

THE NEGOTIABLE INSTRUMENTS ACT, 1881

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1. Introduction to Negotiable Instruments

1.1 DEFINITION OF NEGOTIABLE INSTRUMENT (SEC 13)

Negotiable instrument means

- ✓ a promissory note; or
- ✓ bill of exchange; or
- ✓ cheque

Payable

- ✓ either to order; or
- ✓ to the bearer.

1.2 MEANING OF NEGOTIABLE INSTRUMENT

Negotiable instrument means

An instrument the property in which is acquired by anyone who takes it –

- ✓ Bonafide; and
- ✓ For value
- ✓ notwithstanding any defect in the title of any prior party.

1.3 ESSENTIALS OR CHARACTERISTICS OF NEGOTIABLE INSTRUMENT (Sec.13)

1. Freely transferable from one person to another
2. Transferable infinitum (i.e. indefinitely).
3. HDC gets a good title to negotiable instrument even though the title of transferor is defective.
4. A negotiable instrument may more than one payee jointly or alternatively.

2. Meaning of promissory Note (Sec 4)

2.1 MEANING OF PROMISSORY NOTE (Sec.4)

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 –
 - ✓ a certain person; or
 - ✓ the order of a certain person.

2.2 ILLUSTRATION

A signs an instrument in following terms **"I Promise to Pay B or order Rs. 500."**

2.3 SPECIMEN OF A PROMISSORY NOTE (Sec.4)

Rs 1000	Delhi, April 25, 2014
Three months after date I Promise to pay Shyam Sunder or order the sum of one thousand rupees, for value received.	
To Shyam Sunder D-323, Laxmi Nagar Delhi-92	Stamp Sd/-Ram

2.4 PARTIES OF A PROMISSORY NOTE (Sec.4)

- **Maker** : The person who makes the promissory note is called as maker. His liability is primary and unconditional.
- **Payee** : The person to whom money is to be paid is named in the promissory note. He is called as payee.

2.5 ESSENTIALS CHARACTERISTICS OF A PROMISSORY NOTE (Sec.4)

- **In writing** :-An oral promise to pay is not sufficient
- **Express promise to pay**:-There must be express promise to pay. Mere acknowledgement of indebtedness is not sufficient.
- **Definite and unconditional promise** :-If a promise to pay is dependent upon an event which is certain to happen, although the time of its happening is uncertain, the promise to pay is unconditional.
Example
 - ✓ "I promise to pay B Rs.500 seven days after my marriage with C." The promise is conditional since the promise is dependent upon marriage of the promisor with C, which may or not happen.
 - ✓ "I promise to pay B Rs.500 on D's death." The promise is not conditional, but definite since death of D is certain. Therefore, the promissory note is valid.
- **Signed by maker**:- A promissory note must be signed by the maker. The signatures may be made on any part of the instrument.
- **Promise to pay a certain sum**
Example:-"I promise to pay B Rs.500 and all other sums which shall be due to him." Since the amount payable is not certain, it is not a valid promissory note.
- **Promise to pay money only**
Example:-"I promise to pay B Rs.500 and to deliver to him my black horse on 1st January next." It is not a valid promissory note since the promisor is required to deliver his black horse also, which is not 'money'.

- **Payee must be certain** :-The name of payee must be specified in the promissory note, otherwise it will be invalid.
- **Stamped** :-A promissory note must be stamped.

3. Bill of Exchange (Sec 5)

3.1 MEANING OF BILL OF EXCHANGE

A 'bill of exchange' is an

- instrument in writing
- Containing an unconditional order
- 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.

3.2 ILLUSTRATION-1

Shyam of Delhi buys goods on credit from Krishan of Mumbai for Rs. 500 to be paid 3 months after date. Krishan Buys goods from Ram of Delhi for Rs. 2000 on similar terms. Now Krishan may order shyam to pay the sum of Rs. 500 to Ram. The order will be a bill of exchange.

3.3 ILLUSTRATION-2

A sells goods worth Rs 800 to B, and allows him three months time to pay the price. A will then draw a bill on B in the following terms "Three months after date pay to my order the sum of Rs. 800 for value received."

3.4 SPECIMEN OF A BILL OF EXCHANGE (ILL 1)

Rs 500

Mumbai, Jan. 10, 2014

Three months after date pay to Ram or order the sum of five hundred rupees, for value received.

To

Shyam
D-323, Laxmi Nagar
Delhi-92

Stamp

Sd/-Krishan

Accepted
Shyam

3.4 PARTIES TO A BILL OF EXCHANGE

➤ Drawer

- ✓ The person who draws the bill (i.e. the person who makes the bill) is called as drawer.
- ✓ His liability is secondary and conditional
- ✓ His liability is primary and conditional until the bill is accepted.

➤ Drawee

- ✓ The person on whom the bill is drawn is called as drawee.
- ✓ On acceptance of the bill
 - he is called as acceptor;
 - he becomes liable for the payment of the bill;
 - his liability is primary and unconditional.

➤ Payee.

- ✓ The person to whom money is to be paid is named in the bill. He is called as payee.

3.5 ESSENTIALS CHARACTERISTICS OF A BILL OF EXCHANGE

- It must be in writing
- It must contain an express order to pay
- The order to pay must be definite and unconditional
- It must be signed by the drawer
- The sum contained in the order must be certain
- The order must be to pay money only
- Drawer, drawee and payee must be certain (usually, same person is the drawer and payee)
- It must be stamped.

