

## Chapter 4

### Negotiable Instruments

#### Meaning of Negotiable Instruments

A Negotiable Instrument is a document guaranteeing the payment of a specific amount of money, either on demand, or at a set time, whose payer is usually named on the document.

A Negotiable Instrument is an instrument which entitles a person holding it to a sum of money and which is transferable from person to person by mere delivery like cash. The transferee becomes entitled to the money and also to the right to further transfer it.

**A Negotiable Instrument is a written document signed by the maker or drawer of the instrument, that contains an unconditional promise or order to pay an exact sum of money (with or without interest in a specified amount or at a specified rate) on demand or at an exact future time to a specific person, or to order, or to its bearer.**

#### Definition of Negotiable Instrument

According to section 13(a) of the Negotiable Instrument Act, 1881 "Negotiable Instrument means a promissory note, bills of exchange or cheque payable either to order or to bearer".

#### Essential elements or features

- **Must be in writing:** A negotiable instrument must be in writing. This includes handwriting, typing, printing and engraving, etc.
- **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.
- **Unconditional promise or order to pay:** In every negotiable instrument there must be an unconditional order or promise for payment.
- **Payment of certain sum of money:** 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.
- **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.
- **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.
- **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.
- **Title:** Negotiability confers absolute and good title on the transferee. It means that a person who receives a negotiable instrument has a clear and undisputable title to the instrument. However, the title of the receiver will be absolute, only if he has got the instrument in good faith and for a



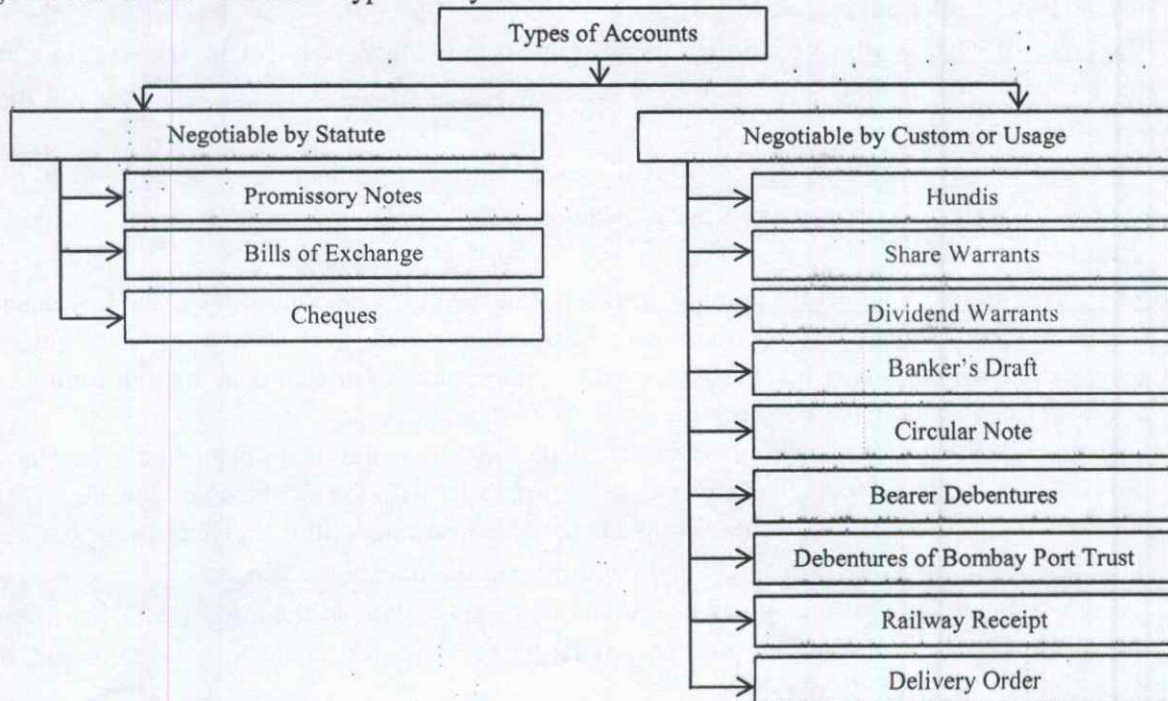
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consideration. Also the receiver should have no knowledge of the previous holder having any defect in his title. Such a person is known as holder in due course.

- **Easy Transferability:** A negotiable instrument is freely transferable. Usually, when we transfer any property to somebody, we are required to make a transfer deed, get it registered, etc. But, such formalities are not required while transferring a negotiable instrument. The ownership is changed by mere delivery (when payable to the bearer) or by valid endorsement and delivery (when payable to order). Further, while transferring it is also not required to give a notice to the previous holder.
- **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.
- **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.
- **Notice of transfer:** It is not necessary to give notice of transfer of a negotiable instrument to the party liable to pay.
- **Presumptions:** Certain presumptions apply to all negotiable instruments, for example consideration is presumed to have passed between the transferor and the transferee.
- **Number of transfer:** These instruments can be transferred indefinitely till they are at maturity.
- **Rule of evidence:** These instruments are in writing and signed by the parties, they are used as evidence of the fact of indebtedness because they have special rules of evidence.
- **Exchange:** These instruments relate to payment of certain money in legal tender, they are considered as substitutes for money and are accepted in exchange of goods.

### Kinds or Types of Negotiable Instrument

Negotiable Instruments are of 2 types. They are





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**A. Instruments Negotiable by Statute:** Negotiable Instruments recognized by statute are

- Promissory Notes
- Bills of Exchange
- Cheques

(NOTE: Explain the Promissory Notes, Bills of Exchange and Cheques from their respective contents given in the notes)

**B. Instruments Negotiable by Custom or Usage:** There are certain other instruments which have acquired the character of negotiability by usage or custom of trade. The list of negotiable instruments thus appears to be flexible and inclusive.

