3 (A) Kinds and Characteristics of Negotiable Instrument

Subject : Commerce

Lesson : Kinds and Characteristics of Negotiable Instrument

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3 (A) Kinds and Characteristics of Negotiable Instrument

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Chapter 3 (A) Kinds and Characteristics of Negotiable Instrument

Introduction

The earliest foundation of trade was set when man realized the need for goods and services, which he could not produce on his own. He felt the desire to possess the things available with someone else and that let to idea of exchanging goods and services. This exchange of goods and services is known as trade. In the past, goods were exchanged according to barter system whereby people exchanged goods and services as a consideration for trade.

This had several limitations among which equality of value was the most predominant, which was overcome by the introduction of money where all the goods and services were valued in terms of money, and traders materialized their transactions through payment of money. As the volume and scale of transactions increased, money couldn't remain the only medium of exchange and need for supplements of money was felt as it became both inconvenient and risky to carry out all transactions in cash. This led to the emergence of a third category of medium of exchange such as bills of exchange, cheques, bank drafts, hundis etc. collectively grouped as negotiable instruments. A negotiable instrument is a written document, which entitles a person to a certain sum of money, which can be transferred from one person to another by delivery or by endorsement and delivery. The introduction of negotiable instruments made business transactions much easier. It is no longer required to execute each and every transaction in cash. The Negotiable Instruments Act, 1881 seeks to regulate the dealings in such instruments, it aims to legalise the system under which negotiable instruments pass from hand to hand in negotiation like ordinary goods.

3 (A) Kinds and Characteristics of Negotiable Instrument

The scope of the Unit is given below:

20.1 Meaning and Definition of Negotiable Instruments
20.2 Characteristics of Negotiable Instruments
20.3 Presumptions About Negotiable Instruments
20.4 Relevant Provisions of RBI Act, 1934
20.5 Kinds of Negotiable Instruments
20.6 Promissory Note
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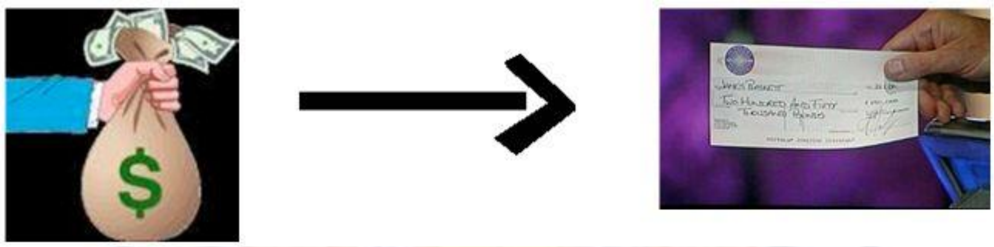

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20.1 Meaning and Definition of Negotiable Instrument

The meaning and definition of negotiable instruments are discussed below:

20.1.1 Meaning

The word " negotiable" means "transferable from one person to another by mere delivery or by endorsement and delivery, in return for consideration, and " instrument" means a written document creating a right in favor of some person, which may be a duty for another". Therefore a 'negotiable instrument' is

Figure 20.1 Negotiable Instrument

a. A written document
b. Signed by the maker or drawer of the instrument
c. That contains an unconditional promise or order to pay
d. A fixed amount of money (with or without interest which may be a specified amount or at a specified rate)
e. Payable on demand or at a specified exact future date
f. To a specific person or to order or to its bearer

Illustration
Ganesh a rice dealer sells rice worth Rs. 100,000 to Shyam for four months and he writes an order addressed to Shyam that Shyam has to pay after four months Rs 100,000, to Ganesh or anyone holding the order and presenting it. The order has to be signed by Shyam which shows his acceptance to pay. And Ganesh can hold the order for four months and place it before Shyam for collection of money on due date.

Therefore, a negotiable instrument must fulfill the following conditions:

a. The document must be freely transferable, either by delivery (when it is payable to the bearer of the document), or by endorsement and delivery (when the document is payable to order).

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Illustration
If we continue with the previous illustration only, where the instrument was with Ganesh for receiving payment from Shyam. Ganesh can use the same to carry on other transactions. For example if he requires money after fifteen days he can borrow it from Ajeet and pass the order documen to Ajeet. For this he has to give instructions on the back of the document to Shyam to make a payment to Ajeet. Thereafter Ajeet becomes the owner of the signed document and he can claim money from Shyam on the due date.

b. Even if the title of the Transferor is defective the transferee, taking the instrument in good faith and for consideration, gets a good title to it.

Illustration
Kartik writes a negotiable instrument in favour of Chariter, but before the due date it is stolen by Shakti who passes it to Geeta for consideration, by endorsing it to her (he forges Chariter's signatures on the document). Geeta accepts the document in good faith, and for value. Now, on due date Geeta holds a good title to the instrument, even if Shakti's title is defective.

c. The party holding the instrument should be entitled to maintain a suit thereon, in case, the instrument gets dishonored while in his custody.

Figure 20.2 Bona Fide Holder

Illustration
Tinu writes a negotiable instrument in favor of Jai and later doesn't pay him on due date. Jai can sue Tinu in court of law for payment.

20.1.2. Definition of Negotiable Instrument

The term negotiable instrument is not adequately defined in the Negotiable Instruments Act. Some of the definitions given below throw light on various aspects of a negotiable instrument.

