

NEGOTIABLE INSTRUMENTS

(1) GOVERNING LAW

All negotiable instruments are governed by the Bills of Exchange Ordinance of 1927. Our Ordinance is a verbatim reproduction of the English statute.

(2) WHAT ARE NEGOTIABLE INSTRUMENTS?

Crouch Vs. Credit Foncier of England Ltd. (1873):

“where an instrument is by the custom of trade transferable like cash, by delivery, and is also capable of being sued upon by the person holding it, it is entitled to the name of a negotiable instrument, and the property in it passes to a transferee who has taken it for value and in good faith.”

(3) ESSENTIAL FEATURES OF A NEGOTIABLE INSTRUMENT

- (a) The property and rights in the negotiable instrument passes by delivery alone, or by delivery and endorsement. No further evidence of transfer is required.
- (b) The holder of the instrument can sue on it in his own name.
- (c) No notice need to be given to the debtor (i.e. the person who is liable to pay) in respect of the instrument.
- (d) Valuable consideration is presumed to have been given for the instrument (English law concept of consideration applicable).
- (e) The transferee of a negotiable instrument obtains good title to the instrument although the transferor's title may be defective. For example, transferee is not affected by defences such as fraud. However, to enjoy this privilege, the transferee should have received the instrument in good faith for value.

(4) NEGOTIABILITY VS. TRANSFERABILITY

- All negotiable instruments are transferable, but not all transferable instruments are negotiable.
- Transferability relates to the process of passing title in an instrument while negotiability usually relates to the quality of the title of the instrument that is passed.
- E.g. watch & a banknote
Watch: intention should be present for ownership to pass. If lost or stolen, original true owner does not lose ownership. Transferable. Non-negotiable.
Banknote – if lost or stolen and comes into the possession of a person who takes it in good faith and for value, becomes the true owner. Transferable. Negotiable.

(5) MAIN EXAMPLES OF NEGOTIABLE INSTRUMENTS

- Bills of Exchange
- Cheques
- Promissory Notes

The courts have refused to recognise the following as negotiable instruments:

- Money orders
- Postal orders
- Fixed Deposit receipts
- Share certificates
- Letters of Credit
- Bills of Lading

(6) BILLS OF EXCHANGE

- Section 3(1):

A bill of exchange is an **unconditional order** in **writing, addressed** by one person to another, **signed** by the person giving it, requiring the person to whom it is addressed 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 bearer.

- Section 3(2):

An instrument which **does not comply** with these conditions, or which orders **any act to be done in addition** to the payment of money, is **not** a bill of exchange.

- Section 3(3)

An order to pay out of a particular fund is not unconditional within the meaning of this section, but an unqualified order to pay, coupled with (a) an indication of a particular fund out of which the drawee is to reimburse himself, or a particular account to be debited with the amount, or (b) a statement of the transaction which gives rise to the bill, is unconditional.

- Section 3(4)

A bill is not invalid by reason –

- (a) that it is not dated;
- (b) that it does not specify the value given or that any value has been given therefore; or
- (c) that it does not specify the place where it is drawn, or the place where it is payable.

- “Unconditional Order”

There must be an “order”, that is something in the nature of a command, such as “Pay” or “Please pay”. A document reading “I should be pleased if you would pay” would not be a bill of exchange because those words would constitute not an order but a request. Further, the order must be “unconditional”, that is unqualified. Therefore, an order to pay out of a particular fund- such as “Pay B Rs. 500/- out of my number 2 account” – is not unconditional. The reason is that payment is made to depend upon the number 2 account having a minimum of Rs. 500/- to its credit. But if the order were to read – “Pay B Rs. 100/- and charge to my number 2 account” – it would constitute an unconditional order even though it would include an “indication” of the particular account to be debited because that indication would not be a condition precedent to the operation of the order. [See Section 3(3)]

The following judicial decisions further illustrate this requirement that “the order be unconditional”:

A simple request will not satisfy the requirements of an order. *Hamilton vs. Spottiswoode (1849) E Exch 200* - The phrase “we hereby authorize you to apply on our account to the order of” was held not to be an order. That phrase did not create a clear obligation to pay. The words “I should be obliged if you would arrange to pay” will also not qualify as an order.

