IS A BANK UNDER A LEGAL DUTY TO ACT POSITIVELY IN ORDER TO PROTECT THE INTERESTS OF THIRD PARTIES WHEN APPROPRIATING FUNDS DEPOSITED IN A CLIENT'S ACCOUNT?

***Spar Group Ltd v FirstRand Bank Ltd* 2017 1 SA 449 (GP)**

OPSOMMING

Rus daar 'n regsplig op 'n bank om positief op te tree ten einde die belange van derdes te beskerm by die aanwending van fondse wat in 'n kliënt se rekening gedeponeer word?

Die *Spar*-saak handel oor verskeie aspekte van die bank/kliënt verhouding. Dit handel in die besonder oor die eiendomsreg van fondse wat in 'n bankrekening gedeponeer word, die vraag of 'n bank geregtig is om sodanige fondse by wyse van skuldvergelyking aan te wend, asook 'n sogenaamde kwasie-vindikatoriese aksie deur 'n derde wat nie die rekeninghouer is nie maar die fondse opeis wat in 'n kliënt van die bank se rekening gedeponeer is. Van besondere belang vir doeleindes van hierdie bespreking is die vraag of 'n bank, wanneer hy fondse aanwend wat in 'n kliënt se rekening gedeponeer is, 'n regsplig het om positief op te tree ten einde die belange van derdes te beskerm. Hierdie bespreking is tot laasgenoemde vraag beperk.

1 Introduction

The *Spar* case deals with as number of aspects regarding the bank/customer relationship (in respect of which see Malan *et al Malan on bills of exchange, cheques and promissory notes* (2009) para 217; Itzikowitz and Du Toit "Banking and currency" 2(1) *LAWSA* (2003) para 343; Sharrock (ed) *The law of banking and payment in South Africa* (2016) ch 4; Nagel and Pretorius "Mandate and the bank and customer relationship – *DA Ungaro & Sons (Pty) Ltd v Absa Bank Ltd* [2015] 4 All SA 783 (GJ)" 2016 *THRHR* 514 and authorities cited). In particular, it deals with the ownership of moneys deposited into a bank account, the bank's entitlement to appropriate such deposits by way of set-off (in respect of which see Nagel and Pretorius "The bank and customer relationship, combination of accounts and set-off" 2016 *THRHR* 660) and a so-called *quasi*-vindicatory action by a third party who is not the account holder but who claims ownership of the moneys held in a client's account with a bank (in respect of which, see Nagel and Pretorius "Ownership and appropriation of funds deposited in a bank account – *Spar Group Ltd v FirstRand Bank Ltd*" 2017 *THRHR* 308).

Of particular importance to this note is the question whether a bank, when appropriating moneys deposited into a client's account, is under a legal duty to act positively in order to protect the interests of third parties. This note is confined to the decision in the latter regard in *Spar*.

2 Facts of *Spar* and issues to be decided

For a proper understanding of *Spar* it is necessary to explain the facts of the case in some detail. Spar instituted two so-called *quasi*-vindicatory and two delictual claims against FirstRand Bank ("FirstRand" or "the Bank") for repayment of a sum in excess of R5 million. The circumstances that gave rise to these claims are

as follows. Spar as wholesaler supplied goods and services on credit to an enterprise called Umtshingo, a retailer. The latter registered a notarial bond over its movable assets as security for its indebtedness to Spar. The bond provided that should Umtshingo fail to pay to Spar any amount as it became due, or fail to comply with any of the provisions of the bond, Spar "would be entitled to enter upon, seize and take full possession of the business and all the assets of Umtshingo and to hold same as security for the repayment of all amounts due to Spar" (*Spar* para 2). Umtshingo operated three different businesses. The proceeds of speed-point sales of the businesses were deposited into three accounts held at FirstRand, namely, account A, held in the name of Central Route; and accounts B and C, held in the name of Umtshingo (para 3). At the beginning of March 2010 Umtshingo was indebted to Spar in excess of R2 million. Spar applied to court for the perfection of the notarial bond. The provisional order granted on 5 March 2010 was executed on 8 March 2010 and the three businesses were attached and placed in Spar's possession (para 4). As a result, Spar operated the three businesses for its own profit or loss as from 9 March 2010 (para 5) and requested FirstRand to change the accounts into which the proceeds from the above-mentioned speed-point sales would be paid. Umtshingo, represented by one Paulo, however, refused to give permission for the accounts to be changed in favour of Spar. Consequently, as of 9 March 2010, the proceeds of the three businesses continued to be paid into accounts A, B and C respectively (para 6). It was common cause between the parties that:

