A LEGAL ANALYSIS OF BANK DUTIES AND LIABILITIES IN RELATION TO CUSTOMER PROTECTION IN UGANDA

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DECLARATION

I, declare that this thesis is the work of Imaniragaba Gloria alone except where due acknowledgement is made in the text, It does not include materials for which any other University degree or Diploma has been awarded.

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...17th/11/2015.........

Date

APPROVAL

I Certify that I have Supervised and read this work "A legal Analysis of Bank Duties and Liabilities in Relation To Customer Protection In Uganda" and in my opinion it conforms to acceptable standards of scholarly presentation and is fully adequate in scope and quality as a dissertation in partial fulfilment for the Degree of a Master of Laws (Commercial Law) of Kampala International University.

Name of supervisor ....Muhamud Sewaya........

Signature of supervisor ....

Date ....17/11/2015........

DEDICATION

I dedicate this piece of work, to the family of Mr. and Mrs. Maniragaba Claver of their wonderful contribution in my academic career.

ACKNOWLEDGEMENTS

Above all, the researcher thanks God the Almighty for his providence towards the accomplishment of this program in her life time.

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LIST OF ACRONYMS

BOU:	Bank of Uganda
CPR:	Civil Procedure Rules
CRB:	Credit Reference Bureau
GDP:	Gross Domestic Product
CRM:	Customer Relationship Management
IMF:	International Monetary Fund
MMSR:	Marketing Models of Service and Relationships
NPL:	Non Performing Loans
PIS:	Participating institutions

STATUTES

Anti-Money Laundering Act (2012)

Bank of Uganda act Cap 51

Bank of Uganda statute No 5 of 1993

Bill of Exchange Act Cap 68

Code of Good Banking Practice, 2003

Companies Act, 2012

Financial Institutions Act, 2004

The Foreign Exchange Act, 2004

Micro Finance Deposit Taking Institutions Act, 2003

Penal Code Act Cap 120

The Constitution of the Republic of Uganda 1995

GUIDELINES

Bank of Uganda Financial Consumer Protection Guidelines, 2011

The Financial Institutions (Credit Reference Bureau) Regulations, 2005

LIST OF CASES

Avi Enterprises Ltd v Orient Bank Ltd & Anor [2013] Ugcommc 65

Australia v Smith (1991) 102 ALR 453.

Bank of New South Wales v Rogers (1941) 65 CLR 42.

Bankers Trust Company v Shapira 1980 WLR 1274.

Broomfield v Kosow 212 NE (2d) 556 (1965)

Commercial Bank of Australia Ltd v Amadio(1983) 151 CLR 447.

Commercial Cotton Co v United California Bank 209 Cal Rptr 551 (Cal App 4th dist 1985) (at 554):

Cooper v National Provincial Bank Ltd [1945] 2 All E. R. 641.

Daly v Sydney Stock Exchange (1986) 160 CLR 371 At 385

Dart Industries Inc v Decor Corporation Pty Ltd (1993) 179 CLR 101

Deist v Wachholz (1983). 678 P 2d 188, 193

Dresdner Bank Vs Sango Bay Number 4 (1971) ULR 82.

Eckman and Others v Mildland Bank Ltd and Another (1973)1 Q.B 519.

G.A Schmittches Weigh v Leslie 1967 (2) comm.

Hilton v West minister Bank Ltd (1926) 135 LT 358

James v Australia and New Zealand Banking Group Ltd (1986) 64 ALR 351.

Keech v Sandford [1726] EWHC Ch J76.

Kornark Investments (U) Ltd. Vs Stanbic Bank Uganda Ltd Civil Suit NO 116 of 2010.

Lloyds Bank v Bundy (1975) Q.B 326

Makumbi v National Insurance Corporation (1979) HCB 230.

Marrison V Coast Finance Ltd (1966) 55 DLR (2d) 710 (BCCA).

McInerney v. MacDonald [1992] 2 SCR 138.

Muchinski v Dodds (1986) 60 ALJR 52.

National Bank of Hopkins v International Machines Corporation 156 NW 2d 86, 88-9 (1968)

National Provincial Bank of England Ltd v. Glanusk [1913] 3 K. B. 335.

National Westminster Bank v Morgan [1985] A.C 686

Nocton v Lord Ashburton [1914] AC 932

Obed Tashobya vs DFCU Bank Ltd HCT - 00 - CC - CS – 742 – 2004.

Ottoman Bank v Mawani (1965) EA 464.
Pastori Mukwatanise v Centenary Rural Development Bank Ltd (HCT-05-CV-CS-0066-2002).
Re Metway Bank Ltd (1991) 1 Qd R 120.
Robertson v Canadian Imperial Bank of Commerce (1995) ALL ER 825.
SC Bank of Marin V England (1996) 385 US 99.
Selangor United Rubber Estates v Cradock (No 3) [1968] 2 All ER 1073
Shaddock & Associates Pty Ltd v Council of the City of Paramatta [1981] 55 ALJR 713.
Standard Bank of West Africa v Attorney General of Gambia, (1972) 3 ALR comm.449.
Tassel v Cooper(1850) 9 C.B.509.

ABSTRACT

The thesis "Legal Analysis of Bank Duties Liabilities in Relation to Customer Protection in Uganda" is motivated by the background of the study to pertinently contribute remedies that can securely address the banking sector challenges in meeting duties and obligations to protect customers. It should be noted that while there is a law in place to govern bank duties and obligations to customers, in total this law has not been successfully drawn and implemented. The study examines the efficacy of the legal and institutional frameworks of banks in protecting customers. This is in order to establish why in the presence of good laws and policies the bank-customer relationship remains highly challenged. Reflecting on this setting, efficiency of the banking law in Uganda is examined particularly, in the execution of fiduciary duty in loan management. The purpose of the study is to find out the gaps in the existing legislation in the bank-customer protection relationship and to suggest possible interventions in meeting equity. Circumstances leading to breach of fiduciary duties were identified as failure to protect a trust, secret commissions and bribes, misleading advice, undue influences, conflict of duties and interest, lack of trust by bank customers among others and the Thesis provides recommendations. The study concludes that fiduciary issues are determined purposely to bring equity, but courts increasingly recognize bank failure in fiduciary duties owing to conflict of interest hence non performing loans. Legislative measures have to work hand in hand with customer consent.

CHAPTER ONE
GENERAL INTRODUCTION

1.1 Introduction

The study "Legal Analysis of Bank Duties and Liabilities in Relation to Customer Protection in Uganda" comes after the realization of increased seeking of equity intervention by customers as a matter of continued breach of banker-customer relationship world over[1]. ***Louis Kasekende, the deputy governor of the Bank of Uganda,*** **while presenting a lecture titled; "Corporate Governance and the Performance of the Financial Sector"**[2], said that "due to poor corporate governance in banks, several intrinsic characteristics of the financial sector make it particularly vulnerable to conflicts of interest whereby the "insiders", who are those with the power to control the management of financial institutions, can exploit their power to profit at the expense of other stakeholders, the so called "outsiders" who include depositors, non-controlling shareholders and the general public. More so information in banks is not perfect. Instead there are informational asymmetries. Insiders are often much better-informed about the future prospects for financial assets, which they control than are outsiders, in large part because the future value of such assets is subject to actions taken by the insiders themselves". There is also the inadequacy of support by banks in managing the new challenges of internet fraud and misrepresentation that result from the opportunities provided by the digital era hence challenges are on the increase.[3] The study therefore recognizes the universality of the duty and obligation of banks to protect customers and at the same time shows the difficulty in meeting this protection. It is admitted that

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[1] *Tournier v National Provincial and Union Bank of England* Ombudsman News (April 2005) the "banker's duty of confidentiality to the customer," Issue 45.

[2] *At the MUBS' 5th Annual International Leadership Conference on June 26, at which he presented a lecture titled; 'Corporate Governance and the Performance of the Financial Sector.'*

[3] *EDS U.S. Financial Services Privacy and Customer Relationship Management Survey," by EDS, 2005, page 8.*

there is a long history of concern with this duty more broadly the maintenance of the bank-customer relationship in both municipal and international law.

1.2 Background of the Study

The evolution of banking traces right from ancient Rome and during the Jewish renaissance period. Indeed according to De Albuquerque and Martim, it is asserted that it was during this period that the term bank was applied by the Jewish Florentine Bankers as adopted from an Italian word *banco* meaning desk/bench. The bankers would transact above a desk covered with a green cloth. However, with Matyszak[4] the story is different. Banking activity traces from the ancient times of Rome when moneylenders would set up stalls in the middle of enclosed courtyards called *macella* on a long bench called a *bancu* from which the words *banco* and *bank* are derived. Those that were in need of borrowing or exchanging would queue to be served. During this era the creditors had the power to imprison and destroy the lives of debtors, more likely to the international financial system of today for poor countries that borrow from developed states (In particular, where the International Monetary Fund (IMF) effectively acts as an agent of all international creditors to dictate economic policies and impose economic austerity programs other than imprison debtors).[5]

The relationship between customer and bank was merely a debtor-creditor relationship[6] until in 1924 when the duty to uphold the interests of customers became central to the policies of most banks[7] following ***Tournier's case.***[8] The notion of customer protection relationship is therefore not a new phenomenon to banks. Today, while banker's relationships with those who use their services are recognized to have a fiduciary nature in at least some of their aspects, the past

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[4] (2007)
[5] (2009), The Attorneys Forum: How does a Debt Management Plan work?
[6] John Glover, *Banks and Fiduciary Relationships*, Monash University.
[7] *Tournier v National Provincial and Union Bank of England* [1924] 1 KB 461.
[8] *Tournier v National Provincial and Union Bank of England.*

was different. Mutual obligations were thought to be entirely described by the terms of the contractual retainer subsisting between the parties[9] and implied contract as different from modern banking.

Apart from accepting deposits and channeling them to lending activities, today banks have become multifunctional institutions associated with security activities centered on the customer. For this, banking law must acknowledge the reality and include in its framework a discussion of securities law.[10]

Following the evolving nature of advanced technology misuses and cutthroat competition, bank duties and obligations have been and continue to be extended by the legal mandate to range from not only deposit taking, regulating and repayment, but also to concerns of fiduciary, confidentiality, care, and reliance among others, but such duties do not come without challenges. While customer Relationship Management (CRM) is arguably the most important area of concern, the banking industry remains constrained with limitedness of information and support. Indeed according to Ross, banks although seemingly closer to their customers, they are still failing to bring the relevant scale to bear in customer protection.

1.2.1 Evolution of the Banking Sector in Uganda

In Uganda like elsewhere, the evolution of the banking sector has been characterized by closures, mergers and acquisitions[11] mainly resulting from CRM approaches which affect the nature of protection expected. Before the country's independence in 1962, the banking sector was dominated mainly by foreign

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[9] John Glover, *Banks and Fiduciary Relationships,* Monash University.

[10] Ross Cranston, *Principles of Banking Law,* Second Edition, Oxford University Press, Pg 235.

[11] Beck, T. and Hesse, H., 2006. "*Bank Efficiency, Ownership and Market Structure: Why Are Interest Spreads So High in Uganda?", World Bank Working Paper Series WPS4027.TheWorld Bank: Washington, D.C.*

owned commercial banks[12] widely criticized for short-term lending. General discontentment over lending policies of these banks necessitated government intervention for the banking system to play a more supportive role in development.[13] This saw the establishment of Uganda Commercial Bank and Cooperative Banks with financial policies redesigned to control banking markets for developmental and other non-commercial objectives. By 1970 the banking market in Uganda had grown with over 290 branches but owing to political instabilities the number tremendously reduced to 84 during 1970 to 1980's[14] hence the financial repression.

Reforms were later on initiated in 1998 to address major misalignments of the banking sector that affected economic growth such as inefficient allocation of credit, limited access to services and an absence of a sound banking sector which guaranteed customer security.[15] New laws were enacted and the financial sector transformed with open market based approaches and divestitures.

The study conceptually perceives that the relationship of a banker to a customer is one of contract and is basic to all transactions and special other contracts which may arise as a matter of being in the relationship.[16] It is for this matter therefore that banks owe duties to their customers and have liabilities. In Uganda just like in the rest of the world, banks undertake a number of duties in protecting the customer. These range from the duty of care, secrecy, fiduciary to reliance, but never exhaustive. Some duties are considerably more important

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[12] Beck, T. and Hesse, H., 2006. "*Bank Efficiency, Ownership and Market Structure: Why Are Interest Spreads So High in Uganda?", World Bank Working Paper Series WPS4027.TheWorld Bank: Washington, D.C.*

[13]Adam Mugume *Market Structure and Performance in Uganda's Banking Industry .PP 9-10.*

[14] *Association of African Central Banks, November 2003.*

[15] Research report by Lawrence Bategeka and Luka Jovita Okumu (Economic policy Research centre, Uganda) Editors: Kavaljit Singh (madhyam), myriam Vander Stichele(SOMO) December 2010 at p9,*Banking Sector liberalization in Uganda Process, results and Policy options.*

[16] *Paget's law of banking Twelfth ed pg 115.*

than others and have often become the center of litigation in courts.[17] Therefore, the complexity of banking law as an obstacle to customer protection is not uncommon.

In different parts of the world, banks continue to grapple with equity issues with customers. For example in Europe and the United States of America, the banking industry is at the forefront of responding to opportunities provided by the digital era to deal with customer oriented challenges. While this is the case, sophisticated support remains limited especially where new internet fraud challenges arise. Commercial banks are facing greater challenges than ever before in their customer management strategies. As banks strive to create and manage customer relationships, several emerging trends affect the approach and tools banks employ to achieve growth in protecting their customers.[18] Challenges are on the increase for example in managing the security of growing customer contact channels; intensified competition has put customers at the center of decision making; managing escalating attacks on customer information; managing the rising customer expectations; and at the same time the challenge to effectively capitalize on new market opportunities alongside the executive agenda of banks.[19]

Just like the rest of world, Uganda experiences the same problems in its' banking sector. Challenges of customer protection have for long been widely experienced by banks in Uganda, let alone the rest of the world. Many reforms have been introduced as prior presented, but not much has been achieved and current efforts require to be stepped up if the banking sector policies are to make an impacting change in protecting customers.

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[17] Shamsul Bahrin Bin Baharuddin, (2005), "Duties of a Banker Towards his Customers" MARA Institute of Technology.
[18] EDS U.S. Financial Services Privacy and Customer Relationship Management Survey," by EDS, 2005, page 8.
[19] EDS U.S. Financial Services Privacy and Customer Relationship Management Survey," by EDS, 2005, page 8.

The Constitution[20] with due respect obliges Bank of Uganda to control the financial system for the stability of the economy hence endorses it with the power to regulate other banks with all their subsidiaries. The *Financial Institution Act*[21] with due respect obliges Bank of Uganda to control the financial system as endorsed by the Constitution to ensure stability of the financial economy. However being supervised by the central bank does not relieve banks of their contractual obligations.

The study is motivated by the above background to pertinently contribute remedies that can securely address the banking sector challenges in meeting duties and obligations to protect customers. It should be noted that while there is a law in place to govern bank duties and obligations to customers, in total this law has not been successfully drawn and implemented. The study examines the efficacy of the legal and institutional frameworks of banks in protecting customers. This is in order to establish why in the presence of good laws and policies the bank-customer relationship remains highly challenged. Reflecting on this background and setting, efficiency of the banking law in Uganda is examined particularly, in the execution of fiduciary duties in loan management while at the same time protecting customers.

Uganda's financial system is dominated by banking. Like many developing countries in Africa, Latin America and Asia, Uganda's banking system is centered in the capital[22] and big towns with a few if any financial service in rural areas. [23]

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[20] Constitution of the Republic of Uganda 1995, Article 162.
[21] Section 89
[22] Edith SM. Lederer (2006) *Association Press*.
[23] Kavaljit Singh (Madhyam), Miriam Vander Stichele *Banking sector liberalization in Uganda- (SOMO) (2010)*.

1.3 Statement of the Problem

Banking law[24] provides that, officers and directors are not expected to have a conflict of interest thus cannot take part in any discussion or decision of a matter in which they have an interest. The law also expects a director to stand in a fiduciary relationship and without derogation maintains the duty to; act honestly and in good faith; act in the best interest and for the benefit of the bank; act free from undue influence; access and be equipped with necessary information in order to be able to execute responsibilities effectively in addition to providing guidelines on investment advice to manage its assets and liabilities and freezing of accounts with funds which are proceeds of crime. The law also holds accountable the directors/managers/officers of banks who fail to take reasonable steps to secure compliance and those that knowingly or recklessly make statements or give information which is false or misleading in any circumstance that surrounds the banking sector.[25]

However, the laws have not effectively been designed and hence bank-customer relationship in Uganda remains complex and of great concern. Because corporate governance is low in banks, several intrinsic characteristics of the financial sector make it particularly vulnerable to conflicts of interest whereby the "insiders", who are those with the power to control the management of financial institutions, can exploit their power to profit at the expense of other stakeholders - the so called "outsiders" who include depositors, non-controlling shareholders and the general public. More so information in banks is not perfect. Instead there are informational asymmetries. Insiders are often much better-informed about the future prospects for financial assets, which they control than are outsiders, in large part because the future value of such assets is subject to actions taken by the insiders themselves. As a result, the balance sheets of banks are inherently not transparent, especially because a large share of their assets comprises loans

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[24] The Financial Institution Act (2004) Sections 54, 56, 60, 118 and 126.

[25] Banks in Uganda are governed by the *Financial Institution Act 2004*, the Code *of Good Banking Practice*, the *Anti-Money Laundering Act of 2012* and many more.

whose true value is not directly observable by outsiders. Hence it is very difficult for outsiders to evaluate accurately the true value of a bank's assets and thus its true financial condition.[26] Precisely customer awareness of bank duties and liabilities remains very low which has exposed banks to equity interventions as sought by customers.

The study therefore questions the effectiveness of the existing framework and how it guarantees security of the banking sector as well as that of customers to come up with positively impacting approaches from which lessons can be drawn to address the concerns therein. It is therefore hoped that this research will investigate the adequacy of the existing legal and banking policy frameworks that hinder the recognition of the bank-customer relationship causing persistence of equity charges and losses to banks in Uganda.

