

DP02

Law on Banking and Finance

8 APRIL 2003

1. Time allowed : Three (3) hours
2. Total number of questions : Five (5) questions
3. Number of questions to be answered : Four (4) questions [25 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**.
7. Blank pages are provided at the end of the question paper for rough work.

ANSWER FOUR (4) QUESTIONS ONLY

1. (a) Mr A is an officer in Bank Besar. Mr X, a security guard of the bank next door to Bank Besar, is Bank Besar's existing savings account customer with nominal balances for the past two years. Today, Mr X brings in RM600,000 in cash and instructs Bank Besar to open three trust accounts for his three minor children in equal amounts (i.e. RM200,000 each). Mr X is to be named as the trustee for all the three accounts.

Mr A's manager, who has just attended a course on "Anti-Money Laundering", alerts Mr A that he has certain legal obligations under the Anti-Money Laundering Act 2001 (AMLA).

In the context of the above scenario, answer all of the following:

- (i) What is "money laundering" as defined in AMLA? [5]
- (ii) What are Bank Besar's and Mr A's legal duties and obligations under AMLA? Your answer should describe the duties of the bank and the bank officer, offences to avoid, and the penalties involved. [10]
- (b) Is it possible for an individual or a partnership to carry on banking business in Malaysia? Give a reason for your answer. [5]
- (c) If bankers are supposed to keep customers' information confidential, how are they able to provide bankers' opinions to other banks? [5]
- (Total:25 marks)

2. (a) In relation to banker-customer relationship, define the term "customer" (including cases and examples) and explain the legal significance of being a customer. [15]

- (b) Mr and Mrs AB have been married for ten years. Mr AB has been forging his wife's signature on cheques that were paid by the bank. Mrs AB discovered the forgeries and threatened to reveal them to the bank, but agreed not to do so after Mr AB told her that the money was used to help a sick childhood friend.

One year later, Mrs AB found out that Mr AB had used the money to buy shares and had suffered big losses in the stock market. After a heated quarrel, Mr AB left home and could not be found.

Mrs AB went to the bank and revealed her husband as a forger. She demanded that the bank repay the money that has been paid on the forged cheques.

Will Mrs AB be able to recover the money from the bank? Why? [10]
(Total:25 marks)

3. (a) Define all of the following terms:
- (i) Bill of exchange [5]
 - (ii) Promissory note [5]
 - (iii) Cheque [5]
- (b) State **three** main differences between (treating each question separately):
- (i) bills of exchange and promissory notes. [5]
 - (ii) bills of exchange and cheques. [5]
- (Total:25 marks)

4. X Sdn Bhd approaches Bank Pinjam Bhd for credit facilities and offers the following assets (owned by X Sdn Bhd) as security. Describe how each of the following assets can be taken by Bank Pinjam Bhd as collateral/security:

- (a) Land (which has been issued with an individual title) with a factory built thereon [5]
- (b) Other assets such as machinery, motor vehicles and stock-in-trade [10]
- (c) Stocks and shares [10]

[Your answer should include the definition or description of the various methods of taking the securities and how (the documentation and legal procedures involved) these securities are taken.](Total:25 marks)

5. (a) Is a “negative pledge” a form of security? Why? [5]
- (b) State the differences in the procedure involved to foreclose on charges taken over land held under Registry titles and charges taken over land held under Land Office titles. [5]
- (c) In Bank Maju Bhd, RH works as an officer and KT as a clerk. KT is not authorised by Bank Maju Bhd to have access to the bank’s computers. However, RH trusts KT very much and usually lets KT use RH’s password and access codes to the bank’s computers.
- What is the statutory offence committed by RH? State the nature of the offence and the punishment for the offence. [5]
- (d) Datuk MW was recently issued with a debit card by Bank Plastik Bhd. Datuk MW is worried about unauthorised transactions and fraud that may occur.
- Describe Bank Plastik Berhad’s and Datuk MW’s liabilities for unauthorised transactions and fraud on the said debit card account as contained in the Code of Good Banking Practice and Bank Negara Malaysia Guidelines. [10]
- (Total:25 marks)

