

Negotiable Instruments



Negotiable Instruments

Negotiable Instruments Act, 1881

Concept/Object/Purpose:

The object is to provide legal protection to different mercantile instruments.

- The Act regulates the issue & negotiation of the negotiable instruments as mentioned in this Act.
- In case of no explicit provisions in the Act, the rights and obligations of the respective parties shall be governed by the provisions of Contract Act.



Negotiable Instruments

Negotiable Instruments Act, 1881

Concept/Object/Purpose:

Negotiable instruments are one of the modes of settlement of transactions.

- Transactions can be settled through cash or anyother mode. for example, through a cheque etc.



Negotiable Instruments

Negotiable means the quality of transferability by delivery or by endorsement and delivery.

Instrument means a written document by which a right is created in favor of some person.

- **Negotiable Instrument** means a written document, which is freely transferable and which creates a right in favor of some person to receive some money.



Negotiable Instruments

According to Section 13 of this Act,

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

- The Act besides above three negotiable instruments recognizes any other instrument satisfying the characteristics of negotiability, as a Negotiable Instrument.



Negotiable Instruments

Quasi Negotiable Instruments- (Instruments recognized as such)

1. Dividend Warrants
2. Share Warrants
3. Bearer Debentures
4. Government Promissory Notes etc.



Negotiable Instruments

Promissory Note

According to Section 4:

“A promissory note is an instrument in writing (not being a bank note or a currency note) containing unconditional undertaking, signed by the maker to pay on demand or at a fixed or determinable future time a certain sum of money only to or to the order of a certain person, or to the bearer of the instrument.



Negotiable Instruments

Specimen of a Promissory

Rs. 500,000/- Lahore February 12,

2008

Ninety days after date, I promise to pay Faisal Hameed or order the sum of rupees five hundred thousand only for value received.

Signature

Kamran Ahmad

Revenue Stamps

(The Maker)



Negotiable Instruments

Promissory Note: Contd..

The Notes given below do not qualify to be called promissory note in the light of definition contained in section 4

Thirty days after date, I promise to pay Mr. Ahmad Kamal or order the sum of rupees one hundred thousand only and the amounts which may be due to Ahmed Kamal by due date.



--This is not the promissory note since the amount promised is not certain and ascertainable on the date of making the promise/ undertaking.



Negotiable Instruments

Promissory Note: Contd..

The notes given below do not qualify to be called promissory note in the light of definition contained in section 4

- **I owe Rs 100,000 to MR. Ahmad Kamal**
--This is not a promissory note since it is just an acknowledgement not an undertaking

- **I promise to pay Rs 100,000 to Mr. Ahmad Kamal thirty days after getting admission in a University.**
--This is not a promissory note since the time of payment is not certain/ ascertainable at the time of making the promise.



Negotiable Instruments

Parties in a Promissory Note

1. Maker
2. Payee



Negotiable Instruments

Essentials of a Promissory Note:

- In writing
- Promise to pay
- Unconditional promise
- Signed by maker
- Maker a certain person
- Payee is a certain person
- Certain sum
- Legal tender money to be paid
- Time of payment
- Other formalities.



Negotiable Instruments

Essentials of a Promissory Note

- Properly stamped under Stamp Act.
- Promise to pay for lawful consideration
- Date of issue and place of issue to be contained therein.



Negotiable Instruments

Bill of Exchange

According to Section 5:

“A bill of exchange is an instrument in writing containing an unconditional order, signed by maker, directing a certain person, to pay on demand or at fixed or determinable future time a certain sum of money only to, or to the order of, a certain person or to the bearer of the instrument”.



Negotiable Instruments

Specimen of Bill of Exchange
Rs. 100,000/- Lahore

August 20, 2007

Ninety days after date, pay to Mr. Ahmad
Kamal or order rupees one hundred
thousand only for value received

Signature

Accepted by

Yasir Mehmood Drawee XYZ

(Drawee)

(Drawer)

Revenue Stamp



Negotiable Instruments

Essentials of Bill of Exchange

- In writing
- Order to pay
- Unconditional order
- Signed by the drawer
- Drawee certain person
- Time of payment



Negotiable Instruments

Essentials of Bill of Exchange

- Certain sum
- Legal tender money
- Payee certain person
- Other formalities
 - i. Date
 - ii. Place
 - iii. Lawful consideration
 - iv. Revenue stamp



Negotiable Instruments

Cheque

According to Section 6:

“A cheque is a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand”.