1.4 Purpose of the Study

The purpose of the study is to find out the gaps in the existing legislation in the bank-customer protection relationship to suggest possible interventions in meeting equity.

1.5 Objectives of the Study

1.5.1 General Objective

The major objective of this study is to analyze bank's Fiduciary duty in relation to customer protection in Uganda and to provide recommendations on how to bridge the gaps in the existing laws.

[26] Dealing with bank corporate governance risks. *Sunday, 06 July 2014 21:12* By the Independent Team. *Louis Kasekende (PhD), the deputy governor of the Bank of Uganda, was a key note speaker at the MUBS' 5th Annual International Leadership Conference on June 26, at which he presented a lecture titled; 'Corporate Governance and the Performance of the Financial Sector.'*

1.5.2 Specific Objective

i) To examine the legal framework of the financial sector in general and for the bank's fiduciary duty in particular in relation to customer Protection in Uganda;

ii) To examine the effectiveness of the legal and institutional framework governing bank Duties and Liabilities in Uganda in relation to Customer Protection in Uganda ;

iii) To examine the policy challenges facing the Financial sector while ensuring their fiduciary duty towards customers

iv) To provide recommendations and conclusions.

1.6 Research Questions

i) What is the general legal framework governing the financial sector in relation to bank duties in Uganda?

ii) What is the effectiveness of the legal and institutional framework governing bank Duties and Liabilities in Uganda in relation to Customer Protection in Uganda ;

iii) What are the policy challenges facing the Financial sector while ensuring their fiduciary duty towards customers.

iv) What are the possible recommendations and conclusions?

1.7 Scope of the Study

1.7.1 Geographical Scope

The study was carried out within the city center of the central region of Kampala District. Kampala district is selected purposely because it is a busy city with many different bank branches close to each other, hence was easy to reach in generating the required data for this study.

1.7.2 Content Scope

In terms of content, the study examines the recognition of customer protection as a bank's duty and obligation. It is limited to critically examining the effectiveness of the relevant municipal laws to the realization of customer protection issues to comprehend the effectiveness of the policies and frameworks. Under this component, fiduciary duties will be discussed. In terms of customer protection, loan management will be looked at. Examples are drawn from other jurisdictions in Africa and Europe to show that the realization of customer protection requires holistic interventions beyond statutory frameworks. It is hoped that this study shall contribute to the noble fight in protecting Uganda's financial institutions generally and to the upholding of fiduciary rights of customers specifically.

1.7.3 Theoretical Scope

In Uganda banks are among the most vulnerable institutions susceptible to losses upon failure to maintain their fiduciary obligations in protecting customers. Banks protect customers by maintaining their privacy and yet have a legal need to advise effectively and disclose by law. Failure of banks to meet their obligations implies a breach of contract. Violations of customer relations may lead to loss of customers, a drop in business, and customer shift exchanges. This study questions the challenges responsible for the continued breach of bank fiduciary obligations in customer protection in particular in the management of loans.

1.7.4 Time Scope

This research focuses on the period 1980 to 2014 with a brief historical perspective is provided for comparative purposes in generating sufficient data.

This period is singled out because it is during this time that the law[27] was adopted.

1.8 Significance of the Study

A clear perception and documentation of relationship between bank duties and obligations in customer protection is significant in establishing key approaches required to improve bank-customer relationship as this provides policy makers and implementers with information required to effectively plan for future interventions.

The study is also expected to provide information that will help the government, legislators, financial institutions, the community and academicians as well as researchers in the field of banking to promote the respect of bank duties and liabilities to customer protection. For the government and legislators, the findings of this study provide a basis for the review of the existing legal and policy frameworks governing the relationship between commercial banks and customers. For financial institutions, the community, stakeholders and other policy makers, the study findings provide material information for their programme designs.

The study enables policy makers to benefit from an improved understanding of the existing relationship between bank duties and obligations and customer protection issues in determining the alternative approaches to be adopted in improving the legal and institutional framework of banks. The findings further act as a guide to future researchers and academicians who will refer to it in narrowing down future gaps, thus it is an addition to the database to serve as a foundation for future reference in enriching researcher's skills and knowledge.

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[27] The Financial Institution Act (2004), the Code *of Good Banking Practice*, the *Anti-Money Laundering Act of 2012 and others.*

1.9 Literature Review

This part presents a discussion of the available information related to the fiduciary and secrecy duties and obligations of banks in protecting customers in loan management in particular. A lot of literature has been written about the subject of banks as financial institutions and their fiduciary duties and obligations most of which is regional and international but not quite much has been written specifically on banks in Uganda. The overall main challenge however is that not much specific literature has been written on the bank's duty and right to hold and disclose information in protecting customers. As a result, this section reviews literature on the subject with a view to identifying possible gaps in fiduciary banking laws that impact on customer protection. The review is presented in the order of objectives and a number of the concepts are explained.

1.9.1 Concepts, Ideas and Opinions from Authors and Experts.

Bank; it is a financial intermediary that accepts deposits and channels them into lending activities and thus active players in the financial markets.[28] Hart defines bank as a company carrying on business of receiving moneys, and collecting drafts for customers subject to obligation of honoring cheques drawn upon them from time to time by the customer to the extent of the amounts available on their accounts.[29] Banks are further defined as multifunctional institutions that accept financial deposits from customers to channel them to lending institutions, provide transactional advice, offer loans to customers, bank overdraft, standing orders, make direct debits, credit transfers, travelers cheques and provide reconciliation statements.[30] In Uganda, it is any company licensed to carry on

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[28] Ross Cranston, *Principles of Banking Law*, Second Edition, Oxford University Press, Pg 235.

[29] Shamsul Bahrin Bin Baharuddin, (2005), *"Duties of a Banker Towards his Customers" MARA Institute of Technology.*

[30] Mugerwa James *Commerce for Schools and Colleges, Revised Edition, Uganda Catholic Training Center 1996.*

financial institution business as its principal business, as specified in the Second Schedule to the *Financial Institution Act* and includes all branches and offices of that company.[31] Here court must ascertain without prejudice the businesses predominated primarily by the institution.

A fiduciary is someone who has undertaken to act for and on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence.32 Fiduciary responsibilities not only involve relations of debtor and creditor but expressed accordingly on a running account basis, within the paradigm of an exclusively contractual relation.33 These are usually circumstances where the contract specifies a degree of trust and loyalty or it can be inferred by the court.

Bank Duties; express the obligations or functions of the bank to collect deposits and maintain them safely, regulating credit, duty to repay on demand, conforming to customer instructions, fiduciary duty,[34] duty of reliance or duty to disclose[35] and power to regulate unconscionable conduct, the duty of care in carrying out the contract,[36] and the duty of secrecy.[37] According to **Mugembe (2008)**[38], a bank is conducting banking normally when it; accepts deposits of money from the public repayable on demand or at the expiry of a fixed period or after notice, employ such deposit wholly or partly by lending or other means for the account of and the risk of the person accepting the deposits, present to another bank for payment, cheques, drafts or orders received from customers.

[31] Section 3 of the *financial institutions act of 2004.*
[32] *Bristol & West Building Society v Mothew* [1998] Ch 1 at 18.
[33] *Re Metway Bank Ltd* (1991) 1 Qd R 120.
[34] *Golby v Commonwealth Bank of Australia* (1999) 72 FCR 134 at 136.
[35] *Demagogue Pty Limited v Ramensky* (1992) 39 FCR 31 at 32.
[36] *Selangor United Rubber Estates v Cradock* (No 3) [1968] 2 All ER 1073.
[37] E.P. Ellinger and Eva Lomnika, *Modern Banking Law* 3rd Edition, Oxford University Press, USA, 2002.
[38] *Electronic banking and effective financial performance.*

Bank Customer; According to **Shamsul**[39] it is argued that when a person opens an account with a bank, it is seldom realized that a contract has been entered in form of debtor-creditor relationship which establishes the duties of both parties. In Uganda the law does not precisely specify in definition the bank customer and thus decided cases can be referred to appreciate the legal interpretation of what constitutes a customer.

The study therefore borrows from **Rust and Siong Chung**[40] theory of Marketing Models of Service and Relationships (MMSR) to comprehend the banking sector marketing strategies and how these affect their services and relationships in protecting customers. While the theory appreciates analytical approaches to pricing, it does not ignore emerging issues of the approaches such as trade-offs between privacy and customization which attract increasing attention and personalized interactions. The theory holds that the long term value of a firm is largely determined by the value of the company's customer relationships which result in equity. And that the nature of relationships increasingly leads to financial impact examined within customer and across product rather than the traditional reverse hence the increasing importance of analyzing customer lifetime value as well as managing the firm's customer equity.

Indeed according to **Ross Cranston**[41] bank's security services are centered on the customer hence in this pretext banks should not only become customer centered but examine their system within the challenges that may arise in the Bank-customer relationship as a result of the customer contribution. Indeed the Tournier case approach attributes the realization of the right to secrecy as more

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[39] Shamsul Bahrin Bin Baharuddin, (2005), "*Duties of a Banker Towards his Customers" MARA Institute of Technology.*

[40] Roland T. Rust and Tuck Siong Chung (2006), *Marketing Models of Service and Relationships, Rober H. Smith School of Business, University of Maryland, College Park.*

[41] Ross Cranston, *Principles of Banking Law,* Second Edition, Oxford University Press, Pg 235.

than just an implementation of the law.[42] The approach confers upon banks an implied duty not to divulge information to third parties[43] unless under special circumstances demanded by law[44] to draw evidence on potential financial fraud.

In this similar regard ***E.P. Elliger and Eva***[45] state that economically a person whose calling involves confidential work would, if engaged at law have a discretion that can be relied upon in certain cases in the interest of the state as this is given much more significance than the customer's interest. This study puts into consideration the effectiveness of the need for banks to explore potential customer challenges and inform customers about the details of the relationship at the beginning of the relationship as a principle of good banking practice, hence the customer optimal interactions proposed by Rust and Siong Chung in the adopted theory.

1.9.2 Banks Fiduciary Responsibilities and Duties

Fiduciary responsibilities are related to a party's reliance on another and take two forms as explained by John Glover.[46] A) the one sided, where a party places trust in and relies on the other because he or she is reasonably entitled to do so in the circumstances, or because the reliant party is in a position of vulnerability, subordination or information inequality. The customer relies on the bank's trust-worthiness and trust is invested in the bank and b) the two-sided': where it is mutual, or reciprocated, as in a partnership or joint venture. We are concerned with the 'one-sided' case.

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42 World Health Organization (WHO), Trends in Maternal Mortality: 1990 to 2010. WHO, UNICEF, UNFPA and the World Bank Estimates, 2012. Available from www.unfpa.org/webdav/site/global/shared/documents/publications/2012/Trends_in_maternal_mortality_A4-1.pdf.

43 Andrew Laid Law and Graham Robert , *Law Relating to Banking Law*, London, 1992.

44 Grace Patrick T. Mukubwa, *African Banking Law and Practice*, Uganda Law Watch, 1998.

45 Supra No.37

46 John Glover, *Banks and Fiduciary Relationships, Bond Law Review: Monash University Vol.7: Issue 1, Article 5. 1995. available at http://epublications.bond.edu.au/blr/vol7/iss1/5*

According to Glover, the most common circumstance where a fiduciary duty will arise is between a trustee whether real or juristic, and a beneficiary. The trustee to whom property is legally committed is the legal common law owner of all such property. The beneficiary, at law, has no legal title to the trust; however, the trustee is bound by equity to suppress his own interests and administer the property only for the benefit of the beneficiary. In this way, the beneficiary obtains the use of property without being its technical owner. Others, such as corporate directors may be held to a fiduciary duty similar in some respects to that of a trustee.

This happens when, for example, the directors of a bank are trustees for the depositors, the directors of a corporation are trustees for the stockholders or a guardian is trustee of his ward's property. A person in a sensitive position sometimes protects himself from possible conflict of interest charges by setting up a "blind trust" in placing his financial affairs in the hands of a fiduciary and giving up all right to know about or intervene in their handling.

In English common law fiduciary relation is arguably the most important concept within the portion of the legal system known as equity thus once a fiduciary duty is imposed equity requires a stricter standard of behavior. When a fiduciary duty is undertaken by the bank it creates an ethical relationship of confidence and trust between the bank and customer when customer justifiably reposes confidence, good faith, reliance and trust in the bank whose aid or protection is sought in some matter.[47] Accordingly, in such a relationship, good conscience requires to act with loyalty to those interests for the sole benefit of customer. A fiduciary has a duty not to be in a situation where personal interests and duty conflict, a duty not to be in a situation where his fiduciary duty conflicts with another fiduciary duty, and a duty not to profit from his fiduciary position without

[47] Stephen Warne, *The Latest on Fiduciary Relationships, on professional negligence, regulation and discipline around the world., the latest on fiduciary relationships.htm J;* News Limited v Australian Rugby Football League Limited.

express knowledge and consent. A fiduciary cannot have a conflict of interest thus fiduciaries must conduct themselves "at a level higher than that trodden by the crowd[48] and that the distinguishing or overriding duty of a fiduciary is the obligation of undivided loyalty.[49] In this similar regard, banks as fiduciaries are not expected to have conflicting interests.

Glover[50] portrays that modern banking practices involve a highly complicated structure of credit and other complexities which often thrust a bank into a role of an advisor, thereby creating a relationship of trust and confidence which result in a fiduciary duty thrust upon the bank.[51] In this same regard Glover notes that property in the money was treated as transferred outright and the banker is only obliged to account to the depositor for the value of what was entrusted despite the customer's deposits with the banker. Mutual obligations of the parties from the time of the deposit are expressed accordingly on a running account basis, within the paradigm of an exclusively contractual relation. Similarly Njaramba **Gichuki**[52] presents this as a duty of trustee when bank owes a duty of care to the beneficiary of a trust but may not be liable as a trustee unless appointed as such.

Stephen Warne points out that, courts have consciously refrained from attempting to provide a general test for determining when persons stand in a fiduciary relationship. The term "fiduciary relationship" defies definition. This owes to the difficulty of stating a comprehensive principle suitable for application to different types of relationships that carry different obligations. For this, courts have recognized certain classes of persons as falling within established categories of fiduciary relationships. Examples of these include trustee and

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[48] [1996] 186 CLR 71.
[49] [1998] 1711 FCA.
[50] John Glover, *Banks and Fiduciary Relationships*, Monash University.
[51] *Deist v Wachholz* (1983). 678 P 2d 188, 193.
[52] Njaramba Gichuki, *Law of Financial institutions in Kenya pp101-102.*

beneficiary, agent and principal, solicitor and client, director and company, employee and employer, and partners. Apart from the established categories therein, perhaps the most that can be said is that a fiduciary relationship exists where a person has undertaken to act in the interests of another and not in his or her own interests but all of the facts and circumstances must be carefully examined to see whether the relationship is in substance fiduciary.[53]

However, several other factors have been referred to as pointing to the existence of a fiduciary relationship which are important. But these can only be to the extent to which they disclose an expectation in one party that the other will act in his or her interests as summarized in Professor Finn's remarks on Equity, Fiduciaries and Trusts that;[54]

> *the actual circumstances of a relationship are such that one party is entitled to expect that the other will act in his interests in and for the purposes of the relationship to include ascendancy, influence, vulnerability, trust, confidence or dependence doubtless as important in making this out only to the extent that they evidence a relationship suggesting that entitlement.*

The critical matter in the end is the role that the alleged fiduciary has, or should be taken to have, in the relationship. It must so implicate that party in the other's affairs or so align him with the protection or advancement of that other's interests that foundation exists for the 'fiduciary expectation.[55]

According **to Stephen Warne**, it is established that contractual and fiduciary relationships may co-exist if relationship conforms to the terms of the contract and if it cannot be superimposed upon the contract in a way that alters the operation of which the contract was intended to have during its construction. But

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[53] Youdan TG (ed), *"The Fiduciary Principle"*, Equity Fiduciaries and Trusts, *Law Book Co, 1989, at p 46-47.*
[54] Supra no.54,
[55] Supra no.55

a contractual term may be so precise in its regulation of what a party may do that there is no scope for the creation of a fiduciary duty. In Warne's view therefore, it is open to the parties to a contract to exclude or modify the operation of fiduciary duties.

It may well be that a fiduciary cannot exclude liability for fraud or deliberate dereliction of duty but beyond that there appears to be no restriction in the law to prevent a fiduciary from contracting out, or modifying his or her fiduciary duties, particularly where no prior fiduciary relationship existed and the contract defines the rights and duties of the parties as expressed in the **Law Commission Consultation Paper.**[56]

A fiduciary relationship is said to be founded upon a contract where the ordinary rules of construction of contracts apply. Whether a party is subject to fiduciary obligations and the scope of any fiduciary duties is to be determined by construing the contract as a whole in the light of the surrounding circumstances known to the parties and the purpose and object of the transaction.

A fiduciary relationship arises between a financial adviser and its client where the adviser holds itself out as an expert on financial matters and undertakes to perform a financial advisory role for the client.[57] The same principle will usually apply to financial advisers and corporate advisers. Each will owe fiduciary obligations to the client because each undertakes to act in the client's interests and not solely in its own interests.

According *to* **Stephen Warne,** a bank which gives its customers financial advice in the course of a transaction that includes an advance of money to the client may be in a fiduciary relationship with the client in its role as adviser. The bank may be expected to act in its own interests in ensuring the security for the loan

[56] *Law Commission Consultation Paper Fiduciary Duties and Regulatory Rules,* United Kingdom, Report No 236 (1995) at 2.11, 7.3. 3.3.13

[57] *Daly v The Sydney Stock Exchange Limited* (1986) 160 CLR 371 at 377

but it will undertake fiduciary obligations to the client if it creates an expectation that it will advise in the customer's interests on the wisdom of the investment.

In order to be exonerated, a fiduciary must give full and frank disclosure of all material facts and consent need not be given expressly; it may be implied in all the circumstances.

According to **Njaramba Gichuki**[58] by acting as an agent to the customer, the bank performs a duty of care by paying and collecting cheques and thus may be held liable if it pays a forged or altered cheque.

