NEGOTIABLE INSTRUMENT ACT

DEFINITION

The word "Negotiable" means "Transferable by delivery", and the word "Instrument" means "A written document by which a right is created in favor of some person". Thus, the term "Negotiable instrument" literally means "a written document transferable by delivery".

According to Section 13 of the Negotiable Instruments Act,

"A negotiable instrument means a promissory note, bill of exchange or cheque payable either to order or to bearer."

Features of Negotiable Instruments

1. **Must be in writing-**

   A negotiable instrument must be in writing. This includes handwriting, typing, computer print out and engraving, etc.

2. **Unconditional Order**

   In every negotiable instrument there must be an unconditional order or promise for

payment. 3. **Payment**

   The instrument must involve payment of a certain sum of money only and nothing else. For example, one cannot make a promissory note on assets, securities, or goods.

4. **The time of payment must be certain**

   It means that the instrument must be payable at a time which is certain to arrive. If the time is mentioned as 'when convenient' it is not a negotiable instrument. However, if the time of payment is linked to the death of a person, it is nevertheless a negotiable instrument as death is certain, though the time thereof is not.

5. **The payee must be a certain person**

   It means that the person in whose favor the instrument is made must be named or described with reasonable certainty. The term 'person' includes individual, body corporate, trade unions, even secretary, director or chairman of an institution. The payee can also be more than one person.

6. **Signature**

   A negotiable instrument must bear the signature of its maker. Without the signature of the drawer or the maker, the instrument shall not be a valid one.

7. **Delivery**

   Delivery of the instrument is essential. Any negotiable instrument like a cheque or a promissory note is not complete till it is delivered to its payee. For example, you may issue a cheque in your brother's name but it is not a negotiable instrument till it is given to your brother.

8. **Stamping-**

Stamping of Bills of Exchange and Promissory Notes is mandatory. This is required as per the Indian Stamp Act, 1899. The value of stamp depends upon the value of the pronote or bill and the time of their payment.

9. **Right to file suit**

The transferee of a negotiable instrument is entitled to file a suit in his own name for enforcing any right or claim on the basis of the instrument.

10. **Notice of transfer**

It is not necessary to give notice of transfer of a negotiable instrument to the party liable to

pay. 11. **Presumptions**

Certain presumptions apply to all negotiable instruments, for example consideration is presumed to have passed between the transferor and the transferee.

CLASSIFICATION OF NEGOTIABLE INSTRUMENT

- Bearer Instruments

To become payable to the bearer there are two significant conditions for negotiable instruments. Right off the bat, parties involved in such transaction should express such instruments to be so payable. Besides this, the bearer name shall be written clearly in the endorsement blank.

When these two pre-conditions are satisfied then this infers that any holder of such instruments can get paid for them. For instance, a bill of exchange is payable to any individual who holds it. These instruments incorporate checks, bills of exchange and promissory notes.

- Order Instruments

In some specific cases, negotiable instruments can regularly be payable to order. And it will be payable when the instruments explicitly declare them to be so. Moreover, they might be payable to order to a particular individual. The main necessity is that there ought to be no forbiddance on their transferability.

- Inland Instruments

Negotiable Instrument Act Section 11 talks about inland instruments. The provisions of Section 11 of NI's Act basically takes care of the instruments that are created and are payable in India. Alternately, if these instruments are drawn upon an India citizen they might be payable outside India.

- Foreign Instruments

Any negotiable instrument that is not an inland instrument is a foreign instrument. These negotiable instruments are made in a foreign nation, howsoever, they can be payable within India too. Moreover, foreign negotiable can be created in India to make the payment to the citizen residing abroad.

- Demand Instruments

Demand instruments are those negotiable instruments that are payable when the bearers demand it. Generally, demand instruments do not carry any due date or maturity period. Some of the common examples of demand instruments are bills of exchange and promissory notes.

- Time Instruments

Time instruments are those negotiable instruments that have fixed due date or maturity period. Once it achieves maturity period it becomes payable. Moreover, they can also be payable once a specific future event happens. One of the common examples of time instrument is promissory note having the maturity period of twenty-four months from the date of issue.