Justice Willis: "A negotiable instrument is the one, the property in which is acquired by anyone, who takes it bona fide, and for value, notwithstanding any defect of title in the person from whom he took it."[53]

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

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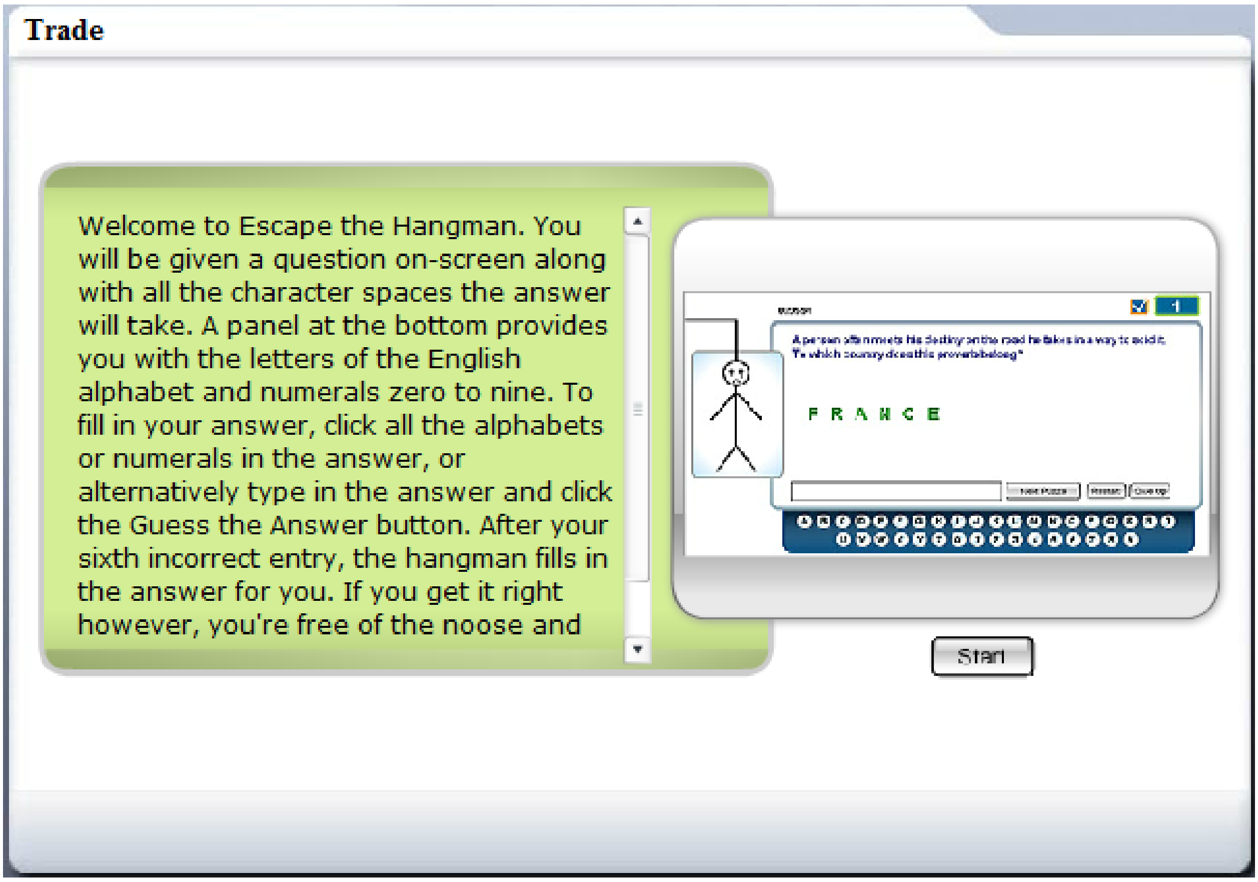
Though the act states these three as negotiable instruments, some other instruments are also acceptable as a custom of trade or under some other acts like hundis, share warrants, drafts, bearer bonds etc.

Check Your Progress



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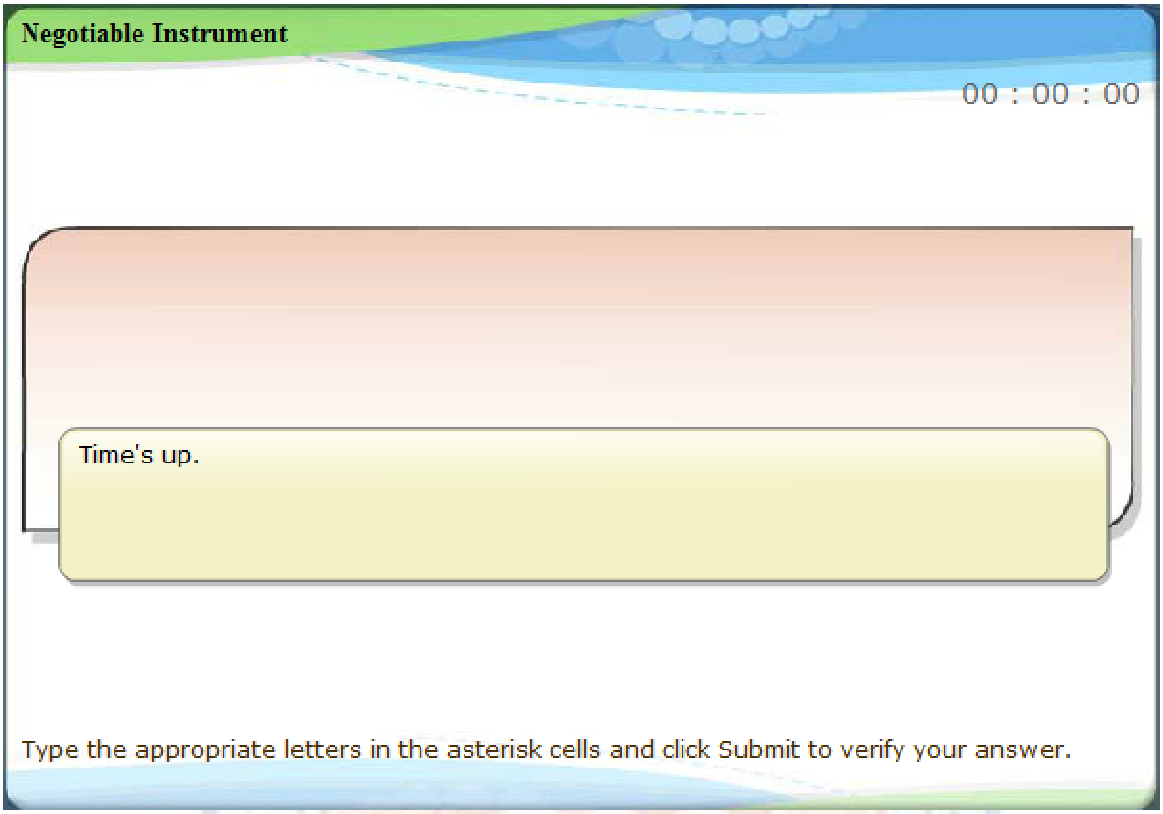

