

**CF03**

# **Law and Practice of Banking**

**10 MAY 2000**

1. Time allowed : Three (3) hours
2. Total number of questions : Six (6) questions
3. Number of questions to be answered : Five (5) questions [20 marks each]
4. Answers should be supported by references to cases and/or statutes.
5. Begin each answer to a new question on a fresh page.
6. Answer **all** questions in **English**.

## ANSWER FIVE (5) QUESTIONS ONLY

1. (a) Ahmad was recently employed as a teller in the financial institution where you work. In the induction course that he attended recently, he was taught that knowledge of law is important in the proper discharge of his duties. Assuming that you are his senior, Ahmad is now asking you to explain to him the various sources of law (that is, the legal rules that make up the law in Malaysia).

Briefly describe the sources of law.

(Hint: You may begin by stating that "The **two** main sources of Malaysian law are written law and unwritten law...") [10]

- (b) Answer "**True**" or "**False**" for each of the following:

- (i) The Privy Council is the highest court of appeal in Malaysia. [1]
- (ii) The Chief Justice of Malaysia is the supreme law of Malaysia. [1]
- (iii) Public law consists of constitutional law and criminal law. [1]
- (iv) The word "customer" is defined in section 2 of the Banking and Financial Institutions Act 1989 as a person having "some sort of an account, either a deposit or a current account or some similar relation with a bank". [1]
- (v) The debtor-creditor nature of the banker-customer relationship was described in the case *Carlill v Carbolic Smoke Ball Co. Ltd.* [1]

- (c) Ms Dolly Tan walks into Bank Wawasan Bhd and she tells Mr Muthu, the Customer Relations Officer, that she wants to open a savings account. Once the savings account is opened, a contract is entered into between Ms Dolly Tan and Bank Wawasan Bhd.

In this context, describe what a "contract" is.

(Your answer should define the word "contract" and list down at least **five** elements of a contract.) [5]

(Total:20 marks)

2. (a) In relation to contract law, state the main difference between an "offer" and an "option". [5]

- (b) Name the statutes (Acts of Parliament) which provide for the following legal principles or areas of law:

- (i) A minor is someone below the age of 18 years. [1]
- (ii) Discretionary remedies; such as injunctions. [1]
- (iii) Law of cheques. [1]
- (iv) Law governing the agent and principal relationship. [1]
- (v) Law concerning charges over land in West Malaysia. [1]

- (c) Answer "**True**" or "**False**" for each of the following:

- (i) According to section 4(1) of the Contracts Act 1950, the communication of the offer is complete when it comes to the knowledge of the person to whom it is made. [1]
- (ii) In an auction, an auctioneer inviting bids is making an offer; and when a bidder makes a bid, he is accepting the offer; and the contract of sale is made. [1]
- (iii) Section 26 of the Contracts Act 1950 provides that as a general rule, an agreement without consideration is void. [1]
- (iv) There are no exceptions to the rule that a minor has no legal capacity to enter into valid contracts. [1]