- Ambiguous Instruments

An ambiguous instrument is those negotiable instruments that can be either a bill or a note for its holder. Such circumstances emerge in unconventional conditions such as when the drawee of a negotiable instrument is a fictitious person or incompetent to contract.

The holder of such instruments may treat them either as bills of exchange or as promissory notes under such scenarios. Negotiable Instruments Act section 17 manages such kinds of scenarios.

- Incomplete instruments

The incomplete instrument is those instruments that miss out some of the basic prerequisites of typical negotiable instruments. Moreover, the holders of such incomplete instruments can complete it to the extent mentioned therein. In addition to this, the principal holder, as well as any resulting holder who obtains such instruments, can finish them. This, thus, results in the making of lawfully restricting negotiable instruments that are payable by law.

International Laws Pertaining to Negotiable Instruments

- Section 134 – Law governing the liability of the maker, acceptor, or endorser of a foreign instrument
- Section 135 – The Law of the place of payment governs dishonour
- Section 136 – An instrument made, drawn, accepted or endorsed outside India, but in accordance with the law of India
- Section 137 – Presumption as to Foreign Law

Section 134 – Law governing the liability of the maker, acceptor, or endorser of a foreign instrument

The liability of the maker or drawer of a foreign promissory note, cheque, or bill of exchange is subject to the laws of the place where he makes the instrument.

Further, the liabilities of the acceptor and/or endorser are subject to the laws of the place where the instrument is payable. Also, this rule holds true is there is no contract between the parties which states the contrary.

Section 135 – The Law of the place of payment governs dishonour Let's say that a promissory note, cheque, or bill of exchange is made payable in a different place from that in which it is made or endorsed.

In such cases, the law of the place where the negotiable instrument is payable determines the definition of dishonour. It also determines the rules pertaining to sufficient notice of dishonour.

Section 136 – An instrument made, drawn, accepted or endorsed outside India, but in accordance with the law of India

Let's say that a negotiable instrument is made, drawn, accepted or endorsed outside India. However, it is in accordance with the law of India.
Further, let's say that this instrument is invalid according to the law of the country where it was made. In such a circumstance, its subsequent acceptance or endorsement in India does not invalidate it.

Section 137 – Presumption as to Foreign Law

It is presumed that the law regarding negotiable instruments in any foreign country is the same as that of India. This is unless and until there is proof of the contrary.

A] PROMISSORY NOTE

"A promissory note is an instrument in writing (not being a bank-note or a currency-note) containing an unconditional undertaking, signed by the maker, to pay a certain sum of money only to, or to the order of, a certain person, or to the bearer of the instrument.." [Section 4]
Illustrations A signs instruments in the following terms:
(a) "I promise to Pay B or order Rs.500".
(b) "I acknowledge myself to be indebted to B in Rs.1,000, to be paid on demand, for value received."
(c) "Mr B I.O.U Rs.1,000."
(d) I promise to pay B Rs. 500 seven days after my marriage with C.
(e) I promise to pay B Rs.500/- on 01-10-2005.
(f) "I promise to pay B Rs. 500 and all other sums which shall be due to him." (g) "I promise to pay B Rs. 500 first deducting thereout any money which he may owe me."

The instruments respectively marked (a), (b) and (e) are promissory notes. The instruments respectively marked (c), (d), (f) and (g) are not promissory notes.

The essentials of a valid Promissory note are :-

1. Writing –
A Promissory note must be in writing.

2. Express promise to Pay –
The promissory note must contain an express promise to pay. A mere implied promise to pay or an acknowledgement of debt is not a promissory note. Therefore illustrations at (c) is not a Promissory note.

3. Promise to pay unconditional –
The promise to pay an amount must be unconditional. However, a Promissory note conditional on an event bound to happen is a valid promissory note. Therefore illustrations at (d) is not a valid Promissory note while (e) is a valid Promissory note.

4. Promise to pay in terms of money –
The instrument must be payable in terms of money and money only.

5. Sum payable to be certain –
The amount payable must be certain. Therefore instrument at (f) and (g) are not valid promissory note.

