NEGOTIABLE INSTRUMENTS:

DEFINITION OF A NEGOTIABLE INSTRUMENT:

Instrument:
These are documents of title to a sum of money (legal documents) which prove that the possessor has a right to claim a particular sum of money. The right to claim payment arises on and is embodied in the instrument itself.
Negotiable:
These documents are transferable. The original recipient of the document usually receives it in payment of a debt owed to him and can either claim payment on it or pass it on to another person who, through his possession gains the right to payment or to transfer it on.

Transfer of a negotiable instrument is called **NEGOTIATION**.

Negotiable instruments are thus documents which are used as proof to one's claim to a sum of money (instrument), such right being transferred through the transfer of possession from one person to another (negotiable).

Distinguishing characteristics:

- Negotiable instruments are used as alternatives to cash in the payment of debts as they are more convenient and safer than cash. In order to be viable alternatives to cash, they have to satisfy the following three requirements:

  1. They have to be transferable WITHOUT the need to comply with cumbersome formalities (easy to transfer)
  2. The defences that can be raised against a person claiming payment should be kept to the minimum. (See later)
  3. The legal title of a person who acquires such an instrument in good faith should be open to dispute in exceptional circumstances only.

- These requirements are clearly met by the **TWO** characteristics of negotiable instruments namely:

  1. SIMPLICITY OF TRANSFER
  2. TRANSFER FREE FROM EQUITIES.

THE TWO DISTINGUISHING CHARACTERISTICS OF NEGOTIABLE INSTRUMENTS:

1. **Simplicity of Transfer:**
A negotiable instrument is transferable without compliance with the complex formalities. Because the rights arise on and are embodies in the instrument itself, they can be transferred either by simply transferring the instrument itself (delivery) in the case of bearer instruments, or by signing the back thereof (endorsement) and delivery in the case of order instruments.

2. **Transfer free from equities:**

It is a basic principle of our law that no one can transfer a better (stronger) title in a thing to another than you yourself have (*nemo plus rule*). Thus, if someone has a defence against your claim, he will have the same defence against any person to whom you have transferred your claim. It is said that the recipient of the transferred right takes the right "subject to equities". The law of negotiable instruments creates an exception to this basic rule. In certain cases the person who had a defence against your claim can't raise the same defence against the person to whom you have transferred your claim. In other words, the recipient of a negotiable instrument may sometimes acquire an unquestionable right to payment of a negotiable instrument even though the person from whom he takes it had a questionable right.

Such acquisition of a "better" right than one's predecessor is called acquiring the instrument "free from equities" and only occurs when the recipient acquires the instrument (inter alia):

- **In good faith** i.e. he did not know of any defect in his predecessor's title and
- **For value** i.e. he gave something in return for receiving the instrument.

Transfer free from equities does not always take place!! The person, who takes an instrument as a HIDC, takes it free from equities, but an ordinary holder takes it subject to equities – same as a cessionary.

= Someone who acquires an instrument free from equities is called a HOLDER IN DUE COURSE
= Someone who acquires an instrument subject to equities is called a HOLDER.

NEGOTIATION V CESSION:

What is cession?

Cession is the transfer of a personal right (the right to claim performance from another) from one person to another.

What is negotiation?

Negotiation is the transfer of the right to claim payment of a negotiable instrument from one person to another by transfer of the instrument itself (i.e. the transfer of the **personal rights embodied in the negotiable instrument**).

They are **similar** in that they both involve the transfer of a personal right.

They can however be **distinguished** as follows:

NEGOTIATION is the simplicity of transfer with the transfer free from equities (taking the instrument as a HIDC).
CESSION is the difficulty of transfer with the transfer subject to equities (taking the personal right as the cessionary).

- The permission of the debtor is necessary before the cedent can transfer his personal right he has against the debtor to the cessionary and any defects in the cedent's title, **arising from the original contractual relationship**, are passed onto subsequent creditors (cessionaries). The cessionary can therefore **never acquire a better right** than the cedent (*nemo plus rule*) and is said to take the right "subject to equities". Thus all the advantages the cedent had against the debtor are passed to the cessionary as well as any disadvantages (advantages being security or interest and disadvantages being for example the fact that the debtor was a minor or that there was a misrepresentation rendering the contract between the debtor and the cedent voidable.

Examples:

A, a businessman enters into a contract to purchase 25 uncut diamonds from B, a seedy “diamond” salesman, for R100 000. A does not give B the R100 000 in cash:

SCENARIO 1: A gives B an IOU in which he acknowledges his debt of R100 000 to B.

A and B have entered into a contract of sale in terms of which B is to deliver 25 uncut diamonds to A and

in return A will pay B R100 000. A owes B R100 000 in terms of an IOU. B thus has a **personal right** to claim payment from A. The personal right arose from the creation of the contract between A and B.

WHAT IF A DOES NOT PAY? CAN B SUE A FOR THE R100 000?

Because the sale of uncut diamonds is illegal, any contract for the sale thereof is unenforceable in court. Thus if A does not pay, B will be unable to enforce payment in court because the original contractual relationship between A and B is tainted. Thus, if B did sue A, A would simply raise the fact that the contract is illegal as a defence to B's claim. B therefore has a defective right.

BUT, what if B transferred the right?

Although B can't enforce his personal right against A, he can still transfer it to another party. Let us assume B decides to transfer his right to claim payment from A to C.

Would such transfer be cession or negotiation?

As we have seen, the term "**negotiation**" is only used to describe the transfer of the **rights contained in the negotiable instrument**, whereas **cession** is used to describe **any** transfer of a personal right.

An IOU is NOT a negotiable instrument and thus cannot be negotiated – thus its cession!

Thus B can't "negotiate" his personal right to C. He CAN however, cede his personal right to C.

The consequences of such a cession are:

1. Difficulty of transfer: B must get A's permission before he can cede his right to C.
2. Transfer subject to equities: C cannot acquire a better right than B had, i.e. because B's title is defective, so will C's title be defective. Thus, C, just like B, will be unable to enforce payment by A in court because of the illegality of the underlying contractual relationship. This will be the situation regardless of whether or not C took the IOU in good faith and for value.

SCENARIO 2: A gives B a **promissory note** in which he acknowledges his debt of R100 000 to B and promises to repay it.
As in the above scenario, should A refuse to pay B, B will be **unable** to enforce payment in court because the original contractual relationship between A and B is illegal. B therefore has a defective right.
Although B cannot enforce his personal right, he can transfer his right to claim payment from A to a third party, C.

Would such transfer be cession or negotiation?

A promissory note **is** a negotiable instrument. And, therefore B can **"negotiate"** his personal right to C.

Consequences of such negotiation:

1. Simplicity of transfer: B need not get A's permission to transfer his right to C. because the right to claim payment is embodied on the instrument itself, B need merely deliver the instrument to C in order to transfer the rights therein.
2. Transfer free from equities: C can possibly acquire a better right than B had.

- If C took transfer of the document in **good faith and for value**, he will qualify as a **holder in due course** and acquire a better title than B had (free from equities). The **original contractual relationship** between A and B does **not** affect C's rights because C's rights are determined by what is embodied in the instrument itself and not the underlying contractual relationship between the original parties.

- Thus, C **could sue** A for non-payment, and A will not be able to rely on the illegality of the underlying contract as a defence of his non-payment. i.e. A will have to pay C.

- If C did not take the instrument in good faith and for value, he will take the instrument subject to equities, in which case he will be in the same position as the cessionary – all the rights the previous person had, he will have (which in this case was no rights to sue.)

THREE TYPES OF NEGOTIABLE INSTRUMENTS:

1. **Bills of exchange**: defined as "an unconditional **order** in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a fixed or determinable future time, a sum certain in money to a specified person or his order or to bearer."

2. **Cheque's:** define as "an unconditional **order** in writing, addressed by one person to a bank, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, a sum certain in money to a specified person or his order or to bearer." .

3. **Promissory notes:** defined as "an unconditional **promise** in writing made by one person to another, signed by the **maker,** and engaging to pay on demand or at a fixed or determinable time, a sum certain in money, to a specified person, his order or to bearer."

THE RELATIONSHIPS BETWEEN PARTIES TO AN INSTRUMENT:

There are always **three** different relationships to a negotiable instrument:

1. The underlying relationship: the reasons why the drawer draws the instrument on the drawee in favour of the payee and why the payee negotiates the instrument to the transferee.

(Example, lease, sale, donation, services rendered etc).

2. The relationship arising from agreement to make use of the instrument: the express or implied agreement between the payee and drawer that payment will be effected by means of a negotiable instrument. The payee is not obliged to accept payment by means of negotiable instrument.

3. The relationship on the instrument itself the right to claim payment is reflected on the face of the instrument itself. Thus, the underlying relationships on the instrument become less important as soon as the instrument is transferred to a new recipient. The rights of the new recipient, or subsequent recipients, are determined by the contractual relationship reflected on the instrument itself, and not the contractual relationship between the parties thereto. This gives rise to the possibility of taking the instrument free from equities.

POSSIBLE QUESTION:

Identify the relationships in this example:

A (drawer) draws a cheque on B Bank (drawee bank) in favour of C (the payee) in payment for a lounge suite, which A bought from C. Upon taking the suite home, A finds that it is the incorrect size. A returns the suite to C and demands his money back. C explains that she has already transferred the cheque to her landlord, D, in payment for her rent. D approaches B Bank for payment of the cheque.

1. Underlying relationships: between A and C - the debt, and between C and D for the rent.
2. Arising from agreement to make use of the negotiable instrument: A and C and C and D.
3. Relationship on the instrument itself: A and C, C and D, D and B Bank.

NECESSARY PARTIES:

From the definition of a bill of exchange there are always three different parties:

1. The person giving the order to pay - the DRAWER.
2. The person to whom the order to pay is addressed - the DRAWEE
3. The person to whom the order designated payment - the PAYEE.

From the definition of a cheque, it's merely a specific type of bill of exchange. In line with this, it has the same parties:

1. The DRAWER is the current account (cheque account) holder).

2. The DRAWEE IS ALWAYS a banker (i.e. a cheque is a bill drawn on a banker). The drawee is thus the bank, which holds the current account of the drawer, and at which the drawer has either deposited an amount of money to be used to payout cheques, or with which the drawer has made an arrangement for overdraft facilities.

3. The PAYEE is the person to whom payment must be made.

In contrast, there are only two necessary parties to a promissory note.

1. The person making the promise to pay - THE MAKER
2. The person to whom the promise is made – THE PAYEE

Further parties:

- The **payee** of a negotiable instrument has various options available to him once he has taken possession thereof:

- He can claim payment thereof himself or
- He can transfer the instrument to another person.

- If the **payee** wishes to **transfer** a **bearer** instrument he need merely transfer possession thereof to the new recipient – thus to deliver it to the new recipient. The payee thereby undergoes a change in capacity and is then referred to as the **transferor by delivery.**

- If the **payee** wishes to **transfer** an **order** instrument, he has to **indorse** it (sign the back) **and deliver** it to the new recipient. When the payee does so, he undergoes a change in capacity and becomes known as **the endorser** of the instrument. The person in whose favour the indorsement was made (i.e. the person to

whom the payee now wants payment to be made) is the **indorsee.**

- Both **the possessor** and the **indorsee** now have the same options available as the payee.

- Once the **drawee** has signified his **assent** to the order of the drawer, he undergoes a change in capacity, and is thereafter referred to as the **acceptor** – only applicable to a BILL OF EXCHANGE. (Cheques are never accepted!!)

POSSIBLE QUESTIONS:

1. Comment on the following statements:

(a) "The drawee, the person who is ordered to pay the drawer, is automatically liable on the bill in this capacity."

This statement is true in the sense that the drawee is the person ordered to pay by the drawer. The statement regarding the automatic liability of the drawee – according to s51, a bill is not an assignment of funds in the hands of the drawee and available for payment. If the drawee does not accept the bill, he is not liable on it. By accepting it, he becomes the acceptor and thus incurs liability on it.

(b) "Issue and negotiation of a bill is one in the same thing."

Issue: The term issue refers to the first delivery of a bill, complete in form, to a person who takes it as a holder. Issue is the first delivery, i.e. the delivery by the drawer to the payee. Complete in form: means that all the essential elements of form are met so that the instrument is valid. An incomplete cheque can never be issued.
Negotiation: refers to transfer of possession or title to a cheque to a transferee who qua dies as a holder in due course (called negotiation in terms of common law). When one can negotiate: the payee or bearer to whom an instrument has been issued, if he wants to, can negotiate the instrument, unless words appear on the instrument prohibiting its transfer.

2. What are the difference between an indorser and a transferor by delivery?

An endorser - no contract on the bill which places the obligation on the payee before his signature is placed thereon. Payee is to deliver the document to another having signed it to create a contract. The endorser's liability arises from the contract on the bill and he is liable by virtue of the instrument itself.

Transferor by delivery is not liable on a bill as he didn't sign it. He is the holder of a bill payable to bearer (there is no signature in any capacity). He is not liable as he didn't sign it – there is no question of liability that arises from the contract on the bill.

THE ESSENTIAL ELEMENTS OF AN INSTRUMENT:

- These have to be present before a document will be regarded as a negotiable instrument.

1. Order or promise to pay.
2. Unconditional.
3. In writing.
4. Addressed by one person to another
5. Signed by the person giving it.
6. Requiring the person to whom it is addressed to pay on demand or at a fixed or determinable future time.
7. A sum certain in money.
8. To a specified person or his order, or to bearer.

1. **ORDER OR PROMISE**: the wording of the bill or cheque must be imperative in order to constitute an order or command, and not merely constitute a request. Example "pay X R300" versus "Please oblige me by paying X R300". Regarding a promissory note, we can see from its definition that there need not be an order to pay, but merely a promise to pay. This serves to distinguish promissory notes from bills.

2. **UNCONDITIONAL**: the drawee bank's duty to pay must not be conditional upon the happening of any future uncertain event. Even the fulfillment of the condition will not cure the defect and convert it to a valid negotiable instrument. An example of an invalid order (i.e. conditional): "Pay to C provided the receipt at the back hereof is signed." There are certain special orders that can be incorporated in a negotiable instrument without it being regarded as conditional, like an indication of the particular fund out of which the drawee is to reimburse himself.

3. **IN WRITING**: because the right to claim payment is embodied in the negotiable instrument itself, writing is required to facilitate the easy transfer thereof.

4. **ADDRESSED BY ONE PERSON TO ANOTHER**: in the case of a bill of exchange or cheque, the order is addressed by the drawer to the drawee. The drawee must be named or otherwise indicated on the instrument with reasonable certainty. **An**

instrument may be addressed to two or more drawee's jointly, but NOT to two or more drawee's in the alternative. E.g. A and B versus A or B vs. A and if not A, B. In the case of a promissory note, the promise must be addressed by the maker to the payee.

5. **SIGNED BY THE PERSON GIVING IT**: the drawer's or maker's signature can take various forms (a cross or a mark, a corporate seal, a company stamp etc.). As a general rule, it appears on the bottom right hand side of the document.

6. **REQUIRING THE DRAWEE TO WHICH HIS ADDRESSED TO PAY ON DEMAND OR AT A FIXED OR DETERMINABLE FUTURE TIME**: the due date or time of payment of a negotiable instrument may be either:

- On demand.
- At a fixed future time.
- At a determinable future time.

An instrument will be payable on demand (at any time it is presented) when:

- Its expressed to be payable on demand, at sight (upon acceptance) or on presentation;
- No time for payment is stated
- It is accepted or indorsed when overdue.

In terms of the definition, a cheque must always be payable on demand.

An instrument is payable at a determinable future time when its payable:

- At a fixed time after date
- E.g. "Pay V R400, 6 months after date"

- At a fixed time after sight (acceptance of the bill) E.g. "Pay B R2100 10 days after sight."

- On the happening of a specified event which is certain to happen (time clause)
- E.g. "Pay X R250 on F's death"

- At a fixed period after the happening of a specified event which is certain to happen:
- E.g. "Pay O R300 10 weeks after P's death".

- **The due date is important for many reasons:**

- **It determines the time for payment**
- **The debt on the instrument can only be discharged through payment prior to the due date.**
- **A person who takes an instrument after its due date, can never quality as a holder in due course. (NB see later)**

7. **A SUM CERTAIN IN MONEY**:

The exact amount must be clear on the face of the instrument without need to turn to extrinsic evidence to calculate it. The amount payable need not be expressed in SA currency; it can be in a recognised currency. The order may NOT require anything other than the payment of money. E.g. "Pay Q R250 and deliver 100 bags of wool." Although the law does not require that the amount payable be expressed in words and figures, its general practice to do so. The amount stated in the words differs from the amount written in figures, the Act provides that the amount in words is payable.

8. **TO A SPECIFIED PERSON OR HIS ORDER, OR TO BEARER**:

The order to pay must indicate to whom payment must be made. On the basis of how the payee is indicated, one can distinguish between two types of negotiable instruments:

1. Negotiable instruments payable to a specified person or his order = order instruments
2. Negotiable instruments payable to bearer = bearer instruments.

An instrument will be payable to order (i.e. only a particular person can claim payment) if it is payable to:

- A specified (e.g. Pay C)
- A specified person or his order (e.g. Pay C or order)
- The order of a specified person (e.g. Pay to the order of C)

An instrument may be payable to two or more payees jointly, or to two or more payees in the alternative. E.g. Pay F and G or Pay H and, if not H, pay D. NOTE HOW THIS DIFFERS FROM THE REQUIREMENTS SURROUNDING DESIGNATION OF DRAWEES.

AN INSTRUMENT IS PAYABLE TO BEARER IF: (i.e. any person in possession of the instrument can claim payment)

- It is simply payable to "bearer", "cash" or "cash or bearer"
- It is payable to a specified person or bearer (e.g. Pay C or bearer)
- If the only, or last endorsement, is an "endorsement in blank" (ie. Its an order instrument endorsed on the back with merely a signature of the transferor).
- If the payee OR endorsee of an **order** instrument is someone **without the capacity to contract**.
- If the instrument says “To bearer or order” its deemed to be a bearer instrument.

AN INSTRUMENT IS PAYABLE TO ORDER IF:

- The instrument is made out to Mr. C
- The instrument is made out to Mr. C or order
- The instrument is made out to the order of Mr. C

POSSIBLE QUESTION:

Is the following instrument a valid bill of exchange? Motivate your answer fully.

Pretoria
10 May 2008

To: Sammy Sam or Jannie Jan
123 Church Street
Cape Town
8001

Without recourse to me, Sammy Sam or Jannie Jan will pay Handy Manny or Linky Link on demand the sum of ten thousand rands plus interest at 20% per annum.

R1000,00

Signed: Lizzy Lizz

This is not a valid bill of exchange. The reason is: to be a valid bill of exchange, the bill must have a written, unconditional order, addressed by one person to another person to pay a specified sum of money to a particular specified person, his order, or to bearer, on demand; or at a fixed or determinable future time. This bill must be signed by or on behalf of the person giving the order.
The drawer Lizzy Lizz and she has added "sans recors" – without recourse to me – which has the effect that she cant be help liable if the bill is dishonoured. This particular bill was made payable to Sammy Sam or Jannie Jan on demand. These payees are in the alternative but this is allowed in terms of the Act. Even though the amount is payable with interest, this is allowed as it is still deemed to be "certain". The date is NB in terms of the calculation of the interest and to be sure that payment has taken place within a reasonable time. The place for payment has also been given. The instruction to pay the addressed to the drawees Sammy Sam and Jannie Jan in the alternative, but this is not permitted in terms of the Act and thus the bill is invalid.

THE NON-ESSENTIAL ELEMENTS OF AN INSTRUMENT:

These do **not** affect the validity of the instrument if they are not all present or absent.

1. The date
2. Place of drawing
3. Place of payment
4. Amount
5. Stamps
6. **Without recourse (sans recourse**)- the drawer/endorser of an instrument may insert an express stipulation regarding or limiting his own liability to the future recipients thereof. E.g. Pay X or order without recourse to me" In such instances the drawer or endorser can't be held liable should the cheque subsequently be dishonored.
7. Waiver - the drawer or endorser of an instrument may insert therein an express stipulation waiving as regards himself some or all of the holder's duties.

THE ORDINARY HOLDER:

- The holder of a bill is a person who can claim payment thereon.
- When defining a "holder" it is crucial to distinguish between bearer and order instruments.

  - **BEARER INSTRUMENTS**: the holder of a bearer instrument is simply the person in **possession thereof (the bearer).**

  - **ORDER INSTRUMENTS**: the holder of an order instrument is either:
    The **payee in possession** thereof (if it has not been transferred)
    The **endorsee** in possession thereof (if it has been transferred)

  - NB: because possession is a prerequisite for being a holder, there can only be one holder at any given moment, although there can be many different holders at different times during the "life of the cheque".

Whilst possession is a prerequisite for qualifying as a holder, possession is not necessarily enough:

Example:
X, the **payee** of a bill made payable to **"X or order",** fails to indorse it before transferring it to Y.
Will Y, who is now in possession of the bill, qualify as a holder thereof?
If the person is not named on the bill (like in this case), Y is merely in possession of an order instrument and the requirements to be a holder of an order instrument is possession and endorsement, so here, possession is **not** enough to be a holder.

It's not necessary for the holder of the bill to be in lawful possession or to be the owner thereof to qualify as a holder.

The thief in possession of a bearer instrument (cash cheque) is a holder, as possession is the only requirement to be a holder of a bearer instrument. BUT the thief of an order instrument is not the holder.

THE RIGHTS AND DUTIES OF A HOLDER:

The seven rights of a holder:

1. He may sue on the bill in his own name (although he may sue in his own name he may not necessarily always be successful.)
2. He may present the bill for acceptance (the holder or his authorised representative may present the bill for acceptance to the drawee).
3. He may present the bill for payment (the holder or his authorised representative may present the bill for payment to the drawee/acceptor).
4. He may supplement certain deficiencies in the form of a bill - certain non-essential elements may be inserted by the holder (e.g. he may add to an undated cheque, the date on which he received it).
5. He may make certain additions and altercations to the bill (i.e. he may cross an uncrossed cheque, or add certain details to the crossing, or convert and blank endorsement into a special endorsement).
6. He may request a duplicate from the drawer where it has been lost: where possession has been lost, the "holder" or last person to be in possession thereof, can apply to the drawer/maker to give him a duplicate, provided the bill is not yet overdue.
7. He may have the bill protested for better security.

Possible Questions:

Name 4 rights that the holder of a bill has in terms of the Bills of Exchange Act.

ANSWER: see above.

THE HOLDER IN DUE COURSE:

REQUIREMENTS:

A person is able to take a bill "free from equities" (meaning that someone acquires a valid title to a bill even though his predecessor had a defective title to the bill or no title at all). This recipient is called the "holder in due course".

The holder in due course thus takes the bill **FREE FROM EQUITIES**.

To qualify as a holder in due course, the person must meet all eight requirements:

1. He must be a **holder** of the bill.
2. The bill must have been **negotiated** to him (i.e. mere delivery if it is a bearer instrument or endorsement plus delivery if it is an order instrument).
   THE PAYEE OF AN ORDER INSRUMENT CAN NEVER BE A HOLDER IN DUE COURSE. THE PAYEE OF A BEARER INSTRUMENT CAN BE A HOLDER IN DUE COURSE IF THE REQUIREMENTS ARE MET.
3. The bill must be complete and regular on the face of it.
   Complete: all the essential elements must be present at the time he comes into possession thereof
   Regular: if it is clear that something is improper from the face of the bill, that took place in previous dealings, then the bill is not regular on the face of it (e.g. a torn bill indicates its cancellation).
4. He must become the holder of the bill **before it is overdue**.
5. He must take the bill **without notice** of any previous dishonour (without knowing that it has been dishonoured in the past.)
6. He must take the bill **good faith**. He must act honestly even if negligently. If he is suspicious about any aspect relating to the bill and fails to make enquiries for fear of having his suspicions confirmed, he is not acting honestly.
7. He must take the bill without notice of any defect in the title of the transferor.
8. He must take the bill either for **due consideration** (not as a gift) or for *quid pro quo*. (Use to be "**for value**" now changed by

section 25). The holder should not have taken the bill as a gift but should have done something in exchange for it.

THE PRIVILEGED POSITION OF THE HOLDER IN DUE COURSE:

The holder in due course takes the bill free from equities, thus he has a privileged position. Some defences cannot be raised against him when he sues for payment of the bill – VERY IMPORTANT (SEE QUESTION ON DEFECTIVE GEAR BOX IN THE CAR BOUGHT!!)

- The **holder** takes the instrument subject to **relative and absolute defences**, i.e. both categories of defences can be raised by the person being sued for payment.
- The **holder in due course** takes the instrument subject only to absolute defences, i.e. only the **absolute defences** can be raised by the person the holder in due course is suing for payment.

RELATIVE AND ABSOLUTE DEFENCES NBNB!!!!:

Relative defences:

1. Defences in *rem*: related to defects in title of previous parties, such as fraud or illegality.
2. Defences in *personam*: arising from the underlying contractual between two parties, such as set-off, part-payment, **latent defects** or misrepresentation).

Absolute defences:

1. Lack of contractual capacity.
2. Forged or unauthorised signatures.
3. Material alteration - this is simply an alteration to a bill which alters the existing liability of the parties to a bill. Like the alteration of the date, amount, time and place of payment. The liability of the parties who have not consented to such an alteration is determined as if not alteration had been made.

The position of the holder in due course is further improved by the operation of *estoppels*, which prevent absolute defences from being raised against holders in due course in certain circumstances (eg. S22 and s21 in forged or unauthorised signatures).

POSSIBLE QUESTIONS:

1. Alison buys a car from Cane for R900 000. In payment of the purchase price, Alison delivers to Cane an uncrossed cheque drawn on B Bank in favour of Cane. Cane negotiates the cheque to Danny. The car however has a faulty engine and Alison thus calls B Bank stops the cheque. Danny claims payment from Alison.

(a) Does Alison have a defence against Danny's claim because Cane committed breach of contract be delivering a defective car?

Alison's defence would be one of "latent defect" which is a relative defect. This defence can successfully be raised only against a holder. Cane was a holder of the cheque. When he however, negotiated it to Danny (we can then assume that Danny too the cheque in good faith and for value as the cheque was "negotiated" to him) Danny then is a HIDC and the relative defence of "latent defects" cant be raised against him (Danny being the plaintiff as he is suing Alison for the money). Danny would then succeed in suing Alison for the R900 000 as Alison's defence that Cane's performance was defective wont succeed against a HIDC plaintiff.

(b) Does Alison have a defence against Danny's claim if Cane was a minor when Cane endorsed the cheque?

If Cane was a minor when he endorsed the cheque, Danny still qualifies as a HIDC, but the absolute defence of "lack of contractual capacity" may be raised against both holders and HIDC's successfully, and thus Alison may raise this defence against Danny and wont have to pay Danny.

(c) Would your answer in (a) be different if the cheque had been crossed and marked "not negotiable"?

Yes, my answer to (a) will differ because the cheque has been crossed and marked "not negotiable" (see later regarding crossings) – the effect of a crossing is merely to ensure the payee / endorsee / transferee by delivery does not receive cash over the counter, but the add the words "not negotiable" to a crossing, means no cash over the counter AND that anyone after the payee wont take the instrument as a HIDC – thus the cheque in the question at hand, is still transferrable but no longer negotiable (meaning it can still be transferred on but that the transferee wont become a HIDC). Danny thus is not a HIDC and Alison may then raise the relative defence of "latent defects" against Danny and won't have to pay him. This is due to the fact that Danny is merely a holder as the cheque that was handed to him was crossed and marked "not negotiable".

(d) Assume that Alison's signature on the cheque was forged by Princess. Princess fraudulently presents herself as Alison's agent, and takes delivery of the car. Does Alison have a defence against Danny's claim?

Yes, Alison may again use the defence of "forged or unauthourised signatures" which may succeed against HIDC's and holders. Since Danny is a HIDC and this defence is

available against him, she wont have to pay Danny and her defence will succeed.

2. Distinguish between relative and absolute defences.

Relative's defences are mere personal defences available to prior parties among themselves. These defences can only be raised against a holder, <u>but not against a holder in due course</u>. Examples of relative defences include: where the debt is a gambling debt; set-off; conditional issue or negotiation; innocent misrepresentation or
latent defences arising form the underlying contractual relationship and which apply to the parties among themselves.

Absolute defences are those defences that may be raised against all holders, including holders in due course. Examples of absolute defences include: lack of capacity to act (i.e. minor that draws cheque without assistance); forged or unauthorised signature and material alterations where the bill or acceptance thereof had been obtained by fraud.

3. On 12 January 2012 Connie sells a stove to Annie for R2 000. Annie pays by cheque. The cheque is drawn on Best Bank and made payable to "Connie or order". The next day, Connie delivers the stove. Annie then discovers that the element of the stove is not warming up. She immediately returns the stove to Connie and stops payment of the cheque.

a. Can Connie hold Annie liable for payment?

Connie cannot hold Annie liable as Annie can raise the defence that payment is not due because the stove is defective and has been returned to Connie. This defence is a relative defence of a latent defect. Because Connie is merely a holder (she is the payee of an order instrument and thus only a holder), the relative defence of "latent defects" can be raised against him. Relative defences may only be raised against holders (and never HIDC's) thus, Annie wont have to pay for the stove.

b. Assume that on 13 January 2012, Connie uses the cheque to repay a debt which he owed to Desmond. Connie endorses the cheque in favour of "Desmond or order" and delivers it to him, When Desmond presents the cheque for payment, he is told that payment had been stopped.