- (v) When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused. [1]
- (d) Datuk Wong maintains a current account with Bank ABC Bhd. A cheque drawn by Datuk Wong was wrongfully dishonoured by Bank ABC Bhd although there was sufficient funds in his account. Datuk Wong's lawyers advised him that, besides a claim in tort, he could also sue for damages as a remedy for breach of contract committed by Bank ABC Bhd.
- Briefly explain what the term "damages" mean. [5]  
(Total:20 marks)
3. (a) Is the sale of stock and shares governed by the Sale of Goods Act 1957? [5]  
(Note: Your answer should either be "**Yes**" or "**No**". Give reasons for your answer.)
- (b) Answer "**True**" or "**False**" for each of the following:
- (i) The Hire-Purchase Act 1967 applies in respect of hire-purchase agreements relating to all consumer goods. [1]
- (ii) Hire-purchase of motorcars, excluding taxi-cabs and hire-cars, are governed by the Hire-Purchase Act 1967. [1]
- (iii) The Hire-Purchase Act 1967 applies in contracts for the hire-purchase of goods mentioned in the Second Schedule of the said Act. [1]
- (iv) The Hire-Purchase Act 1967 does not apply in the states of Sabah and Sarawak. [1]
- (v) The Hire-Purchase Act 1967 provides that all hire-purchase agreements must be in writing. [1]
- (c) Is the law of agency applicable to bankers? Give at least **two** reasons for your answer. [5]
- (d) Answer "**True**" or "**False**" for each of the following:
- (i) **One** of the ways in which an agency may be terminated is by the agent renouncing the business of the agency. [1]
- (ii) An agent's authority may be actual or apparent. [1]
- (iii) Agency may arise by operation of law. [1]
- (iv) The Agency Act 1954 governs the law of agency. [1]
- (v) It is legally possible for a 16 year-old person to act as an agent but not as a principal. [1]  
(Total:20 marks)
4. (a) Choose the **correct word** from the words in the brackets for each of the following:
- (i) (Common law, Contractual, Tortious, Equitable, Vicarious) liability arises from the breach of a duty primarily fixed by the law; this duty is towards persons generally and its breach is redressable by an action for unliquidated damages. [1]
- (ii) The famous case wherein Lord Atkin laid down the legal principle regarding the duty of care and the "neighbour" principle is (*Winfield, Blyth, Haley, Donoghue, Latimer*) v *Stevenson* [1932] AC 562. [1]
- (iii) Section 12 of the Civil Law Act 1956 is the statutory provision on (contributory, professional, strict liability, neighbourhood, consequential) negligence. [1]
- (iv) **One** of the **three** defences to an action for defamation is (conversion, negligence, justification, slander, libel). [1]
- (v) (Conversion, Defamation, Litigation, Liability, Negligence) is the breach of a legal duty to take care which results in damages, undesired by the defendant, to the plaintiff. [1]

- (b) Bank Wang Bhd granted a RM500,000 credit facility to X-File Bhd secured by a charge over a piece of land valued by AB Firm at RM6million. When X-File Bhd defaulted in their repayment, Bank Wang Bhd proceeded with legal action, including foreclosure of the land. It was then discovered that due to their carelessness, the partners of AB Firm had provided Bank Wang Bhd with valuation of the wrong piece of land and that the actual land charged to Bank Wang Bhd (which Bank Wang Bhd had instructed AB Firm to value and of which should have been valued by AB Firm) was only worth RM100,000.

Advise Bank Wang Bhd whether it can succeed in suing AB Firm for damages in respect of the valuation. What would Bank Wang Bhd need to prove in order to succeed? [10]

- (c) What is the legal effect of the addition of the words "account payee" to the crossing on a cheque? [5]  
(Total:20 marks)

5. (a) Fill in the blanks with the **correct word(s)** in each of the following:

- (i) Malaysian land law adopts what is commonly referred to as the \_\_\_\_\_ system of registration of dealings in land. [1]
- (ii) Under the National Land Code 1965, once registered, a title or interest in land is \_\_\_\_\_ (that is, shielded or protected against attacks) except if there is fraud, misrepresentation, forgery or if the title or interest was unlawfully acquired. [1]
- (iii) Under the National Land Code 1965, dealings in land which require registration in order to be effective and valid as such are leases, charges, easements and \_\_\_\_\_ . [1]
- (iv) In Peninsular Malaysia, a \_\_\_\_\_ is a letting of land for a term exceeding **three** years and not more than **99** years in respect of the whole of the land; and **30** years in respect of part of the land. [1]
- (v) The form of caveat which may be lodged by a person with whom the document of title (or land title) has been deposited as security for a loan or an advance is called the \_\_\_\_\_ caveat. [1]

- (b) Encik Rahman borrowed RM300,000 from Bank Pinjam Bhd to finance the purchase of a piece of land in Bandar Baru Bangi, Selangor. A charge over the land was registered in favour of Bank Pinjam Bhd in 1992.

In 1993, Encik Rahman built a house on the land with money he made in the stock market. There is an Olympic-size swimming pool, central air-conditioning, elevators, a fully equipped gymnasium and home theatre in Encik Rahman's house. The house is also furnished with antique furniture and its walls are adorned with priceless paintings and art-works.

