

## 4. NEGOTIABLE INSTRUMENTS ACT, 1881

### PART WISE ANALYSIS OF PREVIOUS EXAMINATIONS

PART	M17	N17	M18 (O)	M18 (N)	N18 (O)	N18 (N)	M19 (O)	M19 (N)	N19 (O)	N19 (N)	N 20(O)	N 20(N)
PART I	-	-	-	-	-	-	-	-	-	-	-	-
PART II	-	-	-	-	-	-	-	-	-	-	-	-
PART III	-	-	-	5	-	-	-	-	-	-	2	-
PART IV	-	-	-	-	-	-	-	-	4	-	-	-
PART V	-	-	-	-	-	-	-	-	-	-	-	-
PART VI	-	-	4	-	-	-	-	-	-	-	-	-
PART VII	-	-	-	-	-	-	-	-	-	-	-	-
PART-VIII	-	-	-	-	-	-	-	-	-	-	-	-
PART IX	-	-	-	-	-	-	-	-	-	-	-	-
PART X	-	-	-	-	-	-	-	2	-	4	-	-
PART XI	4	-	-	4	-	5	-	3	-	-	-	-
PART XII	-	-	-	-	-	-	-	-	-	-	-	-

**NOTE:** YOU CAN EXPECT TO GET ATLEAST 12 MARKS IN THE ICAI EXAM FROM THIS CHAPTER. THERE ARE MORE CHANCES OF GETTING A PRACTICAL QUESTION RATHER THAN THEORY QUESTION.

### CHAPTER OVERVIEW

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### SECTION 1: THEORY FOR CLASSROOM DISCUSSION

## PART 1 - INTRODUCTION

### INTRODUCTION TO NI ACT:

- 1) In India, the Law relating to negotiable instruments is contained in the Negotiable Instruments Act, 1881.
- 2) This Act is enacted (i.e., passed) to facilitate the activities in trade and commerce.
- 3) The Act contains provisions for giving sanctity (i.e., more importance) to the instruments of credit.
- 4) Such instruments of credit can be convertible into money and easily transferrable from one person to another.
- 5) The source of Indian law relating to negotiable instruments is admittedly the English Common Law.
- 6) This is an Act to define and amend the law relating to Promissory Notes, Bills of Exchange and Cheques.

- 7) NI Act was enacted on 09/12/1881 and it came into force from 01/03/1882.
- 8) The Act applies to the whole of India<sup>1</sup> (Including the state of Jammu & Kashmir). Nothing contained in the Act affects:
- a) RBI Act, 1934, (Section 21 of the RBI ACT provides that Banks have the right to transact Government business in India), or
  - b) Any local usage relating to any instrument in an oriental language.
- EXCEPTION:** Such usage of trade may be excluded by any words in the body of the instrument, which indicate an intention that the legal relations of the parties thereto shall be governed by this Act.
- 9) The provisions of this Act are also applicable to Hundis (a form of bill of exchange used in olden days).

**Q.No.1. Define the term Negotiable instrument? State the characteristics of Negotiable Instruments? (D) [NEW SM, OLD SM, OLD PM]**

- 1) The Act does not define the term 'Negotiable Instruments'. However, Section 13 of the Act provides for only three kinds of negotiable instruments namely, Bills of exchange, Promissory notes and Cheques, payable either to order or bearer.
- 2) **MEANING:** Negotiable Instrument is an instrument<sup>2</sup> which is freely transferable from one person to another person by:
  - a) Mere delivery in case of bearer instruments and
  - b) Endorsement and delivery in case of order instruments.
- 3) **CHARACTERISTICS OF A NEGOTIABLE INSTRUMENT**
  - a) It should be in writing.
  - b) It should be signed.
  - c) It is freely transferable from one person to another.
  - d) Holder in Due Course title is free from defects.
  - e) It can be transferred any number of times to its satisfaction. (i.e. transferable infinitum)
  - f) Every negotiable instrument must contain the following:
    - i) A promise to pay money - In case of Promissory Note.
    - ii) Order to pay money - In case of Bill.
    - iii) Such Promise or Order shall be unconditional.
  - g) The above promise, or, order to pay, must be in terms of money only (i.e., monetary form only).
  - h) The holder of a negotiable instrument can sue on the instrument in his own name.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. Transferee who takes the instrument for value and in good faith will get a good title even though there is any defect in the title of any of the prior parties.
2. If an order or promise is made in Non - monetary form, then such instrument is invalid. Also, the money payable must be certain (clear and specified).
3. A negotiable instrument may be made payable to two or more payees jointly. It may be made payable in the alternative to one of two, or one or some of several payees.

**NOTE:** Dear students, each of the technical words, being used in this answer, will be discussed in a detailed manner in further questions. Don't expect faculty to explain each and every point here itself. It is not possible to teach everything in this question itself. Don't panic even if you don't understand any of the points discussed in this question, as you will get detailed discussion in further questions.

1) Prior to 1956, NI Act was not applicable to the state of Jammu and Kashmir. However, the state of Jammu and Kashmir has been covered under the scope of NI act by Jammu and Kashmir (Extension of Laws) Act, 1956.

2) The word instrument means a document in writing.

**Q.No.2. "NI Act has recognized only 3 instruments as negotiable". What is the legal status of other instruments that are not covered under the NI Act 1881 but still being negotiated in day to day business? (Or) What is the additional advantage being enjoyed by the 3 instruments that have been recognized by NI Act? (D) [Out of SM]**

1) NI Act does not define the term 'Negotiable Instrument'. However, Section 13 of the Act provides for only three kinds of negotiable instruments namely,

- a) Bills of exchange,
- b) Promissory notes and
- c) Cheques, payable either to order or bearer.

But it does not mean that there can be no other negotiable instruments other those enumerated in the Act.

2) **NI ACT DOES NOT APPLY TO:**

- a) Indian Paper Currency Act, 1871
- b) The local usage relating to any instrument in a vernacular language (For example, Hundies). But where no such custom is established, the Act will apply to Hundies also.

3) Instruments like Share warrant, Dividend Warrant, Bearer Debentures, Dock warrants, Railway Receipt, Bill of Lading, Government promissory notes, delivery orders, etc. are not recognized as negotiable instruments under the provisions of the NI Act.

But these instruments are freely negotiated either as per the prevailing Customs of Trade or as per the provisions of some other Acts.

4) Even though such instruments are not recognized under the NI Act, they are still negotiable and the general principles of Indian Contract Act may apply to such instruments.

The instruments covered under the NI Act will get a protection that the transferee gets a good title to the instrument, even though the title of the transferor is defective, provided he takes the instrument in good faith and for consideration. Such protection is not available to other instruments which are not covered under this Act.

## PART 2 - NEGOTIABLE INSTRUMENTS & ITS TYPES

**Q.No.3. What is a promissory note? Who are the parties to a promissory note?**

**(D) [NEW SM, OLD SM, M12 - 8M]**

1) **DEFINITION [Sec 4]:** A Promissory note is:

- a) An instrument in writing (*not being a bank note or currency note*)
- b) Containing an unconditional undertaking
- c) Signed by the Maker,
- d) To pay a certain sum of money only
- e) To a certain person, or to the order of a certain person, or to the bearer of the instrument.

2) **PARTIES TO A PROMISSORY NOTE:**

a) **MAKER:**

- i) The person who makes (*i.e. who prepares*) the promissory note and promises to pay money stated therein is called 'Maker' of the instrument. (*Nothing but Debtor*)
- ii) He must sign the instrument.
- iii) Maker's liability is primary and unconditional.

b) **PAYEE:** The person to whom the amount of promissory note is payable (*i.e. to whom the promise of payment is made*) is called payee of the instrument. (*Nothing but Creditor*)

**NOTE:**

1. Provisions of Negotiable Instruments Act, 1881 which are applicable to Promissory Note shall not apply to Bank Note, Currency Note.
2. "or to the bearer of the instrument" - **You will know meaning of these words in next question.**

**Q.No.4. State the essential elements or characteristics or distinguishing features of a valid Promissory Note?**  
(D) [NEW SM, OLD SM, OLD PM, RTP - M13]

**PROMISSORY NOTE:** First write the definition of Promissory Note.

**ESSENTIAL ELEMENTS OF A PROMISSORY NOTE:**

- 1) **Only in writing:** An oral promise to pay is not sufficient. It must be in writing<sup>3</sup>.
- 2) **"Promise to Pay":**
  - a) The instrument must contain an express promise to pay.
  - b) Mere acknowledgement of debt is not a Promissory Note.
- 3) **Signed by the Maker:** PN is valid only if it is signed by the maker otherwise it is incomplete and ineffective.
- 4) **Definite and unconditional:**
  - a) The Promise to pay must be definite and unconditional.
  - b) Therefore, instruments payable on performance or non-performance of a particular act or on the happening or non-happening of an event, are not promissory notes.
  - c) However, the promise to pay may be subject to a condition, which is bound to happen but exact time of happening is uncertain.<sup>4</sup>
- 5) **Promise to pay money:** PN can be issued in terms of money and money only<sup>5</sup>.
- 6) **Certainty in sum of money:**
  - a) The sum payable as indicated in the instrument must be certain or definite.
  - b) The amount payable must not be capable of additions or subtractions based on contingencies.
- 7) **Delivery:** Promissory note must be delivered to the Payee (or to any person on behalf of Payee).
- 8) **Certain Parties:** The Maker and Payee must be certain, definite and different persons.
- 9) **Stamped:** PN must be properly stamped. Such stamp must be duly cancelled by maker's signature/s or initial/s or otherwise.

**NOTE:** You will get more clarity on Bearer & Order Instruments in further questions.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. Dear students, for better understanding of this question faculty will briefly explain you the meaning of following technical terms:

- Endorsement
- Blank endorsement, Full endorsement
- Bearer instrument, order instrument

But you will get detailed discussion of these technical terms in further questions. So, don't expect faculty to explain the meaning of these terms in a detailed manner.

2. Refer Appendix 1 to see how a Promissory Note will look like.
3. The term 'Promissory Note' denotes a note containing 'certain promise'.
4. **Certain amount:** If rate of interest is specified, the sum shall be deemed to be certain. But, expressions like 'market rate of interest' don't make the amount certain since market rate may vary with the source of borrowing, purpose of borrowing, financials standing of the borrowing, and so on.

3) Writing includes Printing and Typewriting.

4) E.g. Instrument payable on the death of a person.

5) The order to pay anything in kind will invalidate the Negotiable instruments.



However, an instrument containing an undertaking to pay the amount 2% above the bank rate shall be valid. It is because there is one bank rate at the given point of time.

5. It is not compulsory to use the word 'Promise'. Whatever the language is used, it must clearly show that the maker is unconditionally bound to pay the sum.
6. The signatures can be made on any part of the instrument. But is generally signed by the Maker on the right bottom corner, on the face (front side) of the instrument.
7. If PN is not signed by the maker, it is invalid.
8. Certainty of sum of money is compulsory: However, in the following cases the sum of money payable is deemed to be certain and hence considered as valid Promissory Notes:
  - Where it is payable along with interest and interest is expressed as an amount or as a percentage.
  - Where it is payable in foreign currency at the prevailing rate of exchange on the date of Payment.
  - Where it is payable by installments with a provision that on default the unpaid balance shall become due.
9. Demand instrument or Time instrument: A promissory note can be made payable on demand (demand instrument) or after a definite period of time (Time instrument). *You will get to know more about these words, in further questions.*
10. Even though the words 'or to the bearer of the instrument' are there in the definition of Promissory Note they have become inoperative due to the provisions of Sec. 31(2) of the RBI Act. It provides that no person in India other than RBI and CG can make or issue promissory note payable to the bearer of the instrument.
11. Hence a Promissory Note can be made payable only to a certain person or to the order of a certain person. But it can't be made payable to the bearer [Sec.31(2) of the RBI Act, 1934]

Of course, this restriction will apply at the time of making the promissory note. There is no restriction on making a blank endorsement of Promissory Note so as to make it Payable to Bearer. *(You can understand this point only after completion of the question "Different types of Endorsements" but not now).*

12. Parties to the Instrument: The name of the Payee must be specified in the promissory note, otherwise it is invalid u/s 31 of RBI act, 1935. (Generally, Payee name is mentioned along with reference like S/o, D/o, W/o or any other suitable reference)  
The instrument must point out as to who the "maker" is and who the "payee" is. The "maker" and "payee" need not be identified by their names and they may be sometimes identified by description.  
Thus, if a Promissory note is payable to a manager of a bank, it is valid.  
However, a promissory note cannot be made payable to the maker himself, unless he becomes the payee in ordinary course (Negotiation Back).
13. Stamp duty is to be paid as per the provisions of Indian Stamp Act, 1899.
14. In a promissory note, it is usual and proper to state, the place where it is made and the date on which it is made. However, their omission does not render an instrument invalid.

*For example, if an instrument is not dated, it is deemed to have been dated on the date of delivery.*

#### TEST YOUR KNOWLEDGE:

1. In a promissory note, the promise to pay must be conditional. [M16 - 1.5M]
- A. Incorrect.

Sec 4 of the NI Act, 1881 defines 'Promissory note' as an instrument in writing containing an unconditional undertaking, signed by the maker to pay money only to, or to the order of, a certain person, or to the bearer of the Instrument.

From the definition of promissory note it is clear that the undertaking must be unconditional. Hence, the given statement is wrong.

**(IMMEDIATELY REFER PRACTICAL QUESTION NO.1)**

**Q.No.5. What is meant by Bill of Exchange? Who are the parties to a Bill of Exchange?**

**(B) [NEW SM, OLD SM, M11 - 8M, N14 - 4M, MTP - N15]**

**DEFINITION [SEC 5]:** A Bill of exchange

- 1) An instrument in writing containing an unconditional order,
- 2) Signed by the Maker,
- 3) Directing a certain person,
- 4) To pay a certain sum of money only
- 5) To a certain person, or to the order of a certain person or to the bearer of the instrument.'

**PARTIES TO A BILL OF EXCHANGE:** A Bill of exchange is a Tri-party instrument.

- 1) **Drawer:** The party who draws the bill is known as Drawer. *He is the Maker of the Bill.*
- 2) **Drawee:**
  - a) The person who is directed by the Drawer to pay the Bill is called as Drawee.
  - b) In other words, he is the person on whom bill is drawn.
  - c) Upon acceptance of Bill by Drawee,
    - i) Drawee becomes Acceptor and is liable for payment of the bill.
    - ii) The liability of Drawee becomes primary and unconditional and
    - iii) The liability of Drawer becomes secondary and conditional.
- 3) **Payee:** The person named in the instrument, to whom or to whose order money is payable upon the instrument. Drawer himself can be Payee.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

- 1) Until the Bill is accepted the liability of Drawer is Primary.
- 2) **Acceptor:** An acceptor is the drawee who has signed his assent upon the bill<sup>6</sup> and delivered it to the holder.
- 3) In other words, Drawer can endorse the Bill even before its Acceptance. In such a case his liability will be Primary.
- 4) Refer Appendix 2 to see how a Bill of Exchange will look like.

**NOTE:** You will get more clarity on Bearer & Order Instruments in further questions.

**Q.No.6. State the essential elements or characteristics or distinguishing features of a Bill of Exchange? (D)** **[OLD SM, OLD PM]**

**DEFINITION:** First write what is a Bill of exchange.

**FOLLOWING ARE THE ESSENTIAL ELEMENTS OF A BILL OF EXCHANGE<sup>7</sup>:**

- 1) It must be in writing.
- 2) It must be signed by the Drawer.
- 3) It must contain an express order to pay<sup>8</sup>.
- 4) The order to pay must be definite and unconditional. (*A bill is drawn or made with conditions is invalid*)
- 5) The sum contained in the order must be certain.
- 6) The order must be to pay money and money only.
- 7) Drawer, Drawee and Payee must be certain.
- 8) It must be stamped as required by Indian Stamps Act, 1899.
- 9) Bill must be delivered to Payee, otherwise it is ineffective.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

- 1) Refer Appendix 1 to see how a Bill of exchange will look like.
- 2) We have not given detailed explanation to the above points as they are similar to that of Promissory Note.
- 3) Demand instrument or Time instrument: A Bill can be made payable on demand or after a definite period of time.

6) In case of bill in sets, assent may be made on any of such parts

7) We have not given these features in a detailed manner as they are very much similar to that of Promissory Note. You can make necessary changes and write the same content here.

8) Order does not mean a command. It is a direction for payment. Since this is a distinguishing feature of Bill as compared to Promissory Note, it is highlighted with grey background.

- 4) Note: In case of bill of exchange, Drawer, Drawee and Payee must be certain. They need not be identified by their names and they may be sometimes identified by description. (The Description may be about residential address or work place or designation etc. of drawer, drawee or payee).
- 5) A bill of exchange can't be made payable to the bearer on demand [Sec. 31(2) of the RBI Act, 1934].
- Of course, this restriction will apply only at the time of making the bill. There is no restriction on making a blank endorsement of the bill so as to make it Payable to Bearer.

You can understand this point only after completion of the question "Different types of Endorsements".

#### TEST YOUR KNOWLEDGE:

1. State, giving reasons, whether the given statements are 'correct or incorrect'
- "A bill of exchange may not be in writing". [M16 - 1.5M]
- A. Incorrect. Sec.5 of the NI Act, 1881 clearly defines that it is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay money only to, or to the order of, a certain person, or to the bearer of the Instrument.

(IMMEDIATELY REFER PRACTICAL QUESTION NO.2,3)

#### **Q.No.7. Essentials of valid acceptance of Bill of exchange (D)**

**[OLD SM, OLD PM]**

#### ACCEPTANCE:

- 1) Acceptance is required for Bill of Exchange only.
- 2) It is a process by which Drawee accepts the Drawer's Bill of exchange by signing on the face of the bill.

#### ESSENTIALS OF VALID ACCEPTANCE:

- 1) **Written:** It must be in writing and not oral.
- 2) **Signed:** It must be signed by the Drawee personally or through his duly authorised agent.
- 3) **On the bill:** It must be made on the bill i.e. either on the face or on the back side of the bill.
- 4) **Delivered:** Acceptance must be completed by delivery.

#### TYPES OF ACCEPTANCE (SEC. 86):

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

#### EFFECT OF QUALIFIED ACCEPTANCE (SEC. 86):

- 1) 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.
- 2) If Holder accepts a qualified acceptance without obtaining the consent of the prior parties thereto, then all the prior parties whose consent was not so obtained are discharged.

#### SOME INSTANCES OF QUALIFIED ACCEPTANCE:

- 1) **Qualified subject to condition:** E.g.: "accepted to pay when in funds" or "accepted to pay when the goods are verified and found in order".
- 2) **Qualified as to amount:** The bill is drawn for Rs. 10,000 but accepted for Rs. 4,000 only.
- 3) **Qualified as to place:**
  - The Drawee accepts to pay at a specified place, different from that of the place mentioned in the bill.
  - If place of payment is not specified in the bill then the Drawee agrees to make the payment at a specified place, and not otherwise or elsewhere.
- 4) **Qualified as to time:** The Bill was drawn to be payable, say 3 months after date but was accepted to pay 6 months after date.

**NOTE:** This concept is excluded in the New SM. But without this concept students can't understand further concepts. That is why we have decided to continue this question.

**TEST YOUR KNOWLEDGE:**

1. Referring to the provisions of the Negotiable Instruments Act, 1881, examine the validity of the following: [RTP - N17]  
A Bill of Exchange originally drawn by Mukesh for a sum of Rs. 10,000, but accepted by Deepa only for Rs. 7,000.
- A. As per the provisions of the Negotiable Instruments Act 1881, acceptance may be either general or qualified. It is qualified when the drawee does not accept the bill according to the apparent tenor of the bill but attaches some condition or qualification which have the effect of either reducing his (acceptor's) liability or acceptance of his liability is subject to certain condition. The holder of the bill is entitled to require an absolute and unconditional acceptance, otherwise he will treat it as dishonoured.  
However, he may agree to qualified acceptance, but he does so at his own peril, since he discharges all parties prior to himself, unless he has obtained their consent.  
Thus, in this given case in accordance with the Explanation to Section 86 of the Act, when the drawee undertakes the payment of part only of the sum ordered to be paid, it is a qualified acceptance and the drawer may treat it as dishonoured unless agreed by him. If the Drawer (Mukesh) agrees to acceptance, the drawee (Deepa) is responsible for a sum of Rs. 7000 only.
2. A accepts a bill payable at the Punjab National Bank, Chandni Chowk, and nowhere else.
  - a) Is it a valid acceptance?
  - b) Can the holder treat the bill as dishonoured if he does not accept this acceptance?
- A. a) No                                      b) Yes

**Q.No.8. What is meant by cheque? State the essential elements or characteristics or distinguishing features of a Cheque (C) [NEW SM, OLD PM, M11 - 8M, RTP - N13]**

**CHEQUE [SEC.6]:**

- 1) A "cheque" is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand<sup>9</sup> and
- 2) It includes the electronic image of a truncated cheque and a cheque in the electronic form.

**PARTIES TO A CHEQUE:**

- 1) **Drawer:** The person who draws a cheque is called Drawer. His liability is primary and conditional.
- 2) **Drawee:** The specific Bank on whom cheque is drawn is called as Drawee Bank or Drawee. He makes the payment of cheque. In case of Cheque, Drawee is always a Banker.  
*The expression "Banker" includes any person acting as a banker and including post office savings bank.*
- 3) **Payee:** The person named in the instrument, to whom or to whose order money is to be paid is called Payee. Payee may be the Drawer himself (Self Cheque) or a third party.

**ESSENTIALS OF A VALID CHEQUE:**

- 1) All the essential characteristics of a Bill of exchange will apply to Cheque also (*Students shall rewrite them in the exam*)
- 2) Cheque is always drawn on a specified banker.
- 3) Cheque is always payable on demand.

**Note:**

- These two additional features (i.e. point 2 & 3) will distinguish a Cheque from Bill. Thus, all cheques are Bills while all Bills are not Cheques.
- You will come to know the Electronic Cheque, Truncated Cheque, etc. in further questions.

**TEST YOUR KNOWLEDGE:**

1. "All Cheques are Bills of exchange, but all Bills of exchanges are not cheques". Explain [RTP - N13]
- A. Following are the similarities between a Cheque and a Bill of Exchange:
  - Both are Bills of Exchange.

9) In other words, it must be made payable on demand only. It can't be drafted in any other manner.

A bank draft is only a specie of bill of exchange drawn by one branch of a bank on other branch

- Both have three parties i.e. Drawer, Drawee and Payee.
- In some cases, Drawer and Payee can be one and the same person.
- Both must be written and signed
- Both must contain an unconditional order to pay a certain sum of money.
- Both may be endorsed.

Following are the differences between a Cheque and a Bill of Exchange:

- In case of cheque Drawee is always a Banker whereas in the case of Bill drawee can be any person.
- In case of Cheque grace days are not allowed but they are allowed for Bill.
- In the case of dishonour, notice of dishonour is not necessary for Cheque but it is usually required for Bill.
- A cheque can be drawn to Bearer and made payable on demand, whereas a bill cannot be drawn to bearer if it is made payable on demand.
- Stamping is not required for Cheques but required for Bill.
- A cheque may be crossed, whereas a bill cannot be crossed.

Conclusion: On account of similarities and the difference between the cheque and bill of exchange it can be concluded that "All cheques are bills of exchanges but all bills of exchanges are not cheques."

#### Q.No.9. Write about Bearer & Order Instruments

(A) [NEW SM, OLD SM]

##### 1) BEARER INSTRUMENT:<sup>10</sup>

- It is an instrument
  - Where name of the payee is blank (or)
  - Where name of the payee is specified with the words "or bearer" (or)
  - Where the last indorsement is blank.
- Such instrument can be negotiated by mere delivery.

##### 2) ORDER INSTRUMENT:

- A negotiable instrument is payable to order:
  - When it is expressed to be payable to a specified person (or)s to his order;<sup>11</sup> (E.g. 'Pay to order of A')
  - When it is payable to a specified person without addition of the words 'or his order' and does not contain words prohibiting or restricting its transfer. (E.g. 'Pay to A only Rs.100/-'.)
  - When the last endorsement is full endorsement.
- Such instrument can be negotiated by endorsement and delivery.
- In case of Order instruments, Payee must be indicated with reasonable certainty.

#### TEST YOUR KNOWLEDGE:

1) What are the different forms in which an order instrument can be created?

A. Refer Point 2 above.

#### Q.No.10. Write about Demand Instruments and Time Instruments? (or) Sight and Time Bill

(A) [OLD SM, RTP - M13]

##### 1) Demand Instrument<sup>12</sup> / Instruments payable on demand:

- A promissory note or bill of exchange is payable on demand -
  - When no time for payment is specified (or)
  - When it is expressed to be 'payable on demand' (or) 'at sight'<sup>13</sup> (or) 'on presentment'

10) i) 'Pay to R or bearer'; ii) 'A bill is drawn payable to X who endorses it in blank in favour of Y'.

11) When an instrument is made payable to the order of a specified person and not to him, it is payable to him at his option.

12) "Pay B Rs. 500 on Presentment"; ii) "I promise to pay Rs. 500 on demand"; iii) "I promise to pay B Rs. 500".

- b) A cheque is always payable on demand.
- c) A demand instrument may be presented for payment at any time. *Of course, it has to be presented within reasonable time.*
- d) A demand instrument is not entitled to any grace days.

## 2) Time Instruments:

- a) An instrument in which time for payment (i.e., maturity date) is specified is called Time Instrument
- b) A time instrument may be payable:
  - i) On a specified day (for e.g. "I promise to pay B Rs. 500 on 1<sup>st</sup> July, 2020") or
  - ii) After a fixed period (for e.g. "I promise to pay B Rs. 500 after 3 months") or
  - iii) After sight <sup>14</sup> (for e.g. "I promise to pay B Rs. 500 after sight") or
  - iv) On the happening of an event which is certain to happen (for e.g. "I promise to pay B Rs. 500 after C's death")

### TEST YOUR KNOWLEDGE:

- 1) Cheque is a time instrument. Comment. [RTP - M13]
- A. Incorrect. A time instrument mentions the time for payment. A cheque can never be a time instrument as it cannot be payable otherwise than on demand.

**(IMMEDIATELY REFER PRACTICAL QUESTION NO.4)**

**Q.No.11. Inland instruments & Foreign Instruments. State the liabilities of Parties in case of Foreign Instruments? (A) [NOV20(N),NEW SM, OLD SM]**

- 1) **INLAND INSTRUMENT:** A Negotiable Instrument is said to be an Inland instrument, if any one of the following conditions are satisfied -
  - a) Instrument drawn or made in India and made payable in India, (or)
  - b) Instrument drawn or made in India and drawn upon any person resident in India<sup>15</sup>.
- 2) **FOREIGN INSTRUMENT:** A negotiable instrument which is not an Inland instrument is called as Foreign Instrument.

### ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:

- 1) Thus, basic requirement is that the instrument should be made in India. Instrument made abroad is not Inland instrument. The maker may be Indian citizen or Foreign citizen. Another requirement is that either it should be made payable in India (or) drawn upon a person resident in India.
- 2) An Inland instrument remains inland even if it is endorsed in a foreign country<sup>16</sup>.
- 3) The instrument will be an inland instrument even if it is payable out of India if (a) it is made in India and (b) drawn upon a person resident in India.
- 4) Similarly, the instrument will be an inland instrument even if it is drawn upon a person resident out of India if (a) it is made in India and (b) it is payable in India.
- 5) Following are some foreign instruments:
  - Bills drawn outside India and made payable in or drawn upon any person resident in any country outside India,
  - Bills drawn outside India and made payable in India, or drawn upon any person resident in India;
  - Bills drawn in India made payable outside India or drawn upon any resident outside India, but not made payable in India.
- 6) Inland Bills are drawn in a single copy but foreign bills are drawn in triplicate.

13) In a promissory note or bill of exchange the expressions 'at sight' and 'on presentment' means on demand.

14) In case of Promissory Note, the expression "after sight" means, after specified number of days from the date of presentment for payment. In case of Bill, "after sight" means, after specified number of days from the date of acceptance, or from the date of noting for non-acceptance, or from the date of protest for non-acceptance as the case may be.

15) Ex 1: A bill drawn in Delhi on a merchant in Agra and accepted payable in London.

Ex 2: A bill drawn in Delhi on a merchant in London and accepted payable in Agra.

16) E.g. A bill was drawn in Delhi on a merchant in Agra and accepted payable in Agra. Later the bill was endorsed to a person living in London.

- 7) Liabilities of parties in case of Foreign Instruments (Sec.134): In the absence of a contract to the contrary,
- Liability of the maker (or) drawer of a foreign instrument (promissory note (or) bill of exchange (or) cheque) is regulated by the law of the place where he made the instrument, and
  - Liabilities of the acceptor and endorser is regulated by the law of the place where the instrument is made payable.

**TEST YOUR KNOWLEDGE:**

- How liabilities of parties are determined in case of foreign bills.
- A. Refer point-3 in above answer.

**(NOW REFER PRACTICAL QUESTION NO.5)****Q.No.12. Write about Fictitious bill.****(A) [NEW SM, OLD SM]****FICTITIOUS BILL (Sec.42):<sup>17</sup>**

- A fictitious bill is a bill in which the name of the Drawer or the Payee or both is fictitious.
- In a fictitious bill, the acceptor is liable to Holder in Due Course only.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

If a bill is drawn in the name of a fictitious person and payable to the Drawer's order then the acceptor is liable to pay to the order of the person who signed it as Drawer.

Acceptor cannot be relieved from his liability to the HDC. However, HDC shall establish that the bill was endorsed by the same person who has drawn such instrument.

*EX: i) A bill drawn upon X in favour of P and the drawer is a fictitious person; ii) X drawn a bill upon Y in favour of Z who is a fictitious person.*

**NOTE:** You will know more about Holder & Holder in Due Course in further questions.

**TEST YOUR KNOWLEDGE:**

- Mr. A draws a Bill on Mr. B in favour of Mr. C (who was not in existence). It is payable to Mr. C or his order. Bill was duly accepted by Mr. B. Discuss the validity of Instrument under the following situations:
  - If Bill was endorsed to Mr. Z for consideration, in Good Faith and before maturity.
  - If Bill was kept in the possession of Mr. A.
- In the given case, it is clear that the Drawer and Payee are fictitious persons. Thus, this Bill is a fictitious Bill. Generally, fictitious instrument is invalid. No person can take action using fictitious bill, except HDC.
  - Mr. Z is HDC, so he can recover the amount payable on the instrument from Mr. B. However, B is required to prove that the bill was endorsed by the same person who has drawn such instrument
  - Mr. A is neither holder nor HDC. So, he is not entitled to claim the amount represented by the instrument from Mr. B
- A gives a blank acceptance to one B who fills it up as a bill payable to the drawer's order and himself signs it as the drawer and the first indorser in a fictitious name 'J'. Is A or B liable to the holder of the bill?
- Both A and B are liable to the holder of the bill (sec.41 & 42). Moreover, the acceptance in the instant case is blank and as such the instrument becomes payable to the bearer. The right of the holder of the bill, therefore, will not be affected even if there is an indorsement in the name of fictitious person.

**Q.No.13. Conditional instrument / Escrow.****(D) [OLD SM]**

- An Escrow is a Negotiable Instrument which is delivered:
  - conditionally, (or)
  - for a special purpose as a collateral security, (or)
  - for safe custody only, and
  - not for the purpose of transferring the property therein, absolutely.

17) The word Fictitious means: (i) a non-existing person and (ii) a pretended person, i.e., a person other than the actual person intended by the parties  
In case of Bill, if DRAWEE is fictitious then it is considered as Ambiguous instrument. If Drawer or Payee is fictitious then it is considered as fictitious instrument.

- 2) If a Bill or a Note is negotiated to HDC, the other parties to the bill or note cannot avoid liability on the ground that the delivery of the instrument was conditional or for a special purpose only<sup>18</sup>.

**NOTE:** You will know more about Holder & Holder in Due Course in further questions.

**TEST YOUR KNOWLEDGE:**

1. A company issued a cheque on its bankers. A receipt was appended to the cheque and it ordered the banker to make the payment "provided the receipt form at foot hereof is duly signed, stamped and dated," Is the cheque valid?
  - A. No, because the payment is made conditional upon signing of the receipt.
2. Mr. A entered into a contract with Mr. B to construct a House. Mr. A gave a Promissory Note for Rs.5,00,000 to Mr. B as collateral security i.e. in case of breach of contract by Mr. A, Mr. B can encash that instrument. Discuss the position in the following cases:
  - a) Can Mr. B recover the amount on the instrument even though Mr. A has not violated the terms of the contract?
  - b) Mr. B endorsed the instrument to Mr. C (creditor) in order to discharge legally enforceable debt?
- A. In the given case it was clear that the instrument was delivered by Mr. A to Mr. B on a condition. This is known as Escrow instrument. In Escrow instrument holder will not get any title unless the conditions upon which delivery was made are violated. However, if instrument reaches the hands of HDC, he gets good title on that instrument.
  - a) Mr. B cannot recover the amount on the instrument since Mr. A has not violated the terms of the contract.
  - b) Mr. C can recover the amount on the instrument provided he satisfies all the conditions to become an HDC.

**Q.No.14. Ambiguous Instrument**

**(B) [NEW SM, OLD SM]**

- 1) An instrument which can be construed either as a promissory note or as a bill of exchange is called ambiguous instrument. (Sec.17)
  - a) Holder has a choice to treat it either as a promissory note or as a bill of exchange.
  - b) Once the decision is taken by the Holder it can't be treated differently afterwards.
- 2) **Where the amount is stated differently in figures and in words [Sec.18]:** If the amount undertaken or ordered to be paid is differently stated in figures and in words, the amount stated in words shall be the amount undertaken or ordered to be paid.

**Ex:**

- a) "A bill drawn by Head office on its Branch";
- b) "A bill drawn by an agent acting within his authority upon his principal";
- c) X draws a Bill on Y who is a minor.
- d) A bill drawn by a person on himself in favor of a third person
- e) A bill drawn by a person where the drawee is a fictitious person

**TEST YOUR KNOWLEDGE:**

1. A bill is drawn "Pay to A or order the sum of one thousand rupees". In the margin, the amount stated is Rs.10,000 in figures. (a) Is this a valid bill? (b) If so, for what amount?
  - A. a) Yes. It is a valid bill;
  - b) As per sec.18 of the NI Act, 1881, if the amount undertaken or ordered to be paid is stated differently in figures and in words then the amount stated in words shall be the amount undertaken or ordered to be paid. The Bill is valid for Rs.1000.
2. D drew a bill on A in favour of P. The bill was payable on demand. When the payee sought to present the bill for acceptance or payment, he discovered that no such person as A existed.
  - a) Is this a valid bill?
  - b) To whom should P go for the money?
- A. a) No, as the drawee is not certain (sec 5)
- b) D.

**(NOW REFER PRACTICAL QUESTION NO.6)**

<sup>18</sup> Ex: A, the holder a bill, endorses it to "B or order" for the purpose that B may get it discounted. B negotiates the bill to C who takes it bona fide and for value. C is a holder in course, and he acquires good title to the bill.



**Q.No.15. What is an inchoate Stamped Instrument and state its legal affects? (A) [NEW SM, OLD SM]**

**INCHOATE STAMPED INSTRUMENT [Sec 20]:**

- 1) **Meaning:** An Inchoate stamped instrument means an instrument that is incomplete in certain aspects.  
In case of Inchoate instrument, the person signs and delivers a blank or incomplete instrument to another person and authorizes such person to complete the Instrument.
- 2) **Conditions for an Inchoate instrument:**
  - a) A person signs a paper
  - b) The Paper is stamped
  - c) The paper is either wholly blank or Partially blank
  - d) The Person signing such paper delivers it to another person.<sup>19</sup>
- 3) **Legal Effect:** The holder gets a prima facie authority to make or complete it as a negotiable instrument.
- 4) **Rights of parties in case of an inchoate instrument:**
  - a) HDC can recover the whole amount specified in the instrument but not exceeding the amount covered by the stamp affixed on the instrument.
  - b) Holder (any person other than HDC) cannot recover the amount in excess of the amount intended to be paid by the person delivering the inchoate instrument.

