KEY POINTS

- The *Quincecare* duty is narrow, and banks will rarely be found to have breached it.
- *Singularis v Daiwa*, however, shows that where evidence of fraud is sufficiently clear, banks must prevent payments, failing which they will be in danger of breaching this duty.
- In such cases, the policy of protecting the customer which lies behind the duty will bar banks' reliance on arguments about attribution of knowledge and illegality to avoid liability.

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The banker's duty of care for fraudulent payments

This article considers the scope of the *Quincecare* duty on bankers who refuse to execute payments when "put on inquiry" that the payment is fraudulent. It analyses the recent decision in *Singularis v Daiwa*, a rare case where the duty was breached, and assesses whether the court was correct to reject the bank's reliance on technical arguments to defeat liability.

TAKING CARE FOR ANOTHER'S FRAUD: THE *QUINCECARE* DUTY

Barclays Bank plc v Quincecare Ltd [1992] 4 All ER 363

The bank agreed to loan £400,000 to Quincecare to buy four chemist shops. The loan was guaranteed by the second defendant, UniChem. Quincecare's chairman, Mr Stiller, requested that the bank advance £340,000 to a firm of solicitors he stated was acting for Quincecare. In fact, the solicitors had orders to pay the money on to an account in the USA belonging to Mr Stiller, who absconded.

The bank sought to recover the loan against Quincecare and to enforce the guarantee against UniChem; and Quincecare counterclaimed that the bank had acted negligently in making the payment to the solicitors because the circumstances of that payment should have raised questions in the mind of a reasonable banker as to whether Quincecare had in fact authorised it.

Steyn J set down the following propositions.

- The relationship of customer and banker is primarily that of debtor and creditor. However, in addition the banker acts as the customer's agent in drawing and paying the customer's cheques against the customer's money in the banker's hands.
- The same relationship applies where the banker acts on the customer's order to make a payment by immediate money transfer.
- An agent owes its principal a duty to exercise reasonable care and skill in carrying out the principal's instructions.
- The same rule applies to a banker making a bank payment on its customer's instructions.
- Accordingly, the banker owes the customer a duty of care in tort to take reasonable care when making such a payment; and a like duty will be implied into the contract between the banker and customer.

The judge explained the scope of the duty (the "*Quincecare* duty") as follows:

> 'In my judgment the sensible compromise, which strikes a fair balance between competing considerations, is simply to say that a banker must refrain from executing an order if and for as long as the banker is "put on inquiry" in the sense that he has reasonable grounds (although not necessarily proof) for believing that the order is an attempt to misappropriate the funds of the company… And, the external standard of the likely perception of an ordinary prudent banker is the governing one.'

Each case will turn on its own facts, but the starting point is that commercial dealings progress on mutual trust, and a bank will very rarely expect a director to defraud his company, and so will be slow to accept any such suggestion.

Steyn J dismissed Quincecare's contention that the bank had breached this duty. There was nothing out of the ordinary about the payment; and there was no reason to be suspicious of Mr Stiller.

Lipkin Gorman v Karpnale Ltd [1989] 1 WLR 1340

The Court of Appeal approved *Quincecare* very shortly after that case was decided. *Lipkin Gorman* concerned the payments a bank had made by honouring cheques drawn by a partner in a law firm who was using the firm's monies to fund his gambling addiction.

One of the firm's arguments was that the bank had been negligent in continuing to permit to draw and pay the cheques signed by the fraudulent partner.

The judge at first instance agreed that the bank's manager had shut his eyes or had wilfully and recklessly failed to inquire into the payments.

On appeal, their lordships accepted that the bank owed the firm a duty of care. Parker LJ reiterated the duty in similar terms to Steyn J in *Quincecare*, holding that the test was met when 'if a reasonable and honest banker knew of the relevant facts, he would have considered that there was a real or serious possibility, albeit not amounting to a probability, that its customer might be defrauded'.

The court also noted that the sheer number of cheques presented every day in banks ensured that it would only be "in rare circumstances" that a banker would breach its duty.

However, the court overturned the judge's finding on the facts.

This decision was later reversed by the House of Lords (at [1991] 2 AC 548), but on different grounds.

Verjee v CIBC Bank [2001] Lloyd's Rep Bank 279; and Fielding v RBS plc [2004] EWCA Civ 64

Following *Lipkin Gorman*, the courts have proved slow to find any breach of the *Quincecare* duty. This unwillingness applied a fortiori for individual account holders.