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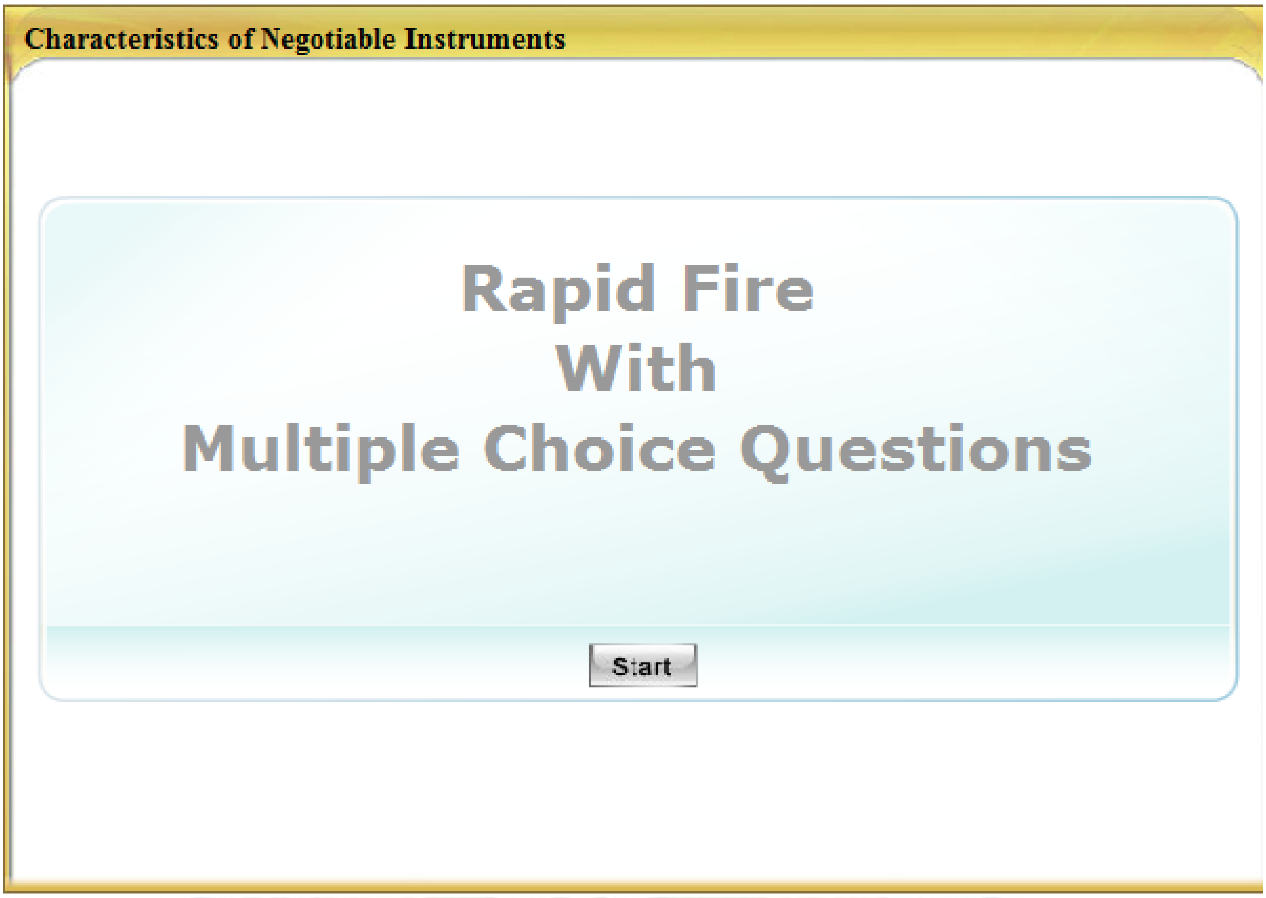

20.2 Characterstics of Negotiable Instruments

The characteristics of negotiable instruments may be described as follows:

1. Writing and Signed by Its Maker: A negotiable instrument being an instrument, must be in writing and signed by its maker. Therefore an oral promise to pay certain sum at a future date with out any written document is not enforceable in the eyes of law. Similarly, if the maker does not sign the instrument, it is not a valid negotiable instrument.

Figure 20.3 Writing of Negotiable Instrument

2 Unconditional: A negotiable instrument contains an unconditional promise or order to pay some money. Therefore if payment of money is conditional to the completion of some condition, then, it is not a valid negotiable instrument.

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Illustration
If Ajay writes a negotiable instrument to pay Rs. 5000 to Garjun subject to the condition that Garjun stands first in the exam, then it is not a valid negotiable instrument as it is not unconditional.

3 Fixed Sum of Money: A negotiable instrument is a promise to pay a fixed sum of money only, which may include interest at a fixed rate. Any promise to pay an uncertain sum will not make a valid negotiable instrument.

Illustration
Sharda makes a negotiable instrument in favor of Alok, to pay whatever dues she has to pay him; in this case, it is not a valid instrument as the amount payable is not mentioned.

4 Transferable: A negotiable instrument is transferable easily from one person to another any number of times. The instrument is freely transferable, either by delivery when it is payable to the bearer of the document, or by endorsement and delivery when the document is payable to order. Transferability is an essential feature of negotiable instruments, but all transferable instruments are not negotiable instruments.

5 Absolute And Good Title: The transferee of a negotiable instrument who receives it in good faith and for value gets the instrument free from all defects. He gets an absolute and good title, irrespective of any defect in the title of the transferor.

Illustration
Jack gets a negotiable instrument drawn in his favor by Gaurav by way of using coercion and later endorses it in favor of Chetan for value, and Chetan accepts the same in good faith. Here, though the title of Jack is defective yet Chetan gets a good title to the instrumet, and can receive payment from Gaurav.