Due to heavy losses in the stock market recently, Encik Rahman defaulted in his loan repayment. Advise Bank Pinjam Bhd, whether the house, swimming pool, central air-conditioning system, elevators, gymnasium, home-theatre, antique furniture, paintings and art-works are covered by the charge in event of foreclosure. Give reasons for your answer.

(Note: Your answer should deal with the definition of "land".) [15]  
(Total:20 marks)

6. (a) Answer "**True**" or "**False**" for each of the following:

- (i) If a bill of exchange is not transferable, it cannot be negotiated. [1]
- (ii) Section 73 of the Bills of Exchange Act 1949 provides that if a cheque bears a date of more than **six** months ago, the cheque is considered as a "stale" cheque. [1]
- (iii) A cheque is not invalid by reason only that it is post-dated. [1]
- (iv) There are only **two** types of crossings recognised in the Bills of Exchange Act 1949; namely, the general crossing and the special crossing. [1]
- (v) A travellers' cheque is a type of promissory notes. [1]

- (b) In relation to bills of exchange, describe the meaning of the term “indorsement”. [5]
- (c) Ahilimah and Baharin are the **two** directors and shareholders of AB Sdn Bhd. They would like to borrow RM80,000 from XY Bank Bhd. XY Bank Bhd requested for the Memorandum and Articles of Association (M & A) of AB Sdn Bhd.

Explain the following:

- (i) What are the M & A? [5]
- (ii) Why is it important for XY Bank Bhd to obtain and examine the M & A? [5]
- (Total:20 marks)

**- END OF QUESTION PAPER -**

## OUTLINE ANSWERS

### Question 1

The most attempted question was on sources of law and “contract”. Most of the candidates answered correctly, with the majority of them scoring above 60% of the allocated marks for this question. Those who did not do well, failed to “describe” the sources of law. They merely itemised the sources. Most candidates did not cite the relevant statutory provisions.

1. (a) The two main sources of Malaysian law are written law and unwritten law.

The components of written law are:

(i) **Federal Constitution**

The Federal Constitution is the supreme law of Malaysia and it lays down the powers of the federal and state governments as well as the basic or fundamental rights of the individual.

(ii) **State Constitutions**

Each state in Malaysia possesses its own constitution governing itself; which makes provisions concerning the rulers, the executive council, the state legislative assemblies, financial provisions, state employees and the amendment of the constitution.

(iii) **Legislation**

Legislation are laws made by Parliament at federal level and by various state legislative assemblies at state levels.

(iv) **Subsidiary legislation**

Subsidiary legislation are proclamations, rules, regulations, orders, notifications, by-laws or other instruments made under any Ordinance, Enactment or other lawful authority and having legislative effect.

Unwritten law comprises:

(i) **English law**

English law is mainly found in English common law and rules of equity. Section 3(1) of the Civil Law Act 1956 provides that in Peninsular Malaysia, the Courts shall apply the common law of England and the rules of equity as administered in England on April 7, 1956. English law is only applied in the absence of local statutes on the particular subject concerned; and only that part of the English law that is suited to local circumstances will be applied.

(ii) **Judicial decisions**

Judicial decisions are also a source of law as judges follow precedents (i.e. decisions previously made by judges); applying the doctrine of binding judicial precedents. Decisions of higher courts bind lower courts and some courts are bound by their own decisions. For example, a previous decision of the Court of Appeal made in similar situations binds the High Court making a decision today.

- (b) (i) False  
(ii) False  
(iii) True  
(iv) False  
(v) False

- (c) A contract is “an agreement enforceable by law” – section 2(b) of the Contracts Act 1950. The elements of a contract are offer, acceptance of the offer, intention to create legal relations, consideration, certainty and capacity.

### Question 2

Candidates’ performance was average in relation to the first part of the question on “offer” and “option”. They however lost marks in the second part. Many candidates were unaware that the Contracts Act governs agency. The answer given was “Agency Act”. Another part where the candidates were weak was on “damages”. Most of them hardly cited the relevant statutory provisions on damages.

