CHAPTER III - PARTIES TO NOTES, BILLS AND CHEQUES

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26. Capacity to make, etc., promissory notes, etc:

Every person competent to contract may bind himself, and be bound, by making, drawing, accepting, indorsing, delivering and negotiating a promissory note, bill of exchange or cheque.

Every person capable of contracting, according to the law to which he is subject, may bind himself and be bound by the making, drawing, acceptance, indorsement, delivery and negotiation of a promissory note, bill of exchange or cheque.

Minor.--A minor may draw, indorse, deliver and negotiate such instruments so as to bind all parties except himself.

> Nothing herein contained shall be deemed to empower a corporation to make, indorse or accept such instruments except in cases in which, under the law for the time being in force, they are so empowered.

Section 26 of the Negotiable Instruments Act, 1881 links liability on a negotiable instrument to capacity to contract. Whether a person can contract is decided by "the law to which he is subject", which is generally his personal law. In India this means the person must have reached the age of majority (18 years under the Indian Majority Act, 1875), must be of sound mind, and must not be disqualified from contracting by any law (s. 11, Indian Contract Act, 1872). A person who has this capacity becomes liable on an instrument by signing it in any of the capacities the section lists: as maker of a note, drawer or acceptor of a bill, or drawer of a cheque. He also becomes liable by indorsing, delivering or negotiating it. The section then makes two qualifications. The first concerns minors. A minor can draw, indorse, deliver and negotiate an instrument, and the instrument remains valid against all the other parties to it. The minor himself is never liable, because a minor's agreement is void (*Mohori Bibee v. Dharmodas Ghose*, (1903) 30 IA 114). The proviso does not mention making or accepting, so a minor cannot be held liable as maker of a note or acceptor of a bill either. The point of the rule is that a minor's signature does not destroy the instrument's negotiability; it only excludes the minor from liability. The second concerns corporations. The section does not give a corporation any power to make, indorse or accept instruments. A corporation can do so only where its constituting law or charter authorises it. For companies, s. 22 of the Companies Act, 2013 provides that a bill of exchange, hundi or promissory note is deemed to be made, accepted, drawn or indorsed on the company's behalf if a person acting under its express or implied authority does so in the company's name. For example, A bill of exchange drawn by D on E is accepted by E and indorsed by D to M, a 16-year-old. M then indorses it to N for value. When the bill falls due, E dishonours it. N can sue E as acceptor and D as drawer, because both were competent to contract, and M's indorsement passed a good title to N. N cannot sue M, because M was a minor and is not liable on his indorsement. Similarly, if M had made a promissory note for ₹10,000 in favour of P, the note could not be enforced against M at all, since a minor cannot bind himself as maker.

27. Agency

A person competent to contract may bind himself, or be bound, through a duly authorised agent acting in his name; but an agent shall not accept or indorse bills of exchange on the principal's behalf unless specifically authorised to do so, and shall not indorse merely because he is authorised to draw.

> Every person capable of binding himself or of being bound, as mentioned in section 26, may so bind himself or be bound by a duly authorized agent acting in his name.
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> A general authority to transact business and to receive and discharge debts does not confer upon an agent the power of accepting or indorsing bills of exchange so as to bind his principal.
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> An authority to draw bills of exchange does not of itself import an authority to indorse.

Section 27 of the Negotiable Instruments Act, 1881 applies the general law of agency to negotiable instruments. Any person who has capacity to contract under s. 26 may make, draw, accept, indorse, deliver or negotiate an instrument either personally or through an agent. To bind the principal, the agent must be duly authorised and must act in the principal's name, so the instrument shows that the liability is the principal's and not the agent's. If the agent signs without indicating that he signs as agent, he may be personally liable on it (s. 28). The section then sets two limits on an agent's implied authority, because accepting or indorsing a bill creates a serious liability that can be enforced by strangers into whose hands the instrument passes. First, a general authority to carry on business and to receive and discharge debts does not include the power to accept or indorse bills of exchange so as to bind the principal; that power must be specifically given. Second, an authority to draw bills does not by itself include an authority to indorse them, since drawing and indorsing are separate acts with separate consequences. Anyone dealing with an agent on a bill must therefore check that the agent actually has the specific authority, and an unauthorised acceptance or indorsement does not bind the principal. For example, R, a cloth merchant, appoints S as manager of his shop with general authority to run the business, collect money from customers and give receipts. S accepts a bill of exchange for ₹2 lakh drawn on R by a supplier, signing "for R, S,

Manager". Because S has only a general authority to transact business and receive and discharge debts, he had no power to accept bills, so R is not liable on the acceptance. Similarly, if R had expressly authorised S only to draw bills on R's customers, S could not validly indorse those bills to a third party in R's name. If R had given S a written power of attorney specifically authorising him to accept and indorse bills, S's acceptance in R's name would bind R.

28. Liability of agent signing

An agent who signs a negotiable instrument without indicating that he signs as agent, or that he does not intend to incur personal responsibility, shall be personally liable on it.

> An agent who signs his name to a promissory note, bill of exchange or cheque without indicating thereon that he signs as agent, or that he does not intend thereby to incur personal responsibility, is liable personally on the instrument, except to those who induced him to sign upon the belief that the principal only would be held liable.

