

## CHAPTER -18

# BILLS OF EXCHANGE

### Definition of bill of exchange

According to Indian Negotiable Instrument Act, 1881 -

"A Bill of Exchange is an instrument in writing, an unconditional order signed by the maker directing to pay a certain sum of money only to the order of a certain person or to the bearer of the instrument."

### Characteristics or Features of Bills of Exchange -

On the basis of the above definition following are the main characteristics of bill of exchange.

1. A bill of exchange must be in writing.
2. It must contain an order and not a request) to make payment.
3. The order must be unconditional,
4. The amount of bill of exchange must be definite.
5. The date of payment must be a fixed one.
6. It must be signed by the maker (drawer) of the bill.
7. It must be signed by the acceptor (drawee).
8. The amount mentioned in the bill is payable either on demand or on the expiry of a fixed period.
9. The amount is payable either to the bearer of the bill or to a specified person or to his order.
10. It bears stamps according to its amount or is drafted on a stamped paper of the court.

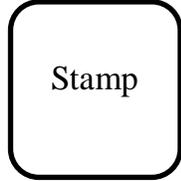
**Parties to a bill of exchange** -There are three parties to a bill of exchange:

- (1) **Drawer:** He is the seller or creditor entitled to receive money from someone. He writes or draws the bill and is known as drawer. The bill of exchange is signed by the drawer of the bill.
- (2) **Drawee or Acceptor:** He is the purchaser or the debtor on whom the bill is drawn and who is liable to pay the amount mentioned in the bill. He accepts to pay the amount by writing the word "Accepted" on the bill and then signs it A bill is called a draft before it is accepted.
- (3) **Payee:** The person to whom the payment is to be made is called payee. The drawer himself or a third party may be the payee of the bill. The drawer will be the payee of the bill, if he retains the bill till the date of maturity and receives the payment.

### SPECIMEN OF A BILL OF EXCHANGE

New Delhi  
1st July, 2019

Rs.5,00,000



Two months after date, pay to me or my order, the sum of Rupees  
Five Lac only, for value received.

(Signed)  
KarunaSagar  
1304, Green Park,  
New Delhi

Accepted  
(Signed)  
Prem Kishore  
13, Lal Bag  
Jaipur

The bank may also be the payee of the bill if the bill is discounted from the bank. In case the bill is endorsed by endorsee will be the payee of the bill. As such, the drawer himself or the bank or the endorsee may be the payee of the bill.

#### Advantages of Bills of Exchange:

- (1) **Helpful in the purchase and sale of goods on credit** - A bill of exchange serves as a written evidence of debt. It is a proof that the purchaser of goods (or the acceptor of the bill) owes the amount written in it. As such the goods can be sold on credit without difficulty.
- (2) **Legal Document-** It is a valid document in the eyes of law. If the drawee fails to make its payment, it would be easier to recover the amount legally in comparison to a verbal promise.
- (3) **Discounting Facility** -The holder of a bill need not wait till the due date of the bill to receive its payment as he can easily turn it into cash by discounting it from the bank before its due date.
- (4) **Endorsement Possible** - A bill of exchange can be easily transferred from one person to another in settlement of debts as it is a negotiable instrument.
- (5) **Relief from sending reminders** - The seller need not approach the purchaser time and again to demand the payment because the date of payment is fixed and written on the bill of exchange.

- (6) **Helpful in planning cash operations** - The seller knows the time when he would receive the money and, as such, he can plan his cash operations accordingly.
- (7) **Convenient means of making foreign payment** - Bills of Exchange enable the firms to receive and make payments in case of foreign trade also. It avoids the trouble and risk of transmitting the foreign currency from one place to another.
- (8) **Saving of money in circulation** - A bill of exchange performs the functions of money. By making payment through bills, the money in circulation will not be used and hence results in the saving of wear and tear in the currency in circulation.
- (9) **Convenience for the purchaser** - By accepting a bill, a purchaser gets time to make the payment. As such, he can purchase more goods and increase his business. Moreover, he cannot be called upon to make the payment at a date earlier than the date fixed in the bill.