- **Hundis:** A Hundi is an unconditional order in writing made by a person directing another to pay a certain sum of money to a person named in the order. Hundis, being a part of the informal system have no legal status and are not covered under the Negotiable Instruments Act, 1881. Though normally regarded as bills of exchange, they were more often used as equivalents of cheques issued by indigenous bankers.
- **Share Warrants:** A share warrant is like an option issued by a company that gives the holder the right to buy stock from the company at a specified price within a certain designated time period. Warrants are not only the other way of participating in companies good performance but they are also more cost efficient in terms of overall returns. A stock warrant is a smart way to own shares of a company because a warrant usually is offered at a price lower than that of a stock option. Like an option, a warrant does not represent actual ownership in the stock of the company and it is simply the right (but not the obligation) to buy shares at a certain price in the future.
- **Dividend Warrants:** Dividend warrant is a type of Negotiable instrument and an order of payment (such as a cheque payable to a shareholder) in which a dividend is paid. A Dividend Warrant is an instrument by which a company pays dividend in the form of cash (money) back to its shareholders from the profits it has made out of its business operations.
- **Bankers Draft:** A banker's cheque or bankers draft is a cheque where the funds are withdrawn directly from a bank's funds, not from an individual's account. If an individual or company operates a current account, they may draw cheques to transfer funds from their account to an account belonging to a creditor. The creditor passes that cheque to their own bank, which will use a clearing house or similar system to arrange for the funds to be moved from the debtor to the creditor during a clearance period of a few days. Any debt is thus settled.
- **Circular Notes:** A circular note is a written request by a bank to its foreign correspondents to pay a specified sum of money to a named person. When presenting the note for payment, the person to be paid must produce a letter (containing the signature of an official of the bank and the person named) called a **letter of indication**, which is usually referred to in the circular note. Circular notes are generally issued against a payment of cash to the amount of the notes, but the notes need not necessarily be cashed, but may be returned to the banker in exchange for the amount for which they were originally issued.
- **Bearer Debentures:** The debentures which are payable to the bearer and whose (the bearer's) names do not appear in the register of debenture holders are known as "Bearer Debentures". Coupons for interest are attached to the document and interest is paid to the holders as it falls due. Bearer Debentures are transferable by mere delivery of the instrument.



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- **Debentures of Bombay Port Trust:** These are the debentures specially issued by Mumbai Port Trust. The debentures are having the same features of general classes of debentures.
- **Railway Receipts:** Railway Receipt (RR) means the receipt issued by Railway Administration on acceptance of goods and which entitles the consignee to take delivery of the goods at the Private Terminal at which the train terminates.
- **Delivery Orders:** A delivery order is a document from a consignee, or an owner or his agent of freight carrier which orders the release of the transportation of cargo to another party. Usually the written order permits the direct delivery of goods to a warehouseman, carrier or other person in the course of their ordinary business.

### **Promissory Notes**

**Meaning:** A Promissory note is a financial instrument in which one party (the maker or issuer) promises in writing to pay a determinate sum of money to the other (the payee), either at a fixed or determinable future time or on demand of the payee, under specific terms.

**Definition:** Section 4 of NI Act defines Promissory Note as, "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 a certain person, or to the bearer of the instrument".

**Parties to a Promissory Note:** The following are the two main parties involved in a promissory note

- **Maker:** Maker is a person who makes the promissory note and promises to pay the money stated therein.
- **Payee:** Payee is a person to whom the amount of promissory note is payable i.e., to whom the promise to pay is made.

### **Essential elements or features of Promissory Notes**

- **The promissory note must be in writing:** Mere verbal promises or oral undertaking does not constitute a promissory note. The intention of the maker of the note should be signified by writing in clear words on the instrument itself that he undertakes to pay a particular sum of money to the payee or order or to the bearer.
- **It must contain an express promise or clear undertaking to pay:** The promise to pay must be expressed. It cannot be implied or inferred. A mere acknowledgment of indebtedness is not enough.
- **The promise to pay must be definite and unconditional:** The promise to pay contained in the note must be unconditional. If the promise to pay is coupled with a condition, it is not a promissory note. It states that the promise to pay must not depend upon the happening of some outside event. It must be payable absolutely.
- **The maker of the pro-note must be certain:** The instrument should show on the fact of it as to who exactly is liable to pay. The name of the maker should be written clearly and ascertainable on seeing the document.
- **It should be signed by the maker:** Unless the maker signs the instrument, it is incomplete and of no legal effect. Therefore, the person who promises to pay must sign the instrument even though it might have been written by the promisor himself.



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- **The maker must be a certain person:** The instrument should clearly show the person engaged in drafting, signing and paying to payee. In case the promisors are more than one, then they may bind themselves jointly or severally.
- **The payee must be certain:** The money must be payable to a definite person or according to his order. The payee must be ascertained by name or by designation or to their order. It should clearly disclose to whom the payment has to be made on a particular date.
- **The amount must be certain:** The amount undertaken to be paid must be definite or certain or not vague. That is, it must not include contingent additions or subtractions.
- **The promise should be to pay money/ Payment must be in legal money of the country:** The promissory note should contain a promise to pay money and money only, i.e., legal tender money. The promise cannot be extended to payments in the form of goods, shares, bonds, foreign exchange, etc.
- **Bank note or currency note is not a promissory note:** As stated in the meaning the section, a bank note or currency note should not form the promissory notes as they are excluded in the definition of promissory notes.
- **It should bear the required stamping:** The promissory note should, necessarily, bear sufficient stamp as required by the Indian Stamp Act, 1889.
- **Demand:** The promissory note may be payable on demand or after a certain definite period of time.
- **Other formalities:** Though the formalities like serial number, date, place, consideration etc., are found on the face of a promissory note, they are not required statutorily. Thus, it will be valid, if the place of its making or the phrase for value received are not written.