Section 28 of the Negotiable Instruments Act, 1881 deals with an agent who signs a promissory note, bill of exchange or cheque. Under s. 27, a principal can be bound by an instrument signed by an agent, but only if the agent acts within his authority. A negotiable instrument passes from hand to hand, though, and later holders rely only on what appears on its face. So the law asks the agent to make his representative capacity clear on the instrument itself. He can do this by signing with words such as "for and on behalf of [Principal]", "per pro [Principal]", or "as agent for [Principal]", or by expressly stating that he does not intend to incur personal liability. If he signs only his own name, a holder is entitled to treat him as the party liable, and he cannot later escape by proving that he was really acting for someone else. Merely adding a description after the name, such as "Manager" or "Secretary", may not be enough. Courts can treat such words as describing the person rather than showing that he signed as agent. The rule has one exception. The agent is not personally liable to those who induced him to sign in the belief that only the principal would be liable. Because that person knew the true position and caused the agent to sign, he cannot hold the agent liable. Anyone else, such as a later holder who did not know of that arrangement, can still enforce the instrument against the agent. For example,

R is the manager of S Traders and signs a cheque for ₹1,00,000 in favour of T for goods supplied to S Traders. He signs only "R" and adds nothing to show that he acts for S Traders. If the cheque is dishonoured, T, or anyone to whom T endorses it, can sue R personally on the cheque. Had R signed "For S Traders, R, Manager", only S Traders would have been liable. And if T himself had asked R to sign that way, assuring him that only S Traders would be held liable, T could not sue R personally. A later endorsee who knew nothing of this assurance still could.

29. Liability of legal representative signing

A legal representative of a deceased person who signs a promissory note, bill of exchange or cheque shall be personally liable on it, unless he expressly limits his liability to the assets received by him as such.

> A legal representative of a deceased person who signs his name to a promissory note, bill of exchange or cheque is liable personally thereon unless he expressly limits his liability to the extent of the assets received by him as such.

Section 29 of the Negotiable Instruments Act, 1881 deals with the position of a legal representative, meaning the person who represents the estate of a deceased person in law (s. 2(11), Code of Civil Procedure, 1908), such as an executor, administrator or heir. When such a person signs a negotiable instrument, the law treats the signature as his own act. He therefore becomes personally liable on it, and the holder may recover the amount from his own property, not merely from the estate he manages. The reason is that a negotiable instrument passes from hand to hand on the strength of the signatures on it. A later holder cannot be expected to find out whether the signer meant to bind only the deceased's estate. The legal representative can protect himself only by expressly limiting his liability in the instrument to the extent of the assets he has received from the deceased, for example by adding words such as "liable only to the extent of the assets of the late X received by me". The limitation must be express. Merely describing himself as "legal representative of X" or "executor of X's estate" is not enough. Where liability is limited this way, the holder can recover only out of those assets, and the representative's personal property is safe. This rule follows the same approach as s. 28, under which an agent who signs without clearly showing that he signs as agent is personally liable. For example, R's father

died owing ₹2 lakh to a supplier, S. R, as his father's legal heir, signs a promissory note in S's favour for ₹2 lakh, describing himself as "R, son and legal representative of the late T". The estate R inherited is worth only ₹1 lakh. Because R did not expressly limit his liability, he is personally liable for the full ₹2 lakh, and S may recover the balance of ₹1 lakh from R's own property. If R had instead written on the note, "My liability is limited to the assets of the late T received by me", S could recover only ₹1 lakh from those inherited assets and nothing from R's personal property.

30. Liability of drawer

The drawer of a bill of exchange or cheque shall compensate the holder when it is dishonoured, if due notice of dishonour has been given to the drawer.

> The drawer of a bill of exchange or cheque is bound in case of dishonour by the drawee or acceptor thereof, to compensate the holder, provided due notice of dishonour has been given to, or received by, the drawer as hereinafter provided.

Section 30 of the Negotiable Instruments Act, 1881 deals with the liability of the drawer, the person who makes the bill or cheque and orders the drawee to pay. When the drawer draws the instrument, he undertakes that it will be accepted (where acceptance is needed) and paid when presented, and that if it is not, he will make good the loss. His liability is secondary and conditional. It arises only when the instrument is dishonoured, either by the drawee's refusal to accept a bill (dishonour by non-acceptance, s. 91) or by the drawee's or acceptor's refusal to pay (dishonour by non-payment, s. 92). He is liable to the "holder", meaning the person entitled to possess the instrument and to recover on it in his own name (s. 8). The holder's right depends on notice of dishonour: as a rule, the holder must give the drawer due notice in the manner and within the time required by ss. 93 to 97. This tells the drawer that he is now liable and lets him protect himself against the drawee. If no proper notice is given, the drawer is discharged. Under s. 98, notice is not needed in some cases, for example where the drawer has dispensed with it, where he has countermanded payment, or where he could not suffer any damage for want of notice, such as when he had no funds with the drawee. The compensation is assessed under s. 117. It generally covers the amount due on the instrument, interest from the date of

dishonour, and the expenses caused by the dishonour. For example, A draws a bill of exchange for ₹1,00,000 on B, ordering B to pay C three months after date. A delivers it to C. On maturity C presents the bill to B, who refuses to pay. C promptly sends A a written notice of dishonour. A is then bound to compensate C for ₹1,00,000, together with interest and the expenses of dishonour. If C had not given notice, and no exception under s. 98 applied, A would be discharged from liability to C. Similarly, if A issues a cheque to D and his bank returns it for "insufficient funds", A must compensate D. Notice is not needed in that case, because A, having no funds in the bank, could suffer no damage for want of notice (s. 98(c)).

31. Liability of drawee of cheque

The drawee bank shall pay a cheque when duly presented if it holds sufficient funds of the drawer available for it, and shall compensate the drawer for any loss caused by wrongful refusal to pay.

> 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.

