

**DP02**

# **Law on Banking and Finance**

**4 SEPTEMBER 2007**

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) A teller of Bank Besar Bhd alerted her officer that a 20-year old unemployed youth wants to deposit RM800,000 into his savings account which usually had low balances averaging RM200. When asked about the source of fund, the youth said that a money-changer gave the money to him and he would like to remit the money later to an individual in Indonesia.

Describe the process and the authorities involved in the process within the regulatory framework (under the Anti-Money Laundering Act 2001) if the officer decides to report this transaction to the authorities concerned. Your answer should also state the relevant statutory obligations of Bank Besar Bhd.

[10]

- (b) Mr BC is an officer with Bank Maju Bhd in Kuala Lumpur. Mr Tan Tua Man is a current and savings account holder at Bank Maju Bhd since 1980. Today, Mr Tan Tua Man's son, Mr Tan Mu Da, presents to Mr BC a power of attorney purportedly signed by his father authorising him to operate all of Mr Tan Tua Man's bank accounts.

In deciding whether to allow Mr Tan Mu Da to operate both the current and savings accounts, Mr BC seeks your advice on the following matters:

- (i) Explain what a "power of attorney" is. [5]
- (ii) Explain what a banker should do when dealing with a person acting by way of a power of attorney. [5]

- (c) ABC Enterprise is a partnership with Ah Chong, Bobby and Carrie as partners. The three partners approached Bank XYZ Bhd to open a current account. While processing the documentation for the opening of the current account, Mary, an officer with Bank XYZ Bhd, noticed that Carrie was only 17 years old.

Explain whether Mary should proceed with the opening of the current account. In your answer, advise Mary on the age requirement to become a partner. [5]

(Total:25 marks)

2. (a) On 29 April 2007 at 10.00am, Mr ZZ, an officer in Bank Baru Bhd received a phone call from Mr Whye who instructed the bank to stop payment of a cheque bearing the number 544445 payable to Mr Kon for the amount of RM9,000 issued from Mr Whye's current account. Mr ZZ advised Mr Whye that Bank Baru Bhd will only stop the payment upon receipt of written instruction from him.

Mr Whye said that he can only reach Bank Baru Bhd at about 11.00am. At 10.40am, Bank Baru Bhd's teller paid the said cheque to Mr Kon. Mr Whye arrived at Bank Baru Bhd at 11.10am with the written instruction to stop payment but he was informed that the cheque was already paid.

In relation to the above context, answer all of the following:

- (i) Should the instruction to stop payment be in writing? Explain your answer. [5]
- (ii) Is Bank Baru Bhd liable to credit back the RM9,000 to Mr Whye's current account? Explain your answer. [5]
- (iii) Can Bank Baru Bhd recover the RM9,000 from Mr Kon? Give reason(s) for your answer. [5]

- (b) Kenny maintains a current account with Bank Caring Bhd since 2001. On 21 August 2007, Kenny was badly injured in an accident and he was paralysed from the neck downwards. Kenny's current account has a credit balance of RM15,000. Kenny is now unable to sign as usual on his cheques. His wife, Lillian, informed Bank Caring Bhd that Kenny wants to withdraw the RM15,000 from his current account.

Advise Lillian how the withdrawal can be made.

[10]

(Total:25 marks)