Due to these advantages, bills of exchange have become extremely popular device for the grant of credit in business.

A bill of exchange closely resembles another document called the "Promissory

**Promissory Note**- Sometimes, the purchaser of the goods or debtor himself write a note, signs it and gives it to the seller of the goods. It is called a 'Promissory Note'. According to Indian Negotiable Instrument Act, "A Promissory Note is an instrument in writing (not being a bank note or a currency note) containing an unconditional undertaking signed by the maker to pay a certain sum of money to, or to the order of a certain person.

**Features:**

- (1) It must be in writing.
- (2) There must be a promise to pay a certain sum of money in it. For example, "owe you rupees ten thousand" is not a promissory note because it is merely an acknowledgement of debt and there is no promise to pay.
- (3) The promise to make payment must be unconditional. For example, "I promise to pay 10,000 as soon as possible" is not a promissory note because it is not unconditional.
- (4) The amount to be paid must be specified (definite).
- (5) It must be signed by the maker or promisor.
- (6) The name of the payee must be mentioned in it.
- (7) The promissory note cannot be made payable to bearer.
- (8) It must be stamped according to its value.

**Parties to a Promissory Note**- There are two parties to a promissory note

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- (1) **Maker-** He is the person who writes a promissory note and signs it. In the above specimen from of promissory Note, Prem Kishore
- (2) **Payee -** He is the person who is entitled to get the payment .In the above case, KarunaSagar is the payee. is entitled to the payment.

There is no acceptor in case of a promissory note because the maker himself is liable to pay the amount

### SPECIMEN OF A BILL OF PROMISSORY NOTE

Rs.5,00,000	<div style="border: 1px solid black; border-radius: 10px; width: 40px; height: 40px; margin: 0 auto; display: flex; align-items: center; justify-content: center;">Stamp</div>	<p style="text-align: right;">Jaipur 1st July, 2019</p> <p>Two months after date, I promise to pay Sh. KarunaSagaror my order, the sum of Rupees Five Lac only, for value received.</p> <p style="text-align: right;">(Signed) PremKishor 13, LalBagh, Jaipur</p>
<p>To, KarunaSagar 1304, Green Park New Delhi</p>		

#### Distinction between a bill of Exchange and a Promissory Note

Basic of Distinction	Bill of Exchange	Promissory Note
1. Parties	There may be three parties to it, viz, the drawer, the acceptor and the payee.	There are only parties to it the marker who draws the note and signs it and the payee to whom the amount is payable.
2. Drawer	It is drawn by the creditor.	It is drawn by the debtor.
3. Order and Promise	It is an order to make payment.	It is a promise to make payment.
4. Acceptance	It needs acceptance by the drawee.	It does not need acceptance.

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5. Liability	The liability of the drawer is secondary. He will be liable only if the acceptor does not pay.	The liability of the drawer (maker) is primary.
6. Payee	Drawer can be the payee of the bill.	Maker cannot be the payee of it.
7. Noting	It is better to get it noted in case of dishonour.	Noting is not necessary in case of a promissory note.
8. Copies	In case of local bills only one copy is prepared but in case of foreign bill three copies are prepared.	Only one copy is prepared whether it is local or foreign.
9. Stamps	There is no need of fixing the stamps on the bills payable 'on demand' but otherwise stamps would be necessary.	Stamps have to be fixed in any case.

**Date of Maturity and Days of Grace:** The date on which the payment of the bill becomes due is called the 'due date' or 'date of maturity'. In other words, the date on which the duration of the bill comes to an end is called the due date.

While calculating the due date of the bill, it is compulsory to add three days to the period of the bill. These three days are called 'Days of Grace'. For example, if a bill is drawn on 1st July, 2016 and is payable 2 months after date, its maturity date will be 4th September, 2016.

