

# Negotiable Instruments Act, 1881 : Introduction

## INTRODUCTIONS

Money can easily and safely be transferred from one place or person to another with the help of negotiable instruments. The holder of the negotiable instruments can transfer these instruments merely by delivery and in some cases by delivery and endorsement. The holder of a negotiable instrument can enforce his claim very quickly.

The provisions relating to negotiable instruments is given in the Negotiable Instruments Act, 1881. The Act is applicable to the whole of India. The Negotiable Instrument Act, 1881 specially deals with Promissory Notes, Bills of Exchange and Cheques. This Act does not exclude other instruments if they satisfy the conditions of negotiability by usage or custom of the trade. For instance, *Hundi* is the most important single example, besides Share Warrant, Port Trust Debenture. etc.

## THE RESERVE BANK OF INDIA ACT. 1934

The Negotiable Instrument Act, 1881 does not affect the provisions of section 31 and 32 of the Reserve Bank of India Act, 1934, The Central Government and the Reserve Bank of India have been given the monopoly rights of issuing notes (currency notes) in India.

Further Sec. 31 of the Reserve Bank of India Act, 1934 lays down that no person in India other than the Reserve Bank of India or the Central Government can draw, accept, make or issue any bill of exchange, *hundi*, promissory note or engagement for the payment of money payable to bearer on demand.

No person other than the Reserve Bank, or the Central Government, can make or issue a promissory note expressed to be payable to the bearer of the instrument.

## PENALTY

Sec.32 of the RBI Act provides penalty for violating the provisions of Sec. 31. If any person makes such instruments, he shall be punishable with fine which may extend to the amount of the bill, note etc such bill, will be illegal.

## DEFINITION OF NEGOTIABLE INSTRUMENT

According to Section 13 "Negotiable Instrument" means a promissory note, bill of exchange or cheque payable either to order or to the bearer.

Sec. 31 of R.B.I. Act. the words 'or to bearer' in respect of promissory notes are inoperative. However, a promissory note or a bill of exchange, on being endorsed in blank can become payable to bearer on demand.

Above definition hardly defines a negotiable instrument, it rather describes a negotiable instrument by saying that it means a promissory note, bill of exchange or cheque as such, the absolute ownership of the property represented by the instrument vests in the holder, so that (1) he is not prejudiced by any defect in his transferor's title and (2) he can sue on the instrument in his own name".

This definition does not explain the salient features of a negotiable instrument. It defines a negotiable instrument as if one defines a horse as a horse-like animal. Hence, we shall examine the following definition given by Justice Willis :

"A negotiable instrument is one, the property in which is acquired by any one who takes it *bona fide* and for value notwithstanding any defect of title in the person from whom he took it."

Above definition concludes that a person acquires a good title if he has taken a negotiable instrument *bona fide* and for value even if the title of the transferor was defective, e.g., if he takes a bearer cheque *bona fide* and for value for even from a thief or a finder, he will acquire a good title.

### FEATURES OF A NEGOTIABLE INSTRUMENT

Following are the characteristics of negotiable instrument

**1. Easy transferability**—The property in a negotiable instrument is transferred by mere delivery, if the instrument is payable to bearer, by delivery and endorsement if payable to order.

**2. Transferee's title free from all defects**—The transferee, who takes it *bona fide* for value and before maturity (called holder in due course) gets a good title.

**3. Transferee can sue in his own name**—A transferee has right to sue upon a negotiable instrument in his own name.

**4. Notice of transfer not necessary**—The transferee is not required to give a notice of transfer to the person liable to pay.

**5. Presumptions**—There are many presumptions which are applied to a negotiable instrument unless the contrary is proved.

In **Marimuthu Kounder v. Radhakrishnan and others, AIR 1991 Ker 39** the Kerala High Court observed that the presumption as to existence of consideration is not irrefutable. When once the Court finds that the defendant has executed the promissory note, then the burden is on the defendant to prove that there is no consideration. The initial burden rests on the plaintiff, who has to prove that the promissory note is executed by the defendant. If there is an admission by the defendant, certainly there is no burden on the plaintiff to prove the execution.

**1. As to Consideration**—Every negotiable instrument deemed to have been made or drawn, accepted, endorsed, negotiated or transferred for consideration. As such the holder need not prove consideration. However, this presumption would not arise if it is proved that the instrument was obtained from its owner by any offence, fraud or for unlawful consideration.

**2. As to Date**—Every negotiable instrument is presumed to have been made on the date which it bears.

**3. As to Acceptance**—It is presumed that every accepted bill was accepted within a reasonable time and before the date of its maturity.

4. **As to transfer**—It is presumed that every transfer was made before maturity.
5. **As to the order of endorsements**—The endorsements are presumed to have been made in the same order in which they appear.
6. **As to Stamp**—In case an instrument is lost it is presumed that it was duly stamped and the stamp was cancelled.
7. **As to holder is a holder in due course.** Every holder is presumed to be a holder in due course.
8. **As to Dishonour**—If a suit is filed for dishonour of an instrument the Court, on the proof of protest, presumes the fact of dishonour of instrument.

If the promisor denies the execution of the promissory note taking the plea that he signed on a blank paper, then the burden is on the plaintiff to prove execution. *Sri Khetramohan Rav v Udayanarayan Panda & Another*, AIR 1991 Orissa 25).

### Types of Negotiable Instruments

The Negotiable Instrument Act deals with only three types of negotiable instruments, viz (i) promissory notes, (ii) bills of exchange and (iii) cheques. However, it does not exclude any other instrument if it is transferable by usage or custom of trade. Accordingly, 'hundi' share warrant', 'dividend warrant', 'bearer debentures', etc, are included in the category of negotiable instruments.

**Status of Bill of Lading**—A bill of lading is not a negotiable instrument as it does not satisfy the twin conditions of negotiability. It is transferable like a negotiable instrument but the transferee does not acquire a good title. It is a semi negotiable instrument.

### PROMISSORY NOTE

According to 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, or to the order of a certain person or to the bearer of the instrument.

The person making the promise to pay is known as "maker". The person to whom the payment is to be made is known as payee.

**Examples.** A signs instruments in the following terms :

- (i) I promise to pay B or order Rs. 2000
- (ii) I acknowledge myself to be indebted to B in Rs. 4000 be paid on demand for value received.
- (iii) "Mr. B., I.O.U. Rs. 4000 (I.O.U. means, I owe you).
- (iv) "I promise to pay B Rs. 2000 and all other sums which shall be due to him."
- (v) I promise to pay B Rs. 2000 first deducting thereout any money which he may owe me."

