) (In India)</p>
CHARACTERISTICS	<ol style="list-style-type: none"> 1. In writing, 2. Signed, 3. Freely transferable, 4. Title free from defects, 5. Can be transferred any number of times, 6. Unconditional promise or order to pay money, 7. Certainty of sum payable, time of payment & payee, 8. Delivery

Let's Revise

REVISION TIME



P/N MEANING	An instrument in writing (not being a bank note or a currency note) containing <ul style="list-style-type: none"> ➤ an unconditional undertaking signed by the maker ➤ to pay a certain sum of money only to a certain person; ➤ or the order of a certain person; or the bearer of the instrument.
CHARACTERISTICS	(a) In Writing, (b) Express Promise to pay, (c) Definite and unconditional promise, (d) Signed by maker, (e) Promise to pay money only, (f) Promise to pay a certain sum, (g) Payee must be certain, (h) Stamped

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

27

Let's Revise

REVISION TIME



BOE MEANING	An instrument in writing containing <ul style="list-style-type: none"> ➤ an unconditional order signed by the maker ➤ Directing a certain person to pay a certain sum of money only to a certain person; ➤ or the order of a certain person; or the bearer of the instrument. <p>Note: BOE cannot be made payable to bearer on demand.</p>
CHARACTERISTICS	(a) In Writing, (b) Express Order to pay, (c) Definite and unconditional order, (d) Signed by drawer, (e) Order to pay money only, (f) Order to pay a certain sum, (g) Drawer, Drawee & Payee must be certain, (h) Stamped

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

28

Cheque



Meaning

A "Cheque" is a BOE

- drawn on a specified banker
- and not expressed to be payable otherwise than on demand (i.e., it is always payable on demand)
- and it includes
 - 'the electronic image of truncated cheque'; and
 - 'a cheque in electronic form'.

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

29

Cheque (Sec. 6)



To Be Noted

A "Cheque" requires

- All the essentials of a bill of exchange.
- Drawn on a specified banker.
- Payable on demand.

A "Cheque" **does not require** (a) stamping; or (b) acceptance;

Payable on demand means- It should be payable whenever the holder chooses to present it to the drawee (the banker).

The expression "Banker" includes any person acting as a banker and any post office saving bank [Section 3]

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

30

Cheque (Sec. 6)

Explanation I

a. **Cheque in the electronic form**-means a cheque drawn in electronic form by using any computer resource, and signed in a secure system with a digital signature (with/without biometric signature) and asymmetric crypto system or electronic signature, as the case may be;

Note- For the purposes of this section, the expressions "asymmetric crypto system", "computer resource", "digital signature", "electronic form" and "electronic signature" shall have the same meanings respectively assigned to them in the Information Technology Act, 2000



Cheque (Sec. 6)

Explanation I

b. "a **truncated cheque**" means a cheque which is truncated during 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.



Cheque (Sec. 6)



Explanation II

For the purposes of this section, the expression “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.

Explanation III

For the purposes of this section, the expressions “asymmetric crypto system”, “computer resource”, “digital signature”, “electronic form” and “electronic signature” shall have the same meanings respectively assigned to them in the Information Technology Act, 2000.

Cheque (Sec. 6)



	Date:.....
Pay	
a sum of Rupees	Rs.
A/C No. 12345678910	
ABC Bank	
622, Vijay Nagar, Indore (M. P.)	
Signature	
01212 1125864 000053 38	

Cheque (Sec. 6)



Drawer

- Who draws or makes the cheque.
- His liability is secondary and conditional.

Drawee

- The specific bank on whom cheque is drawn.

Payee

- The person to whom money is to be paid
- The payee may be the drawer himself or a third party.

“drawee in case of need”— When in the bill or in any indorsement thereon, the name of any person is given in addition to the drawee to be resorted to in case of need such person is called a “drawee in case of need”.