6. Parties certain –
The parties to the instrument must be certain. The person making the payment and the person receiving the payment must be identifiable.

7. Must be signed –
The instrument is complete only when it is signed by the maker.

8. Must bear the stamp –
A promissory note must be properly stamped in accordance with the Indian Stamp Act, 1899 and must also be properly cancelled.

9. Other formalities –
Formalities such as date, place, consideration, etc. are usally found in a promissory note.

10. Requisites of a contract to be complied with –
All requisites of a valid contract like capacity to contract, consideration, free consent, lawful object must be present.

B] BILL OF EXCHANGE

As per Section 5 a "bill of exchange" is "an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument."

The essentials of a Bill of Exchange are :-

1. Number of parties -
A bill of exchange has 3 parties – a) the drawer, who draws the bill of exchange b) the drawee, who has to make the payment c) the payee, who is entitled to the payment. Sometimes the drawer and the payee can be one and the same person.

2. Must be writing –

The Bill of Exchange must be in writing. 3. Express order to pay – This is the essence of a bill of exchange. There must be an 'order by the drawer to the drawee to pay'. The order must be a command and not an excessive request.

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5. Order to pay money only –
Just as a promissory note, the instrument must be for money only.

6. Sum payable to be certain –
The amount payable must be certain. There should be no ambiguity in the amount to be paid through the Bill of Exchange.

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contract to be complied with –

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Types of Bill of Exchange

- **Documentary Bill-** In this, the bill of exchange is supported by the relevant documents that confirm the genuineness of sale or transaction that took place between the seller and buyer.
- **Demand Bill-** This bill is payable when it demanded. The bill does not have a fixed date of payment, therefore, the bill has to be cleared whenever presented. ● **Usance Bill-** It is a time-bound bill which means the payment has to be made within the given time period and time.
- **Inland Bill-** An Inland bill is payable only in one country and not in any other foreign country. This bill is opposite to foreign bill.
- **Clean Bill-** This bill does not have any proof of a document, so the interest is comparatively higher than the other bills.
- **Foreign Bill-** A bill that can be paid outside India is termed as a foreign bill. Two examples of a foreign bill are an export bill and import bill.
- **Accommodation Bill-** A bill that is sponsored, drawn, accepted without any condition is known as an accommodation bill.
- **Trade Bill-** This kind of bill is specially related only to trade.
- **Supply Bill-** The bill that is withdrawn by the supplier or contractor from the government department is known as the supply bill.

Acceptance for honour supra protest.

Where a bill of exchange has been protested for dishonour by non-acceptance, or protested for better security, and is not overdue, any person, not being a party already liable thereon, may, with the consent of the holder, intervene and accept the bill supra protest, for the honour of any party liable thereon, or for the honour of the person for whose account the bill is drawn.

A bill may be accepted for honour for part only of the sum for which it is drawn. An acceptance for honour supra protest in order to be valid must—

be written on the bill, and indicate that it is an acceptance for honour:
be signed by the acceptor for honour.

Where an acceptance for honour does not expressly state for whose honour it is made, it is deemed to be an acceptance for the honour of the drawer.

Where a bill payable after sight is accepted for honour, its maturity is calculated from the date of the noting for non-acceptance, and not from the date of the acceptance for honour.

Payment for honour supra protest.

Where a bill has been protested for non-payment, any person may intervene and pay it supra protest for the honour of any party liable thereon, or for the honour of the person for whose account the bill is drawn.

Where two or more persons offer to pay a bill for the honour of different parties, the person whose payment will discharge most parties to the bill shall have the preference. Payment for honour supra protest, in order to operate as such and not as a mere voluntary payment, must be attested by a notarial act of honour which may be appended to the protest or form an extension of it.

The notarial act of honour must be founded on a declaration made by the payer for honour, or his agent in that behalf, declaring his intention to pay the bill for honour, and for whose honour he pays.

Where a bill has been paid for honour, all parties subsequent to the party for whose honour it is paid are discharged, but the payer for honour is subrogated for, and succeeds to both the rights and duties of, the holder as regards the party for whose honour he pays, and all parties liable to that party.