**NOTE:** You will get more clarity on the words Holder & Holder in Due Course in further questions.

**TEST YOUR KNOWLEDGE:**

1. What is the extent of liability of Drawee or maker in case of Inchoate Instruments?
- A. Refer point D above.
2. A signs, as acceptor, an 80 Paisa stamp with the amount left blank. The amount of Rs 100 in the margin is fraudulently altered to Rs 1000, and the bill is, in words, filled in for a thousand rupees. The bill gets into the hands of H, a holder in due course. Can he recover this amount?
- A. Yes, H (HDC) can recover the amount, provided 80 Paisa stamp covers Rs 1000.
3. X signs his name on a blank but stamped instrument (Each Stamp covers Rs. 5,000, and X affixed 2 stamps). He delivers the instruments to Y with authority to fill upon a promissory note for Rs.8,000 only. Discuss the legal position in the following cases.
  - a) Y fills the note for Rs. 10,000 and endorses it to Z who takes in good faith for valuable consideration.
  - b) Y fills the note for Rs. 12,000 and endorses it to Z who takes in good faith for valuable consideration.
  - c) Y fills the note for Rs. 10,000 and kept with himself till due date.
- A.
  - a) Z, being a holder in due course can recover Rs.10,000 from X.
  - b) Z, being a holder in due course can recover Rs. 10,000 from X being the amount covered by the value of stamp affixed but not more than that.
  - c) Y not being a holder in due course can recover Rs. 8,000 only from X.

**(NOW REFER PRACTICAL QUESTION NO.7)**

## **PART 3 - MATURITY DATE & GRACE DAYS**

**Q.No.16. Write down the provisions relating to maturity and days of grace for negotiable instruments under the NI, Act, 1881? (A) [NEW SM, OLD SM, OLD PM, M18 (N) - 5M]**

- 1) **MATURITY:** Maturity of a negotiable instrument means the date on which the negotiable instrument falls due for payment.

19) E.g.: A person signed a blank acceptance and kept it in his drawer and some person stole it and filled it up for Rs.2000 and negotiated it to an innocent person for value. It was held that the signer to the blank acceptance was not liable to the holder in due course because he never delivered the instrument intending it to be used as a negotiable instrument. So, delivery is very important for validity of an inchoate instrument.

- 2) **DAYS OF GRACE:** A negotiable instrument which is payable otherwise than on demand, at sight or on presentment is entitled to 3 grace days. In other words, all time instruments are entitled to the benefit of grace days.
- 3) **RULES FOR FINDING OUT DATE OF MATURITY IN THE FOLLOWING CASES:**
- If the maturity day of a Note or Bill is a public holiday,<sup>20</sup> then date of maturity is immediately preceding business day.
  - If the maturity day of a Note or Bill is an emergency or unforeseen holiday, then the date of maturity is immediately succeeding business day.
  - While calculating the maturity date with respect to a promissory note or bill of exchange made payable at certain number of days after date or after sight or after a certain event, the day of presentment for acceptance or sight, or of protest for non-acceptance, or the day on which the event happens, shall be excluded.
- 4) **INSTRUMENTS ENTITLED TO 'DAYS OF GRACE' ARE:**
- A bill or note payable on a specified day.
  - A bill or note payable 'after sight'.
  - A bill or note payable after certain period of time,<sup>21</sup>
  - A bill or note payable after the happening of a certain event.
  - Where a Note or Bill is payable in installments, days of grace are allowed on each installment.
- NOTE:** All those instruments which are entitled to grace days must be presented for payment on the last day of grace.
- 5) **INSTRUMENTS NOT ENTITLED TO 'DAYS OF GRACE' ARE:**
- A cheque (as it is intended for immediate payment).
  - A bill or note payable 'at sight' or 'on presentment' or 'on demand' and
  - A bill or note in which 'no time is mentioned'.
- 6) **SOME ILLUSTRATIONS ON FINDING OUT DATE OF MATURITY [SEC.23 and 24]:**

No	SITUATION	DATE OF MATURITY	ILLUSTRATION
1)	Instruments payable on a <u>specified day</u> .	<u>Specified day + 3<sup>rd</sup> day</u>	A bill which specifies the date of payment on 22-03-2017 is payable on 25-03-2017.
2)	Instruments payable <u>certain days after the date of preparation of instrument</u> . (after date)	Date of preparation of instrument + <u>certain days + 3<sup>rd</sup> day</u>	A bill which is prepared on 22-03-2017 and payable after 15 days is due on 09-04-2017. (22-03-2017 + 15 days + 3 <sup>rd</sup> day)
3)	Instruments payable <u>certain days after the date of happening of a certain event</u> .	Date of happening of event + <u>certain days + 3<sup>rd</sup> day</u>	A bill is payable after 7 days from the date of death of C. If C died on 22-03-2017 then bill is payable on 01-04-2017. (22-03-2017 + 7 days + 3 <sup>rd</sup> day)
4)	Instruments payable <u>after certain months from the date of preparation of instrument</u> . (after date)	Date of preparation of instrument + <u>stated number of months + 3<sup>rd</sup> day</u>	A bill is prepared on 22-03-2017 and is payable after 3 months. Then the due date for payment will be 25-06-2017. (22-3-2017 + 3 Months + 3 <sup>rd</sup> day)
5)	Instruments payable <u>after certain months from the date of presentment of instrument for sight</u> . (after presentment)	Date of presentment of instrument + <u>stated number of months + 3<sup>rd</sup> day</u>	A bill is prepared on 22-03-2017 and is payable 3 months from the date of presentment. If the bill is presented for sight on 25-06-2017 then the due date for payment will be 28-09-2017. (25-06-2017 + 3 Months + 3 <sup>rd</sup> day)

20) Any day declared by the Central Government to be a public holiday by notification in the Official Gazette is known as Public Holiday. Public holiday includes Sundays.

21) If in the relevant month, there is no corresponding date, the last day of such month shall be taken.

6)	Instruments payable after certain months from the date of happening of certain event.	Date of happening of event + certain months + 3 <sup>rd</sup> day	A bill is payable after 3 months from the date of death of C. If C died on 22-03-2017 then the due date for payment will be 25-06-2017 (22-03-2017 + 3 months + 3 <sup>rd</sup> day)
7)	If the day of maturity of a Note or Bill is a public holiday	Immediately preceding business day	If maturity date of a bill is 26 <sup>th</sup> Jan. (i.e. Republic day), it falls due on 25 <sup>th</sup> Jan., if 25 <sup>th</sup> Jan. is also a public holiday (i.e. Sunday), it will fall due on 24 <sup>th</sup> Jan. (Provided, 24 <sup>th</sup> Jan. is not a public holiday)
8)	If the day of maturity of a Note or Bill is an Emergency or unforeseen holiday	Immediately succeeding business day	If 9 <sup>th</sup> September is emergency holiday, then the instrument will be payable on 10 <sup>th</sup> September. If 10 <sup>th</sup> September is also holiday, then it is payable on 11 <sup>th</sup> September.

**TEST YOUR KNOWLEDGE:**

- State briefly the rules laid down under the NI Act, 1881, for 'Determining the date of maturity' of a Bill of Exchange. [OLD PM, M18 (N) - 5M]  
A. Refer the Point No.3 in the above answer.
- In what way does the NI Act, 1881 regulate the determination of the "Date of maturity" of a 'Bill of Exchange'. [OLD PM]  
A. Refer the Point No.3 in the above answer.

**PART 4 - HOLDER & HOLDER IN DUE COURSE**

**Q.No.17. Who is a Holder as per Negotiable Instruments act, 1881? (A)**

[NEW SM, OLD SM, OLD PM, N16 - 4M]

**HOLDER (Sec 8):** The "holder" of a promissory note, bill of exchange or cheque means any person entitled -

- to possession of the negotiable instrument<sup>22</sup> in his own name; and
- to receive or recover the amount due on the negotiable instrument from the parties liable on it.

**In other words, A Holder means the owner of a negotiable instrument. Most important condition to be satisfied is "right to possession". A person in physical possession of the instrument without having right to possess, can't be called as Holder.**

**Examples:**

- X obtains a cheque drawn by Y, by way of gift. Here X is a holder (as he satisfies all the conditions.)
- A is the payee of the cheque. He is prohibited from receiving the amount of the cheque, by a court order. Here A is not a holder (as he is not entitled to receive payment on the cheque even though he is in physical possession of the cheque).
- B is the agent of C. B received an instrument in favour of C from A. Here B is not a holder even though, he is in possession of the instrument since it is not endorsed by C to B. (B is holding the instrument on behalf of his Principal but not in his own name)

**(NOW REFER PRACTICAL QUESTION NO.8)**

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

- Holder must be, named in the instrument as
  - Payee or Endorsee in case of Order instrument,
  - Bearer in case of Bearer instrument.
- Sometimes a person may be in possession of a negotiable instrument(s), but law does not consider him as a holder. Following are some of such instances:
  - A person who finds or steals a bearer instrument.
  - A person who takes an instrument under forged endorsement.
  - A beneficial holder claiming through 'BENAMIDAR' is not a holder.

22) In other words, he has right to hold the instrument in his own name.

- d) An agent holding an instrument for his principal is not a holder. An agent can receive payment of the instrument, but he has no right to sue on the instrument in his own name.
- e) A Payee prohibited by an order of court from receiving the amount of the instrument.
3. If the Note, Bill or Cheque is lost or destroyed, its holder is the person who is entitled to receive amount at the time of such loss or destruction.
4. Dear students, for better understanding of this question faculty will briefly explain you the meaning of following technical terms:
- Endorsement
  - Blank endorsement, Full endorsement
  - Bearer instrument, order instrument

But you will get detailed discussion of these technical terms in further questions. So, don't expect faculty to explain the meaning of these terms in a detailed manner.

**Q.No.18. Who is a Holder in due course? (A) [NEW SM, OLD SM, OLD PM, RTP - N16, MTP1 - M15]**

**HOLDER IN DUE COURSE [SEC.9]:** Holder in due course means:

- 1) Any person who for consideration, became
  - the possessor of a negotiable instrument (*in case of bearer instrument*), or
  - the payee or endorsee of a negotiable instrument, (*in case of order instrument*),
- 2) Before the amount mentioned in it became payable<sup>23</sup>, and
- 3) Without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title<sup>24</sup>.

**ESSENTIALS TO BECOME HOLDER IN DUE COURSE:** A Holder must satisfy the following conditions to call himself as Holder in Due Course.

- 1) He must have obtained instrument by paying valuable and lawful consideration for it.<sup>25</sup>
- 2) He must have obtained the negotiable instrument before maturity.
- 3) He must have obtained the instrument in good faith and without negligence<sup>26</sup>.
- 4) The instrument must be complete and regular on the face of it.<sup>27</sup>

**TEST YOUR KNOWLEDGE:**

1. Examine when holder of a negotiable instrument is considered as holder in due course under the provisions of the NI Act, 1881.
- A. Refer point - Essentials to become HDC above.
2. X, by inducing Y, obtains a bill of exchange from him, fraudulently in his (X) favour. Later, he enters into a commercial deal and endorses the bill to Z for consideration. Z knowing about fraud between X and Y takes the Bill. Explain whether he has right to receive the proceeds of the cheque or not.
- A. Here Z is not a holder in due course (Lack of good faith). Z cannot recover money from X since he has no title on that instrument. However, he may recover amount under some other Act like Indian contract act or sale of goods act (as the case may be).
3. X draws a Bill of exchange for Rs.20,000 and hands it over to Y. Later on, Y endorsed the bill to Z after maturity. Explain whether Z has the right to receive the proceeds of the Bill or not.
- A. Even though the title of Z is good and bonafide, he is a holder but not holder-in-due course. Because Z got the Bill after maturity. Of course, as a holder he is entitled to receive Rs.20,000 from the person primarily liable to that instrument..

23) In simple words, Before maturity date

24) In simple words, received the instrument in Good Faith

25) When a holder obtains an instrument as a gift or has been inherited then the transferee cannot become a holder in due course. Of course, he is considered as Holder and he is entitled to receive amount on the instrument.

26) without Knowledge of Holder defective title

27) If a person has some suspicion about an instrument but has no actual knowledge of irregularity, he must make an enquiry to confirm his suspicion. If he does not enquire and accepts a bad instrument, he cannot be granted the status of a holder in due course, just because he obtained instrument in good faith. No reason to suspect & Good faith both shall exist.

4. A promissory note is executed by A in favour of B in consideration of C, a relation of B, forbearing to sue on a prior promissory note executed by B in favour of C. Has the note executed by A in favour of B any lawful consideration?
- A. Yes. Sec 2(d) of the Indian Contract Act, 1872.
5. 'A' draws a cheque for Rs. 1,000 and hands it over to 'B' by way of gift. Is 'B' a Holder-in-due course? Explain whether he has right to receive the proceeds of the cheque or not. (MTP N18 (N))
- A. B is a holder but not a holder in due course as he does not get the cheque for value and consideration. His title is good and bonafide. As a holder he is entitled to receive Rs. 1000 from the bank on whom the cheque is drawn.

(NOW REFER PRACTICAL QUESTION NO.9)

Q.No.19. State the Privileges of a holder in due course?

(A) [NEW SM, OLD SM, OLD PM]

**FIRST WRITE THE DEFINITION OF HOLDER IN DUE COURSE:**

**PRIVILEGES OF A HOLDER IN DUE COURSE:**

- 1) **In case of Inchoate Instrument:** HDC can claim full amount of negotiable instrument (but not exceeding the amount covered by the stamp) even though such amount is in excess of the amount intended by the person delivering an inchoate instrument.
- 2) **In case of instrument obtained by unlawful means or for unlawful consideration:**
  - a) Against HDC, the person liable to pay an instrument cannot contend that the instrument was lost or was obtained from him by an offence or fraud or for an unlawful consideration.
  - b) Thus, HDC gets a valid title to the negotiable instrument even though the title of the transferor was defective.
- 3) **In case of fictitious bill:** In case a bill is drawn in a fictitious name and is payable to his order, the acceptor cannot be relieved from his liability to HDC. However, HDC has to prove that the bill was endorsed by the same person who has drawn such instrument. (Sec 42).
- 4) **In case of conditional instrument or 'escrow':** If an instrument is negotiated to HDC, prior parties cannot argue that instrument was delivered conditionally or for a special purpose only. (Sec 46 and 47).
- 5) **Original validity of the instrument can't be denied:** In a suit by HDC,
  - i) Maker of a promissory note or
  - ii) Drawer of a bill or cheque or
  - iii) Acceptor of a bill for the honour of the drawer
 shall not deny the validity of the instrument as originally made or drawn.
- 6) **Payee's capacity to endorse can't be denied:** In a suit by HDC, either Maker of a promissory note or Acceptor of a Bill of exchange, payable to order, shall not deny the Payee's capacity to endorse the same (Sec.121).
- 7) **A holder, who derives title from the holder in due course has the same rights as that of holder in due course (Sec. 53):** Once a negotiable instrument passes through the hands of a holder in due course, it gets cleansed of all its defects provided the holder himself is not a party to the fraud or illegality which affected the negotiable instrument in some stage of its journey.

**TEST YOUR KNOWLEDGE:**

1. Describe in brief the advantages and protections available to a "Holder in due course" under the provisions of the NI Act, 1881.
- A. Refer - Privileges of a Holder in due course in the above answer.
2. A bill of exchange up to the value of Rs.1,000 requires stamps worth 50 paise. A bill with a stamp of 50 paise on it is duly signed but the amount is not filled in. 'A' accepted the same, delivered to B and authorized B to fill an amount of Rs.500. Answer the following situations:
  - i) If B filled Rs. 900 and retained the instrument till maturity date.
  - ii) If B filled Rs. 900 and endorsed the same to C for consideration.
  - iii) If B filled Rs. 1,400 and endorsed the same to C for consideration.

- A. HDC can recover the whole amount specified in the instrument but not exceeding the amount covered by the stamp affixed on the instrument. Holder (any person other than HDC) cannot recover the amount in excess of the amount intended to be paid by the person delivering the inchoate instrument.
- B, is the Holder of instrument, cannot recover amount in excess of the amount intended to be paid by the person delivering the inchoate instrument. So, B can claim Rs. 500
  - C, is HDC, can recover the whole amount specified in the instrument but not exceeding the amount covered by the stamp affixed on the instrument. So, C can claim Rs. 900
  - C, is HDC, can recover the whole amount specified in the instrument but not exceeding the amount covered by the stamp affixed on the instrument. So, C can claim Rs. 1,000 since stamp value covers Rs. 1,000.
3. X draws a bill on Y but signs it in the fictitious name of Z. The bill is payable to the order of Z. The bill is duly accepted by Y. M obtains the bill from X thus, becoming its holder in due course. Can Y avoid payment of the bill? Decide in the light of the provisions of the Negotiable Instruments Act, 1881.
- A. Sec. 42 of the NI Act, 1881.
- In case a bill is drawn in a fictitious name and is payable to his order, the acceptor cannot be relieved from his liability to HDC. However, HDC shall establish that the bill was endorsed by the same person who has drawn such instrument.
- Accordingly, in the instant case, Y cannot avoid payment by raising the plea that the drawer (Z) is fictitious. The only condition is that the signature of Z as drawer and as endorser must be in the same handwriting.
4. A draws a bill payable to his own order on B, who accepts the same. Afterwards A endorses the bill to C, C to D who is a minor and later D endorsed the same instrument to E. On maturity, holder E demanded amount of instrument from B (acceptor). B denies the demand made by E on the ground that 'E' obtained instrument from D (minor) who has no contractual capacity'. Discuss the validity of Mr. B
- A. B's contention of denying liability was invalid. Reason: Refer Point "6" above.
5. X, by inducing Y, obtains a bill of exchange from him fraudulently in his (X) favour. Later, he enters into a commercial deal and endorses the bill to Z for consideration who takes the Bill in good faith and before maturity. Later Z endorses the same bill to Mr. A. Explain whether Mr. A has right to receive the proceeds of the cheque or not.
- A. Yes. Refer Point 7 above.
6. On a Bill of Exchange for Rs.1 lakh, X's acceptance to the Bill is forged. 'A' takes the Bill from his customer for value and in good faith before the Bill becomes payable. State with reasons whether 'A' can be considered as a 'Holder in due course' and whether he (A) can receive the amount of the Bill from 'X'.
- Section 9 of the Negotiable Instruments Act, 1881: HDC - write about HDC.
- A. In the given case, 'A' became a possessor of the Bill for value and in good faith, before maturity. Hence, he can be considered as HDC.
- However, if a signature on the negotiable instrument is forged then instrument becomes nullity (i.e. Invalid instrument). Forged instrument will not create any rights and obligations on the parties thereto. The holder of a forged instrument cannot enforce payment thereon.
- Even if holder of the forged instrument obtains any payment thereon then he cannot retain the money. The true owner can sue on tort the person who had received. This principle is universal in character, even a HDC is not exempt from it.
- A holder in due course is protected when there is defect in the title. But he derives no title if there is entire absence of title (i.e. as in the case of forgery). Hence 'A' cannot receive the amount on the Bill.
7. A makes a note payable to B who indorses it to C who takes it for value and in good faith. C sues A on the note and a proves that he made it for an illegal consideration. Can C recover the amount?
- A. Yes, as he is a holder in due course and the defence by A that it had been obtained from him for an illegal consideration cannot be set up against C.
8. B makes a note payable to bearer.it passes through several hands and ultimately comes in to the hands of C. C sues on the note. At the trail it is proved that the note was stolen from B. Can C enforce payment on the note?
- A. Yes, as he is a holder in due course.
9. A, the holder of a bill , transfers it to B as payable to him or his order for the express purpose that it shall be discounted B endorses it to C who takes it bona fide and for value . Discuss the position of C as against A and B
- A. C can hold both A and B liable for the payment of the bill (sec.43).

**(NOW REFER PRACTICAL QUESTION NO.10, 11, 12, 13, 14, 15, 16)**

## PART 5 - NEGOTIATION & ITS TYPES

**Q.No.20. Define the term Negotiation and explain various modes by which negotiation can be effected.**  
**(A) [NEW SM, OLD SM, MTP1 M18(O), MTP2 M19(O), MTP N19 (N&O)]**

### 1) MEANING:

- a) When a Negotiable Instrument is transferred to another person, so as to make such other person holder of the instrument, then such instrument is said to be negotiated. (Sec 14)
- b) Negotiation is said to be done only when it is made with an intention of transferring the title of the instrument to the transferee.

### 2) METHODS OF NEGOTIATION:

- a) **Bearer Instrument:** A bearer instrument may be negotiated by mere delivery and such delivery must be voluntary.
- b) **Order Instrument:** An order instrument can be negotiated by endorsement and delivery. Mere endorsement<sup>28</sup> does not amount to negotiation. The instrument must also be delivered.

### ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:

1. One of the essential characteristics of a negotiable instrument is that it is freely transferable from one person to another. The rights in a negotiable instrument can be transferred from one person to another by:

- A. Negotiation under the N.I act
- B. Assignment under Transfer of Property act

2. A person becomes holder of a negotiable instrument as a result of negotiation when he obtains the instrument in good faith without resorting any fraudulent means. Finder of NI or thief of NI cannot become holder of the instrument since the instrument is not being delivered.

E.g.: Ex: A holder of a cheque of Rs. 2000/- gave the cheque to B for payment of previous debt. This is a case of voluntary delivery.

3. If an instrument is delivered with some conditions attached, it is called conditional delivery. In such a case the property in the instrument does not pass to the transferee, till the condition is fulfilled.

When a condition is attached at the time of creating the instrument then such instrument becomes invalid. But conditions can be attached in the course of negotiation.

However, if such instrument is further endorsed to HDC (who accepts instrument without notice of the condition) then such negotiation is valid. HDC is entitled to recover money even though such condition is not satisfied (privilege available to a HDC).

E.g.: P delivers a bearer NI to Q on the condition that Q will not encash or negotiate it unless Q supplies goods to P. There is a conditional delivery by P to Q and the property in the NI will pass to Q only after supplying the goods. If the endorsee i.e. Q encashes the NI before supplying the goods, then P can recover back such money from Q. If Q negotiates it to R, who takes the same in good faith and for value, then R becomes holder in due course and can encash the same. In such a case P can't recover back money from R.

### TEST YOUR KNOWLEDGE:

1. X was the holder of a cheque of Rs. 10,000 payable to Bearer. He delivered this cheque to Y to keep it in his (Y) safe custody. Comment whether negotiation is said to take place or not?
- A. In this case there is no negotiation of cheque from X to Y because the transfer of cheque to Y makes him Bailee and not the holder of the cheque. For negotiation to happen, the instrument must be transferred with an intention to transfer the title of the instrument to the Transferee. So, in this case negotiation is not said to happen.

2. What is meant by Negotiation and what are its techniques? [MTP2 - M19(O), MTP - N19(O)]

- A. Refer meaning and methods of negotiation in the above answer.

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

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

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

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

**(NOW REFER PRACTICAL QUESTION NO.17)**

28) Endorsement means signing of a negotiable instrument for the purpose of negotiation. You will get more discussion in further questions.

**Q.No.21. Write a short note on delivery?****(D) [NEW SM]**

- 1) The contract on a negotiable instrument remains incomplete and revocable until delivery.
- 2) Negotiation is completed only by delivery of the instrument.
- 3) Delivery must be voluntary, and its object should be to pass the property in the instrument to the person to whom it is delivered.
- 4) Delivery of a negotiable instrument is essential
  - For bearer as well as order instruments
  - not only at the time of negotiation but also at the time of making or drawing it.
- 5) Delivery can be, actual or constructive.
- 6) If an instrument is delivered conditionally or for a special purpose then the property in it does not pass to the transferee, even though it is endorsed to him. (Sec.46)

**Exception:** When such instrument is negotiated to HDC.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. The rights in the instrument are not transferred to the Endorsee unless after the Endorsement the same has been delivered.
2. Actual delivery takes place when the instrument is physically handed over to Endorsee,
3. Constructive delivery takes place:
  - When the instrument is delivered to the agent, clerk or servant of the endorsee on his behalf<sup>29</sup> or
  - When the endorser, after endorsement, holds the instrument as an agent of the endorsee<sup>30</sup>.
4. Before delivering the instrument to Endorsee, if the endorser dies then the legal representatives of Endorser cannot negotiate the same, by delivery thereof. (Sec 57).

**(NOW REFER PRACTICAL QUESTION NO.18)**

**Q.No.22. Who are entitled to negotiate a negotiable instrument? State the conditions for negotiation? (D)**

- 1) **PARTIES ENTITLED TO NEGOTIATE:** (a) Maker, (b) Drawer, (c) Payee or (d) Endorsee, or (e) All of several joint Makers, Drawers, Payees or Endorsees of a negotiable instrument may negotiate the same.
- 2) **CONDITIONS TO BE FULFILLED TO NEGOTIATE AN INSTRUMENT:**
  - a) The person should be in lawful possession of the instrument or holder thereof and
  - b) The negotiability of the instrument has not been restricted or excluded by any term used in the NI.
- 3) **UNTIL WHICH DATE THE INSTRUMENT CAN BE NEGOTIATED?** A negotiable instrument may be negotiated:
  - a) By Maker, Drawee or Acceptor - Until the date of maturity.
  - b) By remaining persons - Until the instrument is paid by Maker, Drawee or Acceptor (as the case may be).

**NOTE:** How can negotiability of an instrument be restricted? You will get to know in further questions.

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- 29) Both A and B have their accounts in X bank. A the holder of negotiable instrument payable to bearer, directs the banker to transfer the instrument to B's credit in B's account, with the bank. the banker does so and accordingly now possess the instrument as B's agent. In this case there is constructive delivery.
- 30) A, holder of an order instrument made endorsement to B. Here A is endorser and B is endorsee. A resides at Hyderabad and B resides at Chennai. B ordered A to hold the instrument till its maturity and collect the sale proceeds on behalf of him. In this case, Delivery of instrument is completed by way of constructive delivery.



**PART 6 - ENDORSEMENT & ITS TYPES****Q.No.23. Define the term 'Endorsement'? State the requisites of a valid endorsement?****(C) [NEW SM, OLD SM]****ENDORSEMENT [SEC.15]:****1) Endorsement means:**

- a) Signing on the back or face of the Negotiable Instrument<sup>31</sup> or
- b) Signing on a slip of paper<sup>32</sup> annexed to the Negotiable Instrument
- c) By holder of the Negotiable Instrument<sup>33</sup>.

2) The process of transferring rights in an instrument is called Endorsement.

**PARTIES:**

1) **Endorser:** The person who endorses the instrument is called Endorser.

2) **Endorsee:** The person to whom the instrument is endorsed is called Endorsee.

**ESSENTIALS OF VALID ENDORSEMENT:**

- 1) **Writing:** It must be in writing.
- 2) **Signed:** It must be signed by the Endorser or else it is invalid.
- 3) **By Holder:** It must be made by the holder of the instrument<sup>34</sup>.
- 4) **Delivery:** It is completed by delivery of instrument to Endorsee.
- 5) **Form:** No particular form of words is necessary for an endorsement.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

**EFFECT OF ENDORSEMENT (SEC. 50):** An unconditional endorsement completed by delivery of instrument has following effects-

1. Ownership of instrument is transferred from endorser to endorsee.
2. Endorsee gets rights of further negotiation.
3. Endorsee gets rights to bring an action on his own for recovery against all parties whose names appear on the instrument.

**TEST YOUR KNOWLEDGE:**

1. M drew a cheque amounting to 2 lakhs, payable to N and subsequently delivered it to him. After receipt of cheque N endorsed the same to P but kept it in his safe locker. After some time, N died, and P found the cheque in N's safe locker. Does this amount to endorsement under the Negotiable Instruments Act, 1881?
  - A. No, P will not become the holder of the cheque. The cheque was never delivered to P and hence negotiation is not said to happen. (Section 48, the Negotiable Instruments Act, 1881)
2. Define the term allonge.
- A. An 'allonge' is a slip of paper annexed to an instrument on which extra endorsements are made. Sec.15 of the NI Act, 1881, permits the use of such annexed slips for the purpose of endorsements. In fact, such slip forms part of the instrument.

**Q.No.24. Who may endorse or negotiate the instrument? (D)****[NEW SM]**

- 1) A Maker or Drawer or Payee or Endorsee may endorse or negotiate an instrument only if he is a holder thereof.
- 2) Every sole Maker, Drawer, Payee or Endorsee, or all of several joint Makers, Drawers, Payees, or Endorsees of a negotiable instrument may endorse the same if the negotiability of such instrument is not restricted or excluded as stated in Sec 50 & 51.

31) As per law it can be signed on the face or back of the instrument. But it is customary to sign on the back of the instrument.

32) 'The slip of paper' annexed to instrument is called Allonge. Allonge is a French word.

33) E.g.: X, who is the holder of a Negotiable Instrument, writes on the back thereof: "Pay to Y or order" and signs the instrument. In such a case, X is deemed to have endorsed the instrument to Y. If X delivers the instrument to Y, X ceases to be the holder and Y becomes the holder.

34) When, in a bill payable to order, the indorsee's name is wrongly spelled, he should when he indorses it, sign the name as spelled in the instrument and write the correct spelling within brackets after his indorsement.

- 3) In other words, a stranger (i.e. a person other than those stated above) cannot endorse a negotiable instrument. If a stranger endorses it then the endorsement is void and he cannot be made liable as endorser.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

**Endorsement by legal representative:** If an order instrument was endorsed by the deceased but not delivered, the legal representative of a deceased person cannot negotiate instrument by delivery only (sec 57). A legal representative is not an agent of the deceased.

E.g.: A, the holder of a bill to B, before delivering the bill died, the legal representative of A subsequently delivered the bill to B. The Endorsement is invalid and B cannot sue on the bill.

**Q.No.25. Write about different types of Endorsement?**

**(A) [NEW SM, OLD SM, OLD PM]**

First write the meaning of the term Endorsement.

**DIFFERENT TYPES OF ENDORSEMENT:**

**1) Blank or General endorsement:**

- If the endorser just puts his signature without specifying the name of the endorsee then such endorsement is known as Blank endorsement.
- An instrument endorsed in blank becomes bearer instrument even though it was originally an order instrument<sup>35</sup>.

**2) Full or Special endorsement:**

- 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<sup>36</sup>.
- A blank endorsement can be converted into special one by adding the name of the Endorsee.

**3) Restrictive endorsement<sup>37</sup>:**

- An endorsement is said to be restrictive if it restricts or excludes the right of further negotiation.<sup>38</sup>
- It merely entitles the holder of the instrument to receive the amount on the instrument for a specific purpose.

**4) Partial endorsement:**

- If an endorsement purports to transfer only a part of the amount of the instrument, then it is called partial endorsement.
- Partial endorsement is not valid at law (Sec.56)
- For example: In case of a bill of Rs. 1000 "Pay Rs. 500 to B".

**Exception:** If an amount has been partly paid on the instrument and it is recorded on the instrument then it may be negotiated for the balance amount.

**5) Conditional or qualified endorsement (Sec.52):**

- A Conditional Endorsement is one which makes the transfer of the property in a negotiable instrument from the Endorser to the Endorsee dependent upon the fulfillment of some stated condition.
- Thus, where an Endorser makes his liability on the instrument conditional on the happening of a particular event, it is called Conditional Endorsement, though such event may never happen.

For example: "Pay B or order on the arrival of the ship at Calcutta"

**NOTE:** You can only expect a part of this question in the exam, but not entire question.

- RBI act will not permit to make or draw a Promissory Note payable to bearer and Bill payable to bearer on demand. But during the course of negotiation, an order instrument may get converted into bearer instrument and RBI Act does not restrict the same.
- A Bill was made payable to Rajesh or order (Rajesh is the Payee). Rajesh has written the words 'pay to the order of Sohan' and signed the same. This is a case of full endorsement from Rajesh to Sohan.
- E.g.: D signs the following indorsements on different negotiable instruments payable to bearer: (a) Pay the contents to G only, (b) Pay G for my use, (c) Pay G or order for the account of H. These indorsements exclude the right of further negotiation by G.
- If a negotiable instrument is made / drawn prohibiting negotiation then it is not considered as a negotiable instrument at all. But during the course of negotiation, if any of the endorser makes restrictive endorsement then the instrument will lose its negotiability character, from that date. But endorsement is valid.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. Blank or General endorsement will convert an order instrument into bearer instrument<sup>39</sup>.
2. It is important to understand that restrictive endorsement only restricts further negotiability of the instrument and therefore the instrument itself is not void. Even an instrument containing restrictive endorsement can be endorsed by the endorser. But endorsee will not get a better title than that of endorser. In other words, Endorsee will not get the special protection granted by the NI ACT.
3. **CANCELLATION OF ENDORSEMENT [SEC.40]:**
  - a) If the holder of a negotiable instrument destroys or impairs the endorser's remedy against a prior party without the consent of the endorser then,
  - b) The endorser is discharged from liability of instrument to the holder to the same extent as if it had been paid at maturity<sup>40</sup>.

**TEST YOUR KNOWLEDGE:**

1. What do you mean by an Endorsement? Briefly explain the types of an endorsement. [OLD PM]
- A. First write down the meaning of Endorsement. After that write the parties to endorsement and then list out different types of endorsement.
2. "A partial endorsement does not operate as a negotiation of the instrument" Comment. Describe different kinds of endorsements.
- A. If an endorsement purports to transfer only a part of the amount of the instrument, then it is called Partial Endorsement. Partial endorsement is not valid at law. (and Write types of endorsement given above).

**Q.No.26. Explain different forms / ways of Conditional or qualified endorsement?**

**(A) [NEW SM, OLD SM & PM]**

**FIRST WRITE THE MEANING OF CONDITIONAL ENDORSEMENT. AN ENDORSER CAN ACHIEVE IT IN ANY OF THE FOLLOWING WAYS:**

- 1) **Liability dependent upon a contingency:**
  - a) An endorser:
    - May make his liability to pay money
    - May make the right of endorsee to receive the amount
 depending upon the happening of a certain event, although such event may never happen. (For example: "Pay B or order on the arrival of the ship at Calcutta")
  - b) The liability of endorser arises only upon happening of such specified event,
  - c) The liability of endorser is extinguished if the happening of such event becomes impossible, or the conditions specified in it are not fulfilled.
  - d) However, such endorsement does not affect the position of party who has to pay for it on the date of maturity.
- 2) **Sans-Frais endorsement:** Where the Endorser does not want the Endorsee or any subsequent holder to incur any expenses on his account upon the instrument, the endorsement is 'sans frais'.
- 3) **Facultative endorsement:** Where such words are added to an endorsement whereby the Endorser waives any of his rights, the endorsement is Facultative (Ex: *Right to receive notice of dishonor*).
- 4) **Sans recourse / without recourse:** Endorser relieves himself from the liability to all subsequent endorsees<sup>41</sup>.

39) Ex: A bill is payable to the order of Ram. Ram signs on the back of the bill and does not write anything else. This is a case of Blank endorsement by Ram. In this case, the property in the bill may pass by mere delivery as if the bill is payable to bearer.

40) Ex: A is the holder of a bill of exchange made payable to the order of B, which contains the following endorsements in blank

First endorsement, "B".

Second endorsement, "P".

Third endorsement, "W".

Fourth endorsement "J".

In this bill A puts in suit against J and strikes out, without J's consent, the endorsements by P and W. A is not entitled to recover anything from J.

**NOTE:** You can only expect a part of this question in the exam, but not entire question.

**TEST YOUR KNOWLEDGE:**

- What is meant by 'Sans Recourse Endorsement' of a bill of exchange? How does it differ from 'Sans Frais Endorsement'? [OLD PM, M15 - 4M, M18-4M) (O)]
  - First write the meaning of both the terms.  
Difference: Any endorser can exclude personal liability by endorsing "sans recourse" i.e. without recourse. However, "Sans Frais" endorsement, indicate that no expenses should be incurred on account of the bill.
- Explain the concept and different forms of 'Restrictive & Qualified endorsement'. [OLD PM, N15 - 4M]
  - Restrictive Endorsement:** Such an endorsement has the effect of restricting further negotiation and transfer of the instrument.  
E.g.: (1) Pay to A only, S. Mukerjee (2) For the account of A only N. Aiyar  
**Conditional or qualified endorsement:** Such an endorsement combines an order to pay with condition.  
E.g.: Pay to A on safe receipt of goods. V. Chopra.

**Q.No.27. What are the provisions relating to Negotiation Back?**

**(A)**

**MEANING:** After negotiating an instrument, if an Endorser becomes its holder, before its maturity, then the instrument is said to be negotiated back to the holder.

**EFFECTS:**

- Holder cannot enforce payment against an intermediate party to whom he was previously liable.
- Thus, the general rule that a HDC may sue all the prior parties to the instrument does not apply in this case. (Logic: In order to prevent circuity of action).
- Holder can sue all prior parties, if he had made sans recourse endorsement.

**Ex:** A, holder of bill endorsed it to B. B endorsed it to C to D, D endorsed it again to A. In this case, endorsement by D to A is negotiation back. And B, C and D are not liable to A.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

If an Endorser so excludes his liability and afterwards becomes the holder of the instrument then all intermediates Endorsers are liable to him.

(NOW REFER PRACTICAL QUESTION NO.19)

## PART 7 - CROSSING OF CHEQUES

**INTRODUCTION:**

- Open Cheque:** A cheque which can be presented to the banker and can be paid at the counter of the bank is called an open cheque.
- Crossed Cheque:** When a cheque contains two parallel transverse lines across its face, the cheque is said to be crossed.