Can DESMOND hold ANNIE liable for payment? Explain fully.

Desmond could possibly hold Annie liable for payment if Desmond meets certain requirements, namely the requirements to qualify as a holder in due course. These include, *inter alia,* taking the cheque in good faith and for value. Desmond would be able to sue Annie for the full R2000. Annie can't raise the defence

against Desmond that payment is not due cause she returned the defective stove. By negotiating the cheque to Desmond, Connie transferred her right to claim R2000 from Annie's bank, to Desmond. Here, Desmond acquired the cheque free from equities (provided he complied with the 8 requirements for being a HIDC). If the cheque was negotiated to Desmond and he took it in good faith and for value (repayment of a debt), he is a holder in due course. The relative defence of latent defects can't be raised against a HIDC, as these defences may only be raised and be successful against holders. Annie will have to pay Desmond the R2000 and sue Connie in contract law.

Explain in each instance whether X is a mere possessor, or a holder, or a holder in due course, or a mere possessor.

a) A draws an uncrossed cheque on B Bank in favour of "X or order" and delivers it to X.

X will qualify as a mere holder as he is the payee of an order cheque and can never be a HIDC

b) A draws a bill on B in favour of "C" and delivers it to C. C delivers the bill to X with the intention of transferring his rights to X but neglects to indorse the bill.

Rights in NI's are transferred by negotiation of the bill and all the rights in the bill are contained in the bill itself. To qualify as a HIDC, the bill must be negotiated to you. An order bill is negotiated by way of endorsement plus delivery. In this question C intended to transfer rights. To be liable on a bill and transfer rights in it- endorsement plus delivery is needed. C delivered the bill but did not indorse it. Thus X is a mere possessor of an order bill.

A draws a cheque on B Bank in favour of C or order. The cheque is crossed generally with the words "not negotiable" across its face. C indorses the cheque in blank and delivers it to X, who takes it in good faith and for value.

A holder means "the payee or indorsee of a bill who is in possession of it or the bearer thereof (section 1) or X is the holder because X is the indorsee in possession of the cheque. Despite the addition of the words "not negotiable" the cheque can still be negotiated in such a manner that the transferee is constituted the holder of the cheque (see section 29(1) read with section 80 of the Bills of Exchange Act). If the drawer adds the words "not negotiable" to a crossed cheque, no subsequent holder can become holder in due course of such a cheque (section 80). Thus, X will only be a holder. The endorsement in blank changes the order cheque into a bearer cheque. However, the words not negotiable written on the face of the cheque prevents anyone from becoming a holder in due course. X will thus only be a holder.

Explain whether X is a holder, and a holder in due course, or a mere possessor.

(a) A draws a bill on B in favour of C or order and delivers it to C. C delivers the bill to X with the intention of transferring his rights to X but neglects to indorse the bill.
(b) A draws an uncrossed cheque on B bank in favour of X or order and delivers it to him.
(c) A draws a bill on B in favour of C and delivers it to him. C indorses the bill and delivers it to X when the bill was overdue.

(a) The bill is payable to "C or order", thus it is an instrument payable to order (s 6(3)).
A bill payable to order is negotiated by the indorsement of the holder, followed by delivery. The holder, C, neglected to indorse the bill, therefore no negotiation took place and the transferee (X) did not become holder.
S29(4) provides that if a holder of a bill payable to order transfers it without indorsing it, the transferor gives the transferee (X) such title as the transferor, C, had in the bill, and the transferee acquires the right to have the bill indorsed by the transferor.
The holder of an instrument payable to order may transfer his rights in a bill by means of cession. X, the cessionary, cannot acquire more rights that what C, the cedent had. Because C was a holder, X acquires the rights of a holder by way of cession.

(b) X is a holder of the cheque because he is the payee in possession of the cheque.
X will not be a holder in due course because the cheque was issued - issue is the first delivery of a bill, complete in form, to a person who takes it as holder - and not negotiated - a bill payable to order is negotiated by indorsement of the holder completed by delivery to him.

(c) An overdue bill may still be negotiated. X may therefore become a holder of the bill, but he cannot acquire more rights in respect of the bill than C had. X cannot become holder in due course of the overdue bill because a holder in due course must have become holder of the bill before it became overdue.

A draws a cheque on B payable to "C or order". C delivers the cheque to D but does not indorse it. D gives value for the cheque. Answer the following questions:

Is D holder? Explain.

According to section 1 of the Act a holder is the payee or indorsee of a bill who is in possession of it, or the bearer thereof. D is not the payee, (C was), he is also not the indorsee of the document, and (there is no indorsement). D is also not the bearer of the document,

because we are dealing with an order document. D, does therefore not qualify as a holder.

Does D have any rights? Explain.

A holder's endorsement is required for the negotiation of an instrument payable to order and the endorsement is completed by delivery. Delivery of a bill payable to order without endorsement gives a transferee (D) who has given value such title as the transferor (C) had in the bill & the transferee (D) acquires the right to have the bill indorsed by the transferor (C). D does not become the holder in consequence of such a transfer, because it merely confers on him possession of a bill payable to order without him being either the payee or the endorsee at the time. Where an order bill is negotiated without the holder indorsing it, the transferee (D), although not holder, may institute action in his capacity as cessionary (The holder (D) cedes all his rights to the cessionary (D) by means of ordinary cession that is without indorsing the bill first.

C sells a watch to A. In terms of the agreement, the watch has to be a TAG. C, however, delivers a cheap imitation of a TAG. As A is not aware of the fraud, he pays C with a cheque for R50 000. The cheque was drawn on B Bank in favour of "C or order". C immediately negotiates the cheque to D. D is unaware of C's fraud. When A became aware of C's fraud, he stopped payment on the cheque. D claims R50 000 from A. Will D be able to sue A successfully for R50 000?

D will be a HIDC if he takes the cheque in good faith and for value. If this is the case, he will be able to sue A for payment on the cheque. Discuss all the elements needed to become a HIDC and the privileged position of the HIDC.

What are the requirements of a holder in due course?

See above.

A draws a bill in favour of X and delivers it to X. Is X a holder or a holder in due course (HIDC)?

The bill is drawn in favour of X and is thus an order instrument. As a payee of an order instrument, he can be a holder, because it was signed and delivered to X by A. The payee of an order instrument can never be a holder in due course. The bill was ISSUED to X by A and was not negotiated to X – to become a HIDC, the instrument has to have been negotiated to X by the previous party, here, the drawer, A. The drawer A, is ISSUING the bill, and delivering it to X. The signature he has placed on the bill is an essential element of the bill, and not an endorsement needed for negotiation.

On 15 January 2012, A draws a cheque for R500 on B Bank in favour of "C or order" and delivers it to C as a donation. Three months later, C negotiates the cheque to D by endorsement and delivery to repay a gambling debt that C owes D. five months later, D endorses the cheque in favour of E. Is E a HIDC?

An overdue cheque may still be transferred from one person to another but no person can acquire more rights in respect of the instrument than those which the holder had at the time of its maturity – no person can become a HIDC of this instrument after its due date. An instrument with a fixed date becomes overdue after the expiry of such due date. A bill payable on demand becomes overdue when it appears on the face of it to have been in circulation for an unreasonable amount of time. Thus, E cannot be a HIDC because the cheque is stale.

A draws a bill on B in favour of "C or bearer". C endorses this bill specially in favour of D. discuss the effect of C's special endorsement on this bill.

If an instrument is originally payable to bearer, it cant be converted into one payable to order by special endorsement. If the holder specially endorses a bearer document, the instrument remains payable to bearer despite such endorsement.
The special endorsement is used to transfer an order instrument from the transferor to the transferee, and if coupled with delivery (and intention to transfer) allows for an effective transfer of ownership of the instrument and may allow the transferee to become a HIDC if the requirements for HIDC are complied with.

A draws a cheque on B in favour of C or order. And negotiables the cheque under special endorsement to D. D then endorses under special endorsement to E. E then negotiates it back to A. Can A enforce payment against any of the parties?

Section 35 provides that A is not entitled to enforce payment against any of the intervening parties to whom he was previously liable. A cannot later enforce payment against C, D or E because A was formerly liable to them as drawer.

HOW PARTIES BECOME LIABLE ON A BILL:

There are two requirements that must be met before a party can be held liable on a bill.

He must:

1. **Sign** it and
2. **Deliver** it

The mere fact that a person is named on a bill as a party or that a person has handled the bill is not sufficient to make the person liable for payment thereof.

Capacity to act as a prerequisite:

In line with the general principles of the law of contract, a person must have "capacity to act" before he can be held contractually liable.

Capacity to act refers to the ability of a natural person to perform juristic acts, participate in legal intercourse and conclude valid contracts.

A person's capacity to act can be limited by a number of factors including marriage; age insolvency etc. For our purposes age is the most important determinant. Note the following:

- A contract entered into by a minor without the assistance of his guardian is not enforceable against the minor. Thus, a minor can't be held contractually liable on a bill even if he signed and delivered it, unless his guardian has given the minor consent to enter into the contract.

- Such a contract is, however, not without effect. The obligations created in terms of the contract can still be enforced against the other parties (i.e. the parties to the bill apart from the minor). Thus, the holder still has the right to claim payment from the other parties to the bill, provided they have Signed and delivered the bill.

WHAT IS A SIGNATURE?

The Act does not define a signature, but at Common Law, the term connotes any mark which identifies the act of the party concerned", thus it's not necessary to write entire name/initial and surname.
Initials alone seem sufficient, as do a simple mark, cross, imprint or rubberstamp.
It's also not necessary for the person to sign the bill with his own hand.

A party's signature can be applied to the bill by another person acting under his authority.

Example a juristic person gets a natural person with capacity to act to sign the cheque on behalf of the company who cannot itself sign.

Functions of signatures:

A signature placed on a bill fulfills at least one of the following three functions BUT NEVER ALL THREE:

1. **A constitutive function**: as an essential element of form, a drawer/maker's signature is necessary for the creation of a valid instrument.
2. **A guarantee function**: by signing the bill as drawer, endorser or acceptor, a person undertakes, amongst other things, to compensate the holder or a subsequent endorser who is compelled to pay to pay if the instrument is dishonoured when presented for payment.
3. **A transfer function**: order instruments are transferred by the holder's endorsement completed by delivery.

Which functions are fulfilled by the following party's signatures on a bill?

- A drawer? Constitutive and guarantee
- An acceptor? Guarantee
- An indorser? Guarantee and transfer

FORGED SIGNATURES NBNBNBNB!!!!!!!!!:

A forged signature on a bill is any fraudulent imitation of a signature with the object of deceiving another person.

Questions to ask YOURSELF when answering a question on forged signatures:

1. **Whose signature was forged?**

   In terms of **s21** of the Act, the person whose signature was forged will **never** be liable (regardless of whether the plaintiff is an apparent holder or holder by estoppel, or whether the instrument is payable to order or bearer).

2. **Who did the forging?**

   In terms of s21, the forger will always be liable as if he himself had signed his own name (regardless of whether the plaintiff is an apparent holder or a holder by estoppel or whether the instrument is payable to bearer or to order). The forger is always liable in DELICT or UNJUSTIFIED ENRICHMENT.

3. **What type of instrument is it?**

   If the instrument is payable to **bearer**, endorsement is not necessary to effect transfer of rights. Thus, any forged endorsement will be redundant, and the rights will still be passed by simple delivery of the instrument. All parties (other than the person whose own signature was forged) will thus be liable.

   If the instrument is payable to **order, s22 applies**. S22 states that no rights can be passed on through a forged endorsement ("wholly inoperative" and can never be ratified – the bill is worthless). Thus, no person who comes into possession of the instrument after the forgery can become a holder or a holder in due course thereof.

4. **If the instrument is payable to order: whom is the plaintiff suing?**

   Although no person who comes into possession after the forgery may qualify as a holder or a holder in due course, they may either be an apparent holder (i.e. if the signature had been genuine such a person would have qualified as a holder) or a holder by estoppel (i.e. if the signature had been genuine, he would have qualifies as a holder in due course):

- If the plaintiff is an apparent holder, any defendant would be able to rely on s22 as a defence (i.e. they can raise the defence that someone else's signature had been forged) and will therefore not be liable.

- If the plaintiff is a holder by estoppel some defendants will be unable to rely on s22 as a defence and will therefore be liable.

5. **<u>If the plaintiff is a holder by estoppel: who is the defendant (the one being sued)?</u>**

   There is one defendant who will be unable to raise s22. If the defendant is an INDORSER, he will be liable (unable to raise s22 as a defence) if, on the facts, either the drawer's or previous endorser's signature has been forged (s53 (2) (b)).

DO NOT ANSWER A QUESTION IN THE EXAM BY RECITING THESE QUESTIONS; THEY ARE MERELY A QUICK STEP SOLUTION TO CHECK THE PROVISIONS OF LEGISLATION.

<u>Examples:</u>

<u>Situation A – INDORSER'S SIGNATURE:</u>

A draws a cheque on B Bank in favour of C. X steals the cheque and forges C's endorsement on the back and transfers it to D. D transfers it to E who takes sit in good faith and for value.

A ------- B ---------- C----------X (forger)---------D----------E (pl)

<u>OUESTION 1</u>

C's signature is forged, so C is never liable (s21)

<u>Question 2</u>

X is the forger, so if E sues X, X is always liable, in delict.

<u>Question 3</u>

The instrument is payable to order so s22 applies.

<u>Question 4</u>

<u>E is the plaintiff:</u>

* If he is an apparent holder: A, Band D are not liable (s22 defence).
* If he is a holder by *estoppel*: there is a possibility of *estoppel*.

Question 5

If E is a holder by *estoppel* (which he is):

* A (drawer) is not liable (s22 - no *estoppel*)
* B (drawee) is not liable (s22 - no *estoppel*)
* D (indorser) is liable (*estoppel* – can't rely on s22 defence)

Situation 2 - DRAWER'S SIGNATURE:

(PREVIOUS EXAM QUESTION!!)
X steals a cheque from A and forges A's signature, draws the cheque on B Bank in favour of C. C indorses the cheque and transfers it to D. D then indorses the cheque and transfers it to E who takes it in good faith and for consideration.

A (forged by X) ---------B ---------C ----------D---------E

Question 1

A's signature is forged, so A is never liable.

Question 2

X did the forging, so he is always liable in delict.

Question 3

The instrument is payable to order, so s22 applies.

Question 4

E is the plaintiff.

* If E is an apparent holder: B, C and D are not liable (s22 defence)
* If E is a holder by *estoppel*: possibility of *estoppel*

Question 5

If E is a holder by *estoppel* (which he is):

* B (drawee) is not liable (s22 - no *estoppel*)
* C (indorser) is liable (*estoppel* – can't rely on s22)
* D (indorser) is liable (*estoppel* - can rely on s22)

TYPES OF QUESTIONS ON FORGED SIGNATURES:

A draws a bill on B payable to "C or order" and delivers it to C. D steals the bill from C, forges C's signature on the back of the bill and delivers it to E. E changes the forged "endorsement" to an endorsement in his (E's) name, signs the bill and delivers it to X, who takes it in good faith and for value. Can X enforce payment of the bill against any of the following parties?

(i) A

The forged signature of C cannot perform any function as a forged endorsement is wholly inoperative. No title can be transferred to E, which he can in turn transfer to X. X is not a holder and he consequently cannot claim from A or B and not from C either, C did not sign the bill. Payment by B to X will not affect the discharge of the bill either, since it would not be payment in due course to a holder.

(ii) D

Section 21 stipulates that no person is liable as drawer or endorser of a bill if he has not signed as such and therefore D cannot be held liable on the bill itself. However, D will be liable in delict OR on the basis of undue enrichment.

(iii) C

In terms of section 22 a forged or unauthorised signature is wholly inoperative and there is no right to retain or give a discharge for the bill or to enforce payment thereof against any party. Section 21 stipulates that no person is liable as drawer or endorser of a bill if he has not signed as such. Therefore, C will not be liable against X because he (C) did not endorse the cheque.

(iv) E

The delivery of the cheque to E does not constitute him (E) a holder because of s22, which states that a forged signature is wholly inoperative. The general principle provides that no one can become a holder of a cheque after a forged signature has been made on the cheque. E has no rights, which he can pass to X. However a person who endorses a cheque is precluded from denying to a holder in due course the authenticity and regularity in all respects of the drawer's signature and all previous endorsements (section 53(2)(b)). Because E has endorsed the cheque and delivered it to a holder he will be regarded as an "endorser by estoppel". X may be regarded as a "holder in due course by way of estoppel". Section 53(2)(b) neither makes E a true endorser nor X a true holder in due course, but they are regarded as such for purposes of section 53(2)(b). X will only be regarded as a holder in due course by

estoppel if he satisfies all the other requirements of a holder in due course but for the forged endorsement. E will be liable to X as endorser as provided in s 53(2) (b).

A draws a cheque on B Bank payable to "C or order". D steals the cheque from C, forges C's signature on the back of the cheque and delivers it to E. E indorses the cheque and delivers it to X, who takes it in good faith and for value.
Can X enforce payment against any of the parties? Explain fully.

The answer is as above, but not broken into subsections. The only person liable is a "previous endorser" – endorser by estoppel.

All the questions on this section are pretty much the same as above. The following type of question can also be asked:

i) A draws a bill on B payable to "C or order" and delivers it to C. D steals the bill from C, forges C's signature on the back of the bill and delivers it to E. E changes the forged "endorsement" to an endorsement in his (E's) name, signs the bill and delivers it to X, who takes it in good faith and for value. Can X sue any of the parties?

ii) Would you answer be any different if D stole one of the drawer A's cheques?

In (ii), the drawer's cheque was stolen and not the payee's cheque – see "Situation 2" above.

SECOND ELEMENT FOR LIABILITY:

DELIVERY:

Delivery is the **second** element that has to be fulfilled before a party can become liable on a cheque. Signature in itself is not sufficient. This is reiterated in s 19(1) which states that the "drawer's, acceptor's or an indorser's contract on a instrument becomes complete and irrevocable at the point in time when delivery of the instrument in question takes place." In other words, delivery is used to confirm their liability.

"Delivery" refers to the transfer of possession of the negotiable instrument. Such delivery can take the form of either:

- **"Actual delivery"** - the actual handing over of physical possession of the cheque with the intention of transferring possession thereof or
- **"Constructive delivery"** - includes situations where the cheque is already in the possession of the transferee who, after "delivery", now keeps it for himself or where the cheque is in the possession of a third party who, after "delivery", now holds it on behalf of the transferee.

FUNCTIONS OF DELIVERY:

Delivery of a cheque can fulfill three different functions (never all three):

1. **Constitutive function**: Delivery is required to complete the signature of the drawer of cheque.
2. **Transfer function**: delivery is required for the transfer of both bearer and order (to complete the indorsement) instruments.
3. **Guarantee function**: the drawer or endorser's undertaking to compensate any holder or subsequent indorser, who is compelled to pay if the instrument is dishonoured when presented for payment, becomes enforceable once the drawer or endorser has delivered the cheque to a new holder.

WHICH OF THESE FUNCTIONS ARE FULFILLED BY DELIVERY BY ONE OF THE FOLLOWING PARTIES?

- A drawer? Constitutive & Guarantee
- An endorser? Transfer & guarantee

PRESUMPTIONS OF DELIVERY:

The Act provides for two presumptions in relation to delivery:

1. If a cheque is no longer in the possession of a party who has signed it as a DRAWER OR INDORSER, a valid and unconditional delivery of the cheque is presumed until the contrary is proven.
   I.e. if the person in possession is a HOLDER there is a **rebuttable** presumption of valid and unconditional delivery. In other words we presume there was valid and unconditional delivery until evidence is lead showing it to be untrue.

   BUT:

2. As soon as the cheque comes into the hands of a HOLDER IN DUE COURSE, there is **an irrebuttable presumption** of valid and unconditional delivery. In other words valid and unconditional is said to have taken place despite any indication to the contrary.

TYPES OF QUESTIONS:

A draws a cheque on B Bank in favour of X. A places the cheque in his desk draw with the intention of using the cheque to pay X for certain repairs X is to make to A's car the following day. The following day, X finds the cheque and takes it without repairing A's car. A, upon discovering the loss of the cheque, stops payment thereof. When X presents the cheque for payment, it is dishonoured. X thereafter sues A for the amount of the cheque.

a) Is X a holder or a holder in due course? What is the effect of the presumption of delivery?

X is the payee of an order cheque and is thus merely a holder. The presumption of valid and unconditional delivery is rebuttable and thus when X sues A for payment of the cheque, A can rebut the presumption of valid and unconditional delivery and could succeed in his defence as no delivery took place (one is liable only upon delivery).

b) Assume that X had transferred the cheque to C who took it in good faith and for value. Is C a holder or a holder in due course? What is the effect of/he presumption of delivery?

C is now a holder in due course, as the cheque was negotiated to C (endorsed by X and delivered to C by X) plus X took the cheque in good faith and for value/consideration. Thus the presumption of valid and unconditional delivery is irrebuttable and A will have to pay C.

A draws a cheque on B Bank in favour of C or order and delivers it to C. C indorses the cheque specially to D, with a view of paying D the next day for performance which D has to render in terms of an agreement between them. D however, does not perform but finds the cheque on the desk in C's office and take it. D indorses the cheque and delivers it to X who takes it in good faith and for value. C discovers that the cheque is missing and arranges with A to countermand payment. When X presents the cheque for payment, B Bank refuses to honour it. Discuss the rights of X fully.

Delivery of a bill is a prerequisite of liability (s19 (1)). Delivery is also a requirement for the completion of negotiation of an order bill (s29 (3)). A valid and unconditional delivery of a bill is presumed in favour of a holder until the contrary is proved (s19 (4)). If a bill has come into the hands of a holder in due course, an irrebuttable presumption that there was a valid delivery of the bill by all parties prior to him exists (s19(3)). Non delivery of a bill is a relative defence that cannot be raised against a holder in due course.
If X meets all the requirements of holdership in due course (which he may, since he took the cheque in good faith and for value C will be liable to him as indorser, and he (C) will not be able to raise the defence of non delivery against him. A bank's duty and authority terminates when payment is countermanded. B Bank was accordingly obliged to refuse to honour the cheque. However A as a drawer will be liable to X. D will also be liable to X, as an indorser. If X, for some reason, does not qualify as a holder in due course, which means that he will just be an ordinary holder, it can be proved against him that the cheque was not validly delivered to his predecessor, D, and he will not be successful in his claim.

ISSUE:

- The term "issue" refers to the first delivery of a bill, complete in form, to a person who takes it as a holder.
- Issue is the first delivery, i.e. the delivery by the drawer to the payee (NB DEFINITION!)
- "Complete in form" means that all the essential elements of form are met so that the instrument is valid. An incomplete cheque can never be issued.
- The person taking the cheque must qualify as a holder thereof

REMEMBER!!!!!!!

- THE PAYEE OF A BEARER INSTRUMENT CAN QUALIFY AS A HOLDER IN DUE COURSE
- THE PAYEE OF AN ORDER CHEQUE CAN NEVER QUALIFY AS A HOLDER IN DUE COURSE.

TRANSFER V NEGOTIATION:

NB DEFINITIONS!!!
The Act is not consistent with the use of the words "transfer" and "negotiate". The terms should have the following meanings:

- "**Transfer**" - refers to transfer of possession or title to a cheque to a transferee (called negotiation in terms of the Act)
- "**Negotiate**" - refers to transfer of possession or title to a cheque to a transferee who qua dies as a holder in due course (called negotiation in terms of common law). When one can negotiate: the payee or bearer to whom an instrument has been issued, if he wants to, can negotiate the instrument, unless words appear on the instrument prohibiting its transfer – like s6 (5) which makes the instrument not transferable by stating "To C only" or by adding the words NOT TRANSFERABLE across the face of the instrument. A **crossed cheque marked "not negotiable**" MAY be negotiated in the sense that it can be transferred to a person to take it as a holder. BUT if the cheque is **uncrossed** and the words "**not negotiable**" appear on the face of the cheque, and the cheque is payable to a specific person, it is **not transferable**.
- Eg. A draws a cheque on B Bank in favour of C. The cheque is crossed and marked "not negotiable". C can still "negotiate" the cheque to D, thus endorse and deliver it to D, and D can take it in good faith and for value, BUT D cannot become a HIDC as the cheque was crossed and marked "not negotiable". BUT if A draws a cheque on B Bank in favour of C and the cheque is uncrossed and marked "not negotiable", C may not transfer the cheque further to D. The cheque is not transferable.

ENDORSEMENT:

- A bearer instrument is transferred by mere delivery.
- An order instrument is transferred by endorsement plus delivery.
- The Act sets out various requirements for a valid endorsement.

1. The endorsement must be written on the cheque itself.
2. It must consist of the signature of the endorser, with or without additional words.
3. The endorsement must be for the entire amount payable.
4. If the cheque is payable to the order of two or more payees, who are not partners, all of them must indorse the cheque unless the one indorsing the cheque has the authority to do so on behalf of the others.
5. If the payee or endorsee's name is spelt wrong, he must indorse the cheque so wrongly indicated or designated and add his proper signature.
6. An endorsement is a signature made with the intention to indorse, i.e. the intention to transfer the rights thereon.

There are four types of endorsements:

1. **An endorsement in BLANK**: Has the endorser's signature (e.g. J Jones) and it changes the order to a bearer cheque

2. **A SPECIAL endorsement**: endorser's signature coupled with a direction to pay a specific person (e.g. pay X, signed J Jones). This ensures that an order cheque remains an order cheque.

3. **A RESTRICTIVE endorsement**: Either:

   (a) Endorser's signature coupled with a direction to pay a specific person only (e.g. pay X only, signed J. Jones). Then the order cheque becomes a non-transferable cheque OR

   (b) Endorser's signature couples with an indication of the specific powers which the indorsee is to have in relation to the cheque. (e.g. pay X for collection, signed J. Jones). The endorsee is given the power to deal with the cheque as indicated, but not to transfer it (unless otherwise indicated in which instance it is always subject to equities).

4. **A CONDITIONAL endorsement**: the rights to the instrument are transferred subject to the fulfillment of an uncertain future event

(not the order - see essential elements). The condition is only operative as between the endorser and endorsee. I.e. payment by the drawee is not conditional.

- An order cheque **can** be converted into a bearer cheque through a blank endorsement. A bearer cheque **CANNOT** be converted into an order cheque through a blank endorsement, such endorsement being redundant.

- An order cheque, which has been converted into a bearer cheque through a blank endorsement can, however, be converted back to an order cheque by converting the blank endorsement into a special indorsement. A blank endorsement is converted into a special endorsement by the holder writing above the endorsement in blank a direction to pay:

1. ***HIMSELF***:

   E.g. A draws a cheque on B Bank in favour of C or order. C indorses the cheque in blank (merely signs the cheque) and delivers it to D. D is now in possession of a bearer instrument. D, as holder, can convert C's blank endorsement into a special endorsement by writing a direction to pay himself above C's signature (it now reads "Pay D, signed C"), Should D now wish to transfer the cheque further to E, he would have to indorse and deliver it (D thereby incurring liability),

2. ***ANOTHER PERSON***:

   E.g. D, as holder, can also convert C's blank endorsement into a special endorsement by writing a direction to pay someone else - namely the person to whom he wishes to transfer the cheque, E - above C's signature (i.e. now it reads "Pay E, signed C"), D has successfully transferred the cheque to E without his signature appearing thereon, (incurs no liability on the cheque).

The Act contains various other provisions regarding endorsements, including:

- If there are two or more endorsements on a bill, a rebuttable presumption exists that the endorsements were made in the order in which they appear on the instrument.
- Where any person is under an obligation to indorse in a representative capacity, he may indorse the bill in such terms as to negate personal liability (i.e. add words indicating he is signing in such representative capacity like "p.p" etc, the Amendment Act s24 amended this (see representative signatures above).
- Endorsement is not invalid simply because it is not dated.

POSSIBLE QUESTIONS:

Identify the different types of endorsements used in the following examples:

a. Pay Natania Lock only

(signed) Michelle
Kelly

(i) Restrictive endorsement

(ii) (signed) Michelle

Kelly

(ii) Endorsement in

blank

A draws a cheque payable to B or order, but his name is misspelt. B wants to negotiate the cheque. What must B do?

A payee or indorse whose name is misspelt on a bill payable to order, if he wishes to negotiate the bill, must indorse the bill as he is described in the bill, and add his proper signature.

ACCEPTANCE:

- The mere fact that the drawee is named on the instrument does not mean that he is liable thereon. In the absence of any previous contractual undertaking between the drawee and the drawer, the drawee is not obliged to accept the bill, and if he chooses not to, he is not liable,

- DEFINITION: By accepting, the drawee signifies his assent to the order of the drawer; the drawee undergoes a change in capacity, and is now called the ACCEPTOR. A contract arises between the acceptor and drawer in terms of which the acceptor becomes the ultimate debtor.

When is acceptance necessary?

The acceptance of a bill is not a requirement for its validity, and many bills are created and discharged without ever being accepted. There are only 3 instances that require the holder to present the bill for acceptance – s37:

- where the bill is payable after sight and presentment s necessary to fix the due date.
- where the bill expressly stipulates that it shall be presented for acceptance.
- where the bill is payable at a place other than the place of business or residence of the drawee.

Who accepts and when?

