

7. BILLS OF EXCHANGE

1. FEATURES OF PROMISSORY NOTE / BILL OF EXCHANGE

Particulars	Promissory Note	Bill of Exchange
Nature	Unconditional Undertaking to pay	Unconditional Order to pay
Parties	Maker and Payee	Drawer, Drawee and Payee
Authorisation	It is signed by the maker	It is signed by the drawer
Example	Rupee Note	Bills drawn during normal business
Liability	Liability is on the Maker	(a) Primary liability on the drawee. (b) Secondary liability on the drawer
Act	According to RBI Act a promissory note cannot be made payable to bearer. It should be properly stamped.	Negotiable Instruments Act, 1981 governs the provisions for bills of exchange.

2. CALCULATION OF DUE DATES

Related Term	<ul style="list-style-type: none"> • Sight – Means Acceptance • Grace days – 3
Specified days after sight	Count specified days from the date immediately after the date of acceptance and also include 3 grace days.
Specified days / Months after date	The Starting date shall be date of drawal
When Due date is public holiday and known before	The Due dates shall be the immediate preceding Business (Working) day
When Due date is public holiday & declared suddenly	The Due date shall be the immediate succeeding Business (Working) day

3. NO OF DAYS IN EACH MONTH

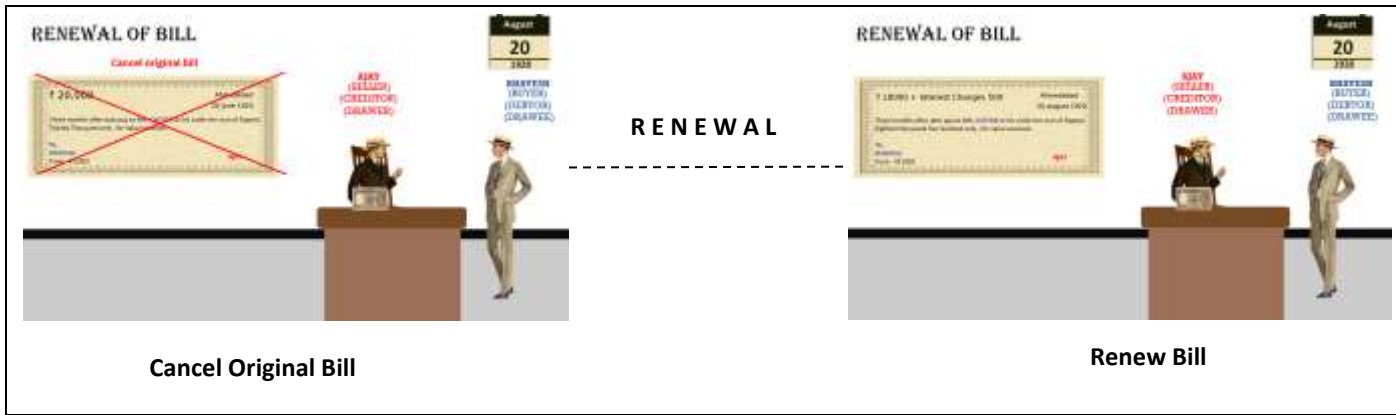
January - 31 Days	April - 30 Days	July - 31 Days	October - 31 Days
February - 28 Days (29 Days if Leap Yr.)	May - 31 Days	August - 31 Days	November - 30 Days
March - 31 Days	June - 30 Days	September - 30 Days	December - 31 Days

4. SIGNIFICANT PUBLIC HOLIDAYS

01.01. - New Year	26.01. - Republic Day	01.05 - May day
02.10. - Gandhi Jayanthi	15.08. - Independence Day	25.12.2010 - Christmas

5. SPECIAL SITUATIONS

Retirement	<ul style="list-style-type: none"> • When bills are paid before the due date. • Calculate Rebate (called discount / Interest) = $\text{Amount paid} \times \text{Int. Rate} \times \text{No. of days or Months between date of payment \& due date} \div 365 \text{ or } 12$ • 'Rebate' is generally equal to the amount of interest for the remaining period of the bill. Rebate is an expense for the party receiving the payment and gain to the acceptor of the bill making the payment.
Renewal	<ul style="list-style-type: none"> • When bills are not paid on due date and are renewed for further period. • Calculate Interest = $\text{Amount Unpaid} \times \text{Int. Rate} \times \text{No. of days or Months between date of renewal \& fresh due date} \div 365 \text{ or } 12$ • Steps for renewal of Bill <ul style="list-style-type: none"> ○ Cancellation of original bill ○ Part payment by drawee to drawer ○ Interest charged by drawer to drawee ○ Fresh bill drawn by drawer on drawee

