

BUSINESS LAW GUIDEBOOK

SECOND EDITION

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CHAPTER 6: BANKING AND FINANCE

TEST YOUR KNOWLEDGE

1. Explain the meaning of 'ADI'.

ANSWER

The *Banking Act 1959* (Cth) is also used to regulate the banking business. This legislation provides generally for those companies entitled to carry on banking transactions in Australia. Such companies are described collectively as authorised deposit-taking institutions (ADIs): s 5(1). Following the Wallis Reforms (1997), any company which carries on the 'business of banking' must obtain authorisation from APRA as an ADI. ADIs include not only banks but also other non-bank nonfinancial institutions which carry on the banking business, such as building societies and credit unions.

2. How do we know what a customer of a bank is despite the fact that the *Cheques Act 1986* (Cth) does not give us a definition?

ANSWER

The *Cheques Act 1986* (Cth) contains no definition of a 'customer', and the determination will depend on the application of the common law decisions to the facts of each case. According to *Commissioners of Taxation v English, Scottish & Australian Bank Ltd* [1920] AC 683 (Privy Council), for example, the word 'customer' signifies a relationship in which duration is not of the essence. A person whose money has been accepted by the bank is a customer of the bank, regardless of whether his or her connection with the bank is of short or long standing.

3. What are the parties to a cheque?

ANSWER

The drawer of the cheque is the person who draws, signs and gives a cheque and is primarily liable on the cheque. The drawee of the cheque is the person on whom a cheque is drawn; a person to whom the cheque is addressed. The indorser is the person who transfers a cheque by signing on the back of it, and undertakes that on due presentment for payment, the cheque will be paid. The indorsee is the person to whom rights are transferred by indorsement of the cheque.

4. Why is a cheque called a particular type of bill of exchange?

ANSWER

A cheque is a bill of exchange within the meaning of the *Bills of Exchange Act 1909* (Cth). However, a cheque is a particular kind of bill of exchange in that unlike the traditional bill of exchange, a cheque is not accepted, but is always drawn on a banker and is payable on demand.

5. Explain the relationship between the financial institution and its customer.

ANSWER

Since the customer of a financial institution will draw cheques on the institution, there is here a relationship between them which is regarded as a contractual relationship. At the same time, the relationship between the financial institution and the customer is that of debtor and creditor: *Foley v Hill* [1843-60] All ER Rep 16 and *Joachimson v Swiss Bank Corp* [1921] 3 KB 110. The financial institution has borrowed money from the customer and is under an obligation to repay the customer. The financial institution has an obligation to honour the customer's cheques and the customer has a right to make a demand (or mandate) for payment.

6. At common law, a customer owes to the financial institution a duty to take reasonable care when drawing cheques. Explain in some detail what that duty is. Refer to decided cases to support your answer.

ANSWER

Customers at common law owe a duty to their financial institution to take reasonable care in the drawing of cheques. When writing a cheque, for example, customers must make sure that a cheque cannot be fraudulently altered. They can do this by being careful not to leave spaces on cheques, such as having gaps between the '\$' sign and the written amount, and if they fail in this duty, they will bear the loss: *Commonwealth Trading Bank of Australia v Sydney Wide Stores Pty Ltd* (1981) 148 CLR 304; *London Joint Stock Bank Ltd v Macmillan* [1918] AC 777 at 789.

7. Cecil drew a cheque for 2000 dollars for R Smith. He asked his friend William to post the cheque for him. William changed the amount by adding 'thirty' to the words and figures in the spaces that Cecil had left when writing out the cheque. William took the cheque to Cecil's bank, the Sydney Bank, and got the cheque cashed. Advise Sydney Bank. What would your answer be if Cecil had crossed the cheque 'not negotiable'?

ANSWER

The true owner of the cheque is Cecil but he had authorised William to post the cheque for him. It is clear that when Cecil signed the cheque he was careless in filling out the cheque by leaving spaces between the words and the figures. In short, Cecil had been negligent in filling out the cheque and if the Sydney Bank paid out on the cheque the loss would fall on Cecil: *Commonwealth Trading Bank of Australia v Sydney Wide Stores Pty Ltd* (1981) 148 CLR 304.

If Cecil had crossed the cheque 'not negotiable' he would have given a specific direction to Sydney Bank not to pay the cheque over the counter upon presentation. It must be paid into an account: Cheques Act, s 54. Crossing the cheque 'not negotiable' acts as a protection to the drawer in case the cheque gets into the hands of the wrong party: *Commissioners of State Savings Bank of Victoria v Permewan Wright & Co Ltd* (1914) 19 CLR 467. If Sydney Bank pays the cheque in a way that is contrary to the crossing, it becomes liable if the true owner Cecil suffers loss: s 93.

8. What is the *Tournier* duty? What is the extent of that duty?

ANSWER

The *Tournier* duty can be best explained by saying that financial institutions must preserve confidentiality or secrecy regarding their customers. This means that they cannot reveal details about either their customers or their customers' financial affairs. The duty of confidentiality is not absolute but is qualified under a number of heads: '(a) where disclosure is made under compulsion by law; (b) where there is a duty to the public to

disclose; (c) where the interests of the bank require disclosure; (d) where the disclosure is made by the express or implied consent of the customer': *Tournier v National Provincial and Union Bank of England* [1924] 1 KB 461 per Bankes LJ at 471–3.

9. It has been said that the *Cheques Act 1986* (Cth) has simplified the concept of crossings on cheques. Explain.

ANSWER

The *Cheques Act* has certainly simplified the law relating to crossings since it has dispensed with the old requirement relating to special crossings leaving only general crossings. The only crossings that are allowed by the *Cheques Act* are either two parallel transverse lines or two parallel transverse lines with the words 'not negotiable' between, or substantially between the lines: s 53 (1).