4. Difference between Promissory Note and Bill of Exchange

PROMISSORY NOTE	BILL OF EXCHANGE
It contains a promise to pay	It contains an order to pay
Liability of maker of maker is primary and absolute.	Liability of drawer of the bill is Secondary and conditional.
It is presented for payment without any previous acceptance by maker.	IF a bill is payable after sometime after sight, it is the required to be accepted either by the drawee himself or by some one else on his behalf
The maker of the note stands in immediate relationship with the payee	The maker or drawer of an accepted bill of exchange stands in immediate relationship with the acceptor and payee
The maker and payee cannot become the same person	The Drawer and payee can be a same person
There are two Parties i.e. Maker and Payee	There are three parties i.e. Drawer, Drawee and Payee.

5. Cheque

5.1 MEANING OF CHEQUE

A cheque is a bill of exchange 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.

5.2 ESSENTIALS CHARACTERISTICS OF A CHEQUE

- ✓ It must be in writing
- ✓ It must contain an express order to pay
- ✓ The order to pay must be definite and unconditional
- ✓ It must be signed by the drawer
- ✓ The sum contained in the order must be certain
- ✓ The order must be to pay money only
- ✓ Drawer, drawee and payee must be certain
- ✓ It is always drawn upon a specified banker
- ✓ It is always payable on demand

A cheque must contain all the characteristics of a bill of exchange

A cheque does not require

- ✓ stamping ; or
- ✓ acceptance.

5.3 PARTIES OF A CHEQUE

➤ **Drawer**

- ✓ The person who draws the cheque, i.e., the person who makes the cheque is called as drawer.
- ✓ His liability is primary and conditional

➤ **Drawee**

- ✓ The bank on whom the cheque is drawn is called as drawee.
- ✓ He makes the payment of the cheque.

➤ **Payee**

- ✓ The person to whom money is to be paid (i.e., the person in whose favour cheque is issued) is named in the cheque. He is called as payee.
- ✓ The payee may be the drawer himself or a third party.

5.4 TRUNCATED CHEQUE

➤ **Meaning of truncated cheque**

- ✓ A truncated cheque means a cheque
- ✓ Which is truncated during the course of a clearing cycle
- ✓ Either by the clearing house or bank whether paying or receiving payment.

- ✓ Immediately on generation of an electronic image.
- ✓ For transmission substituting the further physical movement of cheque in writing

➤ **Duties of collecting banker**

- ✓ The collecting banker shall verify with due diligence and ordinary care –
- ✓ The prima facie genuineness of the cheque to be truncated;
- ✓ As to whether any fraud, forgery or tampering is apparent on the face of the instrument.

➤ **Presentment of truncated cheque**

- ✓ In case of any reasonable suspicion about the genuineness of the electronic image of a truncated cheque (e.g. suspicion as to fraud, forgery, tampering or destruction of the instrument), the paying banker is entitled to –
 - Demand any further information regarding the truncated cheque;
 - Demand the presentment of truncated cheque itself for verification.

5.5 CHEQUE IN ELECTRONIC FORM

➤ **Meaning of 'a cheque in electronic form'**

- ✓ A cheque in electronic form means a cheque
- ✓ Which contains the exact mirror image of a paper cheque
- ✓ and is generated, written and signed in a secure system ensuring the minimum safety standards with the use of digital signature (with or without biometric signature) and asymmetric crypto system.

5.6 DIFFERENCE BETWEEN TRUNCATED CHEQUE & CHEQUE IN ELECTRONIC FORM

Electronic cheque	Truncated cheque
Paper is not used at any stage in creation of an electronic cheque.	A truncated cheque is nothing but a paper cheque, which is truncated during the clearing cycle.
Digital signatures must be used to create an electronic image of cheque. Thus, an electronic cheque contains digital signature.	The paper cheque, which is afterwards truncated, contains no digital signature. The signatures in ink appear on the truncated cheque.
The original writing of an electronic cheque is in electronic form.	The – original writing of a truncated cheque is on paper duly – signed in ink. After the paper cheque is converted into electronic form, it is truncated and thus, it becomes a truncated cheque.

5. Crossing

6.1 MEANING OF CROSSING

Crossing means a direction given by the drawer of the cheque to the drawee bank, not to pay the cheque at the counter of the bank, but to pay it to a person who presents it through a banker.

6.2 PURPOSE OF CROSSING

Crossing makes it possible to trace the person to whom the payment has been made. Thus, it makes the cheque safe.

6.3 TYPES OF CROSSING

➤ General Crossing ; Sec.123

Where a cheque bears across its face an addition of –

- ✓ The words 'and company' or any abbreviations thereof between two parallel transverse lines, or Two parallel transverse lines simply.
- ✓ Where a cheque is crossed generally, the banker on whom it is drawn shall not pay it otherwise than to a banker.

➤ Special Crossing : Sec.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.
- ✓ Two parallel transverse lines are not a must. Where a cheque is crossed specially, the banker on whom it is crossed shall not pay it, otherwise than to the banker to whom it is crossed or his agent for collection.