> "• the Bank, during the period 9 March until 24 June 2010, permitted Central Route to draw cheques and process debit and stop orders on [account A] on condition that Central Route first made deposits or transfers into [account A] in sufficient amounts to cover such debts;
> • as from 24 June 2010, [account A] was frozen in terms of a court order;
> • on 8 March 2010 Central Route was indebted to the Bank in the sum of R1 343 422,92, being the debit balance on [account A];
> • on 9 March 2010 Umtshingo was indebted to the Bank in the sum of R292 140,84, being the debit balance on [account C];
> • the indebtedness of Central Route to the Bank on [account A] was extinguished on or about 12 July 2010 and thereafter the account remained in credit at all times;
> • the indebtedness of Umtshingo to the Bank on [account C] was extinguished on or about 8 May 2010;
> • the Bank did not obtain the plaintiff's permission to set off the speed-point credits of R1 300 051,21 against the indebtedness of Central Route on [account A];
> • the Bank did not obtain the plaintiff's permission to set off the speed-point credits against the overdraft indebtedness of Umtshingo on [account C] as at 8 March 2010, the payment guarantee of R400 000 debited on 25 June 2010, the monthly loan-agreement instalment debited during the period March 2010 to June 2011 and the interest charged by the Bank on a monthly basis on the debit balance from time to time;
> • the quantum of Spar's claims is no longer in dispute" (para 7).

Fourie J summarised the question before the court as

> "whether the Bank is liable towards [Spar] on the basis of alleged unlawful appropriation (claims 1 and 4) and in delict (claims 2 and 3) in respect of an alleged duty of care to avoid economic loss in circumstances where it is alleged that the Bank had knowledge pertaining to the alleged true owner of moneys deposited into the bank accounts referred to above" (para 8).

Claim 1 failed because of the general rule that moneys deposited into a bank account fall into the ownership of the bank (para 44). Fourie J held that someone claiming to have a so-called *quasi*-vindicatory claim to moneys deposited into an account held by a client of a bank will have to prove that the bank entered into an agreement with the client to "warehouse" such moneys on behalf of the claimant (para 50). Spar failed to prove such an agreement and claim 1 was dismissed (para 53). This part of the judgment has been discussed elsewhere (see Nagel and Pretorius 2017 *THRHR* 308). Claim 4 had become prescribed (para 42). The discussion below therefore deals with claims 2 and 3 only.

Claim 2 was for R2 039 948.68 and concerned account B. Claim 3 was for R1 358 890.90 and concerned account C (para 54). Spar's arguments were as follows (para 55):

(a) the funds in question were deposited into accounts B and C for purposes of "warehousing" moneys that actually belonged to Spar, and not to put them at the disposal of Central Route, Umtshingo or Paulo;

(b) FirstRand, as banker, owed Spar, who was a customer of FirstRand's Durban Corporate Division, a duty of care to avoid economic loss to Spar since FirstRand knew that Spar was the true owner of the funds concerned; and

(c) FirstRand wrongfully breached its duty of care to Spar which resulted in Spar suffering damages.

3 Judgment

Fourie J started off his judgment by pointing out that the essence of both claims was the contention that FirstRand should not have allowed Umtshingo, Central Route or Paulo to withdraw funds from accounts B and C (para 56). He stated (*ibid*) that Spar's argument that FirstRand had a duty of care was based primarily on the contention that Spar was a customer of FirstRand's Durban Corporate Division and that FirstRand was aware that Spar, as the true owner thereof, was entitled to the moneys in question. (Spar was a customer of FirstRand's Durban Corporate Division but not a customer of FirstRand's Nelspruit branch.) FirstRand at all times denied the existence of such a duty of care.

Spar's counsel conceded that, as far as he could ascertain, our courts have never been requested to decide on the existence of a duty of care in terms of which a banker is obliged to avoid loss to someone other than the accountholder in respect of moneys deposited into the latter's bank account (para 57). However, counsel "pertinently and forcefully argued" that FirstRand knew that Spar was the true owner of the relevant funds and also knew (or should have foreseen) that if someone else were allowed to withdraw the relevant funds, they might never be recovered by Spar. According to Fourie J, "[c]entral to this argument is the contention that [Spar] was the true owner of the moneys concerned and therefore had an identifiable subjective right with regard to these funds" (*ibid*).