### **Bills of Exchange**

**Meaning:** It is a written order signed by one person (drawer) requiring a second person (drawee) to pay on demand or at a stated date an amount of money to, or to the order of, a specified person or the bearer (payee).

**Definition:** 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 or the instrument - Sec. 5, Negotiable instrument act 1881.

### **Parties to Bills of Exchange**

- **Drawer:** The maker of a bill of exchange and responsible for the contents written in the bill
- **Drawee:** The person who is directed to pay.
- **Payee:** The person to whom the payment is made by the drawee as per the direction of drawer.

Along with these, the Holder and Acceptor also play role in bills of exchange.

- **Holder:** The drawer or the payee who is in possession of the bill is called as Holder.
- **Acceptor:** The person who accepts the bill is termed as Acceptor. He is none other than the Drawee.

### **Essential elements or features of Bills of Exchange**

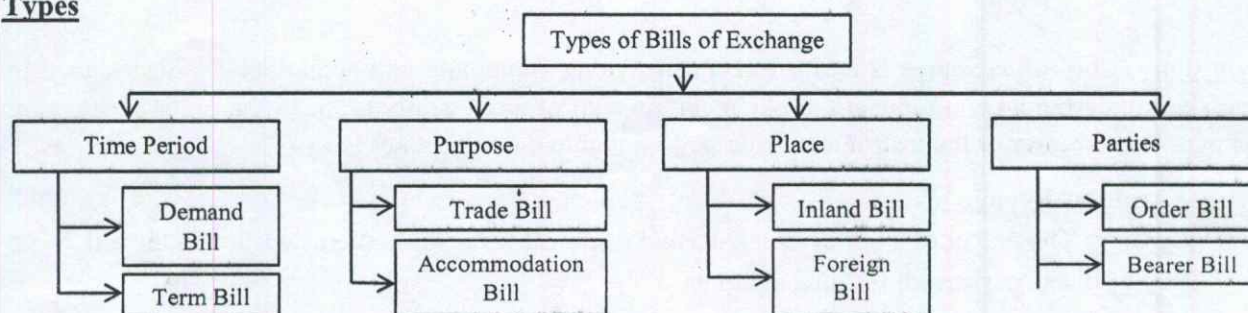
- **It must be in writing:** A bill of exchange must be in writing. It may be written in any language



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- **It must contain an order to pay:** The essence of a bill of exchange is that the drawer orders the drawee to pay money to the payee.
- **The order contained in the bill should be unconditional:** The drawer's order to the drawee must be unconditional and should not make the payment of the bill dependent on some contingency. A conditional bill of exchange is invalid.
- **It must be signed by the Drawer:** A Bill is not valid unless the drawer signs it and if Drawer has not signed it no action can be maintained against the acceptor or any other party.
- **The Drawee must be certain:** The next requisite is that the instrument must order a person to pay the amount of the bill. The person to whom the bill is addressed is called the 'Drawee' and he must be named or otherwise indicated in the bill with reasonable certainty. So that the payee knows the person to whom he should present the instrument for acceptance and payment. A bill cannot be addressed to two or more drawees in the alternative because it would create difficulties as to recourse if the bill were dishonoured.
- **The sum payable must be certain:** The sum payable is certain even though it is required to be paid with interest, or at the indicated rate of exchange or by installment with the provision that on the default in payment of installment, the whole amount shall become due and payable.
- **The instrument must contain an order to pay money and money only:** The medium of payment should be the legal tender i.e. money and nothing else. An instrument containing order to pay money along with some other thing or merely some other thing is not a valid bill. An instrument ordering the delivery of houses in addition to the payment of a sum of money is not a valid bill.
- **The payee must be certain:** A bill must state the person to whom payment is to be made.
- It should be properly stamped.
- There are certain other formalities, such as number, date, etc which are usually found in the bill. But they are not essential in law.

### Types



**A. On the basis of Time Period:** On the basis of period, the bills are grouped into two types

1. **Demand Bill:** It is also known as Sight Bill and these bills have no fixed date for the payment. They become payable at the time, when they are presented before payee by the holder. The time of payment of 'due date' not specified on this type of bill.
  - It is payable on demand or when presented by payee.
  - It may or may not have a maturity date.



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2. **Term Bill:** It is also known as Usance Bill that are payable after specified period of time. The term usance refers to the time period recognized by custom or usage for payment of bills. In other words, usance bills are called Time bills.

- It is payable at a specified future date, known as due date or maturity date.
- Example - Sixty days from date pay Mr. XYZ or to order a sum of Rs. 1,00,000 for value received.

**B. By Purpose/Object:** On the basis of the purpose, the bills are also grouped into two types

1. **Trade Bill:** It is a negotiable instrument issued by a trader for payment on a future date and becomes accepted when signed by acceptor or debtor. It is drawn by a creditor on his debtor for consideration. In accounting term Bills Receivables are termed as trade bill.

- Drawn and accepted for trade on credit.

2. **Accommodation Bill:** It is a document in written drawn by one person and accepted by another person to help each other. These bills do not involve in sale and purchase of goods, rather they are drawn without any consideration.

- It does not involve any trade of goods.
- It is mainly drawn for raising funds among parties and for discounting in money market.
- It is drawn without any consideration.

**C. By Place:** On the basis of the place, the bills are also sub-divided into two categories

1. **Inland Bill:** Bills that are drawn on Indian residents are called 'inland bills', such bills may be endorsed in a foreign country, or may remain in circulation in foreign countries and bill drawn in a foreign country is considered an inland bill if it is drawn on resident of India.

- It is drawn for trade in the same country.
- Drawer and Drawee reside in the same country.