Of all the above instruments only (i) and (ii) are promissory notes and the rest are not promissory notes.

### ESSENTIALS OR CHARACTERISTICS OF A VALID PROMISSORY NOTE

Following are the essentials of a promissory note :

1. **In writing.** A promissory note must be in writing. An oral promise cannot become a promissory note.
2. **Promise to pay.** There must be an express promise to pay. It cannot be implied, A mere acknowledgement of a debt is not sufficient. For example, a promissory note, "I am indebted to pay B Rs. 500", is not a promissory note.

ment as promissory note.

**3. Certain and unconditional.** The promise to be valid must be certain and unconditional.

*Examples.*

(a) "I promise to pay B Rs. 2000 when I am able to pay"

(b) "I promise to pay B Rs. 2000 on my marriage with C."

However, a promise to pay on the condition of the happening of an event which must happen is not conditional within the meaning of Sec. 4 For example :

1. Promise to pay at a specified time.

2. Promise to pay at a specified place.

3. Promise to pay after the happening of an event which is certain to happen.

**4. Signed by the maker**—The promissory note must be signed by the maker even if it has been written by the promisor himself in his own handwriting. The signature may be done at any place, even at the top or at the back of the instrument. It is not necessary that the signature should be done at the bottom. The signature may be in full or in mere initials. It may be in ink or pencil. Even a rubber stamp or facsimile may be used. The only thing is that it should *prima facie* show the intention of the maker to sign the instrument. In case the maker is illiterate, his thumb impression is sufficient.

**5. Sum of Money**—The amount to be paid must be certain, otherwise the instrument will be invalid. For example, X promises to pay Y Rs. 500 and all other sums which become due. This is not a valid promissory note.

A promise to pay money with interest is valid. If the rate of interest is not given, it will not be valid. For example, X promise to pay Y Rs. 2000 with interest is not valid.

A promissory note cannot be drawn payable to the maker himself. Such a note is a nullity. But, if it is endorsed by the maker to some other person, or endorsed in blank, it becomes a valid promissory note [Gay v. Landal (1848) LT CP 286]

**6. Promise to pay must be in legal tender money**—The promise to pay must be in legal tender money.

*Examples :*

(i) Promises to pay to Y 2000 at Agra. It is not a valid promissory note.

(ii) Promises to pay to Y 2000 and a suit. It is also not a valid promissory note.

**7. Bank note or currency note is not a promissory note**—A bank note or a currency note is money itself.

**8. Certain Parties**—The person making the promise, i.e., the person by whom the payment is to be made and the person to whom the payment is to be made must be certain. They may be named or their designations may be given. In case there are two or more persons they will bind themselves jointly but not alternatively.

**FORM OF PROMISSORY NOTE**

The law has not given any specific form of a promissory note. As such it may be in any form but it must satisfy all the essential conditions mentioned above.

**Specimen of a Promissory Note**

Rs. 20,000

On demand, I promise to pay Dr. Rani or order a sum of rupees twenty thousand, for value received

Kanpur  
January 6, 2009

Revenue  
Stamp  
Sd/Deepa

To,  
Dr. Rani  
148, Ramnagar  
Kanpur-208 001

**BILL OF EXCHANGE**

**According to sections 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 or to the order of, a certain person or to the bearer of the instrument.

**There are three parties in it**—The maker of the bill is called the "drawer". The person directed to pay is called the "drawee". The person to whom the money is to be paid is called the "payee". If the payee holds the bill, he is called the holder

It is essential in certain cases for the holder to present the bill to the drawee for the purpose of his acceptance. When the drawee signifies his acceptance by signing on the bill, he becomes an acceptor.

In some cases drawer and drawee may be the same person. When a principal draws a bill on his agent the, drawer and the drawee are the same. Drawer and payee may also be the same.

**Some other Features—**

- (i) Promise to pay money only.
- (ii) It may be payable in instruments.
- (iii) It may be payable on demand or after a definite period.
- (iv) It cannot be made payable to bearer on demand.

**Specimen of a Bill of Exchange**

Rs. 20,000

Three months after date Dr. Ajay Gupta or order a sum of rupees twenty thousand only, for value received

Kanpur  
January 6, 2009

S/d  
Rani  
Revenue  
Stamp

To,  
Vijay Gupta  
148, Vaishali,  
Kanpur-208 001

Accepted  
Sd/- Ajay

**Characteristics of a Bill of Exchange**

The essential elements of a bill of exchange are as follows :

1. It must be in writing.
2. It must contain an order to pay and not a promise or request.
3. The order must not be conditional.
4. The drawer must sign the bill.
5. The sum payable must be certain or capable of being made certain.
6. There are three parties i.e., drawer, drawee and payee.
7. The sum payable must be in legal tender money.
8. It must be stamped.
9. A bill cannot originally be drawn,
10. The other formalities, like, date, place and the words "for value received; are not necessary.

In the specimen given above Rani is the drawer. Vijay is the drawee and Ajay is the payee. When Ajay accepts the bill by signing the bill, he becomes an acceptor also.

### **DIFFERENCE BETWEEN A BILL OF EXCHANGE AND A PROMISSORY NOTE**

There are the following points of distinction between a bill of exchange and a promissory note :

1. A bill is an unconditional order, whereas a note is an unconditional promise.
2. In a bill the drawer and drawee, or drawer and payee can be the same person. A promissory note cannot be made payable to the maker himself.
3. In a bill there can be three parties. In case of a promissory note there are only two parties.
4. A bill payable after sight cannot be presented for payment before it has been accepted. A promissory note is not at all required to be accepted.
5. The position of a drawer in a bill is like that of a surety. In a promissory note the liability of the maker is primary and absolute.
6. A bill can be drawn payable to bearer, whereas a promissory note cannot be drawn payable to bearer.
7. Notice of dishonour of a bill by the holder to the drawer and intermediate endorsers is required. In case of a promissory note no such notice is needed.
8. The drawer of a bill of exchange stands in an immediate relation with the acceptor. The maker of a promissory note, stands in an immediate relation with the payee, and the endorser with his endorsee.
9. Presentment for acceptance is applicable to certain types of bills. A promissory note is not at all required to be accepted.
10. Foreign bills are generally drawn in sets of three. A foreign promissory note is not drawn in sets, only one copy is prepared.
11. A bill can be accepted for honour. A promissory note is not at all required to be accepted.
12. A foreign bill must be protested for dishonour if it is required under the law of the country where it is drawn. In case of a foreign note, there is no need for such a protest.

