

NEGOTIABLE INSTRUMENTS (CHART 6.1)

PROMISSORY NOTE

Meaning : "A 'promissory note' is an instrument in writing (not being a bank-note or a currency-note) containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument."

Parties to promissory note

1. **Maker :** The person who makes the promise to pay is called the Maker. He is the debtor and must sign the instrument.
2. **Payee :** Payee is the person to whom the amount on the note is payable.

Essential Characteristics of a Promissory Note

- a. In writing- An oral promise to pay is not sufficient.
- b. There must be an express promise to pay. Mere acknowledgment of debt is insufficient.
- c. The promise to pay should be definite and unconditional.
- d. A promissory note must be signed by the maker otherwise it is incomplete & ineffective.
- e. Promise to pay money only.
- f. Promise to pay a certain sum.
- g. The maker and payee must be certain, definite and different persons.
- h. **Stamping :** A promissory note must be properly stamped

BILLS OF EXCHANGE

Meaning : A "bill of exchange" is an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument.

Parties to the bill of exchange

- a. **Drawer :** The maker of a bill of exchange.
- b. **Drawee :** The person directed by the drawer to pay is called the 'drawee'. He is the person on whom the bill is drawn. On acceptance of the bill, he is called an acceptor and is liable for the payment of the bill. His liability is primary and unconditional.
- c. **Payee :** The person named in the instrument, to whom or to whose order the money is, by the instrument, directed to be paid.

Essential characteristics of bill of exchange

- (a) It must be in writing.
- (b) Must contain an express order to pay.
- (c) The order to pay must be definite and unconditional.
- (d) The drawer must sign the instrument.
- (e) Drawer, drawee, and payee must be certain. All these three parties may not necessarily be three different persons. One can play the role of two. But there must be two distinct persons in any case. As per Section 31 of RBI Act, 1934, a bill of exchange cannot be made payable to bearer on demand.
- (f) The sum must be certain.
- (g) The order must be to pay money only.
- (h) It must be stamped.

CHEQUE

A "cheque" is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand and it includes the electronic image of a truncated cheque and a cheque in the electronic form.

1. **Drawer :** The person who draws a cheque i.e., makes the cheque (Debtor). His liability is primary and conditional.
2. **Drawee :** The specific bank on whom cheque is drawn. He makes the payment of the cheque. In case of cheque, drawee is always banker.
3. **Payee :** The person named in the instrument (i.e., the person in whose favour cheque is issued), to whom or to whose order the money is, by the instrument, directed to be paid, is called the payee. The payee may be the drawer himself or a third party.

Essential Characteristics of a cheque :

- a. all the essential characteristics of a bill of exchange
- b. Must be drawn on a specified banker.
- c. It must be payable on demand

NEGOTIABLE INSTRUMENTS (CHART 6.2)

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

CLASSIFICATION OF NEGOTIABLE INSTRUMENTS

Bearer Instrument : It is an instrument where the name of the payee is blank or where the name of payee is specified with the words "or bearer" or where the last indorsement is blank. Such instrument can be negotiated by mere delivery.

Order Instrument : It is an instrument which is payable to a person or Payable to a person or his order or Payable to order of a person or where the last indorsement is in full, such instrument can be negotiated by indorsement and delivery.

"Inland instrument" : A promissory note, bill of exchange or cheque drawn or made in India and made payable in, or drawn upon any person resident in India shall be deemed to be an inland instrument.

"Foreign instrument" : A foreign instrument is one which is not an inland instrument.

Place where bill is drawn	Residence of Person on whom drawn and place where made payable	Nature of Instrument
P/N, BOE, C drawn/made outside India	on a person resident in or outside India + made payable in India	are foreign bills.
	on a person residing outside India + payable outside India.	
	on a person residing in India + payable outside India	

NEGOTIABLE INSTRUMENTS (CHART 6.3)

Inchoate and Ambiguous Instruments

1 - Inchoate Instrument : It means an instrument that is incomplete in certain respects. The drawer/ maker/ acceptor/ indorser of a negotiable instrument may sign and deliver the instrument to another person in his capacity leaving the instrument, either wholly blank or having written on it the word incomplete. Such an instrument is called an inchoate instrument and this gives a power to its holder to make it complete by writing any amount either within limits specified therein or within the limits specified by the stamp's affixed on it. The principle of this rule of an inchoate instrument is based on the principle of estoppel.

2 - Liability on drawing inchoate instrument : The person signing and delivering the inchoate instrument is liable both to a holder and holder in due course.

3 - The holder of such an instrument cannot recover the amount in excess of the amount intended to be paid by the signor.

4 - The holder in due course can, however, recover any amount on such instrument provided it is covered by the stamp affixed on the instrument.

Ambiguous Instrument

“Where an instrument may be construed either as a promissory note or bill of exchange, the holder may at his election treat it as either, and the instrument shall be thenceforward treated accordingly.” Thus, an instrument which is vague and cannot be clearly identified either as a bill of exchange, or as a promissory note, is an ambiguous instrument. that the holder may, at his discretion, treat it as either and the instrument shall thereafter be treated accordingly. Thus, after exercising his option, the holder cannot change that it is the other kind of instrument.

NEGOTIATION AND ITS MODES

1 - when a negotiable instrument is transferred to any person with a view to constitute the person holder thereof, the instrument is deemed to have been negotiated.