2. **Foreign Bill:** These are the bills that are drawn in one country and accepted or payable in another country are called foreign bills. Eg. Bill drawn in England and accepted and payable in India, such bills are either;

- It is drawn in one country and payable in another country.
- Drawer and Drawee reside in different countries.
- Drawn in India but made payable outside India.

**D. By Parties:** On the basis of the parties, the bills are also divided further in two types

1. **Order Bill:** It is made out to, or to the order of a particular person and can be transferred by endorsement and delivery of the bill. In practice, the bill is made out either to the shipper's order or to that of the consignee or to his order. E.g. Warehouse receipt.

- It is payable to a specific person whose name is appearing on the bill i.e. either the Drawer or Any Endorsee.
- Example - Sixty days from date pay Mrs. Malini or to order a sum of Rs 2,50,000 for value received.

2. **Bearer Bill:** It states that delivery will be made to whosoever holds the bill. Such bill may be created explicitly or it is an order bill that fails to nominate the consignee whether in its original form or through an endorsement in blank. A bearer bill can be negotiated by physical delivery.



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- It is payable to any person in possession of the Bill on the maturity date.
- Example - Sixty days from date pay Mrs. Malini or to bearer a sum of Rs 2,50,000 for value received.

**E. Others** (NOTE: If given for 12 marks write along with option "E. Others")

1. **Supply Bill:** A supply bill is a bill that is drawn on a government agency by a supplier or contractor to deliver certain goods.
2. **Documentary Bill:** When bills are attached with trade documents, they are called the documentary bills. Such a bill is validated with specific documents that affirm the trade transaction between the supplier and the beneficiary.
3. **Clean Bill:** This bill does not have any proof of a document, so the interest is comparatively higher than the other bills.
4. **Fictitious Bill:** A bill in which the names of either of the party that is drawer or drawee or both are fictitious, is termed as a fictitious bill. This involves fictitious names of the one who makes the bill and the one who receives the bill.

### Difference between Bills of Exchange and Promissory Notes

Basis	Bills of Exchange	Promissory Notes
<b>Meaning</b>	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 demand.
<b>Section</b>	Mentioned in Section 5 of the Negotiable Instrument Act, 1881.	Mentioned in Section 4 of the Negotiable Instrument Act, 1881.
<b>Issued by</b>	Creditor	Debtor
<b>Parties</b>	There are 3 parties namely, drawer, drawee and payee.	There are 2 parties namely, maker and payee.
<b>Nature of payment</b>	It is an unconditional order to pay.	It is an unconditional promise to pay.
<b>Acceptance</b>	It requires acceptance of the drawee before it is presented for the payment.	It does not require acceptance since it is signed by the person who is liable to pay.
<b>Liability</b>	Liability of the maker is secondary and conditional.	Liability of the maker is primary and absolute.
<b>Notice of dishonour</b>	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.
<b>Copies</b>	Bill of Exchange can have copies.	Promissory note allows no copies.
<b>Can drawer / maker be the same person?</b>	Yes, the same person can be drawer and payee.	The same person cannot be drawer and payee.
<b>Protest</b>	Foreign bills must be protested for dishonour when such protest is required by the law of the place where they are drawn.	But no such protest is required in case of promissory note.



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<b>Maker's Position</b>	Drawer of the bill stands in immediate relationship with the acceptor and not the payee.	While in case of a promissory note, the maker stands in immediate relationship with the payee.
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### **Cheques**

**Meaning:** A cheque is a document that orders a bank to pay a specific amount of money from a person's account to the person in whose name the cheque has been issued.

**Definition:** A cheque is a bills of exchange drawn on a specified banker, and not expressed to be payable otherwise than on demand" – Section 6 Negotiable Instrument Act, 1881.

### **Parties**

- **Drawer:** The person who draws the cheque.
- **Drawee:** He is always the drawer's banker on whom the cheque is drawn.
- **Payee:** The person who receives the money through cheque whose name written on it.
- Holder, Holder for value, Holder in due course, Endorser and Endorsee.

### **Contents of the cheque**

- The Drawee, the financial institution where the cheque can be presented for payment
- Payee
- Date of issue
- Amount of currency
- Drawer, the person or entity making the cheque
- Signature of drawer
- Machine readable routing
- Account information

### **Features**

- **It must be in writing:** A cheque is a bill of exchange that is an order in writing but not an oral one. It must be in written format & specified by the bank.
- **An unconditional order:** A cheque is an order but not a request to pay, thus, once a cheque is issued, the drawer or the bearer of the cheque has to be dispensed with amount by the bank as specified in the cheque provided there are sufficient amounts to the credit of the account.
- **On a specified banker:** A cheque is always drawn on a particular banker only, usually the name and address of the banker is clearly printed on the cheque itself. Under the core banking system, a cheque of one branch may be encashed at another branch, anywhere, of the same bank.
- **Payee to be certain:** For the validation of any cheque, it must be made payable to the order of a certain specified person or to his agent or to the bearer there-of, a payee must be a certain person either a real person or an artificial person such as bank, company, businesses etc.
- **A certain sum of money:** A cheque is drafted for specific value of amount only. Any cheques with the words such as at least, above, below values may be out rightly rejected by the banker. However, the customer may have to write the value in figures and words, in case of a difference in amount written in value and words, the banker may consider the amount written is words as final.



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- **Payable on demand:** A cheque is always payable on demand. It is not necessary to use the word "On Demand" like in case of the demand bill. As per Section 19 of the Negotiable Instruments Act, 1881, unless a time factor is specified by the drawer, the cheque is always payable on demand.
- **To be signed by the drawer:** The cheque must be signed by the drawer on the bottom of the right hand side of the cheque where his name as mentioned in the account opening form would be printed. The sign must be specimen signature of the customer and must be matched for the genuineness of the signature.