10. Jenny has stolen a cheque with a blank general crossing on it. She goes to the Austral Bank and obtains cash across the counter for the value of the cheque. What do you think are the rights of the true owner?

ANSWER

It must be pointed out that transverse lines indicate to the drawee bank not to pay the cheque except to another bank or financial institution: s 54. The true owner of the cheque may recover the value of the cheque from the Austral Bank under s 93(1) of the *Cheques Act*. This assumes that at the time of presentment to the bank the cheque did appear to be crossed so that no defence arises under s 93 (2).

11. Someone is given a crossed cheque with the words 'not negotiable' between the lines. Explain the effect of such a cheque.

ANSWER

The effect of crossing a cheque is to stop it from being cashed over the counter of a financial institution, thus offering a protection if the cheque is lost or stolen. A crossed cheque must be collected through a financial institution—e.g., it must be paid into a bank account: *Cheques Act*, s 54. The addition of the words 'not negotiable' between the lines has the effect of destroying the ability of the transferee to obtain the cheque free from defects in the title of the person who negotiated it to him or her. The cheque can still be transferred from one individual to another, but the person receiving it cannot obtain or give a better

title to the cheque than that held by the transferor (s 55). The person who takes a crossed 'not negotiable' cheque is taking it at his or her own risk.

12. What are two important differences between a cheque and a bill of exchange?

ANSWER

In the case of a cheque, a drawee or paying financial institution is obliged to pay the cheque that arises as part of the relationship between financial institutions and their customers, while in the case of a bill of exchange, the obligation arises from the acceptance of the bill. A cheque must be drawn on a financial institution, while a bill of exchange can be drawn on anyone other than the drawer.

13. Name the parties to a bill of exchange.

ANSWER

The drawer of a bill of exchange is the person who draws, signs and gives a bill of exchange. The drawee of a bill of exchange is the person on whom the bill is drawn; a person to whom the bill is addressed. The acceptor is the drawee who signs the bill and therefore accepts the bill, and in so doing agrees to pay the sum at the time stipulated on the bill. The indorser is the person who transfers the bill by signing on the back of it and delivering it to the indorsee. The indorsee is the person to whom rights are transferred by indorsement of the bill. The holder is the person who possesses the bill at its maturity and it is the holder who will present the bill to the acceptor for payment.

14. Why is a promissory note called a 'one-name paper'?

ANSWER

A promissory note is not a bill of exchange because it is not drawn on a third party, but is simply a promise by the maker to pay a sum at a promised time. A promissory note, unlike a bill of exchange, involves only two parties—the maker and the payee/bearer rather than the three parties of a bill of exchange, which are drawer, drawee/acceptor and holder. Thus the parties to a promissory note are the person who gives the promise (the maker) and the person to whom the note is given (the payee). Since a promissory note is, as mentioned, signed only by the maker and not accepted by or drawn on a drawee, it is sometimes called a one-name paper.

PROBLEM QUESTION

Before you attempt the following problem, make sure you read the 'Guidelines for answering problems' and be acquainted with the IPAC method of writing answers to problem questions.

PROBLEM

Lester Armstrong, an English migrant and his wife Anne live with their family in an expensive suburb. Lester has been successful in the construction business and has prospered recently as a result of the recent real estate boom.

Lester has friends as well as enemies in the construction business. On 2 March, a female worker of a rival construction company Mrs Mary Weekes opened an account with the Eastpac Bank at the local Shopping Centre in Anne's name and deposited a cheque. Anne had become a well-known charity worker and was frequently featured in the weekly newspaper. It must be stressed that Mary happened to look like Anne and had obviously taken advantage of this fact. She was also able to forge Anne's signature. On 10 March Mary returned to Eastpac Bank, filled in a pink withdrawal form and withdrew all the money (\$8000) from the account. Anne rang Tom More the manager of Eastpac Bank accusing him of wrongfully cashing the cheque and threatening to sue the bank. You are to advise Anne.

ANSWER

This question involves the issue of when a person becomes a customer of the Eastpac Bank. It also involves the question of why it is important to know if a person is a 'customer'; s 95 of the *Cheques Act 1986* (Cth) is a possible defence for the bank. **(Issue)**

The defence of the bank can be seen in s 95 of the *Cheques Act* which provides that where a financial institution in good faith, and without negligence receives payment of a cheque for a customer, and the customer has no title, or has a defective title to the cheque, the bank has not been negligent. However, such a defence is only applicable where the person (Mary) who deposits the cheque with the bank is a 'customer'. **(Rule)**

In *Commissioner of Taxation v English Scottish and Australian Bank* [1920] AC 683, an impostor stole a cheque payable to the Commissioner of Taxation and with that cheque opened an account with the bank. An important question was whether s 88 of the *Bills of Exchange Act 1909* (Cth) the equivalent of s 95 of the *Cheques Act 1986* (Cth) was available to the defendant bank. This depended on whether the impostor could be considered to be a customer. In this case it was said that the word 'customer' signifies a relationship in which duration is not of the essence. A person whose money has been accepted by the bank is a customer of the bank, regardless of whether his or her connection with the bank is of short or long standing. **(Application)**

On this basis it can be concluded that Mary was a customer of the bank. In respect of the question of negligence of the bank, the court said: 'The test of negligence is whether the transaction of paying in any given cheque was so out of the ordinary course that it ought to have aroused doubts in the banker's mind and caused him to make inquiry'. This defence of the bank is reinforced by s 95 of the *Cheques Act* as referred to above. **(Conclusion)**