Parties:

1. Drawer
2. Drawee (Banker)
3. Payee.



Negotiable Instruments

Essentials of a Cheque

- In writing
- Unconditional order
- Signed by drawer
- Payable on demand
- Specified banker
- Printed form (Cheque Leaves to be printed)
- Payment in money form only
- Certain amount
- Payable to specified person or his order or bearer.
- Date



Negotiable Instruments

Types of Cheques:

1. Bearer Cheques
2. Order Cheques
3. Crossed Cheques



Crossed Cheques and their Collection

- ✓ **Crossing:** Crossing means drawing two
- ✓ parallel transverse lines across the cheque.
- ✓ **General Crossing:** Specimens

A

B & Co

C & payee's AC only



Negotiable Instruments

A

B & Co

C & payee's AC only



Negotiable Instruments

Special crossing: Specimens

A ABC BANK

B WWW BANK

C XYZ BANK LTD—LAHORE BRANCH



Distinguishing Features Between

Promissory Note

& Bill of Exchange

Exchange

1. Maker—debtor
2. Maker & Payee different
3. Two parties
4. Unconditional promise

1. Drawer—creditor.
2. Drawer and Payee may be the same.
3. Three Parties .
4. Contains an order to make the payment



Distinguishing Features Between Cheque & Promissory Note

- Drawer is creditor must have an account in the Bank
- Three parties
- Contains order to Drawee (Bank)
- Always Payable on Demand
- Maker owes some money to another person.
- Two parties
- Contains promise to pay
- Payable on Demand
 - or on a fixed date or
 - determinable future
 - time



Negotiable Instruments Act 1881



Negotiable Instruments

❖ Endorsement:

According to Section 15:

“ When the maker or holder of a negotiable instrument signs the same, otherwise than as such maker, for the purpose of negotiation, on the back or face thereof or on a slip of paper annexed thereto, or so signs for the same purpose a stamped paper intended to be completed as a negotiable instrument, he is said to indorse the same, and is called endorser”.



Negotiable Instruments

❖ Essentials of an Endorsement

1. Endorser must be holder
2. Instrument must be signed by the endorser
3. Intention to negotiate



Negotiable Instruments

❖ Kinds of Endorsement:

- 1) Blank or general. Sec. 16
- 2) Full or special endorsement. Sec. 16
- 3) Restrictive sec. 50
- 4) Without recourse or Conditional sec. 52
- 5) Partial endorsement sec. 56



Negotiable Instruments

❖ Kinds of Endorsement:

■ Full or special endorsement:

-- Endorser mentions the name of endorsee and puts his signature.

Sec 16 (1) If the endorser signs his name only, the endorsement is said to be "**in blank**", and if he 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**", and the person so specified is called the "endorsee" of the instrument.



Negotiable Instruments

❖ Kinds of Endorsement:

- Full or special endorsement: Section 16:
Contd..

"Endorsee".

(2) The provisions of this Act relating to a payee shall apply with the necessary modifications to an endorsee.

Negotiable Instruments

❖ Kinds of Endorsement:

■ **Restrictive Endorsement.**

-- Such endorsement restricts further negotiation of the instruments, for example

Pay AMIT only

Signature of endorser

Negotiable Instruments

❖ Kinds of Endorsement:

■ **Restrictive Endorsement-Sec. 50 (2)**

-- An endorsement is restrictive which either--

(a) restricts or excludes the right to further negotiate the instrument, or

(b) constitutes the endorsee an agent of the endorser to endorse the instrument or to receive its contents for the endorser or for some other specified person.



Negotiable Instruments

❖ Kinds of Endorsement:

❖ Without Recourse Endorsement

-- without responsibility of the endorser . For example:

Pay AMIT without recourse to me

Signature of endorser



❖ Kinds of Endorsement:

❖ **Without Recourse Endorsement**

Sec 52 (Contd.)

The endorser of a negotiable instrument may, by express words in the endorsement, exclude his own liability thereon, or make such liability or the right of the endorsee to receive the amount due thereon depend upon the happening of a specified event, although such event may never happen.



❖ Kinds of Endorsement:

❖ Without Recourse Endorsement

Sec 52 (Continued)

- Where an endorser so excludes his liability and afterwards becomes the holder of the instrument, all intermediate endorsers are liable to him.

Negotiable Instruments

❖ Kinds of Endorsement:

❖ **Without Recourse Endorsement**

■ Sec 52: Contd..

Where the right of an endorsee to receive the amount due on the negotiable instrument is made dependent in the aforesaid manner the condition is valid only as between the endorser and the endorsee.

Negotiable Instruments

- ❖ Kinds of Endorsement:
- ❖ Without Recourse Endorsement
- Sec 52: Contd..

