

# Legal Update

## Court of Appeal confirms that correspondent banking obligations are personal, not proprietary

*First City Monument Bank plc v. Zumax Nigeria Limited* [2019] EWCA Civ 294

The England and Wales Court of Appeal has handed down a judgment which clarifies the circumstances in which a *Quistclose* trust, or any trust, may (or may not) arise, in the context of a series of correspondent banking transactions. In short, correspondent banking transactions will not generally give rise to any trust, and the correspondent bank's obligation to effect the onward payment to the beneficiary bank is personal rather than proprietary in nature. The decision will be welcomed by banks, as it clears up some confusion following the decision at first instance.

### *Quistclose* trusts

Where A lends B money for the sole purpose of discharging B's debt owed to C, a *Quistclose* trust (so named after the House of Lords decision in *Barclays bank Ltd v. Quistclose Investments Ltd* [1970] AC 567) may be deemed to arise in the event that B applies the money for a different purpose. In such circumstances, B may not use the funds save for the stated purpose, and at no point "owns" that money but holds them on trust for A if B misapplies the funds for another purpose. The conventional trusts analysis is that a *Quistclose* trust is a resulting trust in favour of A, coupled with a power granted to B to apply the funds for a stated purpose; if the funds are used for another purpose, the resulting trust is no longer subject to the power and so the funds result back to A.

*Quistclose* trusts are asserted most commonly in insolvency-type contexts, as they enable A as the beneficiary to assert a proprietary (and not merely personal) right over the sums previously advanced to B, which would effectively ringfence those sums to be returned to A in priority over B's unsecured creditors.

### Correspondent banking

Correspondent banking involves a financial institution (the correspondent bank) facilitating transactions as an intermediary on behalf of another financial institution (the originating bank), usually because the originating bank does not have an established relationship with the financial institution where the transaction is destined (the beneficiary bank), or does not have a presence in that jurisdiction.

### (Simplified) Background

Zumax Nigeria Limited ("**Zumax**"), a provider of engineering services to oil companies, held accounts with IMB International Bank plc ("**IMB**"), which later became First City Monument Bank plc ("**FCMB**").

Zumax's invoices to its customers were in US dollars and included instructions that payment should be made into an account held by Zumax's nominee, Redsear, at Chase Manhattan International. It was common ground that Redsear held those funds on trust for Zumax. The funds were either used to meet Zumax's US dollar needs or transferred to Zumax in Nigeria.

IMB held correspondent accounts with Commerzbank, and funds destined for Nigeria would first be transferred to those accounts from Redsear's account.

This decision concerned ten bank transfers so effected in 2000 – 2002, with a total value of around US \$3.75m (the "**Transfers**"). The payment instructions and statement records for each payment indicated that they were "*for further credit to Zumax Nigeria Limited*" (or words to that effect).

### The claim

Zumax alleged that it did not receive any funds from the Transfers. In relation to this aspect of the proceedings, Zumax sought a declaration that FCMB was liable to account to Zumax as trustee for the total value of the Transfers. In particular, Zumax claimed that when IMB received the Transfers into its accounts at Commerzbank, IMB (including FCMB as its successor) held those funds on resulting or constructive trust for Zumax.

### Summary judgment

The Judge at first instance, Barling J, granted summary judgment in favour of Zumax on the basis that FCMB's defences against Zumax's assertion of a trust enjoyed no real prospect of success. The Judge therefore declared that an express trust had arisen in favour of Zumax in relation to the Transfers; alternatively, that this was a *Quistclose* trust.

The Judge's analysis was that:

- the Settlor of the trust was "*Zumax, acting through its agent/nominee Redsear*";
- Zumax was the sole and express beneficiary and so could enforce the trust;
- accordingly, FCMB owed Zumax a fiduciary duty to transmit the value of the Transfers to Zumax.

### Court of Appeal judgment

FCMB appealed. The Court of Appeal reviewed the authorities and overturned the Judge's order for summary judgment, concluding that no trust arose in relation to the Transfers for the reasons summarised below.

1. The fact that a payment was made for a particular purpose does not by itself mean that it is the subject of a trust.
2. On the facts of this case, there was no intention to create a trust in respect of the Transfers, not least because there was nothing to suggest that the funds were not at IMB's free disposal. It is common in correspondent banking transactions for the payment message to identify an "onward" payee / beneficiary bank account to whom the payment should ultimately be credited. This instruction does not by itself give rise to a trust or evince an intention to create a trust. In this regard, it was relevant to note that the Transfers were effected *before* the payment instructions would have been seen by IMB staff.
3. Another factor pointing away from an intention to create a trust was the fact that the Transfers were not transmitted into an IMB account that was segregated in any way. Rather, the funds were commingled with other sums transferred into the same accounts from numerous sources and for the ultimate benefit of a range of recipients. There was therefore nothing to suggest that the funds transferred were not at the free disposal of IMB, or treated differently from other funds transferred at various times into IMB's accounts with Commerzbank. The Court of Appeal observed that a bank does not technically "hold" funds for its customers and payments do not involve the physical movement of anything tangible. Rather, a bank's relationship with its customers is merely one of creditor / debtor and so any funds "received" merely inform the balance in those relationships. In this sense, the customer does not "own" the funds in the account; rather, the bank merely owes that sum to the customer, and that obligation is generally personal rather than proprietary in nature.