Section 31 of the Negotiable Instruments Act, 1881 makes the paying bank (the drawee) liable to its customer (the drawer) for wrongful dishonour of a cheque. The bank must pay when three conditions are met. First, it must hold sufficient funds of the drawer, meaning enough balance or an arranged overdraft. Second, those funds must be properly applicable to the cheque, so they must not be subject to any legal hold such as a garnishee or attachment order, a lien, or a set-off. Third, the cheque must be duly required to be paid, which means it is properly presented: during banking hours, at the right branch, in proper form, within its validity period, and not stopped by the drawer. The bank must also have had no notice of the drawer's death, insolvency or mental incapacity. If the bank refuses payment despite these conditions, its liability is only to the drawer, because the duty arises from the banker–customer contract. The payee has no claim against the bank under this section and must proceed against the drawer, including under s. 138 for dishonour. On compensation, the courts have generally held that a trader whose cheque is wrongfully dishonoured may recover substantial damages for injury to credit and reputation without proving actual loss. A

non-trader ordinarily gets nominal damages unless special loss is proved. For example, A has ₹1,00,000 in his current account with Z Bank and issues a cheque for ₹60,000 to B, a supplier. B presents it in time and in order, but because of a clerical error the bank returns it marked "insufficient funds." B stops supplying goods to A on credit, and A's business suffers. Z Bank is liable to compensate A under s. 31, since it had sufficient funds properly applicable and the cheque was duly presented. B cannot sue the bank and can look only to A for payment. If A's account had been frozen by a court attachment order, the funds would not have been "properly applicable," and the bank's refusal would not have been wrongful.

32. Liability of maker of note and acceptor of bill

The maker of a promissory note and the acceptor of a bill of exchange shall pay the amount at maturity according to the terms of the instrument, and shall compensate any party for loss caused by their failure to pay.

> In the absence of a contract to the contrary, the maker of a promissory note and the acceptor before maturity of a bill of exchange are bound to pay the amount thereof at maturity according to the apparent tenor of the note or acceptance respectively, and the acceptor of a bill of exchange at or after maturity is bound to pay the amount thereof to the holder on demand.
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> In default of such payment as aforesaid, 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.

Section 32 of the Negotiable Instruments Act, 1881 fixes the primary liability on a negotiable instrument. The maker of a promissory note, and the drawee of a bill of exchange once he accepts it (and so becomes the "acceptor"), are the principal debtors. The drawer and endorsers are liable only secondarily, if these primary parties fail to pay (ss. 30 and 35). The maker or acceptor must pay "according to the apparent tenor" of the note or acceptance. This means the terms that appear on the face of the instrument (the amount, the date of payment and the payee), and not some private understanding outside it. The time of payment depends on when the bill is accepted. If it is accepted before maturity, the acceptor must pay at maturity. Maturity is the date on which the instrument falls due, and three days of grace are added for instruments not payable on demand (ss. 22 and 23). If

the bill is accepted at or after maturity, the acceptor must pay the holder on demand. The words "in the absence of a contract to the contrary" let this liability be varied by agreement, for example by a qualified acceptance under s. 86. The second paragraph adds a duty to compensate. If the maker or acceptor defaults, he must make good the loss caused to any party to the instrument, including an endorser who had to pay the holder. That compensation usually takes the form of interest: at the rate stated in the instrument, or at 18% per annum where no rate is specified (ss. 79 and 80). For example, on 1 January A makes a promissory note promising to pay B ₹1,00,000 three months after date. The note matures on 4 April, after adding three days of grace, and A must pay that amount on that day. Suppose B has endorsed the note to C, and A fails to pay. C may recover from B as endorser. B can then sue A, as the party primarily liable, for the ₹1,00,000 plus interest at 18% per annum from the date of maturity, since no rate was stated in the note. In the same way, if D draws a bill on E, and E accepts it before it falls due, E must pay it on the due date. If E only accepts it after it has fallen due, E must pay it as soon as the holder demands payment.

33. Only drawee can be acceptor except in need or for honour

Only the drawee, a drawee in case of need, or an acceptor for honour shall bind himself by acceptance of a bill of exchange.

> No person except the drawee of a bill of exchange, or all or some of several drawees, or a person named therein as a drawee in case of need, or an acceptor for honour, can bind himself by an acceptance.

Section 33 of the Negotiable Instruments Act, 1881 settles who can become an acceptor. A bill of exchange is an order by the drawer to a named person, the drawee, to pay. Acceptance is the drawee's written assent to that order, and it makes him primarily liable on the bill. Because the order is addressed to the drawee, only he can accept it. Where a bill is addressed to several drawees, all or some of them may accept; under s. 34, if they are not partners, each one who accepts is bound only for himself. The section allows two exceptions. The first is a drawee in case of need: a person named in the bill or in an endorsement, in addition to the drawee, to be resorted to if the drawee refuses to accept or pay (s. 7). The second is an acceptor for honour: a person who, after the bill has been noted or protested for non-acceptance, accepts it with the holder's consent for the honour of a party

liable on it (s. 108). Anyone else who writes "accepted" on a bill is not bound as an acceptor, because the bill was never addressed to him and he does not fit either exception. The holder therefore cannot sue that person as an acceptor and must look to the drawee and the other parties to the bill. Whether such a stranger has some other liability, for example as an endorser or guarantor, depends on the facts and is outside the scope of this section. For example, A draws a bill for ₹1 lakh on B, payable to C. D, a friend of B, writes "accepted" across the bill and signs it, but B never accepts. Because the bill is addressed to B and not to D, D's signature does not make him liable as an acceptor, and C cannot sue him on that basis. Now suppose A had named E in the bill as a drawee in case of need. If B refuses to accept, C may present the bill to E, and if E accepts, E is bound as acceptor. Likewise, if the bill is protested for B's non-acceptance and F, with C's consent, accepts it for the honour of A, F is bound as an acceptor for honour.