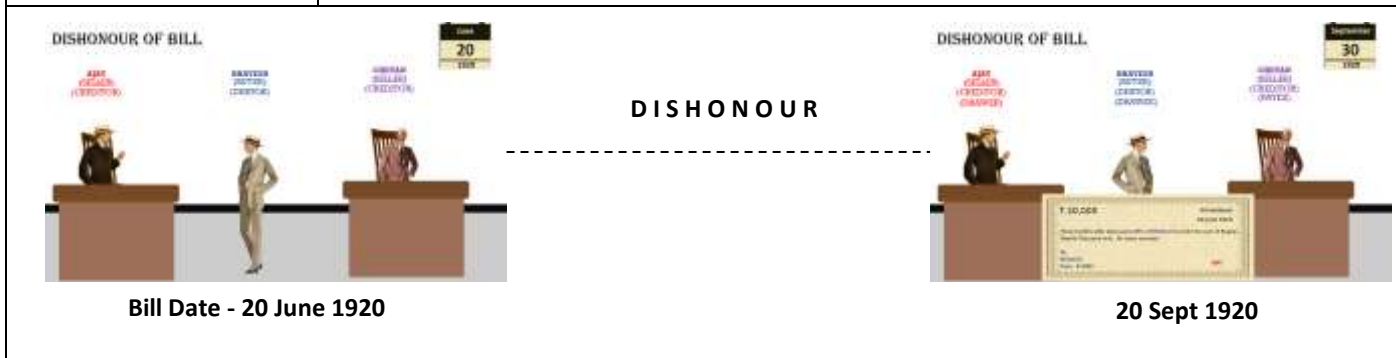


Discounting

- The bills are discounted with the banker by the drawer and Money is received from the bank.
- Discount will be deducted by the bank. $\text{Discount} = \text{Amount of Bill} \times \text{Int. Rate} \times \text{No. of days or Months between date of discounting \& due date} \div 365 \text{ or } 12$
- If the drawee does not pay, then the bank can recover the money from the drawer.
- Discount is an expense for the holder receiving the payment and gain to the bank.

Dishonour

- Acceptor refuses to honour his commitment on due date
- Recording the fact of dishonour on the bill by the 'Notary public' is called "Noting" and the amount charged by him for his services are called 'Noting Charges'.
- Dishonour of bill recorded in Bills receivable Book.



<p>Endorsement</p>	<ul style="list-style-type: none"> • When the bills receivable is transferred in favour of any other person by the drawer. • Transferor – Endorser; • Transferee – Endorsee • There is no limit on number of endorsements that can be made. On due date, the last endorsee holding the bill presents the bill to the acceptor for payment.
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BILL IS ENDORSED TO A THIRD PARTY



SAMEER
(Third Party)



CHINMAY
(SELLER)






<p>Bill sent for collection:</p>	<ul style="list-style-type: none"> • These agencies realise the bills on behalf of the drawer and charge a nominal commission or collection charges for it.
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BILL SENT FOR COLLECTION

BILL SENT FOR COLLECTION



Date - 20 June 1920

BILL SENT FOR COLLECTION



Bank Officer
30 Sept 1920

6. ACCOMMODATION BILLS ('FICTITIOUS BILLS')

- **Meaning:** Bills drawn by one trade on another, when they are in need of funds.
- **Feature:** There is no sale / purchase by one party on the other.

- **Discounting:** The drawer of the above bill will discount the bill with the bank and share the proceeds.
- **Discounting Charges :** are shared by both the parties in the ratio in which they share the amount of bill.

Situations arising in case of Accommodation Bill

- Both the parties, drawer and drawee, honour their commitments on due date i.e. drawer remits his share in accommodation and drawee honours the bill on due date.
- In spite of non-remittance from drawer, drawee honours the bill.
- Drawer remits his share in accommodation, but drawee dishonours the bill.
- Drawer does not remit his share in accommodation and drawee dishonours the bill.

7. JOURNAL ENTRIES

No	Books of Drawer	Books of Drawee
1	<i>Bill drawn duly accepted</i>	
2.	<i>i. Bill retained</i>	
	<i>ii. Bill sent to Bank for collection</i>	
	<i>iii. Bill Discounted with bank</i>	
	<i>iv. Endorsement of bill</i>	

3.	<i>Renewal of bill</i>	
	<i>i. Cancellation of old bill</i>	
	<i>ii. Part payment by drawee</i>	
	<i>iii. Drawl of new bill</i>	
4	<i>Retirement of bill</i>	
5.	<i>Honored on maturity</i>	
	<i>i. Bill retained</i>	
	<i>ii. Bill sent to bank for collection</i>	

iii.	<i>Bill Discounted with Bank</i>	
iv.	<i>Endorsement of bill</i>	
6.	<i>Dishonored on maturity</i>	
i.	<i>Noting charges / Bank charges paid</i>	
ii.	<i>Bill retained</i>	
iii.	<i>Bill sent to Bank for collection</i>	
iv.	<i>Bill Discounted with bank</i>	
v.	<i>Endorsement of bill</i>	

a. Noting charge paid by drawer

b. Noting charges paid by endorsee

7. *Insolvency of drawee :*

i. Bill retained

ii. Bill sent to bank for collection

iii. Bill discounted with bank

iv. Endorsement of Bill

v. Dividend received from insolvent's estate

8. INSOLVENCY OF ACCEPTOR (DRAWEE)

when some amount is realised from the property or estate of the insolvent acceptor, entry for cash received is passed and the balance of amount due from the insolvent acceptor is treated as bad debts.