Paul Raby[59] also states that the duties of a bank are to comply with the customer's mandate and admits the importance of realizing that this duty not only refers to the original mandate completed when the customer opened the account but also various other documents which are interpreted as a banker's mandate, including standing orders, direct debits and cheques (for detailed discussion on each of these, see subsequent chapters). By paying a cheque bearing a forged signature or paying an incorrect amount on a standing order, the bank will have acted in breach of its mandate. The bank is effectively the customer's debtor and this duty is merely the ability of the customer to demand repayment of his debt, the bank promises not to cease to do business with the customer except after giving reasonable notice. But reasonable according to Raby varies from account to account depending on the circumstances and complexity of the account. However he does not discuss how a bank can avoid liability and the defences available to the bank in case it breaches its duties.

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[58]Supra No.52 *p101-110.*
[59] Associateship Series: *Law Relating to Banking services 2nd edn p 6-7.*

Like the rest emphasize on duty of care, **Slaughter and May**[60] complement that the primary duty of a banker is to comply with the terms of a customer's mandate as this is a contractual duty and that a bank incurs liability for breach of contract if it fails without a proper reason to give effect of its customer's instructions. A bank is therefore exposed to a claim for damages if it refuses to repay a deposit or to honor a cheque drawn on an account.

According to **Alliot J**[61] a bank is entitled to treat the customer's mandate at its face value save in extreme cases and that banker is not obliged to question any transaction which is in accordance with the mandate, unless reasonable banker would have grounds for believing that the authorized signatories are misusing their authority for the purpose of defrauding their principal to defeat his true intention. J. Alliot adds that if a bank doesn't have reasonable grounds for believing that there is fraud then it must pay and that mere suspicion or unease do not constitute reasonable grounds and are not enough to justify a bank in failing to act in accordance with a mandate. A fiduciary duty is the highest standard of care at either equity or law thus fiduciary is expected to be extremely loyal to the principal, he must put his personal interests before the duty, he must not profit from his position unless by consent of principal. The researcher agrees with the position that the bank should avoid conflict of interest and should not profit itself at the expense of the bank customers meaning that the bank should give proper accountability. However the author does not provide any literature on how the banks should avoid liability.

Fiduciary relationships of trust may be often found in the undue influence type of case. The relationship is based in the customer's reliance and not the bank's wrong. Transactional advice can result in a fiduciary relationship with bank and

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[60] *Apaper on civil liability for money Laundering.*
[61] *Hilton v West minister Bank Ltd* (1926) 135 LT 358.

customer. In the ***1992 Martin committee report,***[62] the view was adopted that current case law was inadequate in relation to the 'fairness' of guarantee liabilities between banker and customer. Relevant advice and disclosure requirements at the moment were said to be insufficient. In place of the case law regime proposed a Code of Banking Practice and a co-operative scheme to regulate this and other aspects of the banking relationship.[63] Fiduciary doctrine may yet expand to incorporate these recommendations.

In the course of protecting its customer therefore banks also have a duty to advise accurately.[64] In any given case the court is concerned with the particular contract or the duty of care in tort in case of an allegation. This is in addition to the proximity of the parties, reasonableness and justice on the particular facts. The paying bank has a duty of care to protect the customer from fraud of agents during the issuance of cheques and other payment orders. The bank should be in position to provide financial and investment advice as well as explain the effect of security documents. The above argument is in support of the researcher's topic and as such the researcher agrees with the position of the above author.

To sum up the literature review, the researcher identified some gaps in the literature which are that;

Though a few authors have written about fiduciary duties in relation to customer protection many concentrated on the duty of care and less has been written about Ugandan banks and this gap has been filled up by providing that the bank-customer relationship is not only about customer deposit taking and safety security, but involves a relationship of trust arising from the constructs of ordinary rules that apply in fiduciary contracts which henceforth impose on the bank the duty of fiduciary to advise reliably with due protection to the customer's

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[62] A pocket Full of Change: *Banking and Deregulation report of the House of Representatives Standing Committee on Finance and Public Administration (1992).*

[63] Australia Bankers Association Code of Banking Practice : *Part B 'Principles of Conduct'* 1993, *7.0-19.1.*

[64] *Law of Banking 12th edn p 119.*

interests such that Ugandan banks can draw from this and learn how to treat their customers and there is nothing much which has been written in relation to loan management in terms of customer protection yet this is a very sensitive area of concern because Insiders are often much better-informed about the future prospects for financial assets, which they control than are outsiders, in large part because the future value of such assets is subject to actions taken by the insiders themselves. especially because a large share of their assets comprises loans whose true value is not directly observable by outsiders. Hence it is very difficult for outsiders to evaluate accurately the true value of a bank's assets and thus its true financial condition.[65] Precisely customer awareness of bank duties and liabilities remains very low which has exposed banks to equity interventions as sought by customers. The researcher filled this gap by providing all important aspects pertaining to bank's Fiduciary duties in relation to loan management in Uganda sand these authors have not provided any avenues on how banks can avoid liability. According to the researcher, the banks can avoid liability by not providing transactional advice which does not tally with their obligation or carrying out any unconscionable dealings and upholding the principle of Know Your Customer (KYC).

The Authors did not point out the policy challenges facing banks in trying to meet their fiduciary duties in relation to Customer Protection in Uganda. In the researcher's analysis, the challenges are; cut throat competition; Need to raise strong revenues and sound profits which makes banks to over ride some of their policies, Money laundering which has become a threat to the banking sector. In the researcher's opinion the following can be overcome by; ensuring that, those that participate in the legislative process must be knowledgeable enough to

65 Dealing with bank corporate governance risks. *Sunday, 06 July 2014 21:12* By the Independent Team. *Louis Kasekende (PhD), the deputy governor of the Bank of Uganda, was a key note speaker at the MUBS' 5th Annual International Leadership Conference on June 26, at which he presented a lecture titled; 'Corporate Governance and the Performance of the Financial Sector.'*

understand the interpretation and application of the laws if effective laws are to be designed because financial institutions operate under strain due to the absence of proper legislation of debtor/creditor law in protecting the existing customer-bank relationship as seen to be drawn from various legislations which makes the supervisory response procedure a little too slow and weak due to the long process which requires drawing various legal issues to rely upon from the law of insolvency, mortgage, and others which makes debt legislation problematic and at times results into closure of banks in Uganda, Banks require conducting periodic training programmes on ways of combating crimes in the banking system of their customers and other clients when entering other business premises for business relations. This will help organizations to assess the risk it faces in doing business with the client, where there is a former credit rating agency or credit bureau, it is advisable to get in touch with them, There is need for financial institutions to devise mechanisms and systems that can track suspicious transactions such as unusual huge cash deposits by individuals who usually deposit cheques, sudden increase on an account which is then quickly withdrawn and customers who deposit certain counterfeit notes or forged instruments[66] they should also have clear instructions to handle cases of suspicious transactions, In case of fiduciary duty breaches, accountability is a good remedy. It is usually used where the breach of duty was ongoing or when the gain is hard to identify. The idea of an account of profits is that the fiduciary profited unconscionably by virtue of the fiduciary position, so any profit made should be transferred to the beneficiary. The calculation of profits in this sense can be extremely difficult, because profit due to fiduciary position must be separated from profit due to the fiduciary's own effort and ingenuity the last remedy is to seek compensatory damages. Accounts of profits can be hard remedies to establish, therefore, a plaintiff will often seek compensation (damages) instead.

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[66] Shamsul Bahrin, Bin Baharuddin,(2005), "*Duties of a Banker towards his Customers*" MARA Institute of Technology.

Another gap is that no Author tackled the effectiveness of the legal and institutional framework governing banks fiduciary duties in relation to customer protection in Uganda since no much literature has been written about Ugandan banks. The researcher filled up this gap by critically analyzing the relevant laws to determine their effectiveness.

1.10 Methodology

According to the purpose of this study, the design that was adopted was desk legal research meaning the research was conducted using the Library materials. The researcher used both primary and secondary sources.

The study employs a descriptive study design approach particularly observing the qualitative aspects of research as reflected from desk reviews to acquire in-depth understanding of study within a limited time.

1.10.1 Study Design

The study reflects on a qualitative research design as a method of looking at things *holistically and comprehensively, to study it in its complexity and to understand it in its context*[67] based on carefully selected materials from various textbooks, journals and internet sources on banking in order to capture an in-depth description and analysis of the views of the different stakeholders involved in customer-bank relationship.

The major feature of qualitative research is reflected in its designs, being naturalistic and preferring to study things, people and events in their natural settings.[68] Silverman adds that qualitative methods are especially interested in how people observe and describe events[69]. He argues that this gives room for flexibility and for an in depth focus on the study being conducted since the data obtained is in words rather than in numbers.

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[67] Punch, K.F (2005) *Introduction to Social Research , Qualitative and Quantitative approaches, sage Publication limited, London. P.186.*

[68] Silverman, D.(2005) *Doing Qualitative Research, Los Angeles: sage Publication limited, p.140*

[69] *Supra no.67 at pg170.*

The target population consists of banking officials, customers, lawyers, legislators and actors involved in banking institution dealings. Information regarding different banks was considered, the banks in Uganda in particular to provide a better platform during data collection following the commonality of bank-customer relation issues in Uganda.

The secondary data collection method was adopted. This included reviewing the already existing literature on bank duties and obligations in respect to customer protection issues from textbooks, pamphlets, legal reports, databases and electronic publications. This was purposely adopted to avoid biases in data collection as detailed information on fiduciary duties cannot be openly collected from banks, just like some banks do not have banking policies.

1.11 Synopsis of the Chapters

Chapter one provides the General introduction to the study, background of the study, the problem statement, purpose of the research, the objectives of the study, the research questions, Scope of the study, Significance of the study, research methodology, and literature review. Chapter two examines the normative framework governing financial institutions (banks) in particular with their fiduciary duties and obligations in protecting customers at the international and national levels. The third chapter details the examination of the effectiveness of the policy and institutional frameworks governing bank duties and obligations in customer protection. Chapter four presents policy challenges facing the financial sector while ensuring their fiduciary duty towards customers and Chapter five provides conclusions and recommendation resulting from the research.

1.12 Conclusion

The bank-customer relationship is not only about customer deposit taking and safety security, but involves a relationship of trust arising from the constructs of ordinary rules that apply in fiduciary contracts which henceforth impose on the bank the duty of fiduciary to advise reliably with due protection to the customer's interests.

CHAPTER TWO

LEGAL AND INSTITUTIONAL FRAMEWORK GOVERNING BANKING IN UGANDA

2.1 Introduction

Banks as financial intermediaries constitute a fundamental component of the financial system in financial markets hence active players. Banks have become multifunctional institutions with core banking associated with securities activities which were institutionally separate in the past.[70] In this regard banking law must acknowledge the reality and include in its framework a discussion of securities law. Banker's relationships with those who use their services are recognized to have a fiduciary nature in at least some of their aspects.[71]

While mutual obligations were traditionally thought to be entirely described by the implied terms of the contract[72] modern banking practices have imposed a stricter liability with a highly complicated structure of credit and other complexities resulting from a fiduciary relationship of trust and confidence.[73] Similarly, is the duty of secrecy under which banking confidentiality has widely been recognized as playing a legitimate role in concealing the financial affairs of individuals and legal entities as traced from various judge made laws and implied terms in contract. This study examines the law that governs banks in executing their fiduciary responsibilities in the management of loans.

2.2 Structure of Uganda's Financial Structure.

Uganda's financial system is composed of formal institutions that include banks, microfinance Deposit-taking institutions, Credit institutions, Insurance

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[70] Ross Cranston, *Principles of Banking Law*, Second Edition, Oxford University Press, Pg 235.
[71] John Glover, *Banks and Fiduciary Relationships*, Monash University.
[72] *Joachimson v Swiss Bank Corporation* [1921] 3KB 110, 117.
[73] *Deist v Wachholz* (1983). 678 P 2d 188, 193

companies, Development Banks, Pension Funds and Capital Markets; the semi informal institutions that include savings and Credit Cooperative Associations (SACCO) and the other Microfinance institutions, whereas the informal ones are mostly village savings and loans associations. Formal institutions are less prominent in rural areas than urban areas, only serving 14% of the rural population. Informal institutions play an important role in the rural service provisions being that they serve approximately 12% of the rural population [74] and that these numbers indicate that Uganda's financial system is still quite shallow. With regard to access to finance, approximately 62% of Uganda's population has no access to financial services. The number of the population holding accounts in banks is 4 million which is 33% of the 12 million who are bankable thereby leaving the savings to GDP ratio low at 16%. In addition, the financial intermediation as indicated by the stock of private sector credit is so poor at about 11.8% of GDP

Bank of Uganda (BOU) is the Central Bank of the Republic of Uganda. It was opened on the 15th of August 1966. It is 100% owned by the government of Uganda though, however, it is not a government Department. Bank of Uganda works and conducts all its activities in close association with the ministry of Finance, Planning and Economic Development. The primary purpose of the Bank is to foster price stability and a sound financial system. Together with other institutions, the bank also plays a pivotal role as a centre of excellence in upholding macroeconomic stability within the country[75]

The banking sector in Uganda underwent significant restructuring in the early 2000s, several indigenous commercial banks were then declared insolvent, taken over by the central bank and eventually either sold or liquidated. Therefore in the passage of the banking bill of 2004 in parliament new banking institution

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[74] ABC Capital Bank, (2012). *The financial sector in Uganda.* Retrieved from: http://www.abccapitalbank.co.ug/index.php/financial-literacy/the-financial-sector-in-uganda

[75] Bank of Uganda (2013) *welcome to bank of Uganda.* Retrieved from; http://www.bou.or.ug/bou/home.html.

classification guidelines were established. The moratorium on new banks was lifted in July 2007 and during the eighteen months of lifting the moratorium new commercial banks were licensed. During 2008 and 2009, several existing banks went on an accelerated branch expansion either through mergers and acquisition or through new branch openings and this was recorded to be the highest growth in the years. As far as October 2012, there were 24 licensed commercial banks in Uganda, with nearly 500 bank branches and a total of almost 600 automated teller machines[76].

2.3 Bank reforms in Uganda

Faced with increasing economic difficulties and influenced by the worldwide trend toward adjustment policies, the government since 1987, embarked on a wide-ranging structural reform programmes. By the late 1980s, the institutional fabric of the banking industry was severely damaged as a result of misguided financial policies and the effects of civil war and economic decline. This therefore necessitated reforms to liberalize the financial sector and enhance its efficiency. The key financial sector elements in the structural adjustment policy package were the usual traditional policies aimed at resource mobilization.

The reforms started in 1988 with a reduction in directed credit (lending by the government or central bank directly or indirectly). However, major and wide ranging reforms were carried out in the 1990s. These included revision of banking sector laws and regulations, liberalization of interest and exchange rate policy and abolition of controls in current and capital accounts. By 1997, significant policy reforms had been implemented. As the liberalization policy was being pursued, the Government, through privatization, also divested from owning and operating commercial banks.

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[76] Bank of Uganda (2013), *Annual Headline Inflation Rises to 8.0 percent in September*.

Some of the reforms include[77]:

2.3.1 Interest rate liberalization

Interest rate regulations changed by adjusting nominal interest rates to match inflation in 1989.Treasury bill market changed from ad hoc issuance to a market based auction system through which interest rates were determined in1992. Interest rates were fully liberalized and the Central Bank switched to a new interest rate management regime that used monetary policy instruments with Treasury bill interest rate as an Anchor in July 1994. Treasury bonds were introduced as monetary policy instrument in 2004

2.3.2 Reduction in directed credit (lending by the government or central bank directly or indirectly)

Coffee financing was withdrawn from commercial banks in 1988, Direct financing of coffee procurement by the Bank of Uganda (BOU) was reversed In 1991, Rural farmers scheme continued in 1994, Development finance operations at the BOU continued in 2003

2.3.3 Privatization of financial institutions

Government sold its shares in 3 banks jointly owned with foreign Owners in 1994; Government sold 49 % of its shares in UCB to a bank in Malaysia but reversed the sale and placed UCB under the Bank of Uganda management in1996 and 1999

UCB was finally sold to Stanbic Uganda Ltd. In 2002, Government also divested its shares in Bank of Baroda and DFCU Bank in 2002 and 2004 respectively

2.4 Legal and Regulatory reforms:

Until 1993, the *1969 Banking Act* was the basis of prudential regulation and supervision and had become outdated and its provisions were deficient in many respects. The Act failed to delineate appropriate prudential requirements to be followed by the banks. Instead it specified a number of allocative requirements. Consequently, weak prudential regulation failed to curb the prolonged

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[77] Lawrence Bategeka and Luka Jovita Okumu, Research report titled *Economic policy Research centre, Ugand,* December 2010 at p9, *Banking Sector liberalization in Uganda Process, results and Policy options.*

mismanagement of banks, especially the government owned banks and also allowed the emergence of several undercapitalized and imprudently managed banks in the late 1908s and early 1990s.

The cornerstone of the financial sector reform was therefore enactment of a new *Financial Institutions Act* which rectified most of the legislative defects.

The *1993 Financial Institutions Act* was reinforced by the *Bank of Uganda Act of 1993*, which sought to enhance and streamline the formulation and implementation of monetary policy by the central bank. This resulted in the lifting of interest rate ceiling and eliminating credit limits, and liberalization of the foreign exchange market. These were followed by the new *Financial Institutions Act of 2004* aimed at reducing the prevalent insider lending and equity concentration, strengthening banks internal management, and strengthening supervision and regulatory roles of the central bank; *Micro Finance Deposit taking Institutions Act of 2003* which resulted in licensing of four micro finance institutions to take deposits, *Foreign Exchange Act* was enacted in 2004, Ban on licensing banks first imposed in 1996 for two years, extended in 1997 to 2000, and lifted in July 2007.

2.5 Other Reforms.

Other reforms which were introduced in the banking sector are;

National Electric Switch has been introduced. This is where banks share ATMs with other banks normally referred to as visas.

Electronic Funds Transfer at the point of sale for example in supermarkets, fuel purchase at petrol stations and one can purchase goods using an ATM card. What is necessary is the account and the ATM card

Another reform deals with Islamic banking which is not yet regulated in Uganda. The advantage part of it is that it doesn't charge interest.