34. Acceptance by several drawees not partners

Each of several drawees who are not partners shall accept a bill of exchange only for himself, and shall not accept it for another without that other's authority.

> Where there are several drawees of a bill of exchange who are not partners, each of them can accept it for himself, but non of them can accept it for another without his authority.

Section 34 of the Negotiable Instruments Act, 1881 deals with a bill of exchange drawn on two or more drawees (the persons directed to pay, s. 7) who are not partners. Each such drawee is a separate person and does not act as agent for the others, so his acceptance binds only himself. A drawee who accepts becomes liable as acceptor on the bill (s. 32). A drawee who does not accept incurs no liability, even though his name appears on it as drawee. One drawee can accept on behalf of another only if that other has authorised him to do so. Partners are excluded from this rule because a partner normally has implied authority to bind the firm in its business, which can include accepting bills in the firm's name (Indian Partnership Act, 1932, s. 19). Persons who are not partners have no such mutual agency. For the holder, this means each drawee who has accepted can be sued only on his own acceptance. If not all the drawees accept, the holder may treat the bill as dishonoured by non-acceptance and proceed against the drawer and

endorsers (s. 91). Example: D draws a bill for ₹1,00,000 on X, Y and Z, who are three independent traders and not partners. X and Y sign their acceptance, and X also signs "for Z" without Z's permission. X and Y are liable as acceptors, but Z is not bound, because X had no authority to accept for him. If Z had given X written authority to accept on his behalf, X's signature for Z would have made Z an acceptor too.

35. Liability of indorser

Every indorser shall compensate subsequent holders for loss caused by the dishonour of the instrument, provided due notice of dishonour has been given to him.

> In the absence of a contract to the contrary, whoever indorses and delivers a negotiable instrument before maturity, without, in such indorsement, expressly excluding or making conditional his own liability, is bound thereby to every subsequent holder, in case of dishonour by the drawee, acceptor or maker, to compensate such holder for any loss or damage caused to him by such dishonour, provided due notice of dishonour has been given to, or received by, such indorser as hereinafter provided.
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> Every indorser after dishonour is liable as upon an instrument payable on demand.

Section 35 of the Negotiable Instruments Act, 1881 makes the indorser of a negotiable instrument a party liable on it. A person who indorses and delivers a promissory note, bill of exchange or cheque before maturity guarantees that it will be paid when due. If the drawee, acceptor or maker dishonours it, the indorser must compensate every holder who comes after him for the resulting loss. Compensation is measured under s. 117 and covers the amount due, interest, and the expenses of notice and noting. The indorser's liability is secondary. It arises only when the party primarily liable fails to pay. It is also subject to three conditions. First, the parties may agree otherwise. Second, the indorser may expressly exclude his liability, for example by writing "sans recours" (without recourse), or make it conditional, as s. 52 allows. Third, due notice of dishonour must be given to him or received by him under ss. 91 to 98. Under s. 93, an indorser who does not receive the required notice is discharged, except in the cases where s. 98 makes notice unnecessary. The last sentence of the section deals with the indorser's position after dishonour. Once the instrument is dishonoured,

his liability is treated as liability on an instrument payable on demand. This means the holder can claim payment from him at once, without waiting for any further due date. The indorser who pays can in turn recover from the parties before him, since under s. 36 every prior party stays liable to the holder until the instrument is paid. For example, A makes a promissory note for ₹1,00,000 payable to B. B indorses and delivers it to C, and C indorses and delivers it to D, all before maturity. A fails to pay on the due date. If D promptly sends notice of dishonour to B and C, both are liable to compensate D, and D may sue either of them, or A, for the amount with interest and expenses. If D sends notice to C but not to B, B is discharged and only A and C remain liable to D. If C had indorsed the note "sans recours", C would not be liable to D at all, though B would still be liable to D because B had been given notice.

36. Liability of prior parties to holder in due course

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

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

Section 36 of the Negotiable Instruments Act, 1881 protects a holder in due course. Under s. 9, that is a person who obtains the instrument for consideration, before it becomes payable, in good faith and without any reason to believe that the title of the person transferring it was defective. The "prior parties" are everyone whose name appeared on the instrument before the holder got it: the maker of a note, the drawer of a bill or cheque, the acceptor of a bill, and every endorser before the holder. All of them are jointly and severally liable to the holder in due course. The holder may sue any one of them, some of them, or all of them together. The liability continues "until the instrument is duly satisfied," which means until it is paid in due course (s. 10) or the parties are otherwise discharged under the Act. Payment by one party discharges the parties who come after that party, but that party can still recover from those before it. The provision works with other protections for a holder in due course. Under s. 58, a defect in a prior party's title, such as fraud, theft or unlawful consideration, cannot be raised against the holder in due course. Under s. 43, lack of consideration between earlier parties is no defence against such a holder. Under s. 120, the

maker, drawer and acceptor cannot deny that the instrument was valid when made or drawn. To make the drawer and endorsers liable, the holder must still present the instrument properly and give notice of dishonour where the Act requires it (ss. 64 and 93). For example, A makes a promissory note for ₹1,00,000 payable to B or order. B endorses it to C, and C endorses it to D, who pays C full value in good faith before maturity. A, B and C are all prior parties to D. If A fails to pay on maturity and D gives due notice of dishonour, D can recover the full amount from A, B or C, singly or together, until the ₹1,00,000 is paid. Suppose B had obtained the note from A by fraud. A could raise that defence against B, but not against D, because D is a holder in due course. If C pays D, the note is satisfied as far as D is concerned, and C can then proceed against B and A, who are parties prior to C.