### CHEQUE

A cheque is a special type of bill of exchange.

According to section 6 A 'cheque' is a bill of exchange expressed to be payable only on demand.

Although, a cheque is a bill of exchange yet it has following two additional characteristics.

1. A cheque is always drawn on a specified banker with whom the drawer has deposited the money;
  2. It is always payable on demand and not otherwise.
- Thus it can be said that all cheques are bills of exchange but all bills of exchange are not cheques.

### Specimen of Cheque

PAY : D.K. Verma

2-4-2009

RUPEES : Twenty Thousand only

OR ORDER  
Rs. 20,000

A/C No. 611

L.F.

NILS

XYZ BANK

Shastri Nagar, Lajpat Nagar, Kanpur

### DIFFERENCE BETWEEN A BILL OF EXCHANGE AND A CHEQUE

There are following points of difference

1. A bill of exchange may be drawn on any person. A cheque is always drawn on a specified banker.
2. A bill of exchange has to be stamped. Stamp is not necessary on a cheque.
3. A bill of exchange cannot be made payable to bearer on demand. A cheque can be made payable to the bearer on demand.
4. A bill of exchange may be payable on demand or after a certain period. A cheque is always payable on demand.
5. Certain types of bills of exchange must be accepted before they are presented for payment. In case of a cheque acceptance is not necessary.
6. In a bill three days of grace are allowed to the acceptor for payment. In case of a cheque no such grace period is allowed.
7. If a bill of exchange is not presented for payment, the drawer is discharged from his liability. Failure to present the cheque discharges the drawer, only when he has suffered any loss due to the failure of the holder to present the cheque for payment within a reasonable time of its issue.

**Example.** X has 2000 rupees in his bank. X draws a cheque of Rs. 1500 to Y. The bank fails before Y presents the cheque. X is discharged but Y can prove against the bank for the amount of the cheque.

8. Payment of a bill of Exchange cannot be stopped. The payment of a cheque can always be stopped.

9. A bill of exchange cannot be crossed. A cheque can be crossed.

In case the instrument is a bill of exchange and it is marked "after sight" then its payment cannot; be demanded unless it has been presented for acceptance before payment and specified period has been over.

**5. Instrument payable to the bearer on demand.** The Reserve Bank of India Act prohibits issue of bill of exchange or promissory note payable to bearer on demand. It is only the Reserve Bank of India and the Central Government which can issue bills or notes payable to bearer on demand. Any person who issues such bills or notes payable to bearer on demand is punishable with fine which may extend to the amount of the instrument.

### CROSSING OF CHEQUES

A cheque can be made safe by crossing it. To cross a cheque two transverse parallel lines are drawn on the left hand corner of the cheque. It is also usual to write the words '& Co.' in between these two lines. However. It is not necessary to write these words. A crossing is a direction to the paying banker not to pay the money to the holder at the counter.

Crossing of cheques had its origin in London Clearing House. The name of the bank, whose claim was cleared was written across the face of the cheque within two parallel lines. In the beginning of 19th century, this practice became as an element of safety.

Crossing is a unique feature affecting to certain extent the obligation of the paying banker and also its negotiable character. It is a peculiar method of modifying the instrument to the banker for payment of the cheque. *Crossing on a cheque is a direction to the paying banker by the drawer that payment should not be made across the counter.* The payment on a crossed cheque can be collected only through a banker.

According to **Chorley**, crossing may be broadly described as an instruction from the drawer to his banker, that he is only to pay the instrument provided certain conditions are fulfilled." According to Section 123, "Where a cheque bears across its face an addition of the words 'and company' or any abbreviation thereof, between two parallel transverse lines, or of two parallel transverse lines simply, either with or without the words 'not negotiable', that addition shall be deemed a crossing and the cheque shall be deemed to be crossed generally.

Crossing of a cheque is effected by drawing two parallel transverse lines with or without the words 'and company' or any abbreviation thereof. A cheque that is not crossed is called an open cheque.

#### Types of Crossing

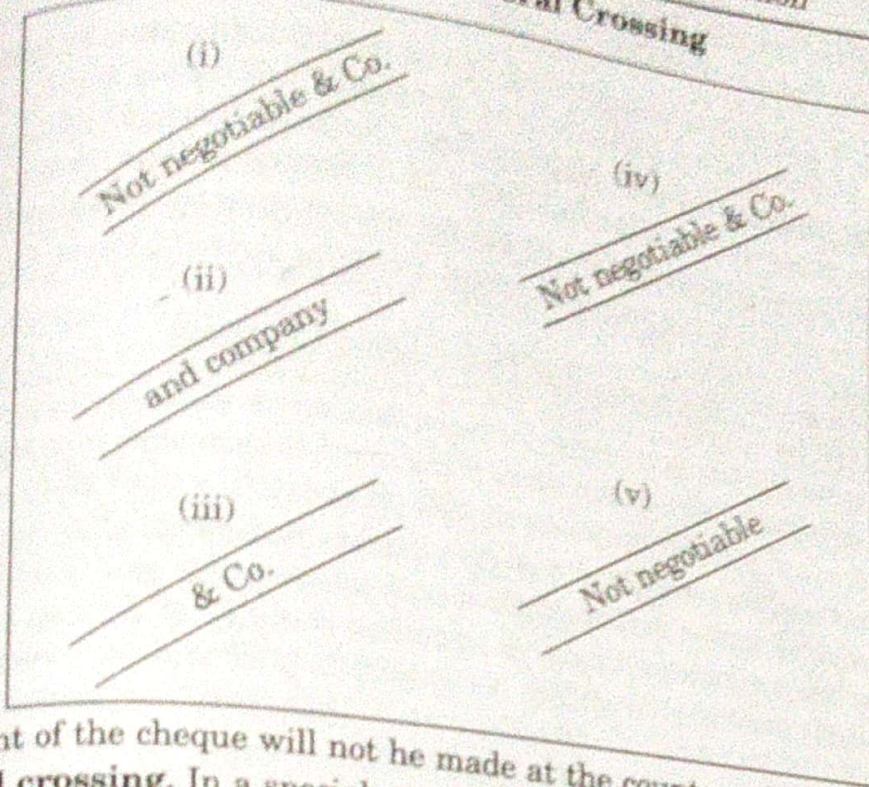
Crossing are of the following types :

1. General crossing.
2. Special crossing.
- (3) However, there is yet one type of crossing which is recognized by usage and custom, called restrictive crossing ;
- (4) Not negotiable crossing.