Classification of NI



Bearer Instrument (Sec. 13)

- A NI which is **expressed to be payable to bearer**, or
- A NI on which the **last endorsement is in blank**.
- Negotiated by **merely delivery**.
- As per the provisions of the **RBI Act, 1934**, -
PN – **cannot** be made **payable to bearer**.
BOE – **cannot** be made **payable to bearer on demand**

Order Instrument (Sec. 13)

- A NI **payable to a particular person**.
- A NI **payable to a particular person or his order**.
- A NI on which the **last endorsement is in Full**.
- Negotiated by **endorsement & delivery**.



Classification of NI

Inland Instrument (Sec. 11)	Place where Instrument drawn and made is payable	Residence of Person on whom Instrument is drawn	Nature of Instrument
	P/N, BOE, C drawn / made in India	+ Payable in India OR + drawn upon a person resident in India	



Inland Instrument


Classification of NI

Example 11:

- (i) A promissory note made in Kolkata and payable in Mumbai.
- (ii) A bill drawn in Varanasi on a person resident in Jodhpur (although it is stated to be payable in Singapore)
- (iii) A, a resident of Agra, drew (i.e., made) a bill of exchange in Agra on B, a merchant in New York. And B accepted the bill of exchange as payable in Delhi. It is an inland bill of exchange. In this case, the bill of exchange was drawn in India and also payable in India.

Inland Instrument

Classification of NI



(iv) A, resident of Mumbai, drew a bill of exchange in Mumbai on B, a merchant in Mathura. And B accepted the bill of exchange as payable in London. It is also an inland bill of exchange. In this case, the bill of exchange was drawn in India on a person resident in India. It is immaterial that the amount is payable in London.


An inland instrument remains inland even if it has been endorsed in a foreign country.

(v) If the bills of exchange mentioned in above two examples, are endorsed in France, they will remain inland bills.

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
39

Foreign Instrument (Sec. 12)

Classification of NI




Place where Instrument drawn	Residence of Person on whom drawn and place where made payable	Nature of Instrument
P/N, BOE, C drawn / made outside India	on a person resident in or outside India + payable in India	Foreign Instrument
	on a person residing outside India + payable outside India	
	on a person residing outside India + payable outside India	

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
40

Foreign Instrument (Sec. 12)

Classification of NI




E.g. 1. A drew a bill of exchange in India on B, a merchant residing in London. It was also made payable in London. It is a foreign bill of exchange.

E.g. 2. A drew a bill of exchange in London on B, a merchant residing in London. But the bill of exchange was made payable in India. It is also a foreign bill.

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
41

Liability of maker/ drawer of foreign bill:

Classification of NI



In the absence of a contract to the contrary, **the liability of the maker or drawer of a foreign PN or BOE or cheque is regulated** in all essential matters by the law of the place where he made the instrument & **the respective liabilities of the acceptor and indorser** by the law of the place where the instrument is made payable (Section 134).

Example 12: A BOE is drawn by A in Berkley where the rate of interest is 15% and accepted by B payable in Washington where the rate of interest is 6%. The bill is indorsed in India and is dishonoured. An action on the bill is brought against B in India. He is liable to pay interest at the rate of 6% only. But if A is charged as drawer, he is liable to pay interest at 15%.

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
42

Inchoate Instrument

Classification of NI



- An inchoate instrument is a blank or an incomplete instrument.
- When a person signs and delivers to another a blank or incomplete stamped instrument, he authorizes the other person to complete a NI for any amount not exceeding the amount covered by the stamp.
- When the NI is so filled up, the person signing the instrument becomes liable, in the capacity in which he has signed, to any holder in due course for such amount.
- The liability of the signer is restricted to the amount specified in the instrument which is covered by the stamp.
- It may be noted here that no person other than a holder in due course can recover from the person delivering the instrument anything in excess of the amount intended to be paid by him.

Inchoate Instrument

Classification of NI



Example 13: A owed Rs.500 to B. He gave a stamped and signed promissory note to B leaving blank the space for amount. And B filled Rs.700, in the space left for amount. In this case, B cannot recover Rs.700 from A as B is not a holder in due course. He can recover Rs.500 only which A intended to pay under the instrument.