3. (a) Encik Ali and his sister, Datin Minah, opened a joint current account at Bank BB Bhd with the mandate of operation, "Either to sign/operate the account". This joint account has a credit balance of RM100,000.
- (i) Can Puan Rokiah (Encik Ali's wife) enquire from Bank BB Bhd on the balance outstanding of that joint account? Give a reason for your answer and state the penalty for contravention, if any. [5]
- (ii) Unknown to Bank BB Bhd, Datin Minah passed away at 4.44am on 4 August 2007. On the same day at 10.30am, Bank BB Bhd allowed Encik Ali to withdraw RM99,900 from the joint account. Datuk Minta, Datin Minah's husband, informed Bank BB Bhd about Datin Minah's death only on 30 August 2007 and he demanded RM50,000 which is half of the credit balance at the point of Datin Minah's death.
- What is the legal position of Bank BB Bhd in respect to Datuk Minta's claim? [10]
- (b) In relation to cheques, answer the following:
- (i) What are **two** main duties of a collecting banker? [5]
- (ii) What are the legal effects when the words "account payee" are added to a crossing on a cheque? [5]
- (Total:25 marks)
4. Cik Mawar and Datuk Wang, directors of Mawar Wang Sdn Bhd, approached Bank CC Bhd for the following credit facilities:
- A personal housing loan of RM1million to be granted to Datuk Wang to finance the purchase of a piece of vacant land (with individual title) in Ipoh and to finance the construction of a two-storey bungalow thereon.
  - A term/fixed loan of RM3million to be granted to Mawar Wang Sdn Bhd to part-finance the construction of a commercial building. The land with individual title upon which the proposed building is to be built belonging to Datuk Wang is free from encumbrances.
- In relation to the above context, answer all of the following:
- (a) Explain how Bank CC Bhd can obtain security for the above credit facilities. Give details of how Datuk Wang and Mawar Wang Sdn Bhd can create the various securities in favour of the bank and the security documentation involved, including the steps and procedures for the perfection of the security documentation. [10]
- (b) Bank CC Bhd also requires personal guarantees to be signed by Cik Mawar and Datuk Wang. Give a reason for this requirement. [5]
- (c) In the event of default, briefly describe the various legal remedies and loan recovery efforts (in relation to securities and guarantees) which may be pursued by Bank CC Bhd. [10]
- (Total:25 marks)
5. (a) "As a general principle, the directors of a company are under a duty to act *bona fide* for the benefit of the company." Explain your answer. [10]
- (b) Define and describe debenture as a type of security. [10]
- (c) In relation to court procedures, briefly explain what "interpleader" means. [5]
- (Total:25 marks)

– END OF QUESTION PAPER –

## OUTLINE ANSWERS

The comments given in the boxes below indicate the areas of weaknesses the examiners have identified and their advice to future candidates.

### Question 1

- Candidates were unable to answer questions relating to power of attorney.

1. (a) Bank Besar Bhd, being a commercial bank licensed under the Banking and Financial Institutions Act 1989 (BAFIA) is one of the reporting institutions as defined in section 3 of the Anti-Money Laundering Act 2001 (AMLA). As RM800,000 is a substantial amount to be paid to a young unemployed man who is Bank Besar Bhd's existing savings account customer with a low credit balance (so little is known about him), the officer was right to inquire about the source of the fund. The reply given about the money-changer's involvement and the intended remittance to Indonesia are grounds for suspicion of money-laundering.

Under section 14 of the AMLA, Bank Besar Bhd has also to promptly report to the competent authority which is the Financial Intelligence Unit (FIU) of Bank Negara Malaysia (BNM) any transaction exceeding the amount specified (for cash transactions, RM50,000 and for telegraphic transfers, RM3,000); and, regardless of the amount, where the identity of person or transaction or circumstances raise suspicions that proceeds of unlawful activity are involved - UPW/GP1. The officer needs to inform his branch compliance officer, who would then lodge a Suspicious Transaction Report with Bank Besar Bhd's compliance officer. The compliance officer then decides whether to forward the Suspicious Transaction Report to the FIU of BNM – the competent authority duly appointed by the Minister of Finance.

The FIU may then channel the information regarding the suspicious transaction to the relevant enforcement agencies responsible for investigating serious offences. In this instance, BNM may be the relevant enforcement agency.

Bank Besar Bhd has to avoid liability due to money-laundering or abetting money laundering which are offences under section 4 of the AMLA.

Under section 13 of the AMLA, the bank being the Reporting Institution must record transactions exceeding a specified amount. Such records are to include the identity and address of the beneficiary of the telegraphic transfer.

As this is a substantial cash transaction, Bank Besar Bhd is to verify, by reliable means, and record identifying information using the identity card or passport, etc. as required under section 16 of the AMLA. Section 17 provides that the bank must maintain the records of such transactions for 6 years from the transaction date.

