2

The Negotiable Instruments Act, 1881

Question 1

*Explain the meaning of negotiable instruments?*

**Answer**

It is an instrument which is transferable (by customs of trade) by delivery, like cash, and is also capable of being sued upon by the person holding for the time being. The property in such an instrument passes to a *bona fide* transferee for value. The attribute of negotiability is acquired by certain documents by custom.

Section 13 of the Negotiable Instruments Act, 1881 does not define a negotiable instrument although it mentions only three kinds of negotiable instruments namely, bills, notes and cheques. But it does not necessarily follow that there can be no other negotiable instruments than those enumerated in the Act. Section 17 of the Transfer of Property Act, 1882 speaks of instruments which are for the time being, by law of custom, negotiable, implying thereby that the Courts in India may follow the practice of the English Courts in extending the character of Negotiable Instruments Act. Thus in India, Government promissory notes, Shah Jog Hundis, delivery orders and railway receipts for goods have been held to be negotiable by usage or custom.

Question 2

*Explain the essential elements of a promissory note. State, giving reasons, whether the following instruments are valid promissory notes:*

(i) X promises to pay Y, by a promissory note, a sum of ₹5,000, fifteen days after the death of B.

(ii) X promises to pay Y, by a promissory note, ₹5000 and all other sums, which shall be due.

**Answer**

**Essential Elements of a Promissory Note:**

1. *Must be in writing.*
2. *Promise to pay:* The instrument must contain an express promise to pay.
3. **Definite and unconditional**: The promise to pay must be definite and unconditional. If it is uncertain or conditional, the instrument is invalid.

4. **Signed by the maker**: The instrument must be signed by the maker, otherwise it is incomplete and of no effect. Even if it is written by the maker himself and his name appears in the body of the instrument, his signature must be there.

5. **Certain parties**: The instrument must point out with certainty as to who the maker is and who the payee is. When the maker and the payee cannot be identified with certainty from the instrument itself, the instrument, even if it contains an unconditional promise to pay, is not a promissory note.

6. **Certain sum of money**: The sum payable must be certain and must not be capable of contingent additions or subtractions.

7. **Promise to pay money only**: The payment must be in the legal tender money of India.

**Answer to Problem**: In the case number 1, the payment to be made in fifteen days after the death of B. Though the date of death is uncertain, it is certain that B shall die. Therefore the instrument is valid.

In the second case - the sum payable is not certain within the meaning of Section 4 of the Negotiable Instruments Act, 1881- Hence the Promissory Note is not a valid one.

**Question 3**

Explain the meaning of ‘Holder’ and ‘Holder in due course’ of a negotiable instrument. The drawer, ‘D’ is induced 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.

**Answer**

Meaning of ‘Holder’ and the ‘Holder in due course’ of a negotiable instrument:

‘Holder’: Holder of negotiable instrument means as regards all parties prior to himself, a holder of an instrument for which value has at any time been given.

‘Holder in due course’: (i) In the case of an instrument payable to bearer means any person who, for consideration became its possessor before the amount of an instrument payable. (ii) In the case of an instrument payable to order, ‘holder in due course’ means any person who became the payee or endorsee of the instrument before the amount mentioned in it became payable. (iii) He had come to possess the instrument without having sufficient cause to believe that any defect existed in the title of transferor from whom he derived his title.

The problem is based upon the privileges of a ‘holder in due course’. Section 42 of the Negotiable Instrument Act, 1881, states that an acceptor of a bill of exchange drawn in a fictitious name and payable to the drawer’s order is not, by reason that such name is fictitious, relieved from liability to any holder in due cause claiming under an endorsement by the same hand as the drawer’s signature, and purporting to be made by the drawer. In this problem, P is
not a fictitious payee and D, the drawer can recover the amount of the cheque from A's bankers [North and South Wales Bank B. Macketh (1908) A.C. 137; Town and Country Advance Co. B, Provincial Bank (1917) 2 Ir. R.421].

**Question 4**

*Referring to the provisions of the Negotiable Instruments Act, 1881, examine the validity of the following Promissory Notes:*

(i) *I owe you a sum of ₹1,000. 'A' tells 'B'.*

(ii) *'X' promises to pay 'Y' a sum of ₹10,000, six months after 'Y's marriage with 'Z'*

**Answer**

*Promissory Note*: A Promissory Note is an instrument in writing containing an unconditional undertaking signed by the maker, to pay a certain sum of money only to, or to the order of certain person, or the bearer of the Instrument. (Section 4, The Negotiable Instruments Act, 1881).

**Essential elements**: *(refer answer no. 2 on the page no. 2.1-2.2)*

Based on the above conditions in accordance with the definition of a promissory note, the answers to the two problems is as under:

(i) It is not a promissory note in the first case, since there is no promise to pay.

(ii) In the second case also it is not a promissory note since as there is probability that Y may not marry.

**Question 5**

*What are the essential elements of a valid acceptance of a Bill of Exchange? An acceptor accepts a “Bill of Exchange” but write on it “Accepted but payment will be made when goods delivered to me is sold.” Decide the validity.*

**Answer**

**Essentials of a valid acceptance of a Bill of Exchange:**

The essentials of a valid acceptance are as follows:

1. **Acceptance must be written**: The drawee may use any appropriate word to convey his assent. It may be sufficient acceptance even if just signatures are put without additional words. An oral acceptance is not valid in law.

2. **Acceptance must be signed**: A mere signature would be sufficient for the purpose. Alternatively, the words ‘accepted’ may be written across the face of the bill with a signature underneath; if it is not so signed, it would not be an acceptance.

3. **Acceptance must be on the bill**: The acceptance should be on the face of the bill normally but it is not necessary. An acceptance written on the back of a bill has been held to be
sufficient in law. What is essential is that must be written on the bill; else it creates no liability as acceptor on the part of the person who signs it.

4. **Acceptance must be completed by delivery**: Acceptance would not be complete and the drawee would not be bound until the drawee has either actually delivered the accepted bill to the holder or tendered notice of such acceptance to the holder of the bill or some person on his behalf.

5. Where a bill is drawn in sets, the acceptance should be put on one part only. Where the drawee signs his acceptance on two or more parts, he may become liable on each of them separately.

6. **Acceptance may be either general or qualified**: An acceptance is said to be general when the drawee assents without qualification order of the drawer. The qualification may relate to an event, amount, place, time etc. (Explanation to Section 86 of the Negotiable Instruments Act, 1881). In the given case, the acceptance is a qualified acceptance since a condition has been attached declaring the payment to be dependent on the happening of an event therein stated.

   As a rule, acceptance must be general acceptance and therefore, the holder is at liberty to refuse to take a qualified acceptance. Where, he refuse to take it, the bill shall be dishonoured by non-acceptance. But, if he accepts the qualified acceptance, even then it binds only him and the acceptor and not the other parties who do not consent thereto (Section 86).

**Question 6**

*Examining the provisions of the Negotiable Instruments Act, 1881, distinguish between a 'Bill of Exchange' and a 'Promissory Note'.*

**Answer**

Distinction between a Promissory Note and a Bill of Exchange:

The distinctive features of these two types of negotiable instruments are tabulated below:-

<table>
<thead>
<tr>
<th>Sl. No.</th>
<th>Promissory Note</th>
<th>Bill of Exchange</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>It contains a promise to pay</td>
<td>It contains an order to pay</td>
</tr>
<tr>
<td>2.</td>
<td>The liability of the maker of a note is primary and absolute</td>
<td>The liability of the drawer of a bill is secondary and conditional. He would be liable if the drawee, after accepting the bill fails to pay the money due upon it provided notice of dishonor is given to the drawer within the prescribed time.</td>
</tr>
<tr>
<td>3.</td>
<td>It is presented for payment without any previous acceptance by maker</td>
<td>If a bill is payable sometime after sight, it is required to be accepted either by the drawee himself or by someone else on his behalf, before it can be presented for payment.</td>
</tr>
<tr>
<td>4.</td>
<td>The maker of a promissory note stands in immediate relationship with the payee and is primarily liable to the payee or the holder.</td>
<td>The maker or drawer of an accepted bill stands in immediate relationship with the acceptor and the payee.</td>
</tr>
<tr>
<td>5.</td>
<td>It cannot be made payable to the maker himself, that is the maker and the payee cannot be the same person.</td>
<td>In the case of bill, the drawer and payee or the drawer and the payee may be the same person.</td>
</tr>
<tr>
<td>6.</td>
<td>In the case of a promissory note there are only two parties, viz. the maker (debtor) and the payee (creditor).</td>
<td>In the case of a bill of exchange, there are three parties, viz., drawer, drawee and payee, and any two of these three capacities can be filled by one and the same person.</td>
</tr>
<tr>
<td>7.</td>
<td>A promissory note cannot be drawn in sets.</td>
<td>The bills can be drawn in sets.</td>
</tr>
<tr>
<td>8.</td>
<td>A promissory note can never be conditional.</td>
<td>A bill of exchange too cannot be drawn conditionally, but it can be accepted conditionally with the consent of the holder. It should be noted that neither a promissory note nor a bill of exchange can be made payable to bearer on demand.</td>
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**Question 7**

*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:*

(i) An oral acceptance

(ii) An acceptance by mere signature without writing the word “accepted”.