Verjee was an application to set aside a statutory demand presented by a bank against a customer whose account was over £20,000 in overdraft following the bank paying against a cheque which the customer alleged had been presented fraudulently. However, there was no dispute that the cheque bore the customer's own signature. Hart J considered that cases where the *Quincecare* duty arose would be rarer where the customer was an individual, because there was no agency problem arising in the case of an individual's account with only one authorised signatory. He held that there had been nothing to give the bank pause for thought in the instant case.

The Court of Appeal in *Fielding* considered a claim by a bank against an individual whose husband had drawn down considerable sums by cheque against a joint bank account without her consent. Both the defendant and her husband were signatories.

Potter LJ was concerned with the purpose of the transaction. He noted that '[w]here the account-holder is a commercial enterprise, there is scope for contending that in so far as the mandate relating to that account authorises the bank to lend money on overdraft, there is an implied qualification that any such lending must be for the legitimate purposes of that enterprise'. However, '[a]bsent some self-imposed limitation, of which the bank is on notice, it is in my judgment no concern of the bank how a husband and wife choose to operate the joint account, provided that such operation is in accordance with the express terms of the mandate'. In those circumstances, and combined with the lack of factors indicating to the bank that the wife had not consented to the payments, the court dismissed the wife's appeal.

These decisions indicated that the courts considered that there was little scope for the *Quincecare* duty in the case of individual account-holders because there is far less scope for unauthorised agents to defraud their principals. However, these cases are of considerably less import for consumers since 2009 because regulation 61 of the Payment Services Regulations 2009 imposes a far stricter duty on banks to repay unauthorised payments (from which duty banks cannot derogate by agreement).

SINGULARIS HOLDINGS LTD (IN OFFICIAL LIQUIDATION) V DAIWA CAPITAL MARKETS EUROPE LTD [2017] 1 LLOYD'S REP 226

The decision

The claimant, Singularis, was a company set up to manage the assets of its sole shareholder, Mr Al Sanea. It became insolvent following the collapse of Mr Al Sanea's business empire, the Saad group. Singularis sought to recover over $200m from the defendant Daiwa, Singularis' stockbroker.

Daiwa had held over $200m in an account for Singularis after closing out the stock lending relationship between the parties. Daiwa had subsequently paid the sums to companies within the Saad group on Mr Al Sanea's orders.

Rose J concluded that Mr Al Sanea had been acting in breach of his director's duties in ordering these payments. She rejected Singularis' contention that Daiwa had dishonestly assisted those breaches on the basis that none of Daiwa's employees had acted dishonestly in approving the payments.

However, she judged that Daiwa had made the payments negligently, in breach of the *Quincecare* duty; but she reduced the damages payable by 25% to represent Singularis' contributory negligence.

A number of factors of this decision are worthy of analysis.

Breach of the *Quincecare* duty

Rose J prefaced her decision that Daiwa had breached the *Quincecare* duty by noting that the factors which tended to militate against any such breach were not present in the case before her. First, Daiwa was not a licensed deposit-taker. Accordingly, it was reasonable to expect a higher level of scrutiny of the instruction for each payment order. Second, Daiwa's witnesses accepted that it was unusual for them to be instructed to execute payments to a third party rather than to the account-holder. This was a result of Daiwa's role as a stockbroker rather than an ordinary banker.

Although Rose J considered that Daiwa's breach of the *Quincecare* duty was so clear that she did not need to decide whether the scope of the duty was affected by the fact that Daiwa was not in a conventional banker–customer relationship with Singularis, her decision offers support for those seeking to argue that bankers offering specialised services will owe a modified *Quincecare* duty.

Thus, banks which hold advisory mandates with customers may be under a more strict duty given the increased likelihood that they will be "put on inquiry". This is coherent with established principles of agency law since the scope of the duties will be shaped by the precise nature of the relationship between principal and agent (see *Kelly v Cooper* [1993] AC 205).

In the event, the judge held that '[a]ny reasonable banker would have realised that there were many obvious, even glaring, signs that Mr Al Sanea was perpetrating a fraud on the company when he instructed that the money to be paid to other parts of his business operations [*sic*]'.

Those signs which were known to Daiwa were as follows:

(1) Mr Al Sanea's and the Saad Group's dire financial straits;
(2) Singularis had substantial creditors who may have been interested in the monies in the Daiwa account;
(3) Mr Al Sanea was operating the Daiwa account in a suspicious manner, moving money into and out of the account (which was not a deposit account) and requesting unusual payments to individuals employed by the Saad group; and

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(4) the production of a sham agreement to justify a large payment which was suspicious on its face.