1. **General crossing**—In a general crossing, simply two parallel transverse line, with or without the words not negotiable in between may be drawn. Such a cheque is crossed generally.

Section 123 in this regard provides "Where a cheque bears across its face addition of the words 'and company' or any abbreviation thereof, between two parallel transverse lines or of two parallel transverse lines simply, either with or without the words not negotiable that additional shall be deemed a crossing and the cheque shall be deemed to be crossed generally."





The payment of the cheque will not be made at the counter.

**2. Special crossing.**

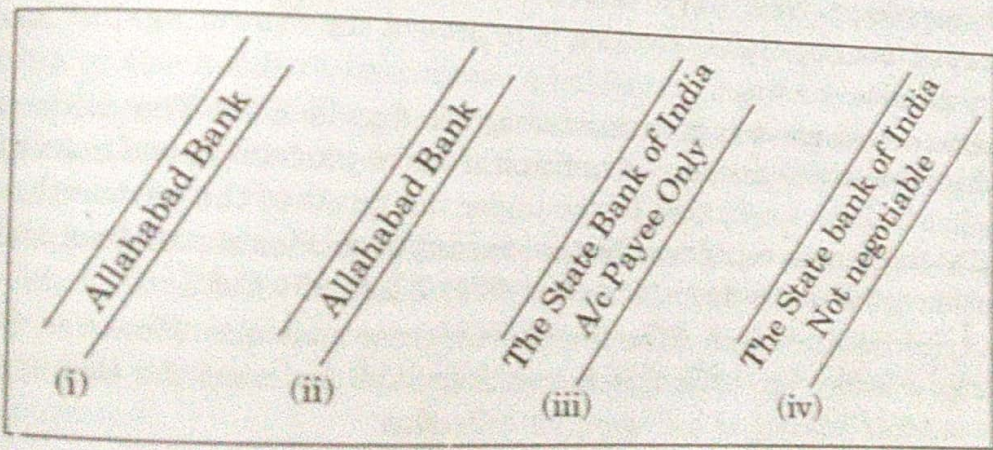
In a special crossing the name of a banker with or without the words 'not negotiable' is written on the cheque. Such a cheque is crossed specially to that banker.

Special crossing implies the specification of the name of the banker on the face of the cheque. Section 124 in this regard, reads: Where a cheque bears across its face an addition of the name of a bank, either with or without the words not negotiable, that addition shall be deemed a crossing, and the cheque shall be deemed to be crossed to that banker. "Drawing two parallel lines is not necessary in case of a specially crossed cheque."

The object of special crossing is to direct the drawee banker to pay the cheque only if it is presented through the particular bank mentioned therein. Two transverse parallel lines are necessary for a general crossing. Whereas for a special crossing no such lines are necessary.

The effect of special crossing is that the paying banker will pay the amount of the cheque only through the bank named in the cheque.

**Specimen of Special Crossing**



discussed in case of a bill of exchange, always a specified bank. In a cheque or bill the drawer and the payee may be one and the same person.

## HOLDER AND HOLDER IN DUE COURSE

According to section 8 the holder of a promissory note, bill of exchange or a cheque means any person entitled in his own name to the possession thereof and to receive or recover the amount thereon from the parties thereto.

### Essential Conditions of a Holder

- (i) He should be entitled in his own name to the possession of the negotiable instrument.
- (ii) Either holder has the possession or he is entitled to recover the possession.
- (iii) He should be a *de jure* (in law) holder and need not be a *de facto* (in fact) holder except in case of a bearer instrument. A person who is not in actual possession of a negotiable instrument but is entitled to the possession of the instrument is a holder.

### Example.

X lost his cheque. It is found by Y, Y is in actual possession but X being the owner, is entitled to the possession of the cheque. Hence, Y is not holder, although he is in possession of the cheque. Here is X the holder, although cheque is not in his possession yet he is entitled to the possession of the instrument in his own name.

A holder in case of an instrument payable order can be a payee or indorsee. If the instrument is payable to bearer, holder means the possessor. Thus, a benamidar or a trustee or a guardian who has taken the instrument in his own name is a holder. A beneficial owner can not be a holder because he is not entitled to the instrument in his own name.

## HOLDER IN DUE COURSE

In a negotiable instrument, the transferee acquires a better title. However, it is possible only when the transferee is a holder in due course.

According to section 9 a holder in due course is a person who acquires a promissory note, bill or cheque bona fide for value and before maturity.

A holder in due course must satisfy the following conditions:

1. **He became the holder for valuable consideration** : For valuable consideration he became possessor of the negotiable instrument if the instrument is payable to bearer, or payee or indorsee, if the instrument is payable to order.

2. **He became the holder before maturity of the instrument** : For a bill or note he should have become a holder before maturity. However, for a cheque, there is no question of maturity. When he becomes holder after maturity or even on the day of maturity, he cannot be called a holder in due course. Consequently, he may not get a better title than that of the transferor.

3. **He became the holder in good faith.** Holder became a holder without having sufficient cause to believe that any defect existed in the title of the person from whom he took it or derived his title.

The test of good faith is whether holder took the negotiable instrument honestly and with due care. If yes, he acquired it in good faith. He should not have been negligent at the time of taking an instrument. If a person has suspicion at the time of taking an instrument he will not be a holder in due course. He must make enquiry so as to find out the truth. If he does not make any enquiry he cannot be called a holder in due course.

*Examples.* (i) A bill which has been torn up into pieces and pasted together creates a doubt. It is just possible that the payee might have cancelled it by tearing.

(ii) Where alteration is apparent on the face of it.

Holder should not have notice of defects whether actual or constructive. Notice should be in relation to defects of the person from whom he took it. A defect in the title of prior party does not affect the title.

**Case Law** : Defendants No. 2 to 4 who were partners in a Firm. Defendant No. 1 supplied certain goods to defendant No. 6 Defendant No. 6 issued two cheques in favour of the firm in part payment of the cost of goods. The cheques were bought by the plaintiff bank and their proceeds were credited to the account of the firm and the amount was withdrawn on various dates. When the cheques were presented for payment these were returned with an endorsement. full cover not received. It was contended that the plaintiff bank was only a collecting agent that there was no consideration for the payment of cheques and he was not a holder in due course. The plaintiff had acted negligently and as such had no cause of action against the defendant.

