



SNS College of Technology
(An Autonomous Institution)
Coimbatore - 35



Department of Management Studies
19BAT604 – Legal Aspects of Business
Unit – III – Negotiable Instruments Act, 1881

1. What is a negotiable instrument?

The term “Negotiable Instrument” literally means “*a document transferable by delivery*”. It means a promising note, bill of exchange or cheque payable either to order or to bearer.

Examples

- Recognized by Statute → Bills of Exchange, Promissory Note, Cheque
- Recognized by Usage or custom → Hundis, Share warrants, Dividend warrants, Banker’s drafts, Circular notes, Bearer debentures, Railway receipts, Delivery orders

2. Distinguish between a promissory note and a bill of exchange

Promissory note	Bill of Exchange
There are two parties in a promissory note. They are the maker and payee.	In a bill of exchange there are three parties, the drawer, the drawee and the payee.
The maker of pronote is the debtor and he undertakes to pay the amount.	In a bill of exchange the drawee is the debtor and the drawer is the creditor who directs the drawee to pay.
The maker and the payee cannot be the same person.	The drawer and the drawee may be the same person. So also drawer and payee may also be the same person.
Pronote contains an unconditional promise to pay.	A bill contains an unconditional order to pay.
The liability of a maker of note is primary and absolute.	The liability of the drawer of a bill is secondary and conditional.
Presentment for acceptance and presentment for payment is not applicable.	It is applicable.

3. Distinguish between a cheque and a bill of exchange

Bill of Exchange	Cheque
In a bill the drawee may be any person	In a cheque the drawee is always a banker.

including bankers.	
A bill requires acceptance from the drawee before he is asked to pay.	The cheque does not require acceptance from the drawee.
A bill may be payable on demand, after sight, or after the expiry of certain period.	A cheque is always payable on demand.
In case of dishonor of a bill protest is advisable.	Protest for dishonor is not necessary.
The drawee is not entitled to any special statutory protection.	Special statutory protection is available to the drawee banker.
A bill has to be stamped according to the Stamp Act.	Stamping is not necessary in the case of cheque.
Notice of dishonor is necessary.	Notice of dishonor is not necessary.

4. What is a promissory note? What are its essential elements?

An instrument in writing 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.

The essential elements of a promissory note are

- Must be in writing
- Must contain an unconditional undertaking to pay
- Must be signed and delivered by the maker
- The sum payable must be definite
- The promise must be to pay money only
- The maker must be a definite person
- The payee must be a definite person
- It must be stamped as required by the Stamp Act

5. What is a cheque? How does it differ from a bill of exchange?

A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand. It is always drawn by a bank & not by any other institutions. It is always payable on demand. A cheque can be bearer, order or crossed. The drawee, that is, the banker named must honour the cheque by making payment to the payee when the cheque is presented for payment to the banker at his office during the usual office hours, provided the cheque is properly and validly drawn and the drawer has sufficient funds to his credit. The signature on the cheque must tally with the specimen signature of the concerned drawer. A cheque must be dated.

6. What is a bill of exchange? Who can accept a bill of exchange?

“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” – Sec 5.

The person who makes or draws the bill is called **drawer**. The person on whom it is drawn is called **drawee** who becomes an acceptor on acceptance of the bill. The person to whom the amount is payable is called the **payee**.

7. Give 2 essential features of negotiable instruments?

The essential features of negotiable instruments are as follows:

- Easy transferability
- Title
- Right to file suit
- Notice of transfer
- Presumption
- Procedure for suits
- Number of transfer
- Rule of evidence
- Exchange

8. What are the different kinds of negotiable instrument?

The following are the different kinds of negotiable instruments

- ❖ Promissory note
- ❖ Bill of Exchange
- ❖ Pay Order
- ❖ Demand Draft
- ❖ Hundi
- ❖ Railway receipt
- ❖ Delivery note
- ❖ Dividend warrants
- ❖ Debentures
- ❖ Railway bonds payable to bearer, etc.

9. Define a ‘holder’ and ‘a holder in due course’

Holder:

According to Sec 8, The holder of a promissory note, bill of exchange or cheque means any person entitled in his own name to the possession thereof and to receive or recover the amount due therein from the parties thereto. Where the note, bill or cheque is lost or destroyed, its holder is the person so entitled at the time of such loss or destruction. So, a person who gets

possession of an instrument by theft is not a holder. Similarly, an agent who is in possession of an instrument is not a holder.