The following points are very significant for calculating the date of maturity-

- (i) If a bill falls due in those months in which there is no corresponding day, 29th, 30th or 31st dates, its maturity date will be the last date of such month. For example, if a bill was drawn on 30th January, 2017 for one month, it will become due on 28th February +3 days of grace 3rd March, 2017, because there is no 30th date in February.
- (ii) Bills drawn on 30th May or 31st May for one month will both become due on 3rd July.

### SHORT ANSWER QUESTIONS

1. Give a definition of Bill of Exchange and give its four characteristics.
2. What are the parties to a bill of exchange?
3. State any two advantages of bill of exchange.
4. what is the difference between a bill of exchange and a draft.

Ans. A bill of exchange is called a draft till its acceptance and a draft.

5. prepare an imaginary specimen of a bill of exchange.
6. Give a definition of Promissory Note and Give its four Characteristics.
7. What are the parties to a promissory note.
8. prepare an imaginary specimen of a promissory note.
9. Give four differences between a Bill of Exchange and a Promissory Note.
10. Distinguish between Bill of Exchange and promissory note on the following basis:
  - (a) Order or promise and parties
  - (b) Acceptance
  - (c) Parties
  - (d) Noting
  
11. What are the different uses available to a holder for dealing with bills receivable?
12. What is meant by 'Retiring a bill under rebate'?
13. Explain in brief the meaning of the following terms'?
  - (i) Endorsement of a bill
  - (ii) Renewal of a bill
  - (iii) Dishonor of a bill
  - (iv) Date of Maturity
  
14. Explain any three of the following:
  - (i) Retiring of a bill of exchange
  - (ii) Discounted of a bill of exchange
  - (iii) Bill sent to bank for collection
  - (iv) Noting charges
  
15. What Journal entries will be made by the drawer in his books, when: -
  - (i) a Bill is drawn;
  - (ii) a Bill is discounted; and
  - (iii) a Bill is dishonored and nothing charges paid.
  
16. What do you mean by dishonor of a bill? What entries will be made in the books of Drawer, if :-
  - (i) Bill is with the drawer himself,
  - (ii) Bill is discounted with the Bank,
  - (iii) Bill is with the endorsee, and
  - (iv) Bill is sent to the Bank for collection.
  
17. What do you mean by 'Accommodation Bill'?

18. Distinguish between an accommodation bill and a trade bill.

**VERY SHORT ANSWER QUESTIONS**

1. Name any two type of commonly used negotiable instruments.

Ans. (i) Bill of exchange (ii) Promissory Note

2. What is a bill of exchange?

3. Write two characteristics of a bill of exchange.

4. Bill of exchange is drawn by a Debtor. Is it Correct?

Ans. No. Bill of exchange is drawn by the Creditor and accepted by the Debtor.

5. Promissory Note is prepared by the Debtor and its payment is also made by him.

Do you agree?

Ans. Yes.

6. What is Promissory note?

7. Does a promissory note?

Ans. It does not require acceptance because it is already a valuable instrument. A bill Receivable requires acceptance.

8. ‘ I owe you Rs. 50,000’. Is it a promissory note?

Ans. It is not a promissory note because it is merely an acknowledgement of debt and there is no promise to pay.

9. Write one distinction between bill of exchange and promissory note.

10. distinguish between bill of Exchange and promissory Note on the basis of acceptance.

11. what is date of maturity of a bill of exchange?

Ans. The date on which the bill becomes due for payment is called date of maturity.

12. Calculate the due date of a bill of exchange written on July 13, 2017 for 30 days.

Ans. August 14, 2017

13. What are days of grace?

Or

How many days of grace are added to the period of a Bill of Exchange?

Ans. While calculating the due date of the bill, it is compulsory to add three days to the period of the bill. These three days are called ‘Days of Grace’.