The Trial Court and the High Court held that the plaintiff was entitled to enforce the liability against the defendant the maker of the cheques. The Supreme Court held that the plaintiff was a holder in due course for value consideration. He could validly maintain action against all the defendants. Under the Indian law a holder in due course must not only acquire the bill, note or cheque for valid consideration but should have acquired the cheque without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title. This condition requires that he should act in good faith and with reasonable caution. However mere failure to prove in good faith or absence or negligence on his part would not negate his claim. In the present case the plaintiff bank provided

...that no indorser of an instrument be permitted to deny the signature to contract of any prior party to the instrument.

## LIABILITY OF PARTIES TO NEGOTIABLE INSTRUMENTS

(Secs. 30 to 32, and 35 to 42)

- 1. Liability of Drawer :** According to Section 30 the drawer of a bill or cheque is bound in case of dishonour by the acceptor or drawee thereof to compensate the holder, provided due notice of dishonour has been given to, or received by, the drawer.
- 2. Liability of drawee of a cheque :** Section 32 lays down that the drawee of a cheque having sufficient funds of the drawer in his hands properly applicable to the payment of such cheque must pay the cheque when duly presented and in default of such payment, must compensate the drawer for any loss or damage caused by such fault.  
This liability of the drawee is towards the drawer only. A holder of a cheque has no right to any compensation for any damage suffered by him.
- 3. Liability of maker of note and acceptor of a bill :** Section 32 lays down that in the absence of a contract to the contrary the maker of a note and the acceptor of a bill are bound to make the payment due on the instrument. In the absence of a contract to the contrary, the maker of a promissory note and the acceptor before maturity of a bill of exchange are bound to pay the amount thereof at maturity according to the apparent tenor of the note or acceptance respectively and the acceptor of a bill of exchange at or after maturity is bound to pay the amount thereof to the holder on demand.  
In default of such payment as aforesaid, such maker or acceptor is bound to compensate any party to the note or bill for any loss or damage sustained by him and caused by such default.
- 4. Liability of indorser :** Section 35 lays down that in the absence of a contract to the contrary every indorser of a negotiable instrument before maturity is liable to every subsequent holder in case of dishonour of the instrument, provided due notice of dishonour has been given to or received by, such indorser, Every indorser, after dishonour is liable as if the instrument is payable on demand.
- 5. Liability of prior parties :** Section 36 lays that all prior parties to a negotiable instrument are liable thereon to a holder in due course until the instrument is duly satisfied.
- 6. Liability of maker, drawer, and acceptor as principal :** Section 37 says that maker of a note or a cheque, the drawer of a bill of exchange until acceptance, and the acceptor, after acceptance, in the absence of a contract to the contrary, are respectively liable on the instrument as principal debtors.

**7. Liability of other parties as surety** : Section 37 further provides that the other parties thereto are liable thereon as sureties for the maker drawer or acceptor, as the case may be.

**8. Liability of prior party in respect of each subsequent party.** Section 38 lays down that each of the above such surety is, in the absence of a contract to the contrary, also liable as a principal debtor in respect of each subsequent party.

*Example.* A draws a bill payable to his own order on B. A later on indorses the bill to C, C to D and D to E. As between E and B, B is the principal debtor, and A, C and D are his sureties. As between A and C, C is the principal debtor and D is his surety.

**9. Liability of agent.** According to Section 28 an agent who signs or indorses a negotiable instrument, without clearly signifying on it, that he is signing merely as an agent, will be personally liable on the instrument.

An agent who signs his name to a agent promissory note, bill of exchange or cheque without indicating thereon that he signs as agent, or that he does not intend thereby incur personal responsibility, is liable personally on the instrument, except to those who induced him to sign upon the belief that the principal only would be held liable.

**10. Liability of legal representative** : Liability of the legal representative who signs a negotiable instrument is unlimited. However, he may, by express agreement, limit his liability. A legal representative of a deceased person who signs his name to a promissory note, bill of exchange or cheque is liable personally thereon unless he expressly limits his liability to the extent of the assets received by him as such.

**11. Liability in case of contract of suretyship** : According to Section 39 of the Act if the holder of an accepted bill of exchange enters into any contract with the acceptor, which under Sec. 134 or 135 of the Indian Contract Act, 1872, would discharge the other parties, the holder may expressly reserve his right to charge the other parties and in such case they are not discharged.

**12. Liability of acceptor when indorsement is forged** : Section 41 lays down that acceptor of a bill of exchange already indorsed is not relieved from his liability by reason, that such indorsement is forged if he knew or had reason to believe the indorsement to be forged when he accepted the bill.

**13. Liability for acceptance of bill drawn in fictitious name** : An acceptor cannot escape his liability on a fictitious bill. An acceptor of a bill of exchange drawn in a fictitious name and payable to the drawer's order is not by reason that such name is fictitious, relieved from liability to any holder in due course claiming under an indorsement by the same hand as the drawer's signature, and purporting to be made by the drawer.

**14. Liability for instrument made etc. without consideration** : According to Section 43 a holder in due course is not affected by the absence of consideration on the part of the prior parties. As such he can hold the transferer liable on the instrument.

## Negotiation

Easy transferability is one of the important characteristics of an instrument, A negotiable instrument may be transferred : 1 . by assignment, or 2. by negotiation.

**1. Transfer by assignment.** Assignment means transfer of ownership by a written document under the provisions of the Transfer of Property law:

**Case Law.** X executed a promissory note in favour of Y. Y sold this note by assignment under a sale deed to Z.Z. sued X to recover the amount. X contended that since Z was not a holder in due course, no suit was maintainable. It was held, although Z was not a holder in due course, yet he is a holder within the meaning of Section 8 of the negotiable instrument Act, 1881 as he is in possession of the note and as an assignee entitled to recover the amount in his own name. An instrument can be transferred by assignment. But a transferee acquires only those rights which the transferor had at the time of assignment and no more. [Narsingh Panda v. A. Narsunha Murthy , (1966)Orissa 194].

**2. Transfer by negotiation.** In the view of section 4, if an instrument is transferred to any person, so as to make that person holder of the instrument, the instrument is said to be negotiated.