2. (a) An “offer” is made when one person signifies to another his willingness to do or to abstain from doing anything with a view to obtaining the assent of that other to the act or abstinence – section 2(a) Contracts Act 1950. Once an offer is accepted, an agreement is reached.

On the other hand, an option is only an undertaking to keep the offer open for a certain period of time.

- (b) (i) Age of Majority Act 1971  
(ii) Specific Relief Act 1950  
(iii) Bills of Exchange Act 1949  
(iv) Contracts Act 1950  
(v) National Land Code 1965
- (c) (i) True  
(ii) False  
(iii) True  
(iv) False  
(v) True
- (d) Section 74 of the Contracts Act 1950 provides for damages to be granted to a party as compensation for the damage, loss or injury he has suffered through a breach of contract. Damages are basically monetary compensation for loss or injury suffered by the plaintiff (Datuk Wong) as a result of breach of contract by the defendant (Bank ABC Bhd). Datuk Wong may, according to section 75 of the Contracts Act 1950, be able to recover a reasonable sum for breach of contract.

### Question 3

The question on Sale of Goods Act 1957 and the law of agency was generally well-attempted. Many candidates managed to score above 60% of the allocated marks for this question.

3. (a) Yes, the sale of stocks and shares are governed by the Sale of Goods Act 1957, besides the Contracts Act 1950. This is because the definition of “goods” provided in the Sale of Goods Act includes stock and shares. “Goods” is defined as every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale.
- (b) (i) True  
(ii) False  
(iii) False  
(iv) False  
(v) True

- (c) The law of agency is relevant to bankers. The reasons are:
- In the relationship between a banker and customer, a banker constantly acts as his customer's agent. The banker acts as an agent when collecting cheques on behalf of his customers and when carrying out his customer's standing instructions and orders.
  - Moreover, employees of financial institutions are agents of their respective financial institutions. Thus, if they commit any tort, fraud or any other act or omission in the course of their employment, the financial institution concerned would be vicariously liable to compensate their affected customers.
- (d)
- (i) True
  - (ii) True
  - (iii) True
  - (iv) False
  - (v) True

#### **Question 4**

The first part of the question where the candidates had to choose the correct words, was well-answered. The second part, however, was not answered very well. This was a question on professional negligence. This shows a lack of knowledge in this area. The question on the legal effect of the word "account payee" to the crossing on a cheque, was also not answered very well. Section 81A of the Bills of Exchange Act 1949, was not cited.

44. (a)
- (i) Tortious
  - (ii) *Donoghue*
  - (iii) contributory
  - (iv) justification
  - (v) Negligence

- (b) It is advised that Bank Wang Bhd may succeed in suing the partners of AB Firm for damages allegedly caused by the careless valuation on the grounds of professional negligence. The Bank would need to prove:
- (i) duty of care
  - (ii) breach of that duty
  - (iii) damages

The duty of care owed by a professional (e.g. a valuer) to his clients (the Bank) is stated in *Lanphier v Phipos* that the professional undertakes to bring a fair, reasonable and competent degree of care and skill. The negligence is judged by the test of the ordinary skilled man exercising and professing to have that special skill. He need not possess the highest expert skill.

The other elements to be proven in this case of professional negligence are:

- (i) The negligence had been committed in the ordinary course of business or professional affairs;
- (ii) One person must have sought information or advice from another;
- (iii) The person who gave the information or advice was not under a contractual or fiduciary obligation to give the information or advice;
- (iv) The information or advice is given in circumstances in which a reasonable man so asked would know that he was being trusted or that his skill or judgment was being relied on; *and*
- (v) The professional chooses to give that information or advice; i.e. there is no disclaimer nor a clear qualification showing that responsibility is not accepted.

Cases on professional negligence include *Neogh Soo Oh & Ors. v Rethinasamy* and *Bank Bumiputra Malaysia Bhd. v Yeoh Ho Huat*.

