CLAW2204 – Exam study

Money, Risk and Regulation of Banking

- Sources of Law
    - Statute
        - *Corporations Act 2001*
        - *Banking Act 1959*
        - *Banks (Shareholdings) Act 1972*
        - *Financial Sector (Shareholdings) Act 1988*
    - Common Law
    - Equity Law
        - Estoppel
- Money
    - Economist definitions
        - Standard monetary unit of measurement
            - Measurement of the market value of something
        - Means of Payment
            - Mechanism for the exchange of goods and services
        - Store of value
            - Wealth can be held in money
    - Legal Definitions
        - Legal tender when issued by a central bank or recognised by a government as legal tender
        - Must accept legal tender for payment unless otherwise stated in a contract
        - Definition of a bank note
            - Promissory note, bill of exchange or other document which;
                - Records an engagement to pay money
                - Is payable to the bearer on demand and
                - Is designed to circulate as money
            - As defined in *Banking Act 2009 (England)*
        - Symbol of national sovereignty
    - Seignorage
        - Financial benefit of producing your own currency
    - Status
        - Notes Legal tender because of *Reserve Bank Act 1959*
        - Coins legal tender because of *Currency Act 1965*
        - Protection of counterfeit money under
            - *Crimes (Currency) Act 1981 (cth)*
- Regulation
    - Modern system introduced from the Wallis inquiry (1997)
    - 3 key regulators
        - RBA
        - APRA
        - ASIC

- Types of banks
  - Commerical
    - Accept deposits and honour cheques from their customers
    - They honour cheques or orders to draw money from their customers account
    - Keep accounts
    - Provide capital for money
    - *Commissioners of the State Savings Bank of Victoria v Permewan Wright & Co Ltd (1914)*
    - *United Dominion Trust Ltd v Kirkwood (1966)*
  - Investment banks
    - Corporate finance
    - Capital raising
    - Sales and trading
    - Research in capital markets
- Risks facing banks
  - Credit risk
    - Risk a borrowers will default on their loan.
  - Liquidity risk
    - Demand on funding, especially cash, to meet debt obligations that exceed to availability of cash.
    - Customers all want their money withdrawn but the bank runs out of cash
  - Market risk
    - Risk of losses in on and off balance sheet positions because of the changes in market positions
  - Operational risk
    - Risk of losses resulting from inadequate system, management failure, faulty controls, fraud or human error.
  - Systemic Risk
    - Risk of a breakdown of the entire banking system arising from the contagion effect of a large number of bank failures in one country or a number of countries
  - Legal risks
    - Losses from uncertainty due to legal actions of changes through the applicability or interpretation of contracts, laws or regulations
    - Some forms or clauses of contract may be unenforceable
- Operational risk
  - Has become an increasingly concerning issue as a result of the GFC and fears over the actions of rogue employees
  - Excessive risk may often turn into fraudulent activity
  - If a banker is doing well they are less likely to be looked into than an employee that is not doing well
  - *Barings Bank and Nick Leeson*
    - Singapore bank, continued to invest in the Nikkei in unauthorised transactions that destroyed the investment bank.
  - Methods to reduce risk
    - Lack of segregation between front and back offices.
    - Failure of senior management to understand the risks

Bank/Customer Contract & Bankers' Duties

- Debtor/Creditor relationship
  - When a customer deposits money with a bank the customer is the bank's creditor and the bank is the customer's debitor.
  - When a loan occurs the opposite is true
  - *Foley v Hill*
    - No fiduciary relationship
    - Money when paid to the bank is no longer the customer's it becomes the bank
    - The bank owes the same about plus interest as outlined in the contract as a debt to the customer
  - *Joachimson v Swiss Bank Corporation*
    - Bank is under no obligation to pay any money until a demand is made on it to make the payment of that money
    - The bank does not hold the money in trust
  - *Balmoral Supermarket Ltd v Bank of New Zealand (1974)*
    - Legal possession of the money is only taken by the bank once the money is counted and processed and a receipt provided to the customer
- Other relationships
  - Creditor/Debtor
  - Mortgagor/Mortgagee
    - Bank (mortgagee) makes a loan secured by property to the mortgagor
    - When the motagagee has a right to sell the property they must act in good faith to obtain a fair market value
  - Bailee/Bailor
    - Bank (bailee) takes control of personal property. The property is in the custody of the bank but is not the bank's
    - The bank must take reasonable care of the customer's property.
  - Agent/Principal
    - Where the bank acts as an agent of the customer
    - Responsibility to honour cheques or accept deposits etc
  - Trustee/Beneficiary
    - Bank (trustee) owes duties to the customer (beneficicary)
    - Bank has a duty to keep the funds separate from the other funds held by the bank
      - If the bank becomes insolvent the trust funds are available only to the beneficiaries and not the general creditors.
    - A bank may also become a constructive trustee
- Terms of the banking contract
  - There are many implied and express terms
  - Implied
    - Joachimson is an example
  - Many of these implied terms have now become express terms included in the relevant PDS
  - PDSs are a compulsory part of any banking relationship
    - Provided for in the *Financial Services Reform Act*