**Mode of negotiation or how negotiation is effected ?**

(i) **Negotiation by delivery** (Sec. 47). The transfer of a negotiable instrument payable to bearer can be effected by mere delivery. Subject to the provisions of Section 58, a promissory note, bill of exchange or cheque payable to bearer is negotiable by delivery thereof.

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.

(a) X the holder of a negotiable instrument payable to bearer, delivers it to Y's agent to keep for Y. The instrument has been negotiated.

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

(ii) **Negotiation by endorsements and delivery** (Sec. 48). A negotiable instrument, payable to order, is negotiable by the holder, by and delivery thereof.

**Example :** A holds a cheque payable to order. A signs on the back of the cheque and writes 'Pay B'. Thereafter A delivers the cheque to B. It is negotiation by endorsement and delivery.

The term 'delivery' is very significant in negotiation. Delivery means actual or constructive delivery with an intention of transferring property in the negotiable instrument. If the instrument is executed but is not delivered, there is no negotiation.

Example : (a) A person executed a promissory note but died before delivering it to the payee. The promissory note was found in his papers and it was delivered to the indorsee. There is no negotiation and payee cannot recover the amount.  
 (b) If an instrument payable to bearer was accidentally lost and picked up by a passer by. A. The passer by did not acquire any title. However, if he transfer it say to Mr. B who takes it for value and in good faith he (B) will acquire a good title to the instrument.

**Kinds of Delivery**

Delivery may be of following types for special purpose.

1. **Actual delivery.** It means physical transfer.
2. **Constructive delivery.** Constructive delivery means delivery in effect. It may happen when the instrument is held by one party as an agent for both the parties.  
**Example :** Both X and Y have their accounts in C Bank. X the holder of a negotiable instrument payable to bearer, directs the banker to transfer the instrument to Y's credit in Y's account with the bank. The banker does so and accordingly now Bank possesses the instrument as Y's agent. In this case there is a constructive delivery.
3. **Conditional delivery. It is delivery for a special purpose.** It is common to deliver instrument conditionally or for a special purpose. If condition is not fulfilled, the transferee will not receive any title.

**Example :** X the holder of a bearer negotiable instrument gave it to a bank for collection. The bank negotiated it by delivery to Y. Y will not acquire any title. However, if Y transfers the instrument to Z, a holder in due course, Z will acquire a good title.

**Distinction between Negotiation and Assignment**

S. No.	Basis	Negotiation	Assignment
1.	<b>Act</b>	It is effected under the Negotiable Instruments Act.	It is effected under the Transfer of Property Act.
2.	<b>Formality</b>	No formality is necessary, as such it can be effected by delivery or by indorsement and delivery.	It must be in writing under the provisions of the Transfer of Property law.
3.	<b>Notice</b>	No notice of negotiation by the transferor to the debtor is required.	Notice of assignment to the debtor must be given to make assignment effective.
4.	<b>Defect of title</b>	The transferee is not affected by the defect of title of the transferor.	The transferee is affected by the defect of title of the transferor, as such transferee will not get a better title than that of the transferor.
5.	<b>Consideration</b>	Consideration is presumed in case of negotiation.	Consideration is not presumed but has to be proved in case of assignment.

Presentment means presenting or showing a negotiable instrument to the drawee, maker or acceptor. This presentment may be (i) for acceptance, (ii) for sight (iii) for payment.

**(i) Presentment for acceptance.** Only certain types of bills of exchange require presentment for acceptance. The following bills must be presented for acceptance :

- (a) A bill payable after sight or after presentment, must be presented for acceptance.
- (b) A bill in which it has been expressly stipulated that it shall be presented for acceptance before payment.

A bill payable on demand, or on a fixed day, or a certain number of days after date need not be presented for acceptance. If presentment for acceptance is optional it is advisable to present the bill for acceptance so as to get the benefit of additional security of drawee's name and immediate cause of action against the drawee for dishonour by non-acceptance.

#### **Rules of valid acceptance are :**

**1. Acceptance must be given on the bill.** The acceptance must be given on the bill. In case the bill is drawn in sets, only one of the copies should be accepted. If the acceptor signs on all the parts, he will be liable to holder in due course as if each part were a separate bill.

**2. Acceptance must be signed by the drawee or by his agent.** Signing on the bill by the drawee, or his duly authorised agent, is essential. The word "accepted" may or may not be used but signature must be there.

**3. Acceptance must be completed by delivering the instrument :** Acceptance is complete only when the accepted bill is delivered to the holder

**4. Presentment must be made in time.** Presentment for acceptance must be made at a reasonable time on a business day and before maturity.

Bill must be presented for acceptance before maturity. Where a period for a presentment is specified, it must be presented within that period. Where no period is specified and the presentment is obligatory, it must be made within a reasonable time.

Further, the presentment must be made on a business day and within business hours.

Regarding place of presentment, a bill should be presented at the place of business and where drawee has no place of business, at his residence. Where the bill is presented at the residence, it must be at the reasonable hour.

**5. Not more than 48 hours should be given to accept the bill.** Not more than 48 hours should be allowed to the drawee to consider whether or not he will accept the bill.

#### **To whom presentment for acceptance be made ?**

Obviously, to the drawee. However, presentment for acceptance may be made to the following :

1. To drawee or his duly authorised agent.



2. To his legal representative, if the drawee, before acceptance, has died.
3. To his Official Receiver or Assignee if the drawee, before, acceptance, has been declared an insolvent (Section. 75).
4. To drawee in case of need (Section 33)
5. To acceptor for honour (Section 108)
6. To all the drawees, in case there are more drawees and they are not partners. In case they are partners, to any of the drawees (Section. 34).

### **Time and place of presentment for acceptance**

**Time of presentment.** If any time has been prescribed, it must be presented within that time otherwise within a reasonable time. Where presentment is not obligatory it should be done as soon as possible, but in any case, before maturity.

According to Section 65. The presentment for payment must be made during the usual hours of business, and if at a banker's, during banking hours. However, if presentment is made at an unreasonable hour but the payment is refused on some other ground, the instrument is deemed to be duly presented for payment.

According to Section 66 a note or bill made payable at a specific period after date or sight thereof, must be presented for payment at maturity. An earlier presentment is ineffective.

According to Section 74 a negotiable Instrument payable on demand must be presented for payment within a reasonable time after receipt by the holder.