If after completing the promissory note for Rs.700, B transfers it to C, a holder in the due course, then C will be entitled to recover the full amount of Rs.700 if the stamp affixed is sufficient to cover Rs.700. And A will be bound to pay the full amount to C.

Ambiguous Instrument

Classification of NI



- An **ambiguous instrument** is one which in form is such that it may **either be treated as a PN or BOE**.
- In such cases, **the holder may** either treat it as a PN or BOE.
- **Once he exercises his option, he is bound by it**, i.e., he cannot fall back that it is the other kind of instrument.

Ambiguous Instrument

Classification of NI



Example a: A firm was carrying on its business in Bombay and Delhi. Its Bombay branch drew a BOE on the Delhi branch. In this case, the holder of the BOE, may also treat it as a promissory note drawn by the Bombay branch payable in Delhi. The reason for the same is that the drawer and the drawee of the bill of exchange are the same person.

Example b: A drew a BOE on B, a fictitious person (not in existence). And A endorsed the BOE in favour of C and delivered the same to him. In this case also, C may treat the bill of exchange as a PN made by A. The reason for the same is that where the drawee is a fictitious person, the instrument is ambiguous.

Let's Revise

REVISION TIME



Cheque [Sec. 6]	<p>A Cheque is a bill of exchange</p> <ul style="list-style-type: none"> ➤ drawn on a specified banker and ➤ not expressed to be payable otherwise than on demand (i.e., it is always payable on demand) and it includes <p>– ‘the electronic image of truncated cheque’; and – ‘a cheque in electronic form’</p>
Characteristics	<p>Characteristics</p> <ul style="list-style-type: none"> ➤ All the essentials of a BOE ➤ Drawn on a specified banker. ➤ Payable on demand. <p>A cheque does not require:</p> <p>(a) Stamping; or (b) acceptance;</p>