OUTLINE ANSWERS

Question 1

- Many candidates did not know the definition of “money laundering”, and thus were not able to state the legal duties and obligations of the various parties under AMLA.
- Although candidates knew that it is not possible for an individual or a partnership to carry on banking business in Malaysia, they could not support their answers with the correct reasons.
- Candidates failed to state the provisions of sections 97 and 99 of the Banking and Financial Institutions Act 1989 to support their answers on how bankers are able to provide bankers’ opinions to other banks when they are supposed to keep customers’ information confidential.

1. (a) (i) The Anti-Money Laundering Act 2001 (“AMLA”) which came into force on January 15, 2002 applies. Bank Besar, being a bank is listed in the First Schedule and therefore is a “reporting institution” – section 3 of the AMLA.

The AMLA defines “money laundering” to mean the act of a person who:

- engages, directly or indirectly, in a transaction that involves proceeds of an unlawful activity;
- acquires, receives, possesses, disguises, transfers, converts, exchanges, carries, disposes, uses, removes from or brings into Malaysia proceeds of any unlawful activity; or
- conceals, disguises or impedes the establishment of the true nature, origin, location, movement, disposition, title of, rights with respect to, or ownership of, proceeds of an unlawful activity;

where:

- as may be inferred from objective factual circumstance, the person knows or has reason to believe, that the property is proceeds from any unlawful activity; or
- in respect of the conduct of a natural person, the person without reasonable excuse fails to take reasonable steps to ascertain whether or not the property is proceeds from any unlawful activity.

- (ii) “Unlawful activity” means any activity that is related to any serious offence or any foreign serious offence. The term “serious offence” covers the offences listed in the Second Schedule of AMLA. Bankers are to avoid committing the offence of money laundering or abetting the commission of money laundering.

Section 4 of AMLA provides for the offence of money laundering. It provides to the effect that any person who engages in, or attempts to engage in, or abets the commission of money laundering, commits an offence punishable with imprisonment for a term of up to 5 years or a RM5million fine or to both such imprisonment and fine.

Here, the officer (Mr A) should be discreetly inquiring from the security guard (Mr X) on the source of funds. The deposit of the large sum of cash is a suspicious transaction as described in BNM/GP 9. The large deposit is inconsistent with the transaction profile of the customer and from the Bank’s knowledge of the customer. Thus, the officer should file a Suspicious Transaction Report.

Section 5(1) provides that where a person in disclosing money laundering to an enforcement agency has contravened subsection 4(1) and the disclosure is made after that act, but the disclosure is made on his initiative as soon as reasonably possible; he does not commit any offence. Thus, if the officer does not disclose the suspicious transaction, he may be said to have abetted the money laundering. Upon disclosure, the officer is protected from the offence.

Pursuant to section 13 of AMLA, Bank Besar is to record transactions in RM exceeding a specified amount. Multiple cash transactions are treated as a single transaction if done in one day or such other period as specified by the competent authority.

Section 14 of the AMLA stipulates that Bank Besar is to promptly report to the competent authority (the Financial Intelligence Unit) the suspicious transaction.

Section 16 of the AMLA provides *inter alia* that Bank Besar has to also verify (by reliable means) and record details such as the identity and representative capacity when opening the new accounts for the three minor children and when performing the substantial cash transactions.

Section 17 provides that a reporting institution is to maintain records for six years from the date the account is closed or transaction completed or terminated to enable reconstruction of transactions exceeding the specified amount for six years from the date the transaction is completed or terminated. The maximum penalty is a fine of RM1 million or a jail term of one year or both such fine and imprisonment.