2.6 The Over View of the Regulatory framework.

According to the Bank of Uganda Annual Supervision report[78] in the year 2011, the banking sector continued to show a significant growth, and within the time new innovative products were introduced. In response to these developments, the Bank of Uganda initiated changes to the financial sector regulatory framework and anticipated in the strengthening of coordination between regulators at the regional level.

The regulatory framework for financial institutions is underpinned by 9 implementing regulations that is to say; licensing, capital Adequacy Requirements, Credit Classification and Provisioning, Limits on Credit Concentration and Large Exposure, Insider-Lending Limits, Liquidity, Corporate Governance, Ownership and Control and Credit Reference Bureaus.

2.6.1 The Constitution of the Republic of Uganda 1995

Banks in Uganda are governed by the central bank which is established under the mandate of the Constitution subject to Article 161, to govern, supervise and oversee the execution of banking activities by all other commercial banks in Uganda in maintaining the stability of the value of currency; regulating the currency system to support economic progress; encouraging and promoting economic development; in addition to ensuring that the financial system is effective and efficient in regard to banking and the credit system. In this similar regard it is the duty and role of the Central Bank to ensure that fiduciary duties are accordingly executed by banks as per the rules and guidelines set forth by the Central Bank.

[78] (2011:7)

2.6.2 The Bank of Uganda Act 2000

a) The regulatory framework of the banking sector in Uganda is fully governed by Bank of Uganda. The functions of the bank shall be to formulate and implement monetary policy directed to economic objectives of achieving and maintaining economic stability[79] and to supervise, regulate, control and discipline all financial institutions and pension funds institutions[80].

The implementing departments are in the Supervision Function of the Bank of Uganda whose mission is aimed at creating a sound, safe and stable financial system/sector.

The Bank of Uganda Act Chapter 51[81], provides that In order to control credit and interest rates, the Bank of Uganda may, in consultation with the minister responsible, by statutory instrument, prescribe the following:

a) the maximum amounts of investments, loans, advances and bills and promissory notes discounted, whether applied in total or to any specified class or classes which each financial institution may have outstanding during the period that may be specified by the bank;

b) the purpose for which loans and advances may be granted and the class of business underlying investments and bills and promissory notes discounted;

c) the maximum period of loans and advances and the type and the minimum amount of security which shall be required and the maximum tenor of bills and promissory notes discounted;

d) the maximum or minimum rates and other charges which in the transaction of their business financial institutions may pay on any type of deposit or other liability and impose on credit extended in any form;

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[79] Section 4(1) of the Bank of Uganda Act
[80] Section 4(2) (j)
[81] Section 39 (1)

e) the maximum charges which in the transaction of their business may impose on any banking transaction.

The Bank of Uganda Act further states that any prescription made under Section 39 (1), shall have regard to commitments which the financial institutions may have entered into with their customers at the time of coming into force of the statutory instrument and that the instrument will not have discrimination of any kind to any financial institution. However, if a financial institution contravenes any prescription made, it shall be liable to pay on being called to do so by the bank, a fine not exceeding one million shillings.

2.6.3 Financial Consumer Protection Guidelines

Financial Consumer Protection Guidelines[82] were issued and circulated to commercial banks and credit institutions. The guidelines aim to promote fair and equitable financial services practices, and apply to all financial service providers regulated by Bank of Uganda as well as their agents in respect of business conducted in Uganda. There are plans to draft other implementing regulations to cover reporting requirements from banks to the Central Bank, internal audit, mergers and acquisitions, and prompt corrective actions[83] .

2.6.4 Credit Reference Bureau in Uganda.

Following the bank failures of 1998-1999 which resulted into the closure of five commercial banks, BOU embarked on a comprehensive review of the legal, regulatory and supervisory framework in order to enhance its capacity to fulfill the statutory mandate of fostering a sound financial system that guarantees safety of depositors' funds.[84]

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[82] Of 2011

[83] *(Bank of Uganda Annual supervision report, 2011:7).*

[84] Supra.

The Bank of Uganda introduced a Credit Reference Bureau (CRB) Services for easy information asymmetry between lenders and borrowers[85]. The Credit Reference Bureau (CRB) in Uganda was launched on 3rd December 2008 by the Governor of Bank of Uganda Mr. Emmanuel Tumusiime Mutebile[86], It was a key milestone in the history of Uganda Credit Industry. The CRB launch was preceded by a lot of deliberation and was eventually mandated by the passing of key legislation namely the Micro Deposit taking Institutions Act 2003 (MDI Act) and the Financial Institutions Act 2004 (FIA). The FIA mandates the Central Bank, its appointed agent or any other appointed persons authorized by the Central Bank to establish a CRB for purposes of disseminating Credit Information amongst BOU regulated Financial Institutions also called Participatory Institutions (PIs).

The CRB ensures; timely information and accurate information on borrowers' debt profile and repayment history since experience has revealed that when financial institutions compete with each other for customers, multiple borrowing and over- indebtedness increases loan default unless the financial institutions have access to databases that capture clients' borrowing behavior; an improved pool of borrowers across the globe; reduced default rates as borrowers seek to protect their reputation collateral by meeting their obligations in a timely manner. The CRB has enhanced a strong motivation for clients to repay their loans since credit reports include both positive and negative information that help in building reputation collateral in the same way as a pledge physical collateral which may improve credit access for the poorest borrowers. According to Mutebile[87] the absence of a CRB in Uganda had been a major bottleneck to

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[85] According to the *Annual Supervision Report (2012.*

[86] Credit Reference Bureau Team (n.d) *Why Banks should embrace Credit reference bureau.* Retrieved from:http://www.google.co.ug/url?sa=t&rct=j&q=&esrc=s&source=web&cd=4&ved=0CDMQFjAD&url=http%3A%2F%2Fugandabankers.org%2Findex.php%3Foption%3Dcom_k2%26view%3Ditem%26task%3Ddownload%26id%3D11%26Itemid%3D75&ei=JBdoUqbxDoyX0QXd1oDoAg&usg=AFQjCNFM01eRxwh0Y1fSPSW4Oue6yifH2w.

[87] Mutebile T. E (2008) *Uganda's new credit reference bureau. Speech by Governor of the Bank of Uganda, at the launch of the Credit reference bureau, Bank of Uganda. Retrieved from: http://www.bis.org/review/r081205c.pdf.*

the expansion of the volume of private sector credit. Indeed, Uganda firms-large, small and medium enterprises consistently cite limited access to credit as one of the greatest barriers to their operations. Up to now, the infrastructure for information sharing and unique borrower identification has been non-existent. The Participating institutions (PIs) (commercial Banks, Credit Institutions and Microfinance Deposit-taking Institutions) had no way of checking and sharing information on the credit history of borrowers. Therefore, PIs have continuously been exposed to high credit risk on account of increased cost of borrowing, thereby making credit more expensive than it would otherwise have been.

BOU in its mandated responsibility supervises the operations of the CRB and FCS to ensure that the information collected is managed securely and responsively at all times. BOU has issued Guidelines for the operation of the CRB. The Guidelines specify the standards that the CRB shall implement in order to ensure a reliable mechanism to process data[88]

According to **the Statutory Instruments 2005 No.59**[89], a credit reference bureau shall;

a) Implement strict quality control procedure in order to ensure the quality of its database and the continuity of its services;

b) Utilize the information collected solely for the purposes set out in these Regulations;

c) Provide authentic, legitimate, reliable, accurate, truthful and current information that reflects the existing situation of the holder at any given time if the information is found to be illicit, inaccurate or no longer valid, the credit reference bureau shall promptly take the corrective measures necessary to remedy the deficiencies;

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[88] Mutebile T. E (2008) *Uganda's new credit reference bureau. Speech by Governor of the Bank of Uganda, at the launch of the Credit reference bureau, Bank of Uganda. Retrieved from:* *http://www.bis.org/review/r081205c.pdf.*

[89] section 20.

d) Provide to the Central Bank, unrestricted access to all the information managed by the credit reference bureau, whether through access to its systems according to published services, or in the manner stipulated by the Central Bank, for the purpose of supervision; and

e) Observe, through its shareholders, directors and officers, a perpetual duty of confidentiality with regard to the information divulged to them by financial institutions and MDIs.

2.6.5 Foreign Exchange Act of 2004

This provides for the exchange of foreign currencies in Uganda and making of international payment transfers of foreign exchange and other related and incidental matters. The BOU is the regulatory authority for purposes of giving effect to this Act. The BOU licenses entities that deal in foreign exchange transactions, regulates their operations and disciplines them in cases of non-compliance.

2.6.6 The Financial Institutions Act and the Micro Finance Deposit Taking Institution (2003)

The Financial Institutions Act [90] governs the regulations and supervision of financial institutions (banks and credit institutions) while the Micro finance Deposit taking institutions act [91] governs the regulation of micro-finance institutions. These Acts provide for the regulation, control and discipline of financial institutions by the central bank. They lay out and prescribe what should or should not be done in respect of licensing, shareholding in financial institutions, capital requirements, prohibitions and restrictions, Accounts and financial statements, corporate governance to mention but a few. These acts give the central bank the mandate to license (entry of financial institutions),

[90] 2004.
[91] 2003.

supervise and discipline (operations and exit of financial institutions) the financial institutions licensed under them.

2.6.7 The Penal Code Act Cap 120

Article 258 provides that; When a person receives, either alone or jointly with another person, any money on behalf of another, the money is deemed to be the property of the person on whose behalf it is received, unless the money is received on the terms that it shall form an item in a debtor and creditor account, and that the relation of debtor and creditor only shall exist between the parties in respect of it. Though the Section does not talk about banks specifically, banks are no exception to this provision of the law because they receive money on behalf of the customers on grounds of keeping the money on behalf of the customers unless a debtor- creditor relationship is established to that effect.

2.7 Control of Banking in Uganda

According to the Bank of Uganda Annual Supervision report[92] in the year 2011, the banking sector continued to show a significant growth, and within the time new innovative products were introduced. In response to these developments, the Bank of Uganda initiated changes to the financial sector regulatory framework and anticipated in the strengthening of coordination between regulators at the regional level.

The legal instruments and institutions that provide for licensing of financial institutions in Uganda include the Central Bank, the Credit Reference Bureau, *the 1995 Constitution of the republic of Uganda, Bank of Uganda Act cap 51, the Financial Institutions Act (FIA) of 2004, the Micro-Finance Deposit-taking Institutions (MDI) Act of 2003, Foreign Exchange Act, 2004, Financial Consumer Protection Guidelines of 2011, The Penal Code Act Cap 120*

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[92] (2011:7).

From the review of these laws, those governing the formal financial sector have undergone more rapid review compared to the others, signifying the rapid developments taking place in the formal financial sector in Uganda. Commercial banks and credit institutions are licensed under the FIA, 2004 and the MDIs are licensed under the MDI Act, 2003, all of which are supervised by the BOU.

2.8 Legal nature of the duty of fiduciary duty

Banks are mandated to operate through the *Financial Institutions Act of Uganda*[93], and no person is allowed to transact banking business, credit institution business or building societies business without a valid license to act so.

A Fiduciary is someone who has undertaken to act for and on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. No single explanation has been concluded on what fiduciary means. As **Gaudron and McHugh JJ** observed in **Breen v Williams**[94], "Australian courts have consciously refrained from attempting to provide a general test for determining when persons stand in a fiduciary relationship". It may be, as their Honours said, that the term "fiduciary relationship" defies definition purposely due to the difficulties in stating a comprehensive principle suitable for application to different types of relationships that carry different obligations as held in **News Limited v Australian Rugby Football League Limited.** [95]

When customer establishes a relationship of trust with the bank, the unequal or vulnerable type of reliance does not often attract the normal species of a

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[93] 2004 (Uganda)
[94] Breen v Williams (1996) 186 CLR 71 at 106.
[95] News Limited v Australian Rugby Football League Limited (1996) 64 FCR 410 at 538 per.

fiduciary relationship.[96] The trust is one of the several resources to remedy the untoward consequences of this specie of reliance.[97] A different type of one-sided fiduciary relationship is involved with the wrong of undue influence. Hence more obviously remedial that conduct of the party relied upon is scrutinized particularly. In the Anglo-Australia case law, parties are unequal as instances of undue influence[98] or unconscionability,[99] but the law is not always consistent. It is increasingly affected by competing strains of theories. In *hospital Products Ltd United States Surgical Corporation,*[100] *Dawson J* held that inherent in the nature of the fiduciary relation was a position of disadvantage or vulnerability on the part of one of the parties causing him to place reliance on the other and thus requires the protection of equity.

In ***Commercial Bank of Australia Limited v Amadio***[101] the Amadios, whose son carried on business as a builder, guaranteed the son's indebtedness to the Commercial Bank. To this end, they executed certain documents the effect of which was to provide the bank with a mortgage over a building which they owned. When the son's business failed, the bank sought to enforce the guarantee. In their defence, the Amadios asserted that the guarantee was unenforceable because it was unconscionable. It was held (High Court of Australia) (by 3-1 majority) that, in all the circumstances, it was unconscionable for the bank to rely on the guarantee. The circumstances which the court took into account in reaching this conclusion included the fact that:

a) The Amadios spoke and understood little English.
b) They did not seek independent advice, nor was the seeking of such advice suggested by the bank.

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[96] In the United States, see, for example, *Broomfield v Kosow* 212 NE (2d) 556 (1965*) and in Canada, Marrison V Coast Finance Ltd* (1966) 55 DLR (2d) 710 (BCCA).
[97] See P Finn 'Fiduciary Principle' in Youdan op cit, 1,27-30.
[98] For example, *Bank of New South Wales v Rogers* (1941) 65 CLR 42.
[99] For example, ***Commercial Bank of Australia Ltd v Amadio*** (1983) 151 CLR 447.
[100] (1984) 156 CLR 41, 142.
[101] (1983) 151 CLR 447.

c) At the time the mortgage was executed, the bank was aware of the son's precarious financial position and knew that the Amadios were not so appraised; and

d) The bank did not advise the Amadios that there was no limit on their liability under the guarantee - the Amadios believed the liability was limited to $50,000.

Dawson J delivered a dissenting judgment in which he said that the facts did not point to the Amadios having been disadvantaged and that, therefore, the bank was not guilty of either unconscionable conduct or misrepresentation. In the course of his judgment, *Mason J* noted that: *Relief on the ground of unconscionable conduct will be granted when unconscious advantage is taken of an innocent party whose will is overborne so that it is not independent and voluntary, just as it will also be granted when such advantage is taken of an innocent party who though not deprived of an independent and voluntary will, is unable to make a worthwhile judgment as to what is in his best interests*[102]

Remedy for general law unconscionability. In cases of proven unconscionability, the courts will set aside the contract or refuse to make an order for specific performance of it. If the unconscionable conduct constitutes a breach of statutory law, broader remedies (including damages) may be available.

In ***Kabwand Pty. Ltd. and Ors v National Australia Bank Ltd***[103] It was held that, a fiduciary liability is said to intrude only where the bank knows that it is being relied upon and that the bank's advance to the customer is also based on all material facts within the bank's knowledge, although this fact is more relevant to breach of a fiduciary duty than characterization of a relation as fiduciary or not illustrates the limitations of the test. The banker acted as banker for both the vendor and the purchaser of a business whereof, bank manager told the purchaser that the business had 'an excellent cash flow situation'. The business

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[102] at 462.

[103] [1989] ATPR 40-950, F. C. A.(Full Court).

was unprofitable, and the bank manager knew that it was so. The case was held unsatisfactory because of deficiencies in the pleadings, which could not be amended. The court found that the 'cash flow' statement was not an assertion that the business was profitable.

2.9 The Law Governing Bank Obligations of Fiduciary.

Under this, the researcher looked at specific provisions of laws that provide for fiduciary duties in regard to loans.

2.9.1 The Financial Institution Act 2004

The *Financial Institution Act 2004* [104] defines a bank as any company licensed to carry on banking business as its principal business and includes all branches and offices of that company in Uganda. According to the *Bank of Uganda Act 1993* Bank means the Bank of Uganda established under Section 3 of this Statute.

Banking business is regulated under the *Financial Institution Act 2004* in regard to; acceptance of money deposits from the public repayable on demand or at the expiry of a fixed period or after notice; employing such deposits wholly or partly by lending or any other means for the account and at the risk of the person accepting such deposits; and presenting to another bank, for payment, cheques, drafts or orders received from customers in the capacity of a banker. Section 55 obliges directors to be in good corporate governance and business performance of the institution by being in full control of the affairs of the bank to ensure that its business complies with the expectations of the laws applicable. Hence the duties to act honestly and in good faith, act in the best interest of the institution without undue influence and the duty to access necessary information to discharge responsibilities effectively subject to section 56 of the same Act.

[104] *The Financial Institutions Act 2004 Second Schedule.*

The Act[105] restricts directors from engaging in any act which may lead to conflicting of interest on behalf of the bank. Directors are therefore obliged that where conflict of interest arises, should exclude self from further attendance as it is states in **section 54(2) of the Act.**

2.9.2 The Leadership Code Act 2002

Sections 8-15 of the Act regulates misconduct of banking managers. Managers are refrained from engaging in any act where they have a conflicting interest where personal interests conflict with duties and responsibilities. Where manager recognizes that he has a conflicting interest then subject to **Section 9** should disclose his interest and withdraw from handling the matter. **Section 10** prohibits bank leaders from acquiring any gifts or donations in exchange for the execution of their duties. Indeed subject to **Section 6 of this Act**, any bank manager who fails to submit correct information and knowingly submits a false declaration of any matter which is misleading and insufficient commits a breach of the code. The law also prohibits managers from allowing banking information to be used by any person for any private gain subject to section 14 of this Act.

2.9.3 The Penal Code Act, Cap 120,

Subject to Chapter III Section 6 of the Penal Code, the general rules for criminal responsibility are set forth, where by ignorance of the law, cannot afford any excuse for any act or omission which constitutes an offence. Thus making reckless misrepresentations by any banking official holds him accountable for the deed and consequences that arise. In respect to **Chapter XXIX Section 304** of the penal Code, false pretence if under such a circumstance, it is established that bank official intentionally made misrepresentations in writing or provided a false fact knowingly then such a person commits an offense.

[105] Ibid Section 54.

