

THE BANK'S FIDUCIARY DUTY: THE EVOLUTION OF THE DOCTRINE OVER THE LAST 30 YEARS

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SUMMARY: I. *The Bank's Fiduciary Duty: Historial View*. II. *The Evolution of the Bank's Fiduciary Duty – The English Model*. III. *The Evolution of the Bank's Fiduciary Duty – The Israeli Model*. IV. *The Need For Harmonization*.

I. THE BANK'S FIDUCIARY DUTY: HISTORIAL VIEW

The concept of imposing a fiduciary duty in commercial contexts is an ancient idea rooted in Roman law and even in the legal systems that preceded it.¹ However, the main development of the idea is connected to the changes that the modern post-industrial society underwent, and to the development of the free professions. These processes led to a fundamental change in the structure of businesses and in the manner of their activities; and as a result thereof — to a change in the nature of the relationship between service providers and their customers.²

In the past, service providers were individuals, familiar to their customers. The business domain of the service providers was limited and understood by the customer. The connection between the service provider and the customer was personal, based on their familiarity. But, in the twentieth century, a new phenomenon began to develop: the creation of business corporations for the purpose of providing services, including multi-functional companies

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¹ Tamar Frankel, *Fiduciary Law*, Fathom, 2008, chapter 1.

² Tamar Frankel, "Fiduciary Law", 71 *Cal. L. Rev.*, 1983, 803-804.

that supplied services in many different fields. These business corporations, in order to perform their functions and as a result of their size, incorporated sophisticated technological means. This technological development increased the ability of these corporations to acquire, store and reproduce information, including information regarding their customers. All of this led to a growing volume of customers, who, mostly, were not personally known to the corporation's employees, and did not receive personal service. As a result, not only the structure of these businesses and their nature of operation changed, but also the nature of their relationship with their customers.³

The processes described above are important to society, because they both promoted individual welfare and increased the efficiency of resource allocation. On the other hand, these processes have led to some basic problems: the creation of new forms of power and the gradual strengthening of this power in the hands of the service providers; the increase of conflicts between the service providers and their clients, or between different clients; the placement of trust and reliance by customers in the service provider, who is perceived by them as an expert, acting professionally in their best interests; the dependency of the individual on the service provider and, as a result, his vulnerability that could possibly be exploited by the service provider.⁴

The appropriate way to deal with all these problems is to impose a legal obligation on the service provider, to act in favor of the client and to protect his interests, especially in situations where the service provider has an incentive to exploit its power to the detriment of the client. This legal duty is the fiduciary duty.

This article will deal with the fiduciary duty imposed on a particular service provider — the commercial bank, when providing core banking services to its clients.

The bank's fiduciary duty, whenever it is applied, sets a very high standard of conduct for the bank. The bank is obliged to act with integrity and fairness. It must also act with professionalism and skill. However, beyond that, the fiduciary duty is underpinned by the duty to exercise its power and authority without abusing them. The key words are loyalty and fidelity. The bank 'as a fiduciary' is required to perform its duties solely for the purpose for which the power was vested in it, without ulterior motives and while protecting the interest of the beneficiary — the customer. The bank must act for

³ Paul D. Finn, "Fiduciary Law and the Modern Commercial World, in E. McKendrick (ed.), *Commercial Aspects of Trusts and Fiduciary Obligations*, 1992, 19 and 20.

⁴ Frankel, supra note 2, *ibidem*.

the best interest of the customer. Moreover, the bank must prefer the interest of its customer to the interests of others, including its own self-interest. Obviously, this is an onerous duty which is difficult to put into practice.⁵

These characteristics of the bank's fiduciary duty are common to the various legal systems that impose such a duty on the banks. But there are remarkable differences between different legal systems, as to the implementation of this duty. Over the past decades, and especially during the last 30 years, various models of the bank's fiduciary duty have been developed in the different jurisdictions.⁶

The article will deal with two models that reflect opposite trends: The English model, under which the concept of the bank's fiduciary duty became very narrow over the years; and the Israeli model, under which the duty is applied extremely broadly.