Where the endorsement of a negotiable instrument purports to be conditional, the payer may disregard the condition and payment to the endorsee is valid whether the condition has been fulfilled or not.

Negotiable Instruments

❖ Kinds of Endorsement:

■ Partial Endorsement:

- the endorser directs the transfer only a part of amount payable on a bill of exchange or promissory note through such endorsement.

Negotiable Instruments

❖ Kinds of Endorsement:

▪ Partial Endorsement: Sec 56

- (1) Negotiation by endorsement must be of the entire instrument.
- (2) An endorsement which purports to transfer to the endorsee only a part of the amount payable, or which purports to transfer the instrument to two or more endorsees severally, is not valid as a negotiable of the instrument; but where such amount has been paid in part, a note to that effect may be endorsed on the instrument, which may then be endorsed for the balance.

Negotiable Instruments

❖ Effect of endorsement

- When a negotiable instrument is endorsed and delivered to the endorsee, the endorsee becomes entitled for the ownership rights in the instrument and also a right is vested in him to further transfer/ endorse the instrument, the right not vested to an endorsee through a restrictive endorsement.



Negotiable Instruments

❖ Maturity of the Instruments

What is Maturity:

It is the date of a promissory note or bill of exchange, at which it falls due.

(Section 22 defines the maturity)



Days of Grace:

- Three days of grace are provided in section 22 for determining payability of instrument but said days of grace are not available when instrument is payable on demand or at sight or on presentment
- Days of Grace are applicable in case of Promissory note and bill of exchange but not cheque, since it is always payable on demand.

Parties to Notes, Bills and Cheques

❖ Parties to Promissory Note:

1. Maker:

- The person who makes the note and undertakes to pay the amount stated in the promissory note.

2. Payee:


- The person to whom the amount is payable under promissory note.

Parties to Notes, Bills and Cheques

❖ Parties to Promissory Note:

3. Holder:

- The person who may be the payee or endorsee of the promissory note. Holder is the person who is entitled to the possession of the instrument in his own name and also entitled to receive the amount due under a promissory note.



Parties to Notes, Bills and Cheques

❖ Parties to Promissory Note: Contd..

4. Endorser

- The person who by endorsement transfers the promissory note to another person.

5. Endorsee

- The person to whom the promissory note is transferred by endorsement .

Parties to Notes, Bills and Cheques

❖ Parties to Bill of Exchange

1. Drawer


- The maker of a bill of exchange is Drawer._

2. Drawee

- The person who is directed by the drawer to pay the amount stated in bill of exchange is called drawee._

3. Acceptor

- The drawee when accepts the **Bill of Exchange**, he becomes acceptor



Parties to Notes, Bills and Cheques


❖ Parties to Bill of Exchange

4. Payee

- The person to whom or to whose order the amount stated in Bill of Exchange is to be paid.

5. Holder

- Explained while discussing promissory note.



Parties to Notes, Bills and Cheques


❖ Parties to Bill of Exchange

6. Endorser

- Explained while discussing promissory note.

7. Endorsee

- Explained while discussing promissory note.



Parties to Notes, Bills and Cheques

❖ Parties to a Cheque:

1. Drawer

- The person who draws/ writes a cheque is called the drawer. (Account Holder)

2. Drawee

- The person who is directed through a cheque to pay the specified amount is called the drawee, however in case of a cheque, drawee must always be a bank.

Parties to Notes, Bills and Cheques

❖ Parties to a Cheque:

3. Payee

- Explained while discussing promissory note.

4. Holder

- Explained while discussing promissory note.

5. Endorser

- Explained while discussing promissory note.

6. Endorsee

- Explained while discussing promissory note.

Parties to Notes, Bills and Cheques

❖ Holder:

- The scope of the holder is contained in section 8 of the negotiable instrument 1881 which is reproduced below:

"Holder"--- The "holder" of a promissory note, bill of exchange or cheque means the payee or endorsee who is in possession of it or the bearer thereof but does not include a beneficial owner claiming through a benamidar. (Sec 8)

Parties to Notes, Bills and Cheques

❖ Holder: Contd..

■ In order to be called a ‘Holder’, the person must satisfy the following two conditions:

1. He must be entitled to the possession of the instrument in his own name
2. He must be entitled to receive or recover the amount due thereon from the parties liable thereto

Parties to Notes, Bills and

❖ **Holder in Due Course:** **Cheques**

- Holder in due course has been explained in section 9 of the Act, which is reproduced below:
- **"Holder in due course"** Sec.9--- "Holder in due course" means any person who for consideration becomes the possessor of a promissory note, bill of exchange or cheque if payable to bearer, or the payee or endorsee thereof, if payable to order, before it became overdue, without notice that the title of the person from whom he derived his own title was defective.