Difference:

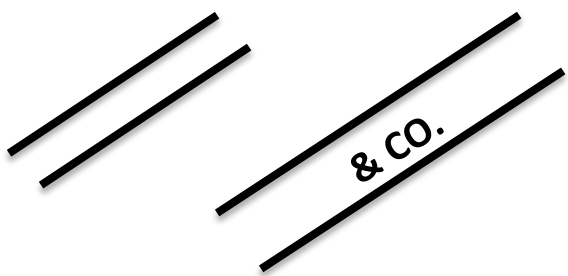
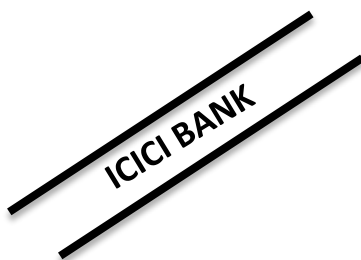
In general crossing the Name of the Bank is not mentioned whereas in special crossing the Name of the Bank is mentioned.

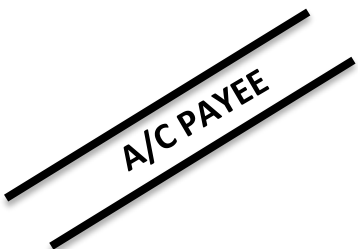
➤ 'Not Negotiable' Crossing : Sec.130.

- ✓ The object of "Not negotiable" crossing is to protect the rights of holder of a cheque.
- ✓ A person taking a cheque crossed generally or specially, bearing in either cases the words 'not negotiable', shall not have, and shall not be capable of giving a better title to the cheque other than that which the person from whom he took it had.

➤ 'Account Payee' Crossing / Restrictive Crossing

- ✓ The purpose of this crossing bearing the words "A/c Payee" is to obviate the risk of a wrong person obtaining payment on a cheque.
- ✓ It is a direction to banker to credit the proceeds only to the account of the payee.

GENERAL CROSSING	SPECIAL CROSSING
	
NOT NEGOTIABLE CROSSING	ACCOUNT PAYEE CROSSING

	
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7. Introduction to Negotiable Instruments

Basis	Bill of Exchange	Cheque
Drawee	Any person can be a drawee	Only Banker can be drawee
Liability	Liability of drawer is secondary	Liability of drawer is primary
Validity period	No validity period	Only valid for 3 months
Stamping	Must be stamped	A cheque does not require stamping
Crossing	A bill cannot be crossed	A cheque can be crossed
Days of grace	Allowed	Not Allowed
Maturity date	A bill may be payable on demand or otherwise than on demand	A cheque is always payable on demand.

8. Capacity of a Person to be a Party to a Negotiable Instrument

Person must be capable of contracting:- A person shall be liable on a negotiable instrument (by reason of making, drawing, accepting endorsing, delivering or negotiating a negotiable instrument) only if he is capable of contracting according to the law to which he is subject.

8.1 IN CASE OF MINOR

- ✓ A minor is not competent to contract
- ✓ Mere presence of a minor as one of the party in a negotiable instrument does not make it invalid.
- ✓ A minor may draw, endorse, deliver and negotiate any negotiable instrument.
- ✓ All the parties shall be bound on such negotiable instrument.
- ✓ However, the minor shall not be bound on such negotiable instrument.
- ✓ 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

8.2 CORPORATION

- ✓ Corporation can be party to a negotiable instrument if authorized by its Articles of Association, otherwise it is ultra vires

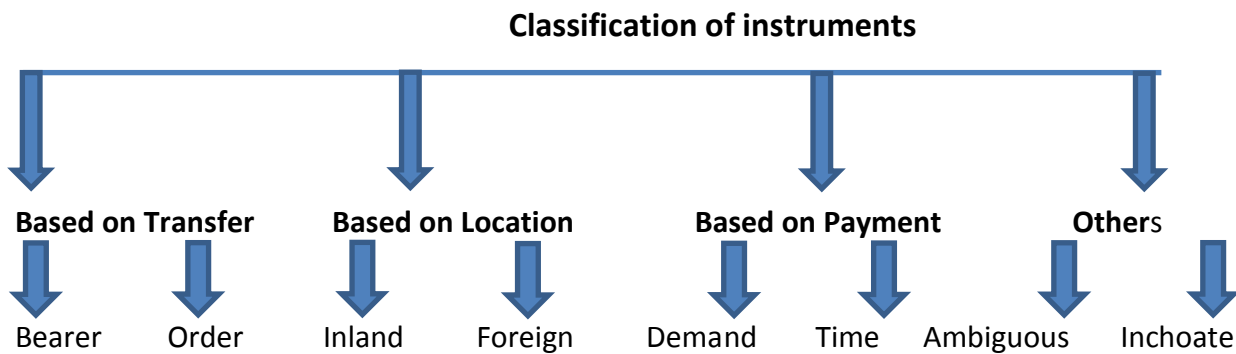
8.3 AGENT

- ✓ 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 sign such document. The form of signature must show that he does not intend to incur personal liability. Otherwise he becomes personally liable.

8.4 LEGAL REPRESENTATIVES

- ✓ 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.

9. Classification of Negotiable Instruments (Sec 13, 19 & 21)



9.1 BASED ON TRANSFER

✚ Bearer Instrument :

An instrument is payable to bearer of –

- ✓ it is expressed to be so payable, or
- ✓ on which the only or last endorsement is an endorsement in blank.

✚ Order Instrument :

An instrument -

- ✓ Payable to a particular person or 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.