### **Types**

#### **1. Open Cheque or Uncrossed Cheque**

- A cheque is classified as "Open" when cash payment is allowed across the counter of the bank.
- When a cheque is not crossed, it is known as an Open Cheque or an Uncrossed Cheque.
- These cheques may be cashed at any bank and the payment of these cheques can be obtained at the counter of the bank or transferred to the bank account of the bearer.
- An open cheque may be a bearer cheque or an order cheque.

##### **a. Bearer Cheque**

- The words "or bearer" printed on the cheque, & it is not cancelled, then the cheque is called a bearer cheque.
- A bearer cheque is made payable to the bearer i.e. it is payable to the person who presents it to the bank for encashment.
- In simple words a cheque which is payable to any person who presents it for payment at the bank counter is called 'Bearer cheque'.
- A bearer cheque may be transferred by delivery without any endorsement.

##### **b. Order Cheque**

- An order cheque is the one that has the word "or order" is written on the face of the cheque and the word "bearer" is cancelled out, such cheque is called an order cheque.
- An order cheque is a cheque which is payable to a particular person. It means that only the individual whose name is mentioned as the payee can receive the specified sum of money.
- The payee may transfer an order cheque by endorsement to another person by signing his name on the back of the cheque.

#### **2. Crossed Cheque**

- Crossing of a cheque means drawing two parallel lines on the face of the cheque with or without additional words like "& Co." or "A/C payee" or "Not Negotiable".
- A crossed cheque may only be credited to the payee's account.
- A crossed cheque cannot be encashed at the cash counter of a bank but it can only be credited to the payee's account.
- This is a safer way of transferring money than an Uncrossed or open cheque.

#### **3. Ante-dated Cheque**

- Cheque in which the drawer mentions the date earlier (date is one that was written before the current date) than the date on which it is presented to the bank, it is called as anti-dated cheque.



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- For example, if the current date is 1 January 2020 but the date on the cheque is 1 December 2019, then it is an ante-dated cheque.

### **4. Post-dated Cheque**

- Cheque on which drawer mentions a date which is yet to come (future date) to the date on which it is presented, is called post-dated cheque.
- **A post-dated cheque bears a date later than the date it was issued on.**
- It can only be cashed after the date specified by the payer.
- The post-dated cheque can be valid after the mentioned date but not before it.
- Even if it is presented to the bank, the bank will not process it until the mentioned date.
- For example- If a cheque presented on 10th Jan 2020 bears a date of 25th Jan 2020, it is a post-dated cheque. The bank will make payment only on or after 25th Jan 2020.

### **5. Stale Cheque**

- If a cheque is presented for payment after a period of three months from the date of cheque, it is called as "Stale Cheque".
- A stale cheque has already passed its validity date and can no longer be cashed. These cheques are dishonored by banks.

### **6. Traveller's Cheque**

- It is issued by a bank.
- A traveller's cheque can be cashed by the payee at another bank in another country.
- The payment will be received in that country's currency.
- It becomes useful when you are heading on a foreign trip and do not wish to carry too much cash.
- A traveller's cheque does not have an expiry date.

**7. Dishonour of Cheque:** When a bank fails to deposit the money specified on the check into the payee's account, it is said to have dishonoured the cheque.

### **8. Blank Cheques**

- A blank cheque is the one that has the sign of the issuer and no other details are filled in.
- Blank cheques pose a high risk because if lost, anyone who finds it can fill in any amount and issue it to themselves.

### **9. Self Cheques**

- A self cheque has the word 'self' written as the payee.
- It is used by the issuer to withdraw money from their bank account.
- A self cheque can be cashed only at the issuer's bank.

### **10. Account Payee Cheques**

- An account payee cheque is a bearer's cheque that has the words "account payee" written on the top left-hand side, within two parallel lines, and crossed twice.
- Amount in such cheques will be transferred only to the person's account that is written on the cheque.



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- It is considered to be the safest way to issue a cheque as the amount is transferred only to the person's account.

**11. Banker's Cheques:** Banker's cheques are the cheques that are issued by the bank so it guarantees payment.

### **12. Mutilated Cheques**

- If a cheque reaches the bank in a torn or otherwise damaged condition, it is called a mutilated cheque.
- If a cheque is torn or the important information is not visible, then it will become an invalid cheque.

### **Difference between Cheques and Bills of Exchange**

Basis	Cheques	Bills of Exchange
<b>Meaning</b>	A cheque is a document that orders a bank to pay a specific amount of money from a person's account to the person in whose name the cheque has been issued.	It is a written order signed by one person (drawer) requiring a second person (drawee) to pay on demand or at a stated date an amount of money to, or to the order of, a specified person or the bearer (payee).
<b>Section</b>	Cheque is defined under Section 6 of The Negotiable Instrument Act, 1881.	Bill of Exchange is defined under Section 5 of The Negotiable Instrument Act, 1881.
<b>Banker</b>	Cheque is always drawn on a banker.	Bill may be drawn on any one, including a banker.
<b>Payment</b>	It can only be drawn and payable on demand.	It may be drawn payable on demand, or on the expiry of a certain period after date.
<b>Acceptance</b>	It does not require acceptance and is intended for immediate payment.	It must be accepted before payment can be demanded.
<b>Grace Period</b>	No grace period is allowed in case of cheque payment.	Grace period of 3 days is allowed in the case of time bills.
<b>Discharge of drawer</b>	Drawer of the cheque is discharged only if he suffers any damage by delay in presentment for payment.	Drawer of the bill is discharged, if it is not presented for payment.
<b>Notice of Dishonour</b>	No notice of dishonour of cheque.	But notice of dishonour of a bill is necessary.
<b>Crossing</b>	Cheque may be crossed.	Bill cannot be crossed.
<b>Stamp</b>	It need not be stamped before payment.	It must be sufficiently stamped before payment.
<b>Discounting</b>	It cannot be discounted.	It can be discounted with a bank.