A bill may be accepted at any moment in its lifetime by the drawee or his authorised representative (although the holder is not obliged to take acceptance from a person other than the drawee). Time for acceptance:

- before it has been signed by the drawer
- while it is otherwise incomplete
- when it is overdue
- after it has already been dishonoured by non-acceptance or non-payment

Form and nature of acceptance:

- Acceptance must be written on the bill itself and signed by the drawee, or his agent, in order to be valid.
- The mere signature of the drawee without any additional words is sufficient to constitute acceptance.
- The acceptance is usually written across the face of the bill, but it need not be written in a particular place on the bill
- Acceptance is invalid if it stipulates that the drawee will perform his promise by means other than the payment of money.

Discharge of a bill:

- The instrument is discharged as soon as the acceptor or drawee has effected payment in due course.
- After discharge, the debt on the bill is extinguished, together with all the contracts on the bill.
- The instrument is no longer negotiable and no recipient can become a holder in due course thereof.
- A draws a bill on B in favour of C or order. B accepts the bill. C negotiates the bill to D, D negotiates it to E and E to F. C, D, and E endorsed the bill. F, as the holder, presents the bill for payment on the due date, and B pays in due course. The bill is discharged by payment and not only B, but also drawer A and endorsers C, D and E are released thereby. All the contracts on the bill are discharged, not only the acceptor's contract on the bill, but also those of the drawer and endorsers.
- Suppose B in the example above refuses to pay F on the due date, after F has duly presented the bill for payment, that is, B dishonours the bill by non-payment. Now F must give due notice of dishonour to the drawer, A, and all previous endorsers, that is C, D and E. After this, F may sue any of the previous endorsers or the drawer for payment. Suppose F sues D for payment and D pays. Now D may sue A, B, or C for payment. However, D may not sue E, since E is a "subsequent endorser" as far as D is concerned (s 55(1)). Suppose D sues the drawer, A, and A pays. Now A may sue B only. As long as B refuses payment, the bill is not discharged.

Methods of discharge

A bill may be discharged in various ways.

1. Discharge by payment in due course
   - Payment in due course protects the acceptor in that it discharges the bill and extinguishes the rights of the owner against him (the acceptor).
   - The acceptor may therefore rely on the appearance of legitimacy created by the possession of the instrument. As a rule, negotiable instruments are discharged in this way, that is, by payment in due course by the drawee or acceptor.
   - Section 57(1) provides that a bill is discharged by payment in due course if such payment is made by or on behalf of the drawee or acceptor.
   - Not any payment, but only payment in due course will have this effect. A payment in due course in terms of s 1 entails "payment made at or after the maturity of a bill to the holder thereof in good faith and, if his title to the bill is defective, without notice thereof".

2. Discharge by way of waiver

- At its maturity, the holder of a bill may waive (renounce) his rights against the acceptor wholly and unconditionally (s 60(1)). The renunciation (waiver) must be in writing on the bill, unless the bill is delivered up to the acceptor (s 60(2)).
- According to s 60(3), the holder may also waive the liabilities of any party to the bill at or after its maturity. In terms of s 60(4), this s (s 60) will not affect the rights of the holder in due course who had no knowledge of the renunciation or waiver.

3. Discharge by cancellation of the bill
   - In terms of s 61, a bill may also be discharged if the holder intentionally cancels the bill and the cancellation is apparent on it. The usual manner of cancellation is by drawing a line through the bill, or striking out a signature, or tearing up or cutting up the instrument.

4. Novation
   - Novation occurs when an existing obligation is replaced with a new one, thereby extinguishing the old one. A novation is effected by agreement. If the parties intend to replace the old obligation with a new one, a novation takes place, but not where they lack this intention.

5. Set-off or compensation
   - This is a method by which contractual or other debts are extinguished. It operates when two parties are mutually indebted to each other and both the debts are due.
   - Set-off is made by the operation of law, and it is unnecessary for either party to invoke it. Set-off has the same consequences as payment. A bill is thus only discharged if debts of the acceptor and holder are set off against each other. If set-off is to occur between the holder and any other party, this other party will be discharged but not the instrument itself.

POSSIBLE QUESTIONS:

1. Name the methods of discharge.
2. Name 5 ways in which a bill may be discharged.
3. Define “acceptance”.

CHEQUES:

A cheque has two special characteristics:

1. It is drawn on a banker
2. It is payable on demand

THE BANKER-CUSTOMER RELATIONSHIP:

The two parties to the banker-customer relationship are:

- The banker - the drawee bank
- The customer - the current account holder i.e. the drawer of the cheque.

The banker-customer relationship is generally a combination of three main forms of contract:

- **Debtor-creditor**: if there is a credit balance on the account, the bank is the debtor and the customer the creditor.
- **Mutuum (contract of loan for consumption)**: the bank becomes the owner of all money deposited, subject to the obligation to repay an equivalent amount on demand.
- **Mundatum (contract of mandate)**: the bank (the mandatory) renders services to customer (mandator) without placing itself under the customer's authority i.e. follows all customers' instructions but does not account to customer in relation to the utilisation of deposits.

PAYMENT IN DUE COURSE:

The following requirements must be met for payment in due course:

1. There must be payment.
2. It must be made in good faith.
3. It must be made on or after the due date.
4. It must be made to a holder of a bill (and not a mere possessor).
5. It must be made by or on behalf of the drawee.
6. It must be made without notice of any possible defect in the holder's title to the bill.

There are 3 important **exceptions** to the requirement that payment in due course may be made only to a holder in order to discharge the obligations thereon. The exceptions listed below relate **ONLY** to cheques:

1. Forged indorsements (s58)

2. Crossed cheques paid to another bank (s79)
3. Absence or irregularity of indorsements (s83)

MARKINGS ON A CHEQUE:

The drawer, or certain other specified parties, may make markings on a cheque. These markings qualify the drawer's payment instruction to the drawee bank and may also affect the legal position of holders of a cheque:

There are various markings, which can be placed upon a cheque:

- General and special crossings.
- The effect of the words "not negotiable".
- The effect of the words "not transferable".
- The effect of the words "account payee only".

General crossings:

I. 2 parallel transverse lines.
2. 2 parallel transverse lines "& company" between the lines
3. 2 parallel transverse lines with "not negotiable" between the lines.
4. 2 parallel transverse lines "and co. and not negotiable" between the lines.

EFFECT:

- Drawee must make payment to another bank.
- Thus, it may **not make payment over the counter.**
- Holder deposits cheque into his own account.
- Holder's bank (collecting bank) presents it for payment at drawee bank.
- Drawee bank debits drawer's account.
- Collecting bank credits holder’s account.

Special crossings:

Has the name of the banker, with or without "not negotiable", NB parallel lines are unnecessary, can combine with general crossing. Special crossings are rare.

EFFECT:

- Drawee must make payment to the specific bank named, thus it may not make payment over the counter.
- Holder deposits cheque into account at the specific bank, the specific bank (collecting bank) presents it at the drawee bank.

- Drawee bank debits drawer's account collecting bank credits holder's account.

AMENDMENT TO THE CROSSING OF A CHEQUE REGARDING THE WORDS "AND COMPANY":

- S75 of the Bill of Exchange Amendment Act 56 of 2000 now prohibits the words "and company" or an abbreviation thereof between two parallel transverse lines.
- The Act does not provide for the consequences should a cheque be crossed in such a way. The consequence of such a crossing is that the words "and company" would simply be pro non scripto.
- S75 (2) provides strangely enough that the words "and company" are acceptable in a special crossing.

WHAT IF THE BANK IGNORES THE CROSSING?

If the drawee bank does NOT pay the cheque IN ACCORDANCE with the crossing (thus, it pays cash over the counter), it has disobeyed the drawer's payment instructions and so MAY **NOT DEBIT** THE DRAWER'S ACCOUNT with the amount of the cheque, UNLESS payment has actually been made to the PERSON ENTITLED TO PAYMENT or his agent.

e.g. A draws and issues a generally crossed cheque on B in favour of C or order. The cheque is stolen from C by X, who forges C's indorsement, and delivers it to D, who takes the cheque in good faith and value. D presents the cheque for payment at B Bank and is paid cash over the counter.

What is the result?

The bank may therefore NOT debit drawer's account.

What if C had presented the cheque for payment and received cash over the counter?

Yes, because he was therefore entitled to it.

WHO CAN CROSS A CHEQUE AND WHEN CAN IT BE CROSSED?

Any of the following persons may cross a cheque:

1. The **drawer** can cross the cheque (generally or specially) when he draws the cheque and delete the crossing at any time prior to delivery to the payee (only party who can delete the crossing).

2. Any **holder** may add or alter the crossing (change a general to a special crossing or cross an uncrossed cheque).
3. A **bank** who receives an uncrossed or generally crossed cheque for collection can add a special crossing naming itself.
4. The **bank named in a special crossing** may add a second special crossing to the cheque. This is called a "special crossing for collection" – the bank named in the first special crossing names the bank in the second crossing to collect the cheque on behalf of the first bank.

- A cheque can be crossed at any time before it is discharged through payment in due course.

- A crossing is a material part of a cheque and may not be cancelled, changed or added to except as set out above. If a crossing is tampered with in any other way, this is considered a material alteration (see absolute defences).

THE EFFECT OF ADDING THE WORDS "NOT NEGOTIABLE":

- Crossing a cheque itself does not affect its negotiability or transferability. In principle a crossed cheque may still be freely transferred and it is possible for its holder to become a holder in due course.
  The cheque is no longer negotiable but remains transferable. S80 of the Act states that a person who takes a crossed cheque marked "not negotiable" cannot get a better title to it than the title of the person from whom he took it. I.e. any holder of such a cheque takes it subject to equities and cannot qualify as a holder in due course.
  A CROSSED CHEQUE MARKED NN IS FULLY TRANSFERRABLE BUT AN UNCROSSED CHEQUE MARKED NN IS NOT TRANSFERREBLE!!!

  Example:

  A draws a cheque on B Bank in favour of C. The cheque is crossed and marked "not negotiable". The cheque is in payment of a gambling debt. C transfers the cheque to D who takes it in good faith and for value.

  Does D quality as a holder in due course?

  No, even though he takes it in good faith and for value, and even though C endorsed it and delivered it to D, the cheque is crossed and marked "not negotiable" which prevents anyone to whom the payee transfers the cheque from being a HIDC

  Can he sue A for payment of the cheque?

  A will have defences – namely the fact that the initial contract between A and C was tainted.

2. Section 81 of the Act comes into play to protect the right of the true owner of a lost cheque, which has been crossed and marked in this way (see later).

NON-TRANSFERABLE CHEQUES NBNBNBNBNB!!!!!!!!:

Traditional non-transferable cheques:

- Section 6(5) provides that if a bill contains words prohibiting transfer or indicating an intention that it should not be transferable, it is valid between the parties to the bill but is not negotiable. Example is "Pay C only" – thus only the named payee can be the holder thereof and he is not allowed to negotiate it or transfer it, if he tries to do so, the person receiving it will not be a holder.

Section 75A (2):

- S75A(1) provides that where a cheque bears boldly across its face the words "not transferable" either with or without the word "only" after the payee's name, the cheque will not be transferable, but will be valid between the parties to it.
- Section 75A (1) also provides that such a cheque will be deemed to be crossed generally, unless it is crossed specially.
- Furthermore, the words "non-transferable" may not be cancelled and any purported cancellation will be of no effect.
- Such a cheque contains words indicating an intention to prohibit transfer, and as such, cannot be transferred in such a manner as to constitute the transferee to become the holder of it.
- Such a cheque can also not be negotiated.
- Thus, there are two categories of not transferable cheques – s6(5) traditional and s75A. Make sure you know the difference between them and are able to apply them to questions.
- Even in the case where a cheque has the words "not transferable" written across its face and these words were not written boldly, such a cheque should nevertheless be considered as a cheque that cannot be transferable because it contains words indicating an intention to prohibit transfer thereof.
- S75A(2)(b) provides that a bank will not be negligent "by reason only" of its "failure to concern" itself with words or an intention which prohibits its transfer other than in the manner provided for in s75A.

CHEQUES MARKED "ACCOUNT PAYEE ONLY" NBNBNBNB:

It has become standard practice in certain circles to add the words "account payee only" or "account payee" to crossings on cheques. The effect of such markings was unclear in the past because the Act does not provide for such.

In Dungarvin Trust (Pty) Ltd v Import Refrigeration Co (Pty) Ltd 1971 (4) SA 300 (W) the court held that these words conveyed a clear intention that the cheque may not be transferred to a third party (made the cheque not transferable).

In the subsequent case of Standard Bank of SA v Sham Magazine Centre 1977 (1) SA 484 (A) the Supreme court of Appeal had to decide whether the words "a/c payee only" exclude the transferability of the cheque. Thus the question before the court was whether the words "a/c payee only" prohibited the transfer of the cheque.

To decide this the court had to interpret s6 (5) of the Act and the words "a/c payee only". The court made it clear that such markings do not affect the transferability of a cheque, thus it remains freely transferable and can even be negotiated. The court also said that the words "not negotiable" used in conjunction with the words "a/c payee only" DO NOT exclude the transferability of the cheque. The words "a/c payee only" are only an indication that the cheque must be collected for a specific payee.

POSSIBLE QUESTIONS:

In *Standard Bank of South Africa Limited v Sham Magazine Centre* 1977 (1) SA 484 (A) the Appellate Division came to the conclusion that the *Dungarvin* case does not correctly reflect the law and that the words "a/c payee only" do not exclude transferability of the cheque. Discuss this decision.

It has become standard practice in certain circles to add the words "account payee only" or "account payee" to crossings on cheques. The effect of such markings was unclear in the past because the Act does not provide for such.
In Dungarvin Trust (Pty) Ltd v Import Refrigeration Co (Pty) Ltd 1971 (4) SA 300 (W) the court held that these words conveyed a clear intention that the cheque may not be transferred to a third party (made the cheque not transferable).
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the cheque. To decide this the court had to interpret s6 (5) of the Act and the words "a/c payee only". The court made it clear that such markings do not affect the transferability of a cheque, thus it remains freely transferable and can even be negotiated. The court also said that the words "not negotiable" used in conjunction with the words "a/c payee only" DO NOT exclude the transferability of the cheque. The words "a/c payee only" are only an indication that the cheque must be collected for a specific payee

The Bills of Exchange Amendment Act 56 of 2000, which came into operation on 1 March 2001, amended, among others, the position regarding cheques marked "not transferable" and cheques payable to "payee only". Explain these amendments by discussing the following in full:

The meaning of the words "not transferable" on a cheque.

Section 75A(1) provides that where a cheque bears boldly cross its face the words "not transferable" either with or without the word "only" after the payee's name, the cheque will not be transferable, but will be valid between the parties to it. Section 75A (1) also provides that such a cheque will be deemed to be crossed generally, unless it is crossed specially. Furthermore, the words "not transferable" may not be cancelled and any purported cancellation will be of no effect. Section 75A (2) (b) provides that a bank will not be negligent "by reason only" of its "failure to concern" itself with words or an intention which prohibits its transfer other than in the manner provided for in section 75A. It is unclear what is meant by the words "concern" and "by reason only". He submits that this section must be interpreted to mean that a bank will be negligent where it collected payment of such a cheque on behalf of anyone other than the named payee of the cheque.

Discuss the two different kinds of "not transferable" cheques.

Section 75A is only applicable to certain types of not transferable cheques and other types of cheques may exist that will also be not transferable. This will be, for example, in the case where a cheque is payable to "payee only" "Pay C only". Such a cheque contain words indicating an intention to prohibit transfer, and as such, can not be transferred in such a manner as to constitute the transferee to become the holder of it (section 6(5)). Since an *inter paries* cheque cannot in truth be an order or bearer cheque as provided by the definition of a holder, a transferee will never be the indorsee in possession of an order cheque or the bearer thereof. Such a cheque can also not be negotiated. Thus, there are two categories of not transferable cheques. Even in the case where a cheque has the words "not transferable" written across its face and these words were not written boldly, such a cheque should nevertheless be

considered as a cheque that cannot transferable because it contains words indicating an intention to prohibit transfer thereof.

With reference to the following scenarios, explain fully whether the cheque in each case is transferable or not:

a) A draws a cheque on B Bank in favour of C or order. The cheque is uncrossed and marked "not negotiable".

   This cheque is NOT transferrable because the cheque is not crossed. Only a crossed cheque marked "NN" is transferrable. This cheque, NN with no crossing, is not transferrable but one may receive cash over the counter.

b) A draws a cheque on B Bank in favour of C or order. The cheque is crossed and marked "not negotiable".

   This cheque is transferrable, but the parties receiving the cheque may not become HIDC's as the negotiability has been removed by adding NN into a crossing. No cash over the counter.

c) A draws a cheque on B Bank in favour of C or order. The cheque is crossed and marked "not negotiable – account payee only".

   Crossed cheque = no cash – need a collecting bank. The NN inside the crossing means the cheque is fully transferrable but not negotiable – thus no HIDC. The "a/c payee only" according to Dungarven means NOT transferrable but the Sham case (latest SCA case) said this words "a/c payee only" don't mean anything – thus this cheque is fully transferrable.

PROTECTION OF THE DRAWEE BANK:

WHY DO WE EXTEND SUCH PROTECTION?

- As we have seen, the most frequently encountered method of discharge of a cheque is "**payment in due course**". One of the requirements for payment in due course is that payment must be made to **a holder** of the cheque.
- The general rule is therefore if the drawee bank fails to make payment to the holder of the cheque, the cheque is not discharged and the drawee bank is not entitled to debit the drawer's account.
- If however, this principle is strictly applied, the results may prove to be very unfair on the drawee bank for 2 reasons.

1. One cannot expect the drawee bank to authenticate the validity of every signature on every cheque.

   Example:

   A draws a cheque on B Bank in favour of C; X steals the cheque from C and forges C's indorsement thereon. X then transfers the cheque to D who takes it in good faith and for value. D presents the cheque for payment at B Bank. B Bank pays D.

   D is not the holder of the cheque. B Bank has, therefore not made payment in due course and should not be able to debit A's account with the amount of the cheque.
   BUT how can we expect B Bank to be able to identify the forgery of C's signature.

1. Cheques are generally not presented for payment sent to the drawee bank by the holder or purported holder himself. The holder or purported holder usually deposits the cheque in his account at his bank, and the collecting bank then presents the cheque on behalf of the depositor, to the drawee bank for payment.

   As a result, the drawee bank generally has an idea on whose behalf the collecting bank is presenting the cheque for payment. Surely in such circumstances it would be unfair to penalise the drawee bank for not paying the holder of the cheque, unless the dangers were clearly apparent from the cheque itself?

Example:

A draws a cheque on B Bank in favour of C. X steals the cheque from C and forges C's endorsement thereon. X thereafter deposits the cheque into his bank account at Z Bank and Z Bank collects payment, on X's behalf from B Bank.

X is not the holder of the cheque. B Bank has therefore not made payment in due course, and should be unable to debit A's account with the amount of the cheque. BUT how can we expect B Bank to have known that Z Bank was collecting on behalf of a depositor who was not the holder of the cheque in the absence of indications on the cheque itself?

To address the extreme burden that a strict application of the rule would place on the drawee banks, the Act extends protection to the drawee bank in three instances:

1. **Section 58** that provides protection in the case of forged or unauthorised indorsements on order cheques.
2. **Section 79** that provides protection in the case of crossed cheques paid to a collecting banker.
3. **Section 83** that provides protection in the case of the absence of an indorsement or the presence of an irregular indorsement on a cheque.

In all three instances, the drawee bank is **deemed to have made payment in due course** (to have paid the holder). As result, the drawee bank is **entitled to debit the account of the drawer.**

SECTION 58:

The drawee bank will be DEEMED to made payment in due course (even though a holder was not paid) if the following requirements are met:

- The cheque is an order cheque (NOT a bearer or non-transferable cheque).
- The cheque may be crossed or uncrossed.
- There is a forged or unauthorized indorsement on the cheque (i.e. the person presenting the cheque for payment is purporting to have acquired his right to payment through a forged or unauthorized indorsement.
- The drawee bank has paid the cheque in good faith (honestly even if negligently).
- The drawee bank has paid the cheque in the ordinary course of business (thus, there is nothing unusual about the manner in which the cheque was presented for payment and paid.)

If S58 APPLIES (THUS, ALL THE REQUIRMENTS ARE MET):

- The drawee bank is deemed to have made payment in due course and will be entitled to debit the drawer's account.
- The "true owner" of the cheque will bear the loss (i.e. the person who is entitled to possession of the cheque, who has lost such possession through theft or loss).

Example:

A draws a cheque on B Bank in favour of C. X steals the cheque from C and forges C's indorsement. X then presents the cheque for payment at B Bank, and B Bank pays X in good faith and in the ordinary course of business.

ARE ALL THE REQUIREMENTS MET?

- It is an order cheque.
- It is uncrossed.
- X is pretending to be the indorsee (purporting to have acquired his right to payment through C's forged indorsement.)
- B Bank has paid in good faith.
- B Bank has paid in the ordinary course of business.

S58 therefore applies:

- B Bank is deemed to have made payment in due course, thus it can debit A's account.

- C is the true owner. A will not have to draw another cheque in favour of C because he has already delivered the cheque to C; he has discharged his obligation to pay C. C has therefore not been paid, and therefore bears the loss.

IF S58 DOES NOT APPLY?

- The drawee bank has not made payment in due course, and will therefore not be entitled to debit the drawer's account, i.e. the drawee bank bears the loss.

Example:

A draws a cheque on B Bank in favour of C. X steals the cheque from C. X then presents the cheque for payment over the counter at B Bank, pretending to be C. The teller asks X to sign the back of the cheque, X forges Cs signature on the cheque, and receives payment from B Bank, who pays in good faith and in the ordinary course of business.

ARE ALL THE REQUIREMENTS MET?

- It is an order cheque.
- It is uncrossed.
- X is pretending to be the payee and not the indorsee. The signature placed on the back of the cheque by X is not indorsement - it is not placed on the cheque for the purposes of transferring the cheque, it is for the purposes of IDENTIFICATION AND RECEIPT (National Bank v Paterson & Stapelberg NO v Barclays Bank)

THE TEST:

- Indorsement - signature placed on the cheque before it was presented for payment.
- Identification/receipt — signature placed on the cheque in the presence of the teller.

- **S58 therefore, does NOT apply:**

- B Bank has not made payment in due course, and may therefore not, strictly speaking, debit A's account.
- BUT because A has already delivered the cheque to C, A has discharged his liability and need not draw another cheque in favour of C. So that A does not receive a free discharge of his debt, B Bank will be able to debit A's account with the amount of the cheque.

- In addition, C may claim the amount of the cheque from B Bank. B Bank therefore bears the loss.

S58 PROVISO:

- S58 will not protect the drawee bank (even if the requirements are met) if the forged or unauthorized endorsement is not an endorsement of a person who is a customer of the same branch of the same bank on which the cheque is drawn (i.e. the drawee hank). This is so because banks are suppose to know the signatures of their customers.

Example:

A draws a cheque on B Bank (Sandton branch of ABSA) in favour of C. X steals the cheque from C and forges C's indorsement. X presents the cheque for payment at B Bank. B Bank pays X in good faith and in the ordinary course of business, C is also a customer of B Bank (Sandton branch of ABSA).

ARE THE REQUIREMENTS MET?

- It is an order cheque.
- It is uncrossed.
- X is pretending to be the indorsee (purporting to have acquired his right to payment through C's forged indorsement).
- B Bank has paid in good faith.
- B Bank has paid in the ordinary course of business.

BUT!

C (whose signature is forged) is a customer of the drawee bank. B Bank should therefore, have been able to identify the forgery and not paid the cheque. B Bank is therefore not protected by S58, and will bear the loss.

If C had been a customer of the East Rand branch of ABSA s58 would have applied. The person whose signature was forged must be a customer of the SAME BRANCH OF THE SAME BANK as the bank on which the cheque is drawn.

POSSIBLE QUESTIONS:

A draws a cheque on B Bank in favour of "C or order". X steals the cheque from C. At the bank X professes to be the payee C and, in the presence of the teller, forges C's signature on the back of the cheque. Will B Bank be protected if B Bank pays X? Give reasons in your answer and refer to case law where necessary. (3)

Such a signature, in the presence of the teller, by X, is a signature for identification purposes. X is not indorsing the cheque S58 will not apply here as it only protects the drawee bank if the forged signature purports to be an endorsement. Thus the bank will bear the loss.

Name and briefly discuss the requirements that must all be present simultaneously before a drawee bank will be protected in terms of section 58 of the Bills of Exchange Act. (6)

The requirements for section 58 are as follows:

The cheque must be made payable to order. This also implies that it must be transferable.
The cheque can either be crossed or uncrossed, as section 58 applies to both.
There must be a forged or unauthorised endorsement on the cheque – the person presenting the cheque for payment must be pretending to be the endorsee.
The bank must pay the cheque in good faith, and in the ordinary course of business.

In Stapelberg NO v Barclays Bank (DC) 1963 (3) SA 120 (T) the court stated that the purpose of section 58 of the Bills of Exchange Act is to protect a bank against false and unauthorised endorsements. Not every signature on the back of a cheque is an endorsement in the true sense of the word. Where a thief, at the request of the bank, signs the name of the payee on the back of the cheque, that signature does not purport to be an endorsement in the lawful and technical sense of the word. However, where the thief signs the name of the payee on the back of the cheque without the notice and knowledge of the bank then that signature will constitute an endorsement in the lawful and technical sense of the word. Such a signature alters the cheque to a bearer cheque and the banker must deal with what appears to be a regular and genuine endorsement. Thus, if a bank pays out an order cheque in the ordinary course of business and in good faith, it is deemed to have paid the bill in due course. Provided that such indorsement does not purport to be that of a person who is a customer of the banker at the branch on which the said bill is drawn. The bank is deemed to have paid the cheque in due course.

Discuss the decision of the court in Stapelberg NO v Barclays Bank, with reference to section 58 of the Bills of Exchange Act.

In Stapelberg NO v Barclays Bank court stated that the purpose of section 58 of the Bills of Exchange Act is to protect a banker against false and unauthorized indorsements. Due to the nature thereof such an endorsement is not and cannot be an

indorsement in the lawful and technical sense of the word It can only profess to be one. Section 58 provides that if a bank pays out an order cheque in the ordinary course of business and in good faith, it is deemed to have paid the bill in due course.

This means that towards its customer, the drawee bank is deemed to have complied with its instructions in terms of the bank-customer relationship.

Section 58 thus qualifies the contractual relationship between bank and customer. Section 58 refers to the forged or unauthorized endorsement of the payee or subsequent endorsers and not to the forged or unauthorized signature of the drawer. Not every signature on the back of a cheque is an endorsement in the true sense of the word. If a payee, or person professing to be a payee, wishes to cash a cheque over the counter at the drawee bank, it is customary for the bank to require at person's signature on the back of the cheque that signature serves as identification and a receipt, and it is not placed on the cheque to effect a negotiation of the cheque to the drawee bank.

In the Stapelberg case the court discussed the purpose of signing a cheque where a thief, at the request of the banker, signs on the back of the cheque the name of the payee then the signature does not purport to be an endorsement in the lawful and technical sense of the word. However, where the thief signs the name of the payee on the back of the cheque without the notice and knowledge of the banker then that signature will constitute an endorsement in the lawful and technical sense of the word. Such a signature alters the cheque to a bearer cheque and the banker must deal with what appears to be a regular and genuine endorsement. Thus, if all the requirements of S 58 are complied with the drawee bank will be protected.

A draws an uncrossed cheque on B Bank in favour of C or order. X steals the cheque from C, forges C's signature on the back of the cheque and presents the cheque for payment at B Bank. X obtains payment from B Bank over the counter.
a) What protection will B Bank, in the abovementioned example, enjoy in respect of the forged endorsement?

In terms of s58 a drawee bank, such as B Bank, is deemed to have made payment in due course (i.e. deemed to have made payment to a holder, and thus allowed to debit its customer's account) if the following requirements are met:
1. The cheque is an order cheque (i.e. can be crossed or uncrossed, but cannot be non-transferable). In the case of a bearer cheque it is simple for banks to make payment in due course, the holder simply being any person in possession thereof. But in the case of order instruments, the situation is complicated by the possibility of forged endorsements, the

holder being the payee or endorsee in possession thereof. The cheque in question here is an uncrossed order cheque.
2. The party to whom payment has been made purported to have obtained their rights on the instrument through a forged endorsement (i.e. a signature placed on the cheque to effect negotiation thereof). In other words, the person to whom payment was made purported to be an endorsee - Stapelberg. On the facts, X purported to be an endorsee I e. to have obtained his rights on the instrument through C's endorsement which he forged.
The bank made payment to such person in good faith (i.e. honestly even if negligently). B Bank seems to have made payment in good faith i.e. didn't know or suspect X's defective title.
3. The bank made payment in the ordinary course of business. B Bank seems to have made payment in the ordinary course of business i.e. nothing unusual In the banking practices undertaken here.
4. In addition it seems that the proviso to s58 (i.e. a drawee bank will not enjoy such protection where the forged endorsement purports to be that of a customer of the same bank at the same branch, banks being taken to be able to identify the signatures of all their customers) does not apply here either.
Thus it seems as if B Bank is protected by s58 i.e. it is deemed to have made payment in good faith, and the results will be as follows:
B Bank will be entitled to debit its customer. A's account with the amount of the cheque.
Because A had delivered the cheque to C, in return for having, his account debited, A will get a discharge of his debt to C i.e. he needn't write out another cheque in C's favour.
C, the true owner of the cheque (i.e. the person who is entitled to be in possession, but who is not in possession because the cheque has been stolen or lost) will bear the loss (i.e. A no longer owes him the debt, but he has never been paid), unless he can trace X, the thief.