Finally, Daiwa's dysfunctional structure meant that there was insufficient compliance oversight of payment orders. In those circumstances, the fact that Daiwa did not adopt a consistently high level of scrutiny but in some cases made payments without quibble led Rose J to conclude that Daiwa had been negligent.

The upshot of the judge's reasoning is clear: where there are a number of very clear pointers that a fraud is taking place, a bank is "put on inquiry" and cannot simply wave through payments. *Singularis* should be regarded as a strong case, albeit one which is entirely consistent with the scope of the *Quincecare* duty as laid down in the previous authorities.

Mr Al Sanea's fraud was no bar to relief

Daiwa argued that the *Quincecare* duty was ousted in *Singularis* because the claimant company was a one-man company, and so Mr Al Sanea's fraud should be imputed to the company, which was simply a vehicle of his fraud. The company may have had a claim against Mr Al Sanea, but it was no business of Daiwa's. Further, the claim was barred by the illegality defence, since the company had to rely on its own fraud.

Rose J rejected these arguments. Her fundamental reason was that to impute the knowledge of the fraud to the company would render the *Quincecare* duty otiose in just those situations where the company most needs protection from its banker. She also rejected the submission that Singularis was in fact a one-man company, in any event.

It is submitted that the judge was correct. First, this approach is consistent with *Bilta (UK) Ltd v Nazir* [2016] AC 1 in that the court considered the context and purpose for which the attribution of fraud is relevant. The context and purpose of the *Quincecare* duty is to protect a company where its agent seeks to defraud it and a prudent banker would have suspected such a fraud.

Second, the *Quincecare* duty is a narrow duty only arising when the bank is "put on inquiry" of the fraud. It is not unfair to expect the bank to take care in those circumstances, and to hold the bank to account if it does not do so, even in the case of one-man companies. The scarcity of cases in which a bank has been found liable for breaching the duty is testimony that the duty is not too harsh on bankers.

Third, it will frequently be the case, as here, that the company was in the "penumbra" of insolvency when the fraud was committed. The fraudulent director would thus be required to have regard to the company's creditors (see, eg *BTI 2014 LLC v Sequana SA* [2017] Bus LR 82), and he will often have breached that duty. At this stage, then, the company ceases to be a "one-man" entity and becomes the repository of the interests of the creditors as well as the shareholder. It is thus inappropriate for the court to attribute the shareholder/director's fraud to the company to the creditors' (further) loss.

Accordingly, it will generally be contrary to the public interest to uphold an illegality defence where a banker has breached the *Quincecare* duty – see *Patel v Mirza* [2016] 3 WLR 399.

The analogy with auditors' duties

The bank relied by analogy on *Berg Sons & Co Ltd v Adam* [1992] BCC 661, where the court had found that a one-man company could not succeed in suing its auditors for negligence in failing to identify its own fraud, because the fraud was to be attributed to the company. Rose J also considered two judgments in *Barings plc v Coopers & Lybrand* [2002] EWHC 461 (Ch) and [2003] EWHC 1319 (Ch) to assess whether Daiwa had an equal and opposite claim against Singularis for the deceit of Mr Al Sanea.

The judge rejected the approach in *Berg* on the basis that an auditor owes wide duties to the *shareholders* to report on the company's affairs, while the *Quincecare* duty is a narrower duty owed to the company to protect it from a fraud should the bank become aware of such. It is right that the differing duties should result in differing liability in one-man company cases.

However, Rose J accepted that the *Quincecare* duty and the auditor's duty to investigate the truth of a director's representations were sufficiently similar when dismissing Daiwa's counterclaim in deceit.

In both cases, the bank/auditor was obliged carefully to scrutinise what it was being told by the fraudulent director – the bank because it was "put on inquiry" and the auditor because of its duty of investigation – and so could not simply rely on the director's misrepresentations. This again seems to be the correct approach when the relevant duties are engaged. Should the deceit be outside the scope of a reasonable inquiry by the bank, of course, the bank will have a good counterclaim in deceit.

CONCLUSION

The *Quincecare* duty is narrow. There are few cases in which the duty will arise and a bank will be found to have breached it. However, the decision in *Singularis* shows that in a sufficiently clear case, a bank will be held to have breached the duty.

In such a case, the policy behind the duty will bar reliance by the bank on any technical arguments about responsibility for the company's fraud which aim to reduce or circumscribe that duty. ■

Further Reading:

- Refusing to execute payment instructions where a bank suspects money laundering [2009] 4 JIBFL 190.
- Banking law, fraud and agency in Jersey [2007] 3 JIBFL 143.
- LexisPSL: Banking & Finance: Bank accounts and political instability.