6 Right to Recovery: The transferee has a right to recovery, i.e., he can sue on the instrument in his own name to enforce his rights. Moreover he need not give any notice of transfer to the party liable on the instrument.

Illustration
Padma receives a negotiable instrument drawn in her favor from Rajesh. She endorses it to Jatin who further endorses it in favor of Hiten. Rajesh refuses to pay Hiten stating that Padma did not inform him about endorsements. Hiten can sue Rajesh for recovery in his own name. There is no obligation to inform Rajesh.

7 The operations regarding the negotiable instruments are based on certain presumptions, unless the contrary is proved. These presumptions are discussed below.

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20.3 Presumptions about Negotiable Instruments

Section 118 and 119 of the negotiable Instrument Act provide the following presumptions, which are applicable to all negotiable instruments unless something to the contrary is proved.

1 Consideration: It is presumed that every negotiable instrument has been made or drawn or accepted or endorsed or negotiated or transferred for consideration. This holds both for the original parties, as well as, for subsequent parties.

2 Date: In case a negotiable instrument bears a date, it is presumed that it was drawn on the date which appears on it.

3 Time of Acceptance: In case of a Bill of Exchange, it is presumed that it was accepted within a reasonable time after its date and before its maturity.

4 Time of Transfer: It is presumed that every transfer of a negotiable instrument was made before its date of maturity.

5 Order of Endorsements: It is presumed that the endorsements appearing on a negotiable instrument have been made in the order in which they appear on the instrument.

6 Stamp: Unless the contrary is proved, it is presumed that a lost negotiable instrument was duly stamped.

7 Holder in Due Course: It is presumed that every holder of the instrument is a 'holder in due course'.[54]

20.4 Relevant Provisions of Reserve Bank of India Act 1934

At this stage it is essential to understand the importance of R.B.I Act, particularly section 31 of the Act, which clearly proves the supremacy of the Central Government over the issue of national currency. The said section states that:

Figure 20.4 RBI

Provided that cheques or drafts, including hundis payable to bearer on demand or otherwise, may be drawn on a person's account with a banker, shroff or agent.

- This means that a bill of exchange or hundi cannot originally be made payable to 'bearer on demand'. It may be a 'time' bill payable to bearer or order; as a 'demand' bill payable to order. However, a cheque payable to bearer on demand can be drawn on person's account with a banker.

(2) Notwithstanding anything contained in the Negotiable Instrument Act, 1881 (26 of 1881), no person in India other than the Bank, or, as expressly authorised by the Reserve Bank of India Act, the Central Government, shall make or issue any promissory note expressed to be payable to the bearer of the instrument.

- A promissory note cannot be originally made payable to bearer.

The above provisions do not apply to an order instrument which becomes payable to bearer by an endorsement in blank.

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RBI Acts

T	B	C	H	E	Q	U	J
H	A	S	H	C	B	A	A
U	N	B	H	E	N	D	S
N	B	B	E	T	Q	A	S
D	R	A	F	T	S	U	I
I	A	N	U	T	R	D	E
S	S	K	R	A	V	I	J
W	A	R	R	A	N	T	S

Words to be found:

1. DRAFTS
2. HUNDIS
3. CHEQUE
4. BANK
5. WARRANTS

Set Word Give Up

Click the first and the last letters of the word and then click Set Word button to confirm it.

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20.5 Kinds of Negotiable Instruments

There are many kinds of negotiable instruments, but the Act has considered only three namely a promissory note, bill of exchange and cheque. Apart from these three, any document which fulfills the requirements of a negotiable instrument is recognized by the custom or usage or some other Act as negotiable instrument. These include hundis, treasury bills, banker's drafts and pay orders, share warrants, dividend warrants, bearer debentures, Government Promissory Notes are considered as negotiable instruments as a usage or custom of trade or Companies Act. Further, Sec 137 of Transfer of Property Act also recognizes the negotiability of instruments 'by law or custom'.[55]

20.6 Promissory Note

A promissory note "is an unconditional promise in writing made by one person (maker) to another person(payee), signed by the maker, engaging to pay, on demand or at a fixed or determinable future time, a sum certain in money to, or to the order of, a specified person or to the bearer".

Figure 20.5 Promissory Note

Illustration
Suppose Rahul takes a loan of Rupees Twenty lakh from Hardik. Rahul makes a document stating that he will pay the money to Hardik or to the the bearer of the document after three months. Further endorsements can be made until Rahul makes the final payment to the presenter of the promisee note.

Illustration
Mithit purchased 100 meters of cloth worth Rs.40,000 from his supplier Vineet, he could not pay the amount immediately so he made a document stating that he will pay Rs.40,000 after 2 months to Vineet or the bearer on demand. He signed and stamped the document. This document becomes a promissory note. After 2 months Mithit is under the obligation to pay the amount mentioned on the promissory note (Rs.40,000) to Vineet or to anybody authorized by Vineet through endorsement on the promissory note.

Section 4 of the Negotiable Instruments Act, 1881 defines promissory note as "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".

Note:- Bank notes and currency notes **do not** come under the category of promissory notes (as they are expressly excluded from the definition). Further, the words 'or to the bearer' are redundant by virtue of the provisions of sec.31 of RBI Act, the same has been discussed in 20.5 above.