14. When days of grace are not allowed?

Ans. Days of grace are not allowed when the bill is payable on demand.

15. What is discounting of the bill of exchange?

Ans. Discounting means encasing the bill before the date of its maturity or borrowing from the bank on the security of the bill. Bank deducts a certain amount of discount from the face value of the bill and pays the balance to the person discounting the bill.

16. What is endorsement?

Ans. Endorsement means transfer to the instrument to another person.

17. What is meaning of 'rebate' with reference to Bill of Exchange?

Ans. Rebate is a discount allowed by the payee to the drawee when the drawee makes payment of the bill before its due date.

18. What is meant by Nothing of Bill Exchange?

Ans. Nothing is the recording of the fact of dishonor by a Notary Public.

19. Asha drew a bill on Vipasa accepts the same. Can Vipasa endorse the bill to Sangeeta?

Ans. No. Vipasa cannot endorse the bill to sangeeta because vipasa is drawee. Only Asha, the Drawer can do so.

20. "If the acceptor of the bill refuses to pay the bill on its maturity date, it is called the retirement of the bill". Comment.

Ans. It is not retirement of the bill but is dishonor of the bill.

21. "Cancellation entry is not required when a bill is renewed." Do you agree?

Ans. No. Entries for cancellation of the old bill are passed before recording the entries of the New bill.

22. When is a bill called draft?

Ans. Before its acceptance.

### **OBJECTIVE TYPE QUESTIONS**

**(A) State the accounts to be debited or credited in the following situations:**

**Books of Drawer: -**

- (i) When a bill is sent for collection, the account to be credited is.....
- (ii) When a bill is dishonored, the account to be debit is .....
- (iii) When a discounted bill is dishonored, the account to be debited is..... And the Account to be credit is .....
- (iv) When a bill is dishonored and the noting charges are paid by the endorsee, the account to Credit is.....

**Books of Drawee: -**

- (v) While retiring a bill under rebate, the accounts to be credited are.....
- (vi) When a bill, which is presented by a bank for payment is dishonored, the account to be

credited is .....

(vii) When noting charges are paid by the bank at the time of dishonor of the bill, the drawee Credits .....account.

[Ans.: (i) B/R (ii) Acceptor's (iii) Acceptor's, Bank, (iv) Endorsee's.  
(v) Bank and Rebate on Bill, (vi) Drawer's, (vii) Drawer's.]

**(B) State whether the following statements are 'True' or 'False':**

1. Bill of exchange is an unconditional promise to pay.
2. Bill of exchange is a conditional order to pay.
3. Drawer and payee can be the same person in case of a bill of exchange.
4. There are two parties in a bill of exchange.
5. A Promissory note is drawn and signed by debtor.
6. A Promissory note has only two parties, the drawer and the payee.
7. A Promissory note cannot be made payable to the bearer.
8. Acceptance is necessary in case of a promissory note.
9. The liability of the drawer for the payment of a promissory note is primary.
10. In case of a public holiday the due date of the bill falls one day later.
11. The date of maturity of an "after date" bill is calculated from the date of drawing the bill.
12. The date of maturity of an "after sight" bill is calculated from the date of acceptance of the bill.
13. A bill from the point of view of a creditor is called a bill receivable.
14. At the time of renewal of a bill, interest account is credited in the books of the drawee.
15. When a bill is discounted or endorsed, no entry for payment of the bill is passed in the Books of the drawer.
16. No entry is passed in the books of the drawee when a bill is either discounted or endorsed.
17. When a bill is renewed, the original bill need not be cancelled.
18. In case of dishonor of bill, noting charges are initially paid by the Drawee.
19. In case of dishonor, the drawee always debit bills payable account and credits drawer's Account.
20. In case of dishonor, the drawer always debits the account of drawee whether the bill is Retained, endorsed or discounted.
21. The bill is treated as dishonored in case of insolvency of the drawee.
22. Accommodation bill are drawn without consideration.