Parties to Notes, Bills and Cheques

Conditions for a person to be called 'Holder in Due Course':

- He must be holder
- He obtains the instrument for valuable consideration
- He must become the holder of the instrument before maturity
- he must have obtained the instrument in good faith
- He must take the instrument complete and regular on the face of it.

Parties to Notes, Bills and Cheques

- ❖ **Acceptor's liability to the Holder in Due Course when endorsement forged: Sec 41**
 - An acceptor of a bill of exchange already endorsed is not relieved from liability by reason that such endorsement is forged, if he knew or had reason to believe the endorsement to be forged when he accepted the bill.

Cheques

❖ Privileges of a holder in due course

■ In case of Inchoate stamped instruments:

-- An inchoate stamped instrument can be completed by the transferee/ holder in due course and his right is not affected that the instrument was not bearing the required stamps at the time he acquired the instrument.

■ Prior parties liable to holder in due course:

Sec 36

-- Every prior party to a negotiable instrument is liable thereon to a holder in due course until the instrument is duly satisfied.

Parties to Notes, Bills and Cheques

- ❖ Privileges of a holder in due course: contd..
 - No effect of conditional delivery: Sec 46
 - The making, acceptance or endorsement of promissory note, bill of exchange or cheque is completed by delivery, actual or constructive.
 - Holder in due Course acquires better title than that of the transferor:
 - He acquires a better title to the instrument despite of the fact that there may be defect in the title of the transferor.

Cheques

❖ Distinguishing Features between Holder and Holder in due Course.

Holder

Title of the holder shall not be good if the title of any prior parties is defective.

Holder in Due Course

Holder in due course shall have a good title even if the title of prior parties is defective. However condition is that he should obtain that title in good faith.

Parties to Notes, Bills and

Cheques

Distinguishing Features between Holder and Holder in due Course.

Holder

- Consideration is not necessary to be a holder of an instrument
- A holder does not enjoy any special privileges

Holder in Due Course

- Consideration is necessary
- Enjoys special privileges.

Cheques

Distinguishing Features between Holder and Holder in due Course.

Holder

A holder is a person who is entitled in his own name to the possession of the instrument and to recover or receive the amount due thereon from the parties.

Holder in Due Course

He is a person who has taken the instrument in good faith and for value, and also before its maturity.

Parties to Notes, Bills and Cheques

- ❖ **Liabilities of the parties to an instrument:**
 - ✓ **Liability of Drawer— sec.30**
 - ✓ **Liability of Drawee of a cheque— sec.31**
 - ✓ **Liability of maker of note and acceptor of bill— sec. 32**
 - ✓ **Liability of Endorser— sec.35**

Parties to Notes, Bills and Cheques

- ❖ **Liabilities of the parties to an instrument:**
 - **Liability of Drawer: Sec 30**
 - the drawer of a bill or cheque is bound to **compensate the holder in case dishonored** by the drawee or acceptor provided due notice of dishonour has been given or received by the drawer. **Before acceptance of a bill, drawer's liability is primary and after acceptance his liability becomes secondary to acceptor's liability.**

Parties to Notes, Bills and Cheques

- ❖ **Liabilities of the parties to an instrument:**
 - **Liability of drawee of cheque: Sec 31**
 - The drawee of a cheque having sufficient funds of the drawer in his hands properly applicable to the payment of such cheque must pay the cheque when duly required so to do, and, in default of such payment, **must compensate the drawer for any loss or damage** caused by such default

Parties to Notes, Bills and Cheques

❖ Liabilities of the parties to an instrument:

■ Liability of maker of note and acceptor of bill:

- Sec 32

- 1) In the absence of a contract to the contrary, the maker of a promissory note, by making it, and acceptor before maturity of a bill of exchange by accepting it, engages that he will pay it according to the tenor of the note or his acceptance respectively, and **in default of such payment, such maker or acceptor is bound to compensate any party to the note or bill for any loss or damage sustained by him and caused by such default.** .

Parties to Notes, Bills and Cheques

- ❖ **Liabilities of the parties to an instrument:**
 - Liability of maker of note and acceptor of bill:

Sec 32.
- (2) **The acceptor of a bill of exchange at or after maturity, by accepting it, engages to pay the amount thereof to the holder on demand.**

Parties to Notes, Bills and Cheques

- ❖ **Liabilities of the parties to an instrument:**
 - Liability of endorser: Sec 35
 - In the absence of a contract to the contrary, the **endorser of a negotiable instrument**, by indorsing it, **engages that on due presentment it shall be accepted and paid** according to its tenor and that **if it be dishonored** he will **compensate the holder** or subsequent endorser who is compelled to pay it for any loss or damage caused to him by such dishonor.