**Q.No.28. What is the meaning and purpose of crossing of a Cheque? (C)**

**[NEW SM, OLD SM]**

**1) MEANING OF CROSSING<sup>42</sup>:**

- Crossing of a cheque means an instruction by the drawer to the Drawee banker (i.e. paying bank) that payment shall not be made across the counter but shall be made through a bank only.
- When a cheque bears across its face two parallel transverse lines, the cheque is said to be crossed.
- The lines are usually drawn on the left hand top corner, but may be drawn anywhere.

**2) PURPOSE OF CROSSING:**

- Crossing is a warning to the paying bank, not to make its payment over the counter.

41) Endorser can do so by adding the words 'sans recourse' (without recourse) to the endorsement.

42) When a cheque is crossed it becomes easy to trace the person to whom payment was made. Thus, it makes the cheque safe.

**b) Crossing affects the mode of payment of cheque-**

- An open or uncrossed cheque is payable to payee or holder at the counter of the bank.<sup>43</sup>
- Payment of a crossed cheque can be obtained through a banker only. *So, through crossing one can be sure that only rightful holder gets payment.*

**c) Crossing does not affect the transferability or negotiability of cheque:**

- A crossed cheque can be negotiated just like an open cheque.
- A person acquiring a crossed cheque in good faith becomes its HDC just like an open cheque.

**Q.No.29. Write about various types of crossing of cheque?****(B) [NEW SM, OLD SM]****TYPES OF CROSSING:** Broadly, crossing can be categorized as follows:**1) GENERAL CROSSING (SEC. 123):**

a) A cheque is said to be crossed generally, if 2 parallel transverse lines are drawn on the cheque with or without using any of the following words:

- “and Company” or
- “& Co” or
- “Not Negotiable” or
- “and Company” and “Not Negotiable”
- “& Co” and “Not Negotiable”

b) **Effect:** General crossing is a direction to the drawee banker that payment of such Cheque should not be made across the counter and to pay the amount to a banker, who presents such cheque for payment.

**2) SPECIAL CROSSING (SEC. 124):**

a) A cheque is said to be crossed specially where the lines of crossing bear the name of a banker either with or without any additional words such as “Not Negotiable”.

**b) Effect:**

- Special crossing is a direction to the drawee banker that -
  - Payment of such Cheque should not made across the counter and
  - To pay the amount only to a particular banker whose name is written while crossing the cheque.
- Payment of such cheque can be obtained only through particular banker whose name is written while crossing the cheque.
- The drawee banker will pay only to the banker whose name appears across the cheque.
- *If a cheque contains special crossing to more than one banker, then the paying banker shall refuse to make the payment of the same*<sup>44</sup> (Sec.127).

**Exception:** A banker to whom it is crossed may cross it specially to another banker, his agent, for collection.

**3) ACCOUNT PAYEE OR RESTRICTIVE CROSSING:**

a) When the words “A/C payee” or “A/C payee only” are added to a general or special crossing, it is called restrictive crossing.

**b) Effect:**

- i) In case of A/c payee crossed cheque, the collecting banker is supposed to collect the cheque on behalf of only the payee whose name appears on the face of the cheque.

43) In such a case, if a wrong person takes away the payment of cheque, it is difficult to trace him.

44) However, two crossings with the names of 2 branches of the same bank are allowed. Example: cheque is double crossed with the names of two different banks, namely “SBI” and “Andhra Bank”, it is not payable. But if the two crossings are ‘Andhra Bank, Brodipet branch’, and ‘Andhra Bank, Arundelpet branch’, the cheque remains valid instrument and the payment can be obtained by depositing it into any of the specified branches.

ii) If banker collects this cheque for an endorsee (*i.e. person other than named payee*), then bank can be held responsible if such endorsee turns out to be wrongful holder of the cheque.

c) Thus, liability of a banker enhances to a great extent.

d) *Such type of crossing is not statutorily recognized.*

#### 4) **NOT NEGOTIABLE CROSSING:**

a) This requires writing of words “not negotiable” in addition to the two parallel lines.

b) These words may be written inside or outside these lines.

c) A general or special crossing may be accompanied by the words “Not Negotiable”.

d) Such a cheque loses its special characteristics of negotiability.

e) Not negotiable crossing does not restrict the transferability of instrument. However, a person who takes such cheque does not get a better title than the person from whom he acquired the cheque, including HDC<sup>45</sup> i.e., Negotiable instrument continues to be negotiable, but the title of the transferor is not negotiable.

f) Banker shall make payment against such cheques, only after getting satisfied that the person demanding payment is the person entitled to receive it.<sup>46</sup>

**NOTE:** *You can only expect a part of this question in the exam, but not entire question.*

#### **ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

a) The facility of Crossing is available for cheques only. Promissory notes or Bills of exchange cannot be crossed.

b) A general crossing can be converted into special crossing but a special crossing cannot be converted into general crossing.

c) If the holder converts the special crossing into general crossing by striking off the Banker's name, it amounts to material alteration and the instrument becomes invalid<sup>47</sup>. (You will get detailed discussion on this in further questions)

d) Even when the transferee of a “not negotiable” cheque is a holder in due course, he cannot acquire any better title than its transferor.

e) Cheque crossed ‘not negotiable’ does not affect the transferability of the negotiable instrument in anyway. The cheque still continues to be transferable but only those rights are conveyed to the transferee which the transferor has.

#### **TEST YOUR KNOWLEDGE:**

1. What is meant by ‘Crossing of a cheque? What is the advantage of crossing of a cheque from the point of view of the customer? What is the effect of crossing a cheque?

A. **Meaning of Crossing of a cheque:** Refer previous question.

#### **Advantage to customer:**

a) Customer can feel assured that the payment shall be made only to the desired person.

b) Crossed cheque cannot be paid across the counter, hence possibility of money encashed by person other than payee or endorsee thereof is very remote.

c) Thus, Crossing makes the cheque safe and it is a protection to the holder of the cheque.

**Effect of crossing:** By crossing a cheque, following are affected to certain extent

a) Mode of payment of Cheque.

b) The obligation of the paying banker, and

c) Negotiable character of the cheque.

2. A cheque marked “Not negotiable” is not transferable. (Or) Can a cheque crossed as “Not Negotiable” be negotiated further?

[M11, N15 - 1M]

A. A cheque marked “not negotiable” is a transferable instrument. The inclusion of the words ‘not negotiable’ however makes a significant difference in the transferability of the cheques. The holder of such a cheque cannot acquire title better than that of the transferor.

3. In order to cross a cheque, two parallel transverse lines can be drawn anywhere on the face or back of the cheque. [RTP - N12]

A. **Incorrect:** A crossing is made by drawing two parallel transverse lines across the face of the cheque with or without addition of certain words. Such lines are usually drawn on the left side top corner of the face of the cheque.

45) So, Transferee will not get special protection given by NI Act. Such protection can't be enjoyed even by HDC.

46) Such a cheque is like any other instrument where the title of the transferee is always subject to the title of the transferor.

47) The Parties liability on instrument to holder gets discharged. However, the liability of parties under Indian contract act or sale of goods act (as the case may be) will continue.

4. Explain as to why the combination of not negotiable with account payee crossing is considered the safest form of crossing a cheque?
- A. The safest form of crossing will be a combination of 'Not Negotiable' and 'A/c payee' crossings, because it gives the fullest protection to a cheque. Only the payee of Account payee and not-negotiable crossed cheque can recover the instrument amount.
5. Can a cheque be crossed specially more than once?
- A. A special crossing can be made only once. Where a cheque contains special crossing to more than one banker, then the paying banker shall refuse to make payment of the same.

Exception: When second special crossing is made by one banker on another banker to act as agent of the former then it is valid.

**(NOW REFER PRACTICAL QUESTION NO.20)**

**Q.No.30. Who can cross a cheque?**

**(C) [NEW SM, OLD SM]**

**A CHEQUE MAY BE CROSSED BY THE FOLLOWING PARTIES:**

- 1) **By Drawer:** A drawer may cross it generally or specially.
- 2) **By Holder:**
  - a) A holder may cross an uncrossed cheque generally or specially.
  - b) If the cheque is already crossed generally then the holder may cross it specially.
  - c) If the cheque is already crossed generally or specially then he may add the words "not negotiable".
- 3) **By Banker:**
  - a) A banker may cross an uncrossed cheque.
  - b) If a cheque is already crossed generally then he may cross it specially to himself.
  - c) If a cheque is already crossed specially, the banker to whom it is crossed may again cross it specially to another banker, his agent, for collection.

**THIS INFORMATION CAN BE PRESENTED IN THE FORM OF A TABLE AS FOLLOWS:**

CASE	RIGHT TO CROSS
1) Where a cheque is uncrossed	The holder may cross it generally or specially.
2) Where a cheque is crossed generally	The holder may cross it specially by adding the name of same banker.
3) Where a cheque is crossed generally or Specially	The holder may add the word 'Not Negotiable'
4) Where a cheque is crossed specially	The banker to whom it is crossed <u>may again</u> Cross it specially to another banker (his agent) for Collection.

**Q.No.31. When payment on negotiable instrument is said to be "payment in due course"? (C)**

**[NEW SM, OLD SM]**

**"PAYMENT IN DUE COURSE" <sup>48</sup>[SEC.10]:**

- 1) Payment is made as per apparent tenor of the instrument,
- 2) Payment is made in good faith,
- 3) Payment is made without negligence,
- 4) Payment is made to the person who is in the possession of the negotiable instrument,
- 5) Payment is made in money only.

48) The name of the payee and the amount were chemically erased and the bank paid the cheque. Had the cheque been examined under an ultra violet ray lamp, the defect could have been detected. But the Supreme Court held that, the bank could not be held guilty of negligence on the ground that the cheque was not subjected to that test. (Bank of Maharashtra vs. Automotive Engineering company 1993)

**Q.No.32. State the protection against liability available to paying banker?**

**(B) [NEW SM]**

**PAYING BANKER:** The banker who makes the payment of a crossed cheque is called paying banker.

**IN THE FOLLOWING CASES PAYING BANKER IS LIABLE:**

- 1) **Payment of crossed cheque out of Due Course:** Paying Banker shall be liable to the true owner of the cheque for any loss suffered by him due to irregular payment. If paying banker makes payment in below stated manner then he shall bear the loss and can't debit customer's account:
  - a) Paying a generally crossed cheque to a person other than banker, or
  - b) Paying a specially crossed cheque to any person other than to the banker to whom the same is crossed, or his agent for collection (*which is a banker*)
- 2) **Payment of a cheque on which drawer's signature was forged:** If paying banker pays a cheque on which drawer's signature was forged then such bank shall be liable to the drawer of such cheque.

**PROTECTION AVAILABLE TO PAYING BANKER:**

1) **In case of order cheque:**

- a) Paying Banker is discharged if he makes 'payment in due course'
- b) The protection is available even when:
  - The endorsement subsequently turns out to be a forged one or
  - The endorsement is made by Payee's agent without his authority.

2) **In case of Bearer cheque:**

- a) Paying Banker is discharged if he makes 'payment in due course' to the bearer of the cheque.
- b) It does not matter whether the apparent holder is the owner of the cheque or not.

3) **In case of generally crossed cheque:** Paying banker is discharged if the following conditions are satisfied.

- a) Payment is made to a banker (*i.e., payment is not made across the counter of the Bank*) and
- b) The payment is made in due course

*In such a case Paying banker is not liable even if payment is ultimately received by a wrong person instead of true owner. (This may happen when a generally crossed cheque falls in the hands of a wrong person who deposits the cheque in his account through his banker).*

4) **In case of specially crossed cheque:** Paying banker is discharged if the following conditions are satisfied.

- a) Payment is made to the banker on whom the cheque is crossed or to his agent for collection (*i.e., payment is made to the specified Bank or his agent for collection*) and
- b) Payment is made in due course.

**TEST YOUR KNOWLEDGE:**

1. What is the protection granted to the Paying Banker against wrong payment?
  - A. The Paying banker is protected against wrong payment of cheque, if such payment was made in due course.
2. A banker made payment of a cheque in which the drawer's signature was forged. Can the banker claim protection in respect of such payment? What would be the protection if it was a case of forgery of endorsee's signature? [RTP - M18(O)]
  - A. In case of cheques, the paying banker is given statutory protection against the payment of cheques having forged endorsements. And the banker cannot be held liable if it makes payment in good faith and without any negligence (Section 85, the Negotiable Instruments Act, 1881). But the banker will not be protected where the payment of a cheque is made on which the drawer's signature was forged. The reason for the same is that the banker is protected only in case of forgery of endorser's signature and not in case of forgery of drawer's signature.
3. A cheque is drawn payable to "B or order". It is stolen and the thief forges B's endorsement and endorses it to C. The banker pays the cheque in due course. Whether B can recover the money from the banker. [MTP1 - N18(N)]
  - A. According to Section 85 of NI Act, 1881, the drawee banker is discharged when he pays a cheque payable to order when it is purported to be endorsed by or on behalf of the payee. Even though the endorsement of Mr. B is forged, the banker is protected and he is discharged. The true owner, B, cannot recover the money from the drawee bank.



4. What are the circumstances in which Paying Banker can't enjoy the protection granted it?
- A. i) Payment of crossed cheque out of Due Course,  
ii) Payment of a cheque on which drawer's signature was forged.

**Q.No.33. State the protection against liability available to collecting banker? (C) [NEW SM, OLD SM]**

**Collecting Banker:** The bank which receives the payment of a crossed cheque on behalf of its customer is known as collecting banker.

**Protection to Collecting Banker / Non liability of Banker receiving payment of cheque (Sec.131):**

- 1) Subject to following conditions, a collecting banker will be protected, even if the title of the instrument in the hands of customer is defective.
  - The collecting banker acts as an agent for collection on behalf of the customer.
  - The collecting banker receives payment for a customer and the cheque is crossed.
  - The Cheque must have been crossed before it gets into the hands of the collecting banker.
  - The collecting banker acts in good faith and without negligence.
- 2) In case of uncrossed cheque if the collecting banker obtains the payment for a customer who does not have title for the instrument, the collecting banker is not liable and is protected.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. The section will be restricted to a case where the banker is acting as an agent for collection but not to a case where the banker is himself the holder.
2. The protection can be claimed by the collecting banker even when he credited his customer's A/c with the amount of the cheque before receiving payment thereof.
3. The protection is also available in respect of any draft as defined in sec. 85A.

**TEST YOUR KNOWLEDGE:**

1. Is there any difference in the protection available to a banker in respect of a cheque being 'crossed' or 'uncrossed'? [OLD PM]
- A. If a cheque is uncrossed, the banker is exonerated for the failure to direct either the genuineness, or the validity of the endorsement on the cheque purporting to be that of the payee or is authorised agent.

In case a cheque is crossed, the banker who pays the cheque drawn by his customer, he can debit the drawer's account so paid even though the amount of cheque does not reach true owner. The protection that can be availed are if the payment has been made in due course in good faith and without negligence too any person in possession thereof in the circumstances which do not excite any suspicion that is not entitled to receive the payment of the cheque. In other words, the condition of good faith and without negligence would be the criteria applied for judging the conduct of a collecting banker. Even though the banker is protected for having made payment of the cheque to a wrong person, the true owner of the cheque is entitled to recover the amount of the cheque from the person who had no title to the cheque.

(NOW REFER PRACTICAL QUESTION NO.21, 22, 23, 24, 25, 26)

## PART 8 - PRESENTMENT OF INSTRUMENTS

**Q.No.34. Write a short on 'Presentment of Bill for Acceptance'<sup>49</sup> (B) [NEW SM, OLD SM]**

- 1) Presentment for acceptance means placing the negotiable instrument before a Drawee, for acceptance.
- 2) **EFFECT:** Once the Bill is accepted by Drawee:
  - a) Drawee becomes Acceptor
  - b) the liability of Drawee becomes primay and unconditional and
  - c) the liability of Drawer becomes secondary and conditional.

49) Presentment of a Negotiable instrument arises in 2 situations: (a) Presentment for acceptance, (b) Presentment for Payment. In case of a bill, both the above situations will arise. But in case of Promissory note or a Cheque presentment arises only in case of payment.

### 3) FOLLOWING BILLS MUST BE PRESENTED FOR ACCEPTANCE SO AS TO MAKE THE PARTIES OF THE BILL LIABLE UPON IT:

- a) If a Bill contains express condition that, it must be presented for acceptance before it is presented for payment<sup>50</sup>.
- b) Bill payable after sight:
  - i) Bill payable after sight, means Bill payable after acceptance.
  - ii) It must be presented for acceptance in order to fix its maturity date.
  - iii) But it can be negotiated even before acceptance.

### 4) PROVISIONS RELATING TO PRESENTMENT FOR ACCEPTANCE:

- a) By Whom: Bill must be presented for acceptance by a person entitled to receive the payment. *Thus, a Bill must be presented by the holder or his duly authorised agent.*
- b) To Whom: Bill must be presented to the Drawee of a bill of exchange.
- c) Drawee's time for deliberation: If a Bill is presented to Drawee for acceptance, the holder must allow the Drawee 48 hours of time (excluding Public Holidays) to consider whether he is willing to accept it or not.
- d) Hours & Day for Presentment: Presentment must be made during business hours on a business day.
- e) Time limit for Presentment: Bill must be presented for acceptance within a specified time, after it is drawn. If no time is specified, then bill must be presented within reasonable time.
- f) Place of Presentment: Bill must be presented for acceptance at a specified place.
  - i) If no place is specified, then bill must be presented at the place of Drawee's business.
  - ii) If he has no place of business, then at the Drawee's residence.
- g) Effect of non-presentment: If Bill is not presented for acceptance, then all the prior parties who are liable on the instrument are discharged from their liability, to the person making such default<sup>51</sup>.
- h) When presentment is excused: Presentment for acceptance is excused -
  - i) If the Drawee cannot be found even after reasonable search.
  - ii) If the Drawee is a fictitious person.
  - iii) If the Drawee is incompetent to contract.
- i) Mode of service of Presentment: Presentment through a registered letter is sufficient if it is authorized by agreement or usage.

#### TEST YOUR KNOWLEDGE:

1. When and How a Bill of Exchange can be presented for acceptance.
- B. Refer above answer.

**(NOW REFER PRACTICAL QUESTION NO.27)**

**Q.No.35. Discuss Drawee in case of need and also state his liability in case of his dishonor?**

**(B) [NEW SM, OLD SM, OLD PM, N14 - 2M]**

#### DRAWEE IN CASE OF NEED (SEC.7):

- 1) If the drawer of a bill is afraid that drawee may not accept the bill or make payment then he may specify the name of additional drawee who may be approached for acceptance or payment in case of need.

50) Unless otherwise stated, acceptance is required only for bill of exchange payable after sight (Sec. 61). With respect to other bills there is no express provision in the Act requiring presentment of acceptance before presenting them for payment and there is nothing in the Act to prevent such bill being presented for acceptance. But if the bill is payable after sight or at sight or on demand then acceptance by the drawee is necessary before he can be held liable up on it.

51) Liabilities of Parties under Negotiable instrument may get discharged. However, Parties may still be liable under respective acts i.e. Sale of Goods Act or Indian Contract act, etc.

- 2) Such person is called 'Drawee in case of Need'.
- 3) Originally, the bill must be presented to the Drawee. If he refuses or fails to accept that, then it can be presented to 'Drawee in case of Need'.
- 4) Drawer may specify 'Drawee in case of need' at the time of drawing the Bill.
- 5) **LIABILITY OF DRAWEE IN CASE OF NEED:** The liability of Drawee in case of need arises only when the bill is dishonoured by drawee, due to non-acceptance or non-payment.
- 6) **DISHONOUR OF A BILL:** The bill is not said to be dishonoured until it is dishonoured by such Drawee in case of need also<sup>52</sup>.

**Q.No.36. What is Acceptance for Honour? How can acceptance for Honour be made? (B)**  
**[NEW SM, OLD SM, OLD PM]**

### **ACCEPTOR FOR HONOUR (SEC. 108):**

#### **1) MEANING:**

- a) If bill is dishonoured due to non-acceptance the holder may allow any other person to accept it for the honour of the drawer or for any one of the endorsers. The person who accepts the bill is called "Acceptor for honour".
- b) It is also called as 'acceptance supra protest'.

#### **2) HOW ACCEPTOR FOR HONOR MUST BE MADE:** Any person desiring to accept for honor must declare that he accepts under protest the protested bill for the honor of the drawer or of a particular endorser whom he names, or generally for honor.

#### **3) ACCEPTANCE FOR HONOUR - CONDITIONS:**

- a) The Bill should have been dishonoured by the drawee due to non-acceptance.
- b) The Bill must have been noted or protested for non-acceptance or for better security.
- c) The Acceptance is given -
  - by any person who is already not liable under the bill<sup>53</sup>
  - for the honour of any party already liable under the bill
  - with the consent of the holder of the bill.
- d) The acceptance must be made in writing on the bill.
- e) It must be for the whole amount due on the bill
- f) The Acceptance must be given before maturity of the bill.

#### **4) LIABILITIES OF ACCEPTOR FOR HONOUR:**

- a) He is liable to pay the amount of the bill, if the Drawee does not pay on maturity.
- b) He is liable only to the parties subsequent to the party for whose honour the bill is accepted.

#### **5) LIABILITY ONLY ON PRESENTMENT:** Acceptor for honour is liable to pay the bill, to the holder of the Bill, on maturity day, only if the following conditions are satisfied.

- a) It should be presented to the drawee for payment at maturity for one more time
- b) If the drawee dishonours the bill, it must be noted and protested.
- c) The bill should be presented to the 'Acceptor for honour' immediately on the next day of maturity but not later.

#### **6) 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.

52) If the Bill is not presented to Drawee in case of need then Drawer gets relieved from his liability.

53) Drawee of the bill when he refuses to accept the bill becomes a stranger. He may therefore accept the bill for honor of any party thereto.

**TEST YOUR KNOWLEDGE:**

1. Explain the terms 'Acceptance for Honour' as used in the Negotiable Instruments Act, 1881. [N14 - 2M]
- A. Write Point 1 above.

**Q.No.37. What are the rules governing presentment for payment of promissory notes, bills of exchange and cheques? (B) [NEW SM, OLD SM]**

**MEANING (SEC 64):** Presentment for payment implies presenting an instrument to the party, for obtaining payment.

**Exception:** Presentment for payment is not necessary for a P/N payable on demand, which is not payable at a specified place. *In other words promissory note payable on demand at any place presented for payment.*

**RULES REGARDING PRESENTMENT FOR PAYMENT:**

- 1) **By Whom:** Presentment for payment must be made by the holder or his duly authorized agents
- 2) **To Whom:** Presentment for payment must be made to -
  - a) the maker, acceptor or Drawee, or
  - b) Duly authorized agent of maker, acceptor or Drawee, or
  - c) Legal representative of a deceased party,
  - d) Official Assignee, in case of insolvency.
- 3) **TIME OF PRESENTMENT:**
  - b) **NI payable on demand:** It must be presented for payment within a reasonable time after it is received by the holder.
  - c) **NI payable after date or sight:** Such promissory note or Bill must be presented for payment on the date of maturity.
  - d) **Hours for Presentment:**
    - i) Must be presented during usual business hours of the maker or acceptor,
    - ii) In case of cheque, presentment must be made within banking hours.
- 4) **PLACE OF PRESENTMENT:**
  - a) **When place is specified:** Presentment for payment must be made at the place of payment specified<sup>54</sup> in the instrument (*and not elsewhere*).
  - b) **When no Place is specified:** It must be presented for payment at -
    - the place of business (if any) or
    - the usual residence
 of the maker of P/N, Drawee or acceptor of B/E.
  - c) **If maker, drawee or acceptor has no place of business or fixed residence:**  
 Presentment for acceptance or payment can be made wherever he can be reasonably found.
- 5) **MODE OF PRESENTMENT:** It is sufficient to present through a registered letter, if authorized by agreement or usage of trade<sup>55</sup>.
- 6) **PRESENTMENT OF CHEQUE:**
  - a) **To charge drawer:**
    - i) **Place:** Cheque must be presented at the bank, upon which it is drawn.
    - ii) **Time:** Must be presented within reasonable time but before the relation between Drawer and his Banker gets altered to the prejudice of the Drawer<sup>56</sup>.

<sup>54</sup>) "specified place" implies the precise address of the place; the mere mention of a big city like 'Chennai' is not sufficient.

<sup>55</sup>) By hand or through person.

b) **To charge any other person:** In order to charge any other person, except the drawer, cheque shall be presented within reasonable time, after delivery of such instrument by such person.

7) **EFFECT OF NON-PRESENTMENT:** In default of presentment, all parties to the instrument (*i.e., other than maker, acceptor or Drawee*) are discharged from their liability to the holder, on such default.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. Excuse for delay in presentment for acceptance or payment (sec. 75A):
  - a) Delay in presentment for acceptance or payment is excused if the delay is-
    - i) caused by circumstances beyond the control of holder, and
    - ii) not imputable to his default, misconduct or negligence<sup>57</sup>.
  - b) When the cause of delay ceases to operate, presentment must be made within reasonable time.
2. Promissory note payable in installments:
  - iii) Such Promissory note must be presented for payment on the 3<sup>rd</sup> day after the date fixed for payment of each installment.
  - iv) Non-payment on such presentment has the same effect of non-payment of Promissory note at maturity.
  - v) Thus, even if a single installment is not paid then the whole promissory note can be treated as dishonoured by non-payment.

**Q.No.38. When presentment for payment is not necessary?**

**(B) [NEW SM, OLD SM]**

In the following cases, it is not necessary to presentment the instrument for payment:

1) **AGAINST THE MAKER, DRAWEE OR ACCEPTOR:**

- a) If the maker, drawee or acceptor intentionally prevents the presentment of the instrument.
- b) **In case of instrument payable at his place of business:**
  - When he closes such place, on a business day, during usual business hours or
  - Even though the place is open, neither he nor any other authorized person attends to pay it, at such place, during usual business hours.
- c) **In case of instrument not payable at a specified place:** He cannot be found even after due search.

2) **AGAINST ANY PARTY SOUGHT TO BE CHARGED:** If he agrees to pay, notwithstanding non-presentment (waiver of Presentment).

3) **AGAINST ANY OTHER PARTY:** If, after maturity, with the knowledge that the instrument has not been presented

- a) he makes a part payment towards amount due on the instrument, or
- b) promises to pay the amount due therein, wholly or partly, or
- c) Otherwise waives his right to take advantage of any default in presentment for payment.

4) **AGAINST THE DRAWER:** If the drawer could not suffer damage from the want of such presentment<sup>58</sup>.

5) **OTHER CIRCUMSTANCES:**

- a) If the Drawee is a fictitious person or incompetent to contract
- b) If Drawer and Drawee are the same person
- c) If the Bill is dishonoured by non-acceptance
- d) If presentment has become impossible.

56) On 10/11/2019, Mr. A gave a cheque to Mr. B to discharge the past trade debt amounting Rs.5,00,000. On 10/12/2019 Mr. B deposited the cheque with Bank (This is an unusual delay). Meanwhile on 09/12/2019, Drawee banker filed insolvency petition. Normally, in the event of failure of Bank, Drawer is liable on the Cheque. But in this case Drawer is discharged from liability as Payee made delay in collecting the Cheque as a result of which Drawer is going to suffer the loss. If Payee had collected the Cheque on time then Drawer might have not suffered the loss.

Here the relation between Drawer (Mr. A) and the banker was altered. As a result the Drawer was discharged to the Payee since Payee fails to deposit cheque within the reasonable time

57) Examples: Delay happened because of Postal strike.

**Note:** The presentment for payment is not excused just because the party to whom presentment has to be made has gone abroad.

58) If Drawee is incompetent to Contract or Drawee is fictitious person or both Drawer and Drawee are same person then Drawer's nature of liability is primary.

**TEST YOUR KNOWLEDGE:**

1. What is meant by 'Presentment for payment' of a bill of exchange under the NI Act, 1881? When a bill of exchange presented for payment? State the circumstances when is the presentment not necessary.

A. Refer Meaning, Point C in Q.No.37.

Circumstances when the presentment is not necessary: Refer above answer

**(NOW REFER PRACTICAL QUESTION NO.28)**

**Q.No.39. What are the provisions relating to Payment for honour?**

**(D) [NEW SM]**

**PAYMENT FOR HONOUR:** A bill which has been accepted by the drawee and later dishonoured by non-payment may be paid for honour known as 'payment for honour'.

**PAYER FOR HONOUR:** A person who pays a bill for the honour of any other person is called "payer for honour", even though he is not a party to the Bill.

**CONDITIONS FOR PAYMENT FOR HONOUR (SEC 113):**

- 1) The bill must be dishonoured for non-payment.
- 2) The bill must have been noted or protested for non-payment.
- 3) Payment for honour is made:
  - a) For the honour of any party already liable under the bill.
  - b) By any person whether he is already liable on the bill or not.
  - c) With the consent of the Holder of the bill.
- 4) The person paying the amount must give a declaration to Notary Public about the party for whose honour he is making payment. Such declaration must be recorded by Notary Public.

**RIGHTS OF PAYER FOR HONOUR (SEC.114):**

- 1) The Payer for honour is entitled to all rights of a holder on the bill;
- 2) He can recover all the sums paid by him from
  - a) The party for whose honour he pays or
  - b) All the prior parties to such party.

**Q.No.40. What is the effect of Forged Endorsement?**

**(C) [NEW SM, OLD SM]**

**1) FORGED ENDORSEMENT:**

- a) Forged signature means imitating signature of another so as to transfer the title of instrument to other person. Forgery is an offence under the Indian Penal Code.
- b) In this case the forged signature makes the endorsement Invalid.
- c) **Effect:** The Property remains vested in the person who is the holder at the time of forgery.

**2) EFFECT OF FORGERY IN MAKING OF A NEGOTIABLE INSTRUMENT:**

- a) If the signature of the maker of note, Drawer of a bill is forged, the true owner is entitled to get back the payment from the person who obtained illegally.
- b) Even HDC, cannot claim any protection because forgery amounts to nullity.

**3) EFFECT OF FORGERY IN CASE OF FULL ENDORSEMENT OF A NEGOTIABLE INSTRUMENT:**

- a) Title cannot be based upon a forged endorsement.
- b) Any person claiming amount under forged endorsement cannot acquire rights of HDC even if he is a purchaser for value and in good faith.

**E.g.:** If there is endorsement in favour of G, only G can further negotiate it. A forged signature of G will not give title to the holder.

**4) EFFECT OF FORGERY IN CASE OF BLANK ENDORSEMENT OF A NEGOTIABLE INSTRUMENT:**

- a) NI is negotiated by mere delivery.
- b) If a holder forges the signature of a prior holder and transfers it, the Transferee may ignore the Forged endorsement and rely upon a prior endorsement in blank. He can make a good title through an earliest genuine endorsement in blank<sup>59</sup>.

**5) ACCEPTOR BOUND ALTHOUGH ENDORSEMENT FORGED [SEC.41]:**

- a) An acceptor of a Bill of Exchange, which is already endorsed, does not get relieved from his liability just because such endorsement is forged.
- b) He continues to be liable even if he knows or had reason to believe that the endorsement was forged, at the time of acceptance of the Bill.

**(NOW REFER PRACTICAL QUESTION NO.29)****PART 9 - PARTIES TO NI, THEIR LIABILITIES & WHEN THEY GET DISCHARGED**

**Q.No.41. Discuss the 'Capacity' and 'Authority' of a person to be a party to a negotiable instrument.**  
**(A) [NEW SM, OLD SM, OLD PM]**

**CAPACITY [Sec.26]:** Every person competent to a contract (*according to the law to which he is subject to*<sup>60</sup>) has capacity to bind himself and be bound by making, drawing, acceptance, endorsement, delivery and negotiation of an instrument.

**1) MINOR:**

- a) A minor may draw, endorse, deliver and negotiate any negotiable instrument.
- b) All the parties to such instrument shall be bound on such negotiable instrument.
- c) However, minor shall not be bound on such negotiable instrument.<sup>61</sup>

SITUATION (MINOR IS)	RIGHTS OR LIABILITIES
Drawer of Bill	Not liable to subsequent parties, can recover from Drawee or acceptor
Drawee or Acceptor	Not liable to the instrument.
Endorser	Not liable to the subsequent parties.
Endorsee	Can recover amount of instrument from prior parties.
Holder	Can recover amount of instrument from prior parties.

**2) AGENT:**

- a) Every person, capable of incurring liability, may bind himself or be bound by a duly authorized agent acting in his name.
- b) However, under general authority, agent will not get any power to make, draw, accept or endorse instruments on behalf of principal so as to bind his principal.

**NOTE:** An agent may have authority to draw bills of exchange, but not endorse them. An authority to draw does not imply that he has authority to endorse.

**3) INSOLVENT:**

- a) An insolvent is not competent to enter into a valid contract. So, he cannot draw, make, accept or endorse a negotiable instrument.
- b) If he endorses an instrument to a holder in due course, of which he is payee, then holder in due course can recover the amount from all prior parties except the insolvent.

59) E.g.: A bill of exchange is endorsed in favour of G or his order. G endorses it in blank. It reaches J's hand who passes it on to K by mere delivery. However, K forges J's endorsement and transfers it to L. L does not derive any title through the forged endorsement of J, but through G's endorsement which is genuine, he can sue any of the party to the bill without taking notice of the forged endorsement.

60) For example, how to decide whether a person is a competent or not? It has to be decided based on the Law of Land to which he is subject to.

61) Note: It is the estate of a minor (not the minor as person) which is liable for debts arising out of 'necessaries' supplied to minor.

**4) CORPORATION:**

- a) A Company (*being a distinct legal entity*) has the capacity to contract and therefore it can draw, endorse, transfer or negotiate an instrument.
- b) A trading company has implied powers to bind itself by the negotiable instrument unless prohibited by MOA / AOA.
- c) However, a non-trading firm must have this power specified in MOA / AOA. Otherwise the instrument is void and even whole body of shareholders cannot ratify the same. Therefore, on such bill or promissory note, even HDC cannot make company liable.

**5) PARTNERS:**

- a) Every partner has an implied authority to draw, sign, make and endorse the negotiable instrument in the name of the partnership and make the partnership firm and other partners jointly and severally liable on the instrument.
- b) However, the name of the firm should be mentioned on the instrument.

**NOTE:** DEAR STUDENTS, YOU MAY NOT GET A COMPLETE QUESTION. RATHER YOU MAY GET A QUESTION ON JUST ONE OR TWO POINTS.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

**Joint Payees:** NI may be made payable to 2 or more payees jointly, or it may be made payable in to one of two, or one or some of several payees.

E.g.: Note is drawn as follows

- i) I promise to pay a sum of Rs. 20,000 only, to A and B, 6 months after date.
- ii) I promise to pay a sum of Rs. 20,000 only, to A or B, 6 months after date.

**TEST YOUR KNOWLEDGE:**

1. The director of a company borrowed Rs.10,000 from A and executed a promissory note in favour of A. On the promissory note, there was no indication if the money was borrowed for and on behalf of the company. The company used the money for its purposes. Can the company be held liable to repay the loan on the basis of the promissory note?
  - A. No, the director is personally liable
2. A draws a cheque in favour of M, a minor. M endorses the same in favour of X. The cheque is dishonoured by the bank on the ground of inadequate funds. Discuss the capacity of Minor and state the liability of parties in this regard?
  - A. In this case, M being a minor may draw, endorse, deliver and negotiate the instrument so as to bind all parties except himself. Therefore, M is not liable. X can, thus, proceed against A.
3. A promissory note duly executed in favour of a minor is valid? (OLD PM, N10 - 1M, N15 - 1M)
  - A. Correct. A Minor is incompetent to enter into a contract. He cannot bind himself by becoming a party to a negotiable instrument. But he may draw, endorse, deliver and negotiate such instruments so as to bind all other parties except himself. (Sec. 26 of the NI Act, 1881)
4. A bill is addressed to H who is a partner in the firm of P. H accepts the bill in the firm's name. Explain whether he will be personally liable on the bill or not.
  - A. H is personally liable on the bill as acceptor.

(NOW REFER PRACTICAL QUESTION NO.30, 31)

**Q.No.42. State the liabilities of various parties relating to negotiable instruments. (A) [NEW SM]**

- 1) **LIABILITY OF AGENT (SEC.28):** An Agent is personally liable on the instrument, when he signs it without indicating that -
  - a) he signs in the capacity of agent, or
  - b) he does not intend to incur personal responsibility.

Agent is not liable if he was induced to sign that the Principal would only be liable but not he.

**NOTE:** Holder can sue the agent in an action for falsely representing that he had authority (to accept bill or make note).