**Answer**

**Meaning of Acceptance:** It is only the bill of exchange which requires acceptance. A bill is said to be accepted when the drawee (i.e. the person on whom the bill is drawn), 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. After the drawee has accepted the bill he is known as the acceptor (Section 7 para 3 of the Negotiable Instruments Act, 1881).
Acceptance may be either general or qualified. The acceptance is qualified when the drawer does not accept it according to the apparent term 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 subject to certain conditions. A general acceptance is the acceptance where the acceptor assents without qualification to the order of the drawer.

**Validity of Acceptance:**

(i): 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.

(ii): 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 Negotiable Instruments Act, 1881 i.e. it must appear on the bill and must be signed by the drawee. (Manakchand v. Chartered Bank).

**Question 8**

Is there any difference in the protection available to a banker in respect of a cheque being ‘crossed’ or ‘uncrossed’?

**Answer**

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.

**Question 9**

State whether the following statement is correct or incorrect:

A cheque marked “Not-Negotiable” is not transferable

**Answer**

Incorrect
Question 10

*Define “cheque”, under the Negotiable Instruments Act, 1881. What are the difference between a cheque and a bill of exchange?*

**Answer**

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.

**Essentials:**

1. Cheque is always drawn on a bank.
2. Cheque is always payable on demand.

   Since a cheque is a species of a bill of exchange, it must satisfy all the requirements of a bill of exchange, i.e.

   (i) it must be in writing and signed by the drawer;

   (ii) it must contain an unconditional order to pay;

   (iii) the order must be to pay a certain sum of money to or to the order of a certain person, or to the bearer of the instrument.

**Distinction between a cheque and a bill of exchange**

1. In a cheque the drawee is always a bank, whereas in a bill the drawee may be a ‘bank’ or any other person.
2. In a cheque days of grace are not allowed, whereas in a bill three days of grace are allowed for payment.
3. Notice of dishonour is not needed in a cheque, whereas notice of dishonour is usually required in case of a bill.
4. A cheque can be drawn to bearer and made payable on demand, whereas a bill cannot be bearer, if it is made payable on demand.
5. Cheque does not require presentment for acceptance. It needs presentment for acceptance. Bill, sometimes, require presentment for acceptance and it is advisable to present them for acceptance even when it is not essential to do so.
6. Cheque does not require to be stamped in India, whereas bill must be stamped according to the law.
7. A cheque may be crossed, whereas a bill cannot be crossed.
8. A cheque being a revocable mandate, the authority may be revoked by countermanding payment, and is determined by notice of the customer’s death or insolvency. This is not so in the case of a bill.
9. The drawer of a bill is discharged from liability, if it is not duly presented for payment but the drawer of a cheque is not discharged by delay of the holder in presenting the cheque for payment unless the drawer has suffered some loss due to delay.

Question 11

Who is holder in due course? How he is differing from a Holder?

Answer

Holder in Due Course: It means any person who, for consideration became its possessor before the amount mentioned in it became payable. In the case of an instrument payable to order, ‘holder in due course’ means any person who became the payee or endorsee of the instrument before the amount mentioned in it became payable. In both the cases, he must receive the instrument without having sufficient cause to believe that any defect existed in the title of the person from whom he derived his title. In other words, holder in due course means a holder who takes the instrument bona fide for value before it is overdue, and without any notice of defects in the title of the person, who transferred it to him. Thus, a person who claims to be ‘holder in due course’ is required to prove that:

1. on paying a valuable consideration, he became either the possessor of the instrument if payable to order;
2. he had come into the possession of the instrument before the amount due there under became actually payable; and
3. he had come to possess the instrument without having sufficient cause to believe that any defect existed in the title of transferor’s from whom derived his title.

Distinction between Holder and Holder in Due Course:

1. A holder may become the possessor or payee of an instrument even without consideration, whereas a holder in due course is one who acquires possession for consideration.
2. A holder in due course as against a holder must become the possessor payee of the instrument before the amount thereon become payable.
3. 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.

Question 12

State the privileges of a ‘Holder in due course” under the Negotiable Instruments Act, 1881.

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 Bankers. B the drawer wants to recover the amount from C’s Bankers. Decide in the light of the provisions of Negotiable Instruments Act, 1881-
(i) Whether B the drawer, can recover the amount of the cheque from C’s Bankers?

(ii) Whether C is the Fictitious Payee?

Would your answer be still the same in case C is a fictitious person?

Answer

Privileges of a “Holder in Due Course”: According to the provisions of the Negotiable Instruments Act, 1881, a holder in due course has the following privileges:

(i) A person signing and delivering to another a stamped but otherwise inchoate instrument is debarred from asserting, as against a holder in due course, that the instrument has not been filled in accordance with the authority given by him, the stamp being sufficient to cover the amount (Section 20).

(ii) In case of bill of exchange is drawn payable to drawer’s order in a fictitious name and is endorsed by the same hand as the drawer’s signature. It is not permissible for acceptor to allege as against the holder in due course that such name is fictitious (Section 42).

(iii) In case a bill or note is negotiated to a holder in due course, 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 (Section 42 and 47).

(iv) The person liable in a negotiable instrument cannot set up against the holder in due course the defences that the instrument had been lost or obtained from the former by means of an offence or fraud or far an unlawful consideration (Section 58).

(v) No maker of a promissory note, and no drawer of a bill or cheque and no acceptor of a bill for the honour of the drawer shall, in a suit thereon by a holder in due course be permitted to deny the validity of the instrument as originally made or drawn (Section 120).

(vi) No maker of a promissory note and no acceptor of a bill payable to order shall, in a suit thereon by a holder in due course, be permitted to deny the payee’s capacity, at the rate of the note or bill, to endorse the same (Section 121).

In brief, it is clear that a holder in due course gets a good title in many respects. Answer to problem

According to Section 42 of the Negotiable Instruments Act, 1881 an acceptor of a bill of exchange drawn in a fictitious name and payable to the drawer’s order is not, by reason that such name is fictitious, relieved from liability to any holder in due course claiming under an instrument by the same hand as the drawer’s signature, and purporting to be made by the drawer.

The word “fictitious payee” means a person who is not in existence or being in existence, was never intended by the drawer to have the payment. Where drawer intends the payee to have the payment, then he is not a fictitious payee and the forgery of his signature will affect the validity of the cheque.

Applying the above, answers to the questions asked can be as under:
I. In this case B, the drawer can recover the amount of the cheque from C’s bankers because C’s title was derived through forged endorsement.

II. Here C is not a fictitious payee because the drawer intended him to receive payment.

III. 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.

Question 13

A draws and B accepts 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.

Answer

Section 36 of the Negotiable Instruments Act, 1881 describes the liabilities of prior parties to the holder in due course. This section says that a holder in due course has privilege to hold every prior party to a negotiable instrument liable on it until the instrument is duly satisfied. Here the holder in due course can hold all the prior parties liable jointly and severally. Prior parties includes the maker or drawer, the acceptor and endorsers. Accordingly in the given problem, E, a holder in due course can recover the amount from all the prior parties i.e., D & C (the endorsers), B (an acceptor) and A (the drawer).