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

47

Let's Revise

REVISION TIME

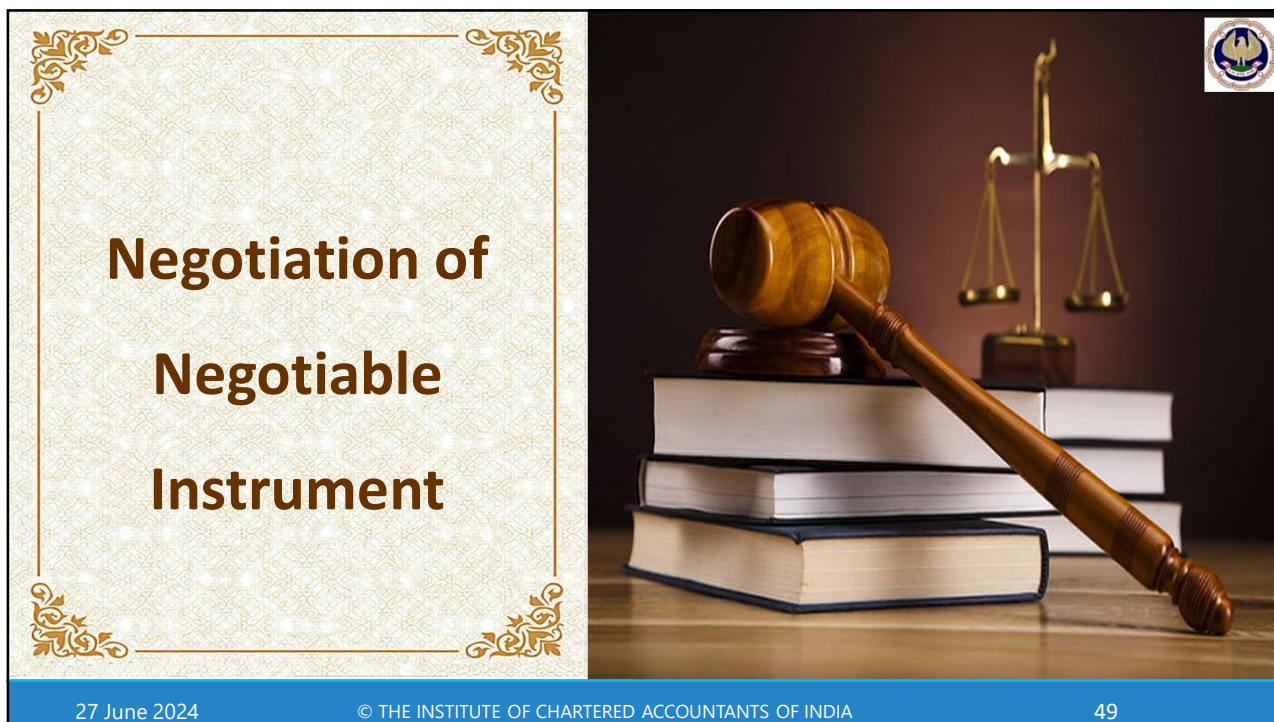


Classification	<p>Bearer Instrument: Expressed to be payable to bearer or the last endorsement is in blank.</p> <p>Order Instrument: Payable to a particular person or order and which does not restrict its further transfer.</p> <p>Inland Instrument: Drawn in India + (Payable in India or Drawn on any person resident in India)</p> <p>Foreign Instrument: Which is not an Inland Instrument.</p> <p>Inchoate Instrument: Incomplete Instrument in certain respects.</p> <p>Ambiguous Instrument: Which either be treated as P/N or BOE. (Once holder exercises his option, he is bound by it)</p>
-----------------------	---

27 June 2024

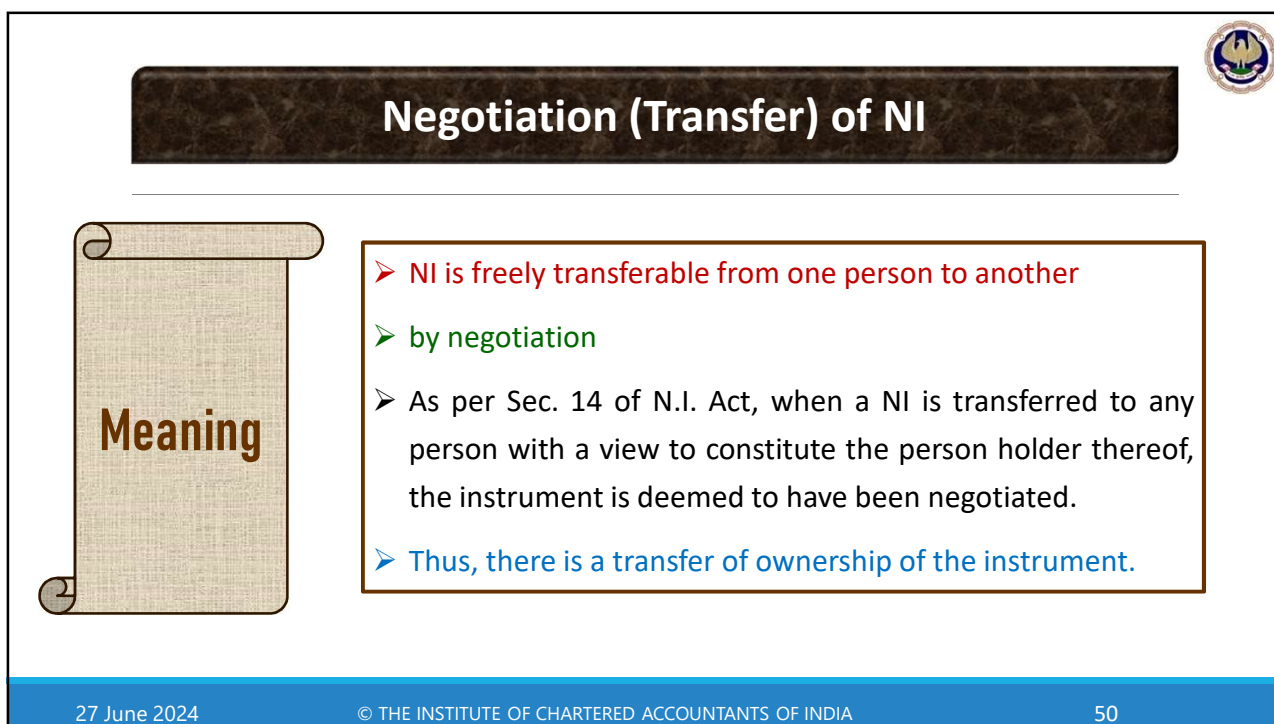
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