As regards Spar's alleged subjective right to the funds in question, Fourie J referred (para 58) to Neethling and Potgieter *Neethling-Potgieter-Visser Law of delict* (2015) 55 in respect of determining wrongfulness by asking whether a legal duty has been breached rather than by asking whether a subjective right has been infringed, and quoted their explanation:

> "Accordingly, in cases of liability for an omission or for causing pure economic loss (with the exception of the infringement of the right to goodwill in the case of

> unlawful competition) wrongfulness is normally determined not by asking whether the plaintiff's subjective right has been infringed, but rather by asking whether, according to the *boni mores* or reasonableness criterion the defendant had a legal duty to prevent harm, in other words whether the defendant could reasonably (according to the *boni mores*) have been expected to act positively" (55 56.)

Fourie J had no doubt that claims 2 and 3 were claims for pure economic loss (para 59). Both claims were based on the contention that FirstRand should not have allowed anyone but Spar to withdraw funds from accounts B and C. In other words, Spar's argument was that FirstRand should have prevented such withdrawals by taking positive action. The question before Fourie J was "therefore whether, according to the *boni mores* or reasonableness criterion, FirstRand had a legal duty to prevent pure economic loss to Spar by acting positively" (*ibid*).

The judge referred (para 60) to *Country Cloud Trading CC v MEC, Department of Infrastructure Development* 2015 1 SA 1 (CC) where it was held that

> "our law is generally reluctant to recognise pure economic loss claims, especially where it would constitute an extension of the law of delict. Wrongfulness must be positively established. It has thus far been established in limited categories of cases, like intentional interferences in contractual relations or negligent misstatements, where the plaintiff can show a right or legally recognised interest that the defendant infringed. In addition, if claims for pure economic loss are too freely recognised, there is the risk of 'liability in an indeterminate amount for an indeterminate time to an indeterminate class' . . . So the element of wrongfulness provides the necessary check on liability in these circumstances. It functions in this context to curb liability and, in doing so, to ensure that unmanageably wide or indeterminate liability does not eventuate and that liability is not inappropriately allocated" (paras 23–25).

Fourie J also referred to Neethling and Potgieter 56 who state that the requirement of a legal duty in respect of wrongfulness is probably because impairment is not *prima facie* wrongful in cases of pure economic loss, but *prima facie* lawful since, in terms of the *boni mores* criterion, there is neither a general duty to prevent loss to others by positive conduct, nor a general duty to prevent pure economic loss (para 61). The authors conclude as follows:

> "Therefore, one must determine in each case whether there is a legal duty to act positively or a duty to avoid pure economic loss. In these cases, it is consequently more appropriate to make use of a breach of a legal duty rather than infringement of a subjective right, to establish and express wrongfulness" (*ibid*).

Referring to *Knop v Johannesburg City Council* 1995 2 SA 1 (A) 27F–I, Fourie J reiterated (para 62) that the existence of a legal duty to prevent loss "is a conclusion of law depending on a consideration of all the circumstances of the case". This requires the application of the general criterion of reasonableness, having regard to the legal convictions of the community as assessed by the court (*ibid*). Fourie J explained the question of wrongfulness pursuant to a legal duty to act positively with reference to *Van Eeden v Minister of Safety and Security (Women's Legal Centre Trust, as Amicus Curiae)* 2003 1 SA 389 (SCA) 396 400:

> "An omission is wrongful if the defendant is under a legal duty to act positively to prevent the harm suffered by the plaintiff. A defendant is under a legal duty to act positively to prevent harm to a plaintiff if it is reasonable to expect of the defendant to have taken positive measures to prevent the harm" (*Spar* para 62).

Turning to the question whether it could be said that FirstRand had a legal duty to avoid economic loss to Spar by acting positively, Fourie J held (para 63) that it should be taken into account that Spar was not a customer of FirstRand's Nelspruit branch, but a customer of FirstRand's Durban Corporate Division. Both accounts B and C were operated in the name of Umtshingo at FirstRand's Nelspruit branch and FirstRand thus had a duty of confidentiality towards Umtshingo which obliged it not to disclose any particulars concerning the latter's bank accounts and transactions concluded by it. With reference to *FirstRand Bank Ltd v Chaucer Publications (Pty) Ltd* 2008 2 SA 592 (C) paras 19 and 20, Fourie J reiterated that considerations of public policy dictate that the bank/client relationship must be of a confidential nature, "unless for reasons of public policy this duty is overridden by a greater public interest" (*Spar* para 63).