37. Maker, drawer and acceptor principals

The maker of a promissory note or cheque, the drawer of a bill of exchange until acceptance, and the acceptor shall be liable as principal debtors, and all other parties shall be liable as their sureties.

> The maker of a promissory note or cheque, the drawer of a bill of exchange until acceptance, and the acceptor are, in the absence of a contract to the contrary, respectively liable thereon as principal debtors, and the other parties thereto are liable thereon as sureties for the maker, drawer or acceptor, as the case may be.

Section 37 of the Negotiable Instruments Act, 1881 decides who is primarily liable on a negotiable instrument and who is liable only secondarily. The principal debtor is the party who undertakes to pay the amount. On a promissory note or cheque, that is the maker or the drawer. On a bill of exchange, the drawer is the principal debtor only until the drawee accepts the bill. Once the drawee accepts, the acceptor becomes the principal debtor, and the drawer's position becomes that of a surety. Every other party, mainly the endorsers and the drawer of an accepted bill, is liable only as a surety for the principal debtor. This means their liability is secondary and depends on the principal debtor's default. A surety becomes liable only when the instrument is dishonoured by the principal debtor and due notice of dishonour has been given to that surety (ss. 30, 35 and 93). Because these parties stand as sureties, they also get the protections a surety

has. For example, if the holder of an accepted bill makes an arrangement with the acceptor that would discharge a surety under ss. 134 or 135 of the Indian Contract Act, 1872, such as giving the acceptor more time to pay, the other parties are discharged unless the holder expressly reserves his right of recourse against them (s. 39). Among the sureties themselves, each earlier party is liable as principal to each later party (s. 38). This order of liability is only a default rule, because it applies "in the absence of a contract to the contrary". An endorser can, for instance, exclude his own liability by endorsing "sans recourse" (s. 52). For example, A makes a promissory note for ₹1,00,000 payable to B. B endorses it to C, and C endorses it to D. A, as maker, is the principal debtor, while B and C are only sureties for A. On maturity, D must present the note to A for payment. If A pays, B and C are free from liability. If A refuses to pay and D gives B and C notice of dishonour, D can recover the amount from B or C. If C pays D, C can recover from B, since B is the earlier party, and either of them can finally recover from A. The same applies to a bill. If X draws a bill on Y in favour of Z, X is the principal debtor until Y accepts. Once Y accepts, Y becomes the principal debtor, and X and any endorsers become sureties for Y.

38. Prior party a principal in respect of each subsequent party

Each prior party shall be liable as a principal debtor to every subsequent party, unless they have contracted otherwise.

> As between the parties so liable as sureties, each prior party is, in the absence of a contract to the contrary, also liable thereon as a principal debtor in respect of each subsequent party.
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> *Illustration*
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> A draws a bill payable to his own order on B, who accepts, A afterwards indorses the bill to C, C to D, and D to E. As between E and B, B is the principal debtor, and A, C and D are his sureties. As between E and A, A is the principal debtor, and C and D are his sureties. As between E and C, C is the principal debtor and D is his surety.

Section 38 of the Negotiable Instruments Act, 1881 builds on s. 37. Section 37 fixes who is primarily liable to the holder: the maker of a note or cheque, or the acceptor of a bill, is the principal debtor, and every other party (the drawer and the indorsers) is a surety for that person. Section 38 then sets the

order of liability among those sureties themselves. Each party in the chain is a principal debtor toward everyone who comes after them and a surety toward everyone who comes before them. Liability therefore runs backwards along the chain. A later party who has to pay can recover from any earlier party, but an earlier party who pays cannot recover from a later one, because the later party is only their surety. The words "in the absence of a contract to the contrary" let the parties change this order. For example, an indorser who signs "sans recourse" excludes their own liability to later parties (s. 52), and parties may agree among themselves on some other arrangement. As an example, P draws a bill on Q payable to P's own order, and Q accepts it. P then indorses the bill to R, R indorses it to S, and S indorses it to T. If Q dishonours the bill at maturity, T can sue any or all of Q, P, R and S. Suppose T recovers the full amount from S. S can then sue R, P or Q, because each of them is prior to S and so is S's principal debtor. If R pays S, R can recover from P or Q but not from S, since S is R's surety and not his principal. If P pays, P can only proceed against Q, the acceptor. Q, as the ultimate principal debtor, has no one to recover from. If R had indorsed the bill "sans recourse", R would owe nothing to S or T, and S would have to look to P or Q instead.

39. Suretyship

The holder of an accepted bill who makes with the acceptor a contract that would discharge the other parties shall keep them liable by expressly reserving his right against them.

> When the holder of an accepted bill of exchange enters into any contract with the acceptor which, under section 134 or 135 of the Indian Contract Act, 1872 (9 of 1872), would discharge the other parties, the holder may expressly reserve his right to charge the other parties, and in such case they are not discharged.