Section 258 obliges bank to protect customer deposits. It provides that when money is received on behalf of another, it is considered as property of the person on whose behalf it has been received unless if circumstances predict otherwise where the debtor-creditor relation exist between the parties in respect to that money received. This implies that when banks act in receivership no diversion of ownership in funds is expected. But banks in Uganda have been held in a situation where they have to freeze accounts on which money has been accepted and received as deposit hence breaching contractual relationship with customer and yet bank may be acting unlawfully but upon orders established through the courts of law. Bank may therefore be liable for criminal trespass subject to **Section 302**. Indeed under **Section 269** any person employed by the bank who does any act or omits to doing any act knowingly that this will amount to financial loss in the course of executing his duties commits an offense.

2.9.4 The Micro Finance Deposit Taking Institutions Act (2003)

Micro Finance banks are restricted from engaging in trust operations subject to **Section 19 (f) of the Act** and yet subject to Section 76 a liquidator is not liable if he relies in good faith on financial statements or written reports of the institution to reflect the financial condition of the institution or upon a report or statement of an advocate or accountant and any other professional advisor by the liquidator.

Section 25 of the Act provides that a director of financial institution stands in a fiduciary relationship and compels directors to act honestly and in good faith; in the best interests and for the benefit of the institution as well as act independently and free from undue influence. This is in addition to accessing information to enable proper control and discharge of responsibilities. **Section 27 (3)** expresses the duties of the finance manager to constitute; limiting loan to deposit ratio, limiting loan to capital ratio, limiting on exposure to single or related customers and flexible limits on the percentage reliance on deposit liability.

2.10 Conclusion

Banker's relationships with their customers have a fiduciary nature in at least one aspect or another which often thrust a bank into a role of an advisor. The trust department of a bank acts in a fiduciary capacity to those whose funds are entrusted to it for investment and thus according the law the principal should not put his personal interests before the duty and neither is he expected to profit from his position as fiduciary. In this way one party relies on another as may be entitled to do so. However, banks while dealing with fiduciary relationships are mandated to operate through the Financial Institution Act.

CHAPTER THREE

EFFECTIVENESS OF THE LAW GOVERNING FIDUCIARY DUTIES AND OBLIGATIONS IN BANKS

3.1 Introduction

Bank of Uganda, as banker to Government and to commercial banks is also bound by trust that exists between a bank and its customers. This implies that, communication being an integral part of monetary policy there is need for transparent, candid explanations to be given to investors, savers, market participants, households and, to fellow citizens.[106]

3.2 Effectiveness of the Laws

3.2.1 Bank of Uganda Financial Consumer Protection Guidelines,

Paragraph (6) (3) (a) (i) (v) provides for Suitability of Advice in that; Where a financial services provider gives advice to a consumer, the financial services provider shall ensure that: (i) the advice is suitable, taking into account the circumstances and needs of the consumer; (v) it clearly informs the consumer of any actual or potential conflict of interest. this is not effective because banks normally give conflicting pieces of advice to their customers with the intentions of benefiting their own interests at the expense of bank customers as is seen In the Ugandan case of **Avi Enterprises Ltd v Orient Bank Ltd & Anor**[107], The judgment of **Wekesa John Magistrate Grade** One was as follows;

The first issue is: whether a contract existed between the plaintiff and the first defendant. Counsel relied on the case of **Edward Thomas Foley versus Thomas Hill and others (1848) 9 ER 1002** for the proposition that a banker/customer relationship is based on contract law and the terms are implied

[106] Ibid.
[107] [2013] Ugcommc 65.

by banking practice. It was not a contract which was ordinary but with extended liabilities in offering other services such as collecting services.

The second issue is: Whether the defendants breached the contract between the first defendant and the plaintiff?

The plaintiff's case is that the first defendant bank had a duty to execute the plaintiff's instructions and to keep its money safe without exposing it to fraud. The defendants took advantage of their fiduciary position and were able to entice the plaintiff to apply for an overdraft facility it did not need. There was fraudulent misrepresentation to the effect that the plaintiff would make a profit within one month. Counsel further relied on the doctrine of undue influence. The accused was made to pay the 22,500,000/= with the lending interest accumulated from that time at the bank rate at that time.

Paragraph 6 (1) (a) provides that; A financial services provider shall act fairly and reasonably in all its dealings with a consumer.
(b) A financial services provider shall not: engage in unfair, deceptive or aggressive practices such as threatening, intimidating, being violent towards, abusing, or humiliating a consumer, discriminate against any consumer on the grounds of sex, race, colour, it's not effective because ,research shows that there is Gender and age discrimination in that women and young people are more likely to be excluded than others[108] The low and unpredictable income of poor people makes it difficult for them to bank with formal financial institutions. However, national and international banks have struggled to find a business case for reaching the world's poorest people given the expectations of their shareholders and the desire for sufficient profit margins. As a result, poor people have largely discounted formal financial institutions and vice versa.) Andfinancial

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[108] Lord Boateng of Akyem and Wembley, *banking on change: breaking the barriers to financial inclusion. The Banking on Change partnership between Barclays, CARE International UK and Plan UK is addressing the global challenge of financial exclusion.*

exclusion has led to the development of resourceful indigenous community-based solutions including savings groups. By saving small amounts (initially as little as 10-50 cents a week)[109], groups gradually begin to save, and subsequently access loans from their own capital. Indeed there is something of a savings-led revolution now taking place across the world, with seven million savings group members) and bank customers have been humiliated during loan recovery because bank officials use aggressive means to recover loans.

Paragraph (6) (2) (a) provides for Provision of Information and Advice to a Consumer Prior to a consumer choosing a product or service, a financial services provider shall: (i) explain clearly in plain language the key features of the range of products and services that the consumer is interested in so as to enable the consumer to arrive at an informed decision about these products and services, including any charges and fees which would be incurred; and (ii) request the consumer to provide all the information needed to verify whether or not the consumer is eligible for a product or service in which then consumer is interested. This is effective because banks do not just offer services without explaining to the customers what the service or product is all about.

In the case of **Obed Tashobya V DFCU Bank Ltd**[110], reference is drawn to **Issue No. 3 & 4:** that is; **whether plaintiff obtained a loan facility from the defendant and if so, whether the plaintiff executed the security documents under duress/undue influence.**

The plaintiff testified that he never applied for and/or received any credit or loan from the defendant and that the mortgage purportedly executed by the plaintiff is null and void. There however is a signed credit agreement dated 27th August 2004 where the defendant bank allegedly lends the plaintiff US$117,000 for an unspecifiedproject.

[109] Supra
[110] HCT - 00 - CC - CS – 742 – 2004.

The defendant concedes that this was not an ordinary loan contract between a bank or and its customer and that no money was advanced to the plaintiff at the time of execution of the security documents.

It is submitted by the defendant that by these documents, the otherwise illegal and unauthorized overdraft to the plaintiff was converted into a legitimate and documented loan.

The second part of the issue to be determined is whether the security documents were executed by the plaintiff under duress or undue influence. The plaintiff contends that on the 26th August 2004 he was called to the defendant's head office at Kimathi Avenue and later taken to the defendant's Rwenzori House office where he was coerced into executing security documents as acknowledgement that he had obtained an overdraft/loan facility from the defendant whereas not. However, the defendant denies that there was any such duress or undue influence on the plaintiff's free will at the time of execution of the security documents. He states that pursuant to this understanding, the parties agreed to convert the whole transaction into a loan by the defendant to the plaintiff.

It was held that; the security documents were designed to put a legal face to this already embarrassing situation for the defendant of the dishonored cheque. The plaintiff did not enter into any credit arrangement as expressed in the said documents.

It's in the researcher's submission that, this contradicts Regulation **6(b) (vi)**[111] which is to the effect that a financial services provider shall not: exert undue influence or duress on a consumer to enter into a transaction;

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[111] Bank of Uganda Consumer Protection Guidelines,2012.

Paragraph 6(10) of the Banking Financial consumer guidelines provides that ; A financial services provider shall not close an account of a consumer without giving the consumer fourteen days notice from the date of receipt of such notice except: (a) where the account is being used for criminal activity; or (b) where the consumer has been threatening, intimidating or violent towards staff of the financial services provider. However this has not been adhered to because Customer's accounts have been closed without notice drawing from different justifications.

This is evidenced from the case of ***Kornark Investments (U) Ltd. Vs Stanbic Bank Uganda Ltd***[112] on grounds of fraudulent acts.
In the above case, it was held interalia that; As far as the prayer for unfreezing of the operations of the said account is concerned, an order issues that the defendant bank unfreezes the plaintiffs account and allows the plaintiff to continue with operations on the said account. ***Honourable Justice Christopher Madrama*** went ahead to say that; on the claim for an award of 200 million Uganda shillings by the plaintiff, I have taken into account the fact that the defendant did not have to freeze the plaintiff's accounts. The plaintiffs' account was frozen for a period of two years. During this period, the value of the money has been eroded by inflation. Secondly the plaintiff has not been able to use this money. It is my finding that the plaintiff is entitled to pecuniary damages.

Paragraph 6(9) (a) of the guidelines provides that ; Where a consumer is unable to repay a loan, a financial services provider shall have the right to take steps to recover the amount owing to it by the consumer. Many financial institutions have not respected this provision because they have interpreted it in the own understanding and they have decided to used awkward steps to recover

[112] Civil Suit No 116 of 2010.

debts from the customers like debting their accounts without giving notice to the customers. Yet banks owe a fiduciary duty to protect the customer's account. This is seen in the case of ***Pastori Mukwatanise v Centenary Rural Development Bank Ltd***[113] **P. K. Mugamba held interalia**; that the plaintiffs account was debited in a dubious manner. This was a wrong done to him for which he is entitled to general damages. He was awarded general damages of Shs. 1,000,000/ at bank interest from the date of judgment until full realization and the Defendant's taxed costs.

3.2.2 Credit Reference Bureau in Uganda.

The **Financial Institutions Act**[114] Provides for a Credit Reference Bureau. It provides that;

(1) The Central Bank or its appointed agent or any other person authorized by the Central Bank shall establish a Credit Reference Bureau for the purpose of disseminating credit information among financial institutions for their business.

(2) All financial institutions shall promptly report to the Credit Reference Bureau—

(a) all the details of non-performing loans classified as doubtful or loss in their portfolio, where the amount owed is not in dispute and the customer has not made any satisfactory proposals for repayment of the debt following formal demand, and the customer has been given at least twenty-eight days' notice of the intention to disclose that information to the Credit Reference Bureau;

Since the Credit Reference Bureau (CRB) ensures; timely information and accurate information on borrowers' debt profile and repayment history since experience has revealed that when financial institutions compete with each other for customers, multiple borrowing and over- indebtedness increases loan default unless the financial institutions have access to databases that capture clients'

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[113] (HCT-05-CV-CS-0066-2002).

[114] Section 78

borrowing behavior; an improved pool of borrowers across the globe; reduced default rates as borrowers seek to protect their reputation collateral by meeting their obligations in a timely manner.

It has become effective in that it has enhanced a strong motivation for clients to repay their loans since credit reports include both positive and negative information that help in building reputation collateral in the same way as a pledge physical collateral which may improve credit access for the poorest borrowers and through the use of credit reference Bureaus and rating agencies, credit managers have been provided with powerful independent third party support for evaluating the creditworthiness of their customers.

This corresponds with Regulation 18 (1)[115] which provides that a credit reference bureau shall collect negative information on the background and credit history relating to the non-performing obligations of persons and enterprises and other organizations as required by law and (2) A credit reference bureau shall, with the authorization of the customer, collect positive information regarding economic, financial and commercial obligations of persons or enterprises in order to determine their overall debt exposure and capacity to repay.
(3) At the time of receiving the information referred to in sub regulations (1) and (2), a credit reference bureau shall ensure that the financial institution or the MDI has obtained the following; (a) identification particulars of the holder. The information under the Credit Reference Bureau is shared by banks not 3rd parties and in most cases it is shared in the ordinary course of business.

Where a credit reference bureau[116]— (a) delays in providing information and documents to the Central Bank; (b) wrongfully alters, modifies or deletes records from its database; or (c) fails to adopt security and control measures that are

[115] Regulation18 of the Financial Institutions(Credit Reference Bureau) Regulations, 2005.
[116] Supra no. 115 Regulation28.

necessary to prevent the wrongful use and management of information, it shall pay a civil penalty of one hundred currency points, and in the case of a continuing offence, an additional fine not exceeding fifty currency points for each day on which the offence continues.

3.3 A Critique of the Law Governing Bank Duty of Fiduciary

Courts have recognized certain classes of persons as falling within established categories of fiduciary relationships. Examples of these include trustee and beneficiary, agent and principal, solicitor and client, director and company, employee and employer, and partners. Apart from the established categories, perhaps the most that can be said is that a fiduciary relationship exists where a person has undertaken to act in the interests of another and not in his or her own interests but all of the facts and circumstances must be carefully examined to see whether the relationship is, in substance, fiduciary.[117]

Transactional advice of a bank is the sort which refers to the explanations given to customers of transactions between the customers and itself. Details of deals entered and the relative obligations of the parties are set out. Advising on transactions is integral to the business of banking. Retail banks enter into commercial relations with their customers every day. A businessman may take out a loan, or parents may guarantee an overdraft extended to a son or daughter.

Before entering those undertakings, the bank will usually explain to the businessman and the parents what their rights and liabilities in the transaction are. Sometimes, the wisdom of the deal from the obligor's perspective is touched on and, at other times, the correlative positions of the bank and third parties are explained. Fiduciary relationships are not the normal way that the law regulates this aspect of the banker's business. Prima facie, and following the principle in

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[117] *Hospital Products* at 71-72 per Gibbs CJ; News Limited *at* 541 per Lockhart, von Doussa and Sackville JJ.

Shaddock & Associates Pty Ltd v Council of the City of Paramatta,[118] if a bank through its proper officer takes it upon itself to explain the mechanics of a transaction to a customer, the bank is under a tortuous duty of care not to misstate the position. Alternatively, persons advised may be able to avoid the transaction in equity by alleging a misrepresentation, or conduct.

However, in Uganda this is under protection of the Financial Institutions Act[119] which stipulates that;

Any person who, being a director, manager or officer of a financial institution, knowingly or recklessly makes any statement or gives any information which is false or misleading in any material particular in answer to any request for information made under any provisions of this Act, commits an offence and is liable on conviction, to a fine not exceeding two hundred and fifty currency points or imprisonment not exceeding three years or both.

The purpose of this law is to restrict the director from telling lies while executing duties.

However, in cases where the employee of the bank has to influence the customers, for the sake of protecting the company's best interest, then they will stand liable whether they lie or not lie and circumstances turn out to be in favour of the bank because the law protects the best interest of the bank so much.

And the law does not provide the facts of what amounts to misstatements which might be to the disadvantage of the customer and to the advantage of the bank. if the facts are misstated, the customers may not know since many Customers rarely distinguish between right and misleading statements and in most cases it amounts to breach of fiduciary duties by banks . Most, if not all, these matters need to be handled with proper care.

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[118] *Shaddock & Associates Pty Ltd v Council of the City of Paramatta* [1981] 55 ALJR 713.

[119] (2004) Act , Section 126(1) (b)

A relationship of trust and confidence exists between a bank and its loan customers which gives rise to a duty of disclosure of facts which may place the bank or a third party at an advantage with respect to the customer.

It may be appropriate to draw a line here. Further extension of fiduciary liability within the banker and customer relation may descend into categories of illusory reference. 'Fiduciary' indeed increasingly looks like a device permitting a secret and even unconscious exercise of a creative choice'.[120] **In *Commercial Cotton Co v United California Bank,*[121]** a corporate customer of a bank informed it that some of its cheque forms were missing. The bank then failed to act promptly and stop payment of the relevant cheques. The customer's account was then debited for payment of cheques which had been forged. When the bank declined to admit its negligence and instead relied on a statute of Limitations defense, the court said;

> *The relationship of bank to depositor is at least quasi-fiduciary and depositors reasonably expect a bank not to claim nonexistent legal defenses to avoid reimbursement when the bank negligently disburses the entrusted funds.*

In a bid to control conflict of Interest the *Financial Institutions[122] Act* accords, under *Section 54 Subsection (1)* that, no director or officer of a financial institution shall take part in the discussion of or taking a decision on any matter in which that person or any of his or her related interest has an interest. (2) In any meeting where subsection (1) of this section applies, every officer or director referred to in subsection (1) shall inform the meeting of his or her interest or that of any of the parties mentioned in subsection (1) and to the extent that the discussion or decision concerns any matter in which he or she has an interest, shall exclude himself or herself from further attendance at that meeting. The

[120] J Stone Legal System and Lawyers' *Reasonings* (1968), 241.
[121] *Commercial Cotton Co v United California Bank 209 Cal Rptr 551 (Cal App 4th dist 1985) (at 554).:*
[122] 2004.

purpose of this law is to deny the directors, who are in any way connected to either party, to be part of the issues determined, because directors may be operating with particular interest in regard to the connection that exists between either of the parties.

However, it is submitted that, this is not a fair law. The law withdraws its faith from allowing the director to execute such duties and thus excludes director from participation, yet in this manner, he/she may be in a better position to provide useful information which can be considered against/for injuries or protection of the parties involved. While this would instead put director in a better position to make rational judgments in decisions taken in the relationship, the law is biased also by thinking that that all the directors will be biased in that position and thus rob them of their contribution in matter that they would have served to the best interest of the bank.

Under the same Act on issues pertaining to conflict of duty *Section 56 (1)* a director shall in relation to the financial institution in which he or she serves, stand in a fiduciary relationship and shall in addition and without derogation owe the financial institution and its shareholders the following duties; (a) a duty to act honestly and in good faith. The purpose of subsection (a) is to emphasize the need for the director to act honestly and in good faith.

The weakness of this law is that, much as the director is restricted to execute his duties with honesty and good faith*, Section 56 (b)* of the same Act requires him to execute his duties with the best interest of the bank, which signifies a contradiction. As the directors serve to the best interest of the bank, they are acting in breach of those, to whom they play a duty of trustee whose interest also has to be protected and thus contradicting with common law especially if the injury that is likely to be caused could lead bank to losses.