- (b) (i) A power of attorney is a formal document usually drawn up by a lawyer wherein the donor authorises the donee to act on the donor's behalf. Thus, when a person gives another person a power of attorney, it means that the person authorises that other person to act on his or her behalf. In West Malaysia, powers of attorney are governed by the Powers of Attorney Act 1949 and must be registered at the High Court in order to be effective and valid.
- (ii) When dealing with a person acting by way of a power of attorney, it is important that the bank requests a copy of the power of attorney to verify what the attorney is empowered to do. When construing a power of attorney, general words must be construed in the light of the stated objects of the power of attorney – *Magnum Finance Bhd v Ling Sing Ping*.

Bank Maju Bhd should also instruct its solicitors to conduct a search at the High Court Registry to confirm that the power of attorney has been registered and not revoked by the donor. However, in practice, as far as operation of accounts is

concerned, Bank Maju Bhd may insist the donor should sign the bank's Letter of Mandate instead of using the power of attorney.

**Optional answer:**

- Powers of attorney are construed strictly in accordance with their wordings.
  - To ensure that the power of attorney has indeed been executed by the donor, banks sometimes do verify with the solicitor who has attested the power of attorney.
- (c) In order to enter into a legal contract, such as a deposit account contract, a customer has to have the full legal capacity to do so. Generally, a person has to be of the age of majority, of sound mind and not be disqualified by law from contracting – section 11 of the Contracts Act 1950.

Thus Mary is advised not to open the account for ABC Enterprise unless Carrie is not to be an authorised signatory until she reaches 18 years of age (the age of majority). This is because Carrie, being a minor, will not be liable upon a cheque under any circumstances.

A minor may enter into a partnership with adults but is not answerable for the firm's debts while he or she is still a minor. However, if the minor continues with the partnership until the he or she reaches the age of majority, then he or she will be liable for the partnership's debts – *William Jacks & Co (Malaya) Ltd v Chan & Yong Trading Co*.

**Question 2**

- Candidates had poor knowledge of the various legal issues pertaining to the banking operations tested in this question.
- Candidates are advised to identify the issues and write “to-the-point” answers as required.

2. (a) (i) The instruction to stop payment may be given orally (so long as the countermand is brought to the bank's notice) but should be followed up with a written instruction (unless orally given using phone-banking or internet banking facilities). Section 75(a) of the Bills of Exchange Act 1949 provides that a bank's authority to pay a cheque drawn on the bank is determined by the countermand of payment.

In *London Provincial and South-Western Bank Ltd v Buszard*, it was held that the countermand must be sent to the branch of the bank where the account is kept. A countermand is not effective until it actually comes to the bank's notice.

If the instruction countermanding payment of the cheque is received by telephone, the customer's written confirmation should be obtained. If the cheque is presented in the meantime, it should be returned with the answer “Oral countermand pending written confirmation”. In *Chua Neoh Kow v Malayan Banking Bhd*, it was held that a countermand may be given orally.

- (ii) Yes, Bank Baru Bhd is liable towards Mr Whye as the bank overlooked an oral countermand – *Bank Bumiputra (M) Bhd v Hashbudin bin Hashim*. Bank Baru Bhd is liable to pay back the sum wrongly debited from the drawer's account as the bank's authority to pay on the cheque is determined by the countermand – section 75(a) of the Bills of Exchange Act 1949.

- (iii) Generally, Bank Baru Bhd may recover the sum wrongly paid to the payee – section 73 of the Contracts Act 1950 which provides *inter alia* that a person to whom money has been paid by mistake must repay it. However, Bank Baru Bhd may be estopped under section 115 of the Evidence Act 1950 if the payee was misled and had acted upon the misrepresentation of the payer. Bank Baru Bhd may be prevented from

correcting its mistake if the customer honestly believes that the entries on his account are correct and alters his or her position in reliance upon them - *Lloyds Bank Ltd v Brookes*. Thus, the question whether Bank Baru Bhd can recover the RM9,000 from Mr Kon depends on the facts - whether there is an estoppel.

- (b) Mr Kenny may have to thumbprint a cheque in order to withdraw the current account balance since he is now paralysed. Applying the Privy Council case, *Chow Yee Wah & Anor v Choo Ah Pat.*, a thumbprinted cheque may be held to be valid so long as when the drawer affixed his thumbprint thereon, he had the mental capacity to do so.