Privileges of a “Holder in Due Course”: According to the provisions of the Negotiable Instruments Act, 1881, a holder in due course has the following privileges:-

i. A person signing and delivering to another a stamped but otherwise inchoate instrument is debarred from asserting, as against a holder in due course, that the instrument has not been filled in accordance with the authority given by him, the stamp being sufficient to cover the amount (Section 20).

ii. In case a bill of exchange is drawn payable to drawer’s order in a fictitious name and is endorsed by the same hand as the drawer’s signature, it is not permissible for acceptor to allege as against the holder in due course that such name is fictitious (Section 42).

iii. In case a bill or note is negotiated to a holder in due course, 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 (Sections 42 and 47).

iv. The person liable in a negotiable instrument cannot set up against the holder in due course the defences that the instrument had been lost or obtained from the former by means of an offence or fraud or for an unlawful consideration (Section 58).

v. No maker of a promissory note, and no drawer of a bill or cheque and no acceptor of a bill for the honour of the drawer shall, in a suit thereon by a holder in due course be permitted to deny the validity of the instrument as originally made or drawn (Section 120).
vi. No maker of a promissory note and no acceptor of a bill payable to order shall, in a suit thereon by a holder in due course, be permitted to deny the payee’s capacity to endorse the same (Section 121).

**Question 14**

A cheque payable to bearer is crossed generally and marked “not negotiable”. The cheque is lost or stolen and comes into 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 it is drawn. The true owner of the cheque claims refund of the amount of the cheque from B.

**Answers**

The cheque in the given case was crossed generally and marked ‘Not Negotiable’. Thereafter, the cheque was lost or stolen and came into the possession of B, who takes it in good faith and gives value for it. Section 130 of the Negotiable Instruments Act, 1881 provides that a person taking a cheque crossed generally or specially, bearing in either case the words ‘not negotiable’, shall not have, and shall not be capable of giving a better title to the cheque than that which the person from whom he took it had. In view of these provisions, B, even though he was a holder in due course, did not acquire any title to the cheque as against its true owner. The addition of the words ‘not negotiable’ entirely takes away the main feature of negotiability, which is, that a holder with a defective title can give a good title to a subsequent holder in due course. B did not obtain any better title than his immediate transferor, who had either stolen or found the cheque and was not the true owner of the cheque. Therefore, as regards the true owner, B was in no better position than the transferor. B is also liable to repay the amount of the cheque to the true owner. He can, however, proceed against the person from whom he took the cheque.

In the given case, both the collecting banker and the paying bankers would be exonerated. Since the collecting banker, in good faith and without negligence, had received payment for B, who was its customer of the cheque which was crossed generally, the banker would not be liable, in case the title proved to be defective, to the true owner by reason only of having received the payment of the cheque for his customer (Section 131). Since the paying banker on whom the crossed cheque was drawn, had paid the same in due course, the banker would also not be liable to the true owner. (Section 128).

**Question 15**

Referring to the provisions of the Negotiable Instruments Act, 1881, examine the validity of the following:

(i) A Bill of Exchange originally drawn by M for a sum of ₹ 10,000, but accepted by R only for ₹ 7,000.

(ii) A cheque marked ‘Not Negotiable’ is not transferable.
2.12 Business Laws, Ethics and Communication

Answer

(i) 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 this 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 (M) agrees to acceptance, the drawee (R) is responsible for a sum of ₹ 7000 only.

(ii) It is wrong statement. 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.

Question 16

What are the essential elements of a "Promissory note" under the Negotiable Instruments Act, 1881? Whether the following notes may be considered as valid Promissory notes:

(i)  "I promise to pay ₹ 5,000 or 7,000 to Mr. Ram."

(ii) I promise to pay to Mohan ₹ 500, if he secures 60% marks in the examination.

(iii) I promise to pay ₹ 3,000 to Ravi after 15 days of the death of A.

Answer

A promissory note is an instrument (not being a bank note or currency note) in writing containing an unconditional undertaking, signed by the maker to pay a certain sum of money only to or the holder of, a certain person or to the bearer of the instrument, (Section 4 of the Negotiable Instruments Act, 1881).

In view of the above provision of the said Act, following are the essential elements of a promissory note-

1. It must be in writing.
2. The promise to pay must be unconditional.
3. The amount promised must be a certain and a definite sum of money.
4. The instrument must be signed by the maker.
5. The person to whom the promise is made must be a definite person.
Thus:

(i) In case (i), it is not a valid promissory note because the amount is not certain.
(ii) In case (ii), it is not a valid promissory note because it is conditional.
(iii) In case (iii), it is a valid promissory note because death of A is a certainty even if time of death is not certain.

Question 17

Discuss with reasons, whether the following persons can be called as a ‘holder’ under the Negotiable Instruments Act, 1881:

(i) X who obtains a cheque drawn by Y by way of gift.
(ii) A, the payee of the cheque, who is prohibited by a court order from receiving the amount of the cheque.
(iii) M, who finds a cheque payable to bearer, on the road and retains it.
(iv) B, the agent of C, is entrusted with an instrument without endorsement by C, who is the payee.
(v) B, who steals a blank cheque of A and forges A’s signature.

Answer

Person to be called as a holder: As per section 8 of the Negotiable Instruments 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.

On applying the above provision in the given cases:

(i) Yes, X can be termed as a holder because he has a right to possession and to receive the amount due in his own name.
(ii) No, 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.
(iii) No, M is not a holder of the Instrument though he is in possession of the cheque, so is not entitled to the possession of it in his own name.
(iv) No, 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.
(v) No, B is not a holder because he is in wrongful possession of the instrument.

Question 18

Give the answer of the following:
2.14 Business Laws, Ethics and Communication

(a) 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 grounds of inadequate funds. Discuss the rights of X.

(b) 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?

(c) A draws a cheque for ₹100 and hands it over to B by way of gift. Is B a holder in due course? Explain the nature of his title, interest and right to receive the proceeds of the cheque.

(d) 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. Can B recover the money from the banker.

Answer

(a) As per Section 26, 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.

(b) As per the provision of the Negotiable Instruments 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.

(c) 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 ₹100 from the bank on whom the cheque is drawn.

(d) According to Section 85, 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.

Question 19

M drew a cheque amounting to ₹2 lakh payable to N and subsequently delivered to him. After receipt of cheque N endorsed the same to C but kept it in his safe locker. After sometime, N died, and P found the cheque in N’s safe locker. Does this amount to Indorsement under the Negotiable Instruments Act, 1881?

Answer

No, P does not become the holder of the cheque as the negotiation was not completed by delivery of the cheque to him. (Section 48, the Negotiable Instruments Act, 1881)
Question 20

M owes money to N. Therefore, he makes a promissory note for the amount in favour of N, for safety of transmission he cuts the note in half and posts one half to N. He then changes his mind and calls upon N to return the half of the note which he had sent. N requires M to send the other half of the promissory note. Decide how rights of the parties are to be adjusted.

Answer

The question arising in this problem is whether the making of promissory note is complete when one half of the note was delivered to N. Under Section 46 of the N.I. Act, 1881, the making of a P/N 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. So the claim of N to have the other half of the P/N sent to him is not maintainable. M 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 P/N.

Question 21

P draws a bill on Q for ₹ 10,000. Q accepts the bill. On maturity the bill was dishonored by non-payment. P files a suit against Q for payment of ₹ 10,000. Q proved that the bill was accepted for value of ₹ 7,000 and as an accommodation to the plaintiff for the balance amount i.e. ₹ 3,000. Referring to the provisions of the Negotiable Instruments Act, 1881 decide whether P would succeed in recovering the whole amount of the bill?

Answer

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.

[Explanation- 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. Other signers may by agreement stand in immediate relation with a holder].

On the basis of above provision, P would succeed to recover ₹ 7,000 only from Q and not the whole amount of the bill because it was accepted for value as to ₹ 7,000 only and an accommodation to P for ₹ 3,000.

Question 22

A Bill is drawn payable at No. A-17 CA apartments, Mayur Vihar, 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?
Answer

Yes, it is a valid Bill and Mr. Vinay is liable thereon. The drawee may be named or otherwise indicated in the Bill with reasonable certainty. In the present case, the description of the place of residence indicates the name of the drawee and Mr. Vinay, by his acceptance, acknowledges that he is the person to whom the bill is directed (Gray vs. Milner 1819).