Would the position differ if X, at B Bank, professes to be the payee C and forged C's signature on the back of the cheque in the presence of the teller? Give reasons for your answer.

Where the payee, or a person professing to be the payee, wishes to cash a cheque over the counter at the bank concerned, it is customary for the bank to require that person's signature on the back of the cheque, such signature serving as an identification and a receipt signature, and not an endorsement. Thus, when he forges C's signature in the presence of the teller, he is not indorsing the instrument i.e. the signature is not placed on the cheque to effect a negotiation of the cheque to the drawee bank. The signature here is merely places on the cheque for the purposes of identification and receipt.
Thus s58 will not apply in this situation here because it only protects the drawee bank if the forged signature purports to be an

endorsement. Thus, the bank will bear the loss because A delivered the cheque to C he has discharged his debt to C, and need not write out another cheque to C; although s58 does not apply, the Bank is still entitled to debit A's account or else he will get a free discharge of his debt to C; and B Bank is also liable to pay C (the true owner) the amount of the cheque.

SECTION 79:

The drawee bank will be deemed to have made payment in due course (even though a holder was not paid) if the following requirements are met:

- The cheque is a CROSSED cheque.
- The drawee bank has paid the cheque in accordance with the crossing (i.e. to a collecting bather if the crossing is general or a specific collecting banker if the crossing is special).
- The drawee bank paid the cheque in good faith.
- The drawee bank paid the cheque without negligence.

In addition:

The drawer will be placed in the same position as if payment had been made in due course if the drawer had already delivered the cheque to the payee (i.e. the cheque was stolen from or lost by the payee of a subsequent party.)

IF S79 APPLIES (all the requirements are met):

- The drawee bank is deemed to have made payment in due course and will be entitled to debit the drawer's account.
- The true owner of the cheque will bear the loss.
    - If the drawer has already delivered the cheque to the payee at the time it was lost or stolen, the drawer is discharged (i.e. he need not draw another cheque in favour of the payee.)
    - If the cheque is stolen or lost before the drawer has delivered it to the payee, the drawer will not be protected (i.e. the drawer will have to draw another cheque in favour of the payee.)

Example:

A draws a crossed cheque on B bank in favour of C. X steals the cheque from C and forges C's indorsement. X then deposits the cheque into his account at Z Bank, and Z Bank presents the cheque for payment at B Bank, on X' s behalf. B Bank pays X in good faith and without negligence.

ARE ALL THE REQUIRMENTS MET?

- It is a crossed cheque
- It has been paid in accordance with the crossing
- It has been paid in good faith
- It has been paid without negligence

S79 therefore applies:

- B Bank is deemed to have made payment in due course, i.e. it can debit A's account.
- A has already delivered the cheque to C, and will, therefore, not have to draw another cheque in favour of C. A is placed in the same position as if payment had been made in due course, i.e. as if B Bank had paid C.
- C has therefore not been paid, and therefore bears the loss. C is the true owner.

Example:

A draws a crossed cheque on B Bank in favour of C. A posts the cheque to C without C's permission, X steals the cheque in the post and forges C's indorsement, X then deposits the cheque into his bank account at Z Bank, and Z Bank presents the cheque for payment at B Bank, on behalf of X. B Bank pays X in good faith and without negligence.

ARE ALL THE REQUIREMENTS MET?

- It is a crossed cheque.
- It has been paid in accordance with the crossing.
- It has been paid in good faith.
- It has been paid without negligence.

S79 therefore applies:

- B Bank is deemed to have made payment in due course, i.e. it can debit A's account.
- A has not delivered the cheque to C and will therefore not be protected by s79. Because A posted the cheque without C's permission, A remains the true owner of the cheque until C received it. A will, therefore have to draw another cheque in favour of C and will bear the loss.

CAN THE TRUE OWNER SUE ANYONE?

- The true owner may sue the thief or the forger in delict, because he has acted in bad faith, or on the basis of unjustified enrichment. But if the thief or forger will be difficult to trace, and even if he is found, the chances of him still being in possession of the money, or of him being able to pay damages are slim.
- The true owner nay, however, not hold the collecting banker or any party to whom the thief or forger transferred possession, provided, such parties acted in good faith, i.e. although the cheque has passed through their hands, they are not liable to the true owner. At common law, the owner of stolen property

has no action for damages against a bona fide possessor of his property.

THE TRUE OWNER IS THUS IN AN UNAPPEALING POSITION!!

IF S79 DOES NOT APPLY:

The drawee bank has not made payment in due course and is not, therefore, entitled to debit the drawer's account. The drawee bank, thus, bears the loss.

Example:

A draws a crossed cheque on B Bank in favour of C. X steals the cheque from C and forges C's indorsement. X presents the cheque for payment at B Bank. B Bank pays the cheque cash over the counter.

ARE ALL THE REQUIREMENTS MET?

- It is a crossed cheque.
- It has NOT been paid in accordance with the crossing – it has not been paid to another bank,

S79 therefore does NOT apply:

- B Bank has not made payment in due source and may, therefore, not debit A's account,

- BUT, because A has ready delivered the cheque to C, A has discharged his liability and need not draw another cheque in favour of C. So that A does not receive a free discharge of his debt, B Bank will be able to debit A's account with the amount of the cheque.

SECTION 58 AND 79:

1. S58 deals with crossed and uncrossed cheques.
   S79 deals with crossed cheques only.
2. S58 requires payment to be made in good faith and in the ordinary course of business.
   S79 requires payment to be made in good faith and without negligence (higher standard of care required by the drawee bank),
3. S58 does not apply when the person whose signature is forged or unauthorized is a customer of the same branch of the same bank as the bank on which the cheque is drawn.
   S79 has no such limitation on its application.
4. S58 protects the drawee bank
   S79 protects the drawee bank and the drawer in certain instances.

CONCLUSION:

Both s58 and s79 apply in the case of crossed cheques, s58 requiring a lesser degree of care on the part of the drawee bank than s79, but s79 offering greater protection than s58.

So when one is dealing with a question involving a crossed cheque:

- First see if s79 applies.
- If s79 does not apply (e.g. paid negligently), check if s58 applies.

CROSSING NON-TRANSFERABLE CHEQUES:

- The distinction between s58 and s79 helps explain the decision of commercial banks to only accept crossed non-transferable cheques for collection.
- In the case of non-transferable cheques, only the named payee may accept payment. If the drawee bank makes payment to the wrong person, it fails to execute its mandate correctly and may not debit the account of its customer with the amount of the cheque.
- But, as we have seen, when the cheque is presented for payment by a collecting banker, it is difficult for the drawee bank to establish whether the cheque is being collected for the correct person.

Don't s58 and s79 give the drawee bank protection??

If the cheque is uncrossed:

- S58 will not apply, because this section only applies to cheques that can be validly indorsed and not non-transferable cheques.
- S79 does not apply because it only applies to crossed cheques.

If the cheque is crossed:

- S58 will still not apply, because this section only applies to cheques which can be validly indorsed and not non-transferable cheques.
- S79 will apply provided the cheque is paid in accordance with the crossing, in good faith and without negligence.

This explains the decision of commercial banks to only accept crossed non-transferable cheques for collection,

POSSIBLE QUESTIONS:

Briefly discuss the differences between sections 58 and 79 of the Bills of Exchange Act 34 of 1964 with regard to the protection of the drawee bank. (6)

1. **S58 deals with crossed and uncrossed cheques. S79 deals with crossed cheques only.**

2. **S58 requires payment to be made in good faith and in the ordinary course of business.**
3. **S79 requires payment to be made in good faith and without negligence (higher standard of care required by the drawee bank),**
4. **S58 does not apply when the person whose signature is forged or unauthorized is a customer of the same branch of the same bank as the bank on which the cheque is drawn. S79 has no such limitation on its application.**
5. **S58 protects the drawee bank. S79 protects the drawee bank and the drawer in certain instances**

A draws a crossed cheque on B Bank in favour of C. A places the cheque in his desk drawer, with the intention of delivering the cheque to C the following day. X steals the cheque from A, forges C's indorsement and presents the cheque for payment at B Bank, B Bank pays the cheque cash over the counter.

This cheque is crossed and thus, we need to see a collecting bank – the cheque must be paid in accordance with the crossing, but the drawee bank paid cash over the counter. Thus, s79 does not protect the drawee bank as the 4 requirements have to be met: 1. The cheque must be crossed; 2. The cheque must be paid in accordance with the crossing; 3. The bank must pay in good faith and 4. The bank must pay without negligence. The bank paid X cash over the counter and NOT to a collecting bank, thus s79 will not protect them and they will be liable to C.

A draws a crossed cheque on B Bank in favour of C, A posts the cheque to C with C's agreement. The cheque is stolen in the post by X, X forges Cs indorsement and deposits the cheque in his account at Z Bank, Z Bank collects payment on behalf of X from B Bank, and B Bank pays the cheque in good faith and without negligence.

S79 will apply to this question – discuss as in the examples provided.

<u>SECTION 83:</u>

- S83 does away with the need to indorse cheques which are deposited in the payee's bank account, saving commercial banks time and labour. It covers two situations:

  1. If the drawee bank pays a cheque drawn on it in good faith and in the ordinary course of business to a collecting banker (i.e. depositor collects payment through a collecting banker).

Example:

A draws a cheque on B Bank in favour of C. C deposits the cheque into his account at Z Bank and B Bank pays Z Bank in good faith and in the ordinary course of business.

2. If the drawee bank pays a cheque drawn on it in good faith and in the ordinary course of business by crediting the depositor's account with the drawee bank (i.e. the depositor is a customer of drawee bank).

Example:

A draws a cheque on B Bank in favour of C. C is a client of B Bank and deposits the cheque without indorsing it into his account with B Bank. B Bank credits C's account in good faith and in the ordinary course of business.

…… the cheque is discharged and the drawee bank does not incur any liability merely because there is no indorsement on the cheque or the indorsement is irregular.

Example:

A draws a cheque on B Bank in favour of C. C negotiates the cheque to D. D deposits the cheque into his account at S Bank without indorsing the cheque. B Bank pays S Bank in good faith and in the ordinary course of business. Has B Bank discharged the cheque according to the provisions of s83).

Answer:

No, s83 does NOT apply.
The cheque cannot be said to have been paid in the ordinary course of business. As part of the "ordinary course of business" commercial banks in SA agree that if a cheque is negotiated and is not deposited in the payee's account and indorsement thereof is required:

- If the cheque has been specially indorsed, the payee's indorsement is sufficient.
- In all other instances, the indorsement of the payee and the depositor are required.

The rationale is probably to enable the collecting banker to identify whose account is to be debited should the cheque be dishonoured and returned.

S83 does not affect payment of a cheque over the counter by the drawee bank. Here, commercial banking practice still requires the payee's signature on the back of the cheque for the purposes of identification and receipt (i.e. is not an indorsement in the true sense of the word a no intention to transfer rights on the cheque

NOTE:

In terms of s84, if a party deposits an order cheque in one's account for collection, the collecting bank acquires the same rights as if the depositor had indorsed the cheque in blank, i.e. he becomes the holder. Normally the collecting bank has no need to become the holder. If the cheque is dishonoured, it merely returns the cheque to its client and debits his account.
The client must then take the necessary steps to obtain payment himself.

SECTION 81 – VERY NBNBNB!!

EXTENDING PROTECTION TO THE TRUE OWNER:

- As we have seen from the discussion of s79, when the requirements of s79 are met, the true owner bears the loss. In addition, the true owner is left in a rather unenviable position being unable to sue anyone other than the thief or forger himself, all other parties generally having acted in good faith.
- S81 seems to superficially improve the position of the true owner of a cheque, in the event of loss or theft, by giving him a right to sue any person who came into possession of the cheque after it was lost or stolen, regardless of whether such a person acted in good faith or in bad faith.

In order to qualify for the relief provided for in s81, the following requirements must be met:

- **The cheque must have been crossed and marked not negotiable.**
- **The cheque must have been lost or stolen whilst so marked.**
- **The drawee bank must have paid the cheque in accordance with the crossing to another bank (the drawee bank protected by s79.)**
- **The plaintiff must be the true owner of the cheque.**
- **The plaintiff must have suffered a loss as a result of the theft or loss.**
- **The defendant must have come into possession of the cheque after it was lost or stolen.**
- **The defendant must have given consideration for the cheque (a quid pro quo) or must have received it as a gift or donation.**

NOTE THE FOLLOWING POINTS:

- Every possessor of a cheque is deemed to have given consideration for it or to have taken it as a gift, until the contrary is proven.

- A collecting bank which receives payment of a crossed cheque marked not negotiable is not regarded as having given consideration for the cheque merely because it has:

* credited its customer's account-with the amount of the cheque before receiving payment thereof.
* it has applied such payment to reduce or settle any debit-owed by the customer to the bank.

- A collecting bank will be-considered to have given consideration for the cheque where it has:

- * paid cash over the counter for such a cheque, or
- allowed its customer to draw immediately against the cheque.

- A party (including the collecting banker) who fails or refuses to furnish any information in connection with the cheque at its disposal, to the true owner upon his request, is deemed to have been a possessor of the cheque and to have either given consideration for it or to have taken it as a gift (even if in fact they have not).

Example:

A draws a cheque on B Bank in favour of C. The cheque is crossed and marked "not negotiable". X steals the cheque from C, forges C's indorsement and deposits it into his bank account at Z Bank. Z Bank collects payment from B Bank on behalf of X. B Bank pays in good faith and without negligence.

ARE THE REQUIREMENTS MET?

- The cheque is crossed and marked "not negotiable"
- It was marked in such a manner when it was stolen
- B bank has paid the cheque in accordance with the crossing, in good faith and without negligence in terms of s79, B bank can debit A's account, and A, because he delivered the cheque to C, has discharged his liability to C.
- C is the true owner,
- C has suffered a loss, because he cannot hold A or B Bank liable for payment to the incorrect person.
- Z Bank was in possession of the cheque after it was stolen.
- If Z Bank gave consideration for the cheque, or took it as a gift, Z Bank will be liable, thus C would be able to sue Z Bank.

BUT, what are the chances that Z Bank gave consideration for the cheque or took it as a gift?

- Z Bank did not take the cheque as a gift
- Z Bank did not pay cash over the counter, or allow X to draw against the cheque immediately and so did not give consideration for it.
- Z Bank did not refuse to furnish any information to C and so is not deemed to have given consideration for it,

Thus, the chances that Z Bank will be held to have taken the cheque as a gift, or to have given consideration for it are minimal, if not non-existent.

SO THE TRUE OWNER IS BACK IN HIS FORMER POSITION – WITH NO ONE TO CLAIM FROM!

Whilst s81 superficially seems to improve the position of the true owner of a cheque in the event of loss or theft, this is not necessarily so. Usually the collecting banker will not be liable under s81. So the only time when s81 may perhaps improve the position of the true owner is if there has been another possessor between the thief and the collecting banker.

Example:

In the above example, X transfers the cheque to D in payment of a debt. D deposits the cheque in his bank account at Q Bank. Q Bank collects payment from B Bank on behalf of D.

ARE THE REQUIREMENTS MET?

- The cheque is crossed and marked not negotiable.
- It was marked in such a manner when it was stolen.
- B Bank has paid the cheque in accordance with the crossing, in good faith and without negligence – in terms of s79, B Bank can debit A's account, and A, because he has delivered the cheque to C, has discharged his liability to C.
- C is the true owner.
- C has suffered a loss, because he cannot hold A or B Bank liable for payment to the incorrect person.
- Z Bank and D were in possession of the cheque after it was stolen.
- Z Bank, as we have seen, will generally not have taken the cheque as a gift or given consideration for it. D has, however taken the cheque for a consideration (in payment of a debt).

RESULT:

C can sue D in terms of s81 (regardless of the fact that D may have acted in good faith).

Surely this provision may prove to be unduly harsh to the possessor??

- In terms of s81(7) any person who has made good the true owner's loss in terms of s81, acquires the same rights against prior possessors as the true owner had against them in terms of s81.

Thus, any party whom the true owner successfully sues in terms of s81, can, in turn, sue another party who was in possession of the cheque prior to him.

POSSIBLE QUESTIONS:

A draws a cheque for R2000 on B Bank in favour of "C or order". A delivers the cheque to C. The cheque is crossed and marked "not negotiable". D steals the cheque from C and after having forged C's signature, negotiates it to E who takes it in good faith and for value. E gives the cheque to a messenger, Y, to pay into his (E's) account at S Bank. B Bank pays S Bank in without negligence. Advise the following persons on their legal position:

1.1 BBank (3)

In terms of section 79, when a crossed cheque has come into the hands of the payee (C), the drawer is protected "as if payment of the cheque had been made to the true owner of it".
It is important to remember that where the post is chosen as mode of delivery, the risk of loss is on the sender, unless the receiver requested that the negotiable instrument should be posted, in which case the risk as well as ownership will then pass to the receiver immediately when the instrument is posted. A's liability on the cheque, as well as on the underlying obligations, are discharged because ownership of the cheque has passed on to E.

1.2 E (7)

In terms of section 81 (1) C, the true owner, acquires a right of recourse against E, the later possessor, if the following requirements of section 81 (1) are met:

(a) the cheque was crossed and marked "not negotiable"
(b) the cheque was stolen while it was crossed and marked as above;
(c) in terms of the Bills of Exchange Act the drawee bank, B, paid under circumstances which did not render the drawee bank liable
(d) C is the true owner of the intercepted cheque
(e) C showed that he has suffered damages as a result of the theft
(f) E had the cheque in his possession after the theft or loss and
(g) E has taken the cheque for value or has received it as a gift.

E will therefore not be able to raise any defence, should C institute an action against him. It appears that all the requirements of section 81(1) are met, therefore C will be able to hold E liable.

1.3 C (2)

C is the true owner. C has suffered a loss because he can't hold A or B Bank liable for payment to the incorrect person.

1.4 SBank (5)

Since B Bank paid in accordance with the crossing to another bank (S Bank), and since payment was made in good faith and without negligence, B Bank will be protected in terms of section 79. B Bank may thus debit the drawee, A's account.

Question 30:

A draws a cheque for R6000 on B Bank in favour of "C or order". At C's request A posts the cheque to him. The cheque is crossed and marked "not negotiable". D intercepts and steals the cheque before it reaches C. D forges C's signature and negotiates it to E who takes it in good faith and for value. E gives the cheque to his messenger, Y to pay it into his (E's) account at S Bank. E owes S Bank R 10 000. Therefore, S Bank applies the deposited cheque of R 5000 towards the reduction of E's debt. B Bank pays S Bank in good faith and without negligence. Discuss the rights of C against the following:

a) The drawer, A (4)

In terms of section 79, when a crossed cheque has come into the hands of the payee (C), the drawer is protected "as if payment of the cheque had been made to the true owner of it".
It is important to remember that where the post is chosen as mode of delivery, the risk of loss is on the sender, unless the receiver requested that the negotiable instrument should be posted, in which case the risk as well as ownership will then pass to the receiver immediately when the instrument is posted.
As the cheque was posted at C's (the payee's) request, risk of loss and the ownership of the cheque passed to C on the posting of the cheque. Therefore, e is the true owner and carries the risk of interception of the cheque followed by a payment that discharges it.
A's liability on the cheque, as well as on the underlying obligations, are discharged because ownership of the cheque has passed on to E.

b) B Bank (3)

Since B Bank paid in accordance with the crossing to another bank (S Bank), and since payment was made in good faith and without negligence, B Bank will be protected in terms of section 79. B Bank may thus debit the drawee, A's account.

c) D (2)

The true owner of the cheque, *E,* will have a right of recourse against D, who intercepted the cheque and acted *male fide.* C's right of recourse is based on delict (or enrichment) and not on the cheque itself.

d) *E* (9)

In terms of section 81 (1) C, the true owner, acquires a right of recourse against E, the later possessor, if the following requirements of section 81 (1) are met:

i) the cheque was crossed and marked "not negotiable" the cheque was stolen while it was crossed and marked as above;
ii) in terms of the Bills of Exchange Act the drawee bank, B, paid under circumstances which did not render the drawee bank liable
iii) C is the true owner of the intercepted cheque
iv) C showed that he has suffered damages as a result of the theft
v) E had the cheque in his possession after the theft or loss and
vi) E has taken the cheque for value or has received it as a gift.

E will therefore not be able to raise any defence, should C institute an action against him. It appears that all the requirements of section 81(1) are met, therefore C will be able to hold E liable.

e) S Bank (5)

In terms of section 81 (5) a collecting bank which receives payment on a cheque, which is crossed and marked "not negotiable", on behalf of one of its customers will not be regarded as having given consideration in respect of such a cheque merely because it has credited the account of its customer with the amount of the cheque before receiving payment of it, or because any such payment has been applied towards the reduction or settlement of any debt owned by that customer to the bank. However, the collecting bank, S Bank, will lose its protection if it paid out cash over the counter for such a cheque, or if it agreed that the customer could immediately draw against that cheque. If S Bank fails to give any information regarding the cheque which is at its disposal, it will be deemed to have been a possessor of the cheque and/or to have given consideration for it, or to have taken it as a donee. In the given situation S Bank will not be liable to C, merely because it applied the cheque towards the reduction of E's debt.

f) the messenger, Y (2)

If Y fails to furnish the true owner (C) with any information in connection with the cheque when so requested, Y will be liable in terms of section 81(3), and on application of section 81(1) he

will be deemed to have been a possessor of the cheque and/or to have given consideration for it, or to have taken it as donee.

Michelle draws a cheque on Big Bank in favour of Brian or order. The cheque is crossed and marked "not negotiable", Bobby steals the cheque from Brian, forges his (Brian's) signature on the back of the cheque and delivers it to Daniel who takes it in good faith and for value. Daniel instructs his messenger, Helen to deposit the cheque for collection in his banking account with Small Bank. Small Bank presents the cheque for payment to Big Bank. Big Bank pays it to Small Bank in good faith and without negligence. Big Bank debits the account of its client, Michelle, and Small Bank credits the account of its client, Daniel. Discuss whether or not Brian can institute a legal action against the following parties:

a) Michelle (4)

In terms of section 79, when a crossed cheque has come into the hands of the payee (Brian), the drawer is protected "as if payment of the cheque had been made to the true owner of it". It is important to remember that where the post is chosen as mode of delivery, the risk of loss is on the sender, unless the receiver requested that the negotiable instrument should be posted, in which case the risk as well as ownership will then pass to the receiver immediately when the instrument is posted. As the cheque was posted at Brian's (the payee's) request, risk of loss and the ownership of the cheque passed to Brian on the posting of the cheque. Therefore, Brian is the true owner and carries the risk of interception of the cheque followed by a payment that discharges it.
Michelle's liability on the cheque, as well as on the underlying obligations, are discharged because ownership of the cheque has passed on to Brian.

b) Big Bank (4)

Since B Bank paid in accordance with the crossing to another bank (S Bank), and since payment was made in good faith and without negligence, B Bank will be protected in terms of section 79. B Bank may thus debit the drawee, Michelle's account.

c) Daniel (7)

In terms of section 81 (1) Brian, the true owner, acquires a right of recourse against Daniel, the later possessor, if the following requirements of section 81 (1) are met:

(a) the cheque was crossed and marked "not negotiable"
(b) the cheque was stolen while it was crossed and marked as above;
(c) in terms of the Bills of Exchange Act the drawee bank, B, paid under circumstances which did not render the drawee bank liable
(d) Brian is the true owner of the intercepted cheque
(e) Brian showed that he has suffered damages as a result of the theft
(f) Daniel had the cheque in his possession after the theft or loss and
(g) Daniel has taken the cheque for value or has received it as a gift.

Daniel will therefore not be able to raise any defence, should Brian institute an action against him. It appears that all the requirements of section 81(1) are met, therefore Brian will be able to hold Daniel liable.

d) Helen (3)

If Helen fails to furnish the true owner (Brian) with any information in connection with the cheque when so requested, Daniel will be liable in terms of section 81(3), and on application of section 81(1) he will be deemed to have been a possessor of the cheque and/or to have given consideration for it, or to have taken it as donee.

e) Small Bank (4)

In terms of section 81 (5) a collecting bank which receives payment on a cheque, which is crossed and marked "not negotiable", on behalf of one of its customers will not be regarded as having given consideration in respect of such a cheque merely because it has

credited the account of its customer with the amount of the cheque before receiving payment of it, or because any such payment has been applied towards the reduction or settlement of any debt owned by that customer to the bank. However, the collecting bank, S Bank, will lose its protection if it paid out cash over the counter for such a cheque, or if it agreed that the customer could immediately draw against that cheque. If S Bank fails to give any information regarding the cheque, which is at its disposal, it will be deemed to have been a possessor of the cheque and/or to have given consideration for it, or to have taken it as a donee. In the given situation S Bank will not be liable to Brian, merely because it applied the cheque towards the reduction of Daniel's debt.

f) Bobby (3)

The true owner of the cheque, Brian, will have a right of recourse against Bobby, who intercepted the cheque and acted *mala fide*. Brian's right of recourse is based on delict (or enrichment) and not on the cheque itself.

Read the following scenario and answer the questions that follow.
Allie draws a cheque for R5000 on B Bank in favour of "Phil Or Order". The cheque is crossed and marked "not negotiable". Allie delivers the cheque from Phil and, after having forged Phil's signature, delivers it to Mary who takes it in good faith and for value. Mary gives the cheque to a messenger, Terry to pay into her (Mary's) account at V Bank. B Bank pays V Bank in good faith and without negligence.
Discuss fully whether or not Phil can institute legal action against the following parties.

(a) Allie (3)
(b) B Bank (3)
(c) Princess (2)
(d) Mary (5)
(e) The messenger, Terry, who refuses to give any information has about the cheque (3)
(f) V Bank (4)

Michelle draws a cheque on Big Bank in favour of Brian or order. The cheque is crossed. Bobby steals the cheque from Brian, forges his (Brian's) signature on the back of the cheque and delivers it to Daniel who takes it in good faith and for value. Daniel instructs his messenger, Helen to deposit the cheque for collection in his banking account with Small Bank. Small Bank presents the cheque for payment to Big Bank. Big Bank pays it to Small Bank in good faith and without negligence. Big

Bank debits the account of its client, Michelle, and Small Bank credits the account of its client, Daniel.

Discuss whether or not Brian can institute a legal action against Daniel.

Brian may not sue Daniel as he took the instrument in good faith. Here, Daniel took the cheque in good faith and for value – this would prevent Brian from suing him as s81 doesn't apply here to assist Brian.

Would your answer above differ if the cheque had been crossed and marked "not negotiable"?

Yes, here s81 would apply if all the requirements for s81 are complied with – discuss as above.

SUMMARY OF SECTIONS 58, 79 AND 81:

SECTION 58:

- DRAWEE bank pays the cheque according to its instructions but pays the wrong person (i.e. does not pay the holder and therefore does not make payment in due course)

REQUIREMENTS:

- Order cheque (not bearer or non-transferable).
- Crossed or uncrossed.
- Forged or unauthorised endorsement.
- Good faith.
- Ordinary course of business.

PROVISO:

Provided the forged endorsement does not purport to be that of a customer of the drawee bank (same branch).

EFFECT:

If s58 applies:

- Drawee bank placed in the same position as if it had paid the holder (i.e. made payment in due course)
- The true owner bears the loss,

If s58 does not apply:

Drawee bank has not made payment in due course and may not debit the drawer's account (the drawee bank bears the loss).

SECTION 79:

- Drawee bank pays the cheque in accordance with the crossing (i.e. to a collecting bank) but pays the wrong person (i.e. does not pay the holder and therefore does not make payment in due course)

REQUIREMENTS:

- Crossed cheque
- Paid in accordance with the crossing
- Good faith

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- Without negligence

NO PROVISO

EFFECT:

If s79 applies:

- Drawee bank placed in the same position as if it had paid the holder (i.e. made payment in due course)
- True owner bears the loss.

If s79 does not apply:

- Drawee bank has not made payment in due course and may not debit the drawer's account (i.e. drawee bank bears the loss)

NOTE:

S79 has the same effect as s58, but the burden of proof is much heavier. So, if the cheque in question is crossed always try apply s79 first and, if s79 does not apply, try s58.

SECTION 81:

- Where a crossed cheque marked "not negotiable" is lost or stolen from the true owner, and the bank is protected by s79.

NOTE:

S81 ONLY APPLIES IF S79 ALSO APPLIES SO CHECK IF 579 APPLIES FIRST.

REQUIREMENTS:

- Crossed cheque marked not negotiable.
- Lost or stolen while so marked.
- Paid in accordance with the crossing (protected by s79).
- Plaintiff is the true owner.
- Plaintiff suffered a loss.
- Defendant came into possession of the cheque after it was lost or stolen.
- Defendant gave consideration for the cheque or took it as a gift.

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NOTE:

The last 2 requirements are deemed to have been met where a person REFUSES to furnish relevant information at their disposal.

EFFECT:

The true owner can sue anyone who was in possession of the cheque after it was lost or stolen and who took it for a consideration or as a gift, regardless of whether the person took the cheque in good faith or not.

THE COLLECTING BANK:

INDAC ELECTRONICS & COLOMBUS JOINT VENTURE:

This section deals with the liability of the COLLECTING BANK (in our examples given its S Bank).