4. Fundamentally, the nature of the relationship between IMB and Commerzbank was the usual one as between a bank and its customer i.e. as a simple debtor and creditor relationship. There is no general trust relationship as between a bank and its customer, whether in relation to payments or to “holding” a customer’s funds in an account. For a banker to be a trustee for a customer would be exceptional.
5. More generally, if a *Quistclose* or other trust were said to arise in these circumstances, it would “confuse and complicate the operation of correspondent accounts”. Many banking relationships – especially correspondent relationships – involve the facilitation of “on behalf of” payments. If the Judge was correct, all correspondent banks would automatically have onerous trustee obligations imposed upon them, unavoidably and against their will, immediately on receipt of funds. If this were the case, “it would paralyse the business of banking”. As regards *Quistclose* trusts specifically, the Court of Appeal confirmed that these do not generally have any bearing on funds in transit between one bank account and another.

## Conclusion

The Court of Appeal’s judgment provides welcome clarification that correspondent banking transactions do not generally give rise to any trusts, *Quistclose* or otherwise, and the onerous trustee obligations that would be entailed. The decision confirms that the nature of the relationship is the same as for any other bank / customer relationship:

a simple one of debtor and creditor. The relationship, and payments made pursuant to that relationship, do not give rise to proprietary interests in funds held on account or transferred for payment, and the bank’s obligations are merely personal in nature. This may come as a relief to the banking industry and to global financial institutions that process billions of transactions per day, for the reasons discussed in the Court of Appeal’s judgment.

If you have any questions about the issues raised in this legal update, please get in touch with your usual Mayer Brown contact or:

### *Susan Rosser*

Partner, London  
E: [srosser@mayerbrown.com](mailto:srosser@mayerbrown.com)  
T: +44 20 3130 3358

### *Devi Shah*

Partner, London  
E: [dshah@mayerbrown.com](mailto:dshah@mayerbrown.com)  
T: +44 20 3130 3669

### *Stephen Moi*

Senior Associate, London  
E: [smoi@mayerbrown.com](mailto:smoi@mayerbrown.com)  
T: +44 20 3130 3730

---

Mayer Brown is a distinctively global law firm, uniquely positioned to advise the world’s leading companies and financial institutions on their most complex deals and disputes. With extensive reach across four continents, we are the only integrated law firm in the world with approximately 200 lawyers in each of the world’s three largest financial centers—New York, London and Hong Kong—the backbone of the global economy. We have deep experience in high-stakes litigation and complex transactions across industry sectors, including our signature strength, the global financial services industry. Our diverse teams of lawyers are recognized by our clients as strategic partners with deep commercial instincts and a commitment to creatively anticipating their needs and delivering excellence in everything we do. Our “one-firm” culture—seamless and integrated across all practices and regions—ensures that our clients receive the best of our knowledge and experience.

Please visit [mayerbrown.com](http://mayerbrown.com) for comprehensive contact information for all Mayer Brown offices.

This Mayer Brown publication provides information and comments on legal issues and developments of interest to our clients and friends. The foregoing is not a comprehensive treatment of the subject matter covered and is not intended to provide legal advice. Readers should seek legal advice before taking any action with respect to the matters discussed herein.

Mayer Brown is a global services provider comprising associated legal practices that are separate entities, including Mayer Brown LLP (Illinois, USA), Mayer Brown International LLP (England), Mayer Brown (a Hong Kong partnership) and Tauil & Chequer Advogados (a Brazilian law partnership) (collectively the “Mayer Brown Practices”) and non-legal service providers, which provide consultancy services (the “Mayer Brown Consultancies”). The Mayer Brown Practices and Mayer Brown Consultancies are established in various jurisdictions and may be a legal person or a partnership. Details of the individual Mayer Brown Practices and Mayer Brown Consultancies can be found in the Legal Notices section of our website. “Mayer Brown” and the Mayer Brown logo are the trademarks of Mayer Brown.

© 2019 Mayer Brown. All rights reserved.

Attorney Advertising. Prior results do not guarantee a similar outcome.