The payer for honour on paying to the holder the amount of the bill and the notarial expenses incidental to its dishonour is entitled to receive both the bill itself and the protest. If the holder do not on demand deliver them up he shall be liable to the payer for honour in damages.

Where the holder of a bill refuses to receive payment supra protest he shall lose his right of recourse against any party who would have been discharged by such payment.

Key Differences between Bill of Exchange and Promissory note represented in a comparison format are as follows

Bill of Exchange	**Promissory Note**
Definition	
A negotiable instrument issued to order the debtor to pay the creditor a certain sum of money within a specific date or on demand.	A negotiable instrument issued by the debtor with a written promise to pay the creditor a certain amount within a specific date or on demand.
Section	
Mentioned in Section 5 of the Negotiable Instruments Act, 1881	Mentioned in Section 4 of the Negotiable Instruments Act, 1881

Issued By	
Creditor	Debtor
Parties Involved	
Three parties involved i.e a drawer, the drawee and a payee.	Two parties involved i.e a drawer/maker and the payee
Acceptance	
Drawee needs to accept the bill of exchange before payment.	No acceptance required from the drawee.
Liability	
Liability of drawer is secondary and conditional.	Liability of drawer is primary and absolute.
Dishonouring of instrument	
Notice served to all the concerned parties involved in the transaction on dishonouring the instrument.	No notice served to the drawer in case of dishonouring the instrument.
Copies	
Bill of exchange can have copies.	The promissory note allows no copies.

Is it Payable to drawer/maker	
Yes, the same person can be drawer and payee.	The same person cannot be drawer and payee.

Meaning of a Cheque

Section 6 of the Negotiable Instruments Act defines what a 'cheque' means. According to this provision, a cheque is basically a bill of exchange drawn on a specific banker. Furthermore, it is not payable otherwise than on demand.

The Negotiable Instruments (Amendment) Act had amended this definition to make it broader in 2015. Accordingly, cheques now include the electronic image of a truncated cheque and also an electronic cheque. Despite this amendment, the basic definition still remains the same.

Features of a Cheque

1. **It must be in writing:** A cheque must be in writing. An oral order to pay does not constitute a cheque.
2. **It should be drawn on banker:** It is always drawn on a specified banker. A cheque can be drawn on a bank where the drawer has an account, saving bank, or current.

3. **It contains an unconditional order to pay:** A cheque cannot be drawn so as to be payable conditionally. The drawer's order to the drawee bank must be unconditional and should not make the cheque payable dependent on a contingency. A conditional cheque shall be invalid.

4. **The check must have an order to pay a certain sum:** The cheque should contain an order to pay a certain sum of money only. If a cheque is drawn to do something in addition to, or other than to pay money, it cannot be a cheque. For example, if a cheque contains '*Pay USD 500 and a TV worth USD 500 to A*' it is not a cheque.

5. **It should be signed by the drawer and should be dated:** A cheque does not carry any validity unless signed by the original drawer. It should be dated as well.

6. **It is payable on demand:** A cheque is always payable on demand.

7. **Validity:** A cheque is normally valid for six months from the date it bears. Thereafter it is termed as stale cheque. A post-dated or antedated cheque will not be invalid. In both cases, the validity of the cheque is presumed to commence from the date mentioned on it.

8. **It may be payable to the drawer himself:** Cheques may be payable to the drawer himself/herself. It may be drawn payable to bearer on demand unlike a bill or a pro-note.

9. **Banker is liable only to the drawer:** The banker on whom the cheque is drawn shall be liable only to the drawer. A holder or bearer has no remedy against the banker if a cheque is dishonored.

10. **It does not require acceptance and stamp:** Unlike a bill of exchange, a cheque does not require acceptance on part of the drawee. There is, however, a custom among banks to mark cheques as 'good' for the purpose of clearance. But this marking is not an acceptance. Similarly, no revenue stamp is required to be affixed on cheques.