Section 39 of the Negotiable Instruments Act, 1881 applies the law of suretyship to bills of exchange. Once a bill is accepted, the acceptor becomes the principal debtor. The drawer and the endorsers stand as sureties for the acceptor in relation to the holder (s. 37 of the Act). Under the Indian Contract Act, 1872, a surety is discharged when the creditor releases the principal debtor, or does any act or omission that discharges him (s. 134). The surety is also discharged when the creditor, without the surety's

consent, compounds with the principal debtor, gives him time, or promises not to sue him (s. 135). If those rules applied without exception, a holder who gave the acceptor extra time to pay, or accepted a reduced sum in settlement, would lose his claim against the drawer and endorsers. Section 39 lets the holder avoid that result by expressly reserving his right to charge the other parties when he makes the arrangement with the acceptor. If he does so, they are not discharged and remain liable on the bill. The reservation must be express and cannot be implied. It protects the other parties as well, because the arrangement then affects only the holder's own remedy against the acceptor. A drawer or endorser who later pays the holder can still recover the amount from the acceptor. Mere forbearance to sue, without any binding contract with the acceptor, does not discharge the sureties at all (s. 137 of the Contract Act), so no reservation is needed in that case. For example, A draws a bill on B for ₹1,00,000, B accepts it, and A endorses it to C, who endorses it to D. On the due date B asks D for three more months to pay, and D agrees in writing. If D says nothing more, the binding grant of time to the acceptor discharges A and C, who are sureties, under s. 135 of the Contract Act. If B then fails to pay, D can sue only B. But if D's agreement with B states that "the holder reserves all his rights against the drawer and endorsers", A and C are not discharged. If B still defaults, D can recover from A or C, and whichever of them pays may in turn recover from B.

40. Discharge of indorser's liability

Where the holder of a negotiable instrument, without the indorser's consent, destroys or impairs the indorser's remedy against a prior party, the indorser shall stand discharged from liability to the holder.

> Where the holder of a negotiable instrument, without the consent of the indorser, destroys or impairs the indorser's remedy against a prior party, the indorser is discharged from liability to the holder to the same extent as if the instrument had been paid at maturity.
>
> *Illustration*
>
> A is the holder of a bill of exchange made payable to the order of B, which contains the following indorsements in blank:--
>
> First indorsement, "B".

Second indorsement, "Peter Williams".

Third indorsement "Wright & Co.".

Fourth indorsement, "John Rozario".

This bill A puts in suit against John Rozario and strikes out, without John Rozario's consent, the indorsements by Peter Williams and Wright & Co. A is not entitled to recover anything from John Rozario.

Section 40 of the Negotiable Instruments Act, 1881 protects an indorser's right of recourse. By indorsing an instrument, the indorser undertakes to pay the holder if it is dishonoured (s. 35), and an indorser who pays may in turn recover from the parties who signed before him, such as the drawer and prior indorsers. The holder must not interfere with that remedy. If the holder, without the indorser's consent, destroys or weakens it, for instance by striking out a prior indorsement, cancelling a prior party's signature, or releasing a prior party from liability, the indorser is discharged as if the instrument had been paid at maturity, and the holder can recover nothing from him. The rule rests on the same principle as Section 139 of the Indian Contract Act, 1872, which discharges a surety when the creditor impairs the surety's remedy against the principal debtor, because an indorser stands in a position similar to a surety for the prior parties. The protection is lost if the indorser consents to the holder's act. In the illustration to the section, A holds a bill indorsed in turn by B, Peter Williams, Wright & Co. and John Rozario. A sues John Rozario after striking out the indorsements of Peter Williams and Wright & Co. without his consent. Since Rozario can no longer proceed against them, A is not entitled to recover anything from him. Similarly, suppose a bill drawn by P in favour of Q is indorsed by Q to R, by R to S, and by S to T. On dishonour, T settles with R and releases him, without S's knowledge, and then sues S. T has destroyed S's remedy against R, so S is discharged and T cannot recover from him. If S had agreed to the release beforehand, S would remain liable.

41. Acceptor bound, although indorsement forged

An acceptor who accepts a bill knowing or having reason to believe that an indorsement on it is forged shall remain liable on the bill.

> An acceptor of a bill of exchange already indorsed is not relieved from liability by reason that such indorsement is forged, if he knew or had reason to believe the indorsement to be forged when he accepted the bill.

Section 41 of the Negotiable Instruments Act, 1881 applies to a bill that already carries a forged indorsement when it is presented for acceptance. Ordinarily a forged signature is wholly inoperative, and no title passes through it. Section 41 makes an exception that binds the acceptor. If he knew of the forgery when he accepted the bill, or had reason to believe the indorsement was forged, he cannot later escape liability by pleading that forgery. By accepting with that knowledge, he undertakes to pay the bill as it stands, and the law will not let him rely on a defect he noticed and chose to overlook. This protects later holders who take the bill relying on his acceptance. The provision is narrow. It covers only an acceptor with actual knowledge or reason to believe, so one who accepted honestly and without reason for suspicion may still raise the forgery as a defence. It also only stops the acceptor from relying on the forgery. It does not make the forged indorsement genuine against the person whose signature was forged, and that person keeps his rights as true owner. The provision fits with the related estoppels in ss. 120 and 121, which likewise stop parties from disputing matters they have already accepted. For example, A draws a bill on B, payable to C or order. D steals the bill, forges C's indorsement and negotiates it to E, who presents it to B for acceptance. B notices that the indorsement does not match C's signature, which he knows well, but accepts the bill anyway. At maturity B refuses to pay E on the ground that C's indorsement is forged. Under s. 41 he cannot take that defence, because he accepted the bill knowing or having reason to believe of the forgery, so he is liable to E. Had the forgery been skilful and B had no reason to suspect it, B could rely on the forgery and refuse payment.

42. Acceptance of bill drawn in fictitious name

The acceptor of a bill drawn in a fictitious name and payable to the drawer's order shall be liable to a holder in due course who claims under an indorsement made in the same handwriting as the drawer's signature.

> An acceptor of a bill of exchange drawn in a fictitious name and payable to the drawer's order is not, by reason that such name is fictitious, relieved from

liability to any holder in due course claiming under an indorsement by the same hand as the drawer's signature, and purporting to be made by the drawer.