II. THE EVOLUTION OF THE BANK'S FIDUCIARY DUTY – THE ENGLISH MODEL

Under the English model, which applies in England, Canada, and other states that adhere to the common law system, the banker-customer relationship is not considered to be a fiduciary relationship.⁷ Nevertheless, the English courts are willing to impose a fiduciary duty on the bank under certain factual situations and circumstances, as discussed below.

1. *Investment Advice*

The main category in which the fiduciary relationship has been recognized is where the bank assumes the role of the customer's advisor, for

⁵ Plato-Shinar, Ruth, "The Bank's Fiduciary Duty under Israeli Law: Is there a need to transform it from an Equitable Principle into a Statutory Duty?", 39 *CLWR*, 2012, 219, 220-221. Plato-Shinar, Ruth, "An Angel named 'The Bank': The Bank's Fiduciary Duty as the basic Theory in Israeli Banking Law", 36 *CLWR*, 2007, 27, 29-30. Plato-Shinar, Ruth, *The Bank's Fiduciary Duty – the Duty of Loyalty*, Israel, Bar Publishing House, 2010, 71-77.

⁶ Plato-Shinar, Ruth, "The Bank's Fiduciary Duty: An Israeli-Canadian Comparison", 22 *BFLR* 1, 2006. Plato-Shinar, Ruth and Weber, Rolf H., "Three Models of the Bank's Fiduciary Duty", 2 *Law and Financial Markets Rev.*, 2009, 422.

⁷ Ellinger, E. P. et al., *Ellinger's Modern Banking Law*, 5th ed., Oxford, Oxford University Press, 2011, 126, 129, 134. J. Wadsley, J. and Penn, G., *The Law Relating to Domestic Banking* 107, 2nd ed., London, Sweet and Maxwell, 2000. Chuah, J., "General Aspects of Lender Liability Under English Law", *Banks, Liability and Risk*, London, Informa Law, W. Blair ed., 2001, 40. In Canada: Ogilvie, Margaret H., *Bank and Customer Law in Canada*, Toronto, Irwin Law, 2007, 196. Crawford, Bradley, *The Law of Banking and Payment in Canada*, vol. 2, Thomson Reuters, Ontario, 2010, §§ 9-49.9, 9-99.

example when the bank provides investment advice.⁸ The leading case in this category is *Woods v Martins Bank*, from 1958.⁹ This case dealt with a simple and unsophisticated man who was persuaded by a bank to purchase shares in a company which had an overdraft at the bank, without disclosing this fact to the purchaser. The purchaser lost his investment, having relied entirely on the bank's advice, in the absence of any business knowledge, experience or common sense of his own. The court found that there was a relationship of trust between the parties, which resulted in the imposition of a fiduciary duty on the bank. By virtue of this duty, the bank was obliged to disclose its conflict of interest to the customer and, by failing to do so, it breached the fiduciary duty.

However, over the years and especially over the past 30 years, the English courts have adopted a much more reluctant approach. The courts have stressed that a fiduciary duty will be recognized only under special circumstances, such as where the customer actually reposed trust and confidence in the bank and relied on its advice; or where the bank actually knew that the customer was relying on its professional judgment; or where the bank was purporting to act in the best interests of the customer. A fiduciary duty may also exist where the customer is in fact accustomed to being guided by the advice of the bank. Another instance is the bank's undertaking to act on behalf of the customer and the customer's reliance upon this undertaking. The recurring motives in the case law are the relationship of special proximity between the parties; relationship of dependency; the customer's inferior-