- (b) Section 2 of the Banking and Financial Institutions Act 1989 (BAFIA) defines the terms “bank” and “banking business”. Section 4 of the BAFIA provides that only a person licensed under section 6 of the BAFIA may carry on banking business and that banks must be public companies. Thus, although the definition of “bank” is wide enough to cover individuals, associations, societies, partnerships and corporations, it is not possible for any entity, other than a public company, to run a bank. Public company is further defined in BAFIA as having the meaning assigned thereto by the Companies Act 1965.
- (c) The customer may claim that the bank giving the opinion has committed a breach of secrecy under section 97 of BAFIA. Banks sometimes do require their customers to give a written standing authority to provide banker’s opinions when requested by third parties in order avail themselves of the permitted disclosure under section 99(1)(a) BAFIA.

Under section 99(1)(c) of BAFIA, a bank may, without a customer’s prior consent, release general information which is required by a party to a *bona fide* commercial transaction (or to a prospective *bona fide* commercial transaction) to which the customer is also a party, to assess the creditworthiness of the customer relating to that transaction. However, the information released must not enable the details of the customer’s account or affairs to be ascertained.

Question 2

- Most candidates were able to give a good definition of “customer” but they missed the second requirement of the question, which was to explain the legal significance of being a customer, which carried more marks. Candidates should read the whole question properly before attempting it.
- Most answers were good and candidates managed to cite the Greenwood case. However, some answers reflected that the candidates did not understand the statutory protection available to paying and collecting banks. For example, some candidates cited section 85 of the Bills of Exchange Act 1949, which relates to collecting banks, but the question here was on the banker’s liability as the paying bank.

2. (a) There is no statutory definition of the term “customer” in Malaysia. Section 2 of BAFIA, however, defines the term “depositor” as “a person entitled to repayment of a deposit, whether made by him or any other person.”

Generally, a person usually must have some form of account with the bank to be a customer. In *Great Western Railway Co. v London and County Banking Co. Ltd*, it was held that a person for whom the bank performs a casual service like cashing a cheque was not a customer of the bank.

A person may be regarded a customer of the bank even before opening an account with the bank. Thus, if a contract exists, a person may be a customer from the time a bank accepts instructions to collect monies from a third party, to pay part of the money to a fourth party, and to retain the balance to the customer's order, although no account is formally opened – *Woods v Martins Bank Ltd*.

The duration of the banker-customer relationship is not important – *Commissioners of Taxation v English, Scottish and Australian Bank Ltd* and *Ladbroke & Co. v Todd*. In *Oriental Bank of Malaya v Rubber Industry (Replanting Board)*, it was stated that a single transaction would suffice to make a person a customer of the bank. However, a person is not a customer if the bank performs a casual service for him – *Barclays Bank Ltd v Okenarhe* and *Tate v Wilts and Dorset Bank*.

A bank may be another bank's customer. In *Importers Company Ltd v Westminster Bank Ltd*, it was held that if a non-clearing bank regularly sends cheques to a clearing bank for clearing, the former is a customer of the latter.

The significance of a person being a "customer" is that the bank owes the person some legal obligations which include a duty of care, contractual obligations as well as statutory duties such as the duty of confidentiality as stated in section 97, BAFIA. Banks also enjoy certain privileges such as statutory protection (as found in the Bills of Exchange Act 1949) when collecting cheques on behalf of customers.

- (b) The facts in this case are similar to those in *Greenwood v Martins Bank Ltd*. In that case, it was held that the customer was breaching their duty of care to the bank if they remained silent about a forgery and thus, allowed the forger to escape. In such a situation, the customer cannot claim from the bank the money paid by the bank on the forged cheques.

Mrs AB owes a duty to the bank to notify the bank promptly of any forgeries ("Greenwood duty"). Failure to do so gives rise to estoppel. This duty of the customer was one of the duties stated in the Malaysian Supreme Court case, *United Asian Bank Bhd v Tai Soon Heng Construction Sdn Bhd*.

Question 3

- The definitions were well given, but there are still some candidates who were confused about which were negotiable instruments and the concept of transferability; some also mistook promissory note as traveller's cheque.
- Candidates should also note that one of the main differences between a bill of exchange and a cheque is that a cheque must be payable "on demand".

3. (a) (i) A bill of exchange is defined in section 3(1) of the Bills of Exchange Act 1949 as:

"[A]n unconditional order in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time a sum certain in money to, or to the order of, a specified person or to bearer."