When discussing this section, look for the part of the question stating "advise C fully about his rights with reference to DECIDED CASES AND THE BILL OF EXCHANGE AMENDMENT ACT! Do not discuss the cases unless this part of the question appears. It can also be asked in this form: "Discuss the Indac case with reference to the liability of the collecting bank." OR "Discuss the liability of the collecting bank towards the true owner with reference to recent case law"

In the Indac case, the court was asked to determine the liability, if any, of the collecting bank towards the true owner. The Supreme Court of Appeal decided in this case, that the collecting bank can be liable towards the true owner, delictually, for negligent payment to the wrong person – provided the elements of a delict were complied with, namely:
a) An act; b) wrongful: c) fault: d) causation and e) damage.

To establish whether or not S Bank (a collecting bank in an exam question – remember you only have a collecting bank if the cheque is crossed) could be delictually liable one needs to look at cases such as Indac Electronics and Columbus Joint Venture.

START HERE: For a long time there was controversy as to whether a collecting bank acquired delictual liability towards the true owner of a cheque if the bank negligently collected payment of the cheque on behalf of the wrong person. However, this question of negligence was settled in the Indac case. Here it was held that the true owner of a stolen cheque can

charge the collecting bank with negligence if the collecting bank negligently collects the cheque on behalf of a client who is not entitled to receive payment on that cheque. It was held further that a collecting bank could be held liable under the extended *lex Aquiliae* for negligence towards the true owner, provided ALL the elements or requirements of Aquilian liability have been met. The true owner needs to prove the following elements in order to be successful in his bid to hold the collecting bank liable for the wrongful collection there has to be:

* an act or an omission;
* the act or omission had to be unlawful;
* there must have been intent or negligence on the part of the person who performed the act or omission;
* there must have been loss suffered; and
* there must have been a casual connection between the act or omission and the loss that was suffered.

In determining negligence, the court also held that the bank would be negligent if it fails to take reasonable steps to determine whether its clients is ex facie entitled to payment of the cheque. Courts have decided on several occasions that when a new client applies to open an account, the bank is legally obliged to take reasonable steps to prevent abuse of that account. The bank is expected to take reasonable care to check the client's personal particulars and identity. In KwaMashu Bakery Ltd cheques were made payable to "KwaMashu Bakery Ltd only" and were therefore not transferable. When they were stolen, an account was opened under the name of "KwaMashu Bakery Ltd Soccer Club" and the cheques were deposited into this account and payment was obtained. The question of the bank's negligence arose. It was held that collecting bank was negligent, as the name of the payee on the cheques was not the same as the name of the account into which the cheques were deposited and for this reason alone the bank was negligent.

In Columbus Joint Venture the court held that a collecting banker owes the owner of a cheque a duty of care not to collect its proceeds negligently on behalf of one not entitled to payment. This duty of care encompasses an obligation to take reasonable care when receiving and processing an application to open a new banking account through which cheques belonging to another are subsequently collected for payment.

There are important differences between the circumstances when a stranger requests that a new bank account be opened and those when an existing customer of the bank makes a similar request.

In the latter case the existing customer generally has a verified identity and confirmed work and residential contact details. Should the new account be used for fraud, the customer can be traced and brought to book In addition, the location of the customer's assets may be known or

traceable through the details already furnished. The pre-eminent consequence is heightened accountability, which substantially diminishes the possibility of the account being used for fraud with impunity. There is thus a significant disincentive to fraudulent use of the account. In contrast, the disincentive to fraud is absent in the case of a new customer, whose identity, location and other details have not been verified. In such circumstances a bank is under a duty to take reasonable measures to ascertain and verify the new customer's identity and trustworthiness, for without the disincentive that verification of the relevant details provides, the risk that the account could be used for fraudulent purposes is heightened.

From the facts it appears that the collecting bank, S Bank is *prima facie* negligent towards C for having collected payment on a non-transferable cheque on behalf of someone who was not *ex facie* the cheque entitled to such payment.

POSSIBLE QUESTIONS:

A draws a crossed cheque on B Bank in favour of "C only" in repayment of a loan. At C's request A posts the cheque to him. X intercepts and steals the cheque before it reaches C. X forges C's signature and negotiates it to D who takes it in good faith and for value. D deposits the cheque for collection in his bank account with S Bank. S Bank presents the cheque for payment to B Bank. B Bank pays S Bank in good faith and without negligence. B Bank debits the account of its customer, A and S Bank credits the account of its customer, D.

Advise C fully about his rights against the following parties with reference to decided cases and the Bills of Exchange Amendment Act of 2000:

a) the drawer, A (5)

In terms of section 79, when a crossed cheque has come into the hands of the payee (e), the drawer is protected "as if payment of the cheque had been made to the true owner thereof ". Where the post is chosen as mode of delivery, the risk of loss is on the sender, unless the payee has requested that the cheque be posted, in which case the risk as well as ownership has passed to the payee immediately when the cheque is posted. As the cheque was posted at C's request, the ownership of the cheque passed to C on the posting of the cheque. C is then the true owner and carries the risk of interception of the cheque followed by a payment that discharges it.

The crossed cheque marked "C only" has resulted in the cheque being non-transferable in terms of section 6(5). In decided cases the court

pointed out that section 79 contains no indication that it applies only to transferable cheques Consequently, section 79 does apply to non-transferable cheques. Furthermore, since the cheque has already come into the hands of the payee, C the provisions of section 79 comes into play and the payee, C has no further claim against the drawer. A's liability on the cheque, as well as on the underlying obligations, are discharged because ownership of the cheque has passed on to C.

b) S Bank (10)

A crossed cheque marked "C only" has resulted in the cheque being non-transferable. There are two categories of non-transferable cheques:

- **The traditional non-transferable cheque which in terms of section 6(5) bears words or conveys an intention to prohibit transfer.**
- **Section 75A will only be applicable where the words "non transferable" are printed boldly across the face of a crossed cheque either with or without the word "only" after the payee's name. In terms of section 75A such a cheque will be not transferable and will only be valid as between the parties to it.**

In this case section 6(5) will be applicable because the cheque is marked 'C only'. Section 75A would have been applicable if the words 'non transferable' were printed boldly across the face of the cheque. A crossed cheque containing words indicating an intention to prohibit transfer will not be transferable. Such a cheque may not qualify as 'non transferable' within the meaning of section 75A, but it is nonetheless a non transferable cheque in terms of section 6(5). A crossed section 6(5) non-transferable cheque may only be deposited into an account bearing a name identical to that of the payee. – *ONLY ADD S75A IN IF THE QUESTION STATES "PAY C ONLY", IF IT DOES NOT STATE "PAY C ONLY" DO NOT DISCUSS S75A!! THEN START THE ANSWER FROM NOW…*

To establish whether or not S Bank could be delictually liable one needs to look at cases such as <u>Indac Electronics and Columbus Joint Venture.</u>

For a long time there was controversy as to whether a collecting bank acquired delictual liability towards the true owner of a cheque if the bank negligently collected payment of the cheque on behalf of the wrong person. However, this question of negligence was settled in the <u>Indac case</u>. Here it was held that the true owner of a stolen cheque can charge the collecting bank with negligence if the collecting bank negligently collects the cheque on behalf of a client who is not entitled to receive payment on that cheque. It was held further that a collecting bank could be held liable under the extended *lex Aquiliae*

for negligence towards the true owner, provided ALL the elements or requirements of Aquilian liability have been met. The true owner needs to prove the following elements in order to be successful in his bid to hold the collecting bank liable for the wrongful collection there has to be:

*** an act or an omission;**
*** the act or omission had to be unlawful;**
*** there must have been intent or negligence on the part of the person who performed the act or omission;**
*** there must have been loss suffered; and**
*** there must have been a casual connection between the act or omission and the loss that was suffered.**

In determining negligence, the court also held that the bank would be negligent if it fails to take reasonable steps to determine whether its clients is ex facie entitled to payment of the cheque. Courts have decided on several occasions that when a new client applies to open an account, the bank is legally obliged to take reasonable steps to prevent abuse of that account. The bank is expected to take reasonable care to check the client's personal particulars and identity. In KwaMashu Bakery Ltd cheques were made payable to "Bakery Ltd only" and were therefore not transferable. When they were stolen, an account was opened under the name of "KwaMashu Bakery Ltd Soccer Club" and the cheques were deposited into this account and payment was obtained. The question of the bank's negligence arose. It was held that collecting bank was negligent, as the name of the payee on the cheques was not the same as the name of the account into which the cheques were deposited and for this reason alone the bank was negligent. OR

In Columbus Joint Venture the court held that a collecting banker owes the owner of a cheque a duty of care not to collect its proceeds negligently on behalf of one not entitled to payment. This duty of care encompasses an obligation to take reasonable care when receiving and processing an application to open a new banking account through which cheques belonging to another are subsequently collected for payment.

There are important differences between the circumstances when a stranger requests that a new bank account be opened and those when an existing customer of the bank makes a similar request.

In the latter case the existing customer generally has a verified identity and confirmed work and residential contact details. Should the new account be used for fraud, the customer can be traced and brought to book In addition, the location of the customer's assets may be known or traceable through the details

already furnished. The pre-eminent consequence is heightened accountability, which substantially diminishes the possibility of the account being used for fraud with impunity. There is thus a significant disincentive to fraudulent use of the account. In contrast, the disincentive to fraud is absent in the case of a new customer, whose identity, location and other details have not been verified. In such circumstances a bank is under a duty to take reasonable measures to ascertain and verify the new customer's identity and trustworthiness, for without the disincentive that verification of the relevant details provides, the risk that the account could be used for fraudulent purposes is heightened.

From the facts it appears that the collecting bank, S Bank is *prima facie* negligent towards C for having collected payment on a non-transferable cheque on behalf of someone who was not *ex facie* the cheque entitled to such payment.

Discuss briefly the decision of the court in *Indac Electronics (Pry) Ltd Volkskas Bank Ltd* 1992 (1) SA 783 (A). (5)

For a long time there was controversy as to whether a collecting bank acquired delictual liability towards the true owner of a cheque if the bank negligently collected payment of the cheque on behalf of the wrong person. However, this question of negligence was settled in the Indac case. Here it was held that the true owner of a stolen cheque can charge the collecting bank with negligence if the collecting bank negligently collects the cheque on behalf of a client who is not entitled to receive payment on that cheque. It was held further that a collecting bank could be held liable under the extended *lex Aquiliae* for negligence towards the true owner, provided ALL the elements or requirements of Aquilian liability have been met. The true owner needs to prove the following elements in order to be successful in his bid to hold the collecting bank liable for the wrongful collection there has to be:

*** an act or an omission;**
*** the act or omission had to be unlawful;**
*** there must have been intent or negligence on the part of the person who performed the act or omission;**
*** there must have been loss suffered; and**
*** there must have been a casual connection between the act or omission and the loss that was suffered.**

Discuss the liability of the collecting bank towards the true owner with reference to recent case law. (10)

AS ABOVE – INDAC AND & KWA MASHU / COLUMBUS.

A draws a cheque on B Bank in favour of C or order. The cheque is crossed and marked "not negotiable. Account payee only. Not transferrable". The cheque is delivered to C by A. The cheque is stolen from C by X, who forges C's endorsement and transferres the cheque to D who takes the cheque in good faith and for value. The cheque is deposited into D's account at Z Bank. B Bank pays Z Bank in good faith and without negligence.
Can C claim payment from:
a) A? (3)
b) D? (7)
c) X? (2)
d) Z Bank (refer to case law and the Bill of Exchange Amendment Act)? (10)

In this question, you have to discuss s81 (due to the fact that the cheque was crossed and marked NN) PLUS you have to discuss Indac; Kwa Mashu & Colombus AND Sham Magazine (crossed and marked A/C only) AND s6(5) with s75A (cheque marked NT).
So……

a) **No C cant sue A because A delivered the cheque to C (discuss)**

b) **Yes, C can sue D – discuss the requirements for s81 (as above) –**

- **the cheque was crossed and marked "not negotiable"**
- **the cheque was stolen while it was crossed and marked as above;**
- **in terms of the Bills of Exchange Act the drawee bank, B, paid under circumstances which did not render the drawee bank liable**
- **Brian is the true owner of the intercepted cheque**
- **Brian showed that he has suffered damages as a result of the theft**
- **Daniel had the cheque in his possession after the theft or loss and**
- **Daniel has taken the cheque for value or has received it as a gift. – discuss!**

c) **Yes, C can sue X in delict / undue enrichment (discuss).**

d) **The traditional non-transferable cheque which in terms of section 6(5) bears words or conveys an intention to prohibit transfer. Section 75A will only be applicable where the words "non transferable" are printed boldly across the face of a crossed cheque either with or without the word "only" after the payee's name. In terms of section 75A such a cheque will be not**

transferable and will only be valid as between the parties to it. It has become standard practice in certain circles to add the words "account payee only" or "account payee" to crossings on cheques. The effect of such markings was unclear in the past because the Act does not provide for such.
In Dungarvin Trust (Pty) Ltd v Import Refrigeration Co (Pty) Ltd 1971 (4) SA 300 (W) the court held that these words conveyed a clear intention that the cheque may not be transferred to a third party (made the cheque not transferable). In the subsequent case of Standard Bank of SA v Sham Magazine Centre 1977 (1) SA 484 (A) the Supreme court of Appeal had to decide whether the words "a/c payee only" exclude the transferability of the cheque. Thus the question before the court was whether the words "a/c payee only" prohibited the transfer of the cheque. To decide this the court had to interpret s6 (5) of the Act and the words "a/c payee only". The court made it clear that such markings do not affect the transferability of a cheque, thus it remains freely transferable and can even be negotiated. The court also said that the words "not negotiable" used in conjunction with the words "a/c payee only" DO NOT exclude the transferability of the cheque. The words "a/c payee only" are only an indication that the cheque must be collected for a specific payee

To establish whether or not S Bank could be delictually liable one needs to look at cases such as Indac Electronics and Columbus Joint Venture.
For a long time there was controversy as to whether a collecting bank acquired delictual liability towards the true owner of a cheque if the bank negligently collected payment of the cheque on behalf of the wrong person. However, this question of negligence was settled in the Indac case. Here it was held that the true owner of a stolen cheque can charge the collecting bank with negligence if the collecting bank negligently collects the cheque on behalf of a client who is not entitled to receive payment on that cheque. It was held further that a collecting bank could be held liable under the extended *lex Aquiliae* for negligence towards the true owner, provided ALL the elements or requirements of Aquilian liability have been met. The true owner needs to prove the following elements in order to be successful in his bid to hold the collecting bank liable for the wrongful collection there has to be:
*** an act or an omission;**
*** the act or omission had to be unlawful;**
*** there must have been intent or negligence on the part of the person who performed the act or omission;**
*** there must have been loss suffered; and**

*** there must have been a casual connection between the act or omission and the loss that was suffered.**

In determining negligence, the court also held that the bank would be negligent if it fails to take reasonable steps to determine whether its clients is ex facie entitled to payment of the cheque. Courts have decided on several occasions that when a new client applies to open an account, the bank is legally obliged to take reasonable steps to prevent abuse of that account. The bank is expected to take reasonable care to check the client's personal particulars and identity. In KwaMashu Bakery Ltd cheques were made payable to "Bakery Ltd only" and were therefore not transferable. When they were stolen, an account was opened under the name of "KwaMashu Bakery Ltd Soccer Club" and the cheques were deposited into this account and payment was obtained. The question of the bank's negligence arose. It was held that collecting bank was negligent, as the name of the payee on the cheques was not the same as the name of the account into which the cheques were deposited and for this reason alone the bank was negligent. OR

In Columbus Joint Venture the court held that a collecting banker owes the owner of a cheque a duty of care not to collect its proceeds negligently on behalf of one not entitled to payment. This duty of care encompasses an obligation to take reasonable care when receiving and processing an application to open a new banking account through which cheques belonging to another are subsequently collected for payment.

There are important differences between the circumstances when a stranger requests that a new bank account be opened and those when an existing customer of the bank makes a similar request.

In the latter case the existing customer generally has a verified identity and confirmed work and residential contact details. Should the new account be used for fraud, the customer can be traced and brought to book In addition, the location of the customer's assets may be known or traceable through the details already furnished. The pre-eminent consequence is heightened accountability, which substantially diminishes the possibility of the account being used for fraud with impunity. There is thus a significant disincentive to fraudulent use of the account. In contrast, the disincentive to fraud is absent in the case of a new customer, whose identity, location and other details have not been verified. In such circumstances a bank is under a duty to take reasonable measures to ascertain and verify the new customer's identity and trustworthiness, for without the disincentive that

verification of the relevant details provides, the risk that the account could be used for fraudulent purposes is heightened.

From the facts it appears that the collecting bank, Z Bank is *prima facie* negligent towards C for having collected payment on a non-transferable cheque on behalf of someone who was not *ex facie* the cheque entitled to such payment.

YOU DON'T HAVE TO DISCUSS ALL OF KWA MASHU AND COLOMBUS – DISCUSS ONE OF THEM AND MENTION THE OTHER BUT DON'T FORGET TO DISCUSS S6(5); S75A; SHAM AND INDAC!!!!

NB definitions for the exam:

Define the following terms:
a) issue:
b) holder
c) delivery
d) negotiation
e) payment in due course
f) cheque
g) acceptance
h) in good faith
i) a bill of exchange
j) bearer

Promissory Notes:

The following is a written promise between colleagues:

"I, Eesa Fredericks, acknowledge that I owe Ernest Maleka R500.00 for repairs done on my computer and will pay the amount to him on Friday, 13 August 2004."

a) Does the above promise constitute a promissory note? (2)

Yes, all the requirements for a valid PN are complied with (see definition of PN).

b) What is Mr. Fredericks's position in terms of the Bills of Exchange Act? (2)

He is the maker of the note and is similar to the acceptor of a bill. He will also be the first endorser if its transferred.

c) Does Mr. Fredericks incur any liability on the note? (2)

Yes he warrants, as the maker, to pay the note and cant deny to the HIDC the existence of the payee and his capacity to endorse at the time.

Name any 3 functions of a promissory note.

Its an instrument of proof; an instrument for obtaining credit or financing; an instrument of investment and an instrument of security.

Methods of payment

1. CREDIT CARDS

Different types of Credit Cards:

There are two types of credit cards,
- ξ two-party credit cards
- ξ three-party credit cards.

In the case of a two-party credit card, there are only two parties involved, namely the card issuer (who is also the supplier) and the cardholder. Two-party credit cards - mainly issued by filling stations to clients who wanted to purchase fuel on credit. Today most large department stores (for example, Edgars, Woolworths, Jet etc) issue two party credit cards to their existing clients.

The name, the account number and the signature of the cardholder is indicated on the card and the cardholder (or client) is entitled to make purchases on credit at various stores within the chain up to a maximum amount agreed to by the parties.

Two-party credit card
The two parties are the card issuer and the cardholder.
With a two party credit card the card issuer is also the supplier of the goods or services purchased.
The card issued by some wholesalers to their clients who purchase in bulk (for example, a Makro card or a Trade Centre card) is not considered to be a two party credit card. These cards are merely used to identify a customer and track purchases but cannot be used to make purchases on credit.

Three-party credit cards
There are three parties involved, the card issuer (which is usually a bank), the cardholder and the supplier.
The card issuer enters into contacts with different suppliers who agree to accept the credit card when presented by the cardholder as payment for goods and services purchased. The card issuer also undertakes to reimburse the supplier (subject to certain conditions and minus a specific percentage) for the purchases made by the cardholder. The card issuer also contracts with the cardholder that the cardholder may make purchases on credit subject to the limit agreed to by the parties.
When the cardholder pays by credit card, a sales slip is completed in duplicate with one copy retained by the cardholder and the other by the

supplier. The supplier sends this copy to the card issuer who compensates the supplier and debits the account holder's account. The account holder is then given a period in which to make payment to the card issuer.

EXAMPLE:
Standard Bank issues a Master Card to P, one of their customers. Standard Bank also concludes an agreement with MacD Ltd, a fast food chain, that the latter will accept all Master Cards issued by the former, as valid payment for purchases made at MacD. P buys fast foods to the value of R110,00 from MacD'S and pays for it with her Master Card.
(a) Which type of credit card is the Master Card in this set of facts?
(b) Which party is the card issuer?
(c) Which party is the cardholder?
(d) Which party is the supplier?
(e) Can MacD refuse to accept P's Master Card as payment?

(a) A three-party credit card.
(b) Standard Bank.
(c) Patsy.
(d) MacD's.
(e) No, except if the credit card is no longer valid.

The legal relationship in terms of a three-party credit agreement:
Because there are three parties involved in respect of a three-party credit card, there are also three different sets of legal relationships flowing from the three-party credit card agreement.
These are:

1. the relationship between the card issuer and the cardholder,
2. the relationship between the card issuer and the supplier, and
3. the relationship between the cardholder and the supplier.

The relationship between the card issuer and the cardholder:
A credit card account is similar to that of a cheque account in that both are examples of current accounts. This means that the individual debts are continuously set-off against each other with only the balance remaining due. If the cardholder's account is in debit, the cardholder borrows money from the bank when making purchases by credit card. The cardholder is given a specific amount of time to repay the debt (either as an interest free loan) or in instalments. If the cardholder's account is in credit, interest will be charged for the loan made to the bank. If purchases are made by the cardholder, the cardholder's loan to the bank is repaid when the bank makes payment to the supplier.

The relationship between the card issuer and the supplier:
This relationship is governed by the express terms of the agreement between the card issuer and supplier. Two of the standardised terms of this agreement are that the card issuer will only pay the supplier if the card used to make purchases by the cardholder is valid or that the amount purchased does not exceed the maximum stipulated in the agreement.

The relationship between the cardholder and the supplier:
A supplier who has concluded a contract with a card issuer is obliged to accept the credit cards when presented as a method of payment. The intention of the parties is that the supplier will receive payment from the card issuer. The cardholder will therefore not be liable for payment to the supplier unless the card issuer fails to pay the supplier. The liability of the cardholder towards the supplier is thus suspended. If the card issuer pays, the liability of the cardholder is extinguished. However, if the card issuer fails to pay the supplier, the suspension of the liability of the cardholder ceases and the supplier may claim payment directly from the cardholder.

The legal relationship in terms of a two-party credit agreement:
The legal consequences of the loss or theft of a two-party agreement is similar to that of a three-party agreement. The only **difference** is that once the cardholder has informed the card issuer, it implies that the cardholder has informed the supplier as well. Generally, this means that once the card issuer has been informed the card issuer/supplier bears the risk of loss for unauthorised payments.

THE UNAUTHORISED USE OF A CREDIT CARD:
Who is responsible for paying where the credit card is used by a thief or some other person who has by chance come into possession of the credit card.
The standard contracts concluded between supplier, issuer and cardholder usually contain provisions in respect of such losses.
In the event of theft or loss of the credit card, the standard-terms agreement between the card issuer and the cardholder provides as follows:

- The cardholder bears the risk of loss until such time that the cardholder has notified the issuer. As stated above, it is possible for the cardholder to obtain insurance against this risk by the payment of an additional premium.
- The issuer bears the risk of loss from the moment that it received the notification until such time as the supplier had been notified.
- Once the supplier had been notified (usually by receipt of a list of missing cards), the supplier is obliged to refuse to accept the card as payment for purchases made. If the supplier does accept the card, the issuer may refuse to compensate the supplier in respect of the purchases made.

The National Credit Act confirms the trade usage and standard terms relating to the party's liability for the unauthorised use of lost or stolen credit cards. The Act now provides statutory protection to the cardholder where the cardholder has informed the card issuer of the loss of the card of the PIN. This protection will however not apply where the card issuer can prove that the cardholder has acted fraudulently.

2. TRAVELLERS' CHEQUES

TRAVELLERS' CHEQUES AND THE BILLS OF EXCHANGE ACT

There is no legislation, which applies specifically to travellers' cheques. However, question is whether a travellers' cheque is a bill of exchange, cheque or a promissory note as described in the Bills of Exchange Act.

The question whether a travellers' cheque amounts to, for example, a bill of exchange, is important for the following reason. If a document qualifies as a bill of exchange or promissory note as defined in the Bills of Exchange Act, the provisions of the Act will regulate the relationships on the document.

However, if a document does not satisfy the definition of a bill of exchange or a promissory note, the parties to the document cannot rely on the provisions of the Act.

In order to answer this question, a distinction is drawn between, on the one hand, those travellers' cheques in terms of which payment by the issuer of the travellers' cheque is made conditional on countersignature by the traveller, and on the other hand, those travellers' cheques in terms of which payment by the issuer of the travellers' cheque is not made conditional on countersignature by the traveller.

In the case of the former, it does not conform to the essential element of unconditionality as required by the Act. If payment of the travellers' cheque by its issuer is subject to the condition that it must be countersigned by the traveller, it is not unconditional as envisaged in the Act.

In the case of those travellers' cheques in terms of which payment by the issuer of the travellers' cheque is not conditional on countersignature by the traveller, it would appear that it conforms to the requirements of a bill of exchange (which includes a cheque) as envisaged in the Act.

It must be noted however that the vast majority of travellers' cheques belong to the former type of travellers' cheque.

Theft and loss of travellers' cheques:
Usually the purchase agreement between the issuer and the buyer will determine their obligations in the case of theft or loss of a travellers' cheque. Generally, the position is as follows. If the travellers' cheque countersigned before presentment of payment (contrary to the purchase agreement) is paid by the issuer, the purchaser of the cheque will not be able to claim a refund against the issuer in the event of the cheque being lost or stolen.
The position is UNCERTAIN where the travellers' cheque is lost or stolen before it has been countersigned. The signature of the original purchaser had been forged so as to obtain payment. In such a case, the purchaser's claim for a refund will depend on the wording of the contract with the issuer and the question of whether the purchaser has complied with all his or her contractual obligations

POSSIBLE QUESTIONS:

Critically discuss whether or not the provisions of the Bills of Exchange Act 34 of 1964 would apply to traveller's cheques.

See above discussion.

3. STOP ORDERS AND DEBIT ORDERS

Stop orders:
The stop order is not an instrument of payment but rather a method of payment.
The stop order is not a negotiable instrument as it cannot be transferred from one person to another.
It is a payment mechanism used in conjunction with a transmission account or a savings account.
It contains a written instruction from the account holder (that is, the customer or client of the bank) to the bank to pay a fixed amount on a regular basis to a specific third party and to debit the customer's account with the amount.
A stop order is used to pay weekly or monthly debts of a fixed amount such as an insurance premium, property tax payable to a municipality or rent.

The legal relationship between the bank and the account holder is based on the contract of mandate where the account holder is the mandator and the bank the mandatory. As in the case of payment of cheques, the banks' obligation to perform is conditional on there being sufficient funds in the account holder's account against which the paid amount may be set-off.
Whereas the payment instruction contained in a cheque reaches the bank indirectly via the creditor, the payment instruction contained in a stop order

is handed directly to the bank by the debtor (the bank's own client). This practical difference has consequences as regards the effect of the different payment instructions on the relationship between debtor and creditor. These are
(i) the creditor does not derive nay rights from the stop order; and
(ii) the underlying obligation is not terminated.

The creditor does not derive any rights from the stop order:
The creditor does not derive any rights from the stop order.
The stop order is an instruction by the debtor to his bank to pay a specified third party a fixed amount of money on a regular basis. The debtor signs the stop order and hands it to his bank where he holds a current cheque, credit card or savings account.
The creditor obtains no rights in terms of the stop order against the bank or the debtor (i.e. account holder) since the stop order results only in an obligation between the bank and the account holder.
The creditor receives payment at the will of the debtor and his bank and the creditor can never be ensured of payment at a specific date.
If the debtor revokes payment without notifying the creditor, the latter cannot sue the debtor or the bank on the stop order.
In the case of a cheque, the creditor (payee) also obtains no rights against the drawee bank on the cheque but a cheque does result in an obligation between the drawer (i.e. the account holder) and the creditor. In terms of section 53(1)(a) of the Bills of Exchange Act the drawer, by drawing the cheque, undertakes that the cheque will be paid when duly presented and that the drawer will compensate the holder if it is dishonoured. The creditor may sue the drawer on the cheque if the latter has countermanded payment of it. Because a cheque is a liquid document, this claim may be enforced by means of provisional sentence unless the drawer can prove that the original debt is unenforceable.

No termination of the underlying obligation
The underlying relationship between the debtor and creditor is not terminated by the debtor's giving the stop order to the creditor.
When a debtor gives a stop order (literally: an order to pay) to his bank no collateral or substitute agreement comes into existence between the debtor (account holder) and the creditor.
The debt owed by the account holder is not paid until the bank has actually paid the amount to the creditor. Therefore, should the bank fail to perform the instruction, the creditor would be entitled to cancel the contract (as the debtor is in breach because of non-payment). The fact that the bank did have reason for non-payment will usually means that the bank did not fulfil its obligation towards its customer. In such a case, the customer would then have a claim for damages against the bank on the grounds of breach of contract. In practice the possibility of such a claim is usually excluded, since the stop order form signed by the account holder determines that the

person giving the order will have no claim against the bank if the bank inadvertently fails to effect payment in terms of the instruction

Debit orders:

The debit order is an authorisation by the debtor to his creditor to request an amount from the debtor's bank, and includes an authorisation to the bank to pay the amount to the creditor. The amount which is requested by the creditor may vary and the bank will pay the amount which is requested by the creditor. A debtor must sign and hand over a debit order only to a creditor who can be trusted.