48



Negotiation of Negotiable Instrument

27 June 2024 © THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA 49

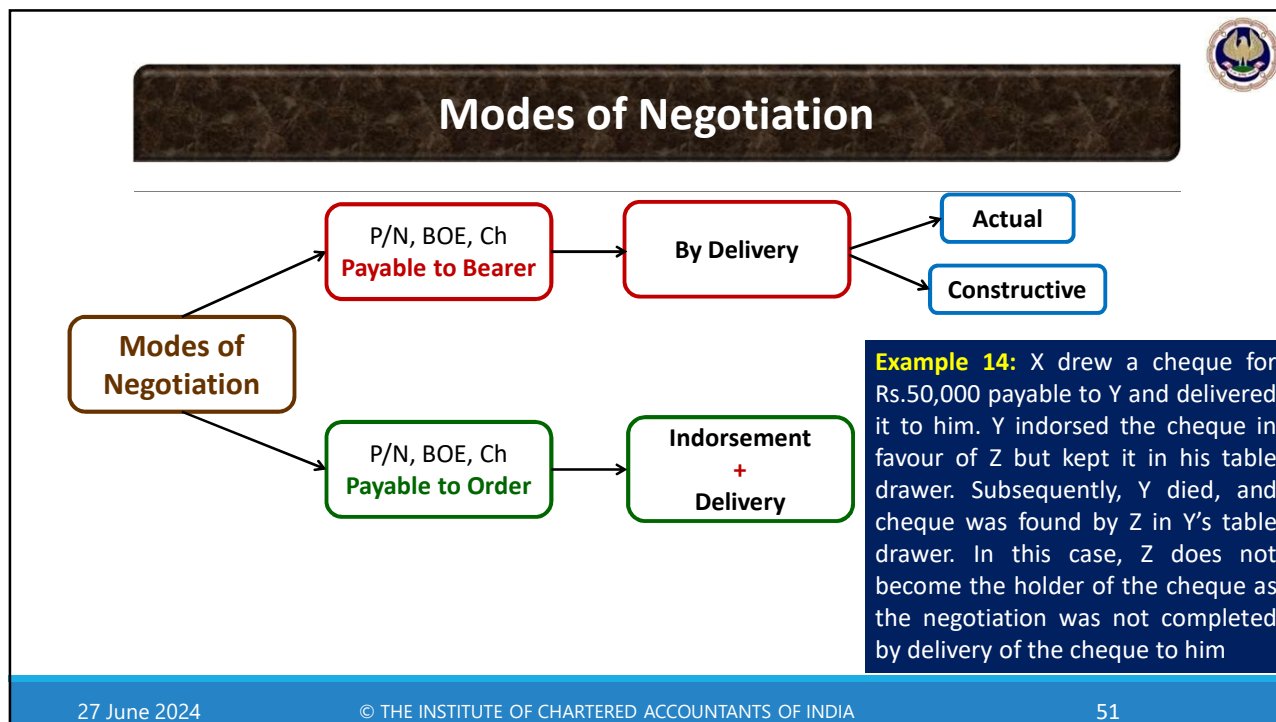


Negotiation (Transfer) of NI

Meaning

- NI is freely transferable from one person to another
- by negotiation
- As per Sec. 14 of N.I. Act, when a NI is transferred to any person with a view to constitute the person holder thereof, the instrument is deemed to have been negotiated.
- Thus, there is a transfer of ownership of the instrument.

27 June 2024 © THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA 50



Modes of Negotiation

Negotiation By Delivery

Subject to section 58 [Instrument obtained by unlawful means or for unlawful consideration], a P/N, BOE or ch. **payable to bearer** is negotiable by delivery thereof.

