

# Can a bank offset your debts with money that actually belongs to someone else?

By [Jonathan Shafir](#)

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In the decision of the Supreme Court of Appeal in *FirstRand Bank Limited v The Spar Group Limited*, handed down earlier this year, the Court answered two important and interrelated questions.



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Firstly, can a bank set off what the customer owes it against credit amounts in the customer's account in circumstances where the bank knows that a third party has a claim to those funds? And, if not, what claim, if any, does the third party have against the bank?

Secondly, does the bank have a legal duty to a third party if it allows the customer to use money deposited into its account by a third party, in circumstances where the bank knows the customer has no valid claim to those funds?

The facts in the *Spar Group Ltd (Spar) v FirstRand Bank (FNB)* case were briefly that Spar conducts business as a wholesaler to the Spar group of independent retailers. Spar fell into a dispute with one of its retailers, Umtshingo Trading 30 (Umtshingo), whose director was Arnaldo Paulo, and which owned or operated a KwikSpar store and two Tops liquor stores. For each store, Umtshingo kept a separate bank account with FNB at its Nelspruit branch.

## Defaults, security and speedpoints

As a form of security for debts owed to it by Umtshingo, Spar held a notarial bond over the assets of Umtshingo. Umtshingo defaulted on its obligations to Spar and as a result Spar obtained a provisional order from the local magistrates' court perfecting its notarial bond over Umtshingo's stores. The terms of the notarial bond permitted Spar to take over the Umtshingo businesses and run them for its own account. Armed with the provisional order, Spar confronted Paulo with the option of closing the shops or allowing Spar to trade for its own account in terms of a 'short term business lease' during the interim period until a final order to perfect the bond was granted. Paulo was keen to avoid closure, supposedly to escape a

loss of business reputation, and he agreed to the terms of a draft agreement which regulated this arrangement, with the exception that Paulo refused to de-link the speedpoint credit card devices of the stores from the bank accounts of Umtshingo.

Spar then ran the stores on the terms of the unsigned draft agreement while crediting the stock on hand to Umtshingo and bringing in new stock. Cash receipts were also deposited into a Spar bank account. However, the stores under Spar's control continued to use speedpoint credit card devices, which allowed for electronic revenue deposits directly into Umtshingo's designated accounts. Spar continued to allow revenue earned from its trading to be deposited into these three accounts, albeit reluctantly, whilst taking several steps to try to get Paulo to consent to a change or to get FNB to redirect the revenue to a Spar account. Spar's failure to achieve either of these objectives resulted in substantial sums of money flowing into Umtshingo's accounts.

## **Paulo's debt, Spar's money**

During this period, while retaining control over these accounts, Paulo made substantial payments from two of them for his own purposes.

In addition, the debit balances of Umtshingo's overdraft liability and its debts to FNB in respect of a loan and a guarantee were settled by FNB applying set off against the credits that were derived from the revenue generated by Spar and deposited into the accounts.

The upshot was that Spar claimed that FNB should not to have allowed disbursements to be made by Paulo because Umtshingo had no right or claim to the funds, and that FNB was not entitled to set off Umtshingo's debts in respect of which Spar had a claim.

In reaching its decision, the Court recognised that there were many cases where a bank's customer is not entitled to the funds which are credited to that customer's account where such funds legitimately belong to a third party who is not the account holder. Such third party is entitled to claim payment from the bank of the credit balance in the account. For example, this occurs when stolen money is deposited into an account or a deposit is made in error.

## **The Court held that:**

1. Where a deposit, to the knowledge of the bank, is made into the bank account of a customer, to which the customer has no entitlement, the bank cannot set off its customer's indebtedness to the bank against the credit in the customer's account which was derived from such deposit. The third party whose moneys were deposited has a claim against the bank for the amount which the bank has claimed by way of set off.
2. A customer, with no entitlement to moneys deposited into its account, who knows that it has no such entitlement, may not make disbursements from the account using credits derived from those moneys. To do so, amounts to theft. A bank that knows that its customer enjoys no such entitlement and nevertheless permits its customer to make

disbursements in these circumstances is a joint wrongdoer with the customer who made the disbursements. As such, the bank owes a legal duty to the third party who was entitled to the moneys deposited and suffers loss as a result of the customer's disbursements.

3. Accordingly, FNB misappropriated the funds when it applied set off and FNB wrongfully allowed Paulo to misappropriate funds from the accounts and was liable to pay Spar the amounts so misappropriated.

## ABOUT THE AUTHOR

Jonathan Shafir is the Director: Litigation at Fluxmans Attorneys. Jonathan is an established commercial litigation and dispute resolution specialist in one of the most successful litigation departments in South Africa, and has been involved in several high profile and complex matters during his career to date.

Knowing that strategic and effective litigation and dispute resolution is critical in finding the best and most efficient resolution, Jonathan uses his extensive experience and skill to determine the best outcome for each client so as to act in their best interests.

His expertise lies in general civil and commercial litigation, arbitrations, insolvency, construction disputes, landlord and tenant disputes, corporate disputes, administrative law, outdoor advertising, and defamation.

Jonathan has also been involved in disputes around tender awards by organs of state such as PRASA, Eskom and various municipalities.

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