Subsection (b) emphasizes director's duty to act in the best interest and for the benefit of the financial institution. The purpose of this law is to ensure that the directors put the bank interest above interest of all other parties involved. It is further submitted that, this is not a fair law because, as the director is bound by law to act giving prior consideration to bank interest then this is already contradicting with *Subsection (a)* where he is supposed to serve contrary to breach because he/she will no longer be working with honesty and faith, but will be giving priority interest to bank and thus biasness in execution of duty. Further still this can be looked at as undue influence, in fear of loosing his/her position at work in case injuries are caused to the bank.

Subsection (c) emphasizes director's duty to act independently, free from undue influence of any other person. The effect is for the director to execute his duty without fear or favour, in other words no persons shall be influential in decisions made by director apart from the fact that he is expected to follow a lawful procedure in executing his roles.

In the researcher's opinion, the weakness of this law is that, while it accords the director to be free from influences of other persons, the law itself has already biased the execution of duties. When the same act requires him to serve to the best interest of the company, director's opinion is already directed/influenced on what direction should be handled while carrying out his/her duties. This puts the director in an unprotected position by the law in case director serves with honesty and faith and the bank makes losses or if the beneficiary or principal looses and finds reasons to sue bank as the fiduciary.

Subsection (d) accords director, a duty to access information to enable him or her to discharge his or her responsibilities. The purpose of this law is to restrict the director from carrying out his duties before critically analyzing the necessary information related to the issue at hand.

This law is unfair in that, the director on reading this information, he is bound to rely on it while taking decisions, but at times this information may put the bank in a dangerous situation, given the transaction at hand. It may not be held vital because it may call for none observation of the "interest of the bank" and which information if relied upon puts the bank's position at stake and is in breach with directors duty to serve with "best interest of bank"

Section 11 (1) of the *Bank of Uganda Act (1993)* states that if financial institution is not in compliance with this regulation and as such has failed to comply with *Section 27(1)* of the Statute, it may determine that a bank is liable to the fine specified in *Section 27(5)* of the Statute. The purposes of these laws are to restrict the directors and employees not to take up any self dealings while settling issues relating to the bank because this makes them bound by the contract that they may either knowingly or unknowingly entered.

A contract made on behalf of the company, should be put in writing if made between private persons and should be signed by the parties to be charged therewith,[123] whether express or implied will by law be valid and this is effectual in law as provided in *Subsection (2) of the Companies Act Cap 110.* A contract made according to this section shall be effectual in law and shall bind the company and its successors and all other parties to it.

This implies that when a contract is made and signed on behalf of the company by its director or officer, whether implied or express becomes binding to the parties that constitute it in other words makes the company liable to any injuries or damages that may arise.

It is argued that, this is not a fair position, especially in cases where bank officer or director operated/signed under undue influence, or through commissions and bribe, which is contrary to the *Financial Institutions Act 2004*[124] and affects the

[123] Section 33 Subsection (1).
[124] *Cap 56 Section 1 (b).*

company's position and yet contract is binding and thus irrevocable, despite the losses that the company might be encountering therein, unless contract is concluded with parties or else is terminated through the same process.

3.4 Circumstances that give Rise to Breach of Relationship

3.4.1 Introduction

In Uganda, the global financial and economic crisis has made it clear that economic growth is dependent on the health of the global economy. The crisis has exposed the risks as well as the opportunities for Uganda in the changing global economic environment. However, the financial sector continues to support the growth and development of the real sector in Uganda.[125] The financial sector consists of Commercial banks, Micro-Finance Institutions, Insurance companies, the Capital Markets Authority among other players.

According to **Manjang**, the cost of borrowing has historically been very high, with interest rates as high as 40% many years ago. There are signs that the increased competition in the banking industry is putting pressure on both deposit and lending rates and the trend is moving towards lower interest rates. However, the business of banking is fraught with dangers arising principally from instability in the world economy and from human error or misjudgment. Banks may be overtaken by events or may be governed unwisely. Bank of Uganda in this case came up with measures of preventing general loss of trust in the financial institutions.[126]

[125] Lamin Manjang, *''The Contribution Of Uganda's Financial Sector To Competitiveness In A Changing Global Economic Environment'*,(2009*), Paper presented at the Fourth National Competitiveness Forum at Serena Hotel, Kampala on 16 October.*

[126]M. Sewaya, *Banking and Negotiable Instrument, Draft Lecture Notes.*

Protection of a Trust: According to the *1915 Stamp Act*[127] a protector of a trust may owe fiduciary duties to the beneficiaries, although there is no case law establishing this to be the case.[128]

After accepting the appointment as trustee, the trustee has a duty to take and keep control of the trust property in accordance with the terms of the trust agreement. If the trustee delays taking control of the assets, any resulting loss will be chargeable to the trustee personally.

Today, given that one of the trustee's functions is ensuring that the trust assets are productive, it would be reasonable for the trustee to consult with qualified investment professionals for advice on the best course to take. . If the trustee merely accepts outside advice without diligently evaluating its suitability for the trust's beneficiaries, the trustee faces being liable for breach of trust and any losses attributable to this. Generally, a trustee must exercise that degree of care, skill and caution that a reasonably prudent person would exercise in dealing with her own property.

The trustee is under a duty of absolute loyalty to the beneficiaries. The trustee must put the beneficiaries' interests before his or her own and administer the trust solely for their benefit. As such, the trustee must not undertake any transaction that would be adverse to the beneficiaries' interests, especially avoiding any self-dealing. If the trustee intermeddles in the trust property, he or she holds such as a constructive trustee and failure to protect a trust, amounts to breach of fiduciary duty.

Accountability; In *McInerney v. MacDonald,*[129] it was held that a fiduciary will be liable to account, if proven to have acquired a profit, benefit or gain from the

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[127] *Cap 342.*

[128] *Canadian Common Law* (www.wikipedia.com.).

[129] *McInerney v. MacDonald* [1992] 2 SCR 138. see C. P. Sherman, *Roman law in the modern world.* New Haven, Conn., U.S.A.: New Haven Law Book, (1992).

relationship by one of three means such as; circumstances of conflict of duty and interest, circumstances of conflict of duty to one person and duty to another person and through taking advantage of the fiduciary position. Therefore, it is said the fiduciary has a duty not to be in a situation where personal interests and fiduciary duty conflict, a duty not to be in a situation where his fiduciary duty conflicts with another fiduciary duty, and not to profit from his fiduciary position without express knowledge and consent.

In banks this situation can be traced in situation of self dealing where bank takes advantage of his position in a transaction and acting for bank own interests rather than for the interests of the beneficiaries of his clients. Self-dealing may involve misappropriation or usurpation of funds or opportunities. Self-dealing is a form of conflict of interest. In the banking sector it is the duty of the banker as the principal to advise the customers accordingly and due to this customers may claim an entitlement to rely' on the bank not to frustrate their takeover plans and bank as a fiduciary is responsible for equitable intervention to protect customers 'reasonable expectations' that their bank will act in their interest, not someone else's interest.[130]

In *James v Australia and New Zealand Banking Group Ltd*[131] Toohey J, discussed that, the customers were members of an established grazing family in Western Australia. They had several farms and were said to be amongst the biggest landholders in the Katanning district. Whilst they had banked at a local branch for several years, it was not their only source of finance. They sought the assistance of the bank only from time to time in order, usually to fund what had already been purchased. Advice from bank concerning the decision to invest was

[130] D waters *'Bank, Fiduciary Obligations and Unconscionable Transactions'* (1986) 65 Can Bar rev 37, 41.
[131] *James v Australia and New Zealand Banking Group Ltd (1986) 64 ALR 351.*

never requested, either generally, or in relation to the instant transaction. Toohey J said that;[132]

> *I do not accept that (the customers) looked to the bank for advice as to what properties they should buy or how they should conduct their farming operations. Indeed, given the long farming history of the James family, it would be surprising if they looked to the branch manager of a bank for farming advice. Thus no fiduciary relationship was found to be in place.*

Relationship between banker and customer may not be one which would ordinarily give rise to presumption of undue influence. In *National Westminster Bank v Morgan*[133] but in cases of undue influence it may be established between the creditor and surety and thus requires bank to make his justified intentions.

In *Lloyds Bank v Bundy*[134] S, the guarantor, was an elderly farmer who had been a customer of the bank for many years. His son formed a company which banked at the same branch. S went to the bank to discuss giving a guarantee to secure the company's overdraft. S relied entirely on the bank manager to advise him about the overdraft and said that he always trusted the bank manager and simply sat back and did as he was told. It was held that; the bank owed a duty to ensure that S had formed an independent and informed judgement. Since the bank had not done so, the guarantee and legal charge would be set aside for undue influence.[135]

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[132] *At 353.*
[133] *National Westminster Bank v Morgan (1985) A.C. 683 at 707-709.*
[134] *Lloyds Bank v Bundy* (1975) Q.B 326.
[135] *Lord Denning alone decided that the case on the wider ground of inequality o bargaining power, but the House of Lords disapproved this attempt at extending existing principles in National Westminster Bank v Morgan [1985] A.C 686, while emphasizing that the majority decisions in the Bundy case was correct. Recent cases have indicated however that the more flexible approach to equitable relief adopted by Lord Denning may be receiving more widespread judicial application.*

Conflict of duty; A fiduciary's duty must not conflict with another fiduciary duty as seen in *Lister v Stubbs.*[136] Conflicts between one fiduciary duty and another fiduciary duty arise most often when a bank, lawyer or an agent such as a real estate agent represent more than one client, and the interests of those clients conflict this is clear in *Deist v Wachholz.*[137]

In Uganda this is provided for under the *Financial Institution Act* [138] "no director or officer of a financial institution shall take part in the discussion of or taking a decision on any matter in which that person or any of his or her related interest has an interest. The purpose of this is to ensure no employee of bank takes part in a matter where they have particular interest or matters in which employee has a connection in either one of the parties or both.

A bank may be expected to act in its own interests in ensuring the security of its position as lender to its customer but it may have created in the customer the expectation that nevertheless it will advise in the customer's interests as to the wisdom of a proposed investment.[139] This may be the case where the customer may fairly take it that to a significant extent his interest is consistent with the bank in financing the customer for a prudent business venture.[140] This can be witnessed in the *Stewart v Phoenix National Bank*[141] where it was decided that a bank as a fiduciary could not enforce a particular mortgage covenant against a customer. The customer had dealt with the bank for 23 years and had come to habitually rely on its advice and for the bank to subsequently resale from a representation that it would not enforce this covenant in the event of default would be to take advantage of its customer's trust.

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136 *(1890) 45 Ch D 1.*

137 *Deist v Wachholz* (1984)678 P2d 188.

138 *(2004) Section 54 (1).*

139 T. Cockburn & M. Shirley, *Equity in a Nutshell* by, Lawbook Co, Sydney, (2005).

140 D waters *'Bank, Fiduciary Obligations and Unconscionable Transactions'* (1986) 65 Can Bar rev 41.

141 *Stewart v Phoenix National Bank* (1937) 64 P 2d 101.

In *Commonwealth Bank of Australia v Smith*[142] fiduciary relations were seen to be created between a customer, who deliberated on whether to purchase a country hotel, and the local bank manager, who offered his advice on the proposal. An 'interest analysis' inherent in the relation was expressed by the court at 476. Trusting and reliance in this case should be seen as integral and non-excludable parts of modern banking. Fiduciary standards of loyalty should apply in many non-deposit aspects of the relationship and appropriate remedies made available accordingly.

Fiduciary relationships may be invoked to protect the trusting aspects of customer's dealings, but the boundaries of where the banker ceases to be the customers' arm's debtor and becomes reliable for the consequences of the customer's reliance may shift. At the same time, it may be wrong to restrict bankers' fiduciary liability for reliance to where they 'chance their arms' to advise.[143] For bankers will then be able to insulate themselves from adverse consequences by the use of well-drawn disclaimers. In other words the reliance needs to be considered in the light of the customer's experience and resources.[144]

For instance a finance director applying for a loan on behalf of a large corporation might be expected to have greater knowledge of loan transactions than a sole trader acquiring a taxi license. If in both cases the bank commits what could be cast as a fiduciary wrong, fiduciary characterization of the relationship may not be the same. It may be less reasonable for the director to claim to have relied upon and reposed trust in the bank.

[142] *Commonwealth Bank of Australia v Smith (1991) 102 ALR 453* .

[143] Kenneth M. Rosen, Fiduciaries, 58 *Alabama Law Review* 1041, University of Alabama School of Law, (2007).

[144] *See First National Bank of Hopkins v International Machines Corporation 156 NW 2d 86, 88-9 (1968) (Minn SC) Murphy J and KW Curtis 'The Fiduciary Controversy: Injection of Fiduciary Principles into the Bank-Depositor and Bank-Borrower Relationships' 20 Loyola L Rev 795 838-9 (1987).*

In *Attorney General (Hong Kong) v Reid*[145] it was held that a bank must not profit from the fiduciary position. This includes any benefits or profits which, although unrelated to the fiduciary position, came about because of an opportunity that the fiduciary position afforded. It is unnecessary that the principal would have been unable to make the profit; if the fiduciary makes a profit, by virtue of his role as fiduciary for the principal, then the fiduciary must report the profit to the principal. If the principal consents then the fiduciary may keep the benefit. If this requirement is not met then the property is deemed by the court to be held by the fiduciary on constructive trust for the principal.

Secret commissions or bribes; These also fall under the no profit rule where bribe shall be held in constructive trust for the principal. The person who made the bribe cannot recover it, since he has committed a crime. Similarly, the fiduciary, who received the bribe, has committed a crime. Fiduciary duties are an aspect of equity and, in accordance with the equitable principles, or maxims, equity serves those with clean hands. Therefore, the bribe is held on constructive trust for the principal, the only innocent party. Bribes were initially considered not to be held on constructive trust, but were considered to be held as a debt by the fiduciary to the principal in *McInerney v. MacDonald,* [146] *This approach has been overruled; the bribe is now classified as a constructive trust as seen* in *Muchinski v Dodds* [147] The change is due to pragmatic reasons, especially in regard to a bankrupt fiduciary.

Constructive trusts; In *Dart Industries Inc v Decor Corporation Pty Ltd*[148] the unconscionable gain by the fiduciary is in an easily identifiable form, such as the recording contract, the usual remedy will be the constructive trust. Constructive trust come up in many aspects of equity, not just in a remedial sense[149] as seen

145 *[1993] 3 WLR 114.*
146 *McInerney v. MacDonald* [1992] 2 SCR 138.
147 *Muchinski v Dodds* (1986) 60 ALJR 52.
148 *Dart Industries Inc v Decor Corporation Pty Ltd* (1993) 179 CLR 101.
149 *Nocton v Lord Ashburton* [1914] AC 932.

in *Nocton v Lord Ashburton* but, in this sense, what is meant by a constructive trust is that the court has created and imposed a duty on the fiduciary to hold the money in safekeeping until it can be rightfully transferred to the principal.

The fiduciary functions of trusts and agencies are commonly performed by a trust company or bank organized for that purpose. When a court desires to hold the offending party to a transaction responsible so as to prevent unjust enrichment, the judge can declare that a fiduciary relation exists between the parties, as though the offender were in fact a trustee for the partner.

Keech v Sandford[150] is foundational case on the fiduciary duty of loyalty which concerns the law of trusts and affected much of the thinking on director's duties in company law. It holds that a trustee owes a strict duty of loyalty so that there can never be a possibility of any conflict of interest. A child had inherited the lease on Romforf Market near London. Mr Sandford was entrusted to look after this property until the child matured. But before then, the lease expired. The landlord had told Mr Sandford that he did not want the child to have the renewed lease. It was held that, Mr Sandford should disgorge his profits because this was a trust for an infant. If a trustee, on refusal to renew, might have a lease to himself, though there may be no fraud for it is very obvious what would be the consequence of letting trustees have the lease, on refusal to renew to cestui que use[151]

In *Foley v Hill*[152], bank pleaded a statute of limitations in defense to its customer's action for the return of a sum deposited. Defense was unmeritorious but deposit had been made years before where on evasion, customer claimed the deposited sum in equity upon which existence of equitable jurisdiction was

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[150] *Keech v Sandford* [1726] EWHC Ch J76.
[151] *New Haven Law Book (1922) Roman Law in the Modern World.*
[152] (1996) SC Bank of Marin V England 385 US 99.

said to arise from the 'complication' of the accounts and from a 'fiduciary relationship' existing between the parties since account had only three entries and was entirely expressed in the pleadings, the first argument was unsuccessful but the second argument amounted in present day terms, to a property based claim to a fiduciary relationship based in an entrusted sum.

The non fiduciary findings of *Lord Lyndhurst LC* in court at first instance was confirmed by all members of the House of Lords in *Foley v Hill* on examination of the facts of banking business.

Bankers advice to customer; Where a banker gives customers advice on their financial affairs, then the banker and customer relations may imply, in addition to any contractual rights, both common law duties of care and fiduciary duties.[153] Remedies in contract, tort and equity may all be called in aid where some forms of defective advice are given.

According to John Glover, modern banking practices involve a highly complicated structure of credit and other complexities which often thrust a bank into a role o an advisor, thereby creating a relationship of trust and confidence which may result in a fiduciary duty thrust upon the bank.[154]

Glover further states that, reliance in particular may inject an equitable element into the banker and customer relation. There are several activities undertaken by banks where customers rely on banks. This is seen in the 1958 case of *Woods v Martin's Bank Ltd*, Salmon J held that;[155]

> *The limits of a banker's business cannot be laid down as a matter of law. The nature of such a business must in each be a matter of fact.*

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[153] *Halsbury's law of England 4th edn, 3(1), [251].*
[154] *Deist v Wachholz* (1983) 678 p2d 188, 193 see U.S. Department of Labor: *Employee Benefits Security Administration*; Meeting Your Fiduciary Responsibilities.
[155] *Woods v Martin's Bank Ltd* (1959) I QB 55.

It was and is within the scope of the defendant bank's business to advise on all financial matters.