- (ii) Section 88(1) of the Bills of Exchange Act 1949 defines a promissory note as an "unconditional promise in writing made by one person to another signed by the maker, engaging to pay, on demand or at a fixed or determinable future time, a sum certain in money to, or to the order of, a specified person or to bearer."

- (iii) The definition of a cheque is derived from reading section 73 together with section 3(1) of the Bills of Exchange Act 1949. A cheque may be defined as:

“An unconditional order in writing addressed by one person to another, who must be a banker, signed by the person giving it, requiring the banker to pay on demand a sum certain in money to, or to the order of, a specified person or to bearer.”

[Note: The answers given need not be worded exactly as per the statutory definitions above. Marks will be given so long as the points required are stated in the answers]

- (b) (i) Three main differences between bills of exchange and promissory notes are:
- Where a promissory note is payable at a particular place, it must be presented for payment at that place in order to render the maker liable. In any other case, presentment for payment is not necessary to make the maker liable. This is not the case with bills of exchange.
 - It is not necessary in the case of a foreign note to protest for dishonour; but it is essential in the case of a foreign bill.
 - Where a note payable on demand is indorsed, it must be presented for payment within a reasonable time of indorsement.
- (ii) Three main differences between bills of exchange and cheques are:
- A bill of exchange may be made payable on demand or at a fixed or determinable future time; whereas a cheque must always be made payable on demand.
 - A cheque may be crossed but a bill of exchange may not be crossed.
 - As a general rule, bills of exchange require presentment for acceptance whereas a cheque need not be accepted.

Question 4

- Some of the candidates' answers stated that the method for assets such as machinery, motor vehicles and stock-in-trade to be taken as security was hire-purchase and leasing – they overlooked the fact that a bank cannot give these types of credit facilities.
- Candidates also failed to mention scrippless shares under the Central Depository System and how such security is taken.

4. The following assets that can be taken by Bank Pinjam Bhd from X Sdn Bhd as collateral may be done as follows:

- (a) Land with a factory built thereon
A charge can be created over the land. And, as the factory built on the land falls within the definition of “land” as defined in section 5 of the National Land Code 1965, the charge over the land will cover the factory as well. A charge does not involve any ownership change but the chargee obtains certain rights over the property, such as the right to be repaid out of the sale proceeds of the property.

A statutory charge is created once the charge is registered at the Land Registry or Land Office concerned – section 243, National Land Code.

- (b) Other assets such as machinery, motor vehicles and stock-in-trade
A debenture can be created. A debenture is an instrument, usually a deed, issued by a company, as acknowledgement of a debt. Under section 4(1) of the Companies Act 1965, “debenture” includes “debenture stock, bonds, notes and any other securities of a corporation whether constituting a charge on the assets of the corporation or not.”

The debenture may incorporate fixed or floating charges. Fixed charges may cover plant and machinery, including its goodwill and its uncalled capital. A floating charge may be created over the motor vehicles and stock-in-trade. The essential characteristics of a floating charge were described in *Re Yorkshire Woolcombers Association Ltd.*

Form 34 of the Companies Act on statements of particulars of charge are to be accepted for registration under section 108, Companies Act 1965.

(c) Stocks and shares

A “share” is defined as “the interest of the shareholder in the company measured by a sum of money, for the purpose of liability in the first place, and for interest in the second, but also consisting of a series of mutual covenants entered into by all the shareholders *inter se...*” – *Borland’s Trustee v Steel Bros. & Co Ltd.* Normally, public listed shares are accepted as security.

Bank Pinjam Bhd can take a legal mortgage over the shares by requiring a Memorandum of Deposit to be executed and stamped. The Bank will require the shares to be transferred to and registered in the name of the Bank’s nominee company. The share certificates will be deposited with the Bank or lodged in the Central Depository System if they are scripless shares. In the case of scripless shares, these shares will be caused to be registered in the securities account of the lender (mortgagee) and this account is called the Pledged Securities Account – section 40, Securities Industry (Central Depositories) Act 1991.