Question 23

Pick out the correct answer from the following and give reason.

P, obtains a cheque drawn by M by way of gift. Here P is a :
1. holder in due course
2. holder for value
3. holder
4. None of the above

Answer

Holder: Yes, P can be termed as a holder because he has a right to possession and to receive the amount due in his own name.

Question 24

J accepted a bill of exchange and gave it to K for the purpose of getting it discounted and handing 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 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 the bill under the provisions of the Negotiable Instruments Act, 1881?

Answer

The problem is based upon the privileges of a 'holder in due course', Section 120 of the Negotiable Instruments Act, 1881 provides that 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 of the bill.

Therefore in the given problem J is liable to pay for the bill. L is a holder in due course, who got the bill in good faith and for value. (Ingham v Primrose)

Question 25

Distinguish between 'Bearer instrument' and 'Order instrument' under the Negotiable Instruments Act, 1881.
Answer

**Bearer and Order instruments:** An instrument may be made payable: (1) to bearer; or (2) to a specified person or to his order.

An instrument is said to be payable to bearer when it is expressed to be so payable to its bearer or when the only or last endorsement on it is an endorsement in blank. (Explanation 2 to section 13)

**An instrument is payable to order,** (1) when it is payable to the order of a specified person or (2) when it is payable to a specified person or his order or, (3) when it is payable to a specified person without the addition of the words “or his order” and does not contain words prohibiting transfer or indicating an intention that it should not be transferable. When an instrument, either originally or by endorsement, is made payable to the order of a specified person and not to him or his order, it is payable to him or his order, at his option.

When an instrument is not payable to bearer (i.e., in case of order instrument), the payee must be indicated with reasonable certainty.

Question 26

*State briefly the rules laid down under the Negotiable Instruments Act for determining the date of maturity of a bill of exchange. Ascertain the date of maturity of a bill payable hundred days after sight and which is presented for sight on 4th May, 2000.*

**Answer**

**Calculation of maturity of a Bill of Exchange:** The maturity of a bill, not payable on demand, at sight, or on presentment, is at maturity on the third day after the day on which it is expressed to be payable (Section 22, para 2 of Negotiable Instruments Act, 1881). Three days are allowed as days of grace. No days of grace are allowed in the case of bill payable on demand, at sight, or presentment.

When a bill is made payable at stated number of months after date, the period stated terminates on the day of the month which corresponds with the day on which the instrument is dated. When it is made payable after a stated number of months after sight the period terminates on the day of the month which corresponds with the day on which it is presented for acceptance or sight or noted for non-acceptance or protested for non-acceptance. When it is payable a stated number of months after a certain event, the period terminates on the day of the month which corresponds with the day on which the event happens (Section 23).

When a bill is made payable a stated number of months after sight and has been accepted for honour, the period terminates with the day of the month which corresponds with the day on which it was so accepted.

If the month in which the period would terminate has no corresponding day, the period terminates on the last day of such month (Section 23).
In calculating the date a bill made payable a certain number of days after date or after sight or after a certain event is at maturity, the day of the date, or the day of presentment for acceptance or sight or the day of protest for non-accordance, or the day on which the event happens shall be excluded (Section 24).

Three days of grace are allowed to these instruments after the day on which they are expressed to be payable (Section 22).

When the last day of grace falls on a day which is public holiday, the instrument is due and payable on the next preceding business day (Section 25).

**Answer to Problem:** In this case the day of presentment for sight is to be excluded i.e. 4th May, 2000. The period of 100 days ends on 12th August, 2000 (May 27 days + June 30 days + July 31 days + August 12 days). Three days of grace are to be added. It falls due on 15th August, 2000 which happens to be a public holiday. As such it will fall due on 14th August, 2000 i.e. the next preceding business day.

**Question 27**

In what way does the Negotiable Instruments Act, 1881 regulate the determination of the ‘Date of maturity’ of a Bill of Exchange. Ascertain the ‘Date of maturity’ of a bill payable 120 days after the date. The Bill of exchange was drawn on 1st June, 2005.

**Answer**

**Calculation of maturity of a Bill of Exchange:** The maturity of a bill, not payable on demand, at sight or on presentment, is at maturity on the third day after the day on which it is expressed to be payable (Section 22, para 2 of Negotiable Instruments Act, 1881). Three days are allowed as days of grace. No days of grace are allowed in the case of a bill payable on demand, at sight, or presentment.

When a bill is made payable as stated number of months after date, the period stated terminates on the day of the month, which corresponds with the day on which the instrument is dated. When it is made payable after a stated number of months after sight the period terminates on the day of the month which corresponds with the day on which it is presented for acceptance or sight or noted for non-acceptance on protested for Non-acceptance when it is payable a stated number of months after a certain event, the period terminates on the day of the month which corresponds with the day on which the event happens. (Section 23).

When a bill is made payable a stated number of months after sight and has been accepted for honour, the period terminates on the day of the month which corresponds with the day on which it was so accepted.

If the month in which the period would terminate has no corresponding day, the period terminates on the last day of such month (Section 23).

In calculating the date a bill made payable a certain number of days after date or after sight or after a certain event is at maturity, the day of the date, or the day of protest for non-acceptance, or the day on which the event happens, shall be excluded (Section 24).
Three days of grace are allowed to these instruments after the day on which they are expressed to be payable. (Section 22).

When the last day of grace falls on a day, which is public holiday, the instrument is due and payable on the next preceding business day (Section 25).

Answer to Problem: In this case the day of presentment for sight is to be excluded i.e. 1st June, 2005. The period of 120 days ends on 29th September, 2005 (June 29 days + July 31 days + August 31 Days + September 29 days = 120 days). Three days of grace are to be added. It falls due on 2nd October, 2005, which happens to be a public holiday. As such it will fall due on 1st October, 2005 i.e., the next preceding Business Day.

Question 28
Bharat executed a promissory note in favour of Bhushan for ₹ 5 crores. The said amount was payable three days after sight. Bhushan, on maturity, presented the promissory note on 1st January, 2008 to Bharat. Bharat made the payments on 4th January, 2008. Bhushan wants to recover interest for one day from Bharat. Advise Bharat, in the light of provisions of the Negotiable Instruments Act, 1881, whether he is liable to pay the interest for one day?

Answer
Claim of Interest: Section 24 of the Negotiable Instruments 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.

Therefore, in the given case, Bharat will succeed in objecting to Bhushan’s claim. Bharat paid rightly “three days after sight”. Since the bill was presented on 1st January, Bharat was required to pay only on the 4th and not on 3rd January, as contended by Bharat.

Question 29
What do you mean by an endorsement. Briefly explain the types of an endorsement.

Answer
The endorsement consists of the signature of the holder made on the back of the negotiable instrument with the object of transferring the instrument. If there is no space on the instrument, the endorsement may be made on a slip of paper attached to it. This attachment is known as “Allonge”.

According to Section 15 of the Negotiable Instruments Act, 1881 “when the maker or holder of a negotiable instrument signs the same, otherwise than as such maker, for the purpose of negotiation, on the back or face therefore or on slip of paper annexed thereto, or so signs for the same purpose a stamped paper intended to be completed as negotiable instrument, he is said to endorse the same, and is called the endorser.”

Types of Indorsements.
1. Endorsement in Blank
2.20 Business Laws, Ethics and Communication

2. Endorsement in Full
3. Restrictive Endorsement
4. Endorsement sans recouer
5. Conditional Endorsement
6. Facultative Endorsement
7. Partial Endorsement
8. Sans frais Endorsement

Question 30

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 the recovery of the money.

With reference to the provisions of the Negotiable Instruments Act, decide whether X will succeed in the case?

Answer

The problem stated in the question is based on the provisions of the Negotiable Instruments Act, 1881 as contained in Section 53. The section provides: ‘Once a negotiable instrument passes through the hands of a holder in due course, it gets cleansed of its defects provided the holder was himself not a party to the fraud or illegality which affected the instrument in some stage of its journey. Thus any defect in the title of the transferor will not affect the rights of the holder in due course even if he had knowledge of the prior defect provided he is himself not a party to the fraud. (Section 53).