Section 42 of the Negotiable Instruments Act, 1881 covers a bill signed by a person using a fictitious name as drawer and made payable to "the order of" that same drawer. Such a bill can be negotiated only by the drawer's indorsement, and since the drawer does not exist, the indorsement is also written by whoever signed the fictitious drawer's name. Ordinarily an acceptor could argue that a non-existent person cannot draw or indorse a bill, so no valid title passed. Section 42 takes that defence away. By accepting the bill, the acceptor agreed to pay it as drawn, and the acceptor is better placed than a later innocent holder to know whether the drawer is real, so the acceptor cannot avoid liability merely because the drawer's name is fictitious. This matches the estoppels in ss. 120 and 121, which prevent an acceptor from denying that the instrument was valid as originally drawn, or that the payee could indorse a bill payable to order. The protection applies only when the bill is drawn in a fictitious name and payable to the drawer's order, the indorsement is in the same handwriting as the drawer's signature and appears to be made by the drawer, and the claimant is a holder in due course, that is, one who took the bill for value, in good faith and before maturity (s. 9). If the indorsement is in a different hand, or the holder knew of the fiction, the section does not apply. For example, T writes out a bill for ₹1,00,000, signs as drawer under the made-up name "Ramesh Traders", addresses it to A, and makes it payable to "the order of Ramesh Traders". A accepts the bill. T then indorses it in the same name and handwriting and sells it to H, who pays full value without knowing the drawer is fictitious. When A refuses payment at maturity on the ground that "Ramesh Traders" does not exist and the indorsement is therefore worthless, s. 42 bars that defence and A must pay H. If, however, the indorsement had been in a different handwriting from the drawer's signature, or if H had known that "Ramesh Traders" was a sham, A could raise the defence.

43. Negotiable instrument made, etc., without consideration

An instrument made, drawn, accepted, indorsed or transferred without consideration, or for a consideration that fails, shall create no obligation of payment between the parties to that transaction. A holder for consideration, and every later holder claiming through him, may

recover the amount from the transferor for consideration or any prior party.

> A negotiable instrument made, drawn, accepted, indorsed, or transferred without consideration, or for a consideration which fails, creates no obligation of payment between the parties to the transaction. But if any such party has transferred the instrument with or without indorsement to a holder for consideration, such holder, and every subsequent holder deriving title from him, may recover the amount due on such instrument from the transferor for consideration or any prior party thereto.
>
> Exception I.--No party for whose accommodation a negotiable instrument has been made, drawn, accepted or indorsed can, if he has paid the amount thereof, recover -thereon such amount from any person who became a party to such instrument for his accommodation.
>
> Exception II.--No party to the instrument who has induced any other party to make, draw, accept, indorse or transfer the same to him for a consideration which he has failed to pay or perform in full shall recover therein an amount exceeding the value of the consideration (if any) which he has actually paid or performed.

Section 43 of the Negotiable Instruments Act, 1881 deals with instruments given without consideration or for a consideration that later fails. The law presumes that every negotiable instrument was made or transferred for consideration (s. 118(a)), but this is a rebuttable presumption. Between the immediate parties to a transaction, the party sued can defend by proving that no consideration was given or that it failed. Such an instrument is only a bare promise, so the immediate party cannot enforce it. Once the instrument reaches someone who gave value for it, the defect no longer protects the parties. A holder for consideration, and every later holder deriving title from him, may sue the person who transferred it to him for value and any party prior to that person, including the original maker. The section has two exceptions. Under Exception I, a person who has paid an accommodation instrument, that is, one signed by another person without consideration to lend credit to him, cannot recover the amount from the accommodation party. Having received the benefit, he must bear the loss himself. Under Exception II, a party who induced another to make or transfer an instrument to him in return for a consideration he has not fully paid or performed can recover only the value of the consideration he actually gave. The related case of partial absence or failure of consideration is dealt with in s. 44. For

example, A makes a promissory note for ₹1 lakh in favour of B as a gift, without consideration. B cannot sue A on it. If B indorses the note to C for ₹1 lakh paid in cash, C is a holder for consideration and can recover the amount from B or from A. A cannot raise the lack of consideration between himself and B as a defence against C. To illustrate Exception I, suppose X accepts a bill drawn by Y purely to help Y raise money, and Y later pays the bill himself. Y cannot then recover that amount from X, who signed only for Y's accommodation. To illustrate Exception II, suppose D induces E to issue a cheque for ₹50,000 to him in exchange for goods, but D supplies goods worth only ₹30,000. D can recover only ₹30,000 on the cheque.

44. Partial absence or failure of money-consideration

Where the money consideration for a promissory note, bill of exchange or cheque is partly absent or has partly failed, a holder in immediate relation with the signer shall recover from him only the amount proportionate to the consideration actually given.

> When the consideration for which a person signed a promissory note, bill of exchange or cheque consisted of money, and was originally absent in part or has subsequently failed in part, the sum which a holder standing in immediate relation with such signer is entitled to receive from him is proportionally reduced.
>
> Explanation.--The drawer of a bill of exchange stands in immediate relation with the acceptor. The maker of a promissory note, bill of exchange or cheque stands in immediate relation with the payee, and the indorser with his indorsee. Other signers may by agreement stand in immediate relation with a holder.
>
> *Illustration*
>
> A draws a bill on B for Rs. 500 payable to the order of A. B accepts the bill, but subsequently dishonours it by non-payment. A sues B on the bill, B proves that it was accepted for value as to Rs. 400, and as an accommodation to the plaintiff as to the residue. A can only recover Rs. 400.