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<b>Revocable</b>	The authority may be revoked by countermanding payment and is determined by notice of the customer's death or insolvency.	Countermanding payment will not be the same in case of a bill.
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### Difference between Cheques and Promissory Note

Basis	Cheques	Promissory Note
<b>Meaning</b>	A cheque is a document that orders a bank to pay a specific amount of money from a person's account to the person in whose name the cheque has been issued.	A Promissory note is a financial instrument in which one party promises in writing to pay a determinate sum of money to the other (the payee), either at a fixed or determinable future time or on demand of the payee, under specific terms.
<b>Section</b>	Cheque is defined under Section 6 of The Negotiable Instrument Act, 1881.	Promissory Note is defined under Section 4 of The Negotiable Instrument Act, 1881.
<b>Drawer of the Instrument</b>	Creditor	Debtor
<b>Order / Promise</b>	It contains an order to pay.	It contains promise to pay.
<b>Number of Parties</b>	In case of cheques there are 3 parties namely, drawer, drawee and payee.	In case of promissory note there are 2 parties namely, maker and payee.
<b>Object</b>	It is used because it is a simple and easy medium of exchange and serving of metallic money.	It is used for receiving and giving credit.
<b>Crossing</b>	It may be crossed.	It cannot be crossed.
<b>Payable to Bearer</b>	A cheque may be drawn as payable to payable to bearer.	A pronote cannot be drawn payable to bearer.
<b>Stop Payment</b>	Its payment can be stopped by giving notice to the bank.	A pronote payment cannot be stopped if once issued.
<b>Use of Form</b>	It is drawn on printed form issued by a particular bank.	It may be drawn on any paper and there is no need of any particular.
<b>Drawee</b>	It is always drawn to a particular bank where account is available.	It can be drawn on any person.
<b>Drawer and Payee</b>	In case of cheques drawer and payee can be the same person.	In case of pronote drawer and payee cannot be the same person.

### Crossing of Cheques

A crossing is an instruction to the paying banker to pay the amount of cheque to a particular banker and not over the counter. The crossing of the cheque secures the payment to a banker. It also traces the person



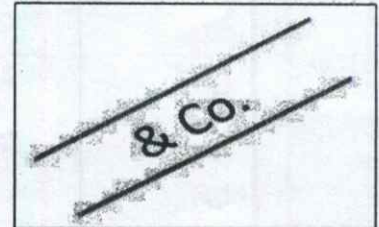
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so receiving the amount of cheque. Addition of words 'Not negotiable' or 'Account Payee only' is necessary to restrain the negotiability of the cheque. The crossing of a cheque ensures security and protection to the holder.

### Types of crossing

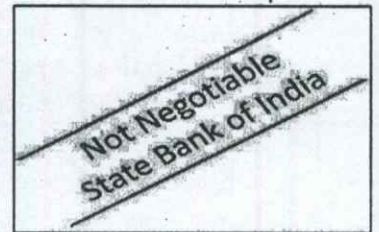
#### 1. General Crossing

- When across the face of a cheque two transverse parallel lines are drawn at the top left corner, along with the words & Co., between the two lines, with or without using the words not negotiable, it is called a general crossing.
- In the case of general crossing on the cheque, the paying banker will pay money to any banker.
- For the purpose of general crossing two transverse parallel lines at the corner of the cheque are necessary.
- The holder of the cheque or the payee will receive the payment only through a bank account and not over the counter.
- The words 'and Co.' have no significance as such.
- The words 'not negotiable' are significant as they restrict the negotiability and thus, in the case of transfer, the transferee will not give a title better than that of a transferor.



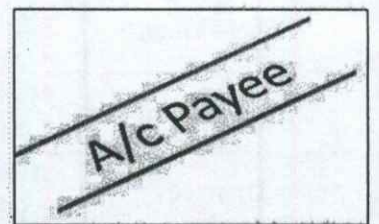
#### 2. Special Crossing

- A cheque in which the name of the banker is written, across the face of the cheque in between the two transverse parallel lines, with or without using the word 'not negotiable'. This type of crossing is called a special crossing.
- In a special crossing, the amount on the crossed cheque is paid only to the banker whose name is written on the cheque.
- Hence, the cheque will be honoured only when the bank mentioned in the crossing orders the same.



#### 3. Restrictive or Account Payee Crossing

- When in between the two transverse parallel lines, the words 'A/c payee' is written across the face of the cheque, then such a crossing is called restrictive crossing or account payee crossing.
- In this case, the cheque can be credited to the account of the stated person only, making it a non-negotiable instrument.
- This type of crossing restricts the negotiability of the cheque.
- It directs the collecting banker that he needs to credit the amount of cheque only to the account of the payee, or the party named.
- Where the collecting banker credits the proceeds of a cheque bearing such crossing to any other account, he shall be guilty of negligence.

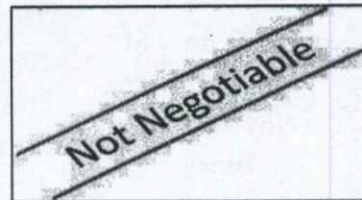




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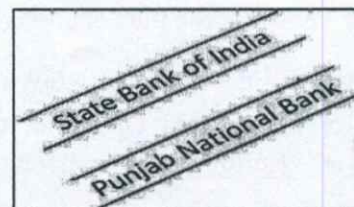
### 4. Not Negotiable Crossing

- When the words not negotiable is mentioned in between the two transverse parallel lines, indicating that the cheque can be transferred but the transferee will not be able to have a better title to the cheque.
- The Not Negotiable Crossing does not mean that the cheque is non-transferrable. A person taking a cheque bearing a general or special crossing with the words 'not negotiable' will not have and is neither capable of giving a better title than that which the person from whom he took it had.
- Only if the title of the transferor is good, the title of the transferee is also good. Hence, in case of any taint in the title of any one of the endorsers, the title of all the subsequent transferees also becomes tainted.
- A person who receives it in good faith, without negligence, for value, before maturity and without knowing the defect in the title of the transferor, gets a good title to the instrument. But, Not Negotiable Crossing takes away this important feature. In this case, the transferee does not get the rights of the holder in due course.