Example:- “Pay to A or order”

9.2 BASED ON LOCATION

✚ Inland Instrument [Sec.11]:

A P/N, B/E or cheque is said to be an inland instrument, if any one of the following conditions is satisfied

- ✓ Drawn or made in India and made payable in India, or
- ✓ Drawn or made in India and drawn upon a person resident in India.

Note: Even if an Inland Bill is endorsed to a foreign country, it continues to be an Inland Instrument.

Example:-

- ✓ A bill is drawn in Delhi on a merchant in Mumbai and accepted payable in Kolkata or London.
- ✓ A bill is drawn in Delhi on a merchant in London and accepted payable in Kolkata.
- ✓ The above bills are indorsed in New York.

✚ Foreign Instrument [Sec.12]:

An instrument which is not an Inland Instrument, is deemed to be a Foreign Instrument.

9.3 BASED ON PAYMENT

Demand Instrument:

An instrument which satisfies the following conditions –

- ✓ Time for payment is not specified.
- ✓ Expressed to be payable on demand.
- ✓ Can be presented for payment at any time.

Time Instrument :

An instrument in which time for payments is specified and may be payable –

- ✓ After a specified period, or
- ✓ On a specified day, or
- ✓ Certain period after, sight, or
- ✓ On the happening of a certain event.

9.4 OTHERS

Ambiguous Instruments [Sec.17]:

- ✓ Where an instrument may be constructed either as a P/N or as a B/E, the holder may at his option treat it as either, and the instrument shall henceforth be treated accordingly, e.g. a B/E drawn in favour of a fictitious person.
- ✓ An Ambiguous Instrument treated as a P/N or as a B/E cannot be treated differently afterwards.

Example:- A bill is drawn by A, an agent, acting within the scope of his authority upon his principal, P. The holder may at his option, treat it as a note or a bill because the drawer (A) and the drawee (P) are the same person.

Inchoate Instruments

➤ Conditions for an inchoate instrument

- ✓ A person signs a negotiable instrument.
- ✓ The negotiable instrument is stamped.
- ✓ The negotiable instrument is either wholly blank or is partially blank.
- ✓ The person signing such negotiable instrument delivers it to another person.

➤ **Example:-** A bill is drawn “payable to.....or order”.

➤ Legal effect

- ✓ The holder gets a prima facie authority to make or complete the negotiable instrument.

➤ Liability on an inchoate instrument

- ✓ Rights of a person to whom an inchoate instrument is delivered
- ✓ He can recover only such amount as he was authorised to fill.

➤ Rights of HDC

- ✓ He can recover the whole amount stated in the instrument, but not exceeding the amount covered by the stamps.
- ✓ **Example:-** A owes B Rs. 1000. He gives B a blank acceptance on a bill which is sufficiently stamped to cover any amount upto Rs. 2,000. B indorses the bill to H, a Holder in due Course. H who fills up the amount as Rs. 2000 can recover the amount.

10. Maturity of a Negotiable Instrument (Sec 22)

Maturity of a negotiable instrument Days of grace

- ✓ It means the date on which the negotiable instrument falls due for payment.
- ✓ A negotiable instrument which is payable otherwise than on demand is entitled to 3 days of grace.

CALCULATION OF DAYS OF MATURITY (Sec.23 to 25)

Case	Date of maturity
Negotiable instrument payable on a specified day	Specified day + 3rd day
Negotiable instrument payable on a stated number of days after date	Date on which negotiable instrument is drawn + stated number of days + 3rd day
Negotiable instrument payable on stated number of days after sight	Date on which negotiable instrument is presented for sight + stated number of days + 3rd day
Negotiable instrument payable on stated number of days after happening of a certain event	Date on which such event happens + stated number of day + 3rd day
Negotiable instrument payable on stated number of months after date	Corresponding day of the relevant month (i.e., date on which negotiable instrument is drawn + stated number of months) + 3rd day
Negotiable instrument payable on stated number of months after sight	Corresponding day of the relevant month* (i.e., Date on which negotiable instrument is presented for sight + stated number of months) + 3rd day
Negotiable instrument payable on stated number of months	Corresponding day of the relevant month* (i.e., Date on which such event happens + stated number of

11. Negotiation- Meaning and Methods (Sec 14)

11.1 MEANING OF NEGOTIATION

Negotiation means transfer of a negotiable instrument to any other person so as to constitute that person the holder of such negotiable instrument.

11.2 METHODS OF NEGOTIATION

➤ Negotiation by delivery

- ✓ A bearer instrument may be negotiated by delivery.
- ✓ The delivery must be voluntary

➤ Negotiation by endorsement and delivery

An order instrument can be negotiated only by way of -

- ✓ endorsement; and
- ✓ delivery.

12. Negotiation Back (Sec 90)

12.1 MEANING OF NEGOTIATION BACK

If a negotiable instrument is negotiated by the holder, but the endorser again becomes the holder of such negotiable instrument **Then** – it is called as negotiation back.

12.2 EFFECT OF NEGOTIATION BACK

- ✓ The holder cannot enforce payment against an intermediate party to whom he was previously liable.
- ✓ The holder can enforce payment against all the parties to whom he was not previously liable.
- ✓ However, the holder can sue all the prior parties (including all intermediate parties to whom he was previously liable), if he had made sans recourse endorsement.