Where a note is made payable by installments, it must be presented for payment on the third day after the date for payment of each instalment, and non-payment on such presentation will have the same effect as non-payment of a note at maturity.

**Place of presentment.** (Section 68, 69, 70 and 71) In case place of presentment is specified, it should be presented at that place, otherwise at the drawee's place of business or residence.

Where a negotiable instrument is made payable at a specified place and not elsewhere, it must be presented for payment at that place in order to make any party liable thereon (Sections 68 and 69). **If no place is specified**, it must be presented for payment at the place of business, if any, or at the usual residence of maker drawee or acceptor, (Section 70). Where the acceptor or maker has no known place of business or fixed residence and no place is specified in the instrument, the presentment may be made to him wherever found (Section 71).

**Consequences or effect of non-presentment :** If presentation for acceptance is compulsory and the holder fails to present the bill for acceptance, the drawee and all the indorsers are discharged from the liability to the holder.

### **Presentment for acceptance when not necessary or excused**

In the following cases presentment for acceptance is not essential.

1. If the drawee is a fictitious person.
2. If the drawee is incapable of entering into contract.
3. If although the presentment is irregular, yet acceptance has been refused.
4. When the drawee is dead or has been declared insolvent, the bill may be presented for acceptance to the legal representative or the Official Receiver or Assignee, as the case may be.

In case of death or insolvency of the drawee. When the bill is not presented to the legal representative or Official Receiver or Assignee, the drawer and other indorsers are not discharged from their liability to the holder.

to pay the amount due on the instrument.

## NOTING

Noting (Section 39) is the recording of the fact of dishonour by a Notary Public upon the negotiable instrument. Thus, it is an authentic proof of dishonour of a note or bill.

Section 99 provides that if a promissory note or bill of exchange has been dishonoured by non-acceptance or non-payment, the holder may cause such dishonour to be noted by a notary public upon the instrument, or upon a paper attached thereto, or partly upon each.

Such note must be made within a reasonable time after dishonour, and must specify the date of dishonour, the reason, if any, assigned for such dishonour, or, if the instrument has not been expressly dishonoured, the reason why the holder treats it as dishonoured, and the notary's charges.

## PROTEST

After a note or bill has been noted for dishonour by a Notary Public, it may be got certified by the Notary Public. Such certificate is called a protest. The protest is the formal certificate given by the Notary Public. This certificate is based upon the above noting.

According to Section 100, when a promissory note or bill of exchange has been dishonoured by non acceptance or non payment, the holder may, within a reasonable time, cause such dishonour to be noted and certified by a notary public. Such certificate is called a protest.

**Protest for better security.** If the acceptor of a bill of exchange has become insolvent or his credit has been publically impeached, before the maturity of the bill the holder may within a reasonable time, cause a notary public to demand better security of the acceptor and on its being refused may, with a reasonable time, cause such facts to be noted and certified as aforesaid. Such certificate is called a protest for better security.

**Contents of protest**-(Section 101). A protest under section 100 must contain the following

- (i) either the instrument itself, or a literal transcript of the instrument and of everything written or printed thereupon;
- (ii) the name of the person for whom and against whom the instrument has been protested;
- (iii) a statement that payment or acceptance, or better security has been demanded of such person by the notary public; the terms of his answer, if any, or a statement that he gave no answer, or that he could not be found;

- (iv) when the note or bill has been dishonoured, the place and time of dishonour, and, when better security has been refused, the place and time of refusal;
- (v) the subscription of the notary public making the protest;
- (vi) in the event of an acceptance for honour or of a payment for honour, the name of the person by whom, of the person for whom, and the manner in which, such acceptance or payment was offered and effected.

A notary public may make the demand mentioned in clause (iii) in person or by his clerk or, where authorised by agreement or usage, by registered letter.

**Notice of protest.** According to Section 102. When a promissory note or bill of exchange is required by law to be protested, notice of such protest must be given, instead of notice of dishonour, in the same manner and subject to the same conditions. The notice may be given by the Notary Public who makes the protest.

**Protest of foreign bills.** According to Section 109. Foreign bills of exchange must be protested for honour when such protest is required by the law of the place where they were drawn.

#### **Right as to compensation (Section 117)**

If a negotiable instrument is dishonoured, the holder or payee is entitled to receive compensation from the person liable to pay.

The rules regarding compensation are as follows :

1. The holder is entitled to the amount due upon the instrument and the expenses properly incurred in presenting, noting and protesting it.
2. If the person charged lives at a place different from that at which the instrument was payable, the holder is entitled to receive such sum at the current rate of exchange between the two places.
3. An indorser, who being liable, after paying the amount, is entitled to the amount so paid with 18% interest p.a. from the date of payment until tender or realisation thereof together, with all expenses caused by the dishonour and non-payment."
4. If the person charged and such indorser reside at different places, the indorser is entitled to receive such sum at the current rate of exchange between the two places.
5. If bill is dishonoured, it is a usual practice to re-draw a bill for the amount due together with expenses properly incurred on noting and protesting, etc. The second bill must be accompanied by the instrument dishonoured and protested. If the second bill is also dishonoured, the compensation in the same manner, as in the case of original bill, can be claimed.

Exercise

The term discharge in relation to negotiable instruments has two connotations (1) discharge of the instrument, and (2) discharge of one or more parties.

**1. Discharge of the instrument.** A negotiable instrument is discharged when all the rights under it are extinguished so that the instrument ceases to be negotiable. For example, if the party primarily liable on the negotiable instrument is discharged, the negotiable instrument is also discharged. After instrument is discharged all the parties are also discharged from their liability. Holder in due course cannot claim the amount of the instrument from any party to the instrument.

**Discharge of one or more parties.** A party is said to be discharged from his liability when his liability on the instrument comes to an end. If only some of the parties to a negotiable instrument are discharged, the instrument continues to be negotiable and the undischarged parties remain liable on it. The discharge of one or more parties to an instrument does not discharge the instrument and the rights under it can still be enforced against those parties who continue to be liable thereon.

The term 'discharge of instrument' is wider than the term 'discharge of party(ies)'. If an instrument is discharged, all the parties to the instrument are also discharged automatically. However, discharge of one or more parties does not necessarily discharge the instrument.

#### Discharge of the instrument

An instrument is discharged in the following ways :

1. **By payment in due course** [Section 10 and 82(c)]. This is the most natural and usual mode of discharge of an instrument. All parties to an instrument are discharged by payment made in due course.