Exception: A P/N, BOE or cheque delivered on condition that it is not to take effect except in a certain event is not negotiable (except in the hands of a holder for value without notice of the condition) unless such event happens.

Example 15(a): A, the holder of a negotiable instrument payable to bearer, delivers it to B's agent to keep for B. The instrument has been negotiated.

Example 15(b): A, the holder of a negotiable instrument payable to bearer, which is in the hands of A's banker, who is at the time the banker of B, directs the banker to transfer the instrument to B's credit in the banker's account with B. The banker does so, and accordingly now possesses the instrument as B's agent. The instrument has been negotiated, and B has become the holder of it.

27 June 2024 © THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA 52



Some Important Points regarding Delivery

- Delivery of an instrument is essential.
- The delivery may be actual or constructive.
- Actual delivery takes place when the instrument changes hand physically.
- Constructive delivery takes place when the instrument is delivered to the agent, clerk or servant of the indorsee on his behalf or when the indorser, after indorsement, holds the instrument as an agent of the indorsee.
- When an instrument is conditionally or for a special purpose only, the property in it does not pass to the transferee, even though it is indorsed to him, unless the instrument is negotiated to a holder in due course.

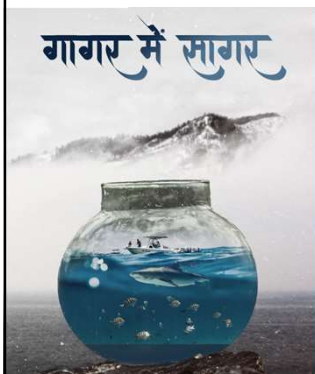


Some Important Points regarding Delivery

- The rights in the instrument are not transferred to the indorsee unless after the indorsement the same has been delivered.
- If a person makes the indorsement of instrument but before the same could be delivered to the indorsee, the indorser dies then the legal representatives of the deceased person cannot negotiate the same by mere delivery thereof. (Section 57)



Dishonour of Cheque (Sec.138 to Sec. 142)



- **Debt** - Cheque was issued to discharge a legally enforceable debt.
- **Reason for dishonor** - insufficiency of funds
- **Presentment of cheque** - Within 3 months or validity period of cheque.
- **Demand made from drawer** - Within 30 days of dishonor
- **Default by drawer to pay** - within 15 days of demand made
- **Complaint by holder** - Within 1 month , with the court.

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

55



Dishonour of Cheque (Sec.138 to Sec. 142)

Nature of Liability

- If a cheque issued by the drawer is dishonoured
- due to insufficiency of funds,
- the drawer is punishable with
- **Imprisonment** upto 2 year or
- **Fine** upto 2 times the amount of cheque or
- **Both.**

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

56



Dishonour of Cheque (Sec.138 to Sec. 142)

Conditions for attracting liability u/s 138

Cheque issued to discharge a liability

- The liability u/s 138 arises only if the drawer had issued the cheque to discharge a legally enforceable debt or other liability.
- Thus, where the drawer issues a cheque as a gift or charity, he is not liable under section 138 even if cheque is dishonored.

- **Presumption in favour of holder (Sec.139).** It shall be presumed that the holder of a cheque received the cheque in whole or in part, of any debt or other liability.
- Thus, the burden to prove that the cheque in a particular case was not given to discharge a legally enforceable debt or liability, lies on the drawer.

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

57



Dishonour of Cheque (Sec.138 to Sec. 142)

Conditions for attracting liability u/s 138

Dishonour due to insufficiency of funds

- The cheque must have been dishonoured due to **insufficiency of funds** in the account of the drawer.

Presentment of cheque within validity period

- Cheque must have been presented for payment to bank within 3 months from the date on which it was drawn.


Notice to drawer

- The payee/ holder must give a notice to the drawer of the cheque. The notice must fulfill the following conditions:
- It must be in writing.
- Must be given within 30 days of receipt of information of dishonor of cheque from bank.
- The notice must require the drawer to make payment of the money due on the cheque, i.e., the payee/holder must demand the money due under the cheque.