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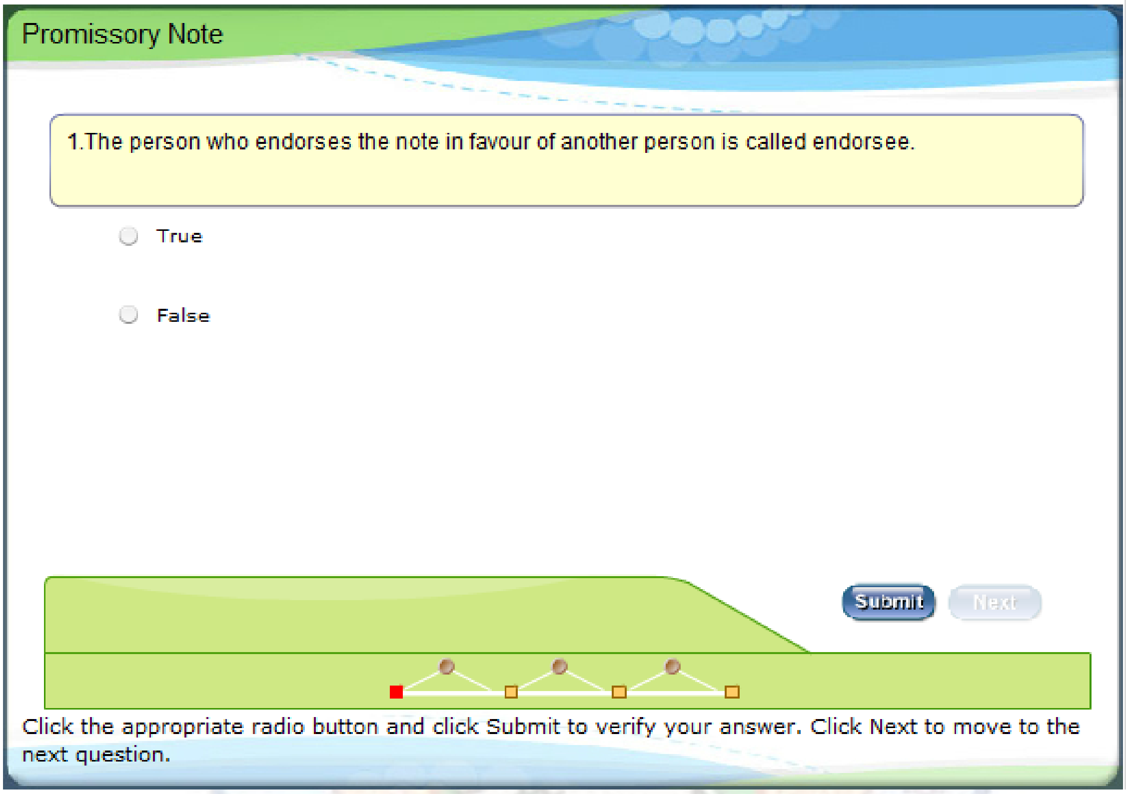

20.6.1 Parties to a Promissory Note

The following is a specimen of a valid promissory note.

The Promissory note involves two parties. They are the Maker and the Payee

i. the maker or drawer is a person who prepares the note and promises to pay the amount written on the note. In the above specimen, Mandeep is the maker or drawer.

ii. **T**he Payee is the person to whom the amount is payable. In the above specimen it is Roshan Lal.

a. In the above specimen when Roshan Lal endorses the note in favour of Ranjeet and Ranjeet consequently endorses it in favour of Jaiveer, then Roshan Lal and Ranjeet both will become endorsers.

b. An Endorsee is a person in whose favour the note is negotiated. In the above specimen the endorsee is Ranjeet and Jaiveer.

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20.6.2 Features of Primissory Note

The features of a promissory note are discussed below:

1. A promissory note must be in ***writing. It must be duly signed*** by its maker and properly ***stamped*** as per the Indian Stamp Act, 1899, and each stamp must be duly cancelled. Therefore an oral promise may be a valid contract, but cannot be considered a valid promissory note. Writing may be in ink or pencil or a typewritten note. Similarly, mere writing in own hand is not sufficient, the signature of the maker must be there, if the maker is illiterate, then his

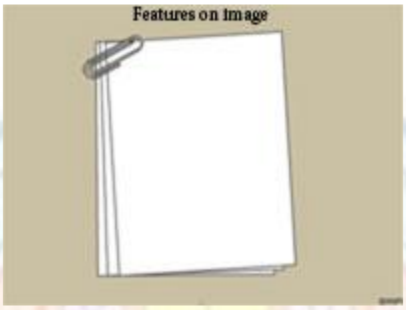

Figure 20.6 Features of Promissory Note

thumb impression must be there to constitute a valid promissory note. It must be noted that an agent of a trading firm can sign a promissory note on its behalf.

Illustration
Shyam writes on a paper "Mohan I promise to pay you Rs. 3000". Does this constitute a valid promissory note? Ans. No, because shyam has not signed the note.

2 It must contain an **undertaking, or express and clear promise to pay**. Mere acknowledgement of indebtedness will not constitute a promissory note. Therefore, an IOU document is not a promissory note.[56]

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Illustration
Illustration: Rohan draws the following note 14/10/2008 Haridwar I am bound to pay Rs. 8000 to Karim, which I received from him. To karim sd/- Rohan Stamp

Is it a valid promissory note?

Ans. No, because there is no express promise to pay. It is an acknowledgement of debt.

A receipt, mentioning terms and conditions on which money has been borrowed, will not be a promissory note. It would be treated as an acknowledgement of debt. If the receipt is accompanied with a promise to pay, it is a promissory note. The main element in determining, whether, an instrument is a promissory note or not, is the intention of parties in drawing up that instrument as a promissory note. A receipt, even if coupled with a promise to pay, was held not to be a promissory note, as it was not intended to be a promissory note.[57]

Case law 1 **In Surjit Singh v. Ram Rattan** **A..IR (1975), Gau. 15**
In Surjit Singh v. Ram Rattan the instrument read- "I have received a sum of Rs. 9,000 from R.R.Shrma. This amount will be repaid on demand. I have received this amount in cash." It was held to be a promissory note as there was a clear promise to pay.[222]

3 The promise must be definite and unconditional. If the promise is uncertain or conditional to the happening of an uncertain event, then the instrument is invalid.

Illustration
Amit writes a promissory note "I promise to pay Ramu Rs. 40,000 on Girish's death, provided Girish leaves me enough amount to pay to Ramu in his will." Is this a promissory note? Ans. No, as the promise is contingent upon the happening of an uncertain event, Girish leaving enough money for Amit. It cannot be a valid promissory note.