**2) LIABILITY OF LEGAL REPRESENTATIVE (SEC.29):**

- a) A Legal Representative of a deceased person who signs<sup>62</sup> his name to a negotiable instrument is personally liable on that instrument.
- b) However, he can expressly limit his liability to the extent of the assets received by him<sup>63</sup>.

**3) LIABILITY OF DRAWER (SEC.30):** Drawer becomes liable to compensate the Holder -

- a) On dishonour of Bill of exchange by Drawee (For non-acceptance or non-payment) or
- b) On dishonour of cheque.

**NOTE:** Drawer is liable to Holder only if receives notice of dishonor from the holder.

**4) LIABILITY OF DRAWEE OF CHEQUE (SEC.31):**

- a) In case of Cheque, Drawee is always a banker.
- b) It is the duty of the bank to pay the cheque when it has sufficient funds of Drawer.
- c) If the banker refuses to make payment, without any sufficient reason, then it must compensate Drawer for any loss occurred.
- d) Bank is liable only to Drawer of the Cheque but not to the Holder / Payee<sup>64</sup>.

**5) LIABILITY OF MAKER OF NOTE AND ACCEPTOR OF BILL (SEC.32):**

- a) In case of Promissory Note Maker is primarily liable.
- b) In case of Bill of Exchange, until the Bill is accepted, Drawer is primarily liable. Once it is accepted, Acceptor is primarily liable and liability of Drawer becomes secondary.

**6) LIABILITY OF ENDORSER (SEC.35):** The Endorser of a negotiable instrument must compensate the holder for any loss or damage caused to him by the dishonour if the following conditions are fulfilled:

- a) The instrument was endorsed and delivered before maturity.
- b) The Endorser has not excluded his own liability (Sans recourse endorsement)
- c) Due notice of dishonour has been given to or received by such Endorser.

**NOTE:** After dishonour, every endorser is liable upon an instrument which is payable on demand.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. **Prior party vs. Subsequent party (Sec.38):** As between the parties liable as sureties, each prior party is also liable on the instrument as a principal debtor in respect of each subsequent party<sup>65</sup>.
2. **Liability of prior parties (Sec.36):** Every prior party to an instrument is liable to a Holder in due course until the instrument is duly satisfied.

**(NOW REFER PRACTICAL QUESTION NO.32, 33, 34)**

**Q.No.43. When does a negotiable instrument gets discharged?**

**(B) [NEW SM, OLD SM]**

**DISCHARGE OF AN INSTRUMENT:** An Instrument is said to be discharged only when the party who is ultimately liable to pay on the instrument is discharged from the liability.

**VARIOUS MODES OF DISCHARGE:** Negotiable instrument can be discharged in any of the following ways

- 62) The legal representative can sign the instrument either as a Maker or Drawer or Acceptor or Endorser. If the Legal representative doesn't sign the instrument then he is not liable under NI act, 1881. However, he is liable under other act  
E.g.: Under Sale of Goods act, 1930, Legal representative of deceased person is liable to the creditor to the extent of estate obtained from deceased.  
what will happen if legal representative does not sign: Legal representative of deceased person is liable to the creditor to the extent of estate obtained from deceased under sale of goods act or Indian contract act (as the case may be).
- 63) Legal representative may add the words like "without recourse to me personally" or "with recourse against the estate of deceased owner".
- 64) There is no privity of contract between the banker and the payee or holder of instrument (other than self cheque).
- 65) EX: A draws a bill payable to his own order on B, who accepts the same. Subsequently A endorses the bill to C, C to D and D to E. As between E and A, A is the principal debtor, and C and D are his sureties. As between E and C, C is the principal debtor and D is his surety.

1) **By Payment in due course**<sup>66</sup>:

- a) A negotiable instrument is discharged if the party primarily liable on the negotiable instrument makes payment in due course.
- b) Payment by a party who is secondarily liable does not discharge the instrument because payer can enforce it against prior endorser and the principal debtor.

2) **By Cancellation**: If the holder of an instrument cancels the name of the party primarily liable on the negotiable instrument, with an intention to discharge him.3) **By Release**: If the holder of an instrument releases or renounces his rights against the party primarily liable on the negotiable instrument.4) **By Negotiable back**: If the party primarily liable on the negotiable instrument becomes the holder of the instrument.5) **By Operation of law**: When the negotiable instrument becomes time barred.6) **Bill coming to acceptor's hands after maturity**: If a Bill which has been negotiated is, at or after maturity, held by the acceptor in his own right then all rights of action on instrument are extinguished (Sec. 90)<sup>67</sup>.**TEST YOUR KNOWLEDGE:**

1. A bill of exchange is payable to Shyam or order. At maturity another person at the same name wrong fully gets possession of the bill and presents it to the acceptor for payment. After being satisfied that the person presenting is Shyam the acceptor makes payment on it in due course. Is the acceptor discharged?
- A. No, Mistake as to identity of Payee, does not discharge acceptor from his liability.
2. A Bill is indorsed to John Smith or order. Another person of the same name gets the bill and presents it. The acceptor pays him. Is the acceptor liable to real John Smith?
- A. Yes

**Q.No.44. When do the parties to a negotiable instrument get discharged? (C) [NEW SM, OLD SM]**

- 1) Party to a Negotiable Instrument is discharged when his liability on the instrument comes to an end.<sup>68</sup>
- 2) When some of the parties are discharged and other parties are still liable on the instrument then such instrument is not said to be discharged.

**CASES WHERE PARTIES ARE DISCHARGED:**

- 1) **By allowing Drawee more than 48 hours to accept**: If the holder of a bill of exchange **allows more than 48 hours (excluding public holidays)** to the Drawee to accept the bill then all prior parties not agreeing to the same are discharged from liability to such holder.
- 2) **Qualified acceptance**: If the holder agrees for qualified acceptance then all the prior parties not agreeing to the same are discharged.
- 3) **By non-presentment of cheque within a reasonable time**: The Drawer of a cheque is discharged to the extent of loss or damage suffered by him if -
  - a) The cheque is not presented for payment within reasonable time of its issue and
  - b) The Drawer suffers the damage because of such delay.
- 4) **By payment**: If payment is made by any party liable on the instrument (*other than party primarily liable on the instrument*), such party and all parties subsequent to him are discharged.

66) When the payment is made, the negotiable instrument must be cancelled, or the fact of payment must be recorded on it. Otherwise the same instrument may once again be presented for payment.

67) A negotiable instrument may be negotiated:

- By Maker, Drawee or Acceptor - Until the date of maturity.
- By remaining persons - Until the instrument is paid by Maker, Drawee or Acceptor (as the case may be).

This rule is based on the general principle that a present right and liability united in the same person cancel each other.

68) When a negotiable instrument gets discharged then all the parties of the instrument will get discharged from their liability. When some of the parties get discharged then the remaining parties are still liable on the instrument and the instrument is not said to be discharged.

- 5) **By Release:** If the holder releases any party liable on the instrument (*other than party primarily liable on the negotiable instrument*) by any method other than cancellation of names then such party and all subsequent parties are discharged.
- Ex: Separate agreement of waiver, release or remission, etc.*
- 6) **By cancellation:** If the holder cancels the name of a party who is liable on the instrument (*other than the party primarily liable on such instrument<sup>69</sup>*) with an intention to discharge him then such party and all subsequent parties are discharged.
- 7) **Failure to give Notice of dishonour:** All the parties to whom notice of dishonour is not given are discharged from liability on such negotiable instrument.
- 8) **By Material Alteration:** If a negotiable instrument is materially altered then any person who was a party to it, at the time of making the material alteration, is discharged unless such party has agreed to it.
- 9) **By operation of law:** A party is discharged from liability under a negotiable instrument in the following cases:
- If the debt becomes time barred.
  - If a party is declared as an insolvent.

**NOTE:** YOU WILL GET BETTER KNOWLEDGE ON THE CONCEPT OF MATERIAL ALTERATION IN FURTHER QUESTIONS.

**TEST YOUR KNOWLEDGE:**

- How do you distinguish between discharge of instrument and discharge of party under the Negotiable Instruments Act, 1881? [OLD PM]
- An instrument is said to be discharged only when the party who is ultimately liable thereon is discharged from liability. Therefore, discharge of a party to an instrument does not discharge the instrument itself. Consequently, the holder in due course may proceed against the other parties liable for the instrument. On the other hand, when a bill has been discharged by payment, all rights there under are extinguished even a holder in due course cannot claim any amount under the bill.
- On 1st January, 2007, A draws a bill on B for Rs.1000, payable to C or order three months after date. B is not indebted to A nor has he agreed to honour A's bill. On 1st February 2007, C negotiates the bill to D who takes it as a holder in due course. D does not present the bill for acceptance but presents it for payment on 4th April, 2007. On a dishonor by B, D gives a notice of dishonor to A. Can A claim to be discharged?
- No
- C of Kolkata drew a bill on H of Hongkong, payable sixty days after sight. The holder retained it for five months and when the ultimately presented it for acceptance, it was dishonoured. Will this delay discharge the prior parties?
- Yes, prior parties to the instrument get discharged as the delay is unreasonable.

(NOW REFER PRACTICAL QUESTION NO.35, 36)

## PART 10 - MATERIAL ALTERATION

**Q.No.45. Define the term Material Alteration under the Negotiable Instruments Act, 1881 (A)**  
[NEW SM, OLD SM, OLD PM, M13 - 4M]

*Sometimes, a negotiable instrument is altered between drawing and presentation period without proper authority from the Drawer. Some of such alterations are considered as material and some are immaterial.*

- 1) **MATERIAL ALTERATION:** An alteration is called material alteration if it alters
- The character or operation (i.e. the legal effect) of negotiable instrument; or
  - The rights and liabilities of any of the parties to a negotiable instrument.

**EXAMPLES OF MATERIAL ALTERATION:**

- Alteration of the date of instrument,
- Alteration of amount payable,
- Alteration of time of payment.

69) This is based upon the principal of law of guarantee that when a principle debtor is discharged, the sureties are also discharged

**2) EFFECT OF MATERIAL ALTERATION [SEC 87 & 88]<sup>70</sup>:****a) Instrument becomes void:**

- i) All the parties to the negotiable instrument, not consenting to material alteration, are discharged.
- ii) However, if an alteration is made with the consent of prior parties then the instrument is not void.  
(i.e., parties are not discharged and are liable).

**b) Alteration by Endorsee:** Any material alteration made by an endorsee shall have the effect of discharging his endorsers, from all liabilities to him, in respect of the consideration thereof.

**c)** In such a case, an Acceptor or Endorser is liable only for the original tenor of the instrument and not for its altered tenor.

**3) MATERIAL ALTERATIONS AUTHORIZED BY THE ACT:** Following material alterations<sup>71</sup> have been authorized by the Act and do not require any consent from prior parties:

- a) Filling blanks of an inchoate instrument [Sec 20]
- b) Conversion of a blank endorsement into a full endorsement [Sec 49]
- c) Crossing of cheques [Sec 125]
- d) Conversion of general crossing into special crossing or not negotiable crossing or A/c Payee crossing (but not vice-versa)

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:****1. SOME MORE EXAMPLES FOR MATERIAL ALTERATION:**

- A. Alteration in the place of Payment
- B. Alteration in rate of Interest
- C. Addition of a new party to an instrument
- D. Alteration of one of the clauses of the instrument containing a penal action
- E. Alteration by tearing material part of the instrument.
- F. Alteration by increasing or affixing stamps (Challamma v Padmanabhan Nair 1970 KLR 682).
- G. Alteration by erasure of an "account payee" crossing (J. Ladies Beauty v State Bank of India AIR 1984 Guj33).

**2. SOME MORE EXAMPLES FOR ALTERATIONS WHICH ARE NOT CONSIDERED AS MATERIAL ALTERATION:**

- A. Correction of honest mistakes in Instrument
- B. An Alteration made before the instrument is issued and made with consent of Parties
- C. Conversion of a bearer instrument into an order instrument.
- D. Elimination of the words 'or order' from an endorsement
- E. Addition of the words 'or demand' to a note in which no time or payment is expressed

**3. PROTECTION TO A PERSON PAYING A MATERIALLY ALTERED INSTRUMENT [SECTION 89]:** The payer of a materially altered instrument is discharged from all liabilities on the instrument if the following two conditions are fulfilled:

- a) The alteration is not apparent (latent) and
- b) The payment is made in due course.

**4. BY MATERIAL ALTERATION THE IDENTITY OF ORIGINAL INSTRUMENT IS DESTROYED**

- a) The parties who had agreed to be liable on the original instrument can't be made liable on the new contract contained in the altered instrument to which they never consented (Gour Chandra vs Prasanna Kumar 33 Cal 812).
- b) It makes no difference whether the alteration is made by a party who is in possession of the same, or by a stranger while the instrument was in the custody of a party, because the party in custody of instrument is bound to preserve it in its integrity.
- c) The rule is defended on the ground that no man shall be permitted to take the chance of committing a fraud without running any risk of loss by the event when it is detected.

70) In Hong Kong and Shanghai Bank vs. Lee Shi (1928), it has been held that an accidental alteration will not render the instrument void.

It is necessary to show that the alteration has been made improperly and intentionally. The effect of making the material alteration, without the consent of effected party, is exactly same as that of cancelling it. In short, we can conclude that all the parties to a negotiable instrument, not consenting to the material alteration, gets discharged.

71) Ex: A promissory note was made without mentioning any time of payment. The holder added the words "on demand" on the face of the instrument. As per the provisions of the Negotiable Instruments Act, 1881 this is not a material alteration. Because a promissory is treated as payable on demand if date of payment is not specified. Hence, adding the words "on demand" does not alter the nature of instrument.

5. The party who consents to the alteration as well as the party who makes the alteration are disentitled to complain against such alteration
- E.g. the drawer of the cheque himself altered the date of the cheque for validating or re validating the same instrument, he cannot take advantage of it by saying that the cheque becomes void as there was a material alteration thereto. It is always open to a drawer to voluntarily re-validate a negotiable instrument including a cheque [Veera Exports v T. Kalavathy (2002) 1SCC97].
6. THE FOLLOWING ALTERATIONS DO NOT AFFECT THE LIABILITY OF PARTIES THERETO:
- If the alteration is unintentional and purely accidental (e.g. accidental disfigurement of document).
  - Alteration made by a stranger without the consent of holder and without any fraud and negligence on his part.
  - An alteration made to correct a clerical error or a mistake. For example, if instead of 1823, the date entered was 1832, the agent of drawer held entitled to correct mistake. Such correction is deemed to be giving effect to the original intention of the parties.
  - Alteration made to carry out common intention of original parties is permitted by Sec. 87. For example, where the words "or order" after the name of payee, inserted subsequently.
  - Alteration with the consent of parties liable thereto.
  - An alteration made before the completion or issue of negotiable Instrument.
  - A material alteration doesn't affect the liability of those parties who become liable after the alteration is made. Sec. 88 provides that the acceptor or Endorser is bound by his acceptance or indorsement notwithstanding any previous alteration of the instrument.
  - An alteration which is not material e.g. an incomplete name of a person converted into complete name of same person.

#### TEST YOUR KNOWLEDGE:

- When is an alteration in a negotiable instrument deemed to be a 'material alteration' under the NI Act, 1881? What are the consequences of such material alteration?
- Refer point 1&2 in the above answer.
- Explain the effect of material alteration specified under the NI act, 1881?
- Refer Point 2 in the above answer.
- D accepted a bill of exchange drawn in London. An Indorsee, in arrangement with the drawer, altered the place of drawing from London to Ottawa a city in Canada. Is D liable on the bill?
- No, since Material alteration takes place.
- In case of negotiable instruments does every alteration be considered as material alteration?
- No. Sometimes, a negotiable instrument is altered between drawing and presentation period without proper authority from the Drawer. Some of such alterations are considered as material and some are immaterial.

An alteration is called to be a material alteration only if it alters or attempts to alter, -

- The character of the instrument and affects or likely to affect, and
- The rights and liabilities of any of the parties to a negotiable instrument.

For Examples: Refer point 2 in additional information for academic interest above.

- State whether the following alterations are material alterations under the Negotiable Instruments Act, 1881?
    - The holder of the bill inserts the word "or order" in the bill,
    - The holder of the bearer cheque converts it into account payee cheque,

The following materials alterations have been authorised by the Act and do not require any authentication:

    - filling blanks of inchoate instruments [Section 20]
    - Conversion of a blank endorsement into an endorsement in full [Section 49]
  - A bill of exchange is accepted at B & C, but is subsequently altered by the holder by crossing the name of B & Co, and substituting the name of C & Co. Discuss the liability of the acceptor to the holder after such alteration.
- The acceptor of the bill is not liable to the holder (sec.87, page 348) as it amounts to material alteration.
- A promissory note was made without mentioning any time for payment. The holder added the words "on demand" on the face of the instrument. Does this amount to material alteration? [M19 (N) - 2M, N19 (N) - 4M]
- As per the provision of NI Act, 1881, this is not a material alteration as a promissory note where no date of payment is specified will be treated as payable on demand. Hence adding the words "on demand" does not alter the business effect of the instrument.

**(NOW REFER PRACTICAL QUESTION NO.37)**

## PART 11 - DISHONOUR OF INSTRUMENTS

A Negotiable Instrument may be dishonoured in either of following ways:

- 1) Dishonour by Non-Acceptance or
- 2) Dishonour by non-payment

**Q.No.46. Write a short note on Negotiable Instrument dishonoured due to non-acceptance? (A)**  
**[NEW SM, OLD SM, N18 (N) - 2.5M]**

**DISHONOUR BY NON-ACCEPTANCE (SEC 91):** A bill is dishonoured by non-acceptance if it is duly presented for acceptance, but it is not accepted.

- 1) **Applicability:** Dishonour by Non-Acceptance can occur with respect to Bills of Exchange only.<sup>72</sup>
- 2) **In the following cases a Bill of exchange is treated as dishonoured by non-acceptance:**
  - a) If a bill is not accepted by Drawee within 48 hours of presentment.
  - b) Where Drawee gives a qualified acceptance and the holder does not accept for the same.
  - c) Where Drawee is incompetent to contract
  - d) Where Drawee cannot be found with reasonable search
  - e) Where Drawee is a fictitious person
  - f) Where there are 2 or more Drawees who are not partners, and the bill is not accepted by all the Drawees.

**Effect:** The holder gets an immediate right to sue all the prior parties, without waiting for maturity of the bill.

**TEST YOUR KNOWLEDGE:**

1. What are circumstances that a bill of exchange can be dishonoured by non-acceptance. [MTP - N19(N), MTP - M19(N)]
- B. Refer dishonor by non- acceptance in the above answer

**Q.No.47. Write a short note on Negotiable Instrument dishonoured due to non-payment? (A)**  
**[NEW SM, OLD SM, N18 (N) - 2.5M]**

**DISHONOUR BY NON-PAYMENT (SEC.92):** A promissory note, bill of exchange or cheque is said to be dishonored by non-payment -

- 1) When the Maker of the promissory note or,
- 2) Acceptor of the bill of exchange or,
- 3) Drawee of the cheque

Defaults in payment on its presentment.

**NOTE:** Also, a negotiable instrument is dishonoured by non-payment when presentment for payment is excused and the instrument remains unpaid even after becoming due.

**TEST YOUR KNOWLEDGE:**

1. Distinction between dishonour by non-acceptance and dishonour by non-payment:
- A. On dishonour by non-acceptance, Drawee cannot be sued because he is not a party to the bill. But on dishonour by non-payment, the Acceptor (Drawee) can be sued.

**Q.No.48. 'Noting' under the NI Act, 1881? (A)** [NEW SM, OLD PM, M19 (N) - 1M, RTP - N18]

**NOTING:**

- 1) Noting means recording the fact of dishonour of a negotiable instrument on the instrument.

<sup>72)</sup> A Promissory note or a Cheque cannot be dishonoured by non-acceptance since a Promissory note or a Cheque does not require acceptance.

- 2) A person appointed under Notaries Act is authorized to make noting. He is officially designated as Notary Public.
- 3) The dishonoured bill is handed over to a notary public who presents it again for acceptance or payment as the case may be, and if the Drawee or acceptor still refuses to accept or pay the bill, then notary public records:
  - a) The date of dishonour
  - b) The fact of dishonour.
  - c) The reasons, if any, assigned for such dishonour.
  - d) The Notary charges<sup>73</sup>.
- 4) Noting must be made within a reasonable time after dishonour of instrument.
- 5) **Is Noting Compulsory or Optional?** In case of foreign bills, Noting is compulsory. In case of inland bills it is optional. Since noting provides an additional evidence of dishonour, it is always better to get the dishonoured bill noted.

**Q.No.49. 'Protest' under the NI Act, 1881?****(A) [NEW SM, OLD PM, M19(N) - 1M, RTP - N18]**

**MEANING:** Protest is a formal certificate issued by the Notary Public stating the fact of dishonour of a bill or note. Protest must be done within a reasonable time after dishonour of instrument.

**CONTENTS OF PROTEST:** Protest is based upon noting. A valid protest must contain all the following particulars:

- 1) A literal transcript of the instrument i.e. everything written or printed on the negotiable instrument.
- 2) The name of the person for whom and against whom the instrument has been protested.
- 3) **The fact and reasons for dishonour:**
  - a) a statement that payment, or acceptance, or better security, was demanded from the person liable to pay on the negotiable instrument by the notary public and
  - b) the terms of answer given by such person, or a statement that he gave no answer, or that he could not be found.
- 4) The place and time of dishonour. When better security has been refused, the place and time of refusal.
- 5) The subscription (signature) of the notary public.
- 6) In case of acceptance for honour or payment for honour, the name of the person accepting or paying and the name of the person for whose honour it is accepted or paid.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. **Notice of protest:** If a note or bill is required by law to be protested then notice of such protest must be given instead of notice of dishonour, in the same manner and subject to the same conditions; but the notice may be given by the notary public who makes the protest (Sec. 102).
2. **Protest for Non-payment after dishonour by Non-acceptance:**
  - a) If bills of exchange -
    - drawn payable at specified place, other than the place of Drawee's residence, and
    - which are dishonoured by non-acceptance then
  - b) such bills may,
    - without further presentment to the drawee,
    - be protested for non-payment,
    - in the place specified for payment, unless paid before or at maturity (Sec. 103).
3. **Distinction between inland and foreign bills:** Foreign bills must be protested for dishonour when such protest is required by law of the place where they are drawn (Sec. 104). Thus, foreign bills must be protested as the law of most countries has made protest compulsory in case of dishonour of a bill. Inland bills need not be protested for dishonour; protest in this case is optional.
4. The merit of protest and noting is that it would become good prima-facie evidence in a court of law that the instrument has been dishonoured. It is pertinent to note that as per Sec. 119, court is bound to recognize a protest, but it may or not recognize noting.

73) The fees charged by Notary Public for noting is called Notary's charges.

5. **REASONABLE TIME:** In determining what is reasonable time for –

- a) Presentment for acceptance or payment,
- b) Giving notice of dishonour and
- c) Noting,

regards shall be had to the nature of the instrument and the usual course of dealing with respect to similar instrument; and, in calculating such time, public holidays shall be excluded (Sec. 105).

**Q.No.50. 'Protest for better security' under the NI Act, 1881? (A) [NEW SM, OLD PM, M19(N) - 1M]**

**PROTEST FOR BETTER SECURITY:**

- 1) Holder of a NI may request the notary public to demand better security from the acceptor in case the acceptor of the bill becomes insolvent<sup>74</sup> (*or his credit has been publicly impeached*) before maturity date of the bill.
- 2) The holder must make such request within a reasonable time.
- 3) If the better security is refused by the acceptor, then the holder may require the notary public to make noting and issue a certificate of protest.
- 4) Such certificate is called as protest for better security.

**NOTE:** *Noting and Protesting are not applicable to a cheque.*

**TEST YOUR KNOWLEDGE:**

1. A bill of exchange has been dishonoured by non- payment. Now, Mr. Sandip, the holder wants a certificate of protest for such dishonoured bill. Advise, Mr. Sandip whether he can get the certificate of protest. Also, advise him regarding the provisions of Protest for better security. [RTP - N18(N)]

- A. **Protest (Sec 100):** If a promissory note or bill of exchange is dishonored due to non-acceptance or non-payment then the holder may cause such dishonor to be noted and certified by a notary public. Such certificate is called protest. Such Protest must be made within a reasonable time.

**Protest for better security:** Holder may requests the notary public to demand better security of the acceptor in case the acceptor of bill has become insolvent before the maturity of the bill. Holder must make such a request within a reasonable time. If the better security is refused by the acceptor, then the holder may require the notary public to make noting and issue a certificate of protest. Such certificate is called as protest for better security.

Thus, Mr. Sandip can get the certificate of protest by following the above provisions.

2. State with reasons whether the given statement is correct or not. "Notary Public is a government servant". (RTP - N13)
- A. The statement is correct. A Notary public is appointed by CG or SG. His functions are to attest deeds, contracts and other instruments that are to be used abroad and to give a certificate of due execution of such documents. He enjoys the confidence of the business world and any certificate given by him is presumed to be true by court of law.

**Q.No.51. In case of Dishonour of NI, state the object of giving notice of dishonor?**

**(C) [NEW SM, OLD SM]**

- 1) The object of notice of dishonour is **to inform (or warn)** -
  - a) **The party** or the person who is liable on instrument about the dishonour of the instrument.
  - b) **Drawer** to enable him to protect himself as against the Drawee or Acceptor who has dishonoured his bill.
- 2) The notice is necessary whatever the nature of the instrument *i.e. whether it is payable at sight or on demand or whether it is an accommodation bill.*
- 3) In order to make the drawer liable, on the dishonour by the drawee or the acceptor, it is necessary that a 'notice of dishonour' must have been given to him.
- 4) The omission on the part of holder to give due notice of dishonour would discharge the drawer not only from his liability upon the cheque, but also upon the original debtor consideration.
- 5) The doctrine of notice of dishonour is based upon the principle of just and equity.

<sup>74</sup>) his credit has been publicly impeached



**Q.No.52. Write down the legal rules regarding 'Notice of dishonour' under the NI Act, 1881? (C) [NEW SM, OLD SM]**

**NOTICE OF DISHONOUR (SECTIONS 93 TO 98):**

- 1) **When required:** A negotiable instrument is dishonoured either by non-acceptance or by non-payment. In both the cases it is required to send notice of dishonour.
- 2) **Notice by Whom:** Notice may be given by the -
  - a) Holder<sup>75</sup> of the negotiable instrument, or
  - b) any other party liable on the negotiable instrument<sup>76</sup>

**Note:**

*Notice of dishonour given by a stranger is not valid.*

*Even notice given by a party to the instrument is not valid, if at the time of giving such notice he is not liable on the instrument.*

- 3) **Notice to Whom:** It must be given to -
  - a) All the parties (Other than the maker or the acceptor or the drawee) whom the Holder seeks to make jointly or severally liable.
  - b) The duly authorized agents of the aforesaid party or parties.
  - c) Legal representatives, in case of death.
  - d) Receiver or official assignee in case of insolvency.
- 4) **Contents of Notice:** Notice must state the fact of dishonour and reason for dishonour.
- 5) **Effect of not giving notice:** 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.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

1. **When the party to whom notice of dishonour is dispatched was dead, but the party dispatching the notice is ignorant of his death, then the notice is sufficient (Sec. 97).**

**Q.No.53. Write a short note on serving of notice of dishonour under the NI Act, 1881? (D)[NEW SM]**

- 1) **FORM:** Notice may be in any form *i.e., oral or written*;
- 2) **POST:** A written notice may be sent by post to the intended person.
 

**Note:** *If the notice is duly directed and sent by post and miscarries, such miscarriage does not render the notice invalid (Sec.94).*
- 3) **TIME LIMIT:** It must be given within reasonable time after dishonour.
  - a) If the holder and the party to whom notice of dishonour is given, carry on business or live (as the case may be) in different place, such notice is given within a reasonable time if it is dispatched by the next post or on the day next after the day of dishonour.
  - b) If the said parties carry on business or live in the same place, such notice is given within a reasonable time if it is dispatched in time to reach its destination on the date next after the day of dishonour (Sec. 106).
- 4) **PLACE:** Notice must be served at the
  - a) Place of business or
  - b) Place of residence (if such party has no place of business).
- 5) **TRANSMISSION BY A PARTY RECEIVING THE NOTICE:** Any party who receives notice of dishonour may give notice of dishonour to his prior party, whom he wants to make liable, within reasonable time (Refer Point 3 for Reasonable time.).

<sup>75</sup> Agent with whom instrument is deposited for presentment, or principal himself can serve the notice.

<sup>76</sup> Party receiving notice shall intimate prior party if he intends to make such prior party liable.

**NOTE:**

**Agent of presentment:** When the instrument is deposited with an agent for presentment, the agent is entitled to the same time to give notice to his principal as if he were the holder giving notice of dishonour, and The principal is entitled to a further like period to give notice of dishonour (Sec. 96).

**Q.No.54. State the circumstances where Notice of Dishonour is not required?**

(D) [NEW SM, OLD SM]

**WHEN NOTICE OF DISHONOUR IS NOT NECESSARY (SEC.98):** In the following cases, notice of dishonour is not necessary either for dishonour by non-acceptance or for dishonour by non-payment

- 1) When notice of dishonour is dispensed with, by a party<sup>77</sup>.
- 2) Where the drawer of the cheque himself has countermanded payment,
- 3) When the party entitled to notice cannot be found even after due search.
- 4) Where the party bound to give notice is unable to give notice without any fault of his own<sup>78</sup>.
- 5) When the party charged could not suffer damage for want of notice.
- 6) No Notice of dishonor is necessary:
  - a) to charge the drawers, when the acceptor is also a drawer
  - b) in the case of a promissory note which is not negotiable;
  - c) Promise to pay: When the party entitled to notice, knowing the facts, promises unconditionally to pay the amount due on the instrument.

**TEST YOUR KNOWLEDGE:**

1. "Notice of dishonour is a material part of cause of action". What are the exceptions to this rule?
  - A. Refer point- when the notice of dishonor is not necessary in the above answer.
2. X, drawer of a Bill informs Y, the holder of the bill, that the bill would be dishonoured on the presentment for payment. Is notice of dishonour necessary in this case? [OLD PM]
- A. Notice of dishonour is not necessary u/s 98 since Drawer already know that the bill will be dishonored on the presentment for payment.
3. P draws a bill on Q payable three months after sight. It passes through several hands before R becomes its holder. On presentation by R, Q refuses to accept. Discuss the duties and rights of R on the bill.
- A. On dishonour of the bill by non-acceptance, it is the duty of R, the holder, to give notice of dishonour to all prior parties. He may also have the instrument noted and protested. Thereafter R is entitled to make P, the drawer of the bill, liable as principal debtor and the intervening endorsers as sureties.
4. Is notice of dishonour necessary in the following case: X having a balance of Rs. 1,000 with his banker and having no authority to over draw, drew a cheque for Rs. 5,000/-. The cheque was dishonoured when duly presented for payment.
- A. Notice of dishonour is not necessary for the reason that party charged could not suffer damage for want of notice as per Sec 98 of the N.I Act, 1881.

(NOW REFER PRACTICAL QUESTION NO.38)

**Q.No.55. State, in brief, the grounds or circumstances on the basis of which a banker can dishonour / refuse a cheque under the provisions of the NI Act, 1881.** (D) [OLD PM, N11 - 8M, N13 - 8M]

**CASES IN WHICH A BANKER IS JUSTIFIED / BOUND TO DISHONOUR A CUSTOMER'S CHEQUE:**

**CASE A:** A banker **must** refuse to honour a customer's cheque in the following cases:

- 1) **Stop Payment:** When the banker receives instructions<sup>79</sup> from the customer not to honour (i.e., stop payment) a particular cheque issued by him.
- 2) **Loss of cheque:** When the banker receives a notice of loss of cheque from his customer.

77) If Endorser made Facultative Endorsement

78) For instance strike by Postal department

79) When the customer countermands the payment of Cheque.

- 3) **Notice of closure:** When the banker receives a notice in respect of closure of account from customer.
- 4) **Garnishee order:** When the banker receives a Garnishee Order, i.e., a prohibition order by any court attaching the money in the customer's account.
- 5) **Signature mismatch:** When the signature of the drawer does not tally with the specimen signature kept by the bank.
- 6) **Material alteration:** When there is a material alteration on the cheque and such alteration has not been authenticated by his customer by putting his signature.
- 7) **Defect in title:** When the banker suspects or has reason to believe that the title of the person presenting the cheque is defective.
- 8) **Irregular endorsement:** When there is an irregular endorsement on the Cheque.
- 9) **Death:** When the banker receives a notice of death of his account holder (i.e. Customer).
- 10) **Insolvency:** When the banker receives a notice of insolvency of his customer.
- 11) **Insanity:** When the banker receives a notice of insanity of account holder.
- 12) **Assignment:** When the banker receives a notice of assignment of his credit balance from a customer.

**CASE B:** A banker **may** refuse to Honour a customer's cheque in the following cases:

- 1) **Undated cheque:** When the cheque is undated.
- 2) **Postdated Cheque:** When the cheque is presented before the actual date on which it is written to be payable.
- 3) **Stale cheque:** When the cheque is presented after 3 months from the date of its issue.
- 4) **Presentment at different branch:** When the cheque is presented at the branch other than the branch where the customer who has issued the cheque, has the account.
- 5) **Presentment after banking hours:** When the cheque is presented after banking hours.
- 6) **Insufficient Funds:** When funds in the customer's account are insufficient to honour the presented cheque.
- 7) **Funds not applicable:** When funds in the customer's account are not applicable for the cheque presented.

**TEST YOUR KNOWLEDGE:**

1. What is a stale cheque?
  - A. A cheque is valid only for a period of 3 months from the date mentioned on it. If the payment is not claimed within 3 months then it becomes a stale cheque. Of course, Drawer of cheque is still liable to pay the amount.
2. State the grounds, on the basis of which a cheque **may** be dishonoured by a banker, inspite of the fact that there is sufficient amount in the account of the drawer.
  - A. Write only Case B in the above answer.
3. PQR Ltd received a cheque for Rs. 50,000 from the customer Mr. LML. After a week, company came to know that the proceeds were not credited to the account of PQR Ltd. due to some 'defects', as informed by the banker. What according to you are the possible defects?
  - A. In case of following defects, banker is justified to dishonour cheque:
    - If cheque is undated.
    - If it is stale cheque (i.e., presented beyond period of 3 months)
    - If it is inchoate
    - If it is postdated and presented before date
    - If it contains material alteration or irregular signature or irregular endorsement.
    - Balance in account is insufficient.

**NOTE:** This concept is excluded in New SM. But without this concept students can't understand further concepts. That is why we have decided to continue this question.

Q.No.56. State the liability of a banker for wrongful dishonour of a cheque?

(D) [OLD SM]

**1) SITUATION:**

- a) Sometimes it may happen that a banker declines payment of a cheque without having valid grounds for doing so,

*Ex: Refusing payment for insufficient funds while there are sufficient funds in the customer's A/c.*

- b) In such cases, banker is liable for wrongful dishonour of the cheque.

**2) LIABILITY OF A BANKER TOWARDS THE DRAWER FOR WRONGFUL DISHONOUR OF A CHEQUE:**

- a) When a banker wrongfully dishonours a cheque, he is in breach of contract with its customer. Hence, he is liable to pay damages to him.
- b) The drawer of the cheque may suffer from loss of reputation because of dishonour of his cheque.
- c) In such a case, even if the drawer does not suffer any monetary loss, loss of reputation can be measured as a great damage.<sup>80</sup>

**3) LIABILITY TOWARDS THE PAYEE (OR HOLDER) OF THE CHEQUE:**

- a) Generally, banker is liable to the Drawer of the cheque (*Drawer being his customer*), and not to the holder. Since there is no privity of contract between the banker and the holder.
- b) But in the following 2 cases a holder can take action against the banker:
- Where a banker pays a generally crossed cheque over the counter of the bank, or a specially crossed cheque otherwise than to the banker to whom it is crossed (i.e. payment out of due course).
  - Where the holder does not present the cheque with the banker within a reasonable time, and the bank fails in the meantime (Sec.84),
- c) The holder of the cheque can directly prove his debt against the banker in its insolvency proceedings. Here the drawer stands discharged as against the holder.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST**

If a banker, without justification, dishonours his customer's cheque, he makes himself liable to compensate the customer for any loss or damage. The words 'loss or damage' used in sec. 31, not only mean the pecuniary loss but also loss of credit or injury to reputation of the customer. Thus, if the customer is a trader or a businessman, the damages may be substantial. But a non-trader is not entitled to recover substantial damages for the wrongful dishonor of his cheque.

In "*Gibbs vs. west minister bank*", Mrs Magaret Gibbons, a non-trader, was awarded only nominal damages because of the absence of any special loss.

**NOTE:** This concept is excluded in the New SM. But without this concept students can't understand further concepts. That is why we have decided to continue this question.