### 5. Double Crossing

Double crossing is when a bank to whom the cheque crossed specially, further submits the same to another bank, for the purpose of collection as its agent. In this situation the second crossing should indicate that it is serving as an agent of the prior banker, to whom the cheque was specially crossed.



### Difference between General Crossing and Special Crossing

Basis	General Crossing	Special Crossing
<b>Meaning</b>	When across the face of a cheque two transverse parallel lines are drawn at the top left corner, along with the words & Co., between the two lines, with or without using the words not negotiable, it is called a general crossing.	A cheque in which the name of the banker is written, across the face of the cheque in between the two transverse parallel lines, with or without using the word 'not negotiable'. This type of crossing is called a special crossing.
<b>Section</b>	General Crossing is defined under Section 123 of The Negotiable Instrument Act, 1881.	Special Crossing is defined under Section 124 of The Negotiable Instrument Act, 1881.
<b>Payment</b>	Payment may be received through any bank.	Payment can be received only from the bank in whose name the cheque has been crossed
<b>Conversion</b>	General crossing can be converted into Special crossing.	Special crossing can never be converted into General crossing.
<b>Words between Parallel Transverse</b>	The words like "& Co", "Not Negotiable", will be used in	The words like "Not Negotiable", "Banker Name", will be used in



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Lines	General crossing.	Special crossing.
<b>Significance of Words between Parallel Transverse Lines</b>	The words like "& Co", "Not Negotiable", used in General crossing does not carry any significance. The use of these words is optional.	In Special crossing, the mention of the name of specific bank between the two parallel lines is essential.
<b>Object / Objective</b>	The objective is to make the cheque secure.	The objective is to provide a greater degree of security to the cheque.

### Endorsement

**Meaning:** The act of signing a negotiable instrument for the purpose of transferring it to somebody else is known as Endorsement.

**Definition:** Section 15, Negotiable Instrument Act, 1881 defines Endorsement as "When the maker or holder of a negotiable instrument signs on the same, otherwise than as such maker, for the purpose of negotiation, on the back or face thereof or on a slip of paper annexed thereto or so signs for the same purpose of stamped paper intended to be completed as a negotiable instrument, he is said to have endorsed the same and is called endorser".

**Parties:** Endorsement involves two parties:

- **Endorser:** The person making the endorsement.
- **Endorsee:** The person to whom the instrument is endorsed.

### Essentials or features

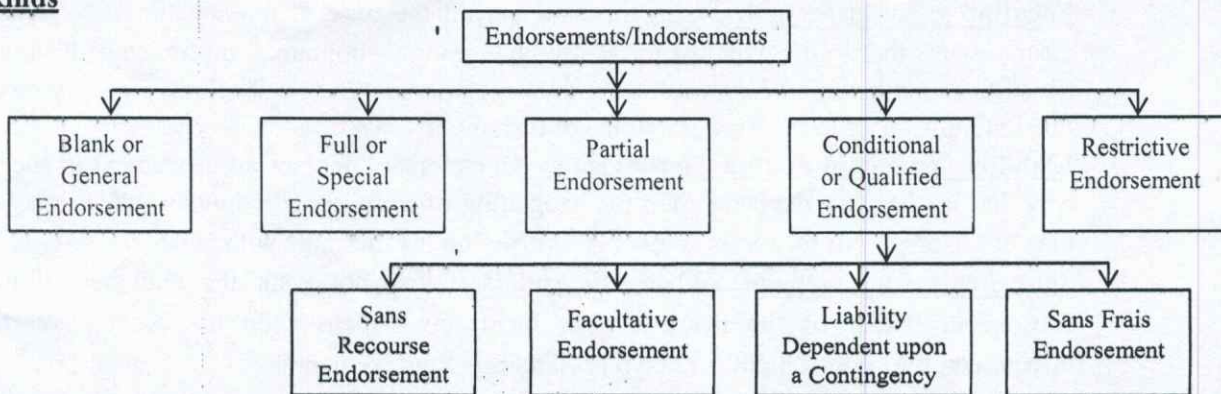
- **It must be on instrument:** It must be on the instrument. The endorsement may be on the back or face of the instrument and if no space is left on the instrument, it may be made on a separate paper attached to it called allonge.
- **Endorsement by Maker or Holder:** It must be made by the maker or holder of the instrument. A stranger cannot endorse it.
- **Signature of Endorser:** It must be signed by the endorser. The endorser should sign the endorsement in the same style and with the same spellings as written in the instrument. If illiterate, Thumb-impression should be attested. Signature may be made on any part of the instrument.
- Signature should be in ink and not by pencil or rubber stamp.
- Mere signatures of the holder, without any words, also constitute endorsement.
- Any number of endorsements may be made on the instrument.
- **No Specific Form:** It may be made either by the endorser merely signing his name on the instrument (it is a blank endorsement) or by any word showing an intention to endorse or transfer the instrument to a specified person (it is a full endorsement). No specific form of words is prescribed for an endorsement, but intention to transfer must be present.
- **Delivery:** It must be completed by delivery of the instrument. The delivery of possession of the instrument with intention of passing the property to endorsee is important. The delivery must be made by the endorser himself or by somebody on his behalf with the intention of passing property therein. If delivery is conditional endorsement is not complete until the condition is fulfilled.