Parties to Notes, Bills and Cheques

- ❖ **Liabilities of the parties to an instrument:**
 - Extent of Liability-- Rules as to compensation: sec 117:
 - The compensation payable in case of dishonour of a promissory note, bill of exchange or cheque, by any party liable to the holder or any endorsee, shall be **determined by the following rules:-**
 - the holder is entitled to the amount due upon the instrument; **together with the expenses** properly incurred in presenting, noting and protesting it.

Parties to Notes, Bills and Cheques

- ❖ **Liabilities of the parties to an instrument:**
 - Extent of Liability-- Rules as to compensation: sec 117:
 - the party entitled to compensation may draw a bill upon the party liable to compensate him, payable at sight or on demand, for the amount due to him, together with all expenses properly incurred by him. Such bill must be accompanied by the instrument dishonoured and the protest thereof (if any). If such bill is dishonoured, the party dishonouring the same is liable to make compensation thereof in the same manner as in the case of the original bill.



Presentment of Negotiable Instrument

❖ Presentment:

- Negotiable instrument may be presented for the following purposes:
 1. Presentment for Acceptance
 2. Presentment for Sight
 3. Presentment for Payment

Presentment of Negotiable Instrument

➤ Presentment for Acceptance: Sec 61

- A bill of exchange payable after sight must, if no time or place is specified therein for presentment, be presented to the drawee thereof for acceptance, if he can, after reasonable search, be found, by a person entitled to demand payment, within a reasonable time after it is drawn and in business hours on a business day. In default of such presentment, no party thereto is liable thereon to the person making such default

Presentment of Negotiable Instrument

- **Presentment for Acceptance: Contd..**
 - Essentials of Valid Acceptance
 - ✓ Must be in writing
 - ✓ Signed by drawee or his agent
 - ✓ Acceptance must appear on the bill
 - ✓ Accepted bill must be delivered to the holder



Presentment of Negotiable Instrument


- **Presentment for Acceptance: Contd..**
 - Who can accept the Bill
 - Drawee or his agent, in case of several drawees, all the drawees can accept
 - In case of death of the drawee, bill can be accepted by the legal representative of the deceased drawee
 - Official receiver, in case drawee declared as insolvent



Presentment of Negotiable Instrument

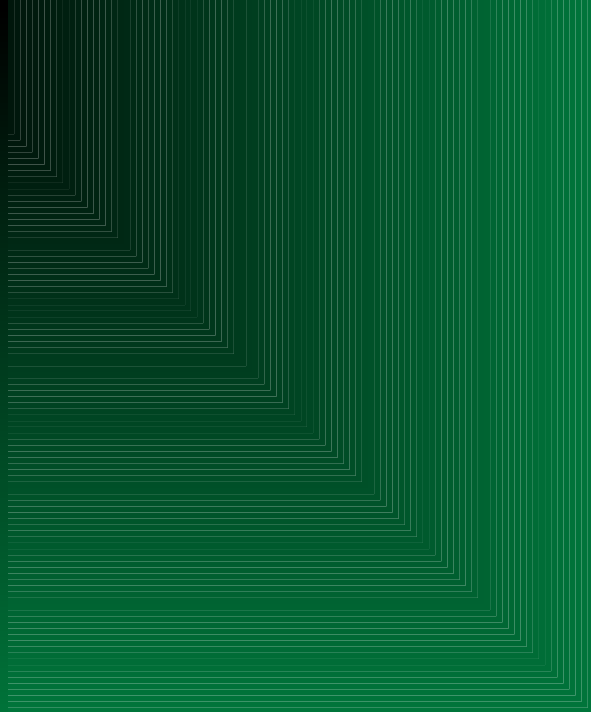
➤ Presentment for Sight: Sec 62

-- A promissory note payable at a certain period after sight, must be presented to the maker thereof for sight (if he can after reasonable search be found) by a person entitled to demand payment, within a reasonable time after it is made and in business hours on a business day. In default of such presentment, no party thereto is liable thereon to the person making such default.



Presentment for Payment: Sec 64 --Subject to the provisions of section 76, promissory notes, bills of exchange and cheques must be presented for payment to the maker, acceptor or drawee thereof respectively, by or on behalf of the holder as hereinafter provided. In default of such presentment, the other parties thereto are not liable thereon to such holder.

Section 76 underlines situations when presentment is unnecessary e.g. Drawee prevents presentment.



THANKS