**TEST YOUR KNOWLEDGE:**

1. "Smaller the amount of the cheque dishonoured, greater is the loss suffered by the drawer". Comment?

A.

- a) When a banker wrongfully dishonours a cheque, he is in breach of contract with its customer, and is liable to pay damages to him.
- b) The drawer of a cheque may suffer from loss of reputation because of dishonour of his cheque.
- c) In such a case, even if the drawer does not suffer any monetary loss, loss of reputation can be measured as a great damage. The principle is that "Smaller the amount of the cheque dishonoured, greater is the loss suffered by the drawer".

(NOW REFER PRACTICAL QUESTION NO.39)

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80) The principle is that "Smaller the amount of the cheque dishonoured, greater is the loss suffered by the drawer".

**Q.No.57. What are the consequences of a cheque being dishonoured for insufficiency of funds in the account?**  
**(A) [NEW SM, OLD SM, OLD PM N18 (N) - 2.5M]**

**PUNISHMENT FOR DISHONOUR OF CHEQUE DUE TO INSUFFICIENCY OF FUNDS (SEC.138):**

When a cheque is dishonoured due to insufficiency of funds in Drawer's bank account, then he is punishable with -

- a) Imprisonment for a term up to 2 years<sup>81</sup> or
- b) Fine which may extend up to twice the amount of the cheque, or
- c) Both

**1) CONDITIONS FOR ATTRACTING LIABILITY UNDER SECTION 138:**

- a) The cheque is drawn to discharge a legally enforceable debt or other liability;
- b) **Cheque must be presented within the validity period.** *In other words, cheque must be presented within 3 months from the date on which it is drawn or within the validity period stated on in cheque, whichever is earlier;*
- c) Cheque is dishonoured by the bank due to insufficiency of funds.
- d) **Demand for payment through the notice: Within 30 days of receipt of information from Bank,** Payee or Holder in due course has demanded payment on cheque from Drawer, in written form.
- e) **Failure of drawer to make payment:** Drawer failed to pay money within 15 days from the date of receipt of such notice;
- f) **Time limit for filing the complaint:** Payee or Holder in due course shall make a written complaint within one month of expiry of aforesaid 15 days u/s 138.

**2) PRESUMPTION IN FAVOUR OF HOLDER (SEC.139):**

- a) It is presumed that holder<sup>82</sup> has received the cheque, for repayment of any debt or other liability, either in whole or in part.
- b) If needed, Drawer shall prove that the cheque was not given in discharge of a legally enforceable debt or liability.

- 3) *Drawer can't defend that when he had issued the cheque he had no reason to believe that, on presentment, the cheque may be dishonoured, for the reasons stated in that section. (Sec 140)*

**TEST YOUR KNOWLEDGE:**

1. State the circumstances under which the Drawer of a cheque will be liable for an offence relating to dishonour of the cheque under the Negotiable Instruments Act, 1881.
- A. Refer point- conditions for attracting liability under sec.138 in the above answer.

**(NOW REFER PRACTICAL QUESTION NO.40, 41, 42, 43, 44)**

**Q.No.58. What is the extent of liability of the company and the person(s) incharge of the company in respect of dishonour of cheques?**  
**(B) [NEW SM, OLD SM, OLD PM]**

1. **LIABILITY OF COMPANY AND PERSON INCHARGE (SEC.141)**<sup>83</sup>: If the person committing an offence under section 138 is a company then

- a) Company and
- b) every person who, at the time the offence was committed, was incharge of and was responsible for the conduct of the business of the company,

He shall be deemed to be guilty of the offence and liable to be proceeded against and punished accordingly.

81) In other words, maximum of 2 years.

82) Presumption prescribed here is a "rebuttable presumption". As the provisions clearly provides that the person issuing the cheque is at liberty to prove to the contrary. The effect of this presumption is to place the evidential burden on the accused.

83) For the purpose of this section

- a) "Company" means anybody corporate and includes a firm or other association of individuals; and
- b) "Director" to a firm, means a partner in the firm.

2. **EXCEPTION:** A person will not be liable in a case:

- a) If such person proves that the offence was committed without his knowledge or
- b) If he had exercised all due diligence to prevent the commission of such offence.
- c) If a person is nominated as a director of a company by virtue of his holding any office or employment in the CG or SG or a financial corporation owned or controlled by the CG or SG, as the case may be.

(NOW REFER PRACTICAL QUESTION NO.45, 46)

## PART 12 - MISCELLANEOUS TOPICS

**Q.No.59. Payment of interest on negotiable instruments**

**(B) [NEW SM]**

**MAKING PAYMENT ON INSTRUMENT:** Party primarily liable on the instrument (i.e. Maker of note, Drawee of Bill) is liable to pay principal amount stated in the instrument along with interest, on the date of Maturity.

### **CALCULATION OF INTEREST**

- 1) **Rate:** Interest shall be calculated at the rate specified in the instrument. If it is not specified, then interest is calculated at the rate of 18% p.a.
- 2) **Amount:** Interest shall be calculated on principal amount due on the instrument.
- 3) **Period:** Interest is calculated for the period,
  - a) **From:** Date of the instrument,
  - b) **To:** (i) Date of realization of such amount, or (ii) Such date as decided by the court, when suit is filed (as the case may be).

**NOTE:** If holder takes action on the Endorser, for dishonour of an instrument by non-payment, then the Endorser is liable to pay interest

- 1) **From:** the time he receives notice of dishonour
- 2) **Till:** the date of payment.

(NOW REFER PRACTICAL QUESTION NO.47)

**Q.No.60. Explain the provisions of the act relating to the liabilities of parties to negotiable instruments drawn accepted or endorsed without consideration? (D) [NEW SM, OLD SM]**

### **LIABILITIES ON INSTRUMENT MADE, DRAWN WITHOUT CONSIDERATION:**

- 1) **Failure of Consideration [Sec 43]:** If a negotiable instrument made, drawn, accepted, endorsed, or transferred
  - a) Without consideration<sup>84</sup>, or
  - b) For a consideration which fails<sup>85</sup>,
 Then it creates no obligation of payment between the parties to the transaction.
- 2) **Exception:**
  - a) If any person receives a negotiable instrument without any consideration but transfers the instrument to a holder for consideration (i.e. HDC),
  - b) Then such HDC and every subsequent holder may recover amount due from the transferor for consideration and from any prior party.

84) X accepts a bill for the accommodation A (drawer). A transfer it to B, without consideration. In this case, neither X nor A has liability to pay bill amount to B as the instrument is drawn or transferred without consideration.

85) X makes a note in favour of Y in anticipation of Y's supplying a bale of cotton. Y fails to deliver the cotton and hence he cannot claim payment from X.

**3) Effect of partial absence or failure of money consideration [Sec 44]:**

- a) If consideration is originally absent in part, or subsequently fails in part,
- b) Parties standing in immediate relation to each other cannot recover more than actual consideration but this rule is not applicable to Holder in Due Course.

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:****No right of Accommodated party to recover from Accommodating Party**

- a) A party for whose accommodation a NI has been made, drawn or accepted or endorsed shall not recover the amount on the instrument from any person who became a party to such instrument for his accommodation (*if he has paid the amount thereof*)<sup>86</sup>.
- b) A party to the instrument who has induced any other party to make, draw, accept, endorse or transfer the same to him for a consideration which he has failed to pay or perform in full shall not recover an amount exceeding the value of the consideration (if any) which he has actually paid or performed.

**Partial failure of consideration not consisting of money [Sec. 45]:**

- a) *Situation: If a part of the consideration for which a person signed a negotiable instrument, though not consisting of money, is ascertainable in money without collateral enquiry, and that part of consideration has not been made.*
- b) *Effect: then claim of the holder standing in immediate relation with the maker of the instrument, shall be proportionately reduced.*
- c) *Exception: If ascertainment of part consideration not consisting of money is possible only with a collateral enquiry then sum cannot be proportionately reduced. It has to be paid in full.*

*E.g. X reminds Y that Y is due Rs. 500/- to X for more than a year. Y hands over a cheque to X, without specifying the amount (Blank cheque). Later, Y remembers that he had already returned Rs.300 to X. Now, the cheque is dishonoured by the Banker after Y countermands its payment. The liability of Y on the dishonoured cheque is only Rs.200/-.*

**TEST YOUR KNOWLEDGE:**

1. A draws a bill on B for Rs. 500 payable to his order. A accepts the bill but subsequently dishonours it by non-payment. A sues B on the bill. B proves that it was accepted for value as to Rs. 400 and as accommodation to A as to the balance. How much can A recover from B?  
A. **Hint:** Rs. 400 as per Section 44 of the Negotiable Instruments Act 1881
2. A owes a certain sum of money to B. A does not know the exact amount and hence he makes out a blank cheque in favour of B, signs and delivers it to B with a request to fill up the amount due, payable by him. B fills up fraudulently the amount larger than the amount due, payable by A and endorses the cheque to C in full payment of dues of B. Cheque of A is dishonoured. Referring to the provisions of the Negotiable Instruments Act, 1881, discuss the rights of B and C.  
A. According to Section 44 of NI Act, 1881, B who is a party in immediate relation with the drawer of the cheque is entitled to recover from A only the exact amount due from A and not the amount entered in the cheque.  
However, the right of C, who is HDC, is not adversely affected and he can claim the full amount of cheque from B.
3. A contract to supply 100 fountain pens of a certain brand to B at Rs. 5 per pen. B executes a promissory note for Rs. 500 in favour of A for the price. After the pens have been delivered, B finds that one-fourth of the pens are damaged are unmerchantable. In a suit by A against B on the note, B claims a set-off of Rs. 200 for the damaged pens. Is he entitled to do so?  
A. No, as the failure of consideration cannot be ascertained without a collateral enquiry. (Sec 45)
4. A agrees to supply a quantity of paper to B. B accepts a bill for Rs.1, 000 drawn by A being the price of the paper. The paper is delivered to B. But it turns out to be not of the quality stipulated for and is worth Rs.500 only. B retains the paper. can A recover from B the full amount of the note?  
A. Yes, A can recover the full amount of the note (sec 45.))
5. Explain the rights and liabilities of parties in case of a bill drawn without or inadequate consideration?  
A. Refer rights and liabilities of parties in the above answer.

**(NOW REFER PRACTICAL QUESTION NO.48, 49)**

**Q.No.61. State Rights and obligations of parties to an instrument obtained by unlawful means and after dishonour or when overdue. (B) [NEW SM]**

- 1) **FINDER OF LOST INSTRUMENT:** If a negotiable instrument is lost then the possessor is not entitled to receive the amount from Maker, Acceptor, Holder, or from any party prior to such holder.

<sup>86</sup> For mutual accommodation of X and Y on 01/04/2019, X drew a 4 months bill on Y for Rs. 4,000, Y returned the bill after acceptance of the same date. X discounts the bill from his bankers for Rs. 3920 and remit 50% of the proceeds to Y. On maturity date, Y (Acceptor) is liable to X (Drawer) to the extent of Rs. 2000 only. If Y has paid Rs. 2,000 to X then X cannot recover any amount from Y.

- 2) **INSTRUMENT OBTAINED BY UNLAWFUL MEANS OR FOR UNLAWFUL CONSIDERATION [SECTION 58]:** If the instrument is obtained from Maker, Acceptor or Holder by way of fraud (unlawful means) or for unlawful consideration then endorsee is not entitled to receive amount.

**EXCEPTION:** However, holder in due course is entitled to claim the amount.

- 3) **INSTRUMENT ACQUIRED AFTER DISHONOUR OR WHEN OVERDUE [SECTION 59]:** If a holder acquires any instrument after its dishonour or after maturity, along with notice thereon, then holder has the rights thereon of his transferor (as against the other parties).

4) **LIABILITIES ON ACCOMMODATION NOTE OR BILL:**

- a) If the bill or note is for the purpose of enabling some party thereto to raise money thereon, it is called an accommodation note or bill.
- b) Any person, who in good faith and for consideration becomes the holder of such instrument, after maturity, can recover amount on the instrument from any prior party.<sup>87</sup>

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:** If the finder obtains payment, the person who pays it in due course may be able to get a valid discharge for it. But the true owner can recover the money due on the instrument as damages from the finder.

**(NOW REFER PRACTICAL QUESTION NO.50, 51)**

**Q.No.62. Once a bearer instrument always a bearer instrument. Comment. (OR) The character or nature of a bearer instrument does not change or always remain the same. Comment (C) [OLD SM]**

- 1) Bearer instrument is an instrument
- a) where the name of the payee is blank or
- b) Where the name of payee is specified with the words "or bearer" or
- c) Where the last indorsement is blank.
- 2) Such instrument can be negotiated by mere delivery
- 3) The instrument may be a promissory note or a bill of exchange or a cheque.
- 4) A holder of negotiable instrument endorsed in blank, may, without signing his own name, by writing above the endorser's signature, instruct that payment must be made to another person. In such a case the feature of the instrument is changed and the instrument is treated as order instrument. (Sec.49)
- 5) If a cheque is actually expressed to be payable to bearer, the drawee gets discharged by payment in due course to the bearer thereof, inspite of any endorsement whether in blank or full appearing thereon. (Sec. 85(2))
- 6) Thus, the given statement "once a bearer instrument always a bearer instrument" is correct relating to cheque but not to promissory notes and bills of exchange. In other words, the original character of the cheque is not altered so far as the paying bank is concerned, provided the payment is made in due course.

## SECTION 2: DIFFERENCES FOR STUDENTS SELF STUDY

**Q.No.63. Distinguish between a 'Bill of Exchange' and a 'Promissory Note' with reference to the provisions of the NI Act, 1881. (A) [OLD SM, M12 - 8M]**

### DISTINCTION BETWEEN A PROMISSORY NOTE AND A BILL OF EXCHANGE:

PARTICULARS	PROMISSORY NOTE	BILL OF EXCHANGE
Definition	A Promissory note is an instrument in	A Bill of exchange is an instrument in

- 87) Generally, holder must have obtained the instrument before due date to become HDC. In case of accommodation instrument, holder will get this privilege even though he has received the instrument after maturity date provided he obtained instrument in good faith and for consideration. In other words, Holder is able to enjoy the special privilege of HDC.

*E.g.: The acceptor of a bill of exchange deposited certain goods as a collateral security with the drawer, for the payment of the Bill, with power to the drawer to sell the goods and apply the proceeds in discharge of the bill if it were not paid at maturity. The bill not having been paid at maturity, the drawer sold the goods and retained the proceeds, but endorsed the bill to A. A's title is subject to the same objection as the drawer's title since A obtained instrument from drawer after its maturity. A cannot recover money from Acceptor.*



	writing ( <i>not being a bank note or currency note</i> ) containing an unconditional undertaking, signed by the Maker, to pay a certain sum of money only to a certain person, or to the order of a certain person, or to the bearer of the instrument.	writing containing an unconditional order, signed by the Maker, directing a certain person, to pay a certain sum of money only to a certain person, or to the order of a certain person or to the bearer of the instrument.
<b>Nature of Instrument</b>	In a promissory note there is a promise to pay money.	In a bill of exchange there is an order for making payment.
<b>Parties</b>	In the case of a promissory note there are only <u>two</u> parties, viz. the maker (debtor) and the payee (creditor).	In the case of a bill of exchange, there are 3 parties, viz., Drawer, Drawee and payee, and any <u>two</u> of these three capacities can be filled by one and the same person.
<b>Acceptance</b>	A promissory note does not require any acceptance, as it is signed by the person who is liable to pay.	A bill of exchange needs acceptance from the Drawee.
<b>Can Maker and payee be the same person</b>	It cannot be made payable to the maker himself, that is the maker and the payee <u>cannot</u> be the same person.	In the case of bill, the drawer and payee may be the <u>same</u> person.
<b>Liability of the person who makes / draws instrument</b>	The liability of the <u>Maker</u> of a note is <u>primary</u> and <u>absolute</u> .	The liability of the <u>Drawer</u> of a bill is <u>secondary</u> and <u>conditional</u> . He will become liable if the Drawee, fails to pay money due upon it, after accepting the bill.
<b>Relationship</b>	The maker of a promissory note stands in immediate relationship with the payee and is primarily liable to the <u>payee</u> or the <u>holder</u> .	The maker or Drawer of an accepted bill stands in immediate relationship with the <u>acceptor</u> and the <u>payee</u> .
<b>Presentment for payment</b>	It can be presented for payment <u>without</u> any previous acceptance from Maker.	If a bill is payable sometime after sight, it is required to be accepted ( <u>either by Drawee himself or by someone else on his behalf</u> ) <u>before</u> it can be presented for payment.
<b>Notice of dishonor</b>	Notice of dishonor is not required to be given to <u>maker</u> .	Notice of dishonor shall be given to drawer.
<b>Can it be drawn or accepted Conditionally?</b>	A promissory note <u>cannot</u> be drawn conditionally.	A bill of exchange too <u>cannot</u> be drawn conditionally, but it can be <u>accepted</u> conditionally with the <u>consent</u> of the <u>holder</u> .
<b>Can it be drawn in sets</b>	A promissory note <u>cannot</u> be drawn in Sets.	A bill of exchange can be drawn in Sets.
<b>Payable to bearer</b>	Note cannot be made payable to bearer by any person other than RBI or CG.	Bill can be made payable to bearer though it cannot be made payable to bearer on demand.

**Q.No.64. Write the similarities and differences between a 'Cheque' and a 'Bill of Exchange' under the provisions of the NI Act, 1881. (A)** **[OLD SM, M11 - 5M]**

**SIMILARITIES BETWEEN BILLS OF EXCHANGE AND CHEQUE ARE AS FOLLOWS:**

- 1) Both are bills of exchange.
- 2) Both have three parties, the Drawer, Drawee, and the payee.

- 3) The drawer and the payee may be one and the same person in both the instruments.
- 4) Both must be written and signed.
- 5) Both must contain an unconditional order to pay a certain sum of money.
- 6) Both may be endorsed.
- 7) Whereas, a cheque is also a bill of exchange but is drawn on a banker and payable on demand.

#### **DIFFERENCES BETWEEN A CHEQUE AND A BILL OF EXCHANGE:**

BASIS	BILLS OF EXCHANGE	CHEQUE
<b>Drawee</b>	Drawee may be Bank or any person.	Drawee is always a bank.
<b>Acceptance</b>	A bill requires acceptance if it is payable certain period after sight, or it contains an express term requiring acceptance.	Acceptance of a cheque is not required in any case.
<b>Liability of Drawer</b>	The liability of Drawer is secondary and conditional. However, until a bill is accepted, the liability of the drawer is primary.	The liability of Drawer is always primary. The Drawee bank is simply a custodian of moneys of the customer (i.e. Drawer).
<b>Bearer</b>	A bill cannot be bearer, if it is made payable on demand.	A cheque can be drawn to bearer and made payable on demand.
<b>Validity Period</b>	There is no validity period in case of bill.	The cheque remains valid only for 3 months from the date of its issue. A cheque becomes stale on the expiry of validity period.
<b>Stamping</b>	Bill must be stamped according to the law.	Cheque does not require stamping
<b>Crossing</b>	Bill cannot be crossed	A cheque can be crossed
<b>Revocation</b>	The order to pay cannot be revoked	The order to pay may be revoked by countermanding payment.
<b>Discharge by non-presentment</b>	If a bill is not presented for payment, the drawer is discharged from liability.	Even if a cheque is not presented for payment, the drawer is not discharged from liability. However, if the bank fails in the meantime, the drawer is not liable.
<b>Noting/Protest</b>	If a bill is dishonoured, it may be noted or protested.	A cheque cannot be noted or protested in case of dishonour.
<b>Criminal liability for dishonor</b>	In case of dishonour of a bill, Sec. 138 does not apply	The Drawer of a cheque is criminally liable for dishonour of a cheque, (sec. 138)
<b>Drawn in Sets</b>	A bill can be drawn in sets.	A cheque cannot be drawn in sets.
<b>Grace Days</b>	3 days of grace are allowed.	Grace days are not allowed.
<b>Notice of Dishonor</b>	Required	Not Necessary
<b>Maturity (Type of Instrument)</b>	A Bill may be payable on demand or otherwise than on demand.	A cheque is always payable on demand.

#### **Q.No.65. Bearer Instrument Vs. Order Instrument**

**(A)**

BEARER INSTRUMENT	ORDER INSTRUMENT
A negotiable instrument which is expressed to be payable to bearer.	A Negotiable instrument payable to a particular person or expressed to be payable to a particular person.
It can be negotiated by <u>mere delivery</u> .	It can be negotiated by <u>endorsement and delivery</u> .
A negotiable instrument on which the last endorsement is blank.	A negotiable instrument on which the last endorsement is Full.

It is a Document of Title. Any person having possession of Bearer instrument is entitled to receive the amount of instrument.	It is a Document showing Title. Person whose name is stated in the instrument is entitled to receive the amount on the instrument.
If Bearer instrument is lost or stolen, any person having possession of instrument can recover amount thereon. It is impossible to trace the person who received the amount.	If Order instrument is lost or stolen, the person having possession of the instrument cannot recover money thereon.

**Q.No.66. Distinction between a 'Holder' and 'Holder in Due Course'.**

**(A) [OLD SM, OLD PM]**

**DIFFERENCE BETWEEN HOLDER AND HOLDER IN DUE COURSE:**

Basis	HOLDER	HOLDER IN DUE COURSE
<b>Consideration</b>	A holder may become the possessor or payee of an instrument even without Consideration.	A holder in due course acquires possession of an instrument for consideration.
<b>Before maturity</b>	A person becomes a holder even if he obtains the negotiable instrument <u>after</u> the <u>maturity</u> .	A holder in due course must become the possessor payee of the instrument before the amount thereon become payable. Exception: Accommodation Bill
<b>Good faith i.e. Bona fide</b>	A person becomes a holder, even if he <u>does not obtain</u> the negotiable instrument in good faith.	A holder in due course as against a holder must have become the payee of the instrument in good faith i.e., without having sufficient cause to believe that any defect existed in the transferor's title.
<b>Right to sue</b>	A holder <u>cannot sue</u> all the prior parties.	A holder in due course <u>can sue all</u> the prior parties.
<b>Better title than transferor</b>	<u>Never</u> get a better title than transferor.	<u>He can acquire</u> a better title than the transferor.
<b>Privileges</b>	A holder is <u>not</u> entitled to the privileges, which are available for HDC	A HDC is entitled to various privileges as specified under the Negotiable Instruments act, 1881.

**Q.No.67. Point out the differences between "Transfer by negotiation" and "Transfer by assignment" under the provisions of the NI Act, 1881. (Or) 'Negotiability' Vs. 'Assignability'. (A) [OLD SM, M13 - 4M]**

BASIS	NEGOTIATION	ASSIGNMENT
<b>Title</b>	Holder in due course can get better title than that of transferor.	Assignee does not acquire the rights of a holder in due course. He gets the same rights as that of assignor.
<b>Notice</b>	Notice of transfer is not necessary to any party.	Notice of assignment must be served by the assignee on his debtor.
<b>consideration</b>	Consideration is presumed	Consideration needs to be proved.
<b>Transfer / endorsement</b>	Bearer instrument can be transferred by mere delivery. Order instrument can be transferred by endorsement and delivery.	Assignment has to be made by a written document and signed by the transferor. The procedure is same for both bearer and order instruments.
<b>Stamp duty</b>	Endorsement does not require payment of stamp duty.	Assignment requires payment of stamp duty.
<b>Applicability of Act</b>	If a negotiable instrument is transferred by way of negotiation, NI Act, 1881 applies.	Right to transfer by way of assignment was governed by, the Transfer of property Act, 1882.
<b>Scope</b>	Negotiation can be made for transferring negotiable instrument only.	Assignment can be made of any right.

### SECTION 3: ACADEMIC INTEREST QUESTIONS – FOR STUDENTS SELF STUDY

Q.No.68. State the presumptions as to negotiable instruments?

(D) [NEW SM, OLD SM]

**PRESUMPTION AS TO NEGOTIABLE INSTRUMENT (SEC 118):** Until the contrary is proved, following presumptions will apply:

1) **Consideration:**

- a) Every negotiable instrument was made or drawn for consideration<sup>88</sup>
- b) Such NI was accepted, endorsed, negotiated or transferred for consideration.

**Exception:** In case of Accommodation Bill or note, the accommodating party can prove that the instrument was created without consideration and he is not liable to the Accommodated party. However, he is liable to the HDC.

- 2) **Date:** Every negotiable instrument bearing a date, was made or drawn on that date.
- 3) **Time of acceptance:** Every bill of exchange was accepted within a reasonable time after its date and before maturity.
- 4) **Time of transfer:** Every transfer of a negotiable instrument was made before its maturity.
- 5) **Order of endorsements:** The instrument is endorsed in the order in which it is appearing on the instrument.
- 6) **Stamp:** Every lost promissory note or bill of exchange was duly stamped.
- 7) **Holder in Due Course:** Every holder of a Negotiable Instrument is a Holder in Due Course.

**TEST YOUR KNOWLEDGE:**

1. State the special rules of evidence regarding the “Presumptions as to negotiable instruments” under the NI Act, 1881? [RTP - M12]
- A. Refer point- presumptions as to negotiable instruments in the above answer.
2. An undated negotiable instrument is not always invalid. Comment. [RTP - M13]
- A. **Correct.** If an undated instrument otherwise possesses all the essentials, it is considered as a valid instrument and the date of execution can be proved by oral / other evidence. Even a holder in due course may write the true date and such an insertion is not considered as a material alteration of the instrument. Such an instrument shall be always payable on mentioned date.

Q.No.69. Write about the conversion of endorsement in blank to endorsement in full? (B)

[NEW SM, OLD SM]

**SEC.49:**

- 1) The holder of a negotiable instrument endorsed in blank may convert the endorsement into full,
  - a) by writing above the endorser's signature,
  - b) A direction to pay to any other person as endorsee,
  - c) Without signing his own name.
- 2) In such a case, the Holder does not incur the responsibility of an endorser<sup>89</sup>

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

E.g.: A is the payee holder of a bill. A endorses it in blank and delivers it to B. B endorses it in full to C or order. C without endorsement transfers the bill to D. D as the bearer is entitled to receive payment or to sue drawer, acceptor, or A who endorsed the bill in blank, but he cannot sue B or C. C can sue B as he received the bill from B by endorsement in full. If, however, C instead of passing the bill to D without endorsement passes it by a regular endorsement, D can claim against all prior parties.

Thus, if an endorsement in blank is followed by an endorsement in full, the instrument still remains payable to bearer and negotiable by delivery against all parties prior to the endorser in full, though the endorser in full is only liable to a holder who acquired title directly through his endorsement, and person deriving title through such holder.

<sup>88</sup>) It is not required to be mentioned on Instrument.

<sup>89</sup>) E.g.: A is the holder of a bill endorsed by B in blank. A writes over B's signature, the word 'Pay to C or order'. A is not liable as an endorser but such writing operates as an endorsement in full from B to C.

**Q.No.70. Can a demand draft be considered as Cheque? (Or) DD Vs. Cheque (C) [OLD PM]**

Section 131 of the NI Act, 1881 is intended to widen the scope of a crossed draft as to contain all incidences of a crossed cheque. This is for the purpose of foreclosing a possibility of holding the view that a draft cannot be crossed. Even if it is possible to construe the draft either as a Promissory note or as a bill of exchange, the law has given the option to the holder to treat it as he chooses. This can be determined from the Section 137 which says that where an instrument may be construed either as a promissory note or bill of exchange, the holder may, at his discretion, treat it as either and the instrument shall thence forward be treated accordingly. This means, once the holder has elected to treat the instrument as a cheque, it cannot but be treated as a cheque thereafter. This is an irretrievable corollary of exercising such an election by the holder himself. A pay order was accordingly held to be a cheque entitling the bank holding the instrument to lodge a complaint u/s 138.

**Q.No.71. State the legal provisions relating to Electronic cheques and Truncated Cheques? (C) [NEW SM]****ELECTRONIC CHEQUE / CHEQUE IN THE ELECTRONIC FORM** - means a cheque

- 1) Drawn in electronic form by using any computer resource, and
- 2) Signed in a secure system with
  - a) A digital signature (with / without biometric signature) and
  - b) Asymmetric crypto system or electronic signature, as the case may be.

**NOTE: For the purpose of this section:** The expressions "asymmetric crypto system", "computer resource", "digital signature", "electronic form" and "electronic signature" shall have the same meanings respectively assigned to them in the Information Technology Act, 2000.

**TRUNCATED CHEQUE:** 'A truncated cheque' means a cheque which is truncated during the course of clearing cycle, either

- by the clearing house<sup>90</sup> or
- by the bank (Paying or Clearing),

immediately on generation of an electronic image for transmission, substituting further physical movement of cheque in writing.

The collecting bank, instead of sending physical cheque, will send its electronic image for clearance. In order to ensure that the cheque is not presented again, the physical cheque (i.e. paper cheque) will be truncated. Once a paper cheque is 'truncated', its further movement can be only by electronic means and not by physical movement.

**Paying bank can ask for further details:** Sec.64(2) provides that where electronic image is presented, the drawee bank (i.e. bank paying the amount) is entitled to demand any further information regarding truncated cheque from the bank holding the truncated cheque, if it has reasonable suspicion about genuineness of apparent (on the face of) tenor of instrument.

**Q.No.72. Distinguish between 'Electronic Cheque' and 'Truncated Cheque'. (D)**

<b>ELECTRONIC CHEQUE</b>	<b>TRUNCATED CHEQUE</b>
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 a 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 a truncated cheque is on paper, duly signed in ink.
The electronic cheque is in electronic form.	Truncated cheque is in paper form.

90) The expression "clearing house" means the clearing house managed by RBI or a clearing house recognized as such by RBI.

**Q.No.73. Exclusion of Endorser Liability [Sec.52]****(C) [NEW SM]**

The Endorser of a negotiable instrument may,

- 1) by express words in the endorsement,
- 2) exclude his own liability thereon, or
- 3) make such liability or the right of the indorsee to receive the amount due thereon depend upon the happening of a specified event, although such event may never happen.
- 4) Where an endorser so excludes his liability and afterwards becomes the holder of the instrument all intermediates indorsers are liable to him.

**Example:** A is the payee and holder of a negotiable instrument. Excluding personal liability by an endorsement, "without recourse", he transfers the instrument to B, and B endorses it to C, who endorses it to A. A is not only reinstated in his former rights, but has the rights of an indorsee against B and C.

**TEST YOUR KNOWLEDGE:**

1. How an endorser can escape from his liability.
- A. Refer above answer with example.
2. What are the different ways to exclude endorser from his liability?
- A. Refer above answer with example.

**Q.No.74. State the holder's right to obtain duplicate of lost bill, as per the provisions of the Negotiable Instruments Act, 1881. (Sec. 45A)****(D) [NEW SM, OLD SM, MTP - M18(N)]**

**HOLDER'S RIGHT TO OBTAIN DUPLICATE COPY OF LOST BILL (SEC. 45A):** Where a bill of exchange has been lost before it is overdue,

- 1) Holder of the Bill may apply to the drawer, to give him another bill of the same tenor
- 2) Holder shall give security to the drawer (if required) to indemnify him (Drawer) against all persons whatever in case the bill alleged to have been lost shall be found again.

**REMEDY IN CASE OF REFUSAL BY DRAWER:** If the drawer on request as aforesaid refuses to give such duplicate bill, he may be compelled to do so.

**Q.No.75. What is the liability of banker for negligently dealing with bill presented for payment?****(C) [NEW SM]****LIABILITY OF BANKER FOR NEGLIGENTLY DEALING WITH BILL PRESENTED FOR PAYMENT**

- 1) The Bill of exchange is accepted as payable at a specified Bank.
- 2) It has been duly presented at the Bank for payment and dishonoured, and
- 3) The banker negligently or improperly keeps, deals with or delivers back such bill as a result of which the Holder incurs a loss

Shall be liable to compensate the Holder for such loss.

**Q.No.76. Write about Presentment of Promissory note for sight****(D) [NEW SM, OLD SM]**

- 1) A promissory note, payable at a certain period after sight shall be presented <sup>91</sup>-
  - a) To the maker of instrument for sight,
  - b) By a person entitled to demand payment,
  - c) Within reasonable time after it is made and
  - d) On a business day,
  - e) During business hours.
- 2) In default of such presentment, prior parties to the instrument are not liable thereon to the person making such default. *In other words the holder who make the default cannot make the prior parties liable.*


91) Nothing but Instrument Payable after sight

**ADDITIONAL INFORMATION FOR ACADEMIC INTEREST:**

Generally, a Promissory Note can be directly presented for payment as it is written and paid by the Maker himself. But in case of Promissory note payable after sight, such Presentment is required to fix the maturity date.



**SECTION 4: APPENDIX****APPENDIX 1: SPECIMEN OR FORMAT OF PROMISSORY NOTE**

K. Maruthi Rao Sells goods to V. Chandra Sekharam for Rs.50000 to be paid in 3 months. Then the promissory note drawn by V. Chandra Sekharam on K. Maruthi Rao will be as follows:

Rs.50000 only	123, HB Colony Guntur - 5 27-05-2018
Three months after date I promise to pay <u>K. MARUTHI RAO</u> or his order the sum of Rupees Fifty Thousand only, for the value received.	
To K. Maruthi Rao, D.No. 7-17-21/12, 7/5, Srinagar, Guntur-522002	 Sd/- [V. CHANDRA SEKHARAM]

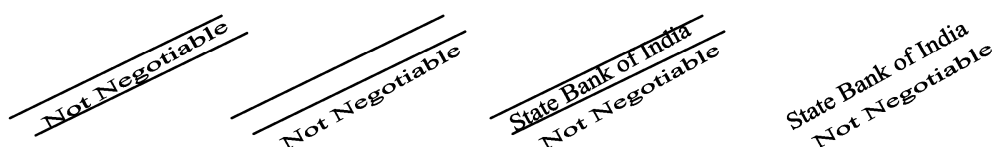
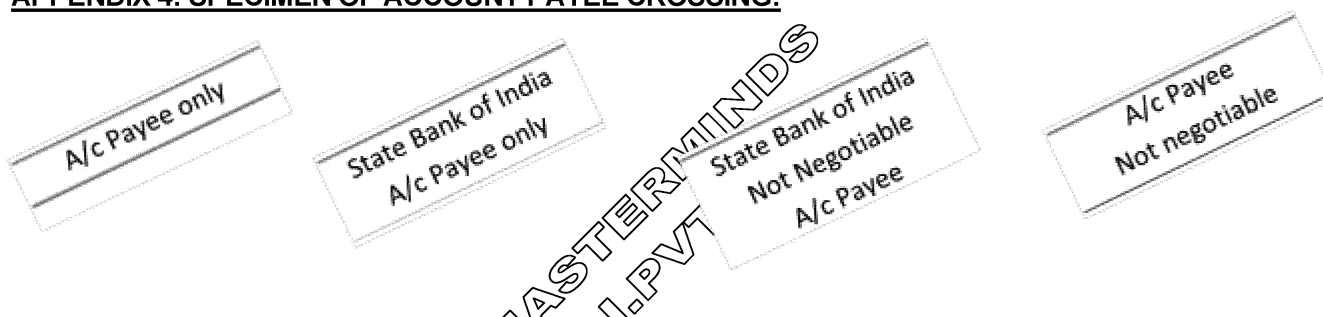
**APPENDIX 2: SPECIMEN OR FORMAT OF BILL OF EXCHANGE:** The usual form of a bill of exchange is given below:

Chandra Sekharam sold goods to Maruthi Rao for Rs.50000 to be paid 3 months after date.