Class Work

1. Prepare Journal entries for the following transactions in K. Katrak's books.

(i) Katrak's acceptance to Basu for ₹ 2,500 discharged by a cash payment of ₹ 1,000 and a new bill for the balance plus ₹ 50 for interest.

(ii) G. Gupta's acceptance for ₹ 4,000 which was endorsed by Katrak to M. Mehta was dishonoured. Mehta paid ₹ 20 noting charges. Bill withdrawn against cheque.

(iii) D. Dalal retires a bill for ₹ 2,000 drawn on him by Katrak for ₹ 10 discount.

(iv) Katrak's acceptance to Patel for ₹ 5,000 discharged by Patel Mody's acceptance to Katrak for a similar amount. (RTP

Nov 18)

Solution:

Books of K. Katrak
Journal Entries

	Particulars		Dr. ₹	Cr. ₹
(i)	Bills Payable Account	Dr.	2,500	
	Interest Account	Dr.	50	
	To Cash A/c			1,000
	To Bills Payable Account			1,550
	(Bills Payable to Basu discharged by cash payment of ₹ 1,000 and a new bill for ₹1,550 including ₹ 50 as interest)			
(ii)	(a) G. Gupta	Dr.	4,020	
	To M. Mehta			4,020
	(G. Gupta's acceptance for ₹ 4,000 endorsed to M. Mehta dishonoured, ₹ 20 paid by M. Mehta as noting charges)			
	(b) M. Mehta	Dr.	4,020	
	To Bank Account			4,020
	(Payment to M. Mehta on withdrawal of bill earlier received from Mr. G. Gupta)			

(iii)	Bank Account Discount Account To Bills Receivable Account (Payment received from D. Dalal against his acceptance for ₹ 2,000. Allowed him a discount of ₹ 10)	Dr. Dr.	1,990 10	2,000
(iv)	Bills Payable Account To Bills Receivable Account (Bills Receivable from Mody endorsed to Patel in settlement of bills payable issued to him earlier)	Dr.	5,000	5,000

2. Mr. B accepted a bill for ₹ 10,000 drawn on him by Mr. A on 1st August, 2017 for 3 months. This was for the amount which B owed to A. On the same date Mr. A got the bill discounted at his bank for ₹ 9,800.

On the due date, B approached A for renewal of the bill. Mr. A agreed on condition that ₹ 2,000 be paid immediately along with interest on the remaining amount at 12% p.a. for 3 months and that for the remaining balance B should accept a new bill for 3 months. These arrangements were carried through. On 31st December, 2017, B became insolvent and his estate paid 40%.

You are required to prepare Journal Entries in the books of Mr. A (RTP Nov 19)

Solution:

Journal Entries in the Books of Mr. A

Date		Particulars	LF	Dr. Amount ₹	Cr. Amount ₹
2017 August	1	Bills Receivable A/c To B (Being the acceptance received from B to settle his account)	Dr.	10,000	10,000
August	1	Bank A/c Discount A/c To Bills Receivable	Dr. Dr.	9,800 200	10,000

		(Being the bill discounted for ₹ 9,800 from bank)			
November	4	B	Dr.	10,000	
		T o Bank Account			10,000
		(Being the B's acceptance is to be renewed)			
November	4	B	Dr.	240	
		T o Interest Account			240
		(Being the interest due from B for 3 months i.e., $8000 \times 3/12 \times 12\% = 240$)			
November	4	Cash A/c	Dr.	2,240	
		Bills Receivable A/c	Dr.	8,000	
		T o B			10,240
		(Being amount and acceptance of new bill received from B)			
December	31	B A/c	Dr.	8,000	
		T o Bills Receivable A/c			8,000
		(Being B became insolvent)			
December	31	Cash A/c	Dr.	3,200	
		Bad debts A/c	Dr.	4,800	
		T o B			8,000
		(Being the amount received and written off on B's insolvency)			

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Prepare Journal Entries in the books of Mr. A

(RTP May 2018)

Solution:

Journal Entries in the Books of Mr. A

Date	Particulars	Dr.	Cr.
2017 August 1	Bills Receivable A/c To B (Being the acceptance received from B to settle his account)	Dr. 10,000	10,000
August 1	Bank A/c Discount A/c To Bills Receivable (Being the bill discounted for ₹ 9,800 from bank)	Dr. Dr. 9,800 200	10,000
Nov 4	B To Bank Account (Being the B's acceptance is to be renewed)	Dr. 10,000	10,000
Nov 4	B To Interest Account (Being the interest due from B for 3 months i.e., $8000 \times 3/12 \times 12\% = 240$)	Dr. 240	240
Nov 4	Cash A/c Bills Receivable A/c To B (Being amount and acceptance of new bill received from B)	Dr. Dr. 2,240 8,000	10,240
Dec 31	B A/c To Bills Receivable A/c (Being B became insolvent)	Dr. 8,000	8,000
Dec 31	Cash A/c Bad debts A/c To B (Being the amount received and written off on B's insolvency)	Dr. Dr. 3,200 4,800	8,000