⁸ Ellinger *et al.*, *ibidem*, at pp. 134-136. In Canada: Ogilvie, Margaret H., *Canadian Banking Law*, 2nd ed., Toronto, Carswell, 1998, at p. 459-466; Ogilvie, *ibidem*, at p. 210-212; See mainly the judgments of *Standard Investments Ltd. v C.I.B.C.*, 1984, 5 D.L.R., 4th, 452, Ont. H.C., revd., 1986, 22 D.L.R., 4th, 410, Ont. C. A.; *Hodgkinson v Simms*, 1994, S.C.J. No. 84, 117 D.L.R., 4th, 161, S.C.C.; *Scaravelli v Bank of Montreal*, 2004., 46 B.L.R., 3rd, 322, 69 O.R., 3rd, 295, Ont. S.C.J., In relation to the *Standard Investment* case, see Ogilvie, Margaret H., "Banks, Advice-Giving and Fiduciary Obligation", 7 *Ottawa L. Rev.*, 1985, 263; Bradely Crawford, "Bankers' Fiduciary Duties and Negligence", 12 *Can. Bus. L. J.*, 1986, 145; R. P. Austin, "The Corporate Fiduciary", 12 *Can. Bus. L. J.*, 1986, 96; Ziegel, Jacob S. "Bankers' Fiduciary Obligation and Chinese Walls: A Further Comment on *Standard v C.I.B.C.*", 12 *Can. Bus. L. J.*, 1986, 21; Marshall, John C., "The Relationship between Bank and Customer: Fiduciary Duties and Confidentiality", 1 *B.F.L.R.* 33, 1986. In relation to *Hodgkinson v Simms*, see Margaret H. Ogilvie, "Fiduciary Obligations in Canada: From Concept to Principle", *J. Bus. L.*, 1995, 638. McCamus, John D., "Prometheus unbound: Fiduciary Obligation in the Supreme Court of Canada", 28 *Can. Bus. L. J.*, 1997, 107. Smith, Lionel D., "Fiduciary Relationship Arising in Commercial Contexts – Investment Advice: *Hodgkinson v Simms*", *Can. Bar Rev.*, 1995, 714. In relation to *Scaravelli v Bank of Montreal*, see Ogilvie, Margaret H., "Judicial Intuition and Bank Fiduciary Obligation: *Scaravelli v Bank of Montreal*", 21 *B.F.L.R.*, 2005, 89.

⁹ *Woods v Martins Bank*, 1 Q. B. 1959, 55; 3 All E.R., 1958, 166; 1 W.L.R., 1958, 1018.

ity and vulnerability, and the bank's hegemony over the customer's affairs; etc. Whatever the special circumstances may be, the general impression is that they are essential for the recognition of a fiduciary duty.¹⁰

Another example for this restrictive approach is the Canadian case of *Hodgkinson v Simms*,¹¹ where it was ruled that the essential requirement for the imposition of a fiduciary duty with regard to investment advice is a voluntary undertaking by the advisor to act on behalf and in favor of the customer. Once it has been ruled that a fiduciary relationship arises only upon a voluntary undertaking of the bank, it is equally clear that the bank can expressly exclude or restrict its liability by contract, in such a way that its relationship with the customer would not include fiduciary duties.¹²

Lately, even circumstances such as those mentioned above have not always been enough to recognize a fiduciary relationship between the bank and the customer. In *J.P. Morgan Chase Bank v Springwell Navigation Corporation*,¹³ it was ruled that "*the mere fact that one party to a commercial relationship "trusts" the other does not predicate a fiduciary relationship. The word "trust" ...has a variety of meanings. In a broad sense, trust is an important element in many commercial dealings...*"¹⁴ In the absence of a legitimate expectation that the bank would subordinate its interests to those of the customer, no fiduciary duty will be imposed.¹⁵

2. Taking Collaterals

Another category where a fiduciary duty has been recognized under English law is the taking of collaterals.¹⁶ The leading case in this category used to be *Lloyds Bank Ltd. v Bundy*.¹⁷ This case dealt with an old and simple man who pledged his house and farm to secure his son's business debts. The bank failed to disclose to the father the true state of his son's financial affairs, or to recommend that the father seek independent advice. A few months later, due to a deterioration in the son's financial situation, the bank enforced the security and sold the property.