A debit order is used to pay weekly or monthly debts of a fixed or varying amount such as a telephone account, a bond payment, a water and electricity account or any other regular payment which may or may not be subject to a regular increase, such as a life insurance premium which is linked to an increase clause to combat the effect of inflation

Similarities between a debit order and a stop order (previous question):

The similarities:

(1) Both are methods of payment.
(2) Both contain an instruction to the bank where the debtor is an account holder to pay a certain sum to the creditor.
(3) Neither of them creates a collateral agreement between the debtor and the creditor. Thus, the creditor cannot sue the debtor on the stop or debit order if the creditor does not receive payment from the bank.
(4) Neither of them is a negotiable instrument.

The differences:

(1) The stop order is a mandate from the account holder to his bank to pay from his account while the debit order is not only a mandate to the bank to pay but also an authorisation to the creditor to request payment from the bank.
(2) The stop order is never given to the creditor while the debit order is handed over to creditor and the duty to request punctual payment rests on the creditor.
(3) The stop order can only be used to provide for a deduction of a fixed amount from the account of the debtor. The debit order, in contrast, may provide for a varying amount to be deducted from the account of the debtor.
(4) The use of a stop order does not suspend the creditor's right to claim payment directly from the debtor, while the creditor's right to claim payment from the debtor is suspended when the creditor accepts a debit order from the debtor. The creditor's right to payment from the debtor is suspended until he has made the necessary request from the debtor's bank.

4. LETTERS OF CREDIT

The operation of the documentary letter of credit:

1. The parties to an international trade contract agree, usually as a term of their contract, that payment will be effected by means of a documentary letter of credit. This trade contract is referred to as the underlying agreement of the exchange agreement. One of the most important principles relating to letters of credit is that the credit agreement concluded between the issuing bank and the beneficiary when the letter of credit is issued, is entirely separate and independent from the underlying obligation.

2. The purchaser/importer arranges with the bank (usually a domestic bank) for the issuance of a letter of credit in favour of the vendor/exporter. This takes place by the purchaser having to complete a standard application form supplied by the bank, in which the various terms and conditions of the letter of credit are stipulated. These could include an undertaking by the bank in favour of the vendor that it will pay the vendor in cash a specified amount, or that it will accept and pay bills of exchange drawn by the vendor on the bank up to a specified amount, or that it will pay bills of exchange drawn by the vendor on the bank and discounted to another bank up to a specified amount, provided certain specified documents are handed to the bank. In addition, the manner and time of repayment of the debt by the purchaser is also included.

3. The bank then issues the letter of credit in favour of the vendor reflecting the terms and conditions stipulated by the purchaser. The letter of credit is forwarded to the vendor (or to another bank in the vendor's country).

4. If another bank is employed, this bank may confirm the letter of credit, thereby itself assuming liability towards the beneficiary to pay the relevant amount; or it may merely advise or notify the beneficiary of the issuance of the letter of credit without itself giving an undertaking to pay. The letter of credit may also indicate an advising bank as the bank (the paying bank) to which the documents must be submitted and from which payment can be obtained. This does not, however, create a personal duty on the part of the advising bank towards the beneficiary.

5. Once the vendor receives or is notified of the letter of credit and if he or she agrees to the terms thereof, the vendor will proceed with the shipment, certification, insurance, etc of the merchandise and will eventually submit all the necessary documents to the issuing, confirming or advising bank in order to receive payment.

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6. Upon receipt of the documents, the bank will inspect the documents in order to ascertain whether they are in strict conformity with the terms stipulated in the letter of credit. If they are, the bank pays the vendor or accepts his or her bills.

7. The paying bank is eventually reimbursed by the issuing bank. The issuing bank will in turn be reimbursed by the purchaser, and it is evident that the title documents (for example, a bill of lading) serve as the bank's security for the payment made by it: unless the purchaser pays the bank, the bank will refuse to hand over the documents required by the purchaser in order to take delivery of the merchandise.

<u>The Bank's undertaking is separate and independent:</u>
The bank is strictly bound by the terms contained in the letter of credit when carrying out its obligation towards the beneficiary (vendor). The bank cannot take into account any stipulations in the underlying contract and should not concern itself with claims and complaints by the applicant (purchaser) resulting from his or her relationship with the beneficiary.
Payment in terms of the letter of credit is effected on the strength of a set of documents to be submitted to the bank by the beneficiary. If the documents that are submitted are in strict compliance with the requirements set out in the letter of credit, the bank is obliged to make payment to the beneficiary. The bank deals only with the credit documents, not with the goods sold in terms the contract of sale between the purchaser and the vendor. The bank is not in a position to verify whether the goods actually shipped by the vendor are in accordance with the underlying contract with regard to quantity. The bank cannot determine, nor can it refuse payment should it discover, that there are differences between the goods invoiced and the goods actually delivered to the purchaser, or that there are defects in the goods so delivered.
There are a limited number of exceptions relating to when the autonomy and independence of the credit agreement may be ignored and the terms and conditions of the underlying contract may be taken into consideration. The issuing bank may thus refuse to enforce the letter of credit when the underlying contract is contrary to law, good morals or public policy, or where there is fraud involved.
If the documents tendered by the beneficiary have been forged or deliberately falsified by beneficiary in order to comply with the requirements of the letter of credit while they do not in fact represent the goods or other performance specified, the beneficiary should not receive payment on the letter of credit. On the other hand, where the documents are neither forged or falsified, but where the purchaser discovers that the performance rendered by the beneficiary in terms of the underlying contract is defective or not in compliance with the stipulations of the underlying contract, the courts have indicated that they will not interfere by granting an interdict to

prevent the bank from paying on the letter of credit. However, where fraud on the part of the vendor has been alleged and proved by the purchaser a court will grant an interdict to prevent the bank from paying on the letter of credit.

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5. ELECTRONIC FUNDS TRANSFER

Payment (by means other than cash payments) usually comprises two basic steps:

1. the payment instruction is given by the debtor to the financial institution which holds the funds.
2. that financial institution will transfer the funds to the account of the beneficiary at the same or another financial institution.

These underlying principles stay the same, irrespective of whether the procedure is paper-based or purely electronic in nature.

An electronic fund transfer is therefore similar to a cheque in that the instruction is given by the customer to the bank for the transfer of money to another account or to the beneficiary. The only **difference** is that in the case of an electronic fund transfer, the instruction is given by means of electronic communication. In this sense, therefore, the bank acts as mandatory of customer and their legal relationship will be governed by the contract of mandate.

Different systems:
Electronic fund transfer systems divided into customer activated systems and systems which are activated by banks to facilitate electronic fund transfers between banks and to send financial messages.
Systems which are activated by banks
Electronic bank transfer systems can be used to send financial messages between banks. Although clearing houses are primarily used to bring about settlement between banks, they are also used to effect electronic fund transfers between banks. In South Africa, the Automated Clearing Bureau (Pty) Ltd, the ACB, is an example of such a clearing house. It is a company, which was established to provide for computerised facilities between banks.
Customer activated systems
There are mainly three electronic fund transfer systems which are activated by customers.
The first system is the ATM (automated teller machine) which can be described as an electronic vault allowing the user to withdraw or deposit money or obtain other banking services.
The second system is EFTPOS (electronic fund transfer at point of sale). In terms of this system, the consumer uses a terminal connected to the seller's cash register and pays electronically for goods purchased from the seller.

The agreed amount of the transaction is electronically transferred from the consumer's account to the seller's account and their respective accounts are debited or credited with the respective amounts.
The third system is home banking. The customer of a bank is able to transfer money between accounts or to check his or her balance by using a terminal or personal computer at home or by using a telephone connection between himself and the bank.

A.T.M (automated teller machine)
The ATM is a machine which is connected to the bank's computer system.
The customer can effect a variety of transactions using his savings or transmission accounts.
Access to the ATM is obtained by means of a plastic card with a magnetic stripe or a chip (containing encoded information) and a PIN (personal identification number). The advantages of customers using ATMs include the

- convenience of the customer being able to access his accounts 24 hours per day;
- the reduction in labour costs and in the volume of paper crossing the bank counter;
- an increase in the number of customers who can be served;
- and direct input of information into the bank's record-keeping system.

Operation of ATM
In an ATM transaction, the plastic card is inserted into the ATM and customer keys in his PIN. When the card is inserted, the encoded information on the magnetic stripe or smart card chip is read. This information identifies the card as a valid card in that system. The customer is required to enter the correct PIN. If the customer is still unsuccessful after a specified number of attempts the card is retained by the machine. As soon as the correct PIN is keyed in, the ATM displays certain information and gives instructions on screen so as to effect the desired transaction. If the customer correctly follows these instructions, the ATM completes the transaction, returns the customer's card and supplies a transaction slip.
ATMs can either be on-line or off-line.
When the ATM is on-line, it is directly linked to the bank's central computing system. This system can immediately (and in real time) check whether the customer has sufficient funds available in his account to cover the transaction as well as determine whether the card used is lost or stolen.
When an ATM works off-line, each transaction is recorded on a magnetic tape or a disk. At the end of each day a courier takes the tape or disk to the particular financial institution for processing.
The dangers associated with a system such this is, for instance, that the balance of the account holder may not be available on any particular day,

and that the banks are then exposed to the possibility of overdrawn account.
The possibility of the black list not having been updated timeously poses a further danger as it may happen that a lost or stolen card is used at such an ATM.

The risk of unauthorised withdrawals:

If an unauthorised person gains access to a customer's ATM card and PIN, the possibility of an unauthorised withdrawal arises. The machine cannot determine whether the person who inserts the card and keys in the correct number, is in fact an authorised person.
The ATM acts only on the card and the accompanying correct number. The question is whether the customer may be debited with the amount of such an unauthorised withdrawal.
This question will usually not arise because most financial institutions ensure that the contract that it concludes with a prospective customer contains a clause, which specifically excludes the bank's liability in such an instance. This term usually states that a customer's account may be debited with all withdrawals made by means of the particular card and accompanying secret number unless the bank is notified of a possible unauthorised withdrawal before it (the withdrawal) takes place.

A bank may only debit its customer if the bank has made payment to the customer or acted in accordance with his or her mandate. Entering in of the correct PIN is the customer's mandate for these purposes. In the absence of an express term there might quite possibly be a tacit term in the banker-customer contract that the customer would carry the risk of an unauthorised withdrawal. If a dispute arose between the bank and its customer, all of the surrounding circumstances, which exist at the conclusion of the contract, will be taken into account when the court has to determine the intention of the parties. A customer who obtains an ATM card realises that the whole system functions by means of a card coupled with a secret number. The customer also realises that the identity of the person who inserts the card and keys in the correct pin number, cannot be checked by the bank. The customer consents to accept his account being debited for any withdrawal made by means of the card and number until such time that the customer informs the bank of the loss and possible unauthorised use of the card.

A.T.M deposits

When a customer makes a deposit over the counter, he receives a copy of the deposit slip. This amounts to an admission by the bank that it has received the indicated amount. If a dispute arises as to whether the deposit was in fact made, this admission will place an onus of rebuttal on the bank. In the case of an ATM deposit, the customer does not enjoy this evidential advantage. The transaction slip supplied by the machine has small evidential value, because it’s a record of what the customer has keyed into

the machine. It does not prove that the customer has actually inserted the alleged amount in cash or a cheque for that amount into the machine.

If the deposit is made by means of a cheque, it is clear that payment to the bank takes place only when the cheque is honoured. Even when cash is deposited into an ATM, it seems that payment of such an amount takes place only when the contents of the envelope are removed by the official.
Only a contract of deposit exists while the envelope is in ATM. The depositary is liable for the loss of the property deposited with him, unless the depositary can prove that such loss was not due to his fault. If this contract of deposit between the bank and the customer were regarded as deposit without reward, the bank's liability would probably be limited to loss caused by intentional or grossly negligent conduct.
If the bank proves that the contents of the envelope deposited into the ATM were either lost or stolen without any fault on the bank's part, it would, therefore, not be liable as depositary towards the customer. If it is accepted that a cash payment already takes place when the money is placed into the machine, the bank would, as from that moment, already be the borrower of the money. Any subsequent loss would, therefore, be the bank's loss.

EFTPOS (electronic fund transfer at point of sale):
EFTPOS – "electronic fund transfer at point of sale".
This system makes it possible to make an electronic payment in a shop with a credit or debit card. In an on-line system the money is electronically transferred directly from the account of the cardholder to the account of the merchant. In an off-line system, the payment instructions are stored on a magnetic tape or disk for processing at a later stage.
Operation of EFTPOS
In an EFTPOS transaction, the customer presents either a debit card or a credit card to the merchant. The magnetic strip or smart card chip on the back of the card is swiped through a reader which is either held at the merchant's cash register or is wirelessly linked to the merchant's computerised payment system.
The customer chooses on a keyboard the account to be debited. The merchant keys in the value of the transaction and the customer keys in his PIN. The particulars of the transaction are then transmitted by the merchant's financial institution or switch network to the cardholder's financial institution.
The PIN and the particulars of the customer's account and the balance thereof are checked in order to determine whether there are sufficient funds. If it is accepted, the amount will be debited against the account of the customer and the merchant's account credited. An EFTPOS transaction is, therefore, essentially a debit transfer.
EFTPOS transaction - a PIN is used for authorisation. There are EFTPOS systems which still use handwritten signatures. The customers' card is swiped through a reader and duplicate transaction slips are printed which

must be signed by the customer. One copy of the transaction slip is kept by the merchant (and handed to the bank should a dispute arise) and the other is handed to the customer.

The legal relationships between the participating parties

EFTPOS transaction consist of a number of adjustments in the bank balances of the respective parties, payment will be complete when the funds are unconditionally credited to the beneficiary's account. This means that payment between the banks is complete when settlement has taken place. If payment to the beneficiary is complete but erroneous (either in terms of the person paid or the amount paid), the beneficiary will be liable for repayment. The grounds for the recovery of an erroneous payment will be unjustified enrichment unless other contractual remedies have been agreed to by the parties.

In an EFTPOS transaction there are at least three interdependent contracts, namely that between customer/merchant, customer/bank and merchant/bank.

Where more than one bank participates in the system, there will also be a further contractual agreement between the settlement banks.

The contract between the customer and the merchant

The contract between the customer and the merchant is a contract of purchase and sale in which the merchant either tacitly or expressly or by implication agrees to accept EFTPOS as a method of payment.

The contract between the customer (or EFTPOS cardholder) and his or her bank

The second contract is that between the customer or EFTPOS cardholder and his bank. Generally, the relationship between the customer and the bank is governed by the agreement, which was concluded when the card was issued to the customer. Although there are differences in the precise details agreed to by the different banks, there are certain standard terms that appear in all the contracts. The customer is liable for all EFTPOS transactions made with his card and/ or PIN, irrespective of whether the transactions are authorised by the customer or not. Contracts indicate that the customer will only be liable until the bank is informed of the loss of the card or the PIN.

A second term that is standard is the obligation of the customer to keep the PIN a secret. If the PIN is correctly inputted even by an unauthorised person, the contractual conditions under which cards are issued make the customer responsible for loss suffered (unless the customer has informed the bank about the loss of the PIN).

A third important standard term is that the EFTPOS transaction is irrevocable. An EFTPOS payment cannot be reversed if the customer decides to return the goods purchased to the vendor. This means that the customer has to take recourse against the vendor directly and claim the money from the vendor.

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The contract between the merchant (vendor/seller) and the bank

The third contract is that between the merchant and the bank. This contract usually takes the form of a standard commercial bank account contract containing particular terms relating to EFTPOS payments. The most important of these relate to the time at which the merchant's account at the bank will be credited with an EFTPOS payment, and to the procedures for dealing with erroneous or unauthorised transactions.

One of the inherent risks is that a customer may not have sufficient funds in his account to pay for the goods or services purchased. The merchant in such a case is only authorised to accept purchases by means of EFTPOS up to a specified amount.

Off-line system problem = is whether the original claim (personal right) of the merchant against the cardholder is extinguished by novation. In other words, may the merchant still claim from the customer if the card issuer or financial institution does not pay?

In an off-line system, the bank undertakes to pay all payment instructions, which are accepted by the system provided that the merchant has complied with certain security procedures (such as checking the cardholder's signature or the so-called black list of stolen or lost cards). In an on-line system, if the payment instruction is accepted, the bank will execute payment, not because of the bank's undertaking, but as mandatory of the customer.

The financial institution or bank will naturally also require the merchant to keep secret all information about the customer, which comes to his knowledge. The merchant will furthermore have to take care that no unauthorised person obtains access to the EFTPOS system.

Home banking (via the telephone or the Internet)

Home banking gives the consumer the opportunity to make use of several financial services from the privacy of the home by using a telephone or the Internet. These include checking of account balances, asking for provisional statements, transferring funds between accounts, payment of creditors, ordering a cheque book, obtaining financial market information, etc.

The advantages of internet banking includes the convenience in terms of time and cost of not being restricted to transacting at a bank or an ATM machine.

The risks of home and Internet banking services

In agreements concluded with customers for the provision of home bank services, the banks usually exclude their liability for any damage that the customer may sustain for using the home banking service. This includes not being liable for damages sustained because of the malfunction of either the customer's computer or the bank's computer system. The bank will not be liable for the erroneous or non-timeous performance of the customer's instruction as a result of any of the above-mentioned circumstances. The

banks also do not accept liability for any damage the customer may sustain as a result of the fact that the service was not available at any given time.
Access to the home banking system is gained through the use of certain codes, which are only made known to the customer.
Similar to a PIN, keeping these codes secret is an NB component in safeguarding the system. The obligations imposed on a client are broadly documented in the contract between the bank and its client. Not only is the client obliged to control and limit access to the system but is also obliged to keep secret all access codes, technical data and all information which pertains to the service and system. Such information may be made available only to authorised persons or employees of the customer.

The banks, thus, do not accept liability for any damage which is sustained as a result of a person's obtaining unauthorised access to the system by using equipment which is in the possession or under the control of the customer. In the agreements between banks and their customers it is, therefore, usually determined that any instruction or transaction which is initiated by the system, is regarded as having been given or initiated by the customer or someone authorised by him or her.

Example of a question:
(1) What is an electronic fund transfer?
(2) Name two main electronic funds transfer systems.
(3) Name three main electronic funds transfer systems which can be activated by customers.
(4) What is EFTPOS?
(5) Name three important interdependent contracts in an EFTPOS transaction.
(6) What is home banking?
(7) What are the advantages of home banking?

(1) An electronic fund transfer can be described as a funds transfer that is effected largely or completely by electronic techniques. It works just like a cheque in that an instruction is given by the customer to the bank for the transfer of money to another account.
(2) Electronic fund transfer systems can be divided into customer activated systems and systems which are activated by banks to facilitate electronic funds transfers between banks.
(3) ATM, EFTPOS and home banking.
(4) EFTPOS is an acronym for electronic funds transfer at point of sale, a system which makes it possible to make an electronic payment in a shop with a credit or debit card.
(5) The customer/merchant contract, the contract between the customer or EFTPOS cardholder and his bank and the contract between the merchant and the bank. Discuss each briefly.

(6) Home banking gives a customer the opportunity to make use of several financial services from the privacy of the home by using a telephone, videotex services and the Internet.
(7) It is possible to check balances, ask for statements, transfer funds between accounts, stop payment of cheques, order cheque books, obtain financial information and correspond with the bank manager

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INTELLECTUAL PROPERTY LAW:

COPYRIGHT:

Section 2 of the Copyright Act provides that the following works, if original, shall be eligible for copyright:
(a) literary works
(b) musical works
(c) artistic works
(d) cinematograph films
(e) sound recordings
(f) broadcasts
(g) programme-carrying signals
(h) published editions
(i) computer programs

** Literary works
Definition: includes
novels, stories and poetical works, dramatic works, stage directions, cinematograph film scenarios, textbooks, treatises, histories, biographies, essays and articles, encyclopedias and dictionaries.
** Musical works
Definition: A musical work is defined in s 1(1) as
a work consisting of music, exclusive of any words or action intended to be sung, spoken or performed with the music.
** Artistic works
Definition: In terms of s 1(1), the concept ``artistic work'' includes, irrespective of the artistic quality thereof, the following:
(a) paintings, sculptures, drawings, engravings and photographs
(b) works of architecture (being either buildings or models of buildings).
** Computer Programs:
Section 1(1) of the Copyright Act now defines a computer program as
a set of instructions fixed or stored in any manner and which, when used directly or indirectly in a computer, directs its operation to bring about a result - a work will be regarded as a computer program only once it has reached the stage of development where it can be used, directly or indirectly, in a computer.

THE REQUIREMENTS FOR THE SUBSISTENCE OF COPYRIGHT IN A WORK:

Inherent requirements

1. Originality
- Section 2(1) states that a work is not eligible for copyright unless it is original.
- There is no definition of what will be regarded as original works for purposes of the Act.
- To enjoy the benefit of copyright protection, the work must emanate from the author himself and must not be copied from some other source. The requirement of originality is the product of this principle.
- Originality = originality of thought or the expression of thought, to original skill or labour in executing the work. Thus where two authors working independently of each other arrive at the same result, each may obtain for his result the protection accorded an original copyright work.

2. Material Embodiment:
- A work, other than a broadcast or programme-carrying signal, shall not be eligible for copyright unless it has been written down, recorded, represented in digital data or signals, or otherwise reduced to a material form.

Formal requirements:

1. Author a qualified person
definition of a qualified person:
In terms of s 3(1), a qualified person is:
(a) in the case of an individual, a person who is a South African citizen or is domiciled or resident in the Republic; or
(b) in the case of a juristic person, a body incorporated under the laws of the Republic.

2. Works first published or made in the Republic
In terms of s 4(1), copyright shall be conferred on every work which is eligible for copyright and which is first published or made in the Republic. In this case the person making the work does not have to be a qualified person.

The author and the owner of copyright: NB!

The author

The Act defines the term author in s 1(1) as meaning, in relation to
(a) a literary, musical or artistic work, the person who first makes or creates the work;
(b) a photograph, the person who is responsible for the composition of the photograph;
(c) a sound recording, the person by whom the arrangements for the making of the sound recording were made;
(d) a cinematograph film, the person by whom the arrangements for the making of the film were made;
(e) a broadcast, the first broadcaster;
(f) a programme-carrying signal, the first person emitting the signal to a satellite;
(g) a published edition, the publisher of the edition;
(h) a literary, dramatic, musical or artistic work or computer program which is computer-generated, the person by whom the arrangements necessary for the creation of the work were undertaken;
(i) a computer program, the person who exercised control over the making of the computer program.

Someone other than the true creator of the work may qualify as its author. It is not necessarily the photographer, for example, who will qualify as the author of the photograph taken by him or her; it could be someone else - if that other person was responsible for the composition of the photograph.

The first owner of copyright:

The **general rule** is that the author of a work will also be the first owner of the copyright therein (**s21(1)(a)).**
However, there are three categories of exceptions to this rule which are contained in s21(1)(b), (c), and (d).

1. Where a literary or artistic work is made by an **author in the course of his employment** by the proprietor of a newspaper, magazine or similar periodical under a **contract of service** or apprenticeship, and is in fact made for the **purpose of publication** in a newspaper, magazine or similar periodical, **that proprietor** (the employer) shall be the **owner of the copyright** in the work for **purposes of such publication** in a newspaper, magazine or similar periodical (s 21(1)(b)).
   This exception applies only to literary and artistic works, and only affects specific employment situations. The copyright in the work vests in

the proprietor (the employer) **only in so far as it relates to the publication thereof in a newspaper, magazine or similar periodical. In all other respects** (eg the publication of the work in book form), the author will be the owner of the copyright subsisting in the work.
TO REMEMBER THE SECTION NUMBER, THINK ALL EXCEPTIONS ARE S21(1) SO THE ONE APPLICABLE TO A JOURNALIST FOR A NEWSPAPER ETC IS "(b) SO THIS IS "BEELD"!"

2. Where a person commissions the taking of a photograph, the painting or drawing of a portrait, or the making of a gravure or a cinematograph film or a sound recording and pays for it in money or money's worth, that person (the person who commissions) shall (subject to the provisions of the preceding subs (b)) be the owner of the copyright in the work (s 21(1)(c)).
   In this case only specific works are affected, namely photographs, painted or drawn portraits, gravures, cinematograph films and sound recordings.
   TO REMEMBER THIS SECTION – "COMMISSION IS (c)!"

3. Where a work is made in the course of the author's employment by another person under a contract of service or apprenticeship, in a case not falling within either subs (b) or (c), that other person (the employer) shall be the **owner** of the copyright in the work (s21(1)(d)). HERE EMPLOYER THE OWNER FOR GOOD, NOT LIKE IN (b) ABOVE.
   This exception applies to all works, except those falling under subss (b) or (c).

4. These exceptions to the general rule that the author of a work will also be the first owner of the copyright therein (subss (b), (c) and (d)) can be excluded by way of agreement between the parties involved (s 21(1)(e)). REMEMBER THIS SECTION AS "EXCEPTIONS IS (e)."

INFRINGEMENT OF COPYRIGHT

- When a work is protected by copyright, the copyright owner has the exclusive right to perform certain acts or to authourise the performance of these acts in relation to the work.
- Sections 6-11 of the Copyright Act contain provisions for each of the categories of works, setting out which acts may be done or authorised exclusively by the copyright owner.

Exclusive rights:
For example, s 6 of the Act provides that the copyright owner of a literary or musical work has the exclusive right to do or to authorise the doing of the following acts:

- **the reproduction of the work;**
- **its publication;**
- **its performance in public;**
- **a broadcast of the work;**
- **the making of an adaptation of the work**.

An adaptation with reference to a literary work also means a translation of the work.

Exclusive rights: computer programs:
Section 11B provides that, in relation to a computer program, only the copyright owner may do or authorise the following acts:

- the reproduction of the computer program in any manner or form;
- the publication of the computer program if it was as yet unpublished;
- making an adaption of the computer program;
- reproducing or publishing an adaptation of a computer program; or
- letting, or offering or exposing for hire by way of trade, directly or indirectly, a copy of the computer program.

Direct infringement:
Copyright infringement can be either direct or indirect. The infringement is direct when the infringer does, or causes any other person to do, any of the acts specifically designated in the Act as the sole prerogative of the copyright owner, without having obtained the permission of the copyright owner.
A copyright owner has the exclusive right to make a reproduction (copy) of an existing copy of his work (indirect copying). The making of a copy of an intervening copy of a work thus also amounts to a direct infringement of the copyright in the original work.
Indirect infringement:
Copyright infringement is indirect when the infringer, although not actually committing any of the acts so designated, knowing that it would constitute an infringement, commits the acts mentioned as infringement (above).
Examples of indirect infringements:

- the importation of an infringing article for a purpose other than for the
- infringer's private or domestic use;
- the selling or letting, or the offering by way of trade for sale or hire, of
- such an article;
- acquiring an article relating to a computer program in the Republic; and
- permitting a place of public entertainment to be used for a public
- performance of a literary or musical work.

One of the exclusive rights of the copyright owner of a literary work is to reproduce the work in any manner or form.
If a person makes a copy of the work, without the consent of the copyright owner, he commits an act of direct infringement.
If he knowingly, and without the consent of the copyright owner, imports into the Republic for a purpose other than his private and domestic use an infringing copy already in existence, he commits an act of indirect infringement.

STATUTORY DEFENCES TO INFRINGEMENT:

There are certain acts which the copyright owner has the exclusive right to do or to authorise. If another person performs any of these acts without the authorisation of the copyright owner, he infringes directly the copyright owner's copyright.

Statutory defences to infringement:

1. Fair dealing
Regarding literary, musical and artistic works, cinematograph films, sound recordings, broadcasts, published editions and computer programs (ie all works except programme-carrying signals), the following acts shall not constitute copyright infringement:
Fair dealing with a work,
1. for the purpose of research or private study or for the purpose of personal or private use
2. for the purpose of criticism or review of that work or another work
3. for the purpose of reporting current events
(a) in a newspaper, magazine or similar periodical
(b) by means of broadcasting or in a cinematograph film
However, before someone will be able to rely on a defence of fair dealing, certain principles apply: the making of a copy of the whole or of a substantial portion of the work concerned will not be permitted; and in cases (2) and (3)(a) above the source must be mentioned as well as the name of the author if it appears on the work.

2. Judicial proceedings
This refers to the use of the work for the purposes of judicial proceedings, or reproducing it for the purposes of a report for judicial proceedings.

3. Illustration
This refers to the use of the work by way of illustration in any publication, broadcast or sound or visual recording for the purpose of teaching.

However, before someone will be able to rely on this defence, certain conditions apply:
** he must mention the source of the work and
**the name of the author if it appears on the work, and
**his use of the illustration must be ``compatible with fair practice'' and to the extent ``justified by the purpose''.

4. Bona fide demonstration
This refers to the use of a work in a bona fide demonstration of radio or television receivers or any type of recording equipment or playback equipment to a client by a dealer in such equipment. (Eg. X, a salesman playing Britney Spears on a hi-fi he is trying to sell to Y, to illustrate the quality of the system).

5. Quotations
With regard to literary and musical works, cinematograph films, sound recordings, broadcasts and computer programs (all works except artistic works, programme-carrying signals and published editions), copyright shall not be infringed by any quotation from a work which is lawfully available to the public.
The following conditions apply:
**the source must again be mentioned and
**the name of the author if it appears on the work and
**the quotation must be compatible with fair practice and may only be used to the extent justified by the purpose.