Holder in due course:

Any person who for consideration and in good faith became the possessor of a promissory note, bill of exchange or cheque if payable bearer, or the payee or indorsee there of, if payable to order the amount mentioned in it became payable

10. What is an accommodation bill?

It is not a genuine bill. It is drawn and accepted only to accommodate a party. *“If, as between the original parties to the bill the one who would prima facie be principal is in fact, the surety; whether he be drawer, drawee, acceptor, or indorser, that bill is called an accommodation bill”.*

11. What is meant by “acceptance” of a bill of exchange?

A bill of exchange is said to be accepted when the drawee puts his signature on it, thereby acknowledging his liability under the bill. The usual mode of acceptance is writing the word “accepted” across the bill and signing under it. The signature may be put anywhere, on the face of the bill or on the back of it.

12. What do you understand by ‘presentment of a negotiable instrument’?

Presentment means presenting a negotiable instrument for getting payment or acceptance (if it is a bill). Presentment of the bill for acceptance is not obligatory in all the cases. The following bills must be presented for acceptance:

- Where the bill is payable after sight, presentation is necessary to fix the maturity of the instrument.
- When it is expressly stipulated that presentment shall be made for acceptance it must be presented for acceptance before payment.

13. When is presentment for acceptance and payment excused?

Presentment for acceptance :

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Presentment Excused :

If the drawee cannot be found after reasonable search [S.61]. Where the drawee is a fictitious person or not having capacity to contract. Where the drawee is dead or has been declared as insolvent.

14. What is a hundi? What are its various kinds?

A hundi is a bill of exchange drawn in Indian languages by Indian merchants and indigenous bankers. The negotiable instruments Act does not apply to hundies except when the parties provide so. The drawer is called **Shroff** or **Nanavathi** and the payee is called **Rakhyadhani**.

The various kinds of hundi are

- Shah Jog Hundi
- Nam Jog Hundi
- Jawabee Hundi
- Zickri Chit
- Darshan Hundi
- Muddati Hundi
- Khoka
- Peth or Perpeth

15. Define 'discharge of a negotiable instrument'?

A negotiable instrument is said to be discharged when it become completely useless, i.e., no action on that will lie and it cannot be negotiated further. After negotiable instrument is discharged the rights against all the parties thereto come to an end and no party, even a holder in due course, can claim the amount of the instrument from any party thereto. Discharge of the party primarily and ultimately liable on instrument result in the discharge of the instrument itself. The term discharge has two connections, viz., (1) discharge of the instruments and (2) discharge of one or more parties from liability on the instrument.

16. Distinguish between negotiation and assignment

Assignment	Negotiation
It is effected under the Transfer of Property Act, 1883	It is effected under the Negotiable Instrument Act, 1881
It must be in writing	No formality is necessary, it can be effected by delivery or by indorsement and delivery.
The assignee of a debt takes it subject to all the defects and equities that may exist in the title of his assignor.	The holder in due course of a negotiable instrument is not affected by the defects in the title of the previous transferors.

An assignment of a debt does not bind the debtor unless a notice of assignment has been given to him and he has, expressly or impliedly, assented it.	Notice of negotiation of a negotiable instrument to the debtor not necessary.
There is no presumption in favour of an assignee. He has to prove that he has given consideration for the assignment.	There are number of presumptions in favour of a holder in due course, eg: he is presumed to have given consideration for the instrument. The burden lies upon the opposite party to show that he had given no consideration.

17. What are the different kinds of endorsements?

- Blank indorsement
- Special indorsement
- Conditional indorsement
 - Sans recourse
 - Sans Frais
 - Facultative indorsement
 - Contingent indorsement
- Restrictive indorsement
- Partial indorsement

18. What is a Cheque?

A cheque (or check in American English) is a document that orders a bank to pay a specific amount of money from a person's account to the person in whose name the cheque has been issued.

19. Write short notes on crossing of cheque.

- Crossing means drawing two parallel lines across the face of the cheque with or without the words “ and company” in between the lines. It is a direction to the drawee bank not to pay the amount at the counter, but only through a bank. It is made to guard payment against forgery by unscrupulous persons.
- The two different kinds of crossing are general crossing and special crossing.
- Rules of crossing:
 - An uncrossed cheque may be crossed generally or specially by the drawer or the holder.
 - A cheque crossed generally, may be crossed specially by the holder.
 - The holder may add the words “not negotiable”
 - The banker to whom the cheque is crossed specially, may recross it but only to another bank as his agent for collection.

- Where an uncrossed cheque or a cheque crossed generally is sent to a banker for collection, he may cross it specially to himself. But he cannot enjoy statutory protection against being sued for conversion.