2 - (i) A promissory note, bill of exchange or cheque payable to bearer is negotiable by the delivery thereof.
(ii) A promissory note, bill of exchange or cheque payable to order is negotiable by the holder by indorsement and delivery thereof.

Importance of Delivery in Negotiation

1 - The delivery can be, actual or constructive. Actual delivery takes place when the instrument changes hand physically. Constructive delivery takes place when the instrument is delivered to the agent, clerk or servant of the indorsee on his behalf or when the indorser, after indorsement, holds the instrument as an agent of the indorsee.

2 - The delivery is essential not only at the time of negotiation but also at the time of making or drawing of negotiable instrument. The rights in the instrument are not transferred to the indorsee unless after the indorsement the same has been delivered. If a person makes the indorsement of instrument but before the same could be delivered to the indorsee the indorser dies, the legal representatives of the deceased person cannot negotiate the same by mere delivery thereof.

Negotiation of instruments between the parties	How delivery is to be made
As between parties standing in immediate relation	Delivery to be effectual must be made by the party making, accepting, or endorsing the instrument, or by a person authorized by him in that behalf.
As between such parties and any holder of the instrument other than holder in due course	It may be shown that the instrument was delivered conditionally or for a special purpose only, and not for the purpose of transferring absolutely the property therein.

NEGOTIABLE INSTRUMENTS (CHART 6.4)

DISHONOUR OF CHEQUES FOR INSUFFICIENCY OF FUNDS IN THE ACCOUNTS

1] - 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 that account
- for the discharge, in whole or in part, of any debt or other liability, [A cheque given as gift or donation, or as a security or in discharge of a mere moral obligation, or for an illegal consideration, would be outside the purview of this section]
- is returned by the bank unpaid,
- either because of the—
amount of money standing to the credit of that account is insufficient to honor the cheque, or
- that it exceeds the amount arranged to be paid from that account by an agreement made with that bank, such person shall be deemed to have committed an offence and shall, be punished with imprisonment for a term which may extend to two years, or with fine which may extend to twice the amount of the cheque, or with both.

2] Cheque presented within validity period : The cheque has been presented to the bank within a period of three months from the date on which it is drawn or within the period of its validity, whichever is earlier.

3] Demand for the payment through the notice : the payee or the holder in due course of the cheque, as the case may be, makes a demand for the payment of the said amount of money by giving a notice, in writing, to the drawer of the cheque, within 30 days of the receipt of information by him from the bank regarding the return of the cheque as unpaid

4] Failure of drawer to make payment : the drawer of such cheque fails to make the payment of the said amount of money to the payee or, as the case may be, to the holder in due course of the cheque, within fifteen days of the receipt of the said notice.

RULES OF COMPENSATION

The compensation payable in case of dishonour of promissory note, bill of exchange or cheque, by any party liable to the holder or any endorsee, shall be determined by the following rules :

(a) the holder is entitled to the amount due upon the instrument, together with the expenses properly incurred in presenting, noting and protesting it;

(b) when the person charged resides at a place different from that at which the instrument was payable, the holder is entitled to receive such sum at the current rate of exchange between the two places;

(c) an endorser who, being liable, has paid the amount due on the same is entitled to the amount so paid with interest at 18% per annum from the date of payment until tender or realisation thereof, together with all expenses caused by the dishonour and payment;

(d) when the person charged and such endorser reside at different places, the endorser is entitled to receive such sum at the current rate of exchange between the two places;

(e) the party entitled to compensation may draw a bill upon the party liable to compensate him, payable at sight or on demand, for the amount due to him, together with all expenses properly incurred by him. Such bill must be accompanied by the instrument dishonoured and the protest thereof (if any). If such bill is dishonoured, the party dishonouring the same is liable to make compensation thereof in the same manner as in the case of the original bill.

NEGOTIABLE INSTRUMENTS (CHART 6.5)

PRESENTMENT OF INSTRUMENTS

Presentment for acceptance

- 1 - A bill of exchange payable after sight must be presented to the drawee thereof for acceptance by a person entitled to demand acceptance, within a reasonable time after it is drawn, and in business hours on a business day.
- 2 - In default of such presentment, no party thereto is liable thereon to the person making such default. If the drawee cannot, after reasonable search, be found, the bill is dishonoured.

Drawee's time for deliberation

- 1 - The holder must, if so required by the drawee of a bill of exchange presented to him for acceptance, allow the drawee 48 hours (exclusive of public holidays) to consider whether he will accept it.

When presentment unnecessary

- (a) (i) If the maker, drawee or acceptor intentionally prevents the presentment of the instrument, or
(ii) If the instrument being payable at his place of business, he closes such place on a business day during the usual business hours, or
(iii) if the instrument being payable at some other specified place, neither he nor any person authorised to pay it attends at such place during the usual business hours, or
(iv) if the instrument not being payable at any specified place, he cannot after due search be found;

- (b) as against any party sought to be charged therewith, if he has engaged to pay notwithstanding non-presentment

- (c) as against any party if, after maturity, with knowledge that the instrument has not been presented—
- 1 - he makes a part payment on account of the amount due on the instrument,
 - 2 - or promises to pay the amount due thereon in whole or in part,
 - 3 - or otherwise waives his right to take advantage of any default in presentment for payment;

- (d) as against the drawer, if the drawer could not suffer damage from the want of such presentment.