¹⁰ *Supra*, notes 7 and 8.

¹¹ *Supra*, note 8.

¹² Ogilvie, *supra* note 7, at p. 197.

¹³ 2008, EWHC 1186 (Comm.).

¹⁴ *Ibidem*, at paragraph 574.

¹⁵ *Ibidem*, at paragraphs 572-578.

¹⁶ Ellinger, Lomnicka, Hare, *supra* note 7, at pp. 131-134. In Canada: Ogilvie, *supra* note 7, at pp. 212-214. Ogilvie, *supra* note 8, at pp. 472-483.

¹⁷ *Lloyds Bank Ltd. v Bundy*, 1974; Q. B., 1975, 326; 3 All E. R., 1974, 757; 3 W. L. R., 1974, 501 (C.A.).

The court held that the bank owed a fiduciary duty to the father, who had placed his trust and confidence in the bank. The bank was aware of the father's reliance, but it, nevertheless, failed to make a full disclosure. The court found that such behavior was tantamount to a breach of the fiduciary duty, and declared the charge null and void.

However, this approach was discredited in the case of *Nat. Westminster Bank plc. v Morgan*,¹⁸ whose basic model was similar to that of the Bundy case (this time, a wife guaranteed a mortgage on the family home to secure business debts of her husband). The House of Lords refused to find that the relationship between the bank and the security provider was a fiduciary relationship. Instead, it applied the doctrine of undue influence, finding it more suitable for the issue of security taking.¹⁹ The House of Lords further cautioned against attempts to precisely define the situations in which a fiduciary duty arises, showing reluctance to acknowledge the doctrine.

During the last 30 years, the Morgan case has become the prevailing precedent, and similar cases of taking collateral from a wife or an aged parent were addressed by applying the doctrine of undue influence rather than the fiduciary duty.²⁰ In 1993 the House of Lords authoritatively ruled that undue influence is the appropriate doctrine for cases of banks taking security inappropriately from weak parties,²¹ and the doctrine of fiduciary duty was abandoned.

In summary, even if, in the past, English courts were willing to recognize the relationship between the bank and the customer as a fiduciary relationship in certain cases, this approach has changed substantially over the last few decades and especially over the last 30 years. Today, under English law, the bank would only be subject to a fiduciary duty in very rare cases.

III. THE EVOLUTION OF THE BANK'S FIDUCIARY DUTY – THE ISRAELI MODEL

Another model of the bank's fiduciary duty is the Israeli model. The Israeli courts adopted the concept of the bank's fiduciary duty from the English law. However, from the moment that it was introduced in Israel, the courts

¹⁸ *National Westminster Bank plc. v Morgan*, 3 All E. R., 1983, 85, revd; 1 A. C., 1985, 686, 1 All E. R., 1985, 821; 2 W. L. R. 588 (H.L.).

¹⁹ Although in the end it was ruled that the bank did not exercise undue influence on the wife.

²⁰ *Supra*, note 16.

²¹ *Barclays Bank Plc. v O'Brien*, 1994, 1 A. C. (H.L.). *C. I. B. C., Mortgages plc v Pitt*, 1994, 1 A.C. 299 (H. L.). *Ogilvie*, *supra* note 8, at p. 477.

expanded it far beyond its original English counterpart. Over the last 30 years, the Israeli courts have created a unique model of the bank's fiduciary duty, which is enormously wide.²²

The idea of the bank's fiduciary duty was introduced in Israel at the first time in the case of *Israel Mortgage Bank v Hershko*,²³ in 1975. This case dealt with a loan provided to a customer. As a result of various limitations, the loan was established through a complex arrangement. The customer was not given a satisfactory explanation as to the essence of the transaction and therefore he did not understand that the way the loan had been established would cause him huge losses. The Israeli Supreme Court adopted the English judgment of Bundy mentioned above,²⁴ and ruled that the bank owed a fiduciary duty to the customer. Further it was ruled that the bank had breached its fiduciary duty by failing to provide the customer with full explanation, even though the customer had received independent advice from his attorney.

