CHAPTER 7

The Negotiable Instruments Act, 1881

PART-A

The Negotiable Instruments Act, 1881

Meaning of Negotiable Instruments (Sec. 13)
P/N, BOE, Cheque – **payable** either to order; or to bearer

Characteristics of Negotiable Instruments:

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

Negotiable Instruments

Promissory Note [Sec. 4]

Meaning

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 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

Bill of Exchange [Sec. 5]

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 a certain person; or the order of a certain person; or the bearer of instrument.

Note: BOE cannot be made payable to bearer on demand.

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) Certain sum
(g) Drawer, Drawee & Payee must be certain
(h) Stamped

Cheque [Sec. 6]

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

Characteristics

(a) All the essentials of a BOE
(b) Drawn on a specified banker.
(c) Payable on demand.

A cheque does not require:

(a) Stamping; or
(b) acceptance;

Classification of Negotiable Instruments

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

Presentment for acceptance (Only for BOE)

<table>
<tr><td>BOE payable after sight must</td><td colspan="2">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)</td></tr>
<tr><td>In default of such presentment</td><td>no party liable thereto</td><td rowspan="2">If Drawee not found after reasonable search, BOE is dishonored.</td></tr>
<tr><td>If BOE is directed to drawee at a particular place</td><td>must be presented at that place</td></tr>
</table>

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

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

When Presentment Unnecessary

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.

Rules as to Compensation (Sec.117)
In case of dishonour of NI, holder can claim 1. Interest 18% pa, from due date of payment to date of realisation 2. Amount due on Negotiable instrument 3. Expenses incurred in presenting, noting & protesting **Note:** In case of foreign currency, current rate of exchange.

Dishonour of Cheques for Insufficiency of Funds in the Accounts [Section 138 to 142]
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

DIFFERENCE BETWEEN PROMISSORY NOTE AND BILL OF EXCHANGE

S.no	Basis	Promissory Note	Bill of Exchange
1.	**Definition**	"A Promissory Note" is 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.	"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.
2.	**Nature of Instrument**	In a promissory note, there is a promise to pay money.	In a bill of exchange, there is an order for making payment.
3.	**Parties**	In a promissory note, there are only 2 parties namely: i. the maker and ii. the payee	In a bill of exchange, there are 3 parties which are as under: i. the drawer ii. the drawee iii. the payee
4.	**Acceptance**	A promissory note does not require any acceptance, as it is signed by the person who is liable to pay.	A bills of exchange needs acceptance from the drawee.
5.	**Payable to bearer**	A promissory note cannot be made payable to bearer.	On the other hand, a bill of exchange can be drawn payable to bearer. However, it cannot be payable to bearer on demand.

QUESTIONS FOR PRACTICE

PART-B

Q1. Rama executes a promissory note in the following form, 'I promise to pay a sum of ₹10,000 after three months.'

Decide whether the promissory note is a valid promissory note.

Sol. The promissory note is an **unconditional** promise in writing. In the above question the amount is certain but the **date and name of payee is missing**, thus making it a bearer instrument.

As per Reserve Bank of India Act, 1934, a promissory note cannot be made payable to bearer - whether on demand or after certain days. Hence, the instrument is illegal as per Reserve Bank of India Act, 1934 and cannot be legally enforced.

Q2. Are the following instruments signed by Mr. Honest is valid promissory Notes? Give the reasons.

(a) I promise to pay D's son ₹10000 for value received (D has two sons)

(b) I promise to pay ₹5000/- on demand at my convenience

Who is the competent authority to issue a promissory note 'payable to bearer'?

Your answers shall be in accordance with the provisions of the Negotiable Instruments Act, 1881.

Sol.

Provision

Promissory Note: As per the provisions of 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 to or to the order of a certain person, or to the bearer of the instruments.

Analysis and conclusion

(a) This is not a valid promissory note as D has two sons and it is not specified in the promissory note that which son of D is the payee.

(b) This is not a valid promissory note as details of the payee are not mentioned in it and it is not an unconditional undertaking.

Moreover, a promissory note cannot be made payable to the bearer (Section 31 of Reserve Bank of India Act, 1934). Only the Reserve Bank or the Central Government can make or issue a promissory note 'payable to bearer'.