Bankers who advise customers on the acquisition of a business or investment are like stockbrokers who tender investment advice. Both have defined non-fiduciary roles in accepting deposits, and buying or selling shares, respectively. Bankers and stockbrokers may each create a fiduciary element in the relation with a customer by assuming to advise a person who is known to rely. In *Daly v Sydney Stock Exchange* [156]a stockbroker acting as an 'investment adviser' was found to be a fiduciary to the extent of his advice. Brennan J expressed the principle that:

> *Whenever a stockbroker or other person who holds himself out as having expertise in advising on investments is approached for advice on investments and undertakes to give it, giving that advice the adviser stands in a fiduciary relationship to the person whom he advises.*

The situation is the same in Uganda where the director or officer who stands and takes responsibility to advise has to be equipped with the necessary information to enable him or her or her to discharge his responsibilities which is in accordance to the *Financial Institution Act.*[157]

Special disadvantage; A fiduciary liability is said to intrude only where the bank knows that it is being relied upon and that the bank's advance to the customer was based on all material facts within the bank's knowledge, although this fact is more relevant to breach of a fiduciary duty than characterization of a relation as fiduciary or not.[158] For instance in United States case of *Stewart v Phoenix National Bank*[159]the parties had a '25 year association'. Or, the customer may be inexperienced in finance or in business where due to 'special

[156] (1986) 160 CLR 371 At 385.
[157] *(2004)* Cap 56 Section (1) (d)
[158] *Ibid no.102*
[159] (1937).64 P 2d 101

disadvantage' in the nature of age, infirmity, poor education or difficulty with the English language the customer perception of the responsibility is affected. This is an 'unconscionable dealing' and it is wrong. However, if the facts include a factor which should alert the properly perceptive banker' to the fact that this advice was being relied upon, then the ordinary fiduciary relationship may imply.[160]

A fiduciary liability can be said to exist depending on one's age for instance as seen in *Deist v Wachholz*[161] a bank customer of 24 years standing, was advised to sell a ranch which he owned. The ranch's purchaser was the secret partner of the bank vice-president. A breach of fiduciary duty was found to be committed without any evidence of fiduciary reliance being received.

Customers ignorance: This may occur due to customer' ignorance coupled with undue influence. An indictment may be dismissed where there is an infirmity of law. Thus Court can conclude that the contract can make one an agent of the company, and for a fiduciary relationship there should be reliance. In other words as a trustee this calls for a duty to act honestly and in good faith, in Uganda this is covered under the *Financial Institution Act*[162] which stipulates that:

> *A director shall in relation to the financial institution in which he or she serves Stand in a fiduciary relationship and shall in addition and without derogation owe the financial institution and its shareholders the following duty to act honestly and in good faith.*

This implies for one to take up fiduciary duties, there should be honesty upon which the other part relies to trust.

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[160] D Waters (1986) 65 Can Bar Rev 37,59.
[161] 678 P2d 188 (1984).
[162] Section 56 (1) (a)

Difficulty with English language may result in unconscionable dealing as seen in *National Westminster Bank Plc v Morgan*[163], use of language to regulate the bank and customer relation was disciplined by House of Lords. A bank manager obtained a customer's agreement to a mortgage after offering her transactional explanation and later the customer alleged that the circumstances of the advice put pressure on her to sign- a fact, she said, should have been evident to the manager at the time. The customer was allowed to avoid the mortgage by reason of the fact that it was obtained in breach of a banker's fiduciary duty of care.[164] However, if the facts include a factor which should alert the 'properly perceptive banker' to the fact that his advice was being relied upon, then the ordinary fiduciary relationship may imply.[165]

Investment advice; This is about the employment of money (or its equivalent) for profit. Funds of money advised upon the customer's own, or funds which the bank purposes to lend. The 'crucial circumstance' giving rise to an advisor's fiduciary status has been said to be whether the bank knows or reasonably ought to know, that its advice is being relied upon by the customer. This happens when banks do not accord the necessary protection to their customers and bank employees end up giving misleading advice to the customers. This means that in most instances, bank employees fail to advice on the financial risks involved in some of the information given to customers and in such cases, the banks are taking advantage of the fiduciary duties at the detriment of bank customers.

In **Avi Enterprises Ltd vs. Orient Bank Ltd & Anor**[166], the bank employee advised as an investment advisor yet under the capital markets authority act, a

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[163] Supra

[164] (1983), 3 All ER 85, Dunn and Slade LJJ.

[165] D Waters *'Bank, Fiduciary Obligations and Unconscionable Transaction' (1986) 65 Can Bar Rev 37, 59.*

[166] (2013) ugcommc 65

bank does not qualify to give investment advice and therefore, the Defendant bank was made to pay 22,500,000/= with lending interest accumulated from that time at the bank's interest rate at that time. This was because the bank employee misled the bank customer hence breaching the fiduciary duty entrusted with banks.

Customer Reliance on Bank; customer reliance on a bank may occur where financial advice has been received in connection with taking a loan. Advice in this connection may relate to the lending transaction itself, or to the use of its proceeds. Alternatively, customer may rely on the bank's loyalty to a particular investment purpose of which they have advised the bank. A customer, for example, may be on one or other side in a corporate takeover war. Not only then a source of funds for that party, the bank may also be in the position of being the party's confidant. Customers in this position may claim an entitlement to rely' on the bank not to frustrate their takeover plans.

A bank may be alleged to have unduly influenced a customer to its advantage. The bank's conduct will be what is evaluated, although in the light of the customer's relative position. Undue influence may otherwise be alleged where a bank takes a security or guarantee from a customer to secure advances made to another. The bank may have unconscionably shifted a bad risk from itself to the customer who provided the security or guarantee. The same situation was held in *Woods v Martin's Bank Ltd.*[167] when bank counseled an inexperienced young man to make an unwise investment.

In Uganda, this is provided for under the *Financial Institution Act*[168] for the directors to have a duty to act in the best interest and for the benefit of the

[167] [1954] 1 QB 55.
[168] *(2004), 56 Section (1) (b)*

financial institution implying that the directors are not supposed to knowingly cause losses to the financial institution.

In *James v Australia and New Zealand Banking Group Ltd*[169] involved a reliance-based fiduciary claim arising from transactional advice, given in a wider investment advice context. The decision pointed out the importance of demonstrating a customer's factual or justified reliance of either kind before a transactional adviser will be found to be a fiduciary. Customers claimed that they received defective transactional advice from bank when they were about to make a substantial rural investment. Loan funds were desperately needed by the customers to meet commitments that they had already undertaken. The manager said that he could not lend the customers what they wanted and recommended that they apply to a particular Perth mortgage broker instead. Whereof customers went to the broker, who turned out to be unlicensed incompetent and they consequently suffered a loss. In this case the bank manager was in argument alleged to be the customer's fiduciary who caused their losses by his breach of duty. Toohey J noted that the customers claimed to this end that;

> *They had come to rely upon the bank for advice in financial matters relating to the conduct of their farming operations.*

False representation by Manager; Concerning the availability of bridging finance and loan servicing were also alleged as a cause of loss. This was held by *Donovan Waters,*[170] that knowing, actually or constructively, of this reliance, the bank may have been negligent in the advice it gave, or in the preparation of documentation it put before the client. It does not need the duty of care in tort law to make the bank liable. The confidence reposed in the bank, the reliance,

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[169] (1986) 64 ALR at 353 (Fed Crt, Toohey J)
[170] '*Banks, Fiduciary Obligations and Unconscionable Transaction' (1986) 65 Can Bar Rev 37, 59-60.*

and the bank's knowledge of that situation may justify the imposition of an express trustee standard of behavior upon the bank.[171]

In Uganda, the *Financial Institution Act of Uganda (2004)* states that, the central bank may, at any time, in consultation with the Minister, revoke a license of a financial institution if it is satisfied that the financial institution is carrying on business in a manner detrimental to the interests of depositors[172]. Although under normal circumstances it is not easy to express exactly what it is in the banker and customer relation that should attract equity's intervention yet others have done this at greater length.[173] This is seen in the closure of former Greenland Bank, ICB and Uganda Commercial Bank for failure to meet banking regulations.

The Bank of Uganda Act[174] determines that if financial institution is not in compliance with this regulation and as such has failed to comply with *Section 27(1)* of the Statute, it may determine that a bank is liable to the fine specified in *Section 27(5)* of the Statute. The purposes of these laws are to restrict the directors and employees not to take up any self dealings while settling issues relating to the bank because this makes them bound by the contract that they may either knowingly or unknowingly entered.

Biasness in consideration of interest; When Bank in its relations with customer, looks only to the customer's interest, the situation is considered to be non-commercial to expect a bank to adverse and lend money with only the interest of the customer in mind, no matter how much the customer may rely. This is contrary to the banking regulations, where bank should not be taken as a charitable institution this is held in *National Westminster Bank plc v Morgan.*[175]

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[171] The Journal of Law and Economics, 36 J.L. & Econ, 1993, 425;
[172] Financial Institution Act (2004) Cap 54 (Uganda).
[173] *(1986) 103 Banking L J 80 and E L Symons, The Banker-Customer Relation.*
[174] (1993)Section II (I).
[175] (1983) 3 All ER 85, 91 LJ (CA).

In this way bank is not expected to be concerned with an alleged fiduciary duty to disclose[176] as seen in *Klein v First Edina National Bank* but to transact business with a depositor/customer without implied special duty to counsel the customer and inform him of every material fact relating to the transaction – including the bank's motive, if material, for the transactions – unless special circumstances exist, such as where the bank knows or has reason to know that the customer is placing his trust and confidence in the bank and is relying on the bank'. In Klein's case, a customer's reliance cannot be expected to elicit complete selflessness from the bank, was there is no special circumstance in the facts of the case which justify a fiduciary response.

Undue influence approaches and unconscionability; According to the *Banker's Association Code of Banking Practice*[177], a bank's transactional advice produces an agreement or disposition to the benefit of the bank, and some element of disadvantage or inequality affects the position of the customer. Doctrines of 'undue influence' and 'unconscionable dealing' tend to be used in Australia where the intuitive idea in both doctrines seems to be that a bank's bargain or benefit cannot be kept if the bank has obtained it by acting oppressively or form a position of strength. In cases where the bank deals with a large commercial customer and that customer suffers a loss through reliance on the bank's transactional explanations or non-disclosures a trusting relationship might not be so easily inferred in this case either. This is seen in *Ottoman Bank v Mawani*,[178] in which the defendant signed a guarantee and in favour of the plaintiff's bank and for the money owed by his parents. When sued on the guarantee under undue influence of his father. It was held that the defense was valid and defendant was not liable on the guarantee.

[176] (196) NW 619 (1972), 623, Curiam
[177] *(2003).*
[178] (1965) EA 464.

Under the *Financial Institution Act*[179] a director is expected to perform his duty to act independently, free from undue influence of any other person. The provision of this law is to ensure that the directors of bank officers do not perform their duties under influence of the clients. The bank customers are expected to consult with attorneys on problems or difficulties in accessing commercial leases as well as advising on contract modifications, risk of loss, undue influence or overreaching, statutory compliance and enforcement, commerce or business transaction practices or methods of competition. As regards general damages, these require no specific proof.

Bank customers lack trust when it comes to payment of bank loans and this has its effects. These result in bad loans and Non Performing Loans (NPL). NPLs are one of the indicators that describe how well or bad the banking sector is faring. An increase in the percentage implies negative growth by the sector and vice versa. NPL's are a deduction from the operating income and therefore substantially reduce the profit for the year,"

These loans generally are deemed to be nonperforming if they are in arrears for a period exceeding 90 days without any form of interest payment or plan for restructuring. Mortgage loans posed one of the biggest problems in the banking sector last year. Falling incomes from new branches opened in 2010 also depleted some banks' earnings, especially the new players, and this compelled bank headquarters to subsidize certain outlets across the country[180].

Aggressive loan recovery efforts saw the bank's impairment loss on loans and advances decline from sh3.1b to sh2.7b during the period[181]. Though this mode of loan recovery is aggressive and humiliating, it has helped banks a lot because

[179] *Article 56 Section (1) (c).*
[180] The East African *Bad loans, backlog of court cases affect bank returns in Uganda* Posted *Saturday, May 24 2014 at 18:12* by Bernard Busuulwa
[181] *Uganda's banking sector back to profitability Publish Date: Apr 29, 2015 in the new vision*

at least they are able to recover their monies back .However The backlog of cases in the judiciary has slowed down efforts to recover bad loans, financial experts argue. Commercial cases filed in Ugandan courts currently take a minimum of six months to dispose of at the first stage of trial, a situation that constrains business decisions[182]

3.5 The Effect of Breach of Fiduciary Duties.

Transactional advice of a bank is the sort which refers to the explanations given to customers of transactions between the customers and itself. Details of deals entered and the relative obligations of the parties are set out. Advising on transactions is integral to the business of banking. Retail banks enter into commercial relations with their customers every day. A businessman may take out a loan, or parents may guarantee an overdraft extended to a son or daughter. Before entering those undertakings, the bank will usually explain to the businessman and the parents what their rights and liabilities in the transaction are. Sometimes the wisdom of the deal from the obligor's perspective is touched on and, at other times, the correlative positions of the bank and third parties are explained.

Fiduciary relationships are not the normal way that the law regulates this aspect of the banker's business. Prima facie, and following the principle in *Shaddock & Associates Pty Ltd v Council of the City of Paramatta,*[183] if a bank through its proper officer takes it upon itself to explain the mechanics of a transaction to a customer, the bank is under a tortuous duty of care not to misstate the position. Alternatively, persons advised may be able to avoid the transaction in equity by alleging a misrepresentation, or conduct.

[182]Supra
[183] [1981] 55 ALJR 713.

In Uganda this is under protection in regard to Section 126(1) (b) of the financial institutions act which provides that; *Any person who, being a director, manager or officer of a financial institution, knowingly or recklessly makes any statement or gives any information which is false or misleading in any material particular in answer to any request for information made under any provisions of this Act, commits an offence and is liable on conviction, to a fine not exceeding two hundred and fifty currency points or imprisonment not exceeding three years or both.*

The purpose of this law is to restrict the director from telling lies while executing duties.

However, in cases where the employee of the bank has to influence the customers, for the sake of protecting the company's best interest, then they will stand liable whether they lie or not lie and circumstances turn out to be in favour of the bank because the law protects the best interest of the bank so much which amounts to breach of the fiduciary duties by the bank.

And the law does not provide the facts of what amounts to misstatements which might be to the disadvantage of the customer and to the advantage of the bank. If the facts are misstated, the customers may not know since many customers rarely distinguish between right and misleading statements. Most, if not all, these matters need to be handled with proper care.

It may be appropriate to draw a line here. Further extension of fiduciary liability within the banker and customer relation may be descend into categories of illusory reference. 'Fiduciary', indeed increasingly looks like a device permitting a secret and even unconscious exercise of a creative choice'.[184] As was in *Commercial Cotton Co v United California Bank.*[185]

[184] J Stone, *Legal System and Lawyers' Reasonings (1968), 241*
[185] 209 Cal Rptr 551 (Cal App 4th dist 1985) (at 554):

A corporate customer of a bank informed it that some of its cheque forms were missing. The bank then failed to act promptly and stop payment of the relevant cheques. The customer's account was then debited for payment of cheques which had been forged. When the bank declined to admit its negligence and instead relied on a statute of Limitations defense, the court said

> *The relationship of bank to depositor is at least quasi-fiduciary and depositors reasonably expect a bank not to claim nonexistent legal defenses to avoid reimbursement when the bank negligently disburses the entrusted funds.*

Account of profits; an account of profits is another potential remedy in *Re Pantmaenog.*[186] It is usually used where the breach of duty was ongoing or when the gain is hard to identify. The idea of an account of profits is that the fiduciary profited unconscionably by virtue of the fiduciary position, so any profit made should be transferred to the principal. It may sound like a constructive trust at first, but it is not. An account for profits is the appropriate remedy when, for example, a senior employee has taken advantage of his fiduciary position by conducting his own company on the side and has run up quite a lot of profits over a period of time, profits which he wouldn't have been able to make without his fiduciary position in the original company. The calculation of profits in this sense can be extremely difficult, because profit due to fiduciary position must be separated from profit due to the fiduciary's own effort and ingenuity.

Compensatory damages; in *Glover v Porter-Gaud* compensatory damages are also available.[187] Accounts of profits can be hard remedies to establish, therefore, a plaintiff will often seek compensation (damages) instead. Courts of equity had no power to award compensatory damages, which traditionally were

[186] [2004] 1 AC 158
[187] (2000) 98-CP-10-613

a remedy at common law, but legislation and case law has changed the situation so compensatory damages may now be awarded for a purely equitable action.

3.5.1 Conclusion

There are laws governing fiduciary relationships of trust, but despite their existence these circumstances of breach are experienced because of some loopholes embedded in the laws. In this way the beneficiaries of the trust in some cases remain unprotected in cases of breach such as conflict of duty, secret commissions and bribe as well as failure to account, which brings about failure to observe the principal of trust.

CHAPTER FOUR

POLICY CHALLENGES FACING THE FINANCIAL SECTOR WHILE ENSURING THEIR FIDUCIARY DUTY TOWARDS CUSTOMERS

4.1 Introduction

This chapter describes certain assumptions that have been made about the general nature of fiduciary duty and fundamental principles governing it should there be a review in Uganda. These assumptions were acquired through desk reviews.

Fiduciary relationship is expressed as that, which is entered when one person accepts to undertake action in a defined matter on behalf of another owing to the arising circumstances that yield trust and confidence.[188] They further emphasized that *"a fiduciary duty is a formal, technical relationship of confidence and trust imposing greater duties upon a fiduciary as a matter of law,"* and that, in general terms it applied to any person who occupies a position of peculiar confidence towards another. But according to Lamin Majang[189] a fiduciary relationship refers to integrity and fidelity which contemplates fair dealing and good faith, rather than legal obligation, as the basis of the transaction." The elements of breach of which in Uganda constitute;

(a) the existence of a fiduciary relationship (either as a matter of law or as a matter of fact) between the plaintiff and the defendant;

(b) defendant's breach of the fiduciary duties accompanying the relationship; and

(c) the breach of the duty that either injured the plaintiff or benefited the defendant. A fiduciary duty may arise formally, as a matter of law, or informally, through moral, social, domestic, or purely personal relationships of trust and confidence.