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

58



Dishonour of Cheque (Sec.138 to Sec. 142)

Conditions for attracting liability u/s 138


Default in payment by drawer

- The liability u/s 138 is attracted only if, **within 15 days** of receipt of notice from the payee/ holder, the drawer fails to pay the whole of the money due under the cheque.
- If drawer makes **only a part payment**, it is considered as a default by drawer. Thus, **the cause of action arises on 16th day** from the day of receipt of notice from the payee/ holder.

Payee / holder must make a complaint with court (S. 142)

- Following points are worth noting in this regard:
 - **The complaint must be in writing.**
 - **within 1 month from the date when cause of action arose**, i.e., within 1 month from the last day on which drawer was liable to pay the money to the payee/holder.
 - **Complaint shall be made with a court** not inferior to that of a metropolitan Magistrate or a judicial Magistrate of the first class.

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
59



Dishonour of Cheque (Sec.138 to Sec. 142)

Conditions for attracting liability u/s 138

Defence not allowed (Sec.140)

- **It shall not be a defence in a prosecution of an offence u/s 138.**
- **That the drawer had no reason to believe**
- **When he issued the cheque**
- **That cheque may be dishonoured on presentment for the reason stated in that section.**

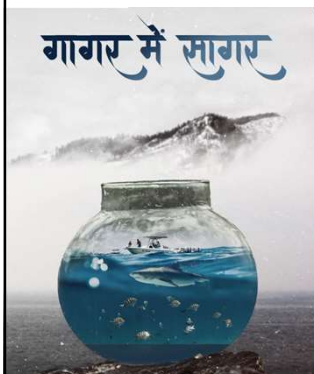
Effect of 'stop payment' order

- **Where the drawer makes 'stop payment' order**
- **to the banker (i.e. he countermands payment) resulting in dishonor of the cheque,**
- **it has the same effect as if the cheque had been dishonoured**
- **due to insufficiency of funds.**
- **Thus, the proceedings u/s 138 may be initiated against the drawer.**

27 June 2024
© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA
60



Dishonour of Cheque (Sec.138 to Sec. 142)



- **Debt** - Cheque was issued to discharge a legally enforceable debt.
- **Reason for dishonor** - insufficiency of funds
- **Presentment of cheque** - Within 3 months or validity period of cheque.
- **Demand made from drawer** - Within 30 days of dishonor
- **Default by drawer to pay** - within 15 days of demand made
- **Complaint by holder** - Within 1 month , with the court.



Presentment of Instrument

Presentment for acceptance (Only for BOE) (S. 61)

BOE payable after sight must	Must be presented within a reasonable time & in business hours on a business day. <i>(Note: 48 hours, excluding public holidays, are given to drawee for acceptance)</i>	
In default of such presentment	no party liable thereto	<i>If Drawee not found after reasonable search, BOE is dishonoured.</i>
If BOE is directed to drawee at a particular place	must be presented at that place	



Presentment of Instrument

Presentment of Promissory Note for sight

P/N payable at a certain period after sight	<p>Must be presented</p> <ul style="list-style-type: none"> ➤ within a reasonable time & ➤ in business hours ➤ on a business day.
In default of such presentment	no party liable thereto

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

63



Presentment of Instrument

Rules regarding presentment for payment (P/N, BOE, CH)

To whom	➤ Maker (P/N), Acceptor (BOE), Drawee (CH)
If default in presentment	➤ no party liable thereto
Exception	➤ If P/N is payable on demand and is not payable at a specified place, no presentment is necessary.
Time	➤ During usual business hours
If instrument payable after date or sight	➤ must be presented for payment at maturity
P/N payable by instalments	➤ must be presented for payment on 3 rd day after date fixed for payment of each instalment

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

64



Presentment of Instrument

Rules regarding presentment for payment (P/N, BOE, CH)

Instrument payable at specified place	➤ Must be presented for payment at that place.
Where no exclusive place specified	➤ must be presented for payment at the place of business (if any) or at the usual residence
No known place of business or residence	➤ presentment may be made to him in person wherever he can be found
Instrument payable on demand	➤ Must be presented for payment within a reasonable time after it is received by the holder.