Thus applying the above provisions it is quite clear that X who originally induced Y in obtaining the bill of exchange in question fraudulently, cannot succeed in the case. The reason is obvious as X himself was a party to the fraud.

Question 31

What is a ‘Sans Recours’ endorsement? 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 Recours’.

Answer

Meaning of Sans Recours Endorsement: It is a type of endorsement on a Negotiable Instrument by which the endorser absolves himself or declines to accept any liability on the instrument of any subsequent party. The endorser signs the endorsement putting his signature along with the words, “SANS RECOURS.”
In the problem X, the endorser becomes the holder after it is negotiated to several parties. Normally, in such a case, none of the intermediate parties is liable to X. This is to prevent ‘circuitry of action’. But in this case X’s original endorsement is ‘sans recours’ 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 (Section 52 para 2).

**Question 32**

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, 1882, decide whether D can recover the money from A in the given case.

**Answer**

Section 53 of the Negotiable Instruments Act, 1881 provides that a holder of negotiable instrument who derives title from a holder in due course has the right thereon of that holder in due course. Such holder of the bill who is not himself a party to any fraud or illegality affecting it, has all the rights of that holder in due course as regards to the acceptor and all parties to the bill prior to that holder. In this case, it is clear that though D was aware of the fraud, he was himself not a party to it. He obtained the instrument from C who was a holder in due course. So D gets a good title and can recover from A.

**Question 33**

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.

**Answer**

Minor being a party to negotiable instrument: Every person competent to contract has capacity to incur liability by making, drawing, accepting, endorsing, delivering and negotiating a promissory note, bill of exchange or cheque (Section 26, para 1, Negotiable Instruments Act, 1881).

As a minor’s agreement is void, 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 parties except himself (Section 26, para 2).

In view of the provisions of Section 26 explained above, the promissory note executed by X and M is valid even though a minor is a party to it. M, being a minor is not liable; but his immunity from liability does not absolve the other joint promisor, namely X from liability [Sulochana v. Pandiyan Bank Ltd., AIR (1975) Mad. 70].
Question 34

A draws a bill on B. B accepts the bill without any consideration. The bill is transferred to C without consideration. C transferred it to D for value. Decide-

(i) Whether D can sue the prior parties of the bill, and
(ii) Whether the prior parties other than D have any right of action inter se?

Give your answer in reference to the Provisions of Negotiable Instruments Act, 1881.

Answer

Problem on Negotiable Instrument made without consideration: Section 43 of the Negotiable Instruments Act, 1881 provides that a negotiable instrument made, drawn, accepted, indorsed 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 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.

(i) In the problem, as asked in the question, A has drawn a bill on B and B accepted the bill without consideration and transferred it to C without consideration. Later on in the next transfer by C to D is for value. According to provisions of the aforesaid section 43, the bill ultimately has been transferred to D with consideration. Therefore, D can sue any of the parties i.e. A, B or C, as D arrived a good title on it being taken with consideration.

(ii) As regards to the second part of the problem, the prior parties before D i.e., A, B, and C have no right of action inter se because first part of Section 43 has clearly lays down that a negotiable instrument, made, drawn, accepted, indorsed or transferred without consideration, or for a consideration which fails, creates no obligation of payment between the parties to the transaction prior to the parties who receive it on consideration.

Question 35

Briefly explain the circumstances of dishonour of a Negotiable Instrument. What are the consequences of a ‘cheque being dishonoured for insufficiency of funds’ in the account?

Answer

Dishonour by non-acceptance (Section 91, the Negotiable Instruments Act, 1881): A bill may be dishonoured either by non-acceptance or by non-payment. A dishonour by non-acceptance may take place in any one of the following circumstances:

(i) when the drawee either does not accept the bill within forty-eight hours of presentment or refuse to accept it;

(ii) when one of several drawees, not being partners, makes default in acceptance;

(iii) when the drawee gives a qualified acceptance;
(iv) when presentment for acceptance is excused and the bill remains unaccepted; and
(v) when the drawee is incompetent to contract.

An instrument is dishonoured by non-payment when the party primarily liable e.g., the acceptor of a bill, the maker of a note or the drawee of a cheque, make default in payment. An instrument is also dishonoured for non-payment when presentment for payment excused and the instrument, when overdue, remains unpaid, under section 76 of the Act.

Dishonour of cheque for insufficiency, etc. of funds in the account: Where any cheque drawn by a person on an account maintained by him with a banker for payment is dishonoured due to insufficiency of funds, he shall be punished with imprisonment for a term which may extend to one year or with fine which may extend to twice the amount of the cheque or with both [Section 138 of the Negotiable Instruments Act, 1881].

Provided that nothing in this section shall apply unless:

(i) such cheque should have been presented to the bank within a period of 3 months of the date of drawn or within the period of its validity, whichever is earlier.

(ii) The payee or holder in due course of such cheque had made a demand in writing for the payment of the said amount of money from the drawer 30 days of the receipt of information by him from the bank regarding the return of the cheque unpaid; and

(iii) The drawer of the cheque had failed to pay the money to the payee or holder in due course of the cheque within 15 days for the written demand for payment.

Question 36

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 company’s account to discharge its legal liability. Subsequently the cheque was dishonoured and the compliant was lodged against him. Does he is liable for an offence under section 138?

Answer

According to Section 138 of the Negotiable Instruments Act, 1881 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. Therefore, he has not committed an offence under section 138.
2.24 Business Laws, Ethics and Communication

Question 37

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 Negotiable Instruments Act, 1881 state whether J has committed an offence under Section 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).

Answer

The facts of the problem are identical with the facts of a case known as H.N.D. Mulla Feroze Vs. C.Y. Somaya Julu, J(2004) 55 SCL (AP) wherein 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 J could not be said to have committed the offence under Section 138 of the Negotiable Instruments Act, 1881. Therefore X also is not liable for the cheque but legally liable for the payments for the goods.

Question 38

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 Negotiable Instruments Act, 1881, whether the said acts of X constitute an offence against him?

Answer

Offence under the Negotiable Instruments Act, 1881: This problem is based on the case of Modi Cements Ltd. Vs. Kuchil Kumar Nandi, 1998. In this case the Supreme Court held that once a cheque is issued by the drawer, a presumption under Section 139 of the Negotiable Instruments 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 preclude an action under Section 138. The object of Sections 138 to 142 of the Act is to promote the efficacy of the banking operations and to ensure credibility in transacting business through cheques. Section 138 is a penal provision in the sense that once a cheque is drawn on an account maintained by the drawer with his banker for payment of any amount of money to another person from out of that account for the discharge in whole or in part of any debt or other liability, is informed by the bank unpaid 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.
Question 39

State, in brief, the grounds on the basis of which a banker can dishonor a cheque under the provisions of the Negotiable Instruments Act, 1881.

Answer

Dishonour of Cheque – Grounds: A banker will be justified or bound to dishonor a cheque in the following cases, viz:

- If a cheque is undated, if it is stale, that is if it has not been presented within reasonable period, which may vary three months to a year after its issue dependent on the circumstances of the case
- If the instrument is inchoate or not free from reasonable doubt
- If the cheque is post-dated and presented for payment before its ostensible date
- If the customer’s funds in the banker’s hands are not ‘properly applicable’ to the payment of cheque drawn by the former. Thus, should the funds in the banker’s hands be subject to a lien or should the banker be entitled to a set-off in respect of them, the funds cannot be said to be “properly applicable” to the payment of the customer’s cheque, and the banker would be justified in refusing payment.
- If the customer has credit with one branch of a bank and he draws a cheque upon another branch of the same bank in which either he has account or his account is overdrawn.
- If the bankers receive notice of customer’s insolvency or lunacy
- If the customer countermands the payment of cheque for the banker’s duty and authority to pay on a cheque ceases
- If a garnishee or other legal order from the Court attaching or otherwise dealing with the money in the hand of the banker, is served on the banker
- If the authority of the banker to honor a cheque of his customer is undermined by the notice of the latter’s death. However, any payment made prior to the receipt of the notice of death is valid.
- If notice in respect of closure of the account is served by either party on the other.
- If it contains material alterations, irregular signature or irregular endorsement.

Question 40

State whether the following statements are correct or incorrect:

The validity period of a cheque is three months.
Answer

The validity period of a cheque is three months. This statement is correct

Question 41

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.