However, if the promise to pay is subject to a normal condition, then it doesn't make the instrument invalid. Moreover, a note, promising to pay at a particular place or after a specified time, is not conditional, and hence valid.

In the above illustration if Amit writes a promissory note "I promise to pay Ramu Rs. 40,000 at India Gate, Delhi on Girish's death," then it is a valid instrument.

4 It must posess a promise to **pay legal tender money** only. If the instrument promises to pay something else other than money, then it will not be a valid promissory note. The following notes signed by Harish are not valid promissory notes

1. 'I promise to pay to Jatin Rs. 20,000 and deliver my Santro car to him on next 23 January.[rd]
2. I promise to pay to Jatin in form of 40 Shares of a XY Ltd. company and 20 units of a Mutual Fund.
3. I promise to deliver 20 crates of soft drink to Jatin.
4. I promise to deliver an air ticket to France to Jatin.

5 The **sum payable** that is written on the note should be **certain, or capable of being made certain.** The sum payable should be in figures. It must not be capable of contingent additions and subtractions. However, sec 5 para 3 of the act states, where the determination of the amount is to be based on some interest calculation or an exchange rate or that the payment would be in instalments, the promissory note would be valid.

Illustration
The following notes are invalid in this respect: • I promise to pay to Karan Rs.9,000, after reducing any amount that he owes to me till 31st January next. • I promise to pay to Kartik RS.9,000 and any fine and financial charges according to rules.

Illustration
Cheenu signed a note stating, 'I promise to pay Shalu Rs.10,000 in 10 monthly instalments of Rs. 100 each on the first of every month. If I default in payment of any instalment on the due date, the whole balance unpaid shall become due.' Is this a valid promissory note in the current context? Ans. Yes, it is valid as there is no uncertainty regarding the amount payable.

Illustration
Kartik sign a note, 'I promise to pay to Tanvi Rs. 20,000 along with simple interest @ 12% per annum.' Is this a valid promissory note? Ans. Yes, interest calculation does not make the amount uncertain.

6 The maker and the payee that are the parties to a promissory note, must be certain. They must be identified in the instrument itself. The parties may be identified by name or by designation e.g. manager of a bank or director of a company. If the payee is misnamed or designated by description only, in such case, the note is valid if the payee can be ascertained by evidence.[58]

If there are joint makers of a note, their nature of liability should be clear-joint or several or both. However, if they bind them alternatively for, e.g., a note signed by two persons as: Dinesh or Pankaj, then this is not allowed, and only the first signatory, i.e., Dinesh shall be liable.

7 A promissory note is **payable on demand, or after a certain date.** For instance 'three months after date I promise to pay Saroj or order a sum of rupees Ten Thousand only' it is a promissory note. Payable on demand means payable immediately or forthwith.

8 There may be other formalities, like **number, place, consideration,** etc., are usually found in an instrument, although they are not essential in law. The omission, of such information, does not invalidate the instrument.

20.7 Bill of Exchange

A bill of exchange is an order in writing directing a person to pay a sum of money to a specified person.

Section 5 of the Negotiable Instruments Act, 1881 defines a bill of exchange as "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"

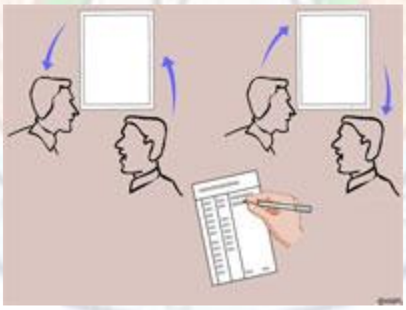

Figure 20.7 Bill of exchange

Illustration
Rishit gives a loan of Rupees Thirty Thousand to Govind. Rishit also has to give some money to Sanjeev. Rishit further makes a document (Bill of exchange) in which he directs Govind to make payment of up to Rupees Thirty Thousand to Sanjeev on demand, or after expiry of a specified period.

Acceptance of a bill of exchange by the drawee must be in writing only, it may be by simply putting up signatures on the bill or writing words such as 'accepted' on the bill and signing the bill.

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20.7.1 Parties to a Bill of Exchange

The following is a specimen of a bill of exchange:

Rs.50,000 Jaipur, October 21, 2008

Three months after date, pay to Girish or order the sum of Rs. Fifty thousand only, for value received.

stamp
Maneet

To Tarun *Accepted*

sd/-

15, West avenue, Punjabi Bagh, New Delhi Tarun

The above bill is drawn by Maneet, who is ordering Tarun to pay Rs. 50,000 to Girish (to whom he is indebted for the same amount), in lieu of goods delivered by Maneet to Tarun.

There are three parties involved in a bill of exchange. They are:

1. **The Drawer –** In the above specimen it is Maneet who is the drawer who is the maker of the bill.
2. **The Drawee –** Tarun in the given specimen is the drawee, to whom the bill of exchange is addressed. when he accepts the bill he becomes the 'acceptor' and is liable on it.
3. **The Payee –** In the given specimen it is Girish who is the payee and to whom the payment is to be made.
4. **Drawee in case of need-** Drawee in case of need is resorted to only when the bill is dishonored by non-acceptance or non-payment. He is the person who is refered to only in cases of need.

20.7.2 Features of a Bill of Exchange

Although a bill of exchange and a promissory note are different in form, the essential requirements are more or less the same.

1 As per Indian Stamp Act "a bill must be in **writing, duly signed by its drawer, accepted by its drawee and properly stamped.** It must contain an **express order to pay**. The only difference between a promissory note and a bill of exchange is that the maker of a note pays the payee personally, rather than ordering a third party to do so". Moreover, a mere request or reminder to pay money is not bill of exchange.

Illustration
A bill of exchange states ' Mr. Raj please pay to Gita or order Rs. 9,000 and oblige. Is it a valid bill of exchange? Ans. Yes it is valid as there is an order to pay made in a polite language.

Illustration
A bill of exchange states 'Mr. Raj please let Gita have Rs. 9,000 and oblige. Is it a valid bill of exchange?