The order must be unconditional. An order to a banker to pay “provided the receipt form at foot hereof is duly signed” will not be a bill of exchange because the banker is ordered to pay only if a condition is fulfilled by the payee, namely signing the form before the banker can pay. It is not an unconditional order to pay (*Bavins Junior and Sims vs. London and South Western Bank Ltd [1900] 1 QB 270*)

- “In Writing”

The whole of the order in the instrument must be in writing. The word “in writing” includes what is typed, printed or written. Either ink or pencil will be sufficient.

- **“Signed by the person giving it”**

This means that the bill of exchange must be signed by the drawer (issuer). It is sufficient, however, if the bill is signed by some duly authorized person on behalf of the drawer.

It was held in the case of *Koster’s Premier Pottery Pty Ltd vs Bank of Adelaide* (1981) 28 SASR 355 that a bill is not signed by the drawer if his signature is forged or placed on the bill by someone without authority. So, forged cheques are not bills of exchange.

- **“Requiring the drawee to pay on demand”**

This requirement refers to the time of payment. The term used is pay on “demand”, which means “pay when asked or requested” (demanded).

Section 10(1) – A bill is payable on demand:

1. which is expressed to be payable on demand, or sight, or on presentation, or
2. in which no time for payment is expressed.

- **“Or at a fixed or determinable future time”**

A “determinable future time” may be a stipulated period after a date, or after sight, or after the occurrence of some event which is certain to happen. But payment cannot depend on contingency, even if the event should occur.

Banker v Efford (1873) 4 All AJR 161 – A document expressed to be payable “six days after the ship named “Sea Lion” leaves “Colombo Harbour” is not a good bill of exchange because the specified event might not happen.

Section 10(2) - where a bill is accepted or endorsed when it is overdue, it shall, as regards the acceptor who so accepts, or any endorser who so endorses it, be deemed a bill payable on demand.

Section 11(1) - a bill is payable at a determinable future time which is expressed to be payable:

- (a) at a fixed period after date or sight, or
- (b) at a fixed period after the occurrence of a specified event which is certain to happen, though the time of happening may be uncertain.

Williamson v Rider [1963] 1 QB 89 – A bill which is payable on or before a given date is bad, because the date of payment may be any date between the date of drawing and the last day for payment.

Section 11(2) – An instrument expressed to be payable on a contingency is not a bill, and the happening of the event does not cure the defect.

Pearson v Garrett (1689) 4 Mod. 242 – “when I marry X” will not satisfy the requirement of a determinable future time, even if in fact the drawer gets married.

- **“A sum certain in money”**

Section 9(1) - the sum payable is certain although it is required to be paid:

- (a) with interest;
- (b) by stated installments;
- (c) by stated installments, with a provision that upon default in payment of any installment the whole shall become due;
- (d) according to an indicated rate of exchange or according to a rate of exchange to be ascertained as directed by the bill.

Standard Bank of Canada vs. Wildey (1919) 19 SW (NSW) 384 – An order to pay a fixed sum “and all bank charges” or “and costs” is not a “sum certain”.

- **“To or to the order of a specified person or to bearer”**

The bill must be payable to:

- (a) a specified person; for example, “Pay X”; or
- (b) the order of a specified person; for example, “Pay X or order”; or
- (c) bearer, for example, “Pay bearer” or “Pay X or bearer”

Of the above (a) and (b) are “order bills” and (c) is a “bearer bill”.

A bill may be drawn payable to, or to the order of the drawer himself. Here the payee and drawer are one and the same person, as happens when a person draws a cheque payable to “self”. Again, the bill may be drawn payable to or to the order of the drawee. This might occur where a person indebted to his banker pays the bank by a cheque drawn on the bank. Payee and drawee are here the same person.

(7) CHEQUES

- Section 73 – A cheque is a bill of exchange drawn on a banker payable on demand.
- Accordingly, the same requirements that are essential to constitute a bill of exchange are required to constitute a cheque.
- There is one major difference. To constitute a cheque, the instrument must be drawn on a banker. Thus no commercial or financial institution other than a bank can pay or collect cheques. This is a major advantage and privilege that banks enjoy.

- Dual aspect of a cheque:

In practice, a cheque plays a dual role. On one hand, it is subject to the Bills of Exchange Ordinance and is considered as a negotiable instrument. On the other hand, from a banker’s stand point, it is a mandate (the cheque) issued by the bank’s customer requiring the bank to pay a stated amount to a stated party on or after the date of the cheque.