Answer

Bill drawn in fictitious name: The problem is based on the provision of Section 42 of the Negotiable Instruments Act, 1881. 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 as against the holder in due course that such name is fictitious. 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.

Question 42

A cheque was dishonoured at the first instance and the payee did not initiate action. The cheque was presented for payment for the second time and again it was dishonoured. State in this connection whether the payee can subsequently initiate prosecution for dishonour of cheque.

Answer

Supreme Court in Sadanandan Bhadran v. Madhavan Sunil Kumar (1998) 4 CLJ 228 held that on a careful analysis of section 138 of the Negotiable Instruments Act, 1881 it is seen that the main part creates an offence when a cheque is returned by the bank unpaid for any of the reasons mentioned therein. The said proviso lays down three conditions precedent to the applicability of the above section and the conditions are:

1. the cheque should have been presented to the bank within three months of its issue or within the period of its validity whichever is earlier;
2. the payee should have made a demand for payment by registered notice after the cheque is returned unpaid; and
3. the drawer should have failed to pay the amount within 15 days of the receipt of notice. It is only when all the above three conditions are satisfied that a prosecution can be launched for the offence under section 138.

So far as the first condition is concerned clause (a) of the proviso to section 138 does not put any embargo 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. The question whether dishonour of the cheque on each occasion of its presentation gives rise to a fresh cause of action, the following facts are required to be proved to successfully to prosecute the drawer for an offence under section 138:-

(1) that the cheque was drawn for payment of an amount of money for discharge of a debt/liability and the cheque was dishonoured;

(2) that the cheque was presented within the prescribed period;

(3) that the payee made demand for payment of the money by giving a notice in writing to the drawer within the stipulated period;

(4) that the drawer failed to make the payment within 15 days of the receipt of the notice.

If one has to proceed on the basis of the generic meaning of the terms “cause of action”, certainly each of the above facts would constitute a part of the cause of action, but it is significant to note that clause (b) of section 142(1) gives a restrictive meaning in that it refers to only one fact which will give rise to the cause of action and that is failure to make the payment within 15 days from the date of receipt of the notice.

Besides the language of section 138 and section 142 which clearly postulates only one cause of action, there are other formidable impediments which negate the concept of successive causes of action. The combined reading of sections 138 and 142 leave no room for doubt that cause of action within the meaning of section 142(1)(c) arises and can arise only once.

The final question as how apparently conflicting provisions of the Act, one enabling the payee to repeatedly present the cheque and the other giving him only one opportunity to file a complaint for its dishonour and that too within one month from the date of cause of action arises can be reconciled, the Court held that the two provisions can be harmonized with the interpretation that on each presentation of the cheque and its dishonour, a fresh right and not initiate such prosecution on the earlier cause of action.

**Question 43**

A, a broker draws a cheque in favour of B, a minor. B indorses the cheque in favour of C, who in turn indorses it in favour of D. Subsequently, the bank dishonoured the cheque. State the rights of C and D and whether B, can be made liable?

**Answer**

According to Section 26 of the Negotiable Instruments Act, 1881 a minor may draw, endorse, deliver and negotiate a negotiable instrument to bind all parties except himself. Therefore, C and D cannot claim from B, who being a minor does not incur any liability on the cheque. C

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can claim payment from A, the Drawer, only and D can claim against C, the endorser and A, the drawer.

**Question 44**

X draws a bill on Y for ₹10,000 payable to his order. Y accepts the bill but subsequently dishonours it by non-payment. X sues Y on the bill. Y proves that it was accepted for value as of ₹8,000 and as accommodation to X for ₹2,000. How much can X recover from Y? Decide with reference to the provisions of the Negotiable Instruments Act, 1881.

**Answer**

According to the provisions of Section 44 of the Negotiable Instruments Act, 1881, when there is a partial absence or failure of money consideration for which a person signed a bill of exchange, the same rules as applicable for total absence or failure of consideration will apply. Thus, the parties standing in immediate relation to each other cannot recover more than the actual consideration. Accordingly, X can recover only ₹8,000.

**Question 45**

What is the extent of liability of the company and the person(s) in charge of the company in respect of an offence for dishonour of cheques?

**Answer**

From a perusal of Section 141, it is apparent that in case where a company committed an offence under Section 138, then not only the company, but also every person who at the time when the offence was committed, was in charge of and was responsible to the company shall deemed to be guilty of the offence and liable to be proceeded against under those provisions, only if that person was in charge of and was responsible to the company for the conduct of its business. [K.P.G. Nair vs. Jindal Menthol Indian Ltd. (2001) 2CLJ 258 SC]

**Question 46**

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?

**Answer**

“The bank” referred to in clause (a) to the proviso to Section 138 of the Negotiable Instruments 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. It, however, does not mean that the cheque is always to be presented to the drawer's bank on which the cheque is issued. The payee of the cheque has the option to present, the cheque in any bank including the collecting bank where he has his account, but to attract the criminal liability of the drawer of the cheque, such collecting bank is obliged to present the cheque in the drawee or payee bank on which the cheque drawn within the period of three months from the date on which it is shown to have been issued. The non presentation
of the cheque to the drawee-bank within the period specified in the Section would absolve the
person issuing the cheque, of his criminal liability under Section 138 or the Act, who shall
otherwise may be liable to pay the cheque amount to the payee in a civil action initiated under
the law. A combined reading of Sections 2, 72 and 138 of the Act would leave no doubt that
the law mandates the cheque to be presented at the bank on which it is drawn, if the drawer is
to be held criminally liable. Such presentation is necessarily to be made within three months at
the bank on which the cheque is drawn whether presented personally, or through another
bank, namely, the collecting bank of the payee [Shri Ishar Alloy Steels Ltd. (v) Jayaswal Neco. Ltd. (2001) LCLI 18 (SC)]

Question 47

Whether giving of notice of dishonour itself constitute receipt of notice for constituting offence
under section 138 of the Negotiable Instruments Act, 1881?

Answer

The above matter was considered by the Supreme Court in Oalmia Cement (Bharat) Ltd
v. Galaxy Traders and Agencies Ltd., (2001) 5 CLJ 26 SC. The Court observed that, the payee
has to make a demand by giving notice in writing to the drawer within 30 days of the receipt of
information from bank regarding the return of the cheque as unpaid. 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 in writing,
is a process of which receipt is the accomplishment. It is therefore clear that 'giving' notice is
not the same as 'receipt' of notice.

Question 48

Whether demand draft is a cheque?

Answer

Section 131 of the Negotiable Instruments 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
under Section 138. [Punjab & Sind Bank v Vinkar Sahakari Bank Ltd., (2001) 4 CLJ 188 (SC)]
Question 49

Mr. Clever obtains fraudulently from J a cheque crossed ‘Not Negotiable’. He later transfers the cheque to D, who gets the cheque encashed from ABC Bank, which is not the Drawee Bank. J, comes to know about the fraudulent act of Clever, sues ABC Bank for the recovery of money. Examine with reference to the relevant provisions of the Negotiable Instruments Act, 1881, whether J will be successful in his claim. Would your answer be still the same in case Clever does not transfer the cheque and gets the cheque encashed from ABC Bank himself?

Answer

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 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 holder in due course by proving that he purchased the instrument in good faith and for value. As Mr. Cleaver in the case in question had obtained the cheque fraudulently, he had no title to it and could not 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 J in both the cases shall be successful in his claim from ABC bank.

Question 50

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.

Answer

Section 44 of the Negotiable Instruments Act, 1881 is applicable in this case. According to Section 44 of this Act, 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 a holder for value, is not adversely affected and he can claim the full amount of the cheque from B.
Question 51

What do you understand by "Material alteration" under the Negotiable Instruments Act, 1881? State whether the following alterations are material alterations under the Negotiable Instruments Act, 1881?

(i) The holder of the bill inserts the word "or order" in the bill,
(ii) The holder of the bearer cheque converts it into account payee cheque,
(iii) A bill payable to ' is converted into a bill payable to X and Y

Answer

As per the Negotiable Instruments Act, 1881, an alteration can be called a material alteration if it alters or attempts to alter the character of the instrument and affects or is likely to affect the contract which the instrument contains or is evidence of. Thus, it totally alters the business effect of the instrument. It makes the instrument speak a language other than that was intended.