Note: Delay in presentment for acceptance or payment is excused if the delay is caused by circumstances beyond the control of the holder.



When Presentment Unnecessary

(NI is dishonoured on due date)

1. Maker, drawee or acceptor intentionally prevents the presentment,
2. Payable at business place & that's closed on business day during usual business hours,
3. Payable at specified place & liable party doesn't attend place,
4. Not payable at specified place & liable party not found after due search,



When Presentment Unnecessary

(NI is dishonoured on due date)

5. Liable party engaged to pay notwithstanding non-presentment,
6. Liable party makes part payment,
7. Liable party waives off his right to take advantage.
8. If drawer could not suffer damage from want of such presentment.



Rules of Compensation (Sec.117)

(NI is dishonoured on due date)

In case of Dishonour of NI, holder can claim:

- Amount due on NI
- Expenses incurred in presenting, noting & protesting.
- Interest 18% p.a. from due date of payment to date of realisation.

Note: In case of foreign currency, current rate of exchange

Let's Revise

REVISION TIME



Presentment for acceptance (Only for BOE)	BOE payable after sight must	Must be presented within a reasonable time & in business hours on a business day. (Note: 48 hours, excluding public holidays, are given to drawee for acceptance)	
	In default of such presentment	no party liable thereto	If Drawee not found after Reasonable search, BOE is dishonored
	If BOE is directed to drawee at a particular place	must be presented at that place	
Presentment of Promissory Note for sight	P/N payable at a certain period after sight	Must be presented within a reasonable time & in business hours on a business day.	
	In default of such presentment	no party liable thereto	

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

69

Let's Revise

REVISION TIME



Rules regarding presentment for payment (P/N, BOE, CH)	To whom	Maker (P/N), Acceptor (BOE), Drawee (CH)
	If default in presentment	no party liable thereto
	Exception	If P/N is payable on demand and is not payable at a specified place, no presentment is necessary.
	Time	During usual business hours
	If instrument payable after date or sight	must be presented for payment at maturity
	P/N payable by instalments	must be presented for payment on 3rd day after date fixed for payment of each instalment
	instrument payable at specified place	Must be presented for payment at that place.
	where no exclusive place specified	must be presented for payment at the place of business (if any) or at the usual residence
	no known place of business or residence	presentment may be made to him in person wherever he can be found
	Instrument payable on demand	Must be presented for payment within a reasonable time after it is received by the holder.
Note: Delay in presentment for acceptance or payment is excused if the delay is caused by circumstances beyond the control of the holder		

27 June 2024

© THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

70

Let's Revise

REVISION TIME



<p>When Presentment Unnecessary (NI is dishonoured on due date)</p>	<ol style="list-style-type: none"> 1. Maker, drawee or acceptor prevents the presentment, 2. Payable at business place & that's closed on business day during usual business hours, 3. Payable at specified place & liable party doesn't attend place, 4. Not payable at specified place & liable party not found after due search, 5. Liable party engaged to pay notwithstanding non-presentment, 6. Liable party makes part payment, 7. Liable party waives off his right to take advantage. 8. If drawer could not suffer damage from want of such presentment.
<p>Rules as to Compensation (Sec.117)</p>	<p>In case of dishonour of NI, holder can claim:</p> <ol style="list-style-type: none"> 1. Amount due on NI 2. Expenses incurred in presenting, noting & protesting. 3. Interest 18% p.a. from due date of payment to date of realisation. <p>Note: In case of foreign currency, current rate of exchange.</p>
<p>Dishonour of Cheques for Insufficiency of Funds in the Accounts [Section 138 to 142]</p>	<p>Debt - Cheque was issued to discharge a legally enforceable debt Reason for dishonour - insufficiency of funds Presentment of cheque - Within 3 months Demand made from drawer - Within 30 days of dishonour Default by drawer to pay - within 15 days of demand made</p>



THANK YOU