6. Broadcasts
With regard to literary, musical and artistic works, sound recordings, published editions and computer programs, copyright shall not be infringed by the reproduction of the work by a broadcaster by means of its own facilities where such reproduction or any copy of it is intended exclusively for lawful broadcasts of the broadcaster.

7. Information purposes
With regard to literary and musical works only, copyright in a lecture, address or other work of a similar nature which is delivered in public shall not be infringed by reproducing it in the press or broadcasting it, if such reproduction or broadcast is for informative purposes.

8. Background inclusion
With regard to artistic works only, copyright shall not be infringed if it is included in a film, a television broadcast or transmission in a diffusion service, if such inclusion is merely by way of background, or incidental to the principal matters represented in the film, broadcast or transmission. Also applies with regard to the inclusion in the abovementioned media of

such works of art as are permanently situated in a street, square or similar public place.

9. Three-dimensional reproductions

s15(3A) Copyright in an artistic work shall not be infringed where a three dimensional reproduction of an artistic work is copied if

- the three-dimensional reproduction has already been made available to the public with the consent of the copyright owner;
- the three-dimensional reproduction has primarily a utilitarian purpose;

and

- it has been made by an industrial process

ABC Cars, a car manufacturer, has the copyright in the production drawing of a spare part. The production drawing is a two-dimensional utilitarian artistic work. ABC Cars manufactures this spare part by an industrial process and sells it to the public. The manufactured spare part is a three-dimensional reproduction of the production drawing. BEN's Cars obtains one of these spare parts (ie. the three dimensional reproduction of ABC Car's artistic work) and copies it. BEN's Cars will not infringe on ABC Car's copyright in the two-dimensional utilitarian artistic work.

10. Excerpts

With regard to programme-carrying signals, copyright in such signals shall not be infringed by the distribution of short excerpts of the programme so carried

- that consist of reports of current events; or
- that are compatible with fair practice, and to the extent justified by the informative nature of such excerpts.

However, if the programme-carrying signal represents a sporting event, this exception shall not apply.

11. Backup copies

A person who is in **lawful** possession of a computer program or has an authorised copy of the computer program (eg. An employee at that moment in time) shall not infringe the copyright in the computer program if:

- he makes copies reasonably necessary for backup purposes;
- a copy so made is intended exclusively for personal or private purposes;

and

- he destroys the backup copies when possession of the computer program in question, or authorised copy thereof, ceases to be lawful.

The person in possession of an authorised copy of a computer program may make copies thereof to the extent that it is reasonably necessary for backup purposes, but such copies may only be used for the person's personal or

private purposes. Furthermore, such copies must be destroyed when the possession of the computer program **ceases to be lawful** (eg he leaves the employ).

No copyright protection

Where a person performs any of the acts listed above, he will not infringe copyright. Apart of these acts, the Act also provides (in s 12(8)) that certain works will not enjoy copyright protection at all. This means that these works may be used freely, and that any such uses will not amount to copyright infringement.

The following do not enjoy copyright protection:

- official texts of a legislative, administrative or legal nature
- official translations of such texts
- speeches of a political nature or in speeches delivered in the course of
- legal proceedings
- news of the day which consists merely of items of press information

REMEDIES FOR INFRINGEMENT:

Section 24(1): a copyright owner may institute an action for copyright infringement, and that relief would be available to him as would be the case in any corresponding proceedings in respect of infringements of other proprietary rights.

The following relief is available to the copyright owner in event of infringement of his rights:

- damages
- interdict
- delivery of infringing copies, or plates used or intended to be used for
- infringing copies
- additional damages (s 24(3))

DURATION OF COPYRIGHT

- General rule, a work enjoys copyright protection for a period of 50 years calculated from the end of the year in which the author of the work dies (s 3(2)(a)).
- This means that a work enjoys copyright protection for the lifetime of the author plus 50 years. This rule applies to literary, musical and artistic works (excluding photographs). The copyright owner is not necessarily the author of a work. The period of protection is determined with reference to the lifetime of the **author.**
- Copyright in computer programs, photographs and cinematograph films subsists for a period of 50 years from the end of the year in which the work was made available to the public with the consent of the owner of the copyright, or in which it was first published. Where the work has not been made available to the public or published

within 50 years from the making of the work, the duration of copyright is 50 years from the making of the work, calculated from the end of the year in which the work is made (s 3(2)(b)).

POSSIBLE QUESTIONS:

Mr Will – I -Am, a journalist employed by "TWEET", a celebrity magazine, writes a series of articles on Sharon D, a famous South African Actress. "TWEET" buys photographs of the famous actress from a freelance photographer, and publishes these together with the articles.

(a) Who will be the author and the copyright owner of these articles? Give reasons for your answers. (3)

(b) Mr Will – I - Am makes a compilation of the series of articles and publishes the articles together with the photographs it in a book. Will his book infringe copyright in the articles and the photographs? (2)

(c) "SHARE-IT", a rival magazine of "TWEET", instructs a famous comic artist, Barry H, to draw a series of comic strips based on the articles that appeared in "TWEET". Will the comic strip infringe copyright? Will it enjoy protection? (2)

(d) Who will be the author and the copyright owner of the comic strip? Give reasons for your answers. (3)

(a) The author is the journalist, creator of the work.
The copyright owner is the proprietor of "TWEET", as this is a literary work in the course of employment by the proprietor of a newspaper, magazine or similar periodical under a contract of service, the proprietor is the copyright owner for purposes of such publication in a newspaper.

(b) No, for purposes other than publication in the newspaper, the author retains copyright in the article. The author does however not own the copyright in the photographs and will therefore infringe the copyright in the photographs.

(c) It will infringe copyright as its an unauthorized adaptation. It will, however, still enjoy protection, but each time exploited it will constitute a new infringement (section 2(3)).

(d) The author is Barry H as he is the creator of the work
The copyright Owner is "SHARE - IT" as they commissioned and paid Barry H. (s21(1)(c).

Sello, the owner of Sello's Motor's and Spares, makes a production drawing of a new spare part he developed which will fit any make of vehicle. Sello then uses the production drawing to manufacture the spare part.

(a) Name the requirements for the subsistence of copyright in Sello's production drawing. (5)
(b) Benny, an employee of Sello, makes a reproduction of the drawing without Sello's permission. Will Benny infringe Sello's copyright in the production drawing? (2)
(c) Tracey, owner of Technical Tracey and a rival of Sello, uses Sello's three-dimensional spare part, and makes her own version from it. Will Tracey infringe Sello's copyright if she makes this reproduction without Sello's permission? (4)

a) The work must meet the inherent and formal requirements for the subsistence of copyright, then it will achieve copyright protection. The inherent requirements are originality and material embodiment. The formal requirements are either that the author must be a qualified person or that the work was first made in South Africa.
b) Yes, infringement takes place when the infringer does, or causes any other person to do, any of the exclusive acts specifically designated in the Act as the sole prerogative of the copyright owner without permission. Reproduction is an exclusive right of the copyright owner.
c) No, this is due to the operation of s15(3A), and the defence of three-dimensional reproductions.
Copyright in an artistic work shall not be infringed where a three-dimensional reproduction of an artistic work is copied if
- **the three-dimensional reproduction has primarily a utilitarian purpose;**
- **it has been made by an industrial purpose.**

Maggie is the owner of Fancy Bags magazine. As he did not find the time to do his own research for an item on Louis Vitton bags, she translates an article that she found on the Internet. Maggie's translation is published in the next edition of Fancy Bags magazine.
Accept that copyright subsists in the Internet article.
Does copyright subsist in Maggie's translation? (4)

Maggie's translation can be protected in terms of copyright, as long as the requirements for the existence of copyright are complied with. S2(3) of the Act states that a work wont be ineligible for copyright only because the making of the work involved an infringement of copyright in some other work – thus Maggie's translation is eligible for copyright even though the making thereof involved an infringement of copyright in an internet article. The requirements for copyright to exist in the translation are:
a) originality;

b) material embodiment and:
c) That Maggie should be a "qualified person" or that the relevant edition of the magazine "Fancy Bags" was first published or made in SA. Maggie will, however, not be able to make use of her copyright, if it does qualify, without infringing the copyright in the internet article.

Kate is starting her own business. She asks Kathy, a freelance graphic designer, to design a logo. Kate is happy with the end result and right away pays Kathy in full.
Accept that copyright subsists in the logo.

1. (a) Who is the author of the logo?

A logo is an "artistic work" in terms of the Act and the author of an artistic work is defined in terms of s1 – "the first person who makes / creates the work". Thus Kathy is the author of the logo.

2. (b) Who is the owner of the copyright in the logo?

There is a general rule in terms of s21(1)(a) that the first owner of the copyright is the author of the copyright. There are exceptions to s21(1) but none of these apply, and thus Kathy is also the first owner of the logo s21(1)(c) doesn't apply here even though Kathy is "freelance" and Kate commissioned her because s21(1)(c) is limited to photos; portraits; gravures; cinematograph films and sound recordings – a logo is part of graphic design – doesn't fall into any of these!

3. (c) What is the duration of the copyright in the logo?

According to the general rule, the duration of a copyright would be the life of the author and 50 years from the end of the year in which the author dies – Kathy.

Koos is employed by PearMac, which is a worldwide software company. He makes a sketch of a "flow chart" to show the creation of a computer program, for the playing of games on a laptop / computer. The game will be called "Gamer".
a) Identify the relevant copyright work/s and its author/s. (4)

The author of a computer program, in this question – Gamer – is the person who exercised control over the making of the computer program. The flow chart is deemed to be a literary work in terms of the Act and the author of the literary work is the maker or the creator of the work.

b) During his employment period with PearMac, Koos makes copies of Gamer for back-up purposes. Will this amount to copyright infringement?

A person may, in terms of the Act, make back-up copies of the program if he is in possession of an authorized copy of the program (which Koos is); he makes copies reasonably necessary for back-up purposes (which he did); the copies are used for only his personal / private purposes; and the copies are destroyed when possession of the program or authorized copies ceases to be lawful. In the question, Koos made copies during his employment with PearMac, and if he used them for private purposes, he wont infringe copyright – and he must destroy them if he leaves the employ of PearMac.

c) PearMac dismissed Koos for operational reasons as their finances are in trouble. Koos reproduces one of the back-up copies of Gamer and sells the reproduction to an OrangeMan shop. Will this amount to infringement?

S11 of the Act provides that the copyright owner has the exclusive rights to do / authorize to reproduce the computer program in any manner or form. Direct infringement takes place when the infringer does any of the acts mentioned in s11 without the permission of the owner. Thus, Koos will be infringing copyright if he reproduces one of the back-up copies and sells it without PearMac's permission.

a) Nellie is a postgraduate student in physics. Nellie writes a dissertation on 'Quantum Physics in 2012'. Nellie makes extensive use of a book entitled 'Quantum Physics USA'. Will this use amount to copyright infringement? (2)

Direct infringement takes place when the infringer does any of the acts mentioned in s6 without the permission of the owner. The owner has the exclusive right to do / authorize the reproduction of the literary work (the book). Therefore, Nellie will infringe the copyright in the literary work if she reproduces a substantial part of the work.

b) Will there be any statutory defence on which Nellie can rely? (4)

There are various defences available in terms of the Act, which then don't amount to infringement. S12(1) deals with "fair dealing" with a work for the purposes of research or private study. But the making of a copy of the whole / substantial portion of the work concerned will not be permitted. Nellie could thus rely on "fair dealing" for research purposes .

c) In her dissertation, Nellie refers to various books and journals. Does the dissertation comply with the requirement of originality? Discuss this requirement. (4)

The requirements for copyright to exist in a work, requires that the work be original (amongst others). Thus, to be original, the work must emanate from the author herself and must not be copied from some other source. Originality refers to the original skill and labour in the making of the work. If one uses other works to make one's own work, the work must be more than a "slavish" copy of that subject matter. The author must have spent sufficient time; skill and labour on his work, which the material he uses doesn't possess and which then distinguishes his work from the material he used.

Jasper has been employed full time as a journalist of Great Muso's Magazine for 10 years. His job is to write entertaining stories on SA's musicians, for the middle section of the magazine of every edition. He is then approached by ZYZ Publishers who would like to publish a couple of his stories from the Great Muso's Magazine but in book form.

a) Who is the author of the stories? (2)

The author of a literary work, according to the Act, is the creator or maker of the work, here then is Jasper.

b) Who is the owner of the copyright in the stories for the purposes of the publication in book form? (2)

The general rule in terms of s21(1)(a) is that the author of the stories is the first owner. As a journalist employed by a periodical (magazine), the proprietor of the magazine is the owner of the stories FOR THE PUBLICATION of the story – s21(1)(b) - Where a literary or artistic work is made by an author in the course of his employment by the proprietor of a newspaper, magazine or similar periodical under a contract of service or apprenticeship, and is in fact made for the purpose of publication in a newspaper, magazine or similar periodical, <u>that proprietor</u> (the employer) shall be the <u>owner of the copyright</u> in the work for <u>purposes of such publication</u> in a newspaper, magazine or similar periodical (s 21(1)(b)). For the publication of the stories in book form, it is Jasper who is the owner.

c) What is the duration of the copyright in the stories? (2)

The Act states that the duration of a copyright in a literary work is the lifetime of the author (Jasper) & 50 years from the end of the year in which the author dies.

Discuss the inherent requirements for the subsistence of copyright in a work. (10)

There are inherent and formal requirements for the subsistence of copyright in a work. Both the inherent and formal requirements should be met before copyright will exist in a work. The inherent requirements relate to the work itself. There are two inherent requirements namely originality and material embodiment.
<u>Originality</u>: Section 2 states that a work is not eligible for copyright unless it is original. This means that the work must emanate from the author himself or herself and must not be copied from some other source. Originality refers not to originality of thought or the expression of thought, but simply to original skill or labour in executing the work. Thus where two authors working independently of each other arrive at the same result, each may conceivably obtain for his result the protection accorded an original copyright work.
Although the work must emanate from the author himself or herself in order to be original, it does not mean that the work must emanate in its entirety from the author and that no use may be made of existing subject-matter. Originality means that where use is made of existing subject-matter, the work must be more than a mere slavish copy of such subject-matter.
The author will be required to expend sufficient skill or labour to impact to this work some quality or character which the material he uses does not possess and which substantially distinguishes the work from that material. Section 2(3) states that a work shall not be ineligible for copyright by reason only that the making of the work involves an infringement of copyright in some other work. This means that copyright can subsist in a work that infringes another copyright work provided that the infringing work itself meets the requirements for copyright protection.
<u>Material embodiment</u>: A work should exist in some or other material form before it qualifies for copyright protection. Section 2(2) states that a work, other than a broadcast or programme carrying signal shall not be eligible for copyright unless it has been written down, recorded, represented in digital data or signals, or otherwise reduced to a material form. A work should both be original and embodied in material form before copyright will subsist therein.

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You are a practising lawyer. Your firm specialises in intellectual property law. Each day you encounter different problems in this field of law. Answer the following questions with reference to relevant case law.

You are instructed to write a legal opinion. You base your whole opinion on an article published in a legal journal. You only translate the article and make a few minor adjustments. You do not acknowledge the source of the article or the name of the author.

a) Will your legal opinion infringe the copyright in the article?

Direct infringement of copyright takes place when the infringer does any of the acts specifically designated in the Copyright Act as the sole prerogative of the copyright owner, without having obtained the permission of the copyright owner.
Section 6 provides that the copyright owner of a literary work has the exclusive right to do or authorise to do the following acts the reproduction of a work, its publication, its performance in public, a broadcast of the work, the making of an adaption of the work, etc. An adaption with reference to a literary work means a translation of the work. You made a translation of the literary work without obtaining the copyright owner's permission.
The Act, however, lists a number of acts the doing of which will not amount to an infringement of the copyright. It thus constitutes a number of defences which can be relied upon by a defendant in the event of an action for infringement.
In terms of section 12(1) the fair dealing with a work for the purpose of research shall not be regarded as constituting an infringement for the purpose of copyright protection. The making of a copy of the whole or a substantial portion of the work concerned will not be permitted. Since you translated the whole of the work you cannot rely on this defence.

You infringed the copyright owner of the article's copyright.

b) Will copyright subsist in your legal opinion?

Copyright can subsist in a work which infringes another copyright work. The mere fact that the translation is an unauthorised adaption will thus not preclude copyright from subsisting in the translation. Provided the work meets the inherent and formal requirements for the subsistence of copyright, it will attain copyright protection independently from the original work. Copyright will vest in the maker or creator of the work (you). The nature of copyright in the translation will be the same as that of other literary works, but it

should be noted that every time you exploit your work (e.g. by making a reproduction), you will infringe copyright in the original work.

TKZ is a Kwaito band. Jazz, an employee of Kick Ass Records, writes a song for TKZ to sing. Kick Ass records the song and instructs Pete, a freelance photographer, to take TKZ's photo for the cover of the album.

7.1 Identify the specific works which are eligible for copyright protection. (2)

- **A musical work**
- **A literary work - the words that constitute the song**
- **An artistic work - a photograph is an artistic work**
- **A sound recording**

7.2 Who is the author of each of the specific works? (4)

- **Jazz is the author of the musical work because Jazz is the maker or creator of the musical work.**
- **Jazz is the author of the literary work because Jazz is the maker or creator of the literary work because he wrote lyrics.**
- **Pete is the author of the artistic work because he is responsible for the composition of the photograph.**
- **Kick Ass Records is the author of the sound recording because it is responsible for the arrangement for the making of the sound recording.**

7.3 Who is the copyright owner of each of the specific works?

The general rule in terms of the Act, is that the author of the work will be the first owner of the copyright, s21(1)(a). there are exceptions in terms of s21(1)(b)-(e).
Kick Ass is the copyright owner of the musical work and the literary work because Jazz is in its employment (section 21(1)(d)). Thus, the exception applies and not the general rule.

Kick Ass Records is the copyright owner in the photo, an artistic work, because it commissioned and paid Pete to take the photo (section 21(1)(c)).

Kick Ass Records will be the copyright owner of the sound recording because it is generally accepted that the author is the owner of copyright.

Bernard is the owner of a small factory that produces designer stationery. It has come to his attention that some of his products, such as letter openers with ornamented handles, are being reproduced by another manufacturer. Bernard wants to institute an action for copyright infringement against the other manufacturer.
Is there a statutory defence that the other manufacturer can rely on? Explain. (5)

s15(3A) Copyright in an artistic work shall not be infringed where a three dimensional reproduction of an artistic work is copied if

- **the three-dimensional reproduction has already been made available to the public with the consent of the copyright owner;**
- **the three-dimensional reproduction has primarily a utilitarian purpose;**
  and
- **it has been made by an industrial process**

If Bernard's letter openers are available to the public and are 3d, they may be copied. If they are in an artistic format, they are protected.

TRADE MARKS:

Section 2(1) of the Trade Mark Act contains the following definition of a trade mark:

- "trade mark", other than a certification mark or collective mark, means a mark used or proposed to be used by a person in relation to goods or services for the purpose of distinguishing the goods or services in relation to which the mark is used or proposed to be used from the same kind of goods or services connected in the course of trade with any other person.

Definition of mark:
"Mark" is defined in s 2(1) as follows:

- "Mark" means any sign capable of being represented graphically, including a device, name, signature, word, letter, numeral, shape, configuration, pattern, ornamentation, colour or container for goods or any combination.

- A "certification mark" is specifically excluded from the definition of a trade mark.
- A certification mark is a mark used upon or in connection with goods or services to certify that they have been examined with regard to kind, quality, quantity, intended purpose, value, geographical origin, mode or time of manufacture, or other characteristic, by government or provincial authority, association or person. Section 42 authorises and regulates the registration of such certification marks, the purpose of which is not, like ordinary trade marks, to distinguish goods or services, but rather to certify goods or services in regard to certain qualities. Well-known certification marks include the Woolmark and the SABS mark.
- A "collective mark" is also excluded from the definition of a trade mark.
- A collective mark is a mark used upon or in connection with goods or services to indicate that they are goods or services of members of a particular association.
- Whereas a certification mark serves to distinguish goods or services certified by the proprietor in respect of quality or some other characteristic, a collective mark serves to distinguish the goods or services of members of an association from the goods or services of non-members.

REQUIREMENTS FOR REGISTRATION

- Capable of distinguishing
- Section 9(1) of the Trade Marks Act states the following:

- In order to be registerable, a trade mark shall be capable of distinguishing the goods or services of a person in respect of which it is registered or proposed to be registered from the goods or services of another person …
- Section 9(2) of the Trade Marks Act provides the following in this regard:
- A mark shall be capable of distinguishing … if, at the date of application for registration, it is inherently capable of so distinguishing or it is capable of distinguishing by reason of prior use thereof.

- A trade mark can lose its capability of distinguishing. This can happen where the public accepts such a mark and starts to use it, no longer as a trade mark or trade name, but rather as the general name of the class of goods concerned. This has taken place, for example, in the case of the marks “Aspirin” and “Cellophane”, “lip-ice”.

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Restrictions on registration

Section 10 of the Act sets out a number of grounds on which the registration of a trade mark may be refused. (These also provide the grounds on which a trade mark registration may be removed from the register.)

Absolute grounds for refusal

These grounds relate to the inherent unregisterability of marks, the applicant for registration and his conduct, marks applied for in bad faith, and deceptive marks.

- A mark which does not constitute a trade mark cannot be registered (s10(1) and (2)).
- A mark which is not capable of distinguishing the goods or services of the proprietor from the goods or services of another person cannot be registered (s10(2)(a)). A mark which serves, in trade, to designate the kind, quality, quantity, intended purpose, value, geographical origin or other characteristics of the goods or services, or the mode or time of production of the goods or the rendering of the services, cannot be registered (s 10(2)(b)). These marks are not registrable because they are not capable of distinguishing. These words or signs are usually, although not necessarily, descriptive or laudatory, for example "perfection", "marvelous" for any type of goods or services, or "dry white" for wine.
- A mark cannot be registered if it consists exclusively of the shape, configuration, colour or pattern of goods where the shape, configuration, colour or pattern is necessary to obtain a specific technical result, or results from the nature of the goods themselves (s10(5)).
- A mark which consists of a container for goods or the shape, configuration, colour or pattern of goods cannot be registered where the registration of such a mark is likely to limit the development of any art or industry (s10(11)).
- A mark cannot be registered where the applicant has no bona fide claim to proprietorship (s10(3)).
- A mark cannot be registered where the applicant has no bona fide intention of using the mark as a trade mark himself or through a licensee (s10(4)).
- A mark cannot be registered if the application was made mala fide (s10(7)).
- A mark which consists of or contains the national flag of the Republic or any convention country (that is a country which is a member of the International Convention for the Protection of Industrial Property) cannot be registered (s 10(8)), a marks that consists of or contains the

armorial bearings or other state emblems of the Republic or a convention country, an official sign or hallmark adopted by the Republic or a convention country and to the flag, armorial bearings, emblems and the name or abbreviation of the name of an international organisation.

- A mark which contains any word, letter or device indicating State patronage, or a mark which has been prohibited by regulation, cannot be registered (s 10(9) and (10)). Marks which belong to public bodies and which have been indicated as being prohibited marks by way of notice in the Government Gazette, such as the SABS mark and the emblem of the South African Nuclear Energy Corporation.
- A mark which is inherently deceptive or is contrary to law, contra bonos mores, or likely to give offence to any class of persons, cannot be registered (s 10(12)). Inherently deceptive marks include marks which are deceptive as to the origin of the goods (eg a mark depicting bagpipes and tartan used on goods would suggest that the goods are made in Scotland when in fact they are made in South Africa) and marks which are deceptive as to the character or quality of goods (eg the mark MERINO used on cotton goods).
- A mark which might otherwise be registrable cannot be registered if it is likely to cause deception or confusion as a result of the manner in which it has been used (s 10(13)).

Relative grounds for refusal

These grounds relate to the conflict between marks and the existing rights of others.

- A mark cannot be registered if its use would be likely to deceive or cause confusion (s10(12)).
- A mark may be likely to cause confusion or deception because of its resemblance to other marks in use in the marketplace (both registered and unregistered trade marks), trading styles, telegraphic addresses etc.
- A mark cannot be registered if it is identical to a registered trade mark belonging to a different proprietor or so similar to it that its use in relation to goods or services in respect of which it is sought to be registered and which are the same as or similar to the goods and services in respect of which the earlier trade mark is registered, would be likely to deceive or cause confusion (s10(14)). An objection under s 10(14) falls away if the proprietor of the earlier mark consents to the registration of the later mark. Section 14 makes special provision for the side-by-side registration of confusingly similar trade marks in instances where both marks have, in good faith, been used in the marketplace (termed “honest concurrent use”) or where other special circumstances are found to exist.
- A mark cannot be registered if it is identical to a mark which is the subject of an earlier application by a different person, or so similar

that its use in relation to the goods or services in respect of which it is sought to be registered, which are the same as or similar to the goods or services in respect of which the earlier application is made, would be likely to cause deception or confusion (s 10(15)). This s gives a prior application the same effect as a prior registration. However, a mark which is the subject of a prior application cannot be registered if the registration would be contrary to the existing rights of the person making the later application.

- A mark which constitutes, or the essential part of which constitutes, a reproduction, imitation or translation of a foreign trade mark which is well known in South Africa cannot be registered in respect of goods or services identical or similar to the goods or services in respect of which the trade mark is well known and where such use is likely to cause deception or confusion (s 10(6)).
- A mark may not be registered if it is identical or similar to a registered trade mark which is well known in the Republic and its use would be likely to take unfair advantage of, or be detrimental to, the distinctive character or repute of the registered trade mark, notwithstanding the absence of deception or confusion (s 10(17)). An objection under this section falls away if the proprietor of the well-known mark consents to the registration of the later mark. Note that this "antidilution'" provision is not confined to identical or even similar goods or services.

EFFECT AND DURATION OF REGISTRATION

The effect of a trade mark registration is to grant the proprietor a statutory monopoly which entitles him to use his trade mark in relation to the goods or services in respect of which it is registered, and to prevent other persons from using or registering the trade mark or a confusingly similar mark in relation to the same or similar goods or services. duration The duration of a trade mark is ten years, but this period may, on certain conditions, be renewed from time to time (see s 37).

INFRINGEMENT OF A TRADEMARK

Acts constituting infringement
Section 34(1) of the Trade Marks covers three types of infringement.

1. Unauthorised use in relation to registered goods or services

- The rights acquired by the registration of a trade mark are infringed by the unauthorised use in the course of trade, in relation to goods or services in respect of which the mark is registered, of an identical mark or of a mark so close as to be likely to deceive or cause confusion (s 34(1)(a)).
- This first type of infringement occurs where some person other than the registered owner uses a mark which is either identical or confusingly similar to the registered trade mark in relation to goods or services for which the trade mark is registered. The allegedly infringing mark must be used as a trade mark, for example, where the alleged infringer uses the trade mark to identify his own goods or services.

2. Unauthorised use in relation to similar goods or services

- The rights acquired by the registration of a trade mark are infringed by the unauthorised use of a mark which is identical or similar to the trade mark registered, in the course of trade in relation to goods or services which are so similar to the goods or services in respect of which the trade mark is registered, that in such use there exists the likelihood of deception or confusion (s 34(1)(b)).
- This second type of infringement is not limited to the precise goods or services covered by the trade mark registration. Note that the term "similar" is subject to an important qualification: the test is whether the goods or services are so similar that in use there exists a likelihood of deception or confusion. In applying this test, the court will have to take all the surrounding circumstances into consideration.

3. Unauthorised use of well-known registered trade mark in relation to any goods or services

- The rights acquired by the registration of a trade mark are infringed by the unauthorised use in the course of trade in relation to any goods or services of a mark which is identical or similar to a trade mark registered, if such trade mark is well known in the Republic and the use of the said mark would be likely to take unfair advantage of, or be detrimental to, the distinctive character or the repute of the registered trade mark, notwithstanding the absence of confusion or deception (s 34(1)(c)).

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- Note that this third type of infringement is only available in the case of registered trade marks which are well known in the Republic. It is not necessary for the offending mark to be used in relation to the same or similar goods or services for which the trade mark is registered. In fact, use on unrelated goods or services is sufficient. It is not necessary for the parties to be trade rivals. Public deception or confusion as to origin, sponsorship or association of the goods or services is not a requirement. However, the use of the offending mark must be likely to take unfair advantage of, or be detrimental to, the distinctive character or repute of the registered trade mark.
- Common form of injury which arises from this third type of infringement is called dilution by blurring. The unauthorised use of a well known trade mark in relation to noncompeting goods or services leads gradually to consumers no longer associating the trade mark with the trade mark proprietor's product. Eg, “our tomato sauce is the Rolls Royce of tomato sauce”.
- Although consumers will not be deceived or confused about the origin of the respective products in relation to which the mark is used, the offending use of the mark will erode its commercial magnetism and selling power and dilute its reputation and distinctive character.