Rs.50,000 only	New Delhi, 17-01-2018
Three months after date pay to me (i.e., <u>V. CHANDRA SEKHARAM</u> ) or order the sum of Rupees Fifty Thousand only, for the value received.	
ACCEPTED  (K. MARUTHI RAO)	
To K. Maruthi Rao, D.No.1-2-3, Brodipet 3 <sup>rd</sup> line GUNTUR - 520004,	 Sd/-

**Specimen of Cheque**

Pay .....	Date :.....
a sum of Rupees.....	Rs. <span style="border: 1px solid black; padding: 2px 20px;"></span>
<span style="border: 1px solid black; padding: 2px 20px;">A/C No. 12345678910</span>	
ABC Bank 622, Vijay Nagar, Indore (M. P.)	Signature
01212 1125864 000053 38	

**APPENDIX 1: SPECIMEN OF GENERAL CROSSING:****APPENDIX 2: SPECIMEN OF SPECIAL CROSSING:****APPENDIX 3: SPECIMEN OF NOT NEGOTIABLE CROSSING:****APPENDIX 4: SPECIMEN OF ACCOUNT PAYEE CROSSING:****SECTION 5: QUESTION WISE ANALYSIS OF PAST EXAMINATIONS – PRACTICAL QUESTIONS**

Q. No.	M17	N17	M18 (O)	M18 (N)	N18 (O)	N18 (N)	M19 (O)	M19 (N)	N19 (O)	N19 (N)	N20 (O)	N20 (N)
CRD 1	-	-	-	-	-	-	-	-	-	-	-	3
CRD 5	-	-	-	-	-	-	-	-	-	-	-	4
CRD 8	-	-	-	-	-	-	-	-	-	-	-	3
CRD 12	-	-	-	-	-	-	-	3	-	-	-	-
CRD 13	4	-	-	-	-	-	-	3	-	3	-	-
CRD 14	4	-	-	-	-	-	-	-	-	3	-	-
CRD 15	-	-	-	-	-	-	-	-	-	3	-	-
CRD 23	-	-	-	-	-	4	-	-	-	-	-	-
CRD 24	-	4	-	-	-	-	-	-	-	-	-	-
CRD 25	-	4	-	-	-	-	-	-	-	-	-	-
CRD 27	-	-	-	-	-	4	-	-	-	-	-	-
CRD 30	-	-	-	-	-	4	-	-	3	-	-	-
CRD 32	-	-	-	-	-	4	-	-	3	-	-	-



CRD 33	-	-	-	-	4	-	-	-	-	-	-	-
CRD 36	-	4	-	-	4	-	-	-	-	-	-	-
CRD 37	-	-	-	-	-	-	-	2	-	4	-	-
CRD 42	-	-	-	4	-	-	-	-	-	-	-	-
CRD 48	-	-	-	-	-	-	-	-	-	-	-	3
CRD 49	-	-	4	-	-	-	-	2	-	-	-	-
SP 7	-	-	-	4	-	-	-	-	-	-	-	-
SP 34	-	-	-	-	-	-	-	2	-	-	-	-

## SECTION 6: PRACTICAL QUESTIONS FOR CLASSROOM DISCUSSION

Q.No.1. State whether the following statements are promissory notes or not?

- 'A' tells 'B' - I owe you a sum of Rs.1,000. [OLD PM]
- 'X' promises to pay 'Y' a sum of Rs.10,000, six months after 'Y's marriage with 'Z' [OLD PM]
- "I acknowledge myself to be indebted to B Rs.1,000 to be paid on demand, for value received". [OLD PM]
- I am liable to B, in a sum of Rs.500 to be paid by installments.
- "I promise to pay B Rs.500 and all other sums which shall be due to him". [RTP - M13]
- "I promise to pay B Rs.1,000 and the fine according to the rules".
- "I promise to pay B Rs.500 by installments with a provision that no payment shall be made after my death".
- "I promise to pay B Rs. 500 when he delivers the goods".
- "I promise to pay B Rs.500 on D's death, provided D leaves me enough money to pay that sum". [OLD PM]
- "I promise to pay B Rs. 500 and to deliver to him my black horse on 1st January next"
- "I promise to pay Rs. 5,000 or 7,000 to Mr. Ram."
- "I promise to pay to Mohan Rs.500, if he secures 60% marks in the examination".
- A promise by way of Promissory note to pay B, his partner, a sum of Rs.1,00,000 in the event of the latter's son being appointed in the partnership firm.
- A Promissory note containing an undertaking to pay the amount of \$1 million at the exchange rate stated by RBI as on payment date.
- A Promissory note containing an undertaking to pay the amount of \$1 million at the exchange rate of Rs.70 per \$1.
- A Promissory note containing an undertaking to pay the amount of Rs.10,00,000 and interest @ 10% p.a. for the period from the date of instrument to the date of payment.
- X promises to pay Y, by a promissory note, a sum of Rs.5,000, fifteen days after the death of B. [OLD PM]
- "I promise to pay myself" Rs.10,000.
- Received from B the sum of one thousand rupees to be paid after three months with interest at 15% Per annum, dated May 19<sup>th</sup> 2007"
- "I acknowledge my self to be indebted to B in Rs 5000, to be paid on demand to B on his attaining the age of majority." (RELATED TO THEORY Q.NO.4)

- It is not a promissory note, since there is no promise to pay.
- It is not a promissory note, since its payment depends upon a contingent event which may never happen i.e. marriage of Y with Z.
- It is a promissory note. The Maker is acknowledging his debt and promises to pay for the value received.
- It is not a promissory note. It is a mere acknowledgement of debt and there is no specific promise to pay the sum.

- e) It is not a promissory note. The amount is uncertain. (In commercial transactions the amount should be certain.)
- f) It is not a promissory note. The amount is uncertain. (In commercial transactions the amount should be certain.)
- g) It is not a promissory note. In this case death is a certain event and a negotiable instrument can be drawn on the basis of such certain event. But this instrument is uncertain as to the amount. In commercial transactions certainty of amount is very important.
- h) It is not a promissory note. A negotiable instrument can't be drawn on the basis of future uncertain event. In this case it is uncertain as to the date of payment. The other party may never deliver the goods.
- i) It is not a promissory note. Negotiable instruments can be drawn to be payable on the basis of some future events which are certain to happen. In this case D's death is a certain event. But D may not leave enough sum which is an uncertain event.
- j) It is not a promissory note. A negotiable instrument must be drawn for money and money only. In this case it is written for partly cash and partly kind.
- k) It is not a promissory note. Amount is not certain.
- l) It is not a promissory note. It is conditional.
- m) It is not a promissory note. It is conditional and also the admission of son of B in the firm is not a certain event.
- n) It is a valid promissory note. The basis for exchange rate was decided and hence amount can be determined.
- o) It is a valid promissory note. Exchange rate was mentioned and amount in rupees can be ascertained.
- p) It is a valid promissory note. Interest rate was mentioned and total amount receivable on the instrument can be ascertained.
- q) It is a valid promissory note. It is not conditional as it is certain that B will die even though the exact date of his death is uncertain.
- r) It is not a promissory note. Payee and maker should not be the same person. So, this is not a valid Promissory Note.
- s) It is not a promissory note. It is a mere acknowledgement of debt and there is no specific promise to pay the sum.
- t) It is not a promissory note. It contains conditional undertaking about attaining the age of majority.

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**Q.No.2. State whether the following instruments are Bills of Exchange or not?**

- a) 'A' tells 'B', I request you to pay a sum of Rs.1,000.
- b) 'A' tells 'B', I beg you to pay a sum of Rs.2,000 to C.
- c) 'X' Orders Y to pay a sum of Rs.10,000, six months after 'Y's marriage with 'Z'
- d) "I order B to pay Rs.500 and all other sums which shall be due to him".
- e) "I order B to pay Rs. 500 to C when C delivers the goods to A".
- f) "I order Mr. Ravi to pay Rs. 5,000 or 7,000 to Mr. Ram."
- g) "I order Shyam to pay Rs.500 to me or my order, if his son secures 60% marks in the examination".
- h) W dismissed his servant R from services and towards his wages, he gave him a draft in the following words: "Mr. N will much oblige Mr. W by paying to Mr. R or order, rupees two hundred on his account. Signed by W." Is this draft a bill of exchange? (RELATED TO THEORY Q.NO.6)

- a) It is not a bill, since there is no order to pay and also no certainty about Payee.
- b) It is not a bill, since there is no order to pay.
- c) It is not a bill, since there is probability that Y may not marry.
- d) It is not a bill. The amount is not certain. (In commercial transactions the amount should be certain.)
- e) It is not a bill. A negotiable instrument can't be drawn on the basis of future uncertain event. In this case, it is uncertain as to the date of payment. The other party may never deliver the goods.

- f) It is not a bill. Amount is not certain.
- g) It is not a bill. It is conditional.
- h) It is a Bill, since introduction of the word 'gratitude' does not destroy the order to pay.

**Q.No.3. A Bill is drawn payable at No.A17, Akshay Apartments, New Delhi, but does not contain Drawee's name. Mr. Vinay who resides at the above address accepts the bill. Is it a valid Bill?**

[OLD PM, RTP - N14]

**X draws a bill of exchange payable at House No: 1, Pitampura, New Delhi. It does not contain the name of any Drawee, although Y lives at the stated address. Y accepts the bill. Would Y be liable under the bill?**

[OLD PM] (RELATED TO THEORY Q.NO.6)

**PROVISION:** As per the provisions of NI Act, 1881, Drawee may be named or otherwise indicated in the bill with reasonable certainty.

**ANALYSIS:** In the present case, the description of the place of residence indicates the name of the Drawee and Mr. Vinay / Mr. Y, by his acceptance, acknowledges that he is the person to whom the bill is directed.

**CONCLUSION:** Therefore, it is a valid Bill and Mr. Vinay / Mr. Y are liable thereon.

**Q.No.4. State with reasons whether each of the following instruments is a Time Instrument or Demand Instrument:**

- I promise to pay B Rs.500.
- I promise to pay B Rs.500 on Demand.
- Pay Rs.500 at sight.
- Pay Rs.500 on presentment.
- I promise to pay B Rs.500 after 3 months.
- I promise to pay B Rs.500 on 1<sup>st</sup> Jan. 2018.
- I promise to pay Rs.500 after 1 month from sight.
- I promise to pay B Rs.500 after C's Death.
- Pay B Rs.500 on or before 1<sup>st</sup> Jan. 2018.

(RELATED TO THEORY Q.NO.10)

CASE	DECISION	REASON
a)	Demand instrument [Sec.19 & 21]	No time for payment has been specified.
b)	Demand instrument [Sec.19 & 21]	It is expressed to be so payable.
c)	Demand instrument [Sec.19 & 21]	The expression 'at sight' means 'on demand'.
d)	Demand instrument [Sec.19 & 21]	The expression 'on presentment' means 'on demand'.
e)	Time instrument [Sec.21]	Fixed period has been specified.
f)	Time instrument [Sec.21]	A particular day has been specified.
g)	Time instrument [Sec.21]	After sight means after presentment for payment. It is payable after one month from the date of presentment for payment.
h)	Time instrument [Sec.21]	It is payable on the happening of an event (i.e. death) which is certain to happen.
i)	Not a negotiable instrument at all	Time is uncertain.

**Q.No.5. State with reasons whether each of the following instruments is an 'Inland Instrument' or Foreign Instrument:**

- A bill drawn in Delhi upon a merchant in Agra and accepted payable in London.
- A bill drawn in Delhi upon a merchant in London and accepted payable in Agra.
- A bill drawn in Delhi upon a merchant in London and accepted payable in London.

- d) A bill drawn in London upon a merchant in Agra and accepted payable in Delhi.
- e) A bill drawn in Delhi on a merchant in Agra but endorsed in London.
- f) A bill drawn in London on a merchant in Agra and endorsed in Delhi.
- g) Ram draws a bill of exchange in Delhi upon Shyam a resident of Jaipur and accepted to be payable in Thailand after 90 days of acceptance.
- h) Ramesh draws a bill of exchange in Mumbai upon Suresh a resident of Australia and accepted to be payable in Chennai after 30 days of sight.
- i) Ajay draws a bill of exchange in California upon Vijay a resident of Jodhpur and accepted to be payable in Kanpur after 6 months of acceptance.
- j) Mukesh draws a bill of exchange in Lucknow upon Dinesh a resident of China and accepted to be payable in China after 45 days of acceptance.

(N20 (N)-4M) (RELATED TO THEORY Q.NO.11)

First state the provisions related to Inland instrument and foreign instrument.

CASE	DECISION	REASON
a)	Inland instrument [Sec 11]	It is drawn in India and the drawee is resident in India.
b)	Inland instrument [Sec 11]	It is drawn in India and is payable in India.
c)	Foreign Instrument [Sec 12]	It is not accepted payable in India and at the same time its drawee is not a resident of India.
d)	Foreign instrument [Sec 12]	It is not drawn in India
e)	Inland instrument [Sec 11]	It is drawn in India and drawee is resident in India.
f)	Foreign instrument [Sec 12]	It is not drawn in India.
g)	Inland instrument [Sec 11]	It is drawn in India and drawee is resident in India.
h)	Inland instrument [Sec 11]	It is drawn in India and is payable in India.
i)	Foreign instrument [Sec 12]	It is not drawn in India.
j)	Foreign Instrument [Sec 12]	It is not accepted payable in India and at the same time its drawee is not a resident of India.

**Q.No.6. State with reasons whether each of the following instrument is an Ambiguous Instrument or fictitious instrument:**

- a) A bill is drawn upon Y who is a major person payable to Z who is a fictitious person.
- b) A bill is drawn upon Y as payable to Z. The drawer is a fictitious person.
- c) A bill is drawn by A, an agent, acting within the scope of his authority, upon his principle P.
- d) X draws a bill on Y who is a fictitious person and negotiates it to himself.
- e) X draws a bill on Y who is a minor.
- f) A bill is drawn by Delhi branch of Dena Bank upon its Bombay branch.

(RELATED TO THEORY Q.NO.14)

CASE	DECISION	REASON
a)	Fictitious instrument [Sec.42]	The payee is a fictitious person.
b)	Fictitious instrument [Sec.42]	The drawer is a fictitious person.
c)	Ambiguous instrument [Sec. 17]	The drawer and the drawee are the same person.
d)	Ambiguous instrument [Sec. 17]	The drawee is a fictitious person.
e)	Ambiguous instrument [Sec. 17]	The Drawee is not competent to contract.
f)	Ambiguous instrument [Sec. 17]	Since Drawer & Drawee are the same person

**Q.No.7. State with reasons whether each of the following instruments is an 'Inchoate Instrument' or not:**

- X signs and delivers an unstamped and blank promissory note to Y.
- X delivers a stamped and blank promissory note to Y without his signature.
- X signs a stamped and blank promissory note and keeps in his safe.
- X signs and delivers a stamped and blank promissory note to Y.
- X signs and delivers a stamped and complete promissory note to Y.

(RELATED TO THEORY Q.NO.15)

CASE	DECISION	REASON
a)	No	It is not stamped. Not a promissory note at all.
b)	No	It has not been signed by the Maker. Not a promissory note at all.
c)	No	It has not been delivered.
d)	Yes	There is a delivery of a signed, stamped & blank instrument.
e)	No	It is not incomplete instrument.

**Q.No.8. Discuss with reasons, whether the following persons can be called as a 'holder' under the Negotiable Instruments Act, 1881:**

- X who obtains a cheque drawn by Y for gift. [RTP - N14]
- A, the payee of the cheque, who is prohibited by a court order from receiving the amount of the cheque. [RTP - N18 (O)]
- M, who finds a cheque payable to bearer, on the road and retains it. [N16 - 2M, MTP - M18 (N)]
- B, the agent of C, is entrusted with an instrument without endorsement by C, who is the payee. [N16 - 2M]
- B, who steals a blank cheque of A and forges A's signature.
- 'M' the payee of the cheque, who is prohibited by a court order from receiving the amount of the cheque.
- 'M' the agent of 'Q' is entrusted with an instrument without endorsement by 'Q' who is the payee. [N16 - 4M] [RTP - May 20] (RELATED TO THEORY Q.NO.17)

**PROVISION:** As per sec 8 of the NI Act, 1881, 'Holder' of a Negotiable Instrument means any person entitled in his own name to the possession of it and to receive or recover the amount due thereon from the parties thereto.

**BY APPLYING THE ABOVE PROVISION IN THE GIVEN CASES:**

- X can be termed as a holder because he has the right to possess and to receive the amount due in his own name.
- He is not a 'holder' because to be called as a 'holder' he must be entitled not only to the possession of the instrument but also to receive the amount mentioned therein.
- M is not a holder of the Instrument though he is in possession of the cheque as, he is not entitled to the possession of it in his own name.
- B is not a holder. While the agent may receive payment of the amount mentioned in the cheque, yet he cannot be called the holder thereof because he has no right to sue on the instrument in his own name.
- B is not a holder because he is in wrongful possession of the instrument.
- 'M' is not a 'holder' because to be called as a 'holder' he must be entitled not only to the possession of the instrument in his own name but also to receive the amount mentioned therein.
- 'M' is not a holder. While the agent may receive payment of the amount mentioned in the cheque, yet he cannot be called the holder thereof because he has no right to sue on the instrument in his own name.

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**Q.No.9. In the following situations identify whether the person in possession of the instrument is a Holder or HDC.**

- Mr. A gave a cheque payable to bearer to Mr. B. The cheque was lost and found by Mr. C. Decide the status of Mr.C.
- Mr. X gave a cheque payable to bearer to Mr.Y. Z steals the same from Mr.Y. Decide the status of Z.
- Mr. Ravi gave an order cheque payable to Mr.Somu. By the time Mr. Somu received instrument, he became insolvent. Decide the status of Mr. Somu.
- X, by inducing Y, obtains a bill of exchange from him fraudulently in his (X) favour. Later, he enters into a commercial deal and endorses the bill to Z for consideration. Z knowing about fraud between X and Y takes the Bill.
- X draws a bill of exchange for Rs. 20,000 and hands it over to Y. Later on, Y endorsed the bill to Z after maturity.
- 'A' draws a cheque for Rs.10,000 and hands it over to 'B' by way of gift. Is 'B' a Holder or HDC?
- X, by inducing Y, obtains a bill of exchange from him fraudulently in his (X) favour. Later, he enters into a commercial deal and endorses the bill to Z for consideration and in good faith before maturity. What is the status of Z?
- X steals a bill of exchange, payable to Bearer, from Y. Later, he enters into a commercial deal and endorses the bill to Z for consideration and in good faith before maturity. What is the status of Z?
- X obtains a bill of exchange from Y under betting agreement. Later, he enters into a commercial deal and endorses the bill to Z for consideration and in good faith before maturity. What is the status of Z?

(RELATED TO THEORY Q.NO.18)

	DECISION	EXPLANATION
a)	Not a Holder	Mr.C is treated as finder of lost instrument. Hence he is not entitled to possess the instrument.
b)	Not a Holder	Mr.Z is not entitled to the possession of the instrument as he has not obtained the instrument through lawful means.
c)	Not a Holder	Mr.Somu is Insolvent. He has no right to receive amount on the instrument.
d)	Holder	Holder but not HDC since he acquired instrument without good faith.
e)	Holder	Holder but not HDC since he acquired instrument after maturity.
f)	Holder	Holder but not HDC since he acquired instrument without Consideration
g)	HDC	Since he satisfied all the conditions
h)	HDC	Since he satisfied all the conditions
i)	HDC	Since he satisfied all the conditions

**Q.No.10. Can an Acceptor of a bill avoid his liability against a person who is a holder in due course or who derives his title from a holder in due course, on the following grounds?**

- That the instrument has not been filled in accordance with the authority given by him.
- That the other parties to the bill were fictitious.
- That the instrument was drawn without consideration.
- That the delivery of the instrument was conditional.
- That the instrument had been lost.
- That the instrument was obtained from him by means of fraud.
- That the instrument was obtained from him for an unlawful consideration.
- That his signature was forged.
- That payee had no capacity to endorse.

(RELATED TO THEORY Q.NO.19)

GROUND	DECISION	EXPLANATION
a)	No	Privilege given to holder in due course U/s 20 provided the stamp put on the instrument was sufficient to cover the amount.
b)	No	Privilege given to a holder in due course u/s 42
c)	No	Privilege given to a holder in due course u/s 43

d)	No	Privilege given to a holder in due course u/s 46
e)	No	Privilege given to a holder in due course u/s 58
f)	No	Privilege given to a holder in due course u/s 58
g)	No	Privilege given to a holder in due course u/s 58
h)	Yes	Forgery passes no title to anyone at all.
i)	No	Privilege given to a holder in due course u/s 121

**Note:** The above decisions also hold good for a person who derives title from a holder in due course.

**Q.No.11.** X, by inducing Y, obtains a bill of exchange from him fraudulently in his (X) favour. Later, he enters into a commercial deal and endorses the bill to Z towards consideration to him (Z) for the deal. Z takes the Bill as a holder in due course. Z subsequently endorses the bill to X for value, as consideration to X for some other deal. On maturity, the bill is dishonoured. X sues Y for recovery of money. With reference to the provisions of NI Act, 1881 decide whether X will succeed in the case or not. [OLD PM, N14, N16 - 4M]

(Or)

S, by inducing T obtains a bill of exchange from him fraudulently in his (S) favor. Later, he enters into a commercial deal and endorses the bill to U towards consideration to him (U) for the deal. U takes the bill as a Holder-in-due-course. U subsequently endorses the bill to S for value, as consideration to S for some other deal on maturity the bill is dishonoured. S sues T for the recovery of the money. With reference to the provisions of NI Act, 1881 decide whether S will succeed in the case or not. (RELATED TO THEORY Q.NO.19)

**PROVISION:** As per Sec.53, a holder who derives title from holder in due course will get all the rights of a holder in due course. However, the holder was himself not a party to the fraud or illegality which affected the instrument in some stage of its journey. Since X derives his title from Z (who is a holder in due course), X will get all the rights of Z.

As per Sec 58 of NI Act, 1881, if an instrument is obtained by fraud, offence or for unlawful consideration then possessor or endorsee (other than holder-in-due course) cannot receive the amount of the Instrument.

**CONCLUSION:** Hence X is not entitled to sue Y as X is not a holder-in-due course because he obtained instrument through fraud.

**Q.No.12.** A owes certain sum of money to B. A does not know the exact amount and hence he makes out a blank cheque in favour of B, signs and delivers it to B with a request to fill up the amount due, payable by him. B fills up fraudulently the amount larger than the amount due, payable by A and endorses the cheque to C in full payment of dues of B. Cheque of A is dishonoured. Referring to the provisions of the Negotiable Instruments Act, 1881, discuss the rights of B and C. [NEW SM, OLD PM, RTP M 20, M19 (N) - 3M] (RELATED TO THEORY Q.NO.19)

**PROVISION:** An Inchoate stamped instrument means an instrument that is incomplete in certain aspects.

As per sec 20 of the NI Act, 1881, in case of Inchoate instrument, the person signs and delivers a blank or incomplete instrument to another person and authorizes such person to complete the Instrument.

The holder gets a prima facie authority to make or complete it as a negotiable instrument.

HDC can recover the whole amount specified in the instrument but not exceeding the amount covered by the stamp affixed on the instrument.

Holder (any person other than HDC) cannot recover the amount in excess of the amount intended to be paid by the person delivering the inchoate instrument.

**CONCLUSION:** Applying the above provision, B who is a party in immediate relation with the drawer of the cheque is entitled to recover from A only the exact amount due from A and not the amount entered in the cheque. The right of C, who is a holder for value, is not adversely affected and he can claim the full amount of the cheque from B.

**Q.No.13.** X draws a bill on Y but signs it in the fictitious name of Z. The bill is payable to the order of Z. The bill is duly accepted by Y. M obtains the bill from X thus becoming its holder in due course. Can Y avoid payment of the bill? Decide in the light of the provisions of the NI Act, 1881.

[N19 (N) - 3M, MTP - M18 (N)]

(Or)

H is the holder in due course of a bill of which A is the acceptor. D, the drawer of the bill, is fictitious. Can 'A' escape from his liability to H? [OLD PM, M17 - 4M] (RELATED TO THEORY Q.NO.19)

**PROVISION:** As per sec 42, in case a bill of exchange is drawn payable to the drawer's order in a fictitious name and is endorsed by the same hand as the drawer's signature, it is not permissible for the acceptor to allege (i.e., to contend) as against the holder in due course that such name is fictitious.

**CONCLUSION:** In the given case, Y cannot avoid payment by raising the plea that the drawer (Z) is fictitious.

The only condition is that the signature of Z as drawer and as endorser must be in the same handwriting.

**Q.No.14. Raman is the payee of an order cheque. John steals the cheque and forges Raman's signatures and endorses the cheque in his own favour. John then further endorses the cheque to Anil, who takes the cheque in good faith and for valuable consideration.**

**Examine the validity of the cheque as per the provisions of Negotiable Instruments Act, 1881 and also state whether Anil can claim the privileges of a Holder in Due course.**

[OLD PM, N15 - 4M, N19 (N) - 3M] (RELATED TO THEORY Q.NO.19)

**PROVISION:** Forgery confers no title and a holder acquires no title to a forged instrument. A forged document is a nullity. The property in the instrument remains vested in the person who is the holder at the time when the forged signatures were put on it. Forgery is also not capable of being ratified.

In case of forged endorsement, the person claiming under forged endorsement, cannot acquire the rights of a holder in due course, even if he is purchaser for value and in good faith.

**CONCLUSION:** Therefore, Anil acquires no title on the cheque.

**Q.No.15. J accepted a bill of exchange and gave it to K for the purpose of getting it discounted and handed over the proceeds to J. K having failed to discount it, returned the bill to J. J tore the bill in two pieces with the intention of cancelling it and threw the pieces in the street. K picked up the pieces and pasted the two pieces together in such a manner that the bill seemed to have been folded for safe custody, rather than cancelled. K put it into circulation and it ultimately reached L, who took it in good faith and for value. Is J liable to pay for the bill under the provisions of the Negotiable Instruments Act, 1881?** [OLD PM, M10 - 5M] (RELATED TO THEORY Q.NO.19)

**PROVISION:** As per Sec.9, 'Holder in due course' means any person who, for consideration, became the possessor of a promissory note, bill of exchange or cheque, if payable to the bearer, or the payee or endorsee thereof, if payable to the order, before the amount mentioned in it became payable, and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title."

As per Sec 120, no drawer of a bill, shall, in a suit thereon, by a holder in due course, be permitted to deny the validity of the instrument as originally drawn. A holder in due course gets a good title to the bill.

**CONCLUSION:** L is a holder in due course, who got the bill in good faith and for value. Therefore, in the given problem, J is liable to pay for the bill.

**Q.No.16. On a Bill of Exchange for Rs.1 lakh, X's acceptance to the Bill is forged. 'A' takes the Bill from his customer for value and in good faith before the Bill becomes payable. State with reasons whether 'A' can be considered as a 'Holder in due course' and whether he can receive the amount of the Bill from 'X'. [NEW SM, OLD PM, RTP - N11, MTP - M18 (N), MTP - N18 (N), MTP1 - M19(N)] (RELATED TO THEORY Q.NO.19)**

**PROVISION:** Sec 9 of the NI Act - Holder in due course

As per Sec 9, 'holder in due course' means any person who for consideration because the possessor of a promissory note, bill of exchange or cheque if payable to bearer or the payee or endorsee thereof, if payable to order, before the amount in it became payable and without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title.

In this case, Prima facie, 'A' became possessor of the bill for value and in good faith before the bill became payable. So, he can be considered as a holder in due course.



But the holder of a forged instrument cannot enforce payment thereon. In the event of the holder being able to obtain payment, in spite of forgery, he cannot retain the money.

The true owner may sue on **tort** (the person who had received). This principle is universal in character; by reason where of even a holder in due course is not exempt from it.

A holder in due course is protected when there is defect in the title. But he derives no title when there is entire absence of title as in the case of forgery. Hence 'A' cannot receive the amount on the bill.

**CONCLUSION:** As signature on the negotiable instrument is forged, it becomes a nullity. Hence 'A' cannot receive the amount on the bill even though he is a holder-in-due course.

**Q.No.17. X was the holder of a cheque for Rs. 10,000 payable to a bearer. He kept the cheque in his safe. Y, a thief stolen the cheque from X's safe. Can this be considered as negotiation of cheque by X to Y? If Y delivers the cheque to Z for consideration and Z receives the same in good faith before its maturity, then what are the rights available to Z? (RELATED TO THEORY Q.NO.20)**

**PROVISION:** According to sec.47 of the NI ACT, 1881, Negotiation is said to be done only when it is made with an intention of transferring the title of the instrument to the transferee.

**Negotiation by delivery:** A bearer instrument may be negotiated by mere delivery and such delivery must be voluntary.

A person becomes holder of a negotiable instrument as a result of negotiation when he obtains the instrument in good faith without resorting any fraudulent means.

Finder of NI or thief of NI cannot become holder of the instrument since the instrument is not being delivered. If such instrument is negotiated to HDC, prior parties cannot argue that instrument was delivered conditionally or for a special purpose only.

**CONCLUSION:**

- i) In this case, there is no negotiation of the cheque from X to Y because the cheque was not voluntarily delivered to Y.
- ii) It may also be noted that if Y delivers this cheque for some consideration to Z who receives the same in good faith and before maturity. Z will become the holder in due course and will be entitled to receive the amount of the instrument.

**Q.No.18. A owes money to B. A makes a promissory note for the amount in favour of B. For safety of transmission, he cuts the note in half and posts one half to B. He then changes his mind and calls upon B to return the half of the note which he had sent. B requires A to send the other half of the promissory note. Decide how the rights of the parties are to be adjusted. RTP - M19 (N), RTP - M19 (O), MTP1 - M19 (N), MTP July 20] (RELATED TO THEORY Q.NO.21)**

**PROVISION:** Under Section 46 of the Negotiable Instruments Act, 1881, the making of a promissory note is completed by delivery, actual or constructive. Delivery refers to the whole of the instrument and not merely a part of it. Delivery of half instrument cannot be treated as constructive delivery of the whole.

**CONCLUSION:** In the given case A makes a promissory note payable to B. For the purpose of safety of transmission, he cuts the note in half and post to B. He then changes his mind and calls for the remaining half.

The claim of B to have the other half of the promissory note sent to him is not maintainable. A is justified in demanding the return of the first half sent by him. He can change his mind and refuse to send the other half of the promissory note. The matter is now at the discretion of A.

**Q.No.19. A bill of exchange is drawn payable to X or order. X endorses it to Y, Y to Z, Z to A, A to B and B to X. State with reasons whether X can recover the amount of the bill from Y, Z, A and B, if he has originally endorsed the bill to Y by adding the words 'Sans Recourse or not? X endorses it to Y [OLD PM, RTP - N11, RTP - M18 (O)] (RELATED TO THEORY Q.NO.26 &27)**

**PROVISION:** Generally, if the endorser becomes the holder after it is negotiated to several parties, none of the intermediate parties is liable to endorser. This is to prevent 'circuitry of action'.

However, as per sec 52, the holder of a bill may endorse it in such a way that he does not incur the liability of an endorser to all subsequent endorsees. He can do so by adding the words 'sans recourse' (without recourse) to the endorsement.

**CONCLUSION:** In the given case X, the endorser becomes the holder after it is negotiated to several parties. In such a case, none of the intermediate parties is liable to X.

But in this case X's original endorsement is 'sans recourse' and therefore, he is not liable to Y, Z, A, and B. But if the bill is negotiated back to X, all of them are liable to him and he can recover the amount from all or any of them (Sec. 52).

**Q.No.20. W drew a cheque crossed not-negotiable in blank and handed it to his Clerk to fill in the amount and the name of the payee. The clerk inserted a sum in excess of her authority and delivered the cheque to 'P' in payment of a debt of her own. Decide. (RELATED TO THEORY Q.NO.29)**

**PROVISION:** According to Section 130, a person who takes 'not negotiable' crossing cheque does not get a better title than the person from whom he acquired the cheque, including HDC. Such a cheque loses its special characteristics of negotiability.

In the given case, W drew a cheque crossed not-negotiable in blank and handed it to his Clerk to fill in the amount and the name of the payee. The clerk inserted a sum in excess of her authority and delivered such cheque to 'P' in payment of a debt of her own.

**CONCLUSION:** On the basis of above analysis, the Clerk had no title to the cheque and as such P had no better title and therefore W was not liable.

**Q.No.21. A induced B by fraud to draw a cheque payable to C or order. A obtained the cheque, forged C's endorsement and collected proceeds to the cheque through his banker. B, the drawer, wants to recover the amount from C's bankers. In the light of the provisions of Negotiable Instruments Act, 1881 decide whether B, the drawer can recover the amount of the cheque from C's bankers? Whether C is the fictitious payee? Would your answer be still the same in case C is a fictitious person? [OLD PM, MTP - M17, M1P1 - N18] (RELATED TO THEORY Q.NO.32 & 33)**

#### **AS PER ICAI STUDY MATERIAL:**

**PROVISION:** As per Section 42 of the NI Act, 1881, if a bill is drawn in the name of a fictitious person and payable to the Drawer's order then the acceptor is liable to pay to the order of the person who signed it as Drawer.

Acceptor cannot be relieved from his liability to the HDC. However, HDC shall establish that the bill was endorsed by the same person who has drawn such instrument.

#### **CONCLUSION:**

Applying the above provision, answers to the questions asked are as under:

- a) In this case B, the drawer, can recover the amount of the cheque from C's banker because C's title was derived through forged endorsement.
- b) Here C is not a fictitious payee because the drawer intended him to receive payment.
- c) The result would be different if C is not a real person or is a fictitious person or was not intended to have the payment

#### **OUR VIEW:**

**PROVISION:** Same as above

#### **CONCLUSION:**

#### **B's banker is not liable:**

- a) Since a paying banker is not liable even if it is subsequently found that any endorsement on the cheque has been forged.
- b) Provided the paying banker made the payment in due course (Sec. 85).

**A's banker is not liable:**

- a) Since collecting banker is not liable for any loss caused to the true owner due to defective title of the holder;
- b) Provided the collecting banker acted in good faith and without negligence while collecting the amount of the crossed cheque as an agent (Sec. 131).

**C's banker is not liable:** Since it has neither collected nor paid the cheque.

**C is not a fictitious payee:** Since C, in fact, exists.

**If C were a fictitious payee, the Answer would have remained same:** Since protection is available to a collecting banker u/s 131 and paying banker u/s 85, irrespective of the fact that the payee is a fictitious person or not.

**Q.No.22. A draws a cheque in favour of B. A's clerk forges B's endorsement and negotiates the cheque to C, who takes it in good faith and for value. C receives payment on the cheque. Discuss the rights of A and C.**

**In the given problem, issues involved are:**

- a) Can A claim the reimbursement of the payment from his bank for the payment having been made to a person under forged endorsement?
- b) C having received the payment; does he enjoy the right of retaining the amount?

**(RELATED TO THEORY Q.NO. 32 & 33)**

**PROVISION:** As per Sec.85 & 126 of the NI Act, 1881, when the payment is made in due course, the paying banker and collecting banker, is not liable even if the endorsement made on the cheque is forged.

But the holder of a forged instrument cannot enforce payment thereon. In the event of the holder being able to obtain payment, in spite of forgery, he cannot retain the money. The true owner may sue the person who had received.

**CONCLUSION:** Therefore:

- a) A cannot claim the reimbursement from his bank as it is protected u/s 85.
- b) C cannot retain the amount of the cheque and he is liable to repay the amount to the true owner of the cheque.

**Q.No.23. Mr. Muralidharan drew a cheque payable to Mr. Vyas or order. Mr. Vyas lost the cheque and was not aware of the loss of the cheque. The person who found the cheque forged the signature of Mr. Vyas and endorsed it to Mr. Parshwanath as the consideration for goods bought by him from Mr. Parshwanath. Mr. Parshwanath encashed the cheque on the very same day from the drawee bank. Mr. Vyas intimated the drawee bank about the theft of the cheque after three days. Examine the liability of the drawee bank. [N18 (N) - 4M, RTP - N19 (N), RTP - N19 (O)] (RELATED TO THEORY Q.NO.32 & 33)**

**PROVISION:** Section 85 of the Negotiable Instruments Act, 1881 – Cheque payable to order

- a) Where a cheque payable to order purports to be endorsed by or on behalf of the payee, the drawee is discharged by payment in due course.
- b) Where a cheque is originally expressed to be payable to bearer, the drawee is discharged by payment in due course to the bearer thereof, notwithstanding any endorsement whether in full or in blank appearing thereon, and notwithstanding that any such endorsement purports to restrict or exclude further negotiation.

As per the given facts, cheque is drawn payable to "Mr. Vyas or order". It was lost and Mr. Vyas was not aware of the same. The person found the cheque and forged and endorsed it to Mr. Parshwanath, who encashed the cheque from the drawee bank. After few days, Mr. Vyas intimated about the theft of the cheque, to the drawee bank, by which time, the drawee bank had already made the payment.

**CONCLUSION:** According to above stated section 85, the drawee banker is discharged when it has made a payment against the cheque payable to order when it is purported to be endorsed by or on behalf of the payee. Even though the signature of Mr. Vyas is forged, the banker is protected and is discharged. The true owner, Mr. Vyas, cannot recover the money from the drawee bank in this situation.

**Q.No.24.** A cheque payable to bearer is crossed generally and is marked "not negotiable". The cheque is lost or stolen and comes into the possession of B who takes it in good faith and gives value for it. B deposits the cheque into his own bank and his banker presents it and obtains payment for his customer from the bank upon which, the cheque is drawn.

- a) Can both the bankers, viz., banker paying the cheque, and the banker collecting it plead exoneration from their liability? [OLD PM, N15, RTP – M17, MTP –N16]
- b) Can B be compelled to refund the money to the true owner of the cheque?

(RELATED TO THEORY Q.NO.29, 32 &33)

**PROVISION:** As per sec 130 of the NI Act, 1881, a person taking cheque crossed generally or specially bearing in the words 'Not Negotiable' can't get a better title than that of transferor. Thus, if the title of the transferor is defective, the title of the transferee will also be defective.