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

(a) filling blanks of inchoate instruments [Section 20]
(b) Conversion of a blank endorsement into an endorsement in full [Section 49]
(c) Crossing of cheque [Section 125]

The important material and non-material alteration are:

<table>
<thead>
<tr>
<th>Material alteration</th>
<th>Non-material alteration</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Alteration of date of instrument (e.g. if a bill dated 1st may, 1998) is changed to a bill dated 1st June, 1998.</td>
<td>1. Conversion of instrument payable to bearer.</td>
</tr>
<tr>
<td>2. Alteration of time of payment (e.g. if a bill payable three months after date is changed to bill payable four months payable after date).</td>
<td>2. Conversion of instrument payable to bearer into order.</td>
</tr>
<tr>
<td>3. Alteration of place of payment (e.g., if a bill payable at Delhi is changed to bill payable at Mumbai).</td>
<td>3. Elimination of the words ‘or order’ from an endorsement.</td>
</tr>
<tr>
<td>4. Alteration of amount payable (e.g., if bill for ₹ 1,000 is changed to a bill for ₹ 2000)</td>
<td>4. Addition of the words ‘or demand’ to a note in which no time or payment is expressed.</td>
</tr>
<tr>
<td>5. Conversion of blank endorsement into</td>
<td></td>
</tr>
</tbody>
</table>
2.32 Business Laws, Ethics and Communication

<table>
<thead>
<tr>
<th>special endorsement.</th>
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<tbody>
<tr>
<td>6. Addition of a new party to an instrument.</td>
</tr>
<tr>
<td>7. Alteration of one of the clauses of the instrument containing a penal action</td>
</tr>
</tbody>
</table>

As per the above sections the changes of serial numbers (i) is non-material and changes of serial numbers (ii) (iii) are material changes in the given problem.

Question 52

Do the following alteration of a negotiable instrument render the instrument void?

(a) The holder of a bill alters the date of the instrument to accelerate or postpone the time of payment.

(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.

(c) A bill payable three months after date is altered into a bill payable three months after sight.

(d) A bill was dated 2002 instead of 2003 and subsequently the agent of the drawer corrected the mistake.

(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.

Answer

(a) Yes.

(b) No.

(c) Yes.

(d) No.

(e) Yes.

According to Section 87 of the Negotiable Instruments Act, 1881, any material alteration of a Negotiable Instrument renders the same void as against any one who is party thereto at the time of making such alteration and does not consent thereto, unless it was made in order to carry out the common intention of the original parties and any such alteration, if made by an endorsee discharges endorser from all liability to him in respect of the consideration thereof. The alteration must be so material that it alters the character of the instrument, to a great extent. Alterations of the date, amount payable, time, place of payment are regarded as material alterations.

Question 53

On a Bill of Exchange for ₹ 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’.

Answer

According to section 9 of the Negotiable Instruments Act, 1881 ‘holder in due course’ means any person who for consideration becomes 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.

As ‘A’ in this case prima facie became a possessor of the bill for value and in good faith before the bill became payable, he can be considered as a holder in due course.

But where a signature on the negotiable instrument is forged, it becomes a nullity. 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 whereof 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.

Question 54

A banker made payment of a cheque in which the drawers 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?

Answer

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.

Question 55

X drew a cheque payable to ‘Y or on order’. Unfortunately it was lost and Y’s endorsement was forged. Subsequently, the banker pays for the cheque. Is the banker discharged from liability? What will be the consequences if the drawer’s signatures were forged?

Answer

The paying banker is discharged from liability, despite the forged Indorsement in favour of the payee, because of special protection granted by section 85(1) of the Negotiable Instruments Act, 1881.
In another instance, where the drawer’s signature is forged, a banker remains liable to the drawer even by a payment in due course and cannot debit the drawer’s account.

**Question 56**

*How do you distinguish between discharge of instrument and discharge of party under the Negotiable Instruments Act, 1881?*

**Answer**

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 thereunder are extinguished even a holder in due course cannot claim any amount under the bill.

**Question 57**

*What will be the effect of the following alterations on the validity of a bill?*

(i) A bill payable with ‘lawful interest’ is altered into one payable with 12% interest.

(ii) 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.

**Answer**

(i) The following alterations are material, i.e., the alteration of –

1. the date,
2. the sum payable,
3. the time of payment,
4. the place of payment,
5. inclusion of place of payment,
6. the rate of interest.

These alterations vitiate the instrument. So, in the given case alteration in the interest rate vitiates the validity of the bill, since lawful interest is 18% under the Banking, Public Financial Institutions & Negotiable Instruments (Amendment) Act, 1988.

(ii) In this case, the alteration is material. It renders the instrument void against persons who were parties thereto before such alteration, unless they have consented to the alteration (Sec. 87)
Question 58

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 provisions of the Negotiable Instruments Act, 1881 and also state whether Anil can claim the privileges of a Holder in Due course.

Answer

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 the case of forged endorsement, the person claiming under forged endorsement even if he is purchaser for value and in good faith, cannot acquire the rights of a holder in due course. Therefore, Anil acquires no title on the cheque (Mercantile Bank vs. D’Silva, 30 Bom.L.R.1225).

Question 59

Is notice of dishonour necessary in the following cases:

(a) X having a balance of ₹ 1,000 with his bankers and having no authority to overdraw, drew a cheque for ₹ 5,000/- . The cheque was dishonoured when duly presented for repayment.

(b) X, drawer of a Bill informs Y, the holder of the bill that the bill would be dishonoured on the presentment for payment.

Answer

Notice of dishonour is not necessary in both the cases. [Section 98 of the Negotiable Instruments Act, 1881].

Question 60

Ram has ₹ 2,000/- in his bank account and he has no authority to overdraw. He issued a cheque for ₹ 5,000/- to Gopal which was dis-honoured by the bank. Point out whether Gopal must necessarily give notice of dishonor to Ram under the Negotiable Instruments Act, 1881?

Answer

As per the provision given under the Negotiable Instruments Act, 1881, in a suit against the drawer on an instrument being dishonored, notice of dishonor is a material part of the cause of action. However, there are certain cases where notice of dishonor is not necessary, when the party charged could not suffer damage for want of a notice. In such a case, it is sufficient if it is shown that at the time of drawing the instrument, there were no funds belonging to the drawer in the hands of the drawee. Thus, it is not necessary for Gopal to give notice of
dishonor to Ram under section 98 of the Act [Subrao vs. Sitaram 2 Bom. L.R. 891].

**Question 61**

A Bill of Exchange is dishonoured by the acceptor. Explain the provisions of “Noting” and “Protest” under the Negotiable Instruments Act, 1881.

**Answer**

The law related to the noting and protest of negotiable instruments is enshrined in Section 99 to 104A of the Negotiable Instruments Act, 1881.

**Noting:** According to section 99, when a promissory note or bill of exchange has been dishonoured by non-acceptance, or non-payment the holder may cause such dishonour to be noted by a notary public upon the instrument, or on a paper attached thereto, or partly upon each. Such note must be made within a reasonable time after dishonour, and must specify the date of dishonour, the reason for the dishonour or if the instrument has not been expressly dishonoured, the reason why the holder treats it as dishonour and the notary’s charges.

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

The contents of a protest are laid down in section 101 of the Act. According to section 102, when a promissory note or bill of exchange is required to be protested, notice of such protest must be given instead of notice of dishonour, in the same manner and subject to the same conditions, but the notice may be given by the notary making the protest. Under section 103, all bills of exchange drawn payable at some other place than the place mentioned as the residence of the drawee, and which are dishonoured by non-acceptance, may, without further presentation to the drawee, be protested for non-payment in the place specified for payment, unless paid before or at maturity.

Neither noting nor protesting is compulsory in the case of inland bills. But under section 104, every foreign bill must be protested for dishonour, when such protest is required by law of the country where the bill was drawn. 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 section 119 the court is bound to recognise a protest, but it may or not recognise noting.

**Question 62**

Explain the terms 'Acceptance for Honour' and 'Drawee in case of need' as used in the Negotiable Instruments Act, 1881.