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Ans. No, it is not a bill of exchange as it contains only a request not an order to pay.

3 The order must be definite and unconditional.

4 It must contain an order to pay in terms of legal tender money only.

5 The order must be to pay a definite sum of money.

6 The parties to a bill must be certain.

7 The formalities relating to number, date, place and consideration, though usually found on a bill, are not necessary in law, and hence their omission does not have any effect on its validity.

- Note- A bill of exchange can be originally be drawn as 'payable to the bearer' but then it cannot be simultaneously be made 'payable on demand' to comply with Sec.31 of R.B.I Act, 1934. Hence, there can be no bill payable to bearer on demand. But there can be a bill payable on demand to a payee.

- A bill which is not expressly made to be payable on demand is entitled to three days of grace with respect to date of maturity.

Illustration
A Bill of Exchange dated 12th July 2008 was payable 2 moths after date, it would mature for payment on 14th September 2008.

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20.8 Cheque

Cheque is one of the forms of negotiable instrument. One can issue cheques in his/her own name or in favour of others, directing the bank to pay the amount specified on the cheque to the person named on the cheque.

The Negotiable Instruments Act, 1881 defines a cheque as **"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 electronic form."**

20.8.1 Parties to a cheque

i. **The Drawer –** The person who draws the cheque. He is the maker of the cheque. In the specimen it is Mrs. Singh.

ii. The on whom the cheque is drawn and who is directed by the maker to make the payment of the amount mentioned on the cheque. In the specimen cheque it is BSBO bank. **The Drawee – banker**

iii. **The Payee –** The person to whom the payment is to be made. In the specimen cheque it is Mr. Rishit

iv. The drawer can be the payee also, if he draws a cheque payable to self.

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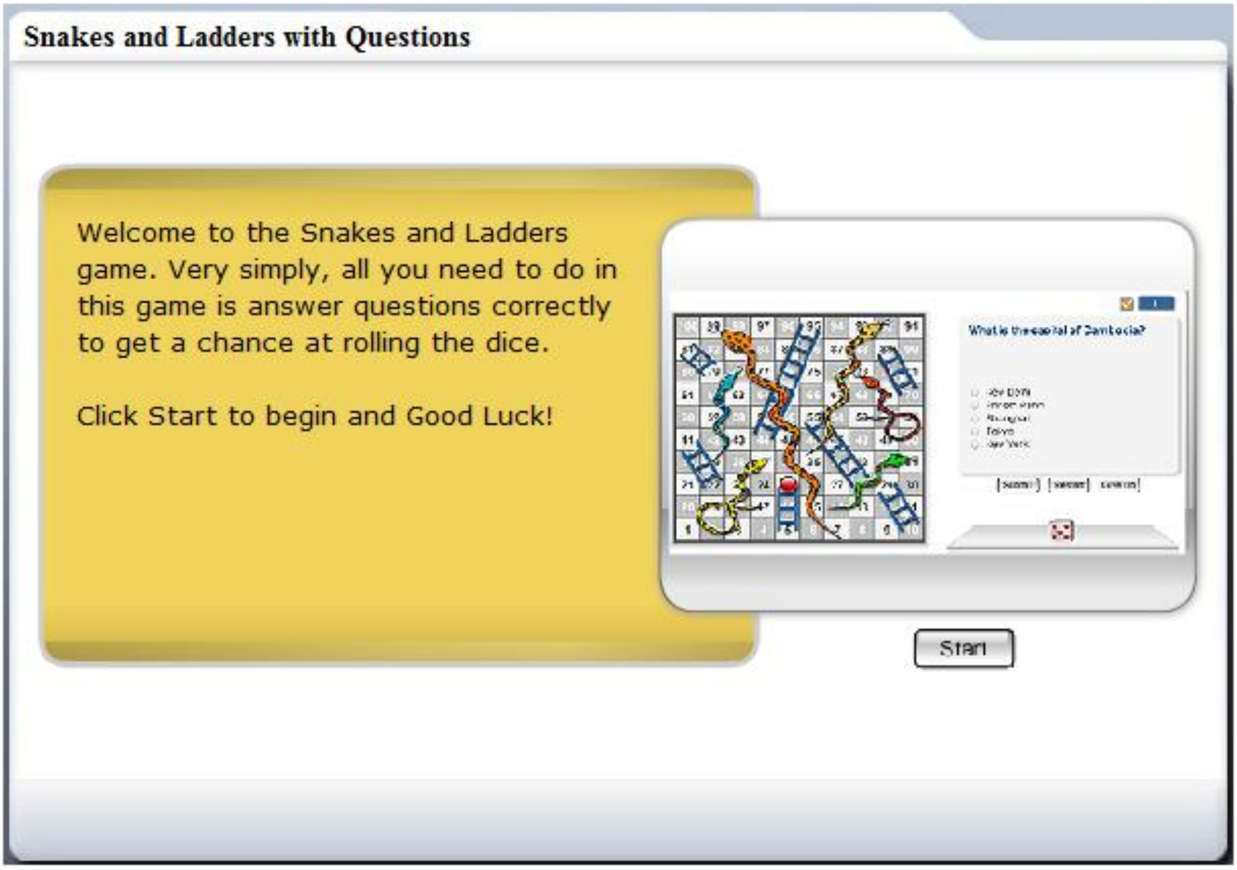

20.8.3 Revocable mandate

A cheque is a revocable mandate, or authority to the drawer's bankers to pay money, and the authority may be revoked any time, until presentation clearance by the bank by countermanding payment.[59]

Illustration
Puneet had drawn a cheque in favour of hi friend Jasmeet as a gift on his birthday. Puneet can revoke this cheque, or issue stop pament orders for that cheque at any time, before it is presented for payment by Jasmeet, and the cheque would not be cleared by the banker.

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20.8.4 Types of Cheque

Broadly speaking, cheques are of four types.

- Open Cheque, and
- Crossed Cheque.
- Bearer Cheque
- Order Cheque

Let us know details about these cheques.

Open Cheque: The holder of an open cheque has the following facilities:
i. He can receive his payment at the bank counter
ii. He can deposit the cheque in the bank
iii. By signing on the back of a cheque he can further endorse it.