On the other hand both collecting banker and paying banker will be protected under the Act, provided the payment and the collection have been made in good faith and without negligence [Sec.128 & 130].

**CONCLUSION:**

- a) Therefore, in the given case, both paying banker and collecting banker can plead exoneration (*i.e.*, exemption) from liability.
- b) Yes. B can be compelled to refund the money as he was not entitled to receive payment upon instrument. This is because even though B was a holder in due course, he did not acquire any title to the cheque as against its true owner.

**Q.No.25.** 'K' is an employee of 'Sumit'. He fraudulently obtains from Sumit a cheque crossed 'not negotiable'. He later transfers the cheque to 'D' who gets the cheque encashed from XYZ Bank, which is not the Drawee bank. Sumit comes to know about the fraudulent act of 'K', sues XYZ Bank for the recovery of money. Examine with reference to the relevant provisions of the Negotiable Instruments Act, 1881, whether Sumit will be successful in his claim? Would your answer be still the same in case 'K' does not transfer the cheque and gets the cheque encashed from XYZ Bank himself?

[N17 – 4M] (RELATED TO THEORY Q.NO.29, 32 &33)

**PROVISION:** According to Section 130 of the Negotiable Instruments Act, 1881 a person taking cheque crossed generally or specially bearing in either case the words 'Not Negotiable' shall not have or shall not be able to give a better title to the cheque than the title the person from whom he took it had. In consequence, if the title of the transferor is defective, the title of the transferee would be vitiated(affected) by the defect.

Thus, based on the above provisions, it can be concluded that if the holder has a good title, he can still transfer it with a good title, but if the transferor has a defective title, the transferee is affected by such defects, and he cannot claim the right of a HDC by proving that he purchased the instrument in good faith and for value.

**CONCLUSION:** Since 'K' in the given case, had obtained the cheque fraudulently, he had no title to it and cannot give to the bank any title to the cheque or money; and the bank would be liable for the amount of the cheque for encashment. (*Great Western Railway Co. v. London and Country Banking Co.*). The answer in the second case would not change and shall remain the same for the reasons given above. Thus, 'Sumit' in both the cases shall be successful in his claim from XYZ Bank.

**Q.No.26.** A cheque is drawn upon Dena Bank. It is stolen by X who hands it over to Y who takes in good faith for valuable consideration. Y deposits the cheque into his own account in Canara bank who presents it and obtains payment from Dena Bank. Discuss the legal position of paying banker, collecting banker, Y and true owner in each of the following alternative cases (*i.e.* when each of the parties get discharged from their liability):

- a) If the Cheque is payable to bearer.
- b) If the Cheque is payable to bearer and is crossed generally
- c) If the Cheque is payable to bearer and is crossed generally with the words 'not negotiable'.
- d) If the Cheque is payable to bearer and is crossed specially with the words 'Canara bank'.
- e) If the Cheque is payable to bearer and is crossed specially with the words 'Allahabad bank'.
- f) If the Cheque is payable to B or order and X forges B's endorsement.
- g) If the Drawer's signatures was forged.

(RELATED TO THEORY Q.NO.32 & 33)

CASE	PAYING BANKER	COLLECTING BANKER	Y	TRUE OWNER
A)	Drawee banker is discharged by payment in due course.	Collecting banker does not incur any liability to the true owner.	He is not liable to true owner.	He can recover from X and not from Y.
B)	Drawee banker is discharged by payment in due course	Collecting banker does not incur any liability to the true owner	He is not liable to true owner	He can recover from X and not from Y
C)	Drawee banker is discharged by payment in due course	Collecting banker does not incur any liability to the true owner	He is liable to true owner because he got a defective title	He can recover from Y or X
D)	Drawee banker is discharged by payment in due course	Collecting banker does not incur any liability to the true owner	He is not liable to true owner	He can recover from X and not Y
E)	Drawee banker is liable to true owner	Collecting banker is liable to true owner	He is not liable to true owner	He can recover from X or paying banker or collecting banker
F)	Drawee banker is discharged by payment in due course	Collecting banker does not incur any liability to the true owner	He is not liable to true owner	He can recover from X and not from Y
G)	Drawee banker is liable to true owner because payment is not in due course	Collecting banker is liable to true owner	He is liable to true owner because forgery passes no title to all	He can recover from Y or paying banker or collecting banker

**Q.No.27. State whether presentment for acceptance is necessary in each of the following alternatives.**

- A bill payable on demand.
- A bill payable 30 days after date.
- A bill payable on 1<sup>st</sup> Jun. 2020.
- A bill payable 3 months after sight.
- A bill payable 3 months after presentment.
- A bill in which there is an express provision that it shall be presented for acceptance before it is presented for payment.
- Where the Drawee cannot be found after reasonable search.
- Where the Drawee is a fictitious person.
- Where the Drawee is a person incapable of contracting. (RELATED TO THEORY Q.NO.34)

**PROVISION:** As per section 61 of NI act, 1881, acceptance is required only for bill of exchange payable after sight (*Unless otherwise stated*). With respect to other bills there is no express provision in the Act requiring presentment of acceptance before presenting them for payment and there is nothing in the Act to prevent such bill being presented for acceptance. But If the bill is payable after sight or at sight or on demand then acceptance by the drawee is necessary before he can be held liable up on it.

**CONCLUSION:**

**Accordingly, Presentment is necessary in the following points:**

- A bill payable 3 months after sight.
- A bill payable 3 months after presentment.
- A bill in which there is an express provision that it shall be presented for acceptance before it is presented for payment

**Presentment is not necessary in the following points:**

- A bill payable on demand.
- A bill payable 30 days after date.
- A bill payable on 1<sup>st</sup> Jun.2020.
- Where the Drawee cannot be found after reasonable search.
- Where the Drawee is a fictitious person.
- Where the Drawee is a person incapable of contracting

**Q.No.28. State whether presentment for payment is necessary to charge the Drawer of instrument in each of the following cases:**

- A promissory note payable on demand and is not payable at a specified place.
- A promissory note or bill of exchange payable at a specified period after day of sight thereof.
- A bill is not payable at a specified place and the acceptor cannot after due search be found.
- A bill is payable at a specified place and neither the acceptor nor any person authorized to pay is present at such place during the usual business hours.
- If the drawer cannot suffer any damage for want of presentment.

(RELATED TO THEORY Q.NO.37 & 38)

- a) **PROVISION:** Presentment for payment is not necessary for a P/N payable on demand, which is not payable at a specified place.

**CONCLUSION:** Presentment is not necessary

- b) **PROVISION:** NI payable after date or sight must be presented for payment on the date of maturity.

**CONCLUSION:** Presentment is necessary

- c) **PROVISION:** If the instrument not being payable at any specified place, Payee cannot after due search be found.

**CONCLUSION:** Presentment is not necessary.

- d) **PROVISION:** If the instrument being payable at some other specified place, neither he nor any person authorized to pay it attends at such place during the usual business hours.

**CONCLUSION:** Presentment is not necessary.

- e) **PROVISION:** Presentment for payment is not necessary if the drawer could not suffer damage from the want of such presentment.

**CONCLUSION:** Presentment is not necessary.

**Q.No.29. X, in the course of business, gets a bill of exchange with three endorsements, those of A, B and C. What would be the result**

- a) If these endorsements are forged but C had taken the instrument for value without notice.

- b) If the signature of the Drawer is forged?

(RELATED TO THEORY Q.NO.40)

**PROVISION:** As per the provisions of NI Act, 1881, if the endorsement is blank, when a holder forges the signature of a prior holder and transfers it, Transferee may ignore the Forged endorsement and rely upon a prior endorsement in blank. He can make a good title through an earliest genuine endorsement in blank.

However, in case of full endorsement, if the endorsement is forged then the title of the instrument will become nullity and even HDC cannot get any title.

**CONCLUSION:**

**Case (a):** If the endorsements of A, B and C were in blank, and even if one of the endorsements of A, B and C were in blank, and even if one of the endorsements is genuine, X can obtain a good title through such genuine endorsement. X will become a Holder claiming under a HDC, i.e., C.

**Case (b):** Where the instrument is forged in respect of an endorsement and forgery as to signature of the drawer, it does not give any title to X, since it is a nullity and even a Holder in due course (i.e., C, even if he has paid value) cannot claim any protection title.

**Q.No.30. Mr. S Venkatesh drew a cheque in favor of M who was sixteen years old. M settled his rental due by endorsing the cheque in favor of Mrs. A the owner of the house in which he stayed. The cheque was dishonored when Mrs. A presented it for payment on grounds of inadequacy of funds. Advise Mrs. A how she can proceed to collect her dues.** [MTP2 - M19 (N), N18 (N) - 4M, N19 (O), MTP1 July 20]

(RELATED TO THEORY Q.NO.41)

**PROVISION:** Section 26 of the Negotiable Instruments Act, 1881- Capacity to make, etc., promissory notes, etc. Every person capable of contracting, according to the law to which he is subject, may bind himself and be bound by the making, drawing, acceptance, endorsement, delivery and negotiation of a promissory note, bill of exchange or cheque.

However, a minor may draw, endorse, deliver and negotiate such instruments so as to bind all parties except himself

As per the facts given in the question, Mr. S Venkatesh draws a cheque in favour of M, a minor. M endorses the same in favour of Mrs. A to settle his rental dues. The cheque was dishonoured when it was presented by Mrs. A to the bank on the ground of inadequacy of funds. Here in this case, M being a minor may draw, endorse, deliver and negotiate the instrument so as to bind all parties except himself.

**CONCLUSION:** Therefore, M is not liable. Mrs. A can, thus, proceed against Mr. S Venkatesh to collect her dues.

**Q.No.31. X draws a bill of exchange on Y. Y authorizes his agent Z to sign the bill on his behalf to signify acceptance of the same. Z while signing the bill did not indicate that he is signing it on behalf of Y. Will Z be personally liable? Discuss with reference to the provisions of the Negotiable Instruments Act, 1881. [N18 (O) - 4M] (RELATED TO THEORY Q.NO.41)**

**PROVISION:** Acceptance is required for Bill of Exchange only. It is a process by which Drawee accepts the Drawer's Bill of Exchange by signing the words 'Accepted' on the face of the bill.

As per Sec 26 and 27 of NI Act, 1881, Every person, capable of incurring liability, may bind himself or be bound by a duly authorized agent acting in his name. The agent may sign in two ways, viz.

- a) He may sign the principal's name. It is immaterial what hand actually signs the name of the principal, when in fact there exist an express authority.
- b) He may sign as an agent, by stating authority on the face of the instrument.

However, under general authority, agent will not get any power to make, draw, accept or endorse instruments on behalf of principal so as to bind his principal.

An agent may have authority to draw bills of exchange, but not endorse them. An authority to draw does not imply that he has authority to endorse.

**CONCLUSION:** In the given question, Z, the agent, while signing the bill of exchange, did not indicate that he is signing it on behalf of Y.

Since, Z did not indicate that he is signing the bill the exchange as an agent, he cannot escape personal liability unless he indicates that he signs as an agent and does not intend to incur personal liability.

**Q.No.32. M, a legal successor of N (a deceased person) signs a bill of exchange in his own name admitted a liability of Rs. 50,000, i.e. the extent to which he inherits the assets from the deceased person, payable to P, after 3 months from 1st January. On maturity, when P presents the bill to M, he (M) refuses to pay for the bill on the ground that since the original liability was that of N, the deceased therefore he is not liable to pay for the bill. Decide whether P can succeed in recovering Rs.50,000 from M. (RELATED TO THEORY Q.NO.42)**

**PROVISION:** As per section 29 of the NI Act, 1881, a legal representative of a deceased person who signs his name to a negotiable instrument is personally liable on that instrument. However, he can expressly limit his liability to the extent of the assets received by him.

**CONCLUSION:** Thus, M cannot refuse to pay the amount since he has inherited the assets of the deceased. He will be liable to the extent of full amount of the bill, even if he has inherited the property valued less than the amount of the bill. M will be liable for the amount of Rs. 50,000. Therefore P can succeed in recovering 50,000 from legal representative of deceased person.

**Q.No.33. A draws and B accept the bill payable to C or order. C endorses the bill to D and D to E, who is a holder-in-due course. From whom E can recover the amount? Examining the right of E, state the privileges of the holder-in-due course provided under the Negotiable Instruments Act, 1881. [OLD PM, N12 - 8M, RTP - N16] (RELATED TO THEORY Q.NO.19 & 42)**

**PROVISION:** Section 36 of the NI Act, 1881 describes the liabilities of prior parties to the HDC. A HDC has privilege to hold every prior party to a negotiable instrument liable on it until the instrument is duly satisfied. Here the HDC can hold all the prior parties liable jointly and severally. Prior parties include the maker or drawer, acceptor and endorsers.

**CONCLUSION:** Accordingly, in the given case, E, a HDC can recover the amount from all the prior parties i.e. D & C (i.e. endorser), B (Acceptor) and A (Drawer).

(Privileges of a "HDC": You can write the answer given in Theory questions)

**Q.No.34. X obtains Y's acceptance to a Bill by fraud. X endorses it to Z who takes it in good faith for valuable consideration. Z endorses the bill to F who knows of the fraud. Discuss the rights of X, and Z.**

(Or)

**B obtains A's acceptance to a bill of exchange by fraud. B endorses it to C who is a holder in due course. C endorses the bill to D who knows of the fraud. Referring to the provisions of the Negotiable Instruments Act, 1881, decide whether D can recover the money from A in the given case.**

[OLD PM, MTP - N18] (RELATED TO THEORY Q.NO.19 & 42)

**PROVISION:**

- a) **Liability of parties to holder in due course (Sec.36):** Every prior party (i.e., maker or drawer, acceptor and all intervening endorser) to an instrument is liable to a holder in due course until the instrument is satisfied. Thus, prior parties of a note are jointly and severally liable for the payment and may be sued jointly.
- b) **A holder, who derives title from holder in due course has the same rights as of that holder in due course (Sec.53):** Once a negotiable instrument passes through the hands of a HDC, it gets cleansed of all its defects provided the holder himself is not a party to the fraud or illegality which affected the negotiable instrument in some stage of its journey.

**CONCLUSION:** By applying the above provisions:

- a) X cannot recover from Y because X is not a holder in due course.
- b) Z can recover from X or Y because Z is a holder in due course.
- c) F can recover from X, Y and Z because F derives the title from Z who is a holder in due course and at the same time Z is not a party to fraud though he was aware of the fraud. [Sec 58].

**Q.No.35. Promissory note dated 1<sup>st</sup> Feb, 2017 payable two months after the date was presented to the maker for payment 10 days after maturity. What is the date of Maturity in this case? Explain with reference to the relevant provisions of the Negotiable Instruments Act, 1881 whether the endorser and the maker will be discharged by reasons of such delay. [OLD PM] (RELATED TO THEORY Q.NO.44)**

**PROVISION: Date of Maturity:** If a promissory note is made payable stated number of months after date, it becomes payable 3 days after the corresponding date of months after the stated number of months. (Sec 23 read with sec 22 NI Act, 1881)

Therefore, in this case the date of maturity of the promissory note is 4<sup>th</sup> April, 2017.

**Delay in presentment for payment of a promissory note:** As per sec 64 of NI Act read with sec 66, a promissory note must be presented for payment at maturity by on behalf of the holder.

In default of such presentment, the other parties of the instrument (i.e., *parties other than the parties primarily liable*) are not liable to such holder. In the given case the promissory note was presented for payment was 10 days after maturity.

**CONCLUSION:** By applying the above provisions, the endorser is discharged by the delayed presentment for payment. But the maker being the primary party liable on the instrument continues to be liable.

**Q.No.36. 'A' is the holder of a bill of exchange made payable to the order of 'B'. The bill of exchange contains following endorsements in the blank. First endorsement 'B', second endorsement 'C', third endorsement 'D', fourth endorsement 'E' - 'A' strikes out, without E's consent, the endorsement by 'C' and 'D'. Decide with reasons whether 'A' is entitled to recover anything from 'E'. [RTP - M18 (N), MTP - M15, N09 - 5M, N12 - 8M, N17 - 4M, N18 (O) - 4M]**

(RELATED TO THEORY Q.NO.44)

**PROVISION:** According to section 40 of the Negotiable Instruments Act, 1881, where the holder of a negotiable instrument, without the consent of the endorser, destroys or impairs the endorser's remedy against a prior party, the endorser is discharged from liability to the holder to the same extent as if the



instrument had been paid at maturity. Any party liable on the instrument may be discharged by the intentional cancellation of his signature by the holder.

In the given question, A is the holder of a bill of exchange of which B is the payee and it contains the following endorsement in blank:

First endorsement, 'B'

Second endorsement, 'C'

Third endorsement, 'D'

Fourth endorsement, 'E'

'A', the holder, may intentionally strike out the endorsement by 'C' and 'D'; in that case the liability of 'C' and 'D' upon the bill will come to an end. But if the endorsements of 'C' and 'D' are struck out without the consent of 'E', 'A' will not be entitled to recover anything from 'E'. The reason being that as between 'D' and 'E', 'D' is the principal debtor and 'E' is surety. If 'D' is released by the holder under Section 39 of the Act, 'E', being surety, will be discharged. Hence, when the holder without the consent of the endorser impairs the endorser's remedy against a prior party, the endorser is discharged from liability to the holder.

**CONCLUSION:** Thus, if 'A' strikes out, without E's consent, the endorsements by 'C' and 'D', 'E' will also be discharged.

**Q.NO.37. Do the following alterations of a negotiable instrument are Material Alteration?**

- a) The holder of a bill alters the date of the instrument to accelerate or postpone the time of payment. [OLD PM]
- b) The drawer of a negotiable instrument draws a bill but forgets to write the words 'or order'. Subsequently, the holder of the instrument inserts these words. [OLD PM]
- c) A bill payable 3 months after date is altered into a bill payable three months after sight. [OLD PM]
- d) A bill was dated 2018 instead of 2019 & subsequently the agent of the drawer corrected the mistake. [OLD PM]
- e) A bill is accepted payable at the Union Bank, and the holder, without the consent of the acceptor, scores out the name of the Union Bank and inserts that of the Syndicate Bank. [OLD PM]
- f) A bill payable with 'lawful interest' is altered into one payable with 12% interest.
- g) A bill is accepted payable at the Indian Bank, Sarita Vihar, New Delhi. The holder without the consent of the acceptor scores out Sarita Vihar and inserts Chandni Chowk instead.
- h) D in possession of an inchoate instrument where the amount has not been written on the instrument, writes the amount himself.
- i) K in possession of an uncrossed cheque received from A, writes "Payees Account only" on the face of the instrument. [OLD PM]
- j) A promissory note was made without mentioning any time for payment. The holder added the words "on demand" on the face of the instrument. [N19 (N) - 4M, M19 (N) - 2M]
- k) A bill "payable to X" is converted into a bill "payable to X and Y". [OLD PM]
- l) The holder of the bearer cheque converts it into account payee cheque [OLD PM]

(RELATED TO THEORY Q.NO.45)

ANSWER	REASONS
a) Yes	Alteration in the time of payment affects the character of the instrument.
b) No	Addition of words to 'or order' to an Order instrument does not affect the character of instrument
c) Yes	Alteration in the time of payment affects the character of instrument.
d) No	Correction of mistakes in Instrument does not affect the character of instrument
e) Yes	Alteration of operation of instrument affect the character of instrument
f) Yes	Since lawful interest is 18% under the Banking, Public Financial Institutions & Negotiable Instruments (Amendment) Act, 1988.
g) Yes	Addition of new party to an instrument affects the character of instrument.
h) No	Filling blanks of an inchoate instrument does not affect the character of instrument
i) Yes	Crossing of Cheques affects the character of instrument

j) No	Addition of words to 'on demand' to a Demand instrument does not affect the character of instrument.
k) Yes	Addition of new party to an instrument affects the character of instrument.
l) Yes	Crossing of Cheques affects the character of instrument

**Q.No.38. Ram has Rs. 2000 in his bank account and has no authority to overdraft. He issued a cheque for Rs.5000 to Gopal which was dishonoured by the bank. Point out whether Gopal must necessarily give notice of dishonoured to Ram under NI Act 1881.**

[OLD PM, M14 - 4M]

(RELATED TO THEORY Q.NO.54)

**PROVISION:** Sec.98 of the NI Act, 1881 prescribes the cases in which notice of dishonour is not necessary.

This includes and also states when drawer has not sufficient balance and issues cheque of excess amount and also has no authority to overdraft and if that cheque was dishonoured by bank then notice is not required to be given to drawer.

**CONCLUSION:** In the present case, the conditions mentioned in Sec.98 have been satisfied. Therefore, no notice is required.

**Q.No.39. A issued a cheque for Rs.25000 in favour of B. A has sufficient amount in his account with the Bank. The cheque was not presented within a reasonable time to the Bank for payment and the Bank fails in the meantime. Decide under the provisions of NI Act, 1881, whether B can recover the money from A?**

(Or)

[OLD PM, RTP – N15, MTP - M18 (O)]

A' issued a cheque for Rs.5000/- to 'B'. 'B' did not present the cheque for payment within a reasonable period. The Bank fails. However, when the cheque was ought to be presented to the bank, there was sufficient fund to make payment of the cheque. Now, 'B' demands payment from 'A'. Decide the liability of 'A' under the NI Act, 1881.

[OLD PM, M14 – 4M, MTP - M18 (N)]

(RELATED TO THEORY Q.NO.56)

**PROVISION:** As per Sec 84 of the NI Act, 1881, where a cheque is not presented by the holder for payment within a reasonable time of its issue and the drawer suffers actual damage through the delay because of the failure of the bank, he is discharged from liability to the extent of such damage.

In determining what is reasonable time regard shall be had to the nature of the instrument and the usual course of dealing with respect to similar instrument; and, in calculating such time, public holidays shall be excluded (Sec. 105).

But the holder of the cheque will be treated as creditor of the bank, in place of drawer. He will be entitled to recover the amount from Bank. [Sec 84(3)]

**CONCLUSION:** Hence, the drawer is discharged from the liability to pay the amount of cheque to B. However, B being a creditor of bank can recover the amount of cheque from bank.

**Q.No.40. A cheque was dishonoured at the 1<sup>st</sup> instance and the payee did not initiate action. The cheque was presented for payment for the 2<sup>nd</sup> time and again it was dishonoured. State in this connection whether the payee can subsequently initiate prosecution for dishonour of cheque.**

[OLD PM]

(RELATED TO THEORY Q.NO.57)

**RELEVANT CASE LAW:** Sadanandan Bhadran v. Madhavan Sunil Kumar.

**PROVISION:** In the above case, Supreme Court held that on a careful analysis of Sec. 138 of the NI Act, 1881 it is seen that a cheque is said to be dishonoured when it is returned by the bank unpaid for any of the reasons mentioned therein. The said proviso lays down 3 conditions for the applicability of the above section. They are:

- The cheque should have been presented to the bank within 3 months;
- Within 30 days of receipt of information from Bank, Payee or Holder in due course has demanded payment on cheque from Drawer, in written form.
- The drawer should have failed to pay the amount within 15 days of the receipt of notice.

Prosecution u/s 138 can be launched only when all the 3 conditions are satisfied.

So far as the first condition is concerned, proviso to sec 138(a) does not put any restriction upon the payee to successively present a dishonoured cheque during the period of validity.

It is not uncommon for a cheque being presented again and again within its validity period in the expectation that it would be encashed.

Sec.138 apparently conflicts with sec 142(c) of the Act. Sec.138 enables the payee to repeatedly present the cheque but Sec.142(c) gives him only one opportunity to file a complaint for its dishonour and that too within one month from the date the cause of action arises.

The Court held that the 2 provisions can be harmonized with the interpretation that on each presentation of the cheque and its dishonour, a fresh right and not cause of action accrues in his favour.

**Conclusion:** Therefore, the holder / payee of a cheque cannot initiate prosecution for an offence u/s 138 for its dishonour for the second time, if he had not initiated such prosecution on the earlier cause of action.

**Q.No.41. Whether giving of notice of dishonour itself constitutes receipt of notice for constituting offence u/s 138 of the Negotiable Instruments Act, 1881. [OLD SM] (RELATED TO THEORY Q.NO.57)**

**RELEVANT CASE LAW:** Dalmia Cement (Bharat) Ltd Vs. Galaxy Traders and Agencies Ltd

**PROVISION:** The Court observed that, the payee has to make a demand by giving notice in writing and it is a failure on the part of the drawer to pay the amount within 15 days of the receipt of the said notice. Then the drawer of the Cheque is liable u/s 138 of the NI Act, 1881. Giving notice in writing is a process for which receipt is the accomplishment.

**CONCLUSION:** Hence, it is clear that 'giving of notice' is not the same as 'receipt of notice' for constituting offence under this Act.

**Q.No.42. X draws a cheque in favour of Y. After having issued the cheque he informs Y not to present the cheque for payment. He also informs the bank to stop payment. Decide, under provisions of the NI Act 1881; whether the said acts of X constitute an offence against him?**

**Mr. D, a drawer issues the cheque in favour of the E. Later D informs the E not to present the cheque due to inadequacy of the fund in the account because of withdrawal of the money in urgency as well as informs the bank to stop payment. Does the act of D constitute an offence under the Act?**

**Examine, whether there is an offence under the NI Act, 1881, if a drawer of a cheque after having issued the cheque, informs the Drawee not to present the cheque as well as informs the bank to stop the payment.** (RELATED TO THEORY Q.NO.57)

**PROVISION: Offence under the NI Act, 1881:** The Supreme Court in *Modi Cements Ltd. vs. Kuchil Kumar Nandi* [1998] 2 CLJ 8 held that once a cheque is issued by the drawer, a presumption u/s 139 of the NI Act, 1881 follows and merely because the drawer issues a notice thereafter to the Drawee or to the bank for stoppage of payment, it will not prevent an action u/s 138.

The object of Sec 138 to 142 of the Act is to promote the efficacy of the banking operations and to ensure credibility in transacting business through cheques.

As per Sec.138 (Penal Provision) of NI Act, 1881,

- Once a cheque is drawn on specified banker to discharge a legally enforceable debt or other liability.
- He is informed by the bank about non-payment of cheque either because of insufficiency of amount to honour the cheques or the amount exceeding the arrangement made with the bank,
- Such a person shall be deemed to have committed an offence.

**CONCLUSION:** Thus, X (Drawer) is liable to have committed an offence u/s 138 of the NI Act, 1881.

**Q.No.43. V makes a gift of Rs.10000 to W through a cheque issued in favour of W. Later he (V) informs W not to present the cheque for payment and informs the bank also to stop payment. Examining the provisions of the NI Act, 1881, decide whether V's above acts constitute an offence.** (RELATED TO THEORY Q.NO.57)

**PROVISION:** Sec 138 of the NI Act - Dishonour of cheque for insufficiency, etc., of funds in the A/c,

Sec 139 of the NI Act - Presumption in favour of holder. A cheque is liable u/s 138 only if a cheque is issued to discharge a legally enforceable debt or other liability.

Presumption of consideration is not applicable because it can be proved that the cheque was given as a gift (Sec.139)

In the present case, the cheque has been issued by V as a gift to W, and not for discharge of a legally enforceable debt or other liability. (Sec. 138)

**CONCLUSION:** V is not liable for an offence u/s 138.

**Q.No.44. For cognizance of offence for the dishonour of cheque, should the cheque necessarily be presented to the Drawee's (payee's) bank or can it be presented before any bank within the stipulated period?** [OLD PM] (RELATED TO THEORY Q.NO.57)

**PROVISION:** The "Bank" referred under proviso to sec 138 (a) of the NI Act, 1881, mean the 'Drawee-bank' on which the cheque is drawn and not all banks where the cheque is presented for collection including the bank of the payee, in whose favour the cheque is issued.

**CONCLUSION:** Cheque must be presented to Drawee's bank within the specified period in order to make drawer liable under Sec 138.

**Q.No.45. A promoter who has borrowed a loan on behalf of company, who is neither a director nor a person-in-charge, sent a cheque from the companies account to discharge its legal liability. Subsequently the cheque was dishonoured and the complaint was lodged against him. Does he liable for an offence u/s 138?** [OLD PM, M16 - 5M] (RELATED TO THEORY Q.NO.58)

**PROVISION:** As per sec 138, where any cheque drawn by a person on an account maintained by him with a banker for payment of any amount of money to another person from/out of that account for discharging any debt or liability, and if it is dishonoured by banker on sufficient grounds, such person shall be deemed to have committed an offence and shall be liable.

However, in this case, the promoter is neither a director nor a person-in-charge of the company and is not connected with the day-to-day affairs of the company and had neither opened nor is operating the bank account of the company.

Further, the cheque, which was dishonoured, was also not drawn on an account maintained by him but was drawn on an account maintained by the company.

**CONCLUSION:** Therefore, he has not committed an offence u/s 138.

**Q.No.46. J, a shareholder of a Company purchased for his personal use certain goods from a Mall (Departmental Store) on credit. He sent a cheque drawn on the Company's account to the Mall (Departmental Store) towards the full payment of the bills. The cheque was dishonoured by the Company's Bank. J, the shareholder of the company was neither a Director nor a person in-charge of the company.**

**Examining the provisions of the NI Act, 1881 state whether J has committed an offence u/s 138 of the Act and decide whether he (J) can be held liable for the payment, for the goods purchased from the Mall (Departmental Store)** [OLD PM, RTP - N15, RTP (O) - N17] (RELATED TO THEORY Q.NO.58)

**RELEVANT CASE LAW:** H.N.D. Mulla Feroze Vs. C.Y. Somayajulu

**PROVISION:** The Andhra Pradesh High Court held that although the petitioner has a legal liability to refund the amount to the appellant, petitioner is not the drawer of the cheque, which was dishonoured and the cheque was also not drawn on an account maintained by him but was drawn on an account maintained by the company.

Hence, it was held that the petitioner could not be said to have committed the offence u/s 138.

**CONCLUSION:** Hence, J is not liable for the cheque but legally liable for the payments for the goods.

**Q.No.47.** Bharat executed a promissory note in favour of Bhushan for Rs.5 Crores. The said amount was payable three days after sight. Bhushan, on maturity, presented the promissory note on 1<sup>st</sup> January 2008 to Bharat. Bharat made the payments on 4<sup>th</sup> January 2008. Bhushan wants to recover interest for one day from Bharat. Advise Bharat, in the light of provisions of the NI Act, 1881, whether he is liable to pay the interest for one day?

[NEW SM, OLD PM, M16, N16, N17, RTP - M15, MTP - M15]

(RELATED TO THEORY Q.NO.59)

**PROVISION:** Sec 24 of the NI Act, 1881 – states that where a bill or note is payable after date or after sight or after happening of a specified event, the time of payment is determined by excluding the day from which the time begins to run.

In the given case Promissory note was presented for sight on 1st January, which is to be excluded for computing due date and the Promissory Note is payable on 4th January.

Bharat paid rightly paid on 04th January “three days after sight”.

**CONCLUSION:** Therefore, in the given case, Bharat will succeed in objecting to Bhushan’s claim for payment of interest for one day. (i.e. he need not pay interest for 1 day).

**Q.No.48.** X accepts a bill for the accommodation of A (drawer). A transfers it to B, without consideration. B transfers it to C without consideration. C transfers it to D for value. D transfers it to E without consideration. On the due date, the bill is dishonoured by X. Discuss the rights of A, B, C, D and E. [OLD PM, M17, RTP – M16, RTP - M18 (O), MTP – M16, M19 (N) – 2M, N20 (N)-3]

(RELATED TO THEORY Q.NO.60)

**PROVISION:** Sec 43 of the NI Act, 1881 provides that a negotiable instrument made, drawn, accepted or endorsed without consideration, creates no obligation of payment between the parties to the transaction.

But if any such party has transferred the instrument to a holder for consideration, such holder, and every subsequent holder deriving title from him, may recover the amount due on such instrument from the transferor or any prior party thereto.

**CONCLUSION:** By applying the above provisions.

- a) A cannot recover from X because a negotiable instrument without consideration creates no obligation of payment between the parties to the transaction.
- b) B cannot recover from X and A because a negotiable instrument without consideration creates no obligation of payment between the parties to the transaction.
- c) C cannot recover from B, X and A because a negotiable instrument without consideration creates no obligation of payment between the parties to the transaction.
- d) D can recover from X, A, B and C because all prior parties to the instrument are liable to holder-in-due course.
- e) E can recover from X, A, B and C because a person who derives the instrument from holder-in-due course will get the same rights as that of the holder-in-due course.

**Q.No.49.** A draws a bill of exchange on B for Rs.1000 payable to the order of A. B accepts the bill but subsequently dishonours it by non-payment. A sues B on the bill. B proves that it was accepted for value of Rs.800 and as an accommodation to the plaintiff for the balance amount i.e., Rs.200. Can A recover Rs.1000 from B? [OLD PM, N10 - 8M, M18 (O) - 4M]

(Or)

P draws a bill on Q for Rs.10000. Q accepts the bill. On maturity the bill was dishonoured by non-payment. P files a suit against Q for payment of Rs.10000. Q proved that the bill was accepted for value of Rs.7000 and as an accommodation to the plaintiff for the balance amount i.e. Rs.3000. Referring to the provisions of the NI Act, 1881 decide whether P would succeed in recovering the whole amount of the bill? [OLD PM, M18 (O) - 4M, MTP - M16, MTP2 - M19 (N), MTP - N19 (N)]

(RELATED TO THEORY Q.NO.60)

**PROVISION:** As per Section 44 of the Negotiable Instruments Act, 1881, when the consideration for which a person signed a promissory note, bill of exchange or cheque consisted of money, and was originally absent in part or has subsequently failed in part, the sum which a holder standing in immediate relation with such signer is entitled to receive from him is proportionally reduced.

The drawer of a bill of exchange stands in immediate relation with the acceptor. The maker of a promissory note, bill of exchange, or cheque stands in immediate relation with the payee, and the endorser with his endorsee.

**CONCLUSION:** On the basis of above provision, P would succeed to recover Rs. 7,000 only from Q and not the whole amount of the bill because it was accepted for value as to Rs.7,000 only and an accommodation to P for Rs.3,000.

**Q.No.50. A executed a promissory note in favour of B. Without B's demanding payment, A paid the money due on the note but left the note in his hands. Subsequently B endorsed it to C for consideration. C had knowledge of the payment made by A. C brings a suit against A and B for recovery of money on the note. Will he succeed against either or both? [OLD PM]**  
(RELATED TO THEORY Q.NO.61)

**PROVISION:** As per sec.9 of the NI Act, Holder in due course means any person who,

- For consideration, became the possessor of a promissory note, bill of exchange or cheque, if payable to the bearer, or the payee or endorsee thereof, if payable to the order,
- Before the amount mentioned in it became payable, and
- Without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title."

As per sec 58 - If the instrument is obtained from Maker, Acceptor or Holder by way of fraud (unlawful means) or for unlawful consideration then endorsee is not entitled to receive amount.

However, holder in due course is entitled to claim the amount

**CONCLUSION:** By applying the above provisions he can succeed against A as well as against both as per Sec 9 and 58 of the NI Act, 1881.

**ALTERNATIVE ANSWER IN OUR VIEW:** He cannot succeed against A. he can succeed against B per Sec 9 and 58 of the NI Act, 1881.

**Q.NO.51. A bill is dishonoured by non-acceptance. The bill is endorsed to A. A endorses it to B. As between A & B, the bill is subject to an agreement as to the discharge of A. The bill is afterwards endorsed to C, who takes it with notice of dishonour. Decide, with reason, whether C is entitled to accept the bill in the capacity of a holder in due course. (RELATED TO THEORY Q.NO.61)**

**PROVISION:** As per section 59, if a holder acquires any instrument after its dishonour or after maturity, along with notice thereon, then holder has the rights thereon of his transferor (as against the other parties).

**CONCLUSION:** C takes the bill subject to the agreement between A and B, and cannot have a better title than his transferor B. Further, C is not a holder in due course u/s 9 because he has not acquired the NI before it became payable, [i.e. C has acquired the B/E after its dishonour by non-acceptance].