Exclusions

The Act lists a number of situations in which the use of a registered trade mark does not amount to an infringement of the trade mark proprietor's rights. Basically the following acts in relation to a registered trade mark will not amount to an infringement:

- the bona fide use by a person of his own or his predecessor's name, or the name of his or his predecessor's place of business (s 34(2)(a))
- the use by any person of any bona fide description or indication of the kind, quality, quantity, intended purpose, value, geographical origin or other characteristics of his goods or services, or the mode or time of production of the goods or rendering of the services (s 34(2)(b))
- the bona fide use of a trade mark in relation to goods or services where it is reasonable to indicate the intended purpose of such goods including spare parts and accessories, or the rendering of services (s 34(2)(c))
- the importation into or distribution, sale or offering for sale in the Republic of goods to which the trade mark has been applied by or with the consent of the proprietor (s 34(2)(d))
- the bona fide use by any person of any utilitarian features embodied in a container, shape, configuration, colour or pattern which is registered as a trade mark (s 34(2)(e))
- the use of a registered trade mark where such use is within the scope of a limitation entered in the register against the registered trade mark (s 34(2)(f))

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- the use of any identical or confusingly or deceptively similar trade mark which is registered (s 34(2)(g))

Remedies for infringement

The Act makes specific provision for the relief which will be available in the case of the infringement of a trade mark. The available remedies are the following:

- an interdict
- damages
- an order for the removal of the infringing mark from all material and,
- where the infringing mark is inseparable or incapable of being removed from the material, an order that all such material be delivered up to the proprietor
- in lieu of damages, a reasonable royalty which would have been payable by a licensee for the use of the trade mark concerned

PROTECTION OF WELL-KNOWN FOREIGN TRADE MARKS

- Section 35 prohibits the unauthorised use of a trade mark which has become well known in the Republic. It is not necessary that the mark should have been registered or used in the Republic. The proprietor may restrain the use of any mark which constitutes a reproduction, imitation or translation of his well-known trade mark in relation to goods or services which are similar to the goods or services for which the trade mark is well known, provided such use is likely to cause deception or confusion. well known In determining whether a trade mark is well known in Republic, due regard must be given to the knowledge of the trade mark in the relevant sector of the public, including knowledge which has been obtained as a result of the promotion of the trade mark (s 35(1A)).
- A mark will be regarded as well known if it has acquired a reputation in the Republic among a substantial number of persons (for example, potential customers) interested in the goods or services to which it relates.
- Section 35 confers rights on the proprietor of an unregistered mark irrespective of whether or not he carries on business or has any goodwill in South Africa.
- The Act preserves local vested rights in trade marks acquired through continuous and bona fide use prior to 31 August 1991 or the date on which the foreign trade mark became well known in the Republic, whichever is the later date.

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	S34(1)(c)	S35
Similarities	Unauthorised use.	
	The trade mark that is being infringed must be "well known" in South Africa.	
	The infringing mark must be identical or similar to the registered trade mark.	The infringing mark must be a reproduction/imitation/translation of the mark that is being infringed.
	The infringed trade mark must be registered in South Africa.	It is not necessary that the infringed trade mark should have been registered or used in South Africa.
	Goods/services need not be related at all.	Goods/services are similar.
Differences	The infringing mark is likely to take unfair advantage of, or be detrimental to the distinctive character or repute of the registered trade mark.	Likelihood of deception or confusion.

POSSIBLE QUESTIONS:

During his stay in the USA, Jarrod visited a chain of internet café's called Surfer's. He was so impressed with the atmosphere, laptops and decor of these café's that he wants to open similar café's in South Africa. Although the name Surfer's is registered as a trade mark in relation to internet café's and web surfing throughout the USA, it has not been registered as a trade mark in South Africa.
Advise Jarrod whether there are any provisions in the Trade Marks Act which will prevent him from using the name "Surfer's" for his own internet café's.

Section 35 prohibits the unauthorised use of a trade mark which has become well known in the Republic. It is not necessary that the mark should have been registered or used in the Republic. The proprietor may restrain the use of any mark which constitutes a reproduction, imitation or translation of his well-known trade mark in relation to

goods or services which are similar to the goods or services for which the trade mark is well known, provided such use is likely to cause deception or confusion. In determining whether a trade mark is well known in Republic, due regard must be given to the knowledge of the trade mark in the relevant sector of the public, including knowledge which has been obtained as a result of the promotion of the trade mark (s 35(1A)).
A mark will be regarded as well known if it has acquired a reputation in the Republic among a substantial number of persons (for example, potential customers) interested in the goods or services to which it relates.
Section 35 confers rights on the proprietor of an unregistered mark irrespective of whether or not he carries on business or has any goodwill in South Africa.

X owns a chain of coffee shops called "Cafe Ole" in Europe.
Your client visited one of these shops during a trip overseas. He was so impressed with the atmosphere and decor of this shop that he wants to open similar shops in South Africa. He wants to use exactly the same name, decor and colour scheme. Although X has registered the name "Cafe Ole" as a trade mark in relation to restaurant services and coffee shops throughout Europe, he has not registered the name as a trade mark in South Africa. Advise your client whether there are any provisions in the Trade Marks Act which will prevent him from using the name "Cafe Ole".

Section 35 prohibits the unauthorised use of a trade mark which has become well-known in the Republic. It is not necessary that the mark should have been registered or used in the Republic. The proprietor may restrain the use of any mark which constitutes a reproduction, imitation or translation of his well-known trade mark in relation to goods or services which are similar to the goods or services for which the trade mark is well known, provided such use is likely to cause deception or confusion.

In determining whether a trade mark is well known in the Republic, due regard must be given to the knowledge of the trade mark in the relevant sector of the public (s 35(1 A)). A mark will be regarded as well known in the Republic if it has acquired a reputation in the Republic among a substantial number of persons interested in the goods or services to which it relates *(McDonald's).*

Section 35 confers rights on the proprietor of an unregistered mark irrespective of whether or not he carries on business or has any goodwill in South Africa.
It is irrelevant if Cafe Ole was a registered trade mark in South Africa.

In terms of Section 35 this trade mark will be protected if Cafe Ole has acquired reputation in South Africa among a substantial number of persons interested in Coffee Shops.

R is the administrator of the trade mark STARWARS which is registered in respect of beer. Since 1980 R has marketed his STARWARS beer intensively. According to a recent market survey, the STARWARS brand is one of the most popular brands of beer in South Africa. S commences marketing a new range of designer beer bottle openers under the trade mark STARWARS.
(a) Can R prevent S from using the trade name STARWARS for beer bottle openers in South Africa?

(a) R's STARWARS trade mark is registered in SA. S is making unauthorised use of the identical mark. Beer and beer bottle openers are similar goods. R will probably be able to show that beer and beer bottle openers are so similar that if STARWARS is used in respect of R's beers as well as S's beer bottle openers deception or confusion is likely and thus R can rely on s34(1)(b).

(b) Would your advice have been different if S had marketed sunglasses under the STARWARS mark?

Beer & sunglasses are unrelated goods so R can thus not use s34(1)(b) but could rely on s34(1)(c) if all the requirements of this section are met. This section needs R's mark to be registered in the Republic and that S's mark must be similar or identical to R's mark. Its thus required that R's STARWARS mark must be well known in SA. From the survey it seems that R's mark is well known in SA. R will have to show that S's use of STARWARS for sunglasses will be likely to take unfair advantage of or be detrimental to the distinctive character or repute of STARWARS. Deception or confusion is not required. R will thus have to show that S's conduct will erode the commercial magnetism and selling power of his STARWARS trade mark and dilute its reputation and distinctive character.

Hush Puppy, a shoe manufacturer, is the proprietor of the HEAVENSOLE trade mark which is registered in respect of comfort footwear. Doggy Dog begins to use the HEAVENSOUL mark on their competing comfort footwear. Doggy Dog files an application to register the HEAVENSOUL mark as a trade mark in respect of comfort footwear. Hush Puppy approaches you for legal advice.

1. (a) Hush Puppy whether Doggy Dog's conduct amounts to an infringement of their registered trade mark and, if so, what form of infringement is involved. (5)

Unauthorised use in relation to registered goods or services
The rights acquired by the registration of a trade mark are infringed by the unauthorised use in the course of trade, in relation to goods or services in respect of which the mark is registered, of an identical mark or of a mark so close as to be likely to deceive or cause confusion (s 34(1)(a)).
This first type of infringement occurs where some person other than the registered owner uses a mark which is either identical or confusingly similar to the registered trade mark in relation to goods or services for which the trade mark is registered. The allegedly infringing mark must be used as a trade mark, for example, where the alleged infringer uses the trade mark to identify his own goods or services.

2. (b) Would the Trade Marks Act 194 of 1993 prevent Doggy Dog from registering the HEAVENSOUL mark in respect of comfort footwear?
(2)

ξ **Yes, s10 would prevent Doggy Dog from registering HEAVENSOUL for comfort footwear. A mark cannot be registered if it is identical to a registered trade mark belonging to a different proprietor or so similar to it that its use in relation to goods or services in respect of which it is sought to be registered and which are the same as or similar to the goods and services in respect of which the earlier trade mark is registered, would be likely to deceive or cause confusion (s10(14)). An objection under s10(14) falls away if the proprietor of the earlier mark consents to the registration of the later mark. Section 14 makes special provision for the side-by-side registration of confusingly similar trade marks in instances where both marks have, in good faith, been used in the marketplace (termed "honest concurrent use") or where other special circumstances are found to exist.**

Mavis owns a chain of coffee shops called 'Cool Coffee' in Northern Africa. Evie visited one of these shops and wants to open similar shops in South Africa. 'Cool Coffee' is well known in Northern Africa and in South Africa. Although Mavis has registered the name 'Cool Coffee' as a trade mark in relation to restaurant services and coffee shops throughout North Africa, she has not registered the name as a trade mark in South Africa. Advise Evie:
(a) Whether there are any provisions in the Trade Marks Act which will prevent her from registering 'Cool Coffee' as a trade mark in South Africa.
(4)

S10(6) prohibits the registration of a well-known foreign trade mark in respect if goods or services identical or similar to the goods or services of which the trade mark is well known and where such use us likely to cause deception and confusion. It appears, in this question, that although the trade mark COOL COFFEE has not been used or registered in South Africa, it is well known in South Africa. Therefore, any use of the same trade mark by Evie is therefore likely to cause deception or confusion. Thus Mavis can prevent Evie from registering the trade mark COOL COFFEE in respect of restaurant services and coffee shops in South Africa

(b) Whether Mavis can prevent her from using the trade name 'Cool Coffee' for coffee shops in South Africa. (6)

Section 35 prohibits the unauthorised use of a foreign trade mark which has become well-known in the Republic. The proprietor may restrain the use of any mark which constitutes a reproduction, imitation or translation of his well-known trade mark in relation to goods or services which are similar to the goods or services for which the trade mark is well known, provided such use is likely to cause deception or confusion. It is not necessary that the mark should have been registered or used in the Republic. In determining whether a trade mark is well known in the Republic, regard must be given to the knowledge of the trade mark in the relevant sector of the public. A mark will be regarded as well known in the Republic if it has acquired a reputation in the Republic among a substantial number of persons interested in the goods or services to which it relates (McDonald's). It appears that although the trade mark COOL COFFEE has not been used or registered in South Africa, it has become well known in respect of coffee shops. Any use of the same trade mark by Evie is therefore likely to cause deception or confusion. Accordingly Mavis can prevent Evie from using the trade mark COOL COFFEE in respect of coffee shops in South Africa.

PRIVATE LAW OF COMPETITION:

This area of law is based on nothing more than delict, and is thus based on the actio legis Aquiliae and the actio iniuriarum.
The actio iniuriarum is aimed at obtaining satisfaction on the ground of the intentional infringement of a right of personality.
A trader who has been the victim of unfair competition is scarcely interested in satisfaction for intentional injury to her personality, but rather in compensation for the patrimonial loss which she has suffered.
the delict of wrongfully causing patrimonial loss (damnum iniuria datum) is applicable and thus the actio legis Aquiliae applies if one competitor causes another loss

LIABILITY FOR UNLAWFUL COMPETITION:

- ξ For a competitor to incur liability for unlawful competition in terms of the Aquilian action, the following elements of liability should be established:

1. An act or conduct: A competitor's conduct may consist not only of an act in the strict sense but also behaviour consisting of an omission (a failure to act).
2. Wrongfulness: The competitor's act or conduct must be wrongful (unlawful). The question as to the wrongfulness of competitive conduct is of cardinal importance in the field of unlawful competition.
3 Fault: A plaintiff who suffered damages as a result of unlawful conduct should, in principle, succeed if he can prove either intent or negligence on the part of the defendant. Provided that the requirements for an interdict have been met, the wronged competitor should be entitled to an order restraining the unlawful conduct irrespective of intent or negligence on the part of his rival.
4. Causation: The competitor's conduct must be the cause of the damage suffered by the plaintiff
5. Damage: A plaintiff who wishes to recover damages must show that he has actually suffered patrimonial loss, and its extent. Damage is usually suffered through loss of trade or custom.

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UNLAWFULNESS:

- Before one competitor incurs Aquilian liability in respect of another competitor all the elements of delict must be present.
- The unlawful competition is characterised by an infringement of the competitor's right to attract custom or goodwill it is an immaterial valuable part of the trader's patrimony (not of his personality) which can be sold and transferred.
- It has been described as the totality of attributes that entice clients to support a particular business.
- Goodwill has been regarded as moveable incorporeal property
- In unlawful competition the wrongfulness lies in the infringement of a competitor's right to attract custom or goodwill.

THE CRITERIA FOR UNLAWFULNESS:

- When is one dealer's interference with another's goodwill lawful, and when is it wrongful? In dealing with this question our courts have declined to formulate a general definition of the limits set to competition by Aquilian liability.
- Their approach has been to decide in each instance whether the particular conduct under consideration could be recognised as an infringement of the plaintiff's right (ie the rival trader's right), and therefore as a delict in our law. In this process emphasis was initially placed on the criteria of "**fairness and honesty in competition"**
- The boni mores test is thus an objective test based on reasonableness.
- The conflicting interests of the plaintiff and the defendant must be considered by the court in the light of all the relevant circumstances and pertinent factors, including the public interest, in order to decide whether the infringement of the plaintiff's interests was reasonable or unreasonable.
- Besides the above principles which were formulated by the courts, the "**competition principle**" has been proposed as an alternative standard by authors for judging the wrongfulness of behaviour between rivals. In terms of this standard, the rival who renders the most meritorious performance justifiably succeeds in trade at the expense of a rival who renders a weaker performance. If, for example, trader A doubles his turnover because he reduces the price of his product or improves its quality, rival B cannot complain about the prejudice which he suffers as a result of A's merit competition. A's advantage does, in fact, find its equivalent in the actual or potential prejudice of his competitor, but it is the merit of his performance which is the decisive factor.

- **Merit competition** is competition in accordance with the competition principle. In principle, merit competition is always lawful. In Tuttle v Buck: a banker opened a barber shop with the sole object of ruining a certain other barber. He cut his prices to below the profit margin and made no secret of his intention of closing down as soon as the other barber had been ruined. Any possible benefit (there was none) which he could acquire was out of all proportion to the prejudice which the other barber suffered. Although his acts were based on merit competition, they were wrongful in terms of the additional criterion of reasonableness.

REMEDIES:

In practice, the action of the victim of unfair competition is usually directed at obtaining an interdict and obtaining compensation. A competitor ought to be able to obtain an interdict solely on the grounds of threatening or continuous infringement of his right to goodwill; there is no reason why there should be further requirements, such as fault, in addition to the unlawfulness of the (threatening) act. Damages in accordance with ordinary principles should be recoverable only if there is fault on the part of the wrongdoer, that is, where the competitor's right to his goodwill has been infringed either intentionally or negligently.

RECOGNISED FORMS OF UNLAWFUL COMPETITION:

1. DECEPTION CONCERNING ONE'S OWN PERFORMANCE

A advertises that he is selling copper trays, whereas in fact he has copper coloured trays of an inferior alloy for sale; or A advertises that he sells clothes at factory prices, whereas in reality he charges the normal retail price; or A, with the intention of attracting customers to his shop,

The wrongfulness of A's conduct does not lie in the fact that he misleads the public but lies in the fact that by deception, he prevents clients from drawing a clear distinction between his performance and that of his competitors .
Our courts view interference with the goodwill of a competitor by means of deception of the public as to the quality, extent, nature etc of one's own enterprise or performance as unlawful. In Geary & Son - B carried on business in competition with A. A manufactured springs for motor vehicles and B did not. A alleged that B had habitually led the public of the city in which they both worked to believe that he (B) manufactured springs; that B had sold, as being of his own manufacture, springs which in fact were manufactured by A. A had allegedly suffered damages as a result of B's

conduct. Action was instituted for damages and for an interdict. A relied on wilful falsehood - intentional unlawful action on the part of B. The AD said that A's action was Aquilian, and the right upon which he might be presumed to rely was his right to attract custom, and that its clear that this interference is recognised as an infringement of a trader's rights and therefore as a delict in our law.

2. PASSING OFF:

Passing off is one of the most common forms of unlawful competition which takes place where a trader represents to the public that his enterprise, goods or services are those of his competitor. He does so by using or imitating his competitor's distinctive marks.
A trader can use distinctive marks to distinguish his business, goods or services from those of other traders. In the case of a business we are dealing with a trade name, in the case of goods with a trade mark or get-up (a particular method of packaging), and in the case of a service with a service mark. The use or imitation of the distinctive mark by a competitor may constitute unlawful competition.

In a passing-off action a plaintiff must prove the following two things:
(1) that the trade mark, get-up, service mark or trade name which he claims has been imitated is known in the market and has acquired with the public a reputation associated with his goods, service or business
(2) that the defendant's conduct is calculated to deceive the public

Reputation
Where a trader has established a business reputation in a particular area, he is entitled to prevent another trader from carrying on business under his name in that area. In the case of a retail business, the area in which its goodwill is affected is the same area from which it draws its customers. Where a trade mark, trade name business or product of a foreign trader has acquired a reputation within South Africa, he will be entitled to protection against passing off, despite the fact that he has never traded or carried on business there s 35 of the Act which enables the proprietor of an unregistered trade mark which is well-known in the Republic to restrain the use of it where such use is likely to cause deception or confusion. The proprietor of such a well-known trade mark will therefore be protected against passing off in South Africa despite the fact that he does not carry on business or have any goodwill here.
The courts are reluctant to come to the assistance of a trader whose trade mark or get-up is of a form or colour “common to the trade”, that is, generally used in the trade.
The courts will only protect a trader who uses a word in its ordinary sense or meaning in connection with his business if there are exceptional circumstances which indicate the word has acquired a secondary meaning

among his customers, that is, where the word has become distinctive in respect of that undertaking.
Protection is afforded the trader who uses a fancy or invented name or mark for his goods, service or business than the trader who makes use of a descriptive name (a name which is descriptive of his goods, business or service). Descriptive names must again be shown to have acquired secondary meaning through their association with the goods, service or business before they will be protected.
A person may wish to use his surname in respect of his goods, services or business, but that the name may already be used by a rival. The newcomer must restrict himself to the use of his name and must avoid any actions, which may otherwise cause confusion.

Deception
Whether the defendant's trade mark, get-up, service mark or trade name is so similar to that of the plaintiff that it is likely to confuse or deceive the ordinary customer, must be decided in the light of all the available evidence. Where the plaintiff himself has made a material false representation (eg. by claiming in his trade mark that his Chilli sauce is manufactured in some other part of the world when there is evidence that purchasers prefer imported Chilli sauce) the court will, in terms of the equity **doctrine of unclean hands**, afford him no protection. The doctrine is however applied only if there was fraud, dishonesty, or mala fides on the part of the plaintiff.

3. COMPETITION IN CONTRAVENTION OF A STATUTORY PROVISION:

- In a competitive relationship, competitor A may not do something that another competitor B is not allowed to do as this disturbs the equality principle which is the foundation of the law of competition and which maintains the harmonious balance in the relationship between rivals. If A, for example, sells his goods in conflict with a statutory provision, competitor B would not be able to counter A's competition.
- The balance in the competitive relationship between the parties is disturbed by an act against which B cannot defend himself except by breaking the law.
- The competition in contravention of a statutory provision results in unlawful competition **only** if the transgression has infringed or will infringe the plaintiff's **right to goodwill**. A's conduct is not wrongful against B merely because he contravenes the statutory provision. A's conduct is wrongful against B only if it interferes with his right to goodwill.

REQUIREMENTS:

a) Where an act is prohibited in the interests of a particular person or class of persons, for the purposes of an interdict the court will presume that this person or class of persons is damnified (has suffered loss or damage) and grant relief without requiring evidence of damage.

b) Where the statutory prohibition is in the public interest, any member of the public, including a rival trader, who can prove that he has sustained damage, or that he is reasonably likely to sustain damage, is entitled to his remedy. Whether a prohibition is intended to protect a specific person or class of persons, or is in the public interest is, of course, dependent upon the interpretation of the provision concerned.
Under either of these two types of prohibition, the wronged trader who has sustained actual loss has an action for damages, provided, of course that there was fault on the part of the defendant (Patz v Greene).

4. MISAPPROPRIATION OF A COMPETITOR'S TRADE SECRETS OR CONFIDENTIAL INFORMATION

Where a trader by any means whatever acquires and uses the confidential information or trade secrets of a competitor, he interferes with his competitor's goodwill.
Such conduct is contrary to the competition principle and is wrongful.
Not only disclosure of secret information is unlawful but obtaining and using it is also unlawful.
To qualify as a trade secret, the information must be confidential and have economic value.
The information must not be generally available to or known by others.
It must be of value to its holder.
Examples of information which have been recognised as trade secrets: price lists and tender prices, credit records, customer lists, customer connections, business conversations, a technical process, computer software, the know-how of an undertaking and an unpublished trade mark.

5. MISAPPROPRIATION OF A RIVAL'S PERFORMANCE

This form of unlawful competition occurs where a rival trader uses the performance of another as the basis for his own performance.
He does not merely use the idea or distinctive marks of a competitor, but copies a substantial part of the rival's performance.
In the absence of statutory protection (such as patent, copyright or design protection), a rival may copy the idea on which his rival's product is based, provided he uses that idea to create his own product.
Where a trader uses not only his rival's idea but also his performance, we are concerned with the piracy of a rival's performance.
In Schultz v Butt, S used the mould of B's boat to build his own boat. Notwithstanding the fact that S sold the boats under his own trade name (which would otherwise also have amounted to passing off if he had used B's name) the court decided that his conduct constituted unlawful competition.

6. DISPARAGING A RIVAL'S ENTERPRISE, GOODS OR SERVICES

The infringement of a competitor's goodwill by spreading untrue, disparaging allegations about his enterprise, goods or services is wrongful. Such conduct is usually directed at preventing the merits of the competitor's performance from winning the day and so is in conflict with the competition principle. The disparagement may be directed at a competitor's undertaking as a whole, for example by alleging that the undertaking no longer exists, or it may be directed against the performance rendered by the undertaking by, for example, stating that a rival's products are harmful to consumers. Eg, that a certain toilet paper has glass in it!

7. HARASSMENT OF A RIVAL'S CUSTOMERS, EMPLOYEES OR SUPPLIERS

Harassment means the exertion of improper physical or psychological pressure aimed at discouraging others from having trade relations with a rival.
Examples of this type of competitive act (like scaring a competitor's clients away by shooting at them), exerting psychological pressure on likely clients or customers like by setting up pickets which discourage prospective buyers from entering a competitor's premises.

8. THE INSTIGATION OF A BOYCOTT AGAINST A RIVAL:

A distinction can be drawn between primary and secondary boycotts.

- In the case of primary boycotts an undertaking (eg a supplier of goods) refuses to have trade relations with another undertaking. Since an undertaking is free to decide for itself with whom it wishes or may not wish to have trade relations, in general a primary boycott will be completely lawful. For example, in Times Media Ltd v SABC, the SABC refused to broadcast a television advertisement of the Sunday Times because it referred to M-Net, a rival of the SABC. The court found that this did not amount to a boycott and unlawful competition.
- A secondary boycott involves methodically endeavouring to encourage other undertakings to exclude a particular undertaking from trade. A trader who instigates a boycott against a rival trader interferes with the goodwill of the rival. Such conduct is, in principle, unlawful and may only be justified in exceptional circumstances. The perpetrator incurs Aquilian liability if he infringes the rival's right to goodwill either intentionally or negligently. Fault is not a requirement for an interdict.

The instigation of a boycott may often constitute conduct which might also be classified as infringement in the form of harassment.

GROUNDS OF JUSTIFICATION:
Wrongful competition is a delict, thus various grounds of justification can arise in this context, for example, self-defence, necessity and the public interest.

POSSIBLE QUESTIONS:

April manufactures a cleaning aid which he markets under the name "Floral Fresh". Her rival, May commences manufacturing and marketing a similar cleaning aid under the name "Refreshing Flower". May uses a similar shape bottle, and the same yellow and green colours. She even uses a similar lettering for the name of his rival product. The name "Floral Fresh" has not been registered as a trade mark.
Advise April whether she can prevent May from using the name "Refreshing Flower" under the private law of competition.

In Capital, the court said that passing off consists of a representation by one person that his business / goods is that of another, or that it is associated with that of another. The test for passing off is whether there is a reasonable likelihood that members of the public may be confused into believing that the business of the one is, or is connected with that of another.
In a passing off action the plaintiff must prove the following two things:

- **that the trade mark, get-up, service mark or trade name which he or she claims has been imitated is known in the market and has acquired with the public a reputation associated with his or her goods, service or business.**
- **that the defendant's conduct is calculated to deceive the public.**

Reputation
The plaintiff's mark, get-up or name must have become distinctive in relation to the goods, service or business concerned (Brian Boswell & Blue Lion Manufacturing).
Where a trader has established a business reputation in a particular area, he or she is entitled to prevent another trader from carrying on business under his or her name in that area. The courts are reluctant to come to the assistance of a trader whose trade name or get-up is a form or colour "common to the trade". The courts will only protect a trader who uses a word in its ordinary sense or meaning in connection with his or her business if there are exceptional circumstances, which indicate the word has acquired a secondary meaning among his or her customers. Protection is more readily afforded the trader who uses a "fancy" or "invented" name or mark for his or her goods or services.

Deception

The question of whether the defendant's trade name, get-up, service mark or trade name is so similar to that of the plaintiff that it is likely to confuse or deceive the ordinary customer, is one which the court must judge for himself in light of all the available evidence. Ordinary customers are neither the very careful nor the very careless and ignorant, but rather people between the two spectrums. They are generally aware of the particular characteristics of the article they want; they have a general idea of the appearance of the article; and although they do not examine it carefully, they have some idea of its general appearance. They court may take into account the class of persons likely to be purchasers. It is unnecessary to prove that anyone has actually been misled or that confusion has actually arisen. If there is a clear possibility that deception or confusion may arise, a trader is entitled to insist that his or her trade mark, get-up, service mark or trade name may not be used.

Name 3 criteria for judging the wrongfulness of a new competitor's competitive conduct. (3)

Fairness & honesty; boni mores and the competition principle.

Name 3 forms of unlawful competition. (6)

Name and briefly discuss any of the abovementioned forms of unlawful competition (eg. Passing off).

Name and discuss the requirements for the form of unlawful competition called "passing off". (5)

Reputation

Where a trader has established a business reputation in a particular area, he is entitled to prevent another trader from carrying on business under his name in that area. In the case of a retail business, the area in which its goodwill is affected is the same area from which it draws its customers. Where a trade mark, trade name business or product of a foreign trader has acquired a reputation within South Africa, he will be entitled to protection against passing off, despite the fact that he has never traded or carried on business there s 35 of the Act which enables the proprietor of an unregistered trade mark which is well-known in the Republic to restrain the use of it where such use is likely to cause deception or confusion. The proprietor of such a well-known trade mark will therefore be protected against passing off in South Africa despite the fact that he does not carry on business or have any goodwill here.

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A person may wish to use his surname in respect of his goods, services or business, but that the name may already be used by a rival. The newcomer must restrict himself to the use of his name and must avoid any actions, which may otherwise cause confusion.

<u>Deception</u>
Whether the defendant's trade mark, get-up, service mark or trade name is so similar to that of the plaintiff that it is likely to confuse or deceive the ordinary customer, must be decided in the light of all the available evidence.
Where the plaintiff himself has made a material false representation (eg. by claiming in his trade mark that his Chilli sauce is manufactured in some other part of the world when there is evidence that purchasers prefer imported Chilli sauce) the court will, in terms of the equity doctrine of unclean hands, afford him no protection. The doctrine is however applied only if there was fraud, dishonesty, or mala fides on the part of the plaintiff.

Discuss the criteria for unlawfulness in the private law of competition. (10)

Discuss the paragraph on "unlawfulness".

What right of the competitor is infringed by unlawful competition? (1)

Intellectual Property Right

Linc is employed by Funky Frog Clothing. After being dismissed, Linc took the customer lists of Funky Frog Clothing and established his own company. Funky Frog Clothing discovered that Linc has approached its clients to sell them clothing for their personnel at discount prices. Funky Frog Clothing approaches you for advice. (5)

Where a trader by any means whatever acquires and uses the confidential information or trade secrets of a competitor, he interferes with his competitor's goodwill. Such conduct is contrary to the competition principle and is wrongful. Not only disclosure of secret information is unlawful but obtaining and using it is also unlawful. To qualify as a trade secret, the information must be confidential and have economic value.
The information must not be generally available to or known by others. It must be of value to its holder.
Examples of information which have been recognised as trade secrets: price lists and tender prices, credit records, customer lists, customer connections, business conversations, a technical process, computer software, the know-how of an undertaking and an unpublished trade mark. Thus, Linc has committed the form of unlawful competition called "misappropriation of a rival's trade secrets or confidential information". This is deemed a delict and Funky Frog Clothing may sue using the Actio Legis Aquilliae (patrimonial loss) and/ or the actio iniuriarum.