**Answer**

**Acceptance for Honour (Section 108):** It is an unusual kind of acceptance done by any person not being a party already liable thereon bill, to accept the bill for the honour of any
party thereto. This acceptance by such party is allowed when the original drawee refuses to accept or refuses to give better security when demanded by the notary. Such a bill is kept until its maturity and the holder is given an additional person whom the holder may fall back upon if the bill is not paid when due.

**Drawee in case of need:** As per section 7, when in the bill or in any endorsement thereon the name of any person is given in addition to the drawee to be resorted to in case of need, such person is called a “drawee in case of need”. Such a person is resorted to in the event of the bill being dishonoured by non-acceptance or non-payment. According to section 115, the bill will not consider to be dishonoured until it has been dishonoured by such drawee in case of need. Thus, it is obligatory on the holder to present the bill to such drawee and non-presentation of the bill to such drawee absolves the drawer from liability.

**Question 63**

*What is meant by ‘Payment for Honour’ in respect of a Bill of Exchange? When can the ‘Payment for Honour’ be made? What are the rights of the ‘Payer for Honour’?*

**Answer**

**Payment for honour:** It means a payment which is made by any person for the honour of any party liable on the bill after it has been protested for non-payment.

The following conditions are essential for the payment of honour:

1. The bill must have been noted or protested for non-payment.
2. The person paying or his agent declares before Notary Public the party for whose honour he pays.
3. Such declaration must have been recorded by the Notary Public.
4. Payment must be made for the honour of any party liable on the bill or not (Section 113).

The drawee in case of need may, however, accept and pay the bill of exchange without previous protest. (Section 110).

**Right of the payer for honour:** Any person making payment for honour is entitled to all the rights, in respect of the bill, of the holder at the time of such payment. He may recover from the party for whose honour he pays all sums so paid with interest thereon and all expenses properly incurred in making such payment (Section 114).

**Question 64**

*Promissory note dated 1st February, 2001 payable two months after date was presented to the maker for payment 10 days after maturity. What is the date of Maturity? 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.*
Answer

Delay in presentment for payment of a promissory note: If a promissory note is made payable on a stated number of months after date, it becomes payable three days after the corresponding date of months after the stated number of months (Section 23 read with Section 22 Negotiable Instruments Act 1881). Therefore, in this case the date of maturity of the promissory note is 4th April, 2001.

In this case the promissory note was presented for payment 10 days after maturity. According to Section 64 of Negotiable Instruments Act read with Section 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 (that is, parties other than the parties primarily liable) are not liable to such holder. 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.

Question 65

A issues a cheque for ₹ 25,000/- in favour of B. A has sufficient amount in his account with the Bank. The cheque was not presented within reasonable time to the Bank for payment and the Bank, in the meantime, became bankrupt. Decide under the provisions of the Negotiable Instruments Act, 1881, whether B can recover the money from A?

OR

‘A’ issued a cheque for ₹ 5,000/- to ‘B’. ‘B’ did not present the cheque for payment within 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 Negotiable Instruments Act, 1881.

Answer

The problem as asked in the question is based on the provisions of the Negotiable Instruments Act, 1881 as contained in Section 84. The section provides that 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, the usage of trade and bankers, and the facts of the particular case.

Accordingly, in the given case, the drawer is discharged from the liability to pay the amount of cheque to B. However, B can sue against the bank for the amount of the cheque applying the above provisions.

Question 66

‘A’ draws a cheque for ₹ 50,000. When the cheque ought to be presented to the drawee bank, the drawer has sufficient funds to make payment of the cheque. The bank fails before the
cheque is presented. The payee demands payment from the drawer. What is the liability of the drawer?

**Answer**

Section 84 of the Negotiable Instruments Act, 1881 provides that where a cheque is not presented for payment within a reasonable time of its issue and the drawer or person on whose account it is drawn had the right at the time when presentation ought to have been made, as between himself and the banker, to have the cheque paid and suffers actual damage through the delay, he is discharged from the liability, that is to say, to the extent to which such drawer or person is a creditor of the banker to a larger amount than would have been if such cheque had been paid. In determining what is a reasonable time, regard shall be had to the nature of the instrument, the usage of trade and of banker, and the facts of the particular case.

Applying the above provisions to the given problem since the payee has not presented the cheque to the drawer’s bank within a reasonable time when the drawer had funds to pay the cheque, and the drawer has suffered actual damage, the drawer is discharged from the liability.

**Question 67**

(i) *What is meant by ‘Sans Recours Endorsement’ of a bill of exchange? How does it differ from ‘Sans Frais Endorsement’?*

(ii) *‘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’.

**Answer**

(i) **Sans Recourse: Sans Frais (The Negotiable Instruments Act, 1881):**

   *Sans Recourse:* By adding the words ‘Sans Recourse’ after the endorsement the endorser declines to accept any liability on the instrument of any subsequent party. Sometimes, when an endorser who so excludes his liability as an endorser afterwards becomes the holder of the same instrument. In such a case, all intermediate endorsers are liable to him.

   *Sans Frais:* These words when added at the end of the endorsement, indicate that no expenses should be incurred on account of the bill.

   **Difference:** Any endorser can exclude personal liability by endorsing “sans recours” i.e. without recourse. However, “Sans Frais” endorsement, indicate that no expenses should be incurred on account of the bill.

(ii) **Liability of a Minor:** According to Section 26 of the Negotiable Instruments 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 party having
such capacity may himself put his signature or authorize some other person to do so.

A minor may draw, endorse, deliver and negotiate an instrument so as to bind all the parties except himself. A minor may be a drawer where the instrument is drawn or endorsed by him. In that case he does not incur any liability himself although other parties to the instrument can be made liable and the holder can receive payment from any other party thereto.

Therefore, in the instant case, the promissory note is valid and it is binding on 'P' but not on 'Q', a minor.

Question 68

(i) Mr. A is the payee of an order cheque. Mr. B steals the cheque and forges Mr. A signatures and endorse the cheque in his own favour. Mr. B then further endorses the cheque to Mr. C, who takes the cheque in good faith and for valuable consideration. Examine the validity of the cheque as per the provisions of the Negotiable Instruments Act, 1881 and also state whether Mr. C can claim the privileges of a Holder-in-Due course?

(ii) Explain the concept and different forms of Restrictive and Qualified endorsement.

Answer

(i) Title to forged cheque under the Negotiable Instruments Act, 1881: 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 the case of forged endorsement, the person claiming under forged endorsement even if he is purchaser for value and in good faith, cannot acquire the rights of a holder in due course. Therefore, Mr. C acquires no title on the cheque (Mercantile Bank vs. D'Silva, 30 Bom.L.R.1225). Such a holder is not a holder in due course and hence no privilege is available.

(ii) (1) Restrictive Endorsement: Such an endorsement has the effect of restricting further negotiation and transfer of the instrument.

Example:

(1) Pay to A only                     S. Mukerjee

(2) For the account of A only        N. Aiyar

(2) Conditional or qualified endorsement: Such an endorsement combines an order to pay with condition.

Example: Pay to A on safe receipt of goods. V. Chopra

Question 69

State whether the following statements are correct or incorrect:
(i) A cheque marked "Not negotiable" is not transferable.

(ii) A promissory note duly executed in favour of a minor, is valid.

Answer

(i) A cheque marked “Not Negotiable” is not transferable.

Incorrect. 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.

(ii) A promissory note duly executed in favour of a minor, is valid.

Correct. As a minor’s agreement is void, 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 parties except himself (Section 26 of the Negotiable Instruments Act, 1881).

Exercise

1. A draws a bill on B for ₹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 ₹400 and as accommodation to A as to the balance. How much can A recover from B?

[Hint: ₹400 as per Section 44 of the Negotiable Instruments Act, 1881]

2. 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 indorsed 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?

[Hint: He can succeed against A as well as against both as per Sections 9 and 58 of the N.I. Act, 1881]

3. A bill is drawn “Pay to A or order the sum of one thousand rupees”. In the margin, the amount stated is ₹10,000 in figures. (a) Is this a valid bill? (b) If so, for what amount?

[Hint: (a) Yes; (b) For ₹1000 as per section 18 of the N.I. Act, 1881]

4. X draws a bill of exchange payable at 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?

[Hint: The bill is valid and Y shall be liable. By his acceptance, Y acknowledged that he was the intended drawee in the bill]