Q3. Mr. V draws a cheque of ₹11,000 and gives to Mr. B by way of gift. State with reason whether-

(i) Mr.B is a holder in due course as per the Negotiable Instrument Act, 1881?

(ii) Mr.B is entitled to receive the amount of ₹11,000 from the bank?

Sol.

Provision

According to section 9 of the Negotiable Instrument Act, 1881, "Holder in due course" means-any person who for consideration becomes the possessor of a promissory note, bill of exchange or cheque if payable to bearer or the payee or endorsee thereof, if payable to order, before the amount in it became payable and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.

Analysis and conclusion

In the instant case, Mr. V draws a cheque of ₹11,000 and gives to Mr. B by way of gift.

(i) Mr. B is holder but not a holder in due course since he did not get the cheque for value and consideration.

(ii) Mr. B's title is good and bonafide. As a holder, he is entitled to receive ₹11,000 from the bank on whom the cheque is drawn.

Q4. Ram draws a cheque of ₹1 lakh. It was a bearer cheque. Ram kept the cheque with himself. After some time, Ram gives this cheque to Shyam as a gift on his birthday. Decide whether Shyam is having a valid title over the cheque and whether Shyam is a holder in due course or not in relation to this cheque as per the Section 9 of the Negotiable Instruments Act 1881.

Sol.

Provision

"Holder in due course" [Section 9 of the Negotiable Instruments Act, 1881]:

'Holder in due course' means any person who for consideration becomes the possessor of a promissory note, bill of exchange or cheque if payable to bearer or the payee or endorsee thereof, if payable to order, before the amount in it became payable and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.

Analysis and conclusion

In the instant case, Ram draws a cheque for ₹1 lakh and hands it over to Shyam by way of gift. Here, Shyam's title is good and bonafide. As a holder he is entitled to receive ₹1 lakh from the bank on whom the cheque is drawn. However, Shyam is not a holder in due course as he does not get the cheque for value and consideration.

Q5. State with reasons whether each of the following instruments is an Inland Instrument or a Foreign Instrument as per The Negotiable Instruments Act, 1881:

(i) Ram draws a Bill of Exchange in Delhi upon Shyam a resident of Jaipur and accepted to be payable in Thailand after 90 days of acceptance.

(ii) Ramesh draws a Bill of Exchange in Mumbai upon Suresh a resident of Australia and accepted to be payable in Chennai after 30 days of sight.

(iii) Ajay draws a Bill of Exchange in California upon Vijay a resident of Jodhpur and accepted to be payable in Kanpur afster 6 months of acceptance.

(iv) Mukesh draws a Bill of Exchange in Lucknow upon Dinesh a resident of China and accepted to be payable in China after 45 days of acceptance.

Sol.

Provision

"Inland **instrument" and "Foreign instrument" [Sections 11 & 12 of the Negotiable Instruments Act, 1881]** A promissory note, bill of exchange or cheque drawn or made in India and made payable in, or drawn upon any person resident in India shall be deemed to be an inland instrument.

Any such instrument not so drawn, made or made payable shall be deemed to be foreign instrument.

Analysis and conclusion

Following are the answers as to the nature of the Instruments:

(i) In first case, Bill is drawn in Delhi by Ram on a person (Shyam), a resident of Jaipur (though accepted to be payable in Thailand after 90 days) is an Inland instrument.

(ii) In second case, Ramesh draws a bill in Mumbai on Suresh resident of Australia and accepted to be payable in Chennai after 30 days of sight, is an Inland instrument.

(iii) In third case, Ajay draws a bill in California (which is situated outside India) and accepted to be payable in India (Kanpur), drawn upon Vijay, a person resident in India (Jodhpur), therefore the Instrument is a Foreign instrument.

(iv) In fourth case, the said instrument is a Foreign instrument as the bill is drawn in India by Mukesh upon Dinesh, the person resident outside India (China) and also payable outside India (China) after 45 days of acceptance.