12.3 ILLUSTRATION OF NEGOTIATION BACK

Suppose that the endorsements on a Negotiable instrument are as under

P-----A-----B-----X-----Y-----A

- ✓ Here A is the person who is a prior party to the Instrument. He negotiated it to B, B to X, X to Y and again to this very A. on account of this last endorsement, A should have the right to claim money from X, Y and B.
- ✓ The rule is that every prior party is liable to every subsequent party. Thus, conversely, every subsequent party may sue every prior party.
- ✓ As a result of the prior party (A) having been taken back the instrument subsequently, he (A) becomes a 'subsequent party'. Therefore A, by reason of the last endorsement mentioned above, come to have the rights to claim money Y, X or B then Y, X or B in his turn can sue A because of A's Prior endorsement. This will lead to circuity of action.

To prevent this, Section 52 of the Negotiable Instruments Act, 1952 enacts an exception to the general rule to provide that the holder in due course of a negotiable instrument may sue all prior parties thereto. Thus, A, in the above case cannot sue Y, X or B. But A can sue P since the latter is prior to A's original endorsement. If however A, in original endorsement, had signed "sans recourse" there could be no circuity of action and A could sue Y, X or B

13. Endorsement (Sec 15 & 16)

13.1 MEANING OF ENDORSEMENT

Endorsement means

- **Signing**
 - ✓ on the face or back of negotiable instrument; or
 - ✓ on a slip of paper annexed to the negotiable instrument
- **By**
 - ✓ the holder of negotiable instrument
- **For the purpose of**
 - ✓ negotiating such negotiable instrument.

13.2 ESSENTIAL REQUIREMENTS OF A VALID ENDORSEMENT

- **Writing:-**The endorsement must be in writing
- **Signed:-**The endorsement shall not be valid unless it is signed.
- **No form:-** No particular form of words is necessary for endorsement
- **Delivery:-**Endorsement is complete when the instrument is delivered to the endorsee with the intention of passing the property in it to the endorsee. Delivery is to be made by the endorser himself or someone on behalf of him.

13.3 KINDS OF ENDORSEMENTS (Sec 16, 50, 52, 56)

- **General endorsement i.e. endorsement in blank:-**General endorsement means, an endorsement made by the endorser without writing the name of the endorsee.
Effect:-Order instrument is converted into bearer instrument.
- **Special endorsement i.e., endorsement in full :-**Special endorsement means an endorsement made by a holder by –
 - ✓ signing his name, and
 - ✓ adding a direction to pay the amount to a specified person
- **Restrictive endorsement :-**An endorsement which restricts the right of further negotiation is called as restrictive endorsement.
- **Partial endorsement:-**An endorsement which purports to transfer only a part of the amount of the instrument is called as partial endorsement. Partial endorsement is not valid at law.
- **Conditional or Contingent endorsement:-** Endorser makes his liability dependent upon the happening of an event.
Example:- Pay to A on safe receipt of goods
- **Sans Recourse: –** By adding these words after the endorsement, the endorser declines to accept any liability on the instrument of any subsequent party. Endorser relieves himself from the liability to all subsequent endorsees.
Example:- M, the holder of the bill, endorses it “without recourse” to N. N endorses it to P, P to Q, Q to R and R endorses it again to M. M can recover the amount of the bill from N,P,Q and R or any of them. Thus M is not only reinstated in his former rights, but has the right of an endorsee against N,P,Q and R
- **Facultative –** When it is desired to waive certain right, the appropriate words are added to indicate the fact.
Example:-Notice of dishonour dispensed with”

14. Difference between Negotiation and Endorsement

Basis	Negotiation	Assignment
1. Applicable Act	If a negotiable instrument is transferred by way of negotiation, Negotiable Instrument Act, 1881, applies.	Where any right is transferred by way of assignment, the Transfer of Property Act applies.
2. Meaning	Negotiation means transfer of a negotiable instrument to any other person so as to constitute that person the holder of such negotiable instrument.	Transfer of a right to receive the payment of a debt by one person (viz, assignor) to another document is called as assignment.
3. Scope	Negotiation can be made for transferring negotiable instruments only.	Assignment can be made of any right.
4. Method or manner	A bearer instrument can be negotiated merely by delivery, and an order instrument can be negotiated by endorsement and delivery.	Assignment is valid only if it is made in writing and is signed by the assignor.
5. Notice	Notice of negotiation is not required to be given to any party.	Notice of assignment must be given by the assignee to the debtor.
6. consideration	It is presumed that every negotiable instrument was negotiated for consideration.	There is no such presumption in case of assignment.
7. Burden of proof	The other party has to prove that negotiation was without any consideration.	The assignee has to prove that there was some consideration.
8. Better title	The transferee of a negotiable instrument acquires a title better than that of the transfer, i.e., he becomes a holder in due course.	The assignee does not acquire a title better than that of the assignor.
9. Stamp duty	Negotiation does not require payment of stamp duty.	Assignment requires payment of stamp duty.

15. Protection to Paying Banker (Sec 85)

- **Cheque payable to order**
 - ✓ Payment is made in due course.
 - ✓ The protection shall be available notwithstanding that any endorsement subsequently turns out to be a forgery.
- **Cheque originally payable to bearer**
 - ✓ Payment is made in due course
 - ✓ Payment is made to the bearer of the cheque
 - ✓ The protection shall be available notwithstanding that any endorsement appears on the cheque
- **Cheques crossed generally**

- ✓ Payment is made in due course.
- ✓ Payment is made to any banker.