For many years the *Hershko* case was an isolated case regarding the recognition of the bank's fiduciary duty. However, during the late 80' and especially in the 90', the Israeli courts began to use this concept more often. The Israeli courts have determined, in various contexts, that "*the list of situations in which there is a fiduciary relationship is not closed and it exists in a diverse range of legal relations*".²⁵ Thus it was determined that fiduciary duty has broad application and applies "*in every case where a person has power and control over another*".²⁶

Indeed, the bank has power and control over the customer's interests and his financial property. The relations between the bank and the customer are relations of dependence by the customer on the bank. The customer depends on the bank in terms of the consulting services provided by it, in the provision of the service itself and in the determination of the legal arrangement applicable thereto. In the provision of the service, the customer expects the bank to act with a high level of professionalism and responsibility and an exemplary level of good faith. Customers tend to have special confidence in the bank, and in many cases feel no need to seek a second opinion before acting in accordance with the bank's advice. The banks' involvement in the financial life of every individual in the State is so deep and comprehensive that today it would not be possible to imagine the possibility of an individual manag-

²² See the materials in footnotes 5 and 6.

²³ Civil Appeal 1/75 *Israel Mortgage Bank Ltd v Hershko*, 29(2) PD 208, 1975.

²⁴ *Supra* note 17.

²⁵ *Kosoi v Bank Y.L. Feuchtwanger Ltd.*, 1984, 38(3) PD 253, 278.

²⁶ *Ibidem*.

ing his financial affairs without the banks. The bank possesses information that is not available to the general public, and also possesses special skills and technical means which individuals do not possess. All of the above enable the bank to help prevent its customers from sustaining losses, whereas the customer possesses no similar capability. The banks, for their part, are careful to cultivate public confidence in them, and it is even reasonable for duties to be imposed on them which are designed to fulfil the reasonable expectations which they themselves are instrumental in creating.²⁷

The Israeli courts developed an additional justification for the bank's fiduciary duty, one which is based on the quasi-public status of the banks.²⁸ It was explained that their activities have the characteristics of a vital service to the public. The banks perform many public duties, serve as agents for the implementation of government policy and a pipeline for the transfer of government loans to the public, and enjoy the backing of the Bank of Israel to secure the deposits of their customers.²⁹ The individual, for his part, views the bank as a quasi-public body and places a great deal of trust in it.³⁰ The perception of the banks as quasi-public bodies led to the conclusion that the banks should be subject to special duties, including the fiduciary duty.³¹

During the last two decades, the bank's fiduciary duty has been broadly interpreted by the Israeli courts. The courts have applied it in a very wide manner, in four different aspects as follows:

In the personal aspect — The type of customers to whom it applies: The fiduciary duty applies to each and every customer: whether he is an individual or a corporation; whether he is a business customer or a private customer; whether he is an ordinary customer without financial experience, or a sophisticated customer who is familiar with the banking and financial world.³² The fiduciary duty will apply even to customers who have financial power that can

²⁷ For the descriptive theories that lie behind this rhetoric, see Plato-Shinar, *An Angel Named "The Bank"*, supra note 5, at p. 33-36. Plato-Shinar, *the Bank's Fiduciary Duty*, supra note 5, at p. 51-67.

²⁸ *Sahar v Discount Bank*, 51(4) P. D., 1997, 476-477.

²⁹ *Civil Appeal 8068/01 Ayalon Insurance Company Ltd. v The Executor of the Opalgar's Estate*, 59(2) P. D., 2004, 349, 369.