1. **Crossed Cheque:** such cheques can be credited to the bank account of the payee.
2. **Bearer Cheque:** These cheques are payable to any person, who presents it for payment at the bank counter.
3. **Order Cheque:** An order cheque is one which is payable to a particular person and the word 'order' may be written at the back of it.

20.9 Distinction between Promissory Note and Bill of Exchange

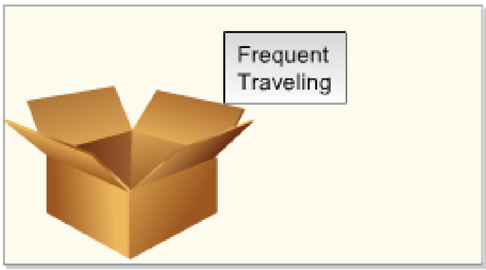
The following are the points of distinction between a promissory note and a bill of exchange:

Point of Distinction	Promissory Note	Bill of exchange
Parties	In case of a promissory note there are two parties namely the maker and the payee.	In case of a bill, there are three parties: the drawer, the drawee and the payee.
Promise and Order	A note contains an unconditional promise to pay.	A bill contains an unconditional order to pay.
Liability of Maker	Liability of maker of a note is absolute and primary.	The liability of the drawer of a bill is secondary and conditional to dishonor by drawee.
Payable to the Maker	A note cannot be made payable to the maker himself.	In case of a bill the drawer and the payee can be one and the same person.
Acceptance	A note does not require any acceptance of the maker before it is presented for payment.	A bill generally requires the acceptance of the drawee, before it is presented for payment.
Payable to Bearer	A note can never be made **'payable to bearer'.**	A bill can be made payable to bearer, but in no case, there can be a bill 'payable to bearer on demand'.
Notice of Dishonor	There is no need of a notice of dishonor to the maker, in case of a note as he, himself has dishonored it.	In case of a bill, the notice of dishonor must be given by the holder to all the prior parties, who are liable to pay the money.

3 (A) Kinds and Characteristics of Negotiable Instrument

Check your Progress

Promissory Note Vs Bill of Exchange



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3 (A) Kinds and Characteristics of Negotiable Instrument

20.10 Distinction between a Bill of Exchange and a Cheque

The distinction between a bill of exchange and a cheque is given below:

Point of Distinction	Bill of exchange	Cheque
Drawee	A bill can be drawn on any person including a banker.	A cheque is always drawn on a banker, who is a custodian of the drawer's money.
Payable on Demand	A bill may be payable on demand, or after the expiry of a certain period.	A cheque is always payable on demand.
Grace period	A bill, is entitled to three days of grace with respect to date of maturity.	A cheque is always payable on demand and hence there is no such grace period.
Acceptance	A bill may be required to be accepted before payment can be demanded from the drawee.	A cheque does not require any such acceptance, as the drawee is the banker of the drawer only, and hence his agent.
Payable to Bearer on Demand	A bill cannot be made payable to bearer on demand.	A cheque can be made payable to bearer on demand.
Protest for Dishonor	A bill may be noted or protested for dishonor.	A cheque is not required to be noted or protested for dishonor.
Crossing	There is no provision of crossing in case of a bill.	A cheque can be crossed, and in that case, payment can be received only through a bank account.
Countermanding Payment	Payment cannot be countermanded in case of bill of exchange.	The drawer of a cheque can request stop payment, and hence payment can be countermanded.

It must be noted that 'all cheques are bills of exchange but all bills of exchange are not cheques'.

3 (A) Kinds and Characteristics of Negotiable Instrument

Check Your Progress

Summary

Introduction

- The negotiable instruments Act was passed in 1881.
- It aims to legalise the system under which negotiable instruments pass from hand to hand.

Meaning and Definition

- A Negotiable Instrument means a promissory note, bill of exchange or cheque payable either to order or to bearer.
- It must be freely transferable either by delivery (when it is payable to the bearer of the document) or by endorsement and delivery (when the document is payable to order).
- The transferee taking the instrument in good faith and for consideration gets a good title to the same even if the title of the transferor is defective.
- The party holding the instrument should be entitled to maintain a suit thereon in case the instrument gets dishonored while in his custody.

Characterstics of Negotiable Instruments

- Writing and Signed by Its Maker
- Unconditional
- Fixed Sum of Money
- Transferable
- Absolute And Good Title
- Right to Recovery

Presumptions about Negotiable Instruments

- Consideration
- Date
- Time of Acceptance
- Time of Transfer
- Order of Endorsements
- Stamp
- Holder in Due Course

Relevant Provisions of RBI Act 1934

- A bill of exchange or hundi cannot originally be made payable to 'bearer on demand'.
- A promissory note cannot be originally made payable to bearer.

Kinds of Negotiable Instruments

3 (A) Kinds and Characteristics of Negotiable Instrument

- Promissory note
- Bill of exchange
- Cheque

Promissory Note

- An unconditional promise in writing made by one person (maker) to another person(payee)
- Signed by the maker
- Stamped
- Promise to pay
- On demand or at a fixed or determinable future time
- A sum certain in money
- Pay in terms of legal tender money only
- To, or to the order of, a specified person or to the bearer.
- The parties i.e. the maker and the payee must be certain.

Bill of Exchange

- An order in writing directing a person to pay a sum of money to a specified person.
- Duly signed by its drawer
- Accepted by its drawee
- Properly stamped
- Express order to pay
- Definite sum of money
- Definite and unconditional order
- Parties to a bill must be certain

Cheque

- A bill of exchange drawn on a specified banker, and not expressed to be payable otherwise than on demand
- Includes the electronic image of a truncated cheque
- Includes a cheque in electronic form
- issued on a specified banker only
- The amount specified is always certain, and must be clearly mentioned
- The payee is always certain.
- Must bear a date
- Types -Open cheque, Crossed cheque, Bearer cheque, Order cheque

3 (A) Kinds and Characteristics of Negotiable Instrument

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