[Ans.: True: 3,5,6,7,9,11,12,13,15,16,19,20,21,22.]

**(C) Fill up the blanks: -**

1. A Bill of Exchange has ..... parties.
2. The party which is ordered to pay the amount of bill of exchange is known as .....
3. The party which is entitled to receive the payment of bill of exchange is known as.....

4. Three days added for ascertaining the date of maturity of bill of exchange are Called.....
5. Due date of a bill of exchange drawn on 29th January 2017 for one-month will be.....
6. Due date of a bill of exchange drawn on 30th January 2017 for one-month will be.....
7. Due date of a bill of exchange drawn on 31st January 2017 for one-month will be.....
8. Due date of a bill of exchange drawn on 23rd October 2016 for 3-month will be.....
9. Due date of a bill of exchange drawn on 27th December 2015 for 2-month will be.....
10. Due date of a bill of exchange drawn on 30th June 2017 for 4-month will be.....
11. Due date of exchange is called a ..... by one who is entitled to receive its Payment.
12. A bill of exchange is called a .....by one who is liable to pay its amount.
13. Payee of a bill can get the amount of its before its due date by getting It.....
14. The person who endorses a bill of exchange is called.....
15. The person is whose favor an endorsement is made is called.....
16. When a bill of exchange is not paid on its due date, it is called .....
17. When a bill is dishonoured, it is customary to get it.....
18. The fee charged for getting the bill noted after its dishonour is called.....
19. If acceptance received from Shakshi was endorsed by us to Ruchika then on its dishonour it will be credited in our books to the account of.....

- [Ans. 1. Three                      2. Drawee                      3. Payee  
4. Days of Grace                5. 3rd March                    6. 3rd March  
7. 3rd March                      8. 25th March                    9. 1st March 2016  
10. 2nd November               11. Noted                        12. Bills Payable  
13. Discounted                    14. Endorser                      15. Endorsee  
16. Dishonour                      17. Noted                        18. Noting Charges  
19. Ruchika ]

**(D) Choose the best Alternate:**

1. What account will be credited when discounted bill is dishonoured?
  - (a) Drawee's Account
  - (b) Drawer's Account
  - (c) Bank Account
  - (d) Endorsee's Account

2. Noting Charges are ultimately borne by:

- (a) Drawer
- (b) Drawee
- (c) Payee
- (d) Bank

3. Liability for a discounted bill is a

- (a) Contingent Liability
- (b) Fixed Liability
- (c) Current Liability
- (d) None of the above

4. If the due date of a bill falls on a public holiday then the bill is due on:

- (a) One day after the due date
- (b) Public Holiday
- (c) One day before the due date
- (d) none of the above

5. Which account will be debited in the books of acceptor at the time of discharge of a bill?

- (a) Bills payable Account
- (b) Cash Account
- (c) Drawer's Account
- (d) Endorsee's Account

6. Under what circumstances the drawer and the payee is the same person, with reference to a Bill of exchange?

- (a) When the drawer discounts the bill with the banker.
- (b) When the drawer endorses the bill to a third party
- (c) When the drawer holds the bill till the date of maturity
- (d) When the drawee dishonour the bill

7. If a bill is accepted and the payment is made before the due date of maturity, the difference Between the paid amount and the bill amount will be called as.....

- (a) Interest
- (b) Discount
- (c) Rebate
- (d) Commission

8. Sohan draws a 40 days bill on Rohan on 20th January,2010. The bill matures on

- (a) March 4, 2010
- (b) February 28, 2010
- (c) March 1,2010
- (d) None of these

9. Bill at sight has a grace period of

- (a) 1 days
- (b) 2 days
- (c) 3 days
- (d) None of these

Ans.

1.(c)	2.(b)	3.(a)	4.(c)	5.(a)	6.(c)	7.(c)	8.(a)	9.(d)
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