³⁰ *Civil Appeal 1570/92 United Mizrahi Bank v Zigler*, 49(1) P. D., 1995, 369, 384. *Civil Appeal 5893/91 Tefachot Israel Mortgage Bank Ltd. v Tzabach*, 48(2) P. D., 1994, 573, 585.

³¹ Rubinstein, Michal and Okon, Boaz, "The Bank as a Social Agency", *Shamgar's Book - Articles*, Part C, Jerusalem, Nevo, 2003, 819, 831. Weinrot, Abraham and Medina, Barak, *Lending Laws - The Borrower's Protection in Israeli Law*, Tel Aviv, Bursi, 1990, 98-102.

³² Ben-Oliel, Ricardo, *Banking Law - General Part*, Jerusalem, Sacher Institute, 1996, 58.

be likened to the strength of the bank.³³ Every customer, by virtue of his very status as a customer, is entitled to a fiduciary duty.

In this regard it should be noted that according to Israeli law, a customer does not need to be an account holder, nor must have a long and regular relationship with the bank. Even someone who conducts a one-time transaction will be deemed to be a customer for the purpose of that particular service which he received from the bank,³⁴ and is entitled to fiduciary protection.

In the topical aspect — The type of the activities to which it applies: The banker's fiduciary duty applies to all the types of banking services, activities and transactions that the bank performs on behalf of the customer.³⁵ We have seen that the fiduciary duty arises from the existence of a bank-customer relationship. The relationship between the parties, by its very definition, is what imposes the fiduciary duty, and not a specific action that the bank wishes to perform.

In the circumstantial aspect: The imposition of the fiduciary duty is not dependent upon the existence of specific circumstances, such as special reliance of the customer on the bank.³⁶ The duty is deemed to be an integral component of the bank-customer relationship. In effect, the fiduciary duty serves as an undeniable presumption that exempts the customer from the burden of proving its applicability in a particular case: The duty always exists.

In the chronological aspect: The fiduciary duty is broadly applied also with respect to the period of time in which it exists. It originates at the pre-contractual stage and it is already binding upon the bank when negotiating with a potential customer.³⁷ Naturally, the duty applies as long as the bank-customer relationship exists. Furthermore, from the moment the fiduciary duty has arisen, it continues to exist, also after the closing of the account and the termination of the contractual relationship between the parties.³⁸

³³ Civil Appeal 7424/96 Mizrahi United Bank Ltd. v Eliahu Garziani, 1988, Co. Ltd, 54(2) P. D., 2000, 145, 161-162.

³⁴ This arises from the definition of the terms "customer" and "service" in The Banking (Service to Customers) Law, 1981.

³⁵ Tefachot Israel Mortgage Bank Ltd. v Tzabach, supra note 30, at 594 and 595. Ben-Oliel, supra note 32, at pp. 102-105.

³⁶ Tefachot, *Ibidem*, at 595.

³⁷ *Ibidem*, at 585, 594. See also: FitzGibbon, Scott "Fiduciary Relationships are not Contracts", 82 *Marq. L. Rev.*, 1999, 303, 309. Compare to the Canadian case Standard Investments Ltd. v Canadian Imperial Bank of Commerce, supra note 8. In this case the bank provided financial advice to a customer regarding the purchase of the controlling shares in a company. It was ruled that the fiduciary duty already existed when the bank offered to provide the service.

³⁸ Civil File (Dimona) 1099/99 Turgeman v Bank Leumi LeIsrael Ltd., 2000(4) Takdin Magistrate, 2000, 1140 at paragraph 6.