TYPES OF CHEQUES

There are various types of cheques that can be issued. Given below is the list of the various cheque types:

1. Bearer Cheque
2. Order Cheque
3. Crossed Cheque
4. Account Payee Cheque
5. Post Dated Cheque
6. Self Cheque
7. Traveler's Cheque
8. Blank Cheque

Bearer Cheque

The bearer cheque is a type of cheque in which the bearer is authorised to get the cheque encashed. This means the person who carries the cheque to the bank has the authority to ask the bank for encashment.

Order Cheque

This type of cheque cannot be endorsed, i.e., only the payee, whose name has been mentioned in the cheque is liable to get cash for that amount. The drawer needs to strike the "OR BEARER" mark as mentioned on the cheque so that the cheque can only be encashed to the payee.

Crossed Cheque

In this type of cheque, no cash withdrawal can be done. The amount can only be transferred from the drawer's account to the payee's account. Any third party can visit the bank to submit the cheque.

In case of a crossed cheque, the drawer must draw two lines at the left top corner of the cheque.

Account Payee Cheque

This is the same as the account payee cheque but no third party involvement is required. The amount shall be transferred directly to the payee's account number.

Post Dated Cheque

If a drawer wants the payee to apply for withdrawal or transfer of money after the present date, then he/she can fill a post dated cheque.

Self Cheque

If the drawer wishes cash for himself he can issue a cheque where in place of the Payee's name he can write "SELF" and get encashment from the branch where he owns an account.

Traveller's Cheque

As the name suggests, the Traveler's cheque can be used when a person is travelling abroad where the Indian currency is not used.

If a person is travelling abroad, he can carry the traveller's cheque and get encashment for the same in abroad countries.

Blank Cheque

When a cheque only has a drawer's signature and all the other fields are left empty, then such a type of a cheque is called a blank cheque.

Difference between cheque and bill of exchange

Cheque	Bill of Exchange
Meaning	
The Cheque is a document which contains an order to a bank to pay fixed amount of money from the account of the client	A bill of exchange is a negotiable instrument which orders to drawee to pay a fixed amount of money to payee on demand
Existence	
A cheque exists in section 6 of the Negotiable Instruments Act, 1881.	A bill of exchange exists in section 5 of the negotiable instruments act, 1881.
Grace period	
A cheque has no grace period once it is presented for the payment.	A bill of exchange has three days of grace period.
Approved	
A Cheque does not need any approval from the parties before presented for payment.	A bill of exchange needs an approval from the drawee for the payment.
Validity	
A cheque has a validity of 3 months.	A bill of exchange has no validity for the payment.
Liability	

Parties remain liable to pay also in case notice of dishonour is not given.	In the bill of exchange, the parties who do not get notice of dishonour are free from the liability of paying.
Notice of Dishonour	
In cheque, notice of dishonour is not compulsory.	In a bill of exchange, notice of dishonour is mandatory.

CRIMINAL PENALTIES IN CASE OF DISHONOUR OF A CHEQUE

Under Section 138 –

Where any cheque drawn by a person on an account maintained by him with a banker for payment of any amount of money to another person from out of that account for the discharge, in whole or part, of any debt or other liability, is returned by the bank unpaid, either because of the amount of money standing to the credit of that account is insufficient to honour the cheque or that it exceeds the amount arranged to be paid from that account by an agreement made with that bank, such person shall be deemed to have committed an offence and shall, without prejudice to any other provision of this Act be punished with imprisonment [a term may be extended to 2 years], or with fine which may extend to twice the amount of the cheque, or with both.

- **Dishonour due to insufficient fund**

It is also necessary that the cheque should be returned by the bank unpaid. Dishonour may

be because of 2 reasons:

1. *Either the amount of money present in the account is insufficient*
2. *Or the amount to be paid has exceeded the amount to be paid from that account as in the agreement made with that bank.*

It has been generally held in various cases that dishonour due to the insufficiency of funds has to be interpreted liberally. Dishonour due to the remarks like "Account closed", "Refer to the drawer" or "Stop payment" of the cheque may be deemed to be covered by the provision contained in Section 138 of the Act.