- Advantages of a cheque as a means of payment:

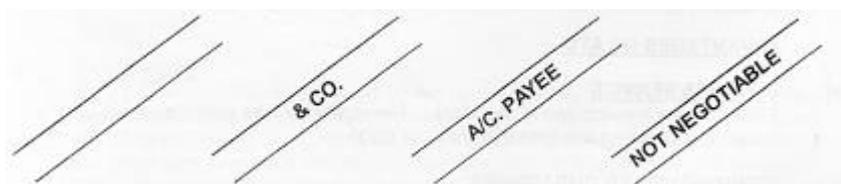
- The cheque dispenses with the need to keep cash with the attendant risks of theft and loss.
- It can be drawn for the exact amount required.
- It can be dispatched by the debtor to the creditor cheaply and safely without the risks of loss and inconvenience which can occur when settling debts in cash.
- Payment by cheque also provides a simple and authentic record of the payment of the debt. Banks retain paid cheques for over six years so that you can always get the bank to produce a cheque to prove your payment.
- Payment by cheque is generally equated to payment by cash. The cheque, when given, is a conditional payment, when honoured (by the bank) it is actual payment. *D & C Builders vs. Rees [1966] 2 QB 617.*
- English common law also treats a cheque as an item of property with value equal to the amount for which it is drawn.

- Effect of crossing a Cheque:

The crossing of the cheque is a direction to the paying bank that the cheque should be paid only to another bank. A bank can ignore the crossing and pay a crossed cheque over the counter. However, if it later turns out that the person paid was not entitled to receive that payment, the paying bank will be liable to the true owner and will also forfeit the statutory protection given by the Ordinance. This is because payment of a cheque in contravention of a crossing would be regarded as negligence by the bank.

- Types of Crossings:

1. General Crossing [Section 76 (1)]: Two parallel transverse lines either with or without the words “Not negotiable”.



2. Special Crossing [Section 76 (2)]: Where a cheque bears across its face an addition of the name of a banker with or without the words, “not negotiable”, that addition constitutes a crossing, and the cheque is crossed specially and to the banker.



3. “Not Negotiable” Crossing (Section 81): Where a person takes a crossed cheque which bears on it the words “not negotiable”, he shall not have and shall not be capable of giving better title to the cheque than that which the person from whom he took it had. The words do not restrict transferability, but transfers only the title that the transferor has. For eg: a person who has taken such a cheque from a thief, in good faith, cannot retain it against the true owner.
4. “Account Payee” Crossing: Notice to the banker that only the account of the payee should be credited.

- Who may cross a cheque (Section 77)?

A drawer, payee of the cheque or a subsequent holder of the cheque can cross it.

- Stale Cheques:

A “stale” cheque in Sri Lanka means a cheque that is more than 6 months old after the date on which it was drawn.

A customer can further limit or restrict the validity of a cheque by writing on the cheque the words, “Validity of cheque limited by thirty days” etc. Many corporate customers do this. This is a good precaution to take because cheques can get lost or get into wrong hands. When you limit the duration of a cheque’s validity there is less time for the cheque to be lost or get into wrong hands. The drawer can therefore limit the period of six months when a cheque automatically becomes stale.

(8) PROMISSORY NOTES

- Promissory notes are a type of negotiable instrument. Although a promissory note is defined in our Bills of Exchange Ordinance and certain parts of that statute is made applicable to them, strictly speaking, promissory notes are not bills of exchange. This is because promissory note ***involves only two parties, the maker of the note and the payee/bearer***, while a normal bill of exchange involves three parties, namely, (i) the drawer (ii) the drawee/ acceptor and (iii) the holder.
- A promissory note must also be distinguished from a cheque. A cheque must always be drawn on a banker, while a promissory note need not involve a bank at all.

- Section 85(1): A promissory note is an **unconditional promise** in **writing** made by **one person to another 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 bearer.
- Section 85(2): An instrument in the form of a note payable to maker's order is not a note within the meaning of this section, unless and until it is endorsed by the maker.
- A promissory note is complete only upon delivery to the payee or drawee –Section 86
- Where a note is payable on demand, it must be presented for payment within a reasonable time – Section 88(1)
- Where it is payable at a particular place, it must be presented for payment there to make the indorser of a note liable. In any other case, presentment for payment is not necessary – Section 89