Fourie J held that a further important consideration to be taken into account was the question whether Umtshingo's accounts were indeed used to "warehouse" moneys belonging to Spar (para 64). As already pointed out above (para 2), Spar failed to prove the alleged warehousing agreement in terms of which the funds in question were actually kept on their behalf, because of which claim 1 was dismissed (para 53).

Spar's counsel suggested that the public would benefit by a better safeguarding of their funds in similar circumstances if liability to prevent pure economic loss were to be imposed on a bank (para 65). According to Fourie J, the problem with Spar's contention was two-fold. First, it assumed that the funds in question belonged to Spar after they had been deposited into Umtshingo's account. This assumption had already been found to be incorrect (para 63 and discussion above).

The second problem identified by Fourie J was

> "that the imposition of such a duty would probably place too heavy a burden on banks to protect the interests of third parties in circumstances where the interests of its own client(s) are also to be taken into account. This can result in a conflict of interests which may have a detrimental effect on the interests of existing clients of a bank" (para 65).

The judge therefore was not convinced that public policy demanded the imposition of such a duty on FirstRand. He held (para 65) that such a duty may result in unmanageably wide or indeterminate liability referred to in *Country Cloud Trading* (quoted *supra*).

Finally, Fourie J held (para 66) that, having regard to all the above considerations and by applying the general criterion of reasonableness, it would be unreasonable to hold that FirstRand had a legal duty to avoid economic loss to Spar. Claims 2 and 3 therefore were dismissed.

4 Comment

It is submitted that Fourie J was correct to hold that a third party (Spar *in casu*) who claims to be entitled to funds deposited into an account held in the name of a client of a bank will have to prove that the bank was a party to an agreement with its client to "warehouse" such moneys on behalf of the third person claiming to be entitled thereto (*Spar* para 50 as set out above; see Nagel and Pretorius 2017 *THRHR* 308).

The first leg of Fourie J's reasons for refusing to recognise a legal duty on the bank in the present case is based on common sense and logic: Spar's incorrect

assumption that it was entitled to the deposits made into Umtshingo's accounts militated against the recognition of a duty on the bank to act positively in not allowing anyone but Spar to withdraw funds from the account in question. A party who is unable to prove any legal entitlement to the funds in question, certainly cannot claim protection against the loss thereof.

Connoisseurs in the field of the law of delict may consider Fourie J's judgment as merely stating what is trite law in view of the principles and guidelines regarding Aquilian liability for pure economic loss that have crystallised in the case law over the years (for a comprehensive overview, see Neethling and Potgieter 305ff and authorities cited and the very useful synopsis by Van der Walt and Midgley "Delict" 15 *LAWSA* (2016) para 87; Neethling and Potgieter in their analysis of *Country Cloud*, "Breach of contract and delictual liability to third parties – *Country Cloud Trading CC v MEC, Department of Infrastructure Development, Gauteng* 2015 1 SA 1 (CC)" 2015 *THRHR* 711 713, even described Khampepe J's remarks regarding wrongfulness in the field of pure economic loss (paras 22–26) – where she referred, *inter alia*, to Van der Westhuizen J in *Loureiro v Imvula Quality Protection (Pty) Ltd* 2014 3 SA 394 (CC) para 53 – as confirming trite law) and for merely reiterating our courts' well-known reluctance to extend Aquilian liability to new instances of pure economic loss because of the risk of indeterminate liability.

However, one must bear in mind what Marais J said in *Arthur E Abrahams & Gross v Cohen* 1991 2 SA 301 (C) 309:

> "A defendant may be held liable *ex delicto* for causing pure economic loss unassociated with physical injury but before he is held liable it will have to be established that the possibility of loss of that kind was reasonably foreseeable by him *and that in all the circumstances of the case he was under a legal duty to prevent such loss occurring*. It is not possible or desirable to attempt to define exhaustively the factors which would give rise to such a duty because new situations not previously encountered are bound to arise and societal attitudes are not immutable" (emphasis in the original).