➤ **Cheques crossed specially**

- ✓ Payment is made in due course
- ✓ Payment is made to the banker to whom the cheque is crossed.

16. Protection to Collecting Banker (Sec 131)

- ✓ A Banker who has in good faith and without negligence
- ✓ received payment for a customer for a cheque
- ✓ crossed generally or specially to himself
- ✓ shall not, in case the title to the cheque proves defective
- ✓ incur any liability to the true owner of the cheque
- ✓ by reason only of having received such payment

17. Liability of a Paying Banker

The paying banker shall be liable to the owner of the cheque for any loss sustained by him in the following 2 cases:-

- ✓ Where the paying banker pays a cheque crossed generally otherwise than to a banker.
- ✓ Where the paying banker pays a cheque crossed specially otherwise than to the specified banker.

18. Banker must refuse to Honour a Customer's Cheque

- **Stop payment:-** When the customer countermands payment i.e. orders the banker not to honour the cheque.
- **Garnishee order :-** When a Garnishee or other legal order attaching or otherwise dealing with the money in banker's hands is received by Banker
- **Death of customer:-** When a Banker receives notice of customer's death. But if he pays the cheque before he receives notice, the payment is valid
- **Insolvency of customer:-** When the customer becomes insolvent or an order of adjudication has been made against him.
- **Insanity or customer:-** When the banker receives notice of the customer's insanity.
- Assignment of funds by customer
- **Defect in title of holder:-** When the banker suspects, or has reason to believe, that the title of the person presenting the cheque is defective
- **Loss of cheque:-** When the holder gives a notice of loss of the cheque to the Banker.
- **Receipt of application for closure of account:-** When the customer gives notice to the banker to close the account.
- **Stale cheque, i.e., outdated cheque**
- **Post dated cheque**
- **Undated cheque**
- **Materially altered cheque, mutilated cheque, cheque of doubtful validity, incomplete cheque**
- **Different signatures**

19. Banker may refuse to Honour a Customer's Cheque

- Insufficient funds
- Funds not applicable
- Presentment at different branch
- Presentment after banking hours

20. Effect of Non-Presentment of Cheque within Reasonable time

No liability of drawer if bank fails Conditions

- ✓ The drawer has sufficient balance when he issue the cheque, and when the cheque ought to be presented for payment.
- ✓ The holder fails to present the cheque within a reasonable time of issue of the cheque.
- ✓ Meanwhile (i.e. after issue of the cheque but before presentation of the cheque by the holder) the bank fails, and consequently the drawer suffers actual damages.

21. Bouncing or Dishonour of Cheques (Sec 31 & 138)

21.1 LIABILITY OF DRAWEE ON DISHONOUR

If The drawer has sufficient funds in the account; and Such funds are properly applicable to payment of the cheque

Then

- ✓ The drawee is duly required to pay the cheque.
- ✓ In case of default by drawee (i.e. Banker), the drawee shall compensate the drawer for loss caused to him.

21.2 LIABILITY OF DRAWER ON DISHONOUR (Sec 138)

➤ Nature of liability

- ✓ Imprisonment – 2 years (Maximum); or
- ✓ Fine - 2 times the amount of cheque (Maximum); or
- ✓ Both

➤ Conditions

- ✓ **Debt:-** Cheque was issued to discharge a legally enforceable debt.
- ✓ **Reason for dishonour:-** The cheque must have been dishonoured due to insufficiency of funds in the account of the drawer
- ✓ **Presentment of cheque:-** The cheque must have been presented for payment to the bank
 - within 3 months from the date on which he is drawn or
 - validity period of the chequewhichever is earlier
- ✓ **Demand should be within 30 days:-** Demand for payment of the said amount of money by giving a notice in writing to the drawer of the cheque within 30 days
- ✓ **Default by drawer to pay** - within 15 days of demand made.
- ✓ **Complaint by holder** – within 1 month, with the Court.

22. Holder (Sec 8 & 9)

22.1 MEANING OF HOLDER

- ✓ He must be entitled to the possession of negotiable instrument in his own name.
- ✓ He must be entitled to receive or recover the amount due on negotiable instrument from the parties liable on negotiable instrument.

23. Holder in due Course

23.1 MEANING OF HOLDER IN COURSE

- ✓ He must be a holder.
- ✓ He must have become the holder for consideration.
- ✓ He must have obtained the possession of negotiable instrument before maturity
- ✓ He must have obtained the negotiable instrument in good faith, i.e. without sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.

23.2 PRIVILEGES OF HOLDER IN COURSE

- ✓ Every prior party to a negotiable instrument is liable to a HDC.
- ✓ A holder who derives title from HDC has the same rights as that of a HDC.
- ✓ No prior party can set up a defence that the negotiable instrument was drawn, made or endorsed by him without any consideration.
- ✓ No prior party can set up a defence that the negotiable instrument was lost or was obtained from him by an offence or fraud or for an unlawful consideration. Thus, HDC gets a valid title to the negotiable instrument even though the title of the transferor was defective.
- ✓ HDC can claim full amount of the negotiable instrument (but not exceeding the amount covered by the stamp) even though such amount is in excess of the amount authorised by the person delivering an inchoate negotiable instrument.