Section 44 of the Negotiable Instruments Act, 1881 extends the rule in s. 43, under which an instrument creates no obligation between the parties to a transaction when consideration is wholly absent or wholly fails, to cases where consideration is missing only in part. If the signer received money for only part of the amount written on the instrument, he is liable only for that

part. This happens either when the consideration was "originally absent in part", because only part of the money was ever given, or when it "has subsequently failed in part", because money was given but part of the bargain later fell through. The reduction is available only against a holder who stands in immediate relation with the signer, that is, a party to the transaction in which the instrument was signed. Under the Explanation, these are the drawer and the acceptor of a bill, the maker of a note, bill or cheque and the payee, and an indorser and his indorsee, and other signers may be placed in immediate relation with a holder by agreement. A remote holder, in particular a holder in due course (s. 9), takes the instrument free of this defence and can recover the full amount. Since consideration is presumed under s. 118(a), the burden of proving the partial absence or failure lies on the signer. The second paragraph of the section applies the same rule where the consideration is not money but can be valued in money without collateral enquiry. For example, M signs a promissory note for ₹1,00,000 payable to N, but N actually lends him only ₹70,000. If N sues on the note, M can prove that ₹30,000 was never advanced, and since N as payee stands in immediate relation with M as maker, N can recover only ₹70,000. The statutory illustration works the same way: B accepted A's bill for ₹500, of which only ₹400 was for value and the remaining ₹100 an accommodation to A, so A, as drawer, can recover only ₹400 from B. If N had instead indorsed the note to R, who took it for value, in good faith and before maturity, R would be a holder in due course not in immediate relation with M, and could recover the full ₹1,00,000 notwithstanding the shortfall in consideration.

45. Partial failure of consideration not consisting of money

Where part of the non-money consideration for a negotiable instrument fails, and that part can be valued in money without collateral enquiry, the amount recoverable from the signer by a holder in immediate relation with him shall be reduced proportionately.

> Where a part of the consideration for which a person signed a promissory note, bill of exchange or cheque, though not consisting of money, is ascertainable in money without collateral enquiry, and there has been a failure of that part, the sum which a holder standing in immediate relation with such signer is entitled to receive from him is proportionally reduced.

Section 45 of the Negotiable Instruments Act, 1881 applies when a person signs a promissory note, bill of exchange or cheque in return for something other than money, such as goods, services or property, and part of that consideration fails. The section covers this non-money situation. Section 44 deals with the matching case where the consideration was money. Two conditions must be met. First, the failed part must be "ascertainable in money without collateral enquiry", which means its money value must be clear from the transaction itself, for example from an agreed unit price, and not need a separate investigation into damages or market value. Second, the reduction can be claimed only against a holder who stands "in immediate relation" with the signer. That means a party who dealt directly with him, such as the payee who supplied the defective consideration. A holder in due course, who took the instrument for value and in good faith without notice of the defect, is not affected and can recover the full amount (s. 9). Where the failed part cannot be valued without collateral enquiry, this section does not apply, and the signer's remedy is a separate claim for damages. For example, A gives B a promissory note for ₹1,00,000 in return for B's promise to supply 100 chairs at ₹1,000 each, and B delivers only 60. The failed part, 40 chairs, is worth ₹40,000 at the agreed rate, which can be worked out without any further enquiry. If B sues A on the note, A is liable for only ₹60,000. But if B had first endorsed the note to C, who took it in good faith for value without knowing about the short delivery, C could recover the full ₹1,00,000 from A, and A would have to pursue B separately. Similarly, if the consideration had been B's services whose value is disputed, the reduction could not be worked out without a separate enquiry. Section 45 would then not apply, and A would have to claim damages from B separately.

45A. Holder's right to duplicate of lost bill

The drawer shall give the holder a duplicate of a bill of exchange lost before maturity, on being given security if required.

> Where a bill of exchange has been lost before it is over-due, the person who was the holder of it may apply to the drawer to give him another bill of the same tenor, giving security to the drawer, if required, to indemnify him against all persons whatever in case the bill alleged to have been lost shall be found again.

> If the drawer on request as aforesaid refuses to give such duplicate bill, he may be compelled to do so.

Section 45A of the Negotiable Instruments Act, 1881 protects the holder of a bill of exchange that is lost before it is overdue, that is, before it matures for payment. A holder usually needs the instrument itself to present it for acceptance or payment and to enforce it. Losing it would leave the holder unable to realise the amount, even though the debt behind the bill still exists. The section therefore lets the person who was the holder at the time of loss ask the drawer for another bill "of the same tenor", meaning one with the same amount, the same date of maturity and the same terms as the lost bill. The drawer is also protected. If the lost bill turns up again, for example in the hands of a holder in due course, the drawer could be made to pay twice. For that reason the drawer may ask the applicant for security, such as an indemnity bond or a surety, against all claims that may arise if the original bill is found. Once the holder offers this security, the drawer cannot refuse without good reason. If he does refuse, the holder can go to court to compel him to issue the duplicate. The right applies only where the bill was lost before it became overdue. Once a bill is overdue, the holder's remedy lies in a suit on the debt or on the lost instrument, not in a duplicate. For example, A draws a bill of exchange for ₹1,00,000 on B, payable three months after date, in favour of C. One month later, before the bill matures, C loses it while travelling. C may ask A to issue a fresh bill for ₹1,00,000 on the same terms and with the same due date. A may insist that C first sign an indemnity bond, backed by a surety, promising to reimburse A if the lost bill is later presented by someone else. If C gives this security and A still refuses to issue the duplicate, C may sue A and obtain an order directing A to issue it. If the bill had been lost after its due date had passed, C could not claim a duplicate under s. 45A and would have to pursue his other legal remedies.