Q6. Explain the meaning of 'Negotiation by delivery' with the help of an example. Give your answer as per the provisions of the Negotiable Instruments Act, 1881

Sol. **Negotiation by delivery:** According to section 47 of the Negotiable Instruments Act, 1881, subject to the provisions of section 58, a promissory note, bill of exchange or cheque payable to bearer is negotiable by delivery thereof.

Exception: A promissory note, bill of exchange 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: 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.

Q7. Anjum' drew a cheque for ₹20,000 payable to 'Babloo' and delivered it to him. 'Babloo' indorsed the cheque in favour of 'Rehansh' but kept it in his table drawer. Subsequently, 'Babloo' died, and cheque was found by 'Rehansh' in 'Babloo's table drawer. 'Rehansh' filed the suit for the recovery of cheque. Whether 'Rehansh' can recover cheque under the provisions of the Negotiable Instrument Act 1881?

Sol.

Provision

According to section 48 of the Negotiable Instrument Act 1881, a promissory note, bill of exchange or cheque payable to order, is negotiable by the holder by indorsement and delivery thereof.

The contract on a negotiable instrument until delivery remains incomplete and revocable. The delivery is essential not only at the time of negotiation but also at the time of making or drawing of negotiable instrument.

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, the legal representatives of the deceased person cannot negotiate the same by mere delivery thereof. [Section 57]

Analysis and conclusion

In the given case, cheque was indorsed properly but not delivered to indorsee i.e. 'Rehansh', Therefore, 'Rehansh' is not eligible to claim the payment of cheque.

Q8. Manoj owes money to Umesh. Therefore, he makes a promissory note for the amount in favour of Umesh, for safety of transmission he cuts the note in half and posts one half to Umesh. He then changes his mind and calls upon Umesh to return the half of the note which he had sent. Umesh requires Manoj to send the other half of the promissory note. Decide how rights of the parties are to be adjusted in reference to the Negotiable Instruments Act, 1881.

Sol.

Provision

The question arising in this problem is whether the making of promissory note is complete when one half of the note was delivered to Umesh. Under Section 46 of the Negotiable Instruments Act, 1881, the making of a promissory note is completed by delivery, actual or constructive. Delivery refers to the whole of the instrument and not merely a part of it. Delivery of half instrument cannot be treated as constructive delivery of the whole.

Analysis and conclusion

So, the claim of Umesh to have the other half of the promissory note sent to him is not maintainable. Manoj is justified in demanding the return of the first half sent by him. He can change his mind and refuse to send the other half of the promissory note.

Q9. Bholenath drew a cheque in favour of Surendar. After having issued the cheque; Bholenath requested Surendar not to present the cheque for payment and gave a stop payment request to the bank in respect of the cheque issued to Surendar. Decide, under the provisions of the Negotiable Instruments Act, 1881 whether the said acts of Bholenath constitute an offence?

Sol.

Provision

As per the facts stated in the question, Bholenath (drawer) after having issued the cheque, informs Surender (drawee) not to present the cheque for payment and as well gave a stop payment request to the bank in respect of the cheque issued to Surender.

Section 138 of the Negotiable Instruments Act, 1881, is a penal provision in the sense that once a cheque is drawn on an account maintained by the drawer with his banker for payment of any amount of money to another person out of that account for the discharge in whole or in part of any debt or liability, is informed by the bank unpaid either because of insufficiency of funds to honour the cheques or the amount exceeding the arrangement made with the bank, such a person shall be deemed to have committed an offence.

Once a cheque is issued by the drawer, a presumption under Section 139 of the Negotiable Instruments Act, 1881 follows and merely because the drawer issues a notice thereafter to the drawee or to the bank for stoppage of payment, it will not preclude an action under Section 138.

Also, Section 140 of the Negotiable Instruments Act, 1881, specifies absolute liability of the drawer of the cheque for commission of an offence under the section 138 of the Act. Section 140 states that it shall not be a defence in a prosecution for an offence under section 138 that the drawer had no reason to believe when he issued the cheque that the cheque may be dishonoured on presentment for the reasons stated in that section.

Analysis and conclusion

Accordingly, the act of Bholenath, i.e., his request of stop payment constitutes an offence under the provisions of the Negotiable Instruments Act, 1881

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