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[188] Leslie Rutherford and Sheila Bone, *Osborn's Concise Dictionary 8th Edition published by Universal Law Publishing Co. PVT LTD in 1993.*

[189] Lamin Manjang, *''The Contribution Of Uganda's Financial Sector To Competitiveness In A Changing Global Economic Environment',(2009), Paper presented at the Fourth National Competitiveness Forum at Serena Hotel, Kampala on 16 October.*

It can therefore be rightly submitted that when banks play a role of mediating in transactional dealings they are somewhat bounded by the duty, as trustees act in good faith and reveal any information that is likely to cause future injuries to the beneficiary for the beneficiary to enter the contract without reliance on another party but at a free will. This puts the bank in a vulnerable, and technical position, and thus if the advising official is in this case, not very careful he/she may as well fail to protect the interest of the bank and end up in conflict of duty. But with contradicting laws the bank is put in an insecure position, while trying to protect the interest of the bank, protecting the beneficiary through trust and at the same time protecting the principal.

4.2 Policy Challenges

The study established that there is an accelerating cutthroat competition among financial institutions which is very tough[190] in Kampala (The reason some of the bank services are now being hawked from the bank premises right to the customer's office desk (for example account opening, money withdrawals and deposits which are now done through mobile telephone for the convenience of customers for example with Centenary Bank). Customers are knowledgeable and demanding with ever changing preferences. New products have to be developed, tested and launched and yet delivery channels are more varied and complex.

Faced with such a range of challenges, operating models and technology components in the banking business need to be modernized for banks to benefit fully. But while technology components are upgraded defrauding customers are also on a get-set to take advantage of the banks during the transition to work hand in hand with bank employees to misuse computers to defraud (but there is a law in place[191]). However, this does not imply that banks will refrain from

[190] Gary Pugh (2012), Modernize or Fail: The Modernization Challenges Facing Banks and the Technology Implications, An Oracle Financial Services Thought Leadership paper, Oracle Financial Services, London.
[191] The Computer Misuse Act (2011) Section 12 for unauthorized persons.

modernizing their operations and technological components, else they lag behind and fail in their customer satisfaction approaches hence in the same regard may fail to maintain their revenues and profits and most importantly fail to please their shareholders.

This study finding implies that there is great need for banks to modernize, but in course of modernization the adopted approaches have to be carefully thought as advised by Narayana[192] especially during the time of testing authenticity to be able to maintain and satisfy the integrity of the systems adopted. Thus Gary advises banks to review all operational processes and IT systems and softwares and revaluate outsourcing policies to improve governance and risk management in regulatory compliant manner while improving business performance management in enhancing customer service. This according to Gary will increase the speed and effectiveness of product manufacture, widen and deepen distribution channels.[193]

Reflecting on the above difficulty, the study also established a fundamental challenge of banks having to generate strong revenues and healthy profits in a banking environment that is surrounded by sophisticated technology and computer fraud and yet technology management is maintained in-house while banks have limited knowledge.[194] This finding implies that, banks exercise a complicated task in a difficult economic condition with high credit risks and complex stresses and yet have to endure to increase liquid capital.

In respect to this finding it can therefore be submitted that the need to become and remain more competitive in the banking environment is a serious challenge for banks which pushes banks to override some of their policies to keep against the stiff competition and thus driven by the customer centricity buzz which is affecting the nature of fiduciary duties afforded by banks in the customer-bank

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[192] Narayana Vyas Kondreddi (2011), *Database Trends and Database Integrity: How Much Availability is Enough?, Verole University of India.*

[193] Supra 189

[194] *Supra No.192*

relationship. For this challenge, banks are losing their ability to provide an edge in meeting demands of all stakeholders.

Further still, it is currently by policy in Uganda for information regarding a borrowing customer to be sought by the intending lender (bank) from other banks. This is mainly to establish the credit worthiness of the customer as monitored through the financial card system. A bank in which borrower has previously acquired a loan has a responsibility to disclose and furnish other banks with detailed information of any cases of credit unworthy dealings of the customer.

This is a policy imposed by bank of Uganda to regulate possible extension of financial loan misconducts to other banks by defaulting borrowers purposely for the efficiency and sustainability of the financial institutions. This is in addition to;[195]reducing the level to which risk bank creditors are exposed to (protect depositors); reducing the risk disruption resulting from adverse trading conditions for banks which has caused multiple major bank failures; avoiding and reducing the risk of bank being used for laundering the proceedings of crime; as well as helping in determining credit allocation depending on credibility and profitability of the clients.

However, in meeting the information disclosure requirement as traced from the financial card, both the consulting and advising banks forget that they both owe customers a duty of fiduciary, hence both banks are in breach and can be held liable as seen in ***Moody v Cox and Hatt.***[196] Indeed in Webster and Webster[197] it is held that a client must at all times be able to look at his solicitor to obtain advice which is independent and impartial but if the same solicitor acts for both parties, then the right to be independently advised is deprived. This implies that

[195] Working Paper (2009*). "Rescuing Banks from the Effects of the Financial Crisis"*

[196] (1971) 2 Ch *71whereby trying to act for both parties bank may put itself in a such a position that it should be liable to one or the other in whatever it does in case there is a misrepresentation.*

[197] *Professional Ethics and Practices for Scottish Solicitors, 3rd Edition.*

the advising bank is serves more than two interests which cannot be met with consistency thus fails to observe the fiduciary duties owed to the client..

In respect to the above it is submitted that while imposing and regulating customer borrowing standards, the bank-customer relationship requires to be maintained as well. To this effect, financial discipline needs to be instituted in the previous bank. This is particularly because, banks as lending institutions are supposed to monitor and evaluate the management process of the loan as a way to help borrowers use the funds efficiently and profitably. However, banks go ahead to issue excessive loans to customers without accurately ascertaining their pledged security and ability to pay back. This is in addition to banks having diverse objectives for lending which originate supply driven loans to prompt borrowers[198] thus the increasing challenges in loan management which are affecting the bank-customer relationship in Uganda when borrowers fail to maintain their solvency.

Money laundering is yet another critical issue that has posed a challenge to banks in Uganda in maintaining the customer-bank relationship. Money laundering is a process of taking the proceeds of criminal activity and making them appear legal.

Laundering allows criminals to transform illegally obtained gain into seemingly legitimate funds and it is a worldwide problem[199]. While banks are expected to report money laundering issues, in practice this is a difficult issue especially in cases of suspicions.

Banks run the risk of committing money laundering offences under the Money Laundering Act,[200] unless they notify the national law enforcement Agencies as is provided under the Financial institutions Act of 2004 that; *A financial institution*

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[198]IMF (2003), *Regulatory Framework for Public Borrowing and Public Debt Management in Uganda.*

[199] Sulltzer, Scott. 1995. *"Money Laundering: The Scope of the Problem and Attempts to Combat It." Tennessee Law Review 63.*

[200] 2009, laws of Uganda.

shall promptly report to the national law enforcement agencies any suspected money laundering activity related to any account held with the financial institution[201].Once a bank makes a report to the National Law Enforcement Agencies, concerning a customer's bank account it will not be able (without running the risk of committing money laundering offences) to undertake any transaction in respect of the funds within that account until such time as appropriate consent has been given.

However, in such circumstances, banks are placed in the unenviable position of being unable to act in accordance with their customer's instructions. Such a situation not only has the propensity to damage the relationship between bank and customer but also carries the risk that the customer might incur some loss due to the bank's inability to act on the customer's instructions.

4.3 Conclusion

Fiduciary relationships between banks and their clients develop through trust and confidence towards another and its existence should contemplate fair dealing and faith. When bank takes up fiduciary responsibilities, then the official mediating on its behalf should work to the best interests of the bank but under certain circumstances, this may contradict but banks may avoid liability by not providing transactional advice or carrying out any unconscionable dealings. However bank may curb cases of liability through distinguished between proprietary remedies, dealing with property, and personal remedies, dealing with pecuniary (monetary) compensation but in cases of Breach of fiduciary relationships profits can be accounted for or banks can pay for compensatory damages.

[201] Section 130 (1)

CHAPTER FIVE

SUMMARY OF THE FINDINGS CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

The chapter presents the summary, conclusions and recommendations of the study carried out on bank's Fiduciary duty in relations to customer protection issues in Uganda.

Summary of the Research Findings

5.2.1 Fiduciary Obligations

Although through fiduciary arrangements, the problems emerging between banks and their clients can legally be solved, it should be noted that, while accounting for fiduciary responsibilities courts are increasingly recognizing bank failure in their roles to serve as fiduciary without conflicting interest.

Despite the current economic crisis, Ugandan banks are relatively strong. They are well capitalized and have satisfactory liquidity ratios. Low levels of non-performing loans continue to be recorded. The recent strengthening of the system is due to the governments focus on upgrading the legal and regulatory framework of the banking system.

5.2.2 Policy Arrangements

While banks in Uganda may not have strict individual banking policies, general policies have been imposed by the central bank to rescue falling bank business for example the financial card policy in managing debt defaulters across banks.

5.3 Conclusions

It is in the researcher's submission that for fiduciary considerations to be given adequate attention, management of the banks must be possessed of the requisite fiduciary determinants. It is crucial, therefore that the necessary fiduciary consideration and awareness of the relevance and importance of trust roles particularly in relation to banking rights be generated. This means that though on the face of it, it seems like banks know their fiduciary obligations, it is not the case and for this matter banks also need to be educated through holding seminars about the efficacy of fiduciary bank duties towards their customers who are a strong foundation of the bank because without customers, the bank would be nonexistent.

There are laws governing fiduciary relationships of trust, but despite their existence these circumstances of breach are experienced because of some loopholes embedded in the laws. In this way the beneficiaries of the trust in some cases remain unprotected in cases of breach such as conflict of duty, secret commissions and bribe as well as failure to account, which brings about failure to observe the principal of trust. In this regard, the researcher stresses that banks must observe their obligation of why they are trusted by customers to stand in for them as trustees but not to act as trustees and at the same time as beneficiaries thus banks need to advise their customers on the rights and liabilities in any undertaking but not to profit themselves at the expense of the customers who are in most cases not enlightened about their rights and liabilities.

Banks may avoid liability by not providing transactional advice which does not tally with their obligation or carrying out any unconscionable dealings and upholding the principle of Know Your Customer (KYC).

5.4 Recommendations

For effective banking system in Uganda, the following recommendations should be adopted.

5.4.1 Reforms in the law;

The law governing fiduciary arrangements in banks in Uganda is of considerable significance to the clients, because it helps the Principal to attain considerable equity and thus relieves them from a position of being robbed. But these laws are too ineffective because many financial institutions operate under strain due to the absence of proper legislation of debtor/creditor law in protecting the existing customer-bank relationship as seen to be drawn from various legislations which makes the supervisory response procedure a little too slow and weak due to the long process which requires drawing various legal issues to rely upon from the law of insolvency, mortgage, and others which makes debt legislation problematic and at times results into closure of banks in Uganda. In particular, the representatives of the people who are the legislators have a low knowledge about the proceeds of the law and yet go ahead to participate in law designing, hence come up with inadequate laws, because they are not conversant with the requirements of the law as reflected from matters that may arise. This study finding reveals that, those that participate in the legislative process must be knowledgeable enough to understand the interpretation and application of the laws if effective laws are to be designed.

5.4.2 Observing responsibilities;

For bank officers to be observant of the rule and regulations governing fiduciary responsibilities to adopt good practices, regional line managers up the chain and the management in the Human Resources Department will need to address internal incentives and practices through staff recognition. Greater attention to incentives for changes in staff behavior will pay off in encouraging a sustained effort to address fiduciary relationship. This should be done hand in hand with dynamic monitoring of bank officers on procedure taken in advising on fiduciary issues.

5.4.3 Improving accountability;

In case of fiduciary duty breaches, accountability is a good remedy. Accountability usually arises where the breach of duty was ongoing or when the gain is hard to identify. The idea of an account of profits is that the fiduciary profited unconscionably by virtue of the fiduciary position, so any profit made should be transferred to the beneficiary

There is need of revitalizing duty bearer accountability through trust based accountability mechanism which will create a regulated framework for the resolution of conflicts and competing interests in banking sector. This is to bring about complete accountability from duty bearers. An account for profits is the appropriate remedy when, for example, a senior employee has taken advantage of his fiduciary position by conducting his own company on the side and has run up quite a lot of profits over a period of time, profits which he wouldn't have been able to make without his fiduciary position in the original company. The calculation of profits in this sense can be extremely difficult, because profit due to fiduciary position must be separated from profit due to the fiduciary's own effort and ingenuity.

5.4.4 Financial Litigations;

There is also need to encourage and nurture public financial litigation into all matters concerning the fiduciary control and regulation of banking functionaries. Financial litigation is an area of legal practice which focuses on dealing with settlements and court cases which involve financial matters. Many national governments have departments which specialize in financial litigation to protect the financial interests of the nation and its citizens, and private law firms handle financial litigation for everyone from mutual funds to individual citizens

A number of different types of cases can fall under the umbrella of financial litigation. In all cases, they involve sums of money, often quite large ones. Some examples include collections, in which a company, organization, or government is obligated to go to court to collect monies owed, along with the flip side of this, fighting collections actions, fines, and other financial assessments. Financial litigation also covers financial fraud, trade the stock and securities markets, restructuring, issues related to loans, and a wide variety of other financial matters.

In some cases, the threat of financial litigation can be enough to reach an out of court settlement. Such settlements may be advantageous to one or both parties in a suit, for a variety of reasons ranging from preserving a company's reputation to potentially recovering more funds out of court than would be possible in court. In other instances, it is necessary to proceed to court to try a case before a judge.

5.4.5 Promoting estoppels;

There is need to apply use of promissory estoppels. The 'promissory' species of estoppels prevents a party's unfair departure from stated intentions. Promissory estoppels can therefore act as a defensive equity, preventing contracting parties from unfairly insisting on their strict legal rights.

Promissory estoppels allow a party to recover on a promise. It prevents, or estops, a person from arguing that his or her promise should not be upheld. The reliance on the promise must be reasonable, and the person trying to enforce the promise must rely on the promise to their detriment. In order to invoke a promissory estoppel, three elements must be present: the promisor, the promisee and a substantial detriment - an economic loss that occurs to the promisee if the promisor declines to honor the promise. This benefits the customers who act basing on the bank's advice. Promissory estoppels, estops the banks from running away from the advice provided to customers and make them to believe that the advice is true and correct,

5.4.6 know Your customer " (KYC)" principle;

This principle needs to be strengthened because it was pointed out that most banks in Uganda have not taken the initiative to get detailed information about their customers. Even when such is got, no measures have been put to find out whether the information given is true or false. Therefore the banks should always look into fictitious bank accounts, forged invoices, usurpations of identities, imitations of signatures among other things because the protection of organizations' infrastructure and systems from cyber threats is a key strategic priority, with cyber-attack identified as a top tier risk .

5.4.7 Strengthen monitoring

There is need to closely monitor smaller banks in case of governance issues and potential market integrity risks that they pose and Bank of Uganda should not provide supervisory forbearance. In other words it should take full scope examination to ensure soundness and the adequacy of risk management controls as well as have the concerned banks submitting their capitalization plans ahead of proposed deadlines.

It is important for central bank besides monitoring, to take prompt appropriate supervisory corrective actions against non-compliant, under-capitalized or non-viable financial institutions as well as avoiding non regulatory forbearance. It should also refrain from providing liberal exemptions from the single borrower limits to banks, to exacerbate the already high loan concentration in the system and undermine the development of much needed financial instruments in the rest of the financial market for commercial papers and syndicated loans.

5.4.8 Review of Standard terms

Banks should also review whether their standard terms of business adequately protect them in the event that claims are made against them for dealing appropriately with suspicions of money laundering and making SARs. In other words banks need to engage legal advocates in taking up such actions and decisions to identify possible gaps and find a legal cover.

5.4.9 Out Sourcing Policies

There is need for banks to re-evaluate their outsourcing policies. While many of the banks realize that improving operational effectiveness and efficiency needs to be maintained in-house, banks are failing to beat the sophisticated technological applications in fraud money wirings and thus should no longer keep certain operations in-house but extend them to technical contractors that is the outsourced service providers (OSPs) who can guarantee to do a better job, improve production and do it at a lower cost thus a reason to outsource to reduce unmanageable liability.

5.4.10 Borrowing Ability

As a measure to curb the growth of Non Performing Loans, banks should now focus more on "the borrower's ability to withstand the economic vagaries that might arise. Since, banks extend credit to their customers, both consumer as well as commercial purposes, Most of the loans given to personal accounts holders fall in the category of consumer credit and therefore for this matter, all banks have to uphold and adopt the techniques of credit scoring for assessing the creditworthiness of individual borrowers by requesting customers to provide specific details that are then fed into the model and a score is produced immediately. This improves turnaround time for processing customer's loan requests.

5.4.11 Independent Legal Advice

The necessity for a lender to not only refer but actually insist that a borrower or a guarantor, in some circumstances, obtain independent legal advice is an issue of significant discussion and speculation.

Independent legal advice will be required when the banker is in a position of conflict of interest either because the solicitor has a personal interest in the transaction, directly or indirectly, or because he or she is proposing to act for sides that are adverse in interest. One should be cautious in acting in matters where the parties are in a conflict of the interest even where both sides are prepared to sign an acknowledgment of the conflict of interest and waive their right to seek and obtain independent legal advice.

Recommending independent legal advice only is insufficient and therefore banks must insist on it because when a client is advised to seek independent legal advice, the advisor can Carefully explain the nature and effect of each of the documents which the client is being asked to sign by the bank and all the potential risks and consequences which may flow from the execution of those documents and this aids customers in making right decisions.

Therefore referring customers to seeking independent legal Advice should be given attention and the Advice should be given by a person who is eligible for example a Justice of the Peace, an advocate, a Notary public, bank manager, a minister of any religion authorised to celebrate marriages, a medical practitioner, and other eligible persons.

5.3.12 Need for financial institutions to devise mechanisms and systems that can track suspicious transactions such as unusual huge cash deposits by individuals who usually deposit cheques, sudden increase on an account which is then quickly withdrawn and customers who deposit certain counterfeit notes or forged instruments· Banks therefore require conducting periodic training programmes on ways of combating crimes in the banking system of their customers and other clients when entering other business premises for business relations. This will help organizations to assess the risk it faces in doing business with the client, where there is a former credit rating agency or credit bureau, it is advisable to get in touch with them.

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