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- **Endorsement of entire bill:** It must be an endorsement of the entire bill. A partial endorsement i.e. which supports to transfer to the endorsee a part only of the amount payable does not operate as a valid endorsement.
- An endorsement is complete only when
  - ✓ The holder signs on the face or back of the instrument.
  - ✓ The instrument is delivered to the endorsee.
  - ✓ It is signed and delivered with the intension of vesting the endorsee with the rights of the holder.

### Kinds



- **Blank or General Endorsement (Secs. 16(1) and 54):** When the endorser signs his name only on the face or back of the instrument, it is known as blank or general endorsement. A blank endorsement specifies no endorsee and the instrument in consequence becomes payable to bearer even though originally it was payable to order (Sec 54).
- **Full or Special Endorsement (Sec. 16(1)):** If the endorser, in addition to his signature, also adds a direction to pay the amount mentioned in the instrument to, or to the order of, a specified person, the endorsement is said to be in full. For example, "Pay R or order" or "Pay to A" etc., followed by the signature of the endorser.
 

A blank endorsement may be converted into a full endorsement. The provision contained in Sec. 49 of the Act. According to this section, the holder of an instrument endorsed in blank, may convert it into an endorsement in full by writing the name of some person (endorsee) above the signature of the endorser. The advantage of such endorsement is that the holder does not become liable as an endorser though he transfers the instrument.
- **Partial endorsement (Sec. 56):** It purports to transfer to the endorsee only a part of the amount payable on the instrument. Such an endorsement does not operate as a negotiation of the instrument and is invalid.
- **Restrictive Endorsement (Sec. 50):** An endorsement is said to be restrictive when the endorser, by express words, restricts the right of further negotiation of the instrument or merely entitles the endorsee of the instrument to receive the contents of the instrument for a specific purpose. For example, "Pay C for my use", "Pay C or order for the account B".
- **Conditional or Qualified Endorsement (Sec. 52):** An endorsement is conditional or qualified which limits or negatives the liability of the endorser. The endorser limits or excludes his



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liabilities by putting some condition in the instrument. It differs from restrictive endorsement. The restrictive endorsement prohibits further negotiability of the instrument. But the conditional endorsement does not prohibit the negotiability. It simply limits or excludes the liability of the endorser. Such an endorsement is done in any one of the following forms

- ✓ **Sans Recourse Endorsement:** When the person making the endorsement makes it clear that he shall not be liable to the endorsee or the subsequent holders of the instrument in case the instrument is dishonoured, such an endorsement is called Sans Recourse Endorsement. Endorser may exclude his personal liability by using the words "Sans Recourse". For example, "Pay to X or order Sans Recourse".
- ✓ **Facultative Endorsement:** When the endorser, at the time of making the endorsement clearly states that in the event of the instrument being dishonoured, no notice of dishonor needs to be served upon him; such an endorsement is known as a facultative endorsement. For Example, "Pay to A or order. Notice of dishonour waived".
- ✓ **Liability dependent upon a Contingency:** An endorser endorses an instrument in such a way that his liability depends upon the happening of some specified event, which may or may not happen. For example, "Pay to A or order on his marriage with B".
- ✓ **Sans Frais Endorsement:** Where the endorser does not want the endorsee or any subsequent holder of the instrument to incur any expenses on his account on the instrument, the endorsement is known as San Frais Endorsement.

### Rules

- All endorsement should be made in ink only, even though, law does not object to an endorsement being made in pencil, but endorsements in pencils are liable to alteration and obliteration. So, they are discouraged.
- It has been held that, a typewritten endorsement is valid under the Act. Even, endorsement in printed character can be accepted. But, in practice bankers do not normally permit it, as it can be duplicated very easily.
- A rubber-stamp endorsement is as valid as a written endorsement. But it is not conducive for the safety of a banker and customer, if it is not accompanied by the handwritten signature of an authorized officer.
- Where an endorsement happens to be in a language which the banker is not expected to know, then, the paying banker can refuse the payment for its confirmation. But he should give the valid reasons for the same.
- **Delivery:** Endorsement must be completed by delivery of the instrument.
- **Signature of the endorser:** The signature on the document for the purpose of endorsement must be that of the endorser or any other person who is duly authorised to endorsement on his behalf.
- **Spelling:** If the endorser signs in block letters, it is not considered as a regular endorsement. Therefore, an endorsement in block letter is not a regular endorsement. Example: JOHN SMITH. No addition or omission of initial of the name: The initial name must neither be added nor be omitted from the name of the payee or endorsee as given in the cheque.
- **Prefixes and suffixes to be excluded:** The prefixes and suffixes to the names of the payee or endorsee need not be included in the endorsement. For example, the words "Mr., Mrs., Miss, Shri,



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Shrimati, General, Dr., Major, etc.” need not be given by the endorser otherwise the endorsement will not be regular.

### **Assignment Questions**

#### **Section A**

1. Give the meaning Negotiable Instrument, Hundi, Crossed Cheque, Endorsement.

(NOTE: Parties involved in Negotiable Instrument is important)

#### **Section B**

1. What is Endorsement? Explain the types of Endorsements.
2. What are the essential features of Negotiable Instrument?

(NOTE: Difference between any of the two Negotiable Instruments may be asked)

#### **Section C**

1. Define Cheque. Explain the different types of cheques.
2. Give the meaning for Bills of Exchange. Briefly explain the types of Bills of Exchange.
3. Explain about the Endorsement of Negotiable Instrument. (All concept of Endorsements are important)
4. What is Crossing and explain the types of crossing?
5. What is Negotiable Instrument? Briefly explain the types of Negotiable Instrument.

(NOTE: Meaning and Features of all Negotiable Instruments that is Promissory Notes, Bills of Exchange and Cheque are important)