20. Define 'Marking of Cheques'.

When the drawee bank marks the cheque or certifies to the effect that it would be honoured when presented for payment, the cheque is called marked cheque. This marking can be done at the instance of the drawer himself when the bank set aside the amount sufficient to pay the cheque, when presented. In such a case, the drawer cannot counter the payment.

This marking can be made at the instance of the holder or the collecting banker. But the banker may refuse payment if there are no sufficient funds to the credit of the customer.

21. What is an inchoate instrument?

It is an incomplete instrument. When one person signs and delivers to another, either blank stamp papers or incomplete stamp papers, such another person completes it to fill up the blanks for any amount not exceeding the sum covered by the stamp. The person signing is liable to holder in due course for such amount.

22. Define 'Escrow'.

When the property in the instrument is transferred conditionally, it is called an 'escrow'. A holder in due course is not affected by 'escrow'.

23. Define Writing and Signature in Negotiable instrument :

Negotiable Instruments must be written and signed by the parties according to the rules relating to Promissory Notes, Bills of Exchange and Cheques. Demand Drafts are also construed as Negotiable Instruments in the limiting case as they have the same property as N.I. Instruments.

24. What is Negotiability?

Negotiable Instruments can be transferred from one person to another by a simple process. In the case of bearer instruments, delivery to the transferee is sufficient. In the case of order instruments two things are required for a valid transfer: endorsement (i.e., signature of the holder) and delivery. Any instrument may be made non-transferable by using suitable words, e.g., "pay to X only."

25. Mention the parties involved in the cheque clearing system.

Drawer: A person who writes cheque for making payment to other parties then that person is called drawer of the cheque. It means he is making an order to his financial

institute to make payment of certain amount. In very simple words person who sign the cheque (as per mandate given in bank) for making payments is called drawer of the cheque.

Drawee: can be bank or any other financial institution where the cheque can be presented for payment. It is receiver of order from drawer and has to make payment of the amount mentioned in cheque to the person whose name is on cheque.

Payee: He is the one who actually receive the payment or he is the person in favour whom cheque is drawn. He is the one whose name is on the cheque.

Some important terms:

- 1. Negotiable instrument-** document transferable by delivery
- 2. Negotiable instrument** – Bill of exchange, Promissory note Cheque
- 3. Non -Negotiable instrument** – Money order, share certificates, postal orders
- 4. Drawer** – Maker of a negotiable instrument
- 5. Drawee-** The person on whom the instrument is drawn
- 6. Holder-** He is either the original payer or any other person to whom the payee has endorsed the instrument. In case of the bearer of the cheque. The bearer is the holder
- 7. Promissory note-** An instrument is writing containing an unconditional undertaking signed by the maker, to pay a certain sum of money to the bearer of the instrument
- 8. Bill of exchange-** An instrument is writing containing an unconditional order signed by the maker, directing a certain person, to pay a certain sum of money to the bearer of the instrument
- 9. Holder in due course:** The Holder in Due Course (HDC) doctrine is a rule in commercial law that protects a purchaser of debt, where the purchaser is assigned the right to receive the debt payments.
- 10. Demand draft:** A demand draft is a negotiable instrument similar to a bill of exchange. A bank issues a demand draft to a client (drawer), directing another bank (drawee) or one of its own branches to pay a certain sum to the specified party (payee). A demand draft can also be compared to a cheque.
- 11. Crossed Cheque:** A crossed cheque is a cheque that has been marked to specify an instruction about the way it is to be redeemed. A common instruction is to specify that it must be deposited directly into an account with a bank and not immediately cashed by a bank over the counter.
- 12. Uncrossed cheque:** a cheque without two vertical lines down its centre, showing that the person named to receive the money can get the amount at the bank of the person
- 13. Open cheque:** An open cheque is a cheque that is not crossed on the left corner and payable at the counter of the drawee bank.

14. Parties in Promissory note: There are two parties to a promissory note. Maker or Drawer is the person who makes or draws the promissory note. He is also called the promisor. Drawee or Payee is the person in whose favour the promissory note is drawn.

15. Parties to a Bill of Exchange : There are three parties to a bill of exchange: Drawer is the maker of the bill of exchange. Drawee is the person upon whom the bill of exchange is drawn. Payee is the person to whom the payment is to be made.

16. Concept of money in Negotiable instrument:

Negotiable instruments are payable by legal tender money of India. The liabilities of the parties of Negotiable Instruments are fixed and determined in terms of legal tender money.

17. What is title in Negotiable instrument?

The transferee of a negotiable instrument, when he fulfils certain conditions, is called the holder in due course. The holder in due course gets a good title to the instrument even in cases where the title of the transferrer is defective.

18. When a contract is discharged?

A contract is discharged when it loses its force and effect as a legal obligation.