Question 5

- Although candidates knew that a negative pledge is a form of security, they gave the wrong reasons to support their answers.
- Only a few candidates knew about the Computer Crimes Act 1997.
- Candidates’ knowledge on Bank Negara Malaysia Guideline 11 (BNM/GP11) was very poor. Hence, they were not able to describe the bank’s and customer’s liabilities for unauthorised transactions and fraud on a debit card account.

5. (a) A negative pledge is not a form of security because it is basically a legally binding promise by a borrower, such as a company, to a lender that it would not create any security over its assets in favour of another creditor. A negative pledge merely gives rise to only contractual rights against the borrower. If the borrower breaches its contractual obligations, the lender may sue for damages only. The negative pledge does not give rise to any proprietary rights.

(b) The differences in the procedure involved to foreclose on charges taken over Registry titles and charges taken over Land Office titles are that for Registry titles, the application (by filing an Originating Summons) for an order for sale by the chargee must be made to the High Court (section 256, National Land Code); whereas in the case of Land Office titles, the application (Form 16G) must be made to the Land Administrator (section 260, National Land Code)

For Registry titles, the High Court will hear the application (hearing of the Originating Summons) and then order the order for sale and provide for the sale by public auction; whereas, for Land Office titles, the Land Administrator would hold an enquiry, order the sale of the land and then provide for the sale to be by public auction – section 261, NLC.

(c) The statutory offence committed by RH as an officer of Bank Maju Bhd in giving his password and access codes to KT, his clerk, without authority is provided in section 6 of the Computer Crimes Act 1997. Section 6 makes it an offence to communicate directly or indirectly a number, code, password or other means of access to a computer to any unauthorised person.

The offence is, upon conviction, punishable with a maximum fine of RM25,000.00 or to imprisonment for a term of up to 3 years or to both.

- (d) Bank Plastik Bhd and Datuk MW's liabilities for unauthorised transactions and fraud on the debit card account are dealt with in the Code of Good Banking Practice and BNM/GP 11. Paragraph 18.3 of the said Code provides that card issuers must inform customers of their maximum liability for transactions not authorised by them in the event of misuse before the card issuer has been notified that a card has been lost or stolen or that someone else knows the PIN. This is usually stated in the cardholder's agreement entered between the issuer and the cardholder.

However, the customer will be liable for all losses if he has acted with "gross negligence", which may be construed as including failures on the part of the customer to comply with the card security precautions specified in para 16.2 of the Code if such failures have caused those losses.

Under para 14 of BNM/GP11, it is the customer's duty to notify errors in his statement of account or possible unauthorised transaction within 60 days from the date of the statement of account. Para 18, however, requires the card issuer to provide an effective and convenient means for the customer to do so.

However, the burden of proof is on the financial institution to show that the transaction was authorised – para 14(3). Para 15(3) provides that a customer is not liable for losses resulting from an unauthorised transaction occurring after he has notified the financial institution that his card has been lost, misused, stolen or that the access code security has been breached.

But if the customer has contributed to a loss resulting from an unauthorised transaction by delaying such notification, the customer is liable for the actual loss which occurred, except for:

- that portion of the loss incurred on any one day which exceeds the daily transaction limit applicable to the card; or
- that portion of the total loss incurred which exceeds the amount of funds standing in the customer's account – para 16.

The Bank is discharged from liability if it is proven that Datuk MW has breached any of the following two duties:

- directly or indirectly disclose to any person the access code of his card; or
- fail to take reasonable care to keep the access code secret – para 15(1).

Datuk MW will not be liable where the losses are:

- not attributable to or not contributed by the customer;
- caused by the fraudulent or negligent conduct of officers of or agents appointed by the financial institution; companies and other financial institutions involved in networking arrangements within Malaysia or merchants who are linked to the card system;
- relating to a card that is forged, faulty, expired or cancelled; or
- occurring before the customer has received his card – para 17, BNM/GP 11.