24. Difference between Holder and HDC

Basis	Holder	HDC
1. consideration	A person becomes a holder even if he obtains the negotiable instrument without any consideration.	A person becomes a HDC only if he obtains the negotiable instrument for consideration.
2. Before Maturity	A person becomes a holder even if he obtains the negotiable instrument after the maturity of the negotiable instrument.	A person becomes a HDC only if he obtains the negotiable instrument before its maturity.
3. Good Faith, i.e., bonafide	A person becomes a holder, even if he does not obtain	For being a HDC, a person must obtain the negotiable

	the negotiable instrument in good faith.	instrument in good faith.
4. Privileges	A holder is not entitled to the privileges, which are available for HDC.	A HDC is entitled to various privileges as specified under the Negotiable Instruments Act, 1881.
5. Right to sue	A holder cannot sue all the prior parties.	A HDC can sue all the prior parties.

25. Payment in Due course (Sec 10)

- ✓ Payment is made as per apparent tenor.
- ✓ Payment is made in good faith-
- ✓ Payment is made without negligence
- ✓ Payment is made to holder of negotiable instrument
- ✓ Payment is made in money only

26. Material Alteration (Sec 20, 49, 87 & 125)

26.1 MEANING OF MATERIAL ALTERATION

An alteration is called as material alteration if it alters –

- ✓ The character or operation (i.e. the legal effect) of a negotiable instrument; or
- ✓ The rights and liabilities of any of the parties to a negotiable instrument

26.2 MATERIAL ALTERATION AUTHORISED BY ACT

- ✓ Filling blanks of an inchoate instrument (Sec.20)
- ✓ Conversion of a blank endorsement into an endorsement in full (Sec.49)
- ✓ Crossing of cheques (Sec.125)
- ✓ Conversion of general crossing into special crossing or not negotiable crossing or A/c Payee Crossing (but not vice – versa)
- ✓ Conversion of a bearer instrument into an order instrument by deleting the word 'Bearer'.

26.3 EFFECT OF MATERIAL ALTERATION (SEC 87)

- ✓ All the parties to negotiable not consenting to the material alteration are discharged.

27. Acceptance (Sec 7 & 86)

27.1 MEANING OF ACCEPTANCE (SEC 7)

- ✓ The drawee signs the bill; and
- ✓ The drawee delivers it to the holder of the bill; or

27.2 EFFECT OF ACCEPTANCE

- ✓ The drawee becomes the acceptor.

27.3 ESSENTIALS OF ACCEPTANCE

- ✓ Writing (whether on the face or back of the bill)
- ✓ Signed (Signature without the word 'accepted' is also valid)
- ✓ Signing on the bill
- ✓ Delivery or intimation to the holder that the bill has been accepted.

27.4 TYPES OF ACCEPTANCE (SEC 86)

- ✓ **General** – Acceptance of bill without any qualification.
- ✓ **Qualified** – Acceptance of bill subject to some qualification (e.g. accepting the bill subject to the condition that the payment of bill shall be made only on happening of an event specified therein).

27.5 EFFECT OF QUALIFIED ACCEPTANCE (SEC 86)

- ✓ The holder may object to the qualified acceptance. In such a case, it shall be treated that the bill is dishonoured due to non – acceptance.
- ✓ He may give his consent to the qualified acceptance. In such a case, all the previous parties, not consenting to it, are discharged.

28. Dishonour by Non-Acceptance (Sec 91)

28.1 MEANING OF DISHONOUR BY NON-ACCEPTANCE

- ✓ A bill is dishonoured by non – acceptance if it is duly presented for acceptance, but the drawee refuses to accept the bill.

28.2 CASES IN WHICH A BILL IS DISHONoured BY NON-ACCEPTANCE

- ✓ Where a bill is not accepted by the drawee within 48 hours of presentment of bill. If the holder allows to the drawee more than 48 hours for acceptance, all the prior parties not consenting to the same are discharged from liability to such holder.
- ✓ In case there are two or more drawees who are not partners, if the bill is not accepted by all the drawees.
- ✓ Where the drawee is a fictitious person
- ✓ When the drawee cannot be found even after a reasonable search.
- ✓ When the drawee is incompetent to contract.
- ✓ Where the drawee gives a conditional acceptance, and the holder does not give his consent to the conditional acceptance.

28.3 EFFECTS OF DISHONOUR BY NON-ACCEPTANCE

- ✓ The holders gets an immediate right to sue all the prior parties.
- ✓ He need not wait till the maturity of the bill for it to be dishonoured on presentment for payment.

28.4 NON-APPLICABILITY

- ✓ A promissory note or a cheque cannot be dishonoured by non – acceptance since a promissory note or a cheque does not require any acceptance.

29. Acceptance for Honour (Sec 108-112)

29.1 MEANING OF ACCEPTANCE FOR HONOUR

- ✓ The person who accepts the bill for the honour of any other person is called as an acceptor for honour;

29.1 CONDITIONS OF ACCEPTANCE FOR HONOUR

- ✓ The bill must have been noted for non – acceptance
- ✓ The acceptance is given –
 - for the honour of any party already liable under the bill.
 - By any person who is already not liable under the bill.
 - With the consent of the holder of the bill.
- ✓ The acceptance must be made in writing on the bill.

29.2 LIABILITY OF ACCEPTOR FOR HONOUR

- ✓ He is liable to pay the amount of the bill, if the drawee does not pay.
- ✓ He is liable only to the parties subsequent to the party for whose honour the bill is accepted.

29.3 RIGHTS OF ACCEPTOR FOR HONOUR

- ✓ He is entitled to recover the amount paid by him from the party for whose honour the bill was accepted, and from all the parties prior to such party.