Fourie J's judgment regarding pure economic loss and the novel question as to the existence of a legal duty in terms of which a banker is obliged to avoid loss to someone other than the accountholder in respect of moneys deposited into the latter's bank account, provides some valuable guidelines in respect of the previously unexplored legal position in this regard. Banks generally will probably welcome the *Spar* judgment – they are, after all, not strangers to litigation regarding the imposition of a legal duty in the context of causing or preventing pure economic loss (see, eg, *Indac Electronics* (*Pty*) *Ltd v Volkskas Bank Ltd* 1992 1 SA 783 (A); *KwaMashu Bakery Ltd v Standard Bank of SA Ltd* 1995 1 SA 377 (D); *Energy Measurements* (*Pty*) *Ltd v First National Bank of SA Ltd* 2001 3 SA 132 (W); *Columbus Joint Venture v Absa Bank Ltd* 2002 1 SA 90 (SCA); *Commissioner*, *South African Revenue Service v Absa Bank Ltd* 2003 2 SA 96 (W); *Peterson v Absa Bank Ltd* 2011 5 SA 484 (GNP); and *Stols v Garlicke & Bousfield Inc* 2012 4 SA 415 (KZP)). It is submitted that Fourie J correctly refused to recognise a legal duty in the "new situation" before him and that it is in accordance with the statement by Brand JA in *Fourway Haulage SA* (*Pty*) *Ltd v SA National Roads Agency Ltd* 2009 2 SA 150 (SCA) para 25:

> "Another policy reason why the extension of delictual liability is sometimes refused is that it would impose an additional burden on the defendant which would be unwarranted or which would constitute an unjustified limitation of the defendant's activities" (with reference to *Minister of Law and Order v Kadir* 1995 1 SA

303 (A) 321C–J; *Steenkamp v Provincial Tender Board, Eastern Cape* 2006 3 SA 151 (SCA); and *Road Accident Fund v Shabangu* 2005 1 SA 265 (SCA).

In the end, the long shot taken by Spar to saddle Firstrand with delictual liability in the circumstances of this case, sadly missed (with apologies to Scott "An unsuccessful long shot aimed at effecting liability for causing pure economic loss – *Itzikowitz v ABSA Bank* 2016 4 SA 432 (SCA)" 2017 *THRHR* 483).

One point of criticism against *Spar* is the use of the term "duty of care" (see, eg, paras 8 11 12 13 55 56 57 of the judgment and the summaries in §§ 2 and 3 above) instead of the term "legal duty" in the context of wrongfulness. Fourie J on two occasions in his judgment used the terms as synonyms by saying "[t]he existence of a duty of care or a legal duty to prevent loss" (para 62) and "a legal duty (or a duty of care) to avoid economic loss" (para 66). It is better not to use the concept "duty of care" in the context of breach of a legal duty as test for unlawfulness. The "duty of care" concept is of English origin and is rather concerned with fault (negligence) and using the term indiscriminately may lead to confusion between wrongfulness and fault. This is succinctly explained by Neethling and Potgieter *Delict* 55 fn 120:

> "[T]he term 'duty of care' may lead to considerable confusion as it is traditionally employed to denote more than one meaning. Sometimes the term relates to *wrongfulness*: the existence of a legal duty to take steps to prevent loss, determined objectively and *ex post facto* (the 'duty issue'); on other occasions it relates to negligence: the duty to take reasonable care – to foresee and prevent loss (the 'negligence issue'). This sometimes results in a failure to distinguish between two fundamentally different elements of delict: wrongfulness and fault."

In the same vein, Van der Walt and Midgley para 81 state:

> "The enquiry into the existence of a legal duty and its breach is very different from enquiries into the so-called policy-based and fact-based notions of a duty of care. The question of a defendant's fault, or negligence, is not in issue. Fault must still be proved. If a duty of care is present, however, both wrongfulness and fault have been established" (footnotes omitted).

They refer (para 81 fn 30) to the warning expressed by Scott JA in *McIntosh v Premier*, *KwaZulu-Natal* 2008 6 SA 1 (SCA) para 12:

> "But the word 'duty', and sometimes even the expression 'legal duty', in this context, must not be confused with the concept of 'legal duty' in the context of wrongfulness which . . . is distinct from the issue of negligence. I mention this because this confusion was not only apparent in the arguments presented to us in this case but is frequently encountered in reported cases. The use of the expression 'duty of care' is similarly a source of confusion. In English law 'duty of care' is used to denote both what in South African law would be the second leg of the inquiry into negligence and legal duty in the context of wrongfulness. As Brand JA observed in *Trustees, Two Oceans Aquarium Trust* at 144F, 'duty of care' in English law 'straddles both elements of wrongfulness and negligence'."

CJ NAGEL
University of Pretoria