- (c) The legal effect of the addition of the words “account payee” to a crossing on a cheque is that the cheque shall not be transferable, but shall only be valid as between the parties thereto – section 81A, Bills of Exchange Act 1949. Thus, normally, cheques crossed with the words “account payee” are collected into the payee’s account only and cannot be transferred nor negotiated.

### **Question 5**

The worst and the least attempted question was on the definition of “land”. Only three candidates managed to pass this question. Although there was a note (hint) given in the question that the answer should deal with the definition of “land” – yet only a handful of candidates took note of this obvious hint.

5. (a) (i) Torrens  
(ii) indefeasible  
(iii) transfers  
(iv) lease  
(v) lien-holder’s
- (b) The main issue here is whether the house, swimming pool, central air-conditioning system, elevators, gymnasium, home theatre, antique furniture, paintings and art-works fall under the definition of ‘land’ under the National Land Code 1965 (NLC). If the particular item falls under the definition of ‘land’, then it would be covered under the charge as charges are taken over ‘land’.

The definition of ‘land’ is found in section 5 of the NLC which provides that ‘land’ includes:

- (a) the surface of the earth and all substances forming that surface;  
(b) the earth below the surface and all substances therein;  
(c) all vegetation and other natural products, whether or not requiring the periodical application of labour to their production, and whether on or below the surface;  
(d) all things attached to the earth or permanently fastened to any thing attached to the earth, whether on or below the surface; and  
(e) land covered by water.

Whether the house, swimming pool, central air-conditioning system, elevators, gymnasium, home theatre, antique furniture, paintings and art-works are part of land charged to Bank Pinjam Bhd would depend on whether they fall under item (d) of the definition of ‘land’ (see above). We therefore have to consider whether the house, swimming pool, air-conditioning system, elevators, gymnasium, home theatre, antique furniture, paintings and art-works are fixtures (which would form part of land) or chattels (properties which do not form part of land).

English law relating to fixtures applies in Malaysia and it provides two tests for establishing whether an item is a fixture or a chattel. These tests are the degree of annexation and the purpose or object of annexation tests – *Holland v Hodgs*.

The degree of annexation test raises a *prima facie* finding of fact by looking at the degree to which an article is affixed to the land. Under this test, an article which is affixed to land, even slightly, gives rise to a rebuttable presumption that it is part of land.

Under the second test, one enquires on the intention of the person who affixes the item. If the purpose of annexation of the item is for the better enjoyment of the land as a whole, this would strengthen the presumption established under the first test that the item is a fixture where the degree of affixation to the land is otherwise than by its own weight.

It is submitted that, applying these two tests, it is likely that the house, swimming pool, central air-conditioning system and elevators are fixtures and are covered by the charge. If the gymnasium equipment and home theatre equipment are movable items, along with the antique furniture, paintings and art-works, these are chattels and are not covered by the charge.

### Question 6

Another poorly attempted question was on M & A. company law seems to be a weak area. Candidates did not understand legal concepts, such as M & A.

6. (a) (i) True  
(ii) False  
(iii) True  
(iv) True  
(v) False
- (b) An indorsement transfers the property in the bill to the transferee and involves liability on the part of the transferor (indorser). An indorsement is essential in order to negotiate order bills. An indorsement is usually in the form of a signature at the back of the bill by the indorser. The indorsement may be made in blank or special (i.e. specifying the name of the indorsee).
- (c) (i) The Memorandum of Association defines the essential components of the structure of the company; in particular, it spells out the object with which it was formed.
- The Articles of Association are basically a set of regulations for the management of the company. Articles represent the contract or terms binding both the company and its shareholders or members; and as a contract between individual members in their capacity as members – *Rayfield v Hands*.
- (ii) It is important for the Bank to obtain and examine the M&A because it is prudent for the bank to ensure that the loan is granted for a purpose permitted by the Memorandum i.e. it is within one of the specified objects of the Memorandum. The bank needs to ensure that the loan or the borrowing is not prohibited in the Memorandum and Articles of Association.
- The Articles need to be examined to see how the company is to be managed; e.g. what is the quorum for meetings, powers of the directors, use of the common seal, etc.