Certain aspects of the fiduciary duty, such as the bank's duty of confidentiality, continue even after the death of the customer.³⁹

In recent years, Israeli courts have ruled that the bank owes a fiduciary duty not only to its customers, but to third parties as well. Thus, a fiduciary duty was recognized vis-à-vis guarantors;⁴⁰ purchasers of apartments that were built by a constructor who received finance from the bank;⁴¹ other creditors of the customer;⁴² a third party who has a right to draw money from the customer's account;⁴³ and "any person when the bank is aware, or should be aware, that such a person might be influenced by the bank's behavior".⁴⁴

Lately, a new approach is being developed by the Israeli courts, according to which the bank has a fiduciary duty vis-à-vis the general public.⁴⁵ It was explained that "The existence of a general contract with the public expands the circle of those eligible to trust the bank, to the entire general public. The existence of such a contract imposes fiduciary duties on the banks to the public, without a direct connection to the particular service that is being provided or to the concrete circumstances surrounding the customer in his activity at the bank. It may be said that the general contract creates a starting threshold of fiduciary duties to the general public as a whole, which will be further intensified if the special circumstances so require".⁴⁶

According to this approach, the imposition of the fiduciary duty to the general public as a whole could lead to the imposition of general obligations which are not expressed only at the level of relations with a particular person. A fiduciary duty to the general public may be binding on the bank

³⁹ Civil Appael 1917/92 Skoler v. Jerby, 47(5) P. D., 1993, 764, 772.

⁴⁰ Miscellaneous Civil Application (Tel Aviv) 3706/03 Bank Hapoalim Ltd. v Rimón, Nevo Database, 2003, at paragraph 5. Opening Motion (Tel Aviv) 672/96 Prioff v Bank Hapoalim Ltd., Takdin District Database, 2000. Civil File (Jerusalem) 1790/88 United Mizrahi Bank Ltd. v Ziegler, District Judgments, 1992 (1) 172, p. 175. See Plato-Shinar, Ruth, "The Bank's Duty of Disclosure towards a Mortgagor of Assets Securing Debts of a Third Party", 49 *Hapraklit L. Rev.*, 2007, 385.

⁴¹ Plato-Shinar, Ruth, "Construction Loans in Israel: Bank's Liability Towards Third Parties", 23 *International Construction Law Review*, 2006, 187, at p. 194-198. Plato-Shinar, Ruth, "Construction Loans – Does the Bank Owe a Fiduciary Duty Towards Buyers of Apartments?", 4 *Land Law J.* 38, 2005, issue no. 6.

⁴² C. F., Tel Aviv, 113219/97 Iris Constructors v Hamizrahi Bank Ltd., 16 *Dinim Shalom* 250, 1999.

⁴³ C. A. 717/89 Bank Igud Le-Israel Ltd v Eran Tours Ltd., 49(1) P. D. 114, 1995.

⁴⁴ Civil File (Tel Aviv District Court) 2069 Farhi Food Services v Bank Hapoalim, not published, 1997.

⁴⁵ Application for Civil Appeal 9374/04 E. & G. Advanced Systems for Driving Teachers Ltd. v Bank Leumi Le-Israel Ltd., 69 *Dinim Supreme* 809, 2004, at paragraph 6(b).

⁴⁶ Rubinstein and Okon, supra note 31, at p. 826, 828. Civil File (Jerusalem) 5272/03, Iluz c. Discount Bank Ltd., Takdin District Database, 2004, at paragraphs 9, 13.

at the time of determining general policy, such as the bank's financial reporting policy or its investment policy, and may even impose on the bank responsibility for the financing of transactions that are detrimental to the public, for example, in the field of environmental quality.⁴⁷

In summary, the discussion above shows that the fiduciary duty imposed on banks under Israeli law is enormously wide.