The person's mental capacity is a question of fact and is independent of his or her physical health. For a cheque to be valid, an existing recently paralysed account holder who is unable to sign his cheque as usual can thumbprint his cheque, witnessed by his banker and, preferably, another independent witness such as a doctor or a lawyer who is satisfied as to his mental capacity.

### Question 3

- Candidates were unable to state the main duties of a collecting banker and the relevant statutory provisions to support the legal principle in this question.
- Statutory provisions, wherever relevant, ought to be used to support the legal principle in the question.

3. (a) (i) No, Puan Rokiah cannot enquire with Bank BB Bhd on the balance outstanding of the joint account as she is not one of the joint account holders. One of the banker's duties is the duty of secrecy. Under section 97(1) of the Banking and Financial Institutions Act 1989 (BAFIA), a banker is under a legal obligation to keep secret his customers' affairs. Bank BB Bhd is bound by this statutory provision not to disclose details of the joint account. The maximum penalty for contravention under section 97 of the BAFIA is 3 years imprisonment or an RM3million fine or both such imprisonment and fine.

- (ii) Bank BB Bhd is not liable for the withdrawal of RM99,900 on 4 August 2007 as the bank had yet to be informed of Datin Minah's death. Notice of the customer's death would terminate the banker-customer relationship and any credit balance in the current account would be vested with his or her personal representatives. The above-mentioned account would be frozen (no more withdrawals to be allowed) until operated by the executors (if Datin Minah died testate with a will) or by the administrators (if Datin Minah died intestate without a will) jointly with her brother, Encik Ali.

Section 75(b) of the Bills of Exchange Act 1949 provides that the bank's authority to pay on cheques is determined upon notice of the drawer's death. Datuk Minta cannot successfully demand the RM50,000 as Bank BB Bhd had paid out the money prior to its receipt of the notice of Datin Minah's death. Since notice of death was only received on 30 August 2007, that is after the account had been debited, Bank BB Bhd had rightfully debited the account and would not be liable thereon.

- (b) (i) The two main duties of a collecting banker are:
- to use reasonable care and diligence when presenting and securing payment of cheques. For example, if a banker forgets or fails to send his customers' cheques for collection, the banker would be liable to the customers for any losses suffered.
  - to give prompt notice to his customers if the cheques deposited are dishonoured. This is usually done by debiting the customers' accounts and returning the cheques to them.

- (ii) The legal effects when adding the words “account payee” to a crossing on a cheque are as follows:

Section 81A of the Bills of Exchange Act 1949 provides that a crossed cheque with the words “account payee” shall not be transferable but shall only be valid between the parties thereto. Thus, “account payee” crossed cheques are not negotiable and such cheques must be credited into the payee’s account only.

**Question 4**

- Candidates did not mention the issue of a debenture when answering the question on methods of obtaining security for credit facilities.
- Candidates were unable to state the reason for the requirement to sign personal guarantees.
- Candidates need to improve their basic knowledge of security documentation.

4. (a) A first- party first-legal charge over that piece of land can be created as security for the RM1million housing loan granted to Datuk Wang. It must be registered pursuant to the requirements of the National Land Code 1965 (NLC) with the Land Registry or Land Office – section 243 of the NLC. The charge must be in the statutory prescribed form, together with a Charge Annexure, be duly executed and stamped, and accompanied by the appropriate fees.

As for the term/fixed loan of RM3million to be granted to Mawar Wang Sdn Bhd, the security documentation would be a debenture. The debenture would incorporate fixed and floating charges. A fixed charge would cover the land, building and equipment, including its goodwill and machinery. Here, since Datuk Wang owns the land, the charge over the land would be a third-party charge first-legal charge since Mawar Wang Sdn Bhd is the borrower. The charge has also to be registered with the Registry or Land Office concerned.

Floating charges over Mawar Wang Sdn Bhd’s assets are also to be incorporated in the debenture. The particulars of the charge, including the negative pledge incorporated in the debenture, would be registered with the Registry of Companies (now called the Companies Commission of Malaysia) by lodging the particulars of charge pursuant to section 108 of the Companies Act 1965.