**Essential rules regarding payment :** These as given below

(1) The payment should be made by the party primarily liable. When the payment is made by any indorser, the instrument will not be discharged; only that indorser and subsequent parties will be discharged.

(2) The payment of the instrument should be made at or after maturity. When the payment is made before maturity, it will not discharge the instrument unless the instrument is cancelled. If it is not cancelled it is likely to reach again in the hands of a holder in due course who can enforce payment [*Burbridge v. Manners* (1812) 3 Camp. 193. 1951.

(3) Section 78 provides that Payment should be made to the holder otherwise it will not discharge the party liable to pay. In the case the instrument is payable to bearer, the payment may be made to any person in possession of the instrument unless there is a suspicion to show that he is not entitled to payment. In that case payment even to thief or finder will

discharge the instrument. Where the instrument is payable to order, the payment should be made to the payee named.

**Example.** A bill was drawn payable to S.N. Another S.N. picked up the bill and got the payment. The acceptor in not discharged. The true S.N. can still recover the amount from the acceptor

However, in case of a cheque, special protection has been granted by Section 85(1) : "Where a cheque payable to order purports to be indorsed by or on behalf of the payee, the drawee is discharged by payment in due course".

**2. Discharge by cancellation** [Sec. 82(a)]. If the holder of an instrument with the intention of discharging the instrument cancels the name of the party primarily liable the instrument is discharged. A negotiable instrument is also discharged if the holder cancels the instrument itself with an intention of discharging all the parties to the instrument. He may cancel the negotiable instrument by scoring it out or tearing it off.

**Example.** X drew a bill for Rs. 2000 on Y. indorsed the bill to Z, Z, to D and D to E, E, the holder of the bill, cancels the name of the drawer X Now Y, Z and D are also discharged as their liability is dependent upon the liability of the drawer X.

It should be noted that cancellation should be intentional. An accidental cancellation will not discharge the instrument. To discharge the instrument, the name of the party primarily liable should be cancelled. When the name of a party who is secondarily liable is cancelled, the instrument will not be discharged; only the subsequent parties will be discharged in that case. The instrument should be destroyed physically so that it may not be used again.

### Case Laws :

X accepted a bill and gave it to Y for getting it discounted. Y failed to 'discount the bill and returned the bill to X, X tore the bill in half with the intention of cancelling it and threw the pieces on the road. Y picked up the pieces and pasted them together so nicely that it appeared to have been folded for safe custody rather than cancelled. Y passed it so that it reached a holder in due course. The court held that X was liable on the bill. [*Ingham v. Primerose* (1897) TCB (NS) :

### 3. By acceptor of a bill becoming its holder (Section 90)

When a bill of exchange which has been negotiated is, at or after maturity, held by the acceptor in his own right, the instrument is discharged.

**4. By release** [Section 82(b)] If the holder of the instrument releases the party primarily liable on the instrument or otherwise discharges him, the instrument is also discharged.

### Discharge of one or more parties to an instrument

**1. By cancellation** [Section. 82(a)] If the holder of an instrument deliberately cancels the name of any of the party (by drawing a line through the name of liable on the instrument with an intent to discharge him from liability thereon, such party and all indorsers subsequent to him, who have a right of action against the party whose name is so cancelled, are discharged from liability. When maker's or acceptor's name has been cancelled the liability of other parties to the instrument, who must have become parties thereto subsequent to the maker and as such must be in the position of sureties to him, comes to an end, which in effect discharges or cancels the instrument itself. But when the name of an indorser has been cancelled then all the indorsers subsequent to him will be discharged but those prior to him will remain liable. Where the cancellation is done under a mistake, or without the authority of the holder it would be inoperative and can not discharge any party.

**2. By release** [Section. 82(b)]. If the instrument releases the party primarily liable on the instrument or otherwise discharges him. The instrument is also discharged.

**3. By payment** [Section. 82(c)]. When the party primarily liable on the instrument makes the payment, the instrument as well as all the parties to the instrument are discharged.

**4. Discharge by allowing more than 48 hours to the drawee to accept the bill** [Section 83] If the holder of bill of exchange allows more than 48 hours to the drawee to consider whether or not he will accept the bill, all previous parties not consenting to such allowance, are discharged from their liability to such holder.

**5. Discharge by delay in presenting cheques** [Section 48]. A cheque must be presented for payment within a reasonable time. Where a cheque is not presented for payment within a reasonable time and the drawer suffers actual damage through the delay, he is to that extent discharged from his liability.

**Example.** X issued a cheque for Rs 5000 to Y. When the cheque should have been presented, there was enough balance in his account. But the cheque is delayed beyond reasonable time and the bank fails in the meantime. X is discharged from his liability. However Y can claim Rs. 5000 from the liquidator of the bank.

In this example if before X could present the cheque in the ordinary course, the bank fails X will not be discharged because X has not suffered any loss due to the presentment of the cheque which was in time.

**6. Discharge by qualified acceptance.** [Section 86]. A holder is entitled to object to a qualified acceptance. However, where he does not object to such qualified acceptance, all other parties who do not consent to such qualified acceptance are discharged to such holder and those claiming under him unless, on notice given by the holder, they agree to such acceptance.

**7. Discharge by material alteration** [Section 87]. Any material alteration of a negotiable instrument renders the same void as against any one who is party thereto at the time of making alteration. However, when the party consents to such alteration or it was made to carry out the common intention of the parties, the alteration does not discharge the original party.

Any alteration made by the indorsee, discharges his indorser from all liability to him. However, an acceptor or indorser is bound by his acceptance of indorsement if the alteration was before he accepted or indorsed the instrument.

An alteration is void only if it is made subsequent to acceptance or indorsement.

**8. Discharge by payment of instrument on which alteration is not apparent.** [Section 89]. When an instrument has been materially altered but does not look like that or where cheque has been crossed but does not appear to have been crossed, e.g., crossing clearly erased, the person paying or the banker is discharged from all liabilities thereon.

Section 89 (1) lays down that where a promissory note, bill of exchange or cheque has been materially altered but does not appear to have been so altered, or where a cheque is presented for payment which does not at the time of presentation appear to be crossed or to have had a crossing which has been obliterated, payment thereof by a person or banker liable to pay, and paying the same according to the apparent tenor thereof at the time of payment shall discharge such person or banker from all liability thereon; and such payment shall not be questioned by reason of the instrument having been altered, or the cheque crossed.