## SECTION 7: THINGS TO REMEMBER

### IMPORTANT SECTION NUMBERS:

CONCEPT	SECTION NO.
Promissory note	4
Bill of exchange	5
Cheque	6
Holder	8
Holder in due course	9

Payment in due course	10
Inland instruments	11
Foreign instruments	12
Negotiable instrument	13
Ambiguous instruments	17
Inchoate instruments	20
Liability of prior parties to HDC	36
Fictitious bill	42
Delivery	46
Effect of endorsement	50
Sans recourse endorsement	52
Notice of dishonor	93 & 94
Notice of dishonour is not necessary	98
Noting	99
Protest	100
Drawee in case of need	115
Presumptions	118
General crossing	123
Special crossing	124
Crossing after issue	125
Payment of crossed cheques	126
Payment in due course of crossed cheque	128
Payment out of due course of crossed cheque	129
Not negotiable crossing of cheque	130
Punishment for Dishonour of Cheque in case of insufficiency of funds	138
Cognizance of offence	142

**PEANLTIES – TO REMEMBER:**

DEFAULT	PENALTY
Penalty for dishonour of a cheque specified u/s 138 of the NI Act, 1881.	<p><u>Drawer</u> shall be punishable with:</p> <ul style="list-style-type: none"> <li>• The penalty can be up to 2 years imprisonment or</li> <li>• fine up to twice the amount of cheque or</li> <li>• Both.</li> </ul> <p>In addition to above penalty, Drawer still liable to make payment of the cheque which was dishonoured.</p>

**TIME LIMITS – TO REMEMBER:**

PARTICULARS	TIME-LIMIT
Maximum time limit for acceptance of bill	48 hours from the presentation of bill for acceptance
Maximum time limit for depositing cheque	3 months from the date mentioned in the cheque
Time limit for giving notice of dishonour by the holder of the cheque to the drawer	30 days from the date of receipt of intimation of dishonour of the cheque from the bank.
Time limit to the drawer for payment of money in respect of dishonour of cheque	15 days from the date of receipt of notice from the payee or the holder
Time limit for filing a case against the drawer for the dishonour of cheque	1 month from the expiry of above 15 days.

## SECTION 8: CASE LAWS FOR STUDENTS SELF STUDY

**AKBAR KHAN vs ATTAR SINGH:** In the given case a document was made with the following words, "This receipt is hereby executed by B ... for Rs.43,000 received from A, the amount to be payable after two years. Interest @ Rs.5% to be charged". Held the instrument was not a promissory note as it was a mere receipt stating the terms of repayment.

**BEARDSLEY vs BALDWIN:** In the given case a promissory note was made with the following words, "I promise to pay B Rs.500 seven days after my marriage with M or S". It was held that this instrument is not a promissory note because the promise to pay is not unconditional. A written undertaking to pay a certain amount within a specified time after defendant's marriage was not recognized as a promissory note because possibly the defendant may never marry, and the sum may never become payable.

**WILSON & MEESON vs PIKERING:** W drew a cheque crossed "Not Negotiable" in blank and handed it to his clerk to fill in the name and amount. The clerk inserted a sum in excess of her authority and delivered the cheque to P in payment of a debt of her own. Held, the clerk had no title to the cheque and as such P had no better title, and therefore W was not liable.

**MYSORE STATE ROAD TRANSPORT CORPORATION vs SOMASHANKAR:** Every unsubstantial alteration is not a material alteration, it is only such alterations as would adversely affect the interests of the other side which can be called material. In a P/N, if the rate of interest was left blank, and was filled up later without the consent of the promisor, it will be a material alteration invalidating the instrument.

**NENU RAM vs SHRI KISHEN :** Notice of dishonour must be given within a reasonable time. A Notice of dishonour given after 4 years after dishonour is not considered to be within reasonable time, it is for the Plaintiff to prove that want of notice of dishonour caused no damage to the Drawer.

**BEVERIDGE vs BURGIS:** Delay caused by circumstances beyond the control of the party desiring to serve notice is excused, provided it is not imputable (guilty) to his default, misconduct or negligence.

**INMARK FINANCE&INVT.CO.PVT.LTD.AND ANOTHER vs METROPOLITAN MAGISTRATE, BOMBAY AND OTHERS::** In order to attract the provisions of sec.138 of Negotiable Instruments Act, it is necessary that cheques are issued in discharge of a debt or a liability. Unless cheques are so issued, the drawer will not be guilty of offences under Sec. 138 even if other conditions are fulfilled.

**SADANANDAN BHADRAN vs MADHAVAN SUNIL KUMAR:** Notice can be served by ordinary post or even telegram. But, the onus of proof of service of notice shall lie on the petitioner. If notice is served within the said 30 days, no fresh cause of action can be created by presenting the cheque again.

**ARAB BANK LTD VS ROSS:** The payee in the promissory note was described as F.N&CO., whereas endorser endorsed the note as F and F.N. omitting the words 'company'. Held, the endorsee did not constitute to be a HDC since the endorser and the payee appeared to be different person making the instrument not complete and regular on the face of it.

**BAHADUR CHAND vs GULAB RAI A.I.R. LAH 577:** The failure to present the bill to drawee in case of need absolves the drawer from liability.

**DORE vs KANCHIWALLA & CO.:** If a bill of exchange has been duly accepted but dishonoured when presented to drawee in the first instance for payment, it cannot be validly presented for payment to the drawee in case of need if it was not first presented to him for acceptance.

**DENA BANK vs K.K. ALEX:** In the given case payment on a traveler cheque was made to a wrong person who forged the signatures of the holder while collecting payment, the payment was not held to be in due course.

**VENKITA SIVARAMAN PRASAD vs RAJESWARI CONSTRUCTIONS:** The essential ingredient to take cognizance of the offence u/s 138 is that there should be a complaint in writing by the payee, and the said complaint should disclose an offence u/s 138.

**HITEN SAGAR vs IMC LTD:** Where a person has drawn a cheque for the discharge of the liability of another person without creating any document, it will not and would not come u/s 138.

**RAJNEESH AGGARWAL vs AMIT J BHALLA:** To invoke the liability of the company, Notice of Dishonour should be served on the Company. However, Notice served on the Director who had signed the cheque was held valid.



**SADANANDAN BHADRAN vs MADHAVAN SUNIL KUMAR:** The combined reading of sec.138 and sec.142 leave no room for doubt that cause of action within the meaning of sec.142(c) arises and can arise only once. As to apparent conflicting provisions of the act, i.e., - (i) the payee can repeatedly present the cheque, but (ii) he is given only one opportunity to file a complaint for its dishonor within one month from the date of cause of action, it was held that – the two provisions can be harmonized with the interpretation that on each presentation of the cheque and its dishonor, a fresh right and not cause of action accrues in his favour.

**MODI CEMENTS LTD vs KUCHIL KUMAR NANDI:** Once a cheque is issued by the drawer, a presumption u/s 139 follows and merely because the drawer issues a notice thereafter to the Drawee or to the Bank for stoppage of payment, it will not preclude an action u/s 138.

**ET&T DEV CORP. LTD vs INDIAN TECHNOLOGIES & ENGINEERS (ELEC.) P.LTD.:** Once a cheque has been drawn and issued to the payee who has in turn presented to the Banker for payment and thereafter if any stop instructions are issued to the Banker, it amounts to dishonor of the cheque and is mischief under sec.138.

**THOMAS VARGHESE vs V.P. JEROME:** If the cheque was stopped by the drawer the complaint cannot be quashed.

## SECTION 9: PRACTICAL QUESTIONS FOR STUDENTS SELF STUDY

**Q.NO.1** What do you mean by an acceptance of a negotiable instrument? Examine validity of the following in the light of the provisions of the Negotiable Instruments Act, 1881:

An oral acceptance

An acceptance by mere signature without writing the word “accepted”.

[OLDPM]

(RELATED TO THEORY Q.NO.7)

**MEANING OF ACCEPTANCE:** Bill of exchange requires acceptance. A bill is said to be accepted when the drawee, after putting his signature on it, either delivers it or gives notice of such acceptance to the holder of the bill or to some person on his behalf. Upon acceptance Drawee becomes acceptor and he is liable for payment of the Bill.

Acceptance may be either general or qualified.

- a) The acceptance is qualified when the drawee accepts the bill subject to some qualification.
- b) A general acceptance is the acceptance where the acceptor assents without qualification to the order of the drawer.

### **VALIDITY OF ACCEPTANCE:**

- a) It is one of the essential elements of a valid acceptance that the acceptance must be written on the bill and signed by the drawee. An oral acceptance is not sufficient in law. Therefore, an oral acceptance of the bill does not stand to be a valid acceptance.
- b) The usual form in which the drawee accepts the Instrument is by writing the word ‘accepted’, across the face of the bill and signing his name underneath. The mere signature of the drawee without the addition of the words ‘accepted’ is a valid acceptance. As the law prescribes no particular form for acceptance, there can be no difficulty in construing acknowledgement as an acceptance, but it must satisfy the requirements of Section 7 of the NI Act, 1881 i.e. it must appear on the bill and must be signed by the drawee.

**Q.NO.2** An acceptor accepts a “Bill of Exchange” but writes on it “Accepted but payment will be made when goods delivered to me are sold.” Decide the validity. (RELATED TO THEORY Q.NO.7)

**PROVISION:** 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. If Holder accepts a qualified acceptance without obtaining the consent of the prior parties thereto, then all the prior parties whose consent was not so obtained are discharged.

**CONCLUSION:** Thus, in the given case, Acceptance is qualified in nature. So, the Holder is entitled to treat the bill as dishonoured due to non-acceptance. However, if the holder accepts the qualified acceptance, it binds only the Holder and the Acceptor and not the other parties who do not consent to such qualified acceptance.

**Q.NO.3 A bill is drawn as “pay to X or order the sum of ten thousand rupees “. In the margin the amount stated is Rs 1000. Discuss the legal position. (RELATED TO THEORY Q.NO.14)**

**PROVISION:** According to sec.18 of the NI Act,1881, if the amount undertaken or ordered to be paid is differently stated in figures and in words, the amount stated in words shall be the amount undertaken or ordered to be paid.

**CONCLUSION:** In light of the above provisions, this bill is a valid bill for Rs. 10,000 because in case of discrepancy between the amount stated in figure and in words, the amount stated in words shall be the amount of the instrument.

**Q.NO.4 A signs, as the maker, a blank stamped paper and gives it to B and authorizes him to fill it as a note for Rs.2,000, it being the amount of advances made by B to A. B fraudulently fills it up as a note for Rs.3,000 and then, for consideration, endorses it to C. Can C enforce the instrument?**

(Or)

'A' signs, as maker, a blank stamped paper and gives it to 'B', and authorizes him to fill it as a note for Rs.500, to secure an advance which 'B' is to make to 'A'. 'B' fraudulently fills it up as a note for Rs.2,000, payable to 'C', who has in good faith advanced Rs.2,000. Decide with reasons, whether 'C' is entitled to recover the amount, and if so, up to what extent?

**[OLD PM] (RELATED TO THEORY Q.NO.15)**

**PROVISION:** As per sec 20 of the NI Act, 1881, An Inchoate stamped instrument means an instrument that is incomplete in certain aspects.

In case of Inchoate instrument, the person signs and delivers a blank or incomplete instrument to another person and authorizes such person to complete the Instrument.

The holder gets a prima facie authority to make or complete it as a negotiable instrument.

HDC can recover the whole amount specified in the instrument but not exceeding the amount covered by the stamp affixed on the instrument.

Holder (any person other than HDC) cannot recover the amount in excess of the amount intended to be paid by the person delivering the inchoate instrument.

**CONCLUSION:** Applying the above provisions, C can enforce the instrument, provided the following two conditions are satisfied:

- a) C is a holder in due course. (In NI Act, 1881, every holder is deemed to be a holder in due course).
- b) The amount filled in i.e. Rs.3000 is covered by stamp amount.

**Q.NO.5 State the law as to calculation of the maturity of negotiable instrument the due dates in the following cases of the instruments: (RTP - N13)**

**A bill of exchange dated 20th Nov 2016, payable 4 months after date**

**A note is made payable 60 days after sight. The note is presented for sight on 15th Apr 2017.**

**(RELATED TO THEORY Q.NO.16)**

**PROVISION:** A negotiable instrument which is payable otherwise than on demand, at sight or on presentment is entitled to 3 grace days. In other words, all time instruments are entitled to the benefit of grace days.

- a) If the maturity day of a Note or Bill is a public holiday, then date of maturity is immediately preceding business day.
- b) If the maturity day of a Note or Bill is an emergency or unforeseen holiday, then the date of maturity is immediately succeeding business day.
- c) While calculating the maturity date with respect to a promissory note or bill of exchange made payable at certain number of days after date or after sight or after a certain event, the day of presentment for acceptance or sight, or of protest for non-acceptance, or the day on which the event happens, shall be excluded.

**CONCLUSION:** In the first case, where a bill of exchange dated 20<sup>th</sup> Nov 2016, is payable on 4 months after date, there the instruments falls due for payment on 23<sup>rd</sup> March, 2017.

Whereas in the second case, promissory note presented for sight on 15<sup>th</sup> Apr, 2017 made payable 60 days after sight, there the due date of the instrument will fall on third day after 14<sup>th</sup> Jun, 2017 i.e. 17<sup>th</sup> Jun, 2017.

**Q.NO.6** J purchases some bills amounting to Rs.1727 for a sum of Rs. 200 only. He knows at the time of purchase that both drawer and the acceptor are in embarrassed circumstances but accepts them without enquiry and explanation. The bill proved to have been obtained by fraud. J insists that he is a holder in due course and is therefore entitled to get the full value of the instrument. Will he succeed?  
(RELATED TO THEORY Q.NO.18)

**PROVISION:** As per sec.9 of the NI Act, Holder in due course means any person who,

- For consideration, became the possessor of a promissory note, bill of exchange or cheque, if payable to the bearer, or the payee or endorsee thereof, if payable to the order,
- Before the amount mentioned in it became payable, and
- Without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title."

**CONCLUSION:** In the given case there are clear grounds of suspicion and J has shown negligence in enquiring the validity of the instrument. So, he can't be considered as holder in due course. Hence, J cannot get the value of the instrument as he is not a holder in due course.

**Q.NO.7** Mr. Varun draws a cheque of Rs. 11,000 and gives to Mr. Abhi by way of gift. State with reason whether -  
[RTP - N18 (O), M18 (N) - 4M]

Mr. Abhi is a holder in due course as per the Negotiable Instrument Act, 1881?

Mr. Abhi is entitled to receive the amount of Rs. 11,000 from the bank?

Give your answer in reference to the Provisions of Negotiable Instruments Act, 1881

(N 20-3M) (RELATED TO THEORY Q.NO.19)

**PROVISION:** Same as previous question.

In the instant case, Mr. Varun draws a cheque of Rs. 11,000 and gives to Mr. Abhi by way of gift.

**CONCLUSION:** Thus, in the given case,

- Mr. Abhi is holder but not a holder in due course since he did not get the cheque for value and consideration.
- Mr. Abhi's title is good and bonafide. As a holder he is entitled to receive Rs. 11,000 from the bank on whom the cheque is drawn.

**Q.NO.9** A bill of exchange purports to be drawn by A on B and is accepted by B. The Bill is payable to C or Order. C negotiates it to D who takes it as holder in due course. In a suit by D on the bill, can B disclaim liability on the ground that A's signature is forged.

(RELATED TO THEORY Q.NO.19)

**PROVISION:** Same as previous question.

**CONCLUSION:** In the given situation, B being an acceptor of the bill for honour of the Drawer, cannot deny the validity of the bill, and therefore liable to D.

**Q.NO.10** M drew a cheque amounting to Rs.2 lakh payable to N and subsequently delivered to him. After receipt of cheque N endorsed the same to C but kept in a safe locker. After some time, N died, and C found the cheque in N's safe locker. Does this amount to endorsement under the Negotiable Instruments Act,1881?  
(MTP July 20) (RELATED TO THEORY Q.NO.23)

**PROVISION:** As per the provisions of the Negotiable Instruments Act,1881 an endorsement is said to be completed by the delivery of the instrument. The delivery must be made by the endorser himself or by somebody on his behalf with the intention of passing property therein.

**ANALYSIS:** In the given case M drew a cheque and delivered to N, later N endorses the same to C but kept in his safe locker without delivery. After, N died, and C found the cheque in N's safe locker.

**CONCLUSION:** Thus, in the above case it does not amount to negotiation as the instrument is not delivered to the endorsee.

**Q.NO.12 A is a payee holder of a bill of exchange. He endorses it in blank and delivers it to B. B endorses it in full to C or order. C without endorsement transfers the bill to D. States giving reasons whether D as bearer of the bill of exchange is entitled to recover the payment from A or B or C. (RELATED TO THEORY Q.NO.25)**

**PROVISION:** According to sec.49 of the NI Act,1881, if an endorsement in blank is followed by an endorsement in full, the instrument still remains payable to bearer and negotiable by delivery against all parties prior to the endorser in full, though the endorser is full is only liable to a holder who acquired title directly through his endorsement, and person deriving title through such holder.

**CONCLUSION:** Thus, in the given case, D, as the bearer of the instrument, can receive payment or sue the Drawer, Acceptor, or A, who endorsed the bill in blank, but he cannot sue B or C.

**Q.NO.13 B accepts a bill drawn upon by A who endorses it to C who in turn endorses it to D, who in turn endorses it to A. Discuss the legal position of A. (RELATED TO THEORY Q.NO.27)**

**Provision:** After negotiating an instrument, if an Endorser becomes its holder, before its maturity, then the instrument is said to be negotiated back to the holder. Holder cannot enforce payment against an intermediate party to whom he was previously liable.

Thus, the general rule that a HDC may sue all the prior parties to the instrument does not apply in this case. (Logic: In order to prevent circuity of action).

**CONCLUSION:** Thus, in the given case, A can sue B only because B is a prior party to his original endorsement. A can't sue C or D because it will lead to circuity of action (i.e., if A is allowed to sue C or D, then C or D in turn can sue A because A is a prior party).

**Q.NO.14 M, the holder of a bill, endorses it "without recourse" to N. N endorses it to P, P to Q to R and R endorses it again to M. Can M recover the amount of the bill from N, P, Q and R, or any of them? Discuss. (RELATED TO THEORY Q.NO.27)**

**PROVISION:** Same as previous question.

Holder can sue all prior parties, if he had made *san recourse* endorsement.

**CONCLUSION:** Thus, in the given case, M can recover the amount from all or any one of them.

**Q.NO.15 A cheque was drawn by a customer on his bank, marked "Payee's Account only". The cheque on the face of it was tampered by someone and converted in to a bearer cheque. The bank was negligent in making payment to a bearer instead of Payee. State whether the bank is liable to pay the amount to customer. (RELATED TO THEORY Q.NO.32)**

**PROVISION:** Paying banker is discharged if the following conditions are satisfied. Payment is made to the banker on whom the cheque is crossed or to his agent for collection (*i.e., payment is made to the specified Bank or his agent for collection*) and payment is made in due course.

**CONCLUSION:** In the given case, the banker was negligent and hence no protection can be given under the NI Act to a negligent paying banker. Hence, the bank will have to reimburse the customer for the loss.

**Q.No.16. A cheque is drawn "payable to N or order". It is stolen and N's endorsement is forged. The banker pays the cheque in due course. Is the Banker discharged from liability? Would it make any difference if the Drawer's signature were forged? Discuss with reference to the N.I Act, 1881. [OLD SM, OLD PM] (RELATED TO THEORY Q.NO.32)**

**PROVISION:** As per sec.85 of the NI Act,1881, paying Banker is discharged if he makes 'payment in due course'. The protection is available even when the endorsement subsequently turns out to be a forged one or the endorsement is made by Payee's agent without his authority

**CONCLUSION:** Thus, in the given case, paying banker is discharged even if the endorsement of 'N' is forged, if he makes payment in due course. If Drawer's signature is forged, the paying banker cannot claim discharge on payment, since the paying Banker is presumed to know the signature of his customer (Drawer).

**Q.NO.17 Mr. X executed an Account payee cheque on the name of the Mr. B for the amount of Rs. 20,000. Mr. B submitted the cheque in the bank. Later, B finds that no amount has been credited to his account. In fact, the amount has been credited to some other person with the same name. State the legal position of B with respect to NI Act 1881. (RELATED TO THEORY Q.NO.33)**

**PROVISION:** As per Section 124 of NI act, 1881, in case of A/c payee crossed cheque, the collecting banker is supposed to collect the cheque on behalf of only the payee whose name appears on the face of the cheque.

As per Sec.131 of NI act, 1881, the collecting banker will be protected, even if the title of the instrument in the hands of customer is defective.

- a) The collecting banker acts as an agent for collection on behalf of the customer.
- b) The collecting banker receives payment for a customer and the cheque is crossed.
- c) The Cheque must have been crossed before it gets into the hands of the collecting banker.
- d) The collecting banker acts in good faith and without negligence.

**CONCLUSION:** In the given case, the collecting banker deposited money in an account other than Mr. B. Therefore, Mr. B can hold the banker liable for negligence for wrongful deposit of funds to other accounts.

**Q.NO.18 Explain the meaning of Holder and Holder in due course of a negotiable instrument. The drawer 'D' is introduced by A to draw a cheque in favour of P who is an existing person. A instead of sending the cheque to P forgoes his name and pays the cheque into his own bank. Whether D can recover the amount of the cheque from A's banker. Decide.**

**PROVISION:** As per Section 124 of NI act, 1881, in case of A/c payee crossed cheque, the collecting banker is supposed to collect the cheque on behalf of only the payee whose name appears on the face of the cheque.

As per Sec.131 of NI act, 1881, the collecting banker will be protected, even if the title of the instrument in the hands of customer is defective.

- a) The collecting banker acts as an agent for collection on behalf of the customer.
- b) The collecting banker receives payment for a customer and the cheque is crossed.
- c) The Cheque must have been crossed before it gets into the hands of the collecting banker.
- d) The collecting banker acts in good faith and without negligence.

**ANALYSIS AND CONCLUSION:** D cannot recover amount from A's banker. Collecting banker is not liable for any loss suffered to real owner due to defective title of holder provided it has acted in good faith and without negligence while collecting amount of crossed cheque as an agent. - Section 131

**Q.NO.19 A acquired in good faith by way of endorsement a promissory note from B. Subsequently he found that it was a forged endorsement. Can A acquire a title to the instrument? (RELATED TO THEORY Q.NO.40)**

**PROVISION:** Forged signature means imitating signature of another so as to transfer the title of instrument to other person. Forgery is an offence under the Indian Penal Code.

In this case the forged signature makes the endorsement Invalid. The Property remains vested in the person who is the holder at the time of forgery.

**CONCLUSION:** In the given case,

- a) The validity of A's title is dependent upon whether the instrument had been endorsed in full or in blank.
- b) If it is an endorsement in full, the person claiming under the forged endorsement, cannot acquire the rights of a HDC. He acquires no title to the bill or note. [Mercantile Bank vs D'Silva]
- c) If it is an endorsement in blank, A can ignore the forgery and sue any prior party for the amount. He can rely upon any prior genuine endorsement.

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**Q.NO.20** X a major, and M, a minor, executed a promissory note in favour of P. Examine with reference to the provisions of the Negotiable Instruments Act, the validity of the promissory note and Whether it is binding on X and M. [OLD PM, M15 - 4M, RTP - N11]

(Or)

'A', a broker draws a cheque in favour of B, a Minor. B endorses the cheque in favour of C, who in turn endorses it in favour of D. Subsequently, the bank dishonoured the cheque. State the rights of C and D and also state whether B can be made liable?

[NEW SM, OLD PM, MTP - M18 (N), MTP - N18 (N)]

(Or)

'P', a major and 'Q', a minor executed a promissory note in favour of 'R', Examine with reference to the provisions of the Negotiable Instruments Act, 1881, the validity of the promissory note and whether it is binding on 'P' and Q. [MTP - M18 (O), OLD PM, M15 - 4M]

(RELATED TO THEORY Q.NO.41)

**PROVISION:** As per sec 26 of the NI Act, 1881, every person competent to contract (according to the law to which he is subject to) has capacity to bind himself and be bound by making, drawing, accepting, endorsing delivering and negotiating an instrument.

A minor may draw, endorse, deliver, and negotiate an instrument so as to bind all the parties except himself.

**CONCLUSION:** Hence, the instrument is valid. So, the instrument is binding on major but not on minor.

**Q.NO.21** X sells a TV to M, a minor, who pays for it by his cheque .X endorses the cheque to Y who in turn endorses it in favour of Z. the cheque is dishonoured. Discuss the legal position.

(RELATED TO THEORY Q.NO.41)

**PROVISION:** Same as previous question.

**CONCLUSION:** In the given case,

- Y can enforce payment of the cheque against X only and not against M because a minor can't bind himself.
- Z can enforce payment of the cheque against X and Y.

**Q.NO.22** A cheque is drawn payable to B or order and delivered in payment of a debt. B's agent, without having any authority to endorse, endorses the cheque "per pro" for B and obtains payment of the money and misappropriates it. Is the banker discharged by payment in due course? (RELATED TO THEORY Q.NO.41)

**PROVISION:** Every person, capable of incurring liability, may bind himself or be bound by a duly authorized agent acting in his name.

However, under general authority, agent will not get any power to make, draw, accept or endorse instruments on behalf of principal so as to bind his principal.

According to sec.85, the banker is discharged when the cheque is purported to be endorsed by or on behalf of the payee and he pays the cheque in due course.

**CONCLUSION:** In the given case, the payment is made in due course and banker is duly discharged. The banker has no knowledge of the fact that B's agent who has endorsed the cheque does not have authority to do.

**Q.NO.23** A bill payable three months after date is altered to a bill payable three months after sight by the holder. The acceptor refuses to make payment. Can the holder enforce its payment against the acceptor or the drawer? (RELATED TO THEORY Q.NO.44 & 45)

**PROVISION:** An alteration is called material alteration if it alters the character or operation (i.e. the legal effect) of negotiable instrument; or the rights and liabilities of any of the parties to a negotiable instrument.

All the parties to the negotiable instrument, not consenting to material alteration, are discharged.

**CONCLUSION:** In the given case, the holder cannot enforce the payment of the bill against any party thereto as the bill has been materially altered. Material alteration renders the instrument void.

**Q.NO.24 C issues a cheque for Rs 15 without writing the word 'only' and gives it to D. D adds the words 'hundred only' after fifteen and adds two zeros after the figure 15 as there is sufficient space for making these additions. The Bank pays Rs 1,500 to D who absconds. Is the bank liable to C for excess payment? (RELATED TO THEORY Q.NO.45)**

**PROVISION:** As per the provisions of NI Act, 1881, the alteration should be apparent on the face of the instrument otherwise it remains a valid security in the hands of a HDC. Sec. 89 provides that where an instrument has been materially altered but doesn't appear to have been so altered, the party paying it will be discharged by payment in due course.

**CONCLUSION:** In the given case, the banker is discharged from all liabilities as he made the payment in due course and alteration was not apparent.

**Q.NO.25 A draws a bill payable three months after sight on B. It passes through several hands before X becomes the holder. On presentment by X, B refuses to accept the bill. Discuss the right of X. (RELATED TO THEORY Q.NO.53)**

**PROVISION:** The effect of dishonor of negotiable instrument, whether by non-acceptance or by non-payment, is to render the drawer and all the endorser liable to the holder.

Thus, in the present case, since the bill is payable certain months (3 months) after sight, acceptance is necessary for fixing its date of maturity.

**CONCLUSION:** Thus, non-acceptance by drawee (B) amounts to its dishonor. X may, therefore, hold the endorser as well as the drawer liable thereon.

However, it must be noted that their liability can be invoked only if the holder (X) gives them notice of such dishonour. The drawee B shall not be liable. The drawee can be held liable only in the event of non-payment of an accepted bill.

**Q.NO.26 A draws a bill in favour of B upon X, B endorses it to C who, in turn endorses it to D who, in turn, endorse to F. On presentment for acceptance, X refuses to accept the bill. Who has a right of action against whom in each of the following alternative cases:**

- a) If F gives no notice of dishonour.      b) If F gives notice of dishonour only to E.  
c) If F gives notice of dishonour only to E and A.      (RELATED TO THEORY Q.NO.53)

**PROVISION:** As per provisions of NI Act, 1881, 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.

**CONCLUSION:** In the given case,

- a) F has no right of action against any prior party because all prior parties who do not receive the notice of dishonour are discharged.  
b) F has right of action against E only and not against A, B, C or D.  
c) F has right of action against E and A only and not against B, C or D.

E has right of action against A and not against B, C or D because A received then notice of dishonour from F.

**Q.NO.27 A endorses and delivers a cheque to B, and B keeps it for unreasonable length of time and then endorses and delivers it to C. C presents the cheque for payment within a reasonable time after its receipt by him and it is dishonoured. Advise C. (RELATED TO THEORY Q.NO.56)**

**PROVISION:** According to sec.84 of the NI Act, 1881, in the following 2 cases a holder can take action against the banker:

Where a banker pays a generally crossed cheque over the counter of the bank, or a specially crossed cheque otherwise than to the banker to whom it is crossed (i.e. payment out of due course).

Where the holder does not present the cheque with the banker within a reasonable time, and the bank fails in the meantime.

**CONCLUSION:** In the given case, C can enforce payment against B but not against A, since an unreasonable time has elapsed as regards endorsement from A.

**Q.NO.28** A drew a cheque for Rs. 5000 in favour of B on 1st January 2009 and gave it to him on the same day. The cheque was presented for payment on the 5th June 2009. In the meantime, the bank had failed in May 2009. Discuss the legal position of B's recourse against A and the bank for recovering the amount. (RELATED TO THEORY Q.NO.56)

**PROVISION:** According to sec.84 of the NI Act, 1881, in the following 2 cases a holder can take action against the banker:

Where a banker pays a generally crossed cheque over the counter of the bank, or a specially crossed cheque otherwise than to the banker to whom it is crossed (i.e. payment out of due course).

Where the holder does not present the cheque with the banker within a reasonable time, and the bank fails in the meantime.

**CONCLUSION:** In the given case, as B presented the cheque for payment after more than five months, which cannot be considered as reasonable period, and the drawer suffered loss due to this long delay, the drawer is discharged from his liability to the extent of the actual damages suffered by him. B, however, can claim as a creditor in the insolvency of the bank for the balance.

**NOTE:** A cheque is valid only for 3 months from the date on which it was drawn. Thereafter the cheque becomes stale and invalid. Generally the Drawer is not discharged. But in this case and therefore, the drawer is discharged.

**Q.No.29.** X draws a cheque for Rs. 1,000. The bank fails before the cheque presented. State the extent to which the drawer shall be discharged if-

X had Rs. 1,000 in his account when the cheque sought to be presented and the cheque is not presented within reasonable time.

X had Rs. 900 in his account when the cheque sought to be presented and the cheque is not presented within a reasonable time.

X had Rs. 1,000 in his account when the cheque sought to be presented but the bank failed before the cheque could be presented within a reasonable time. (RELATED TO THEORY Q.NO.56)

**PROVISION:** Same as previous question.

**CONCLUSION:**

**Case(a):** The drawer is discharged to the extent of Rs. 1,000 but the holder can proceed against the bank for the amount of the cheque.

**Case(b):** The drawer is discharged to the extent of Rs. 900 and the holder can proceed against (a) the bank for Rs. 900 and (b) the drawer for Rs. 100.

**Case(c):** The drawer is not discharged at all.

**Q.NO.30** A issues an open bearer cheque for Rs. 10000 in favour of B who strikes out the word bearer and put crossing across the cheque. The cheque is thereafter negotiated to C and D. when it is finally presented by D's banker, it is returned with remarks "Payment countermanded" by drawer. In response to the legal notice from D. A pleads that the cheques was altered after it had been issued and therefore he is not bound to pay the cheques. Referring to the provisions of the Negotiable Instruments Act, 1881 decide, whether A's argument is valid or not? (RELATED TO THEORY Q.NO.57)

**PROVISION:** Striking off word 'bearer' amount as material alteration but it is authorized under act. Therefore, cheque is not discharged and remains valid. Cheque is dishonoured not for material alteration but for payment countermanded by Drawer.

**CONCLUSION:** In view of the above circumstances, A is liable for payment. He is also liable for dishonour of cheque as per section 138.

**Q.NO.31** X, on attaining the age of majority, makes a fresh promissory note in consideration of a promissory note made by him during his minority. Can a suit be maintained on the fresh promissory note? (RELATED TO THEORY Q.NO.60)



**PROVISION:** According to sec.43 of NI Act, 1881, if a negotiable instrument made, drawn, accepted, endorsed, or transferred without consideration, or for a consideration which fails, then it creates no obligation of payment between the parties to the transaction.

**CONCLUSION:** Thus, A suit cannot be maintained on the fresh promissory note because the fresh promissory note is void in the absence of consideration

**Q.NO.32 X accepts a bill for the accommodation of A (drawer), A transfers it to B for value. The bill is dishonoured by X on the due date. B collects the amount from A. Can A sue X for the recovery of the amount? (RELATED TO THEORY Q.NO.60)**

**PROVISION:** According to sec.43 of the NI Act, if a negotiable instrument made, drawn, accepted, endorsed, or transferred without consideration, or for a consideration which fails, then it creates no obligation of payment between the parties to the transaction.

If any person receives a negotiable instrument without any consideration but transfers the instrument to a holder for consideration (i.e. HDC), then such HDC and every subsequent holder may recover amount due from the transferor for consideration and from any prior party.

**CONCLUSION:** In the given case, A can't sue X for the recovery of the amount (*Accommodated Party cannot recover amount from Accommodating Party*).

**Q.NO.33 'A' draws a bill of exchange payable to himself on 'x' who accept the bill without consideration just to accommodate 'A' 'A' transfers the bill to "P" for good consideration. State the rights of 'A' and 'P' Would your answer be different if 'A' transferred the bill to 'P' after maturity? (RELATED TO THEORY Q.NO.60)**

**PROVISION:** Sec 43 of the NI Act, 1881 - Negotiable instrument made etc., without consideration.

Sec 43 of the NI Act, 1881 provides that a negotiable instrument made, drawn, accepted or endorsed without consideration, creates no obligation of payment between the parties to the transaction.

But if any such party has transferred the instrument to a holder for consideration, such holder, and every subsequent holder deriving title from him, may recover the amount due on such instrument from the transferor for consideration or any prior party thereto.

**CONCLUSION:**

- 1) Rights of A and P:
  - a) A is not entitled to sue X: Because there is no consideration between A and X.
  - b) P is entitled to sue A and X: Since P is a holder for consideration, he can sue the transferor for consideration and every party prior to him.
- 2) The answer will remain same even if A had transferred the bill after maturity. Because the right to sue the transferor for consideration and every party prior to him, is available to 'holder for consideration', even though he is not a 'holder in due course' (i.e. even if the holder for consideration obtains the bill after maturity).

**Q.NO.35 M draws bill N. N accepts the bill without consideration, the bill is transferred to O without consideration. O transferred it to P for Rs.10,000. On dishonor of the bill, P sued O for recovery of the value of Rs.10,000. Examine whether O has any right to action against M and N? [M19 (N) - 2M](RELATED TO THEORY Q.NO.60)**

**PROVISION:** As per the provisions of NI Act, 1881, an instrument made, drawn, accepted, endorsed, or transferred without consideration or for a consideration which fails, creates no obligation of payment between the parties to the transaction. But if any such party has transferred the instrument with or without endorsement to a holder for a consideration, such holder, and every subsequent holder deriving title from him, may recover the amount due on such instrument from the transferor for consideration or any prior party thereto.

**CONCLUSION:** In the given instance the bill was drawn, accepted and transferred without consideration by 'M' to 'N', and from 'N' to 'O' respectively. Therefore, no obligation of payment is created between the parties. So 'O' has no right to action against 'M' and 'N'.

**Q.NO.36 A draw a bill on B in favour of C and C has lost the bill and the finder of the bill forges the endorsement of C and presents it for acceptance by B. B without the knowledge of any forgery accepts it. Discuss?**  
(RELATED TO THEORY Q.NO.61)

**PROVISION:** According to Sec.58 if the holder of an instrument who is not a HDC, obtains an instrument which is lost or is for unlawful consideration or by unlawful means, he is not entitled to recover the money from the maker, acceptor or holder or from any prior party.

**CONCLUSION:** In the instant case, the finder of the Bill is not a HDC and is, therefore, not entitled. However, if B has knowledge of the forgery and still had accepted the bill, he will be liable as per Sec.41

**Q.No.37. A bill is payable to X or order, X endorses the bill in blank. The bill is thereafter lost and comes into the hands of Y. Discuss the legal position in each of the following alternative cases:**

**If Y receives the payment of the bill.**

**If Y passes the bill by simple delivery to Z as a gift.**

**If Y passes the bill after maturity by simple delivery to Z who takes the bill in good faith for valuable consideration.**

**If Y passes the bill before maturity by simple delivery to Z who takes the bill in good faith for valuable consideration.**  
(RELATED TO THEORY Q.NO.61)

**PROVISION:** Same as previous question.

**CONCLUSION:** In the given case,

- a) The true owner can recover the amount from Y because Y had no title to bill.
- b) The true owner can recover the amount from Y and Z because Y and Z (not being holders in due course) had no title to bill.
- c) The true owner can recover the amount from Y and Z because Y and Z (not being holders in due course) had no title to bill.
- d) The true owner can recover the amount from Y and not from Z because Z being holders in due course had a good title to bill.

**THE END**

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