- (b) Although guarantees are, strictly speaking, not securities, joint and several guarantees can be obtained from the directors of Mawar Wang Sdn Bhd. A guarantee is a “contract to perform the promise, or discharge the liability, of a third person in case of his default”. The reason for this requirement is that Mawar Wang Sdn Bhd is a separate legal entity – *Salomon v Salomon* and the company is separate and distinct from its directors and shareholders. If not for the joint and several guarantees by both directors, the directors would not be personally liable for the company’s debts. Thus, requiring the guarantees from the directors ensures that the directors would be committed to repay the company’s debts. Failure to do so may result in Bank CC Bhd suing the directors personally by virtue of their liabilities as guarantors.
- (c) If there is a default in repayment on the mentioned facilities which are secured by charges over land, Bank CC Bhd can pursue the following remedies:
- right to possession
  - power of sale

The rights of the chargee to enter into possession are provided in sections 271 to 277 of the NLC. Section 253 of the NLC provides that the provisions of sections 253 to 269 of the NLC enable the chargee to obtain the sale of the land to which his charge relates in event of breach by the chargor. The application for an order for sale will be made in the High Court (in the case of a Registry title) or with the Land Office (in the case of a Land Office title).

Enforcement of the debenture is by way of appointing a receiver and manager to manage the company's affairs and to realise the security. The floating charge would also crystallise and thus the chargor cannot deal with the company's floating assets anymore. The receiver would get in the assets charged and collect all receipts to realise the security on behalf of the debenture-holder in discharge of its debt and also must discharge the company's liabilities in the proper order of priorities.

To recover the amounts guaranteed, Bank CC Bhd can take legal action against the guarantors. A letter of demand will be sent to the guarantor's address given in the guarantee. If there is no response, Bank CC Bhd can proceed to sue for and prove the debt. The process of enforcement ends with the High Court giving judgment on the guarantor's liability, after which Bank CC Bhd may proceed with enforcement via the writ of seizure and sale, judgment debtor summons and bankruptcy proceedings.

#### Question 5

- Candidates wrote on the commercial benefits, instead of explaining the duty to act *bona fide*.
- Candidates were unable to explain the meaning of interpleader.

5. (a) As a general principle, a company's directors are under duty to act *bona fide* for the company's benefit. In *Rolled Steel Products (Holdings) Ltd v British Steel Corp.*, the English Court of Appeal held that the "directors of a company will not have actual authority from the company to exercise any express or implied powers other than for the purposes of the company as set out in its memorandum of association."

So if the directors enter into a transaction that does not benefit their company, they may be exercising their powers for an improper purpose. The transaction is voidable at the option of the person to whom the duty is owed, namely, the company. This is an important issue when taking security, especially guarantees, from a company to secure a third-party debt. It is common practice for banks lending to companies within a group to seek guarantees from other members of the group. One of the more problematic issues is determining whether the giving of securities to secure another company's indebtedness benefits the company. – *Charterbridge Corporation Ltd v Lloyds Bank Ltd* and *ANZ Executors & Trustee Company Ltd v Quintex Australia Ltd*.

- (b) A debenture is an instrument, usually a deed, a company issues, as acknowledgement of a debt. Under section 4(1) of the Companies Act 1965, a 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".

It may incorporate either a fixed or floating charge, or both, over the company's assets. Fixed charges may cover plant and machinery, including its goodwill and its uncalled capital. In *Re Yorkshire Woolcombers Association Ltd.*, a floating charge is described as a class of company assets, present and future, which would be changing from time to time and which the company is free to deal with, until crystallisation.

- (c) In relation to court procedure, "interpleader" means as follows. Where a banker or financier holds any money (for example, deposits of cash), goods or chattels (for example, items placed in safe deposit boxes) and he expects to be sued for or in respect of that money, goods or chattels, by two or more persons, the banker or financier can protect himself by calling on all such claimants to interplead. To "interplead" means to claim against one another, so that the Court can decide to whom the money, goods or chattels rightly belong.