30. Payment for Honour (Sec 113-114)

30.1 MEANING OF 'PAYER FOR HONOUR'

- ✓ A person who pays a bill for honour of any other person is called as 'payer for honour'

30.2 CONDITIONS FOR 'PAYMENT FOR HONOUR'

- ✓ The bill must have been noted for non – payment.
- ✓ Payment for honour is made –
 - for the honour of any party already liable under the bill.
 - By any person (whether or not he is already liable under the bill).
 - With the consent of the holder of the public.
- ✓ The payment must be recorded by Notary Public.

30.3 RIGHTS OF PAYER FOR HONOUR'

- ✓ The payer for honour is entitled to all the rights of a holder.
- ✓ He can recover all the sums paid by him from –

- the party for whose honour he pays; and
- all the parties prior to such party.

31. Dishonour by Non-Payment (Sec 92)

Kinds of negotiable instrument	A negotiable instrument shall be dishonoured by non – payment if default in payment is made by the following parties
Promissory note	Maker
Bill	Acceptor (Drawee, in case the bill does not require acceptance)
Cheque	Drawee

32. Notice of Dishonour (Sec 108-112)

32.1 NOTICE BY WHOM

- ✓ Notice may be given by the holder or any party liable on the negotiable instrument.

32.2 NOTICE TO WHOM

- ✓ Notice must be given to all the parties to whom the holder seeks to make liable.

32.3 CONTENTS OF NOTICE

- ✓ Notice must disclose the fact of dishonour of negotiable instrument

32.4 EFFECT OF DEFAULT

- ✓ A party (other than the party primarily liable on the negotiable instrument) to whom notice of dishonour is not given is discharged from liability on the negotiable instrument.

32.5 WHEN NOTICE OF DISHONOUR IS UNNECESSARY OR EXCUSED (SEC 98)

- ✓ When notice of dishonour is dispensed with by a party.
- ✓ Where the drawer of the cheque has countermanded payment, notice to drawer is not required to be given.
- ✓ When the party entitled cannot be found even after due search.
- ✓ Where the party bound to give notice is unable to give notice without any fault of his own.

33. Noting and Protesting (Sec 99-103)

33.1 MEANING OF NOTING

- ✓ Recording the fact of dishonour of a negotiable instrument on the negotiable instrument.

33.2 PROCEDURE AND CONTENTS OF NOTING

- ✓ The dishonoured bill is handed over to a Notary Public.
- ✓ Notary Public presents it again for acceptance/payment.

- ✓ If the drawee/acceptor refuses to accept or pay the bill, the Notary Public records the fact of dishonour on the bill.

33.2 NOTING IS OPTIONAL

- ✓ It is not mandatory to get the fact of dishonour noted.

33.3 MEANING OF PROTEST

- ✓ A certificate issued by Notary Public stating the fact of dishonour.

34. Drawee in case of Need (Sec 7-115)

- ✓ The name of any person may be given in a bill as 'drawee in case of need'.
- ✓ His liability arises on the bill only when the bill is not accepted by the drawee named in the bill.
- ✓ The bill is not dishonoured until it has been dishonoured by drawee in case of need.

35. Discharge of a Negotiable Instrument

The Negotiable Instrument is deemed to be discharged in the following cases –

- **Payment [Sec.78]:-**
 - ✓ When the party primarily liable on the instrument i.e. Maker of P/N, Acceptor of B/E or Drawee Bank, makes the payment in due course to the Holder at or after maturity.
 - ✓ Payment by a party who is secondarily liable does not discharge the instrument because the payer holds it to enforce it against prior endorsers and the principle Debtor.
- **Cancellation of N/I [Sec.82]:-** When the holder cancels an instrument with intention to release the party primarily liable thereon from liability, the instrument is discharged and ceases to be negotiable.
- **Express Waiver of Rights by Holder:-**The N/I is discharged when the Holder, at or after its maturity absolutely and unconditionally renounces in writing, his rights against all the parties to the instrument.
- **Lapse of time:-**An instrument becomes discharged by lapse of time making the debt time barred under the limitation Act.
- **Insolvency of party primarily liable:-** When the party primarily liable becomes insolvent, the instrument is discharged and the holder cannot make any other prior party liable thereon.
- **Material Alteration to Instrument:-**The instrument stands discharged when it is rendered void by a material alteration to the Instrument.

36. Presumptions as to Negotiable Instrument (Sec 118)

Unless the contrary is proved, the following presumptions shall be made –

- **As to consideration:-**That every negotiable instrument was made or drawn for consideration and that every such instrument when it has been accepted, endorsed or negotiated has been for consideration.
- **As to date:-**That every negotiable instrument bearing a date was made or drawn on such date.
- **As to time of acceptance:-**That every accepted bill of exchange was accepted within a reasonable time after its date and before its maturity.
- **As to time of transfer:-**That every transfer of a negotiable instrument was made before its maturity.
- **As to order of endorsements:-**That the endorsements appearing upon a negotiable instrument were made in the order in which they appear thereon.
- **As to stamp:-**That a lost promissory note or bill of exchange was duly stamped.
- **That holder is a holder:-**That the holder of a negotiable instrument is a holder in due course.
- **As to dishonour:-**If a suit is filed upon an instrument which has been dishonored, the court shall, on proof of the protest, presume the fact of dishonour.