Is there any explanation for such an approach? It seems that the reason for the wide approach of the Israeli courts is the unique position of the Israeli banking sector, and the enormous economic powers of the Israeli banks. The Israeli banking market is characterized by centralization and a lack of competition.⁴⁸ In the Israeli banking system, five banking groups are prominent, when two of them (Bank Leumi and Bank Hapoalim) control over sixty percent of the banking operations.⁴⁹ The possibility of additional banks entering into the system is regulated pursuant to the Banking (Licensing) Law 1981, and requires approval from the Bank of Israel. However, it would appear that the Bank of Israel has not only made no attempts to halt the trend of centralization, but it has even tried to encourage this trend, out of the belief that centralization and power would be conducive to the stability of the banks.⁵⁰ The huge market power possessed by the banks, and—in particular—the two major banks, in conjunction with the significant gaps in information, and the lack of a developed system of credit rating, aggregate to high entry thresholds for new players in the sector.⁵¹ This centralized structure constitutes an oligopoly (or to be more precise, a duopoly), that strengthens the power of the existing banks.⁵²

⁴⁷ Rubinstein, Okon, *supra* note 31, at p. 832. For criticism on this approach, see Ruth Plato-Shinar, "To Whom Does The Bank Owe a Fiduciary Duty?", 29 *Quarterly Banking Review*, 2004, 67 Issue no. 154. Plato-Shinar, *The Bank's Fiduciary Duty*, *supra* note 5, at p. 146-148.

⁴⁸ The Report of the Parliamentary Interrogatory Committee regarding the Banking Fees (2007) at 14-16. Available at: http://www.knesset.gov.il/committees/heb/docs/bank_inq.pdf (the "Banking Fees Report"). With regard to the centralization of the banks in the capital market, see The Report of the Inter-Ministerial Team regarding Reform in the Capital Market (2004) at p. 14. Available at: http://ozar.mof.gov.il/hon/2001/hon_dep/bachar.asp, the "Bachar Report". Meir Chet, *Banking in Israel: Structure, Activities and Crisis*, The Jerusalem Institute for Israel Studies, 1994, at p. 14-21, 31.

⁴⁹ The Bachar Report, *supra* note 48, at p. 15.

⁵⁰ The Banking Fees Report, *supra* note 48, at p. 22.

⁵¹ The Bachar Report, *supra* note 48, at p. 15.

⁵² Ben-Horin, Moshe, *The Securities and Capital Market*, 1996, 161. For another approach, see Shifron, Gad, "The Centralization of the Banks in Israel and in Other Countries", 31 *Quarterly Banking Review*, 1993, Issue no. 124, 28-33. Akiva Sternberg, "Competition in the

Against this background, the Israeli courts' approach is understandable, in that it attempts to restrict the banks from abusing their power. The suitable tool for this purpose is the fiduciary duty.

IV. THE NEED FOR HARMONIZATION

Whereas, according to English law, the bank is not usually deemed to be a fiduciary, the situation in the Israeli law is totally different, as was shown above. The difference between the two legal systems —the English and Israeli— is not merely theoretical, but it is reflected in practice in a wide spectrum of cases. One can point to numerous Israeli judgments in which the customer's claim against the bank was accepted on the basis of the determination that the bank had breached the fiduciary duty that is imposed on it. Had these claims been heard under English law, they would have been dismissed due to non-recognition of the existence of a bank's fiduciary duty. I will demonstrate this in a number of contexts.

One example relates to the duty to provide information.⁵³ As a rule, the English courts loath to broaden the duty of disclosure that is imposed on the bank. An example of this is the matter of *Suriya and Douglas v. Midland Bank plc*,⁵⁴ in which a customer required an interest bearing current account on which checks could be drawn. As this type of account was not customary at the bank, the customer was forced to run two separate accounts concurrently: one of which was an interest bearing account and another account on which checks could be drawn. At a later stage, the bank introduced a new type of current account which suited the customer's precise needs. However, the bank failed to disclose this to the customer and caused him to continue holding the non-interest bearing account for another four years. The customer sued the bank for loss of interest, claiming that there had been a contractual obligation on the bank to inform him about the aforesaid innovation. The court rejected the claim and held that a bank-customer relationship does not impose a duty of disclosure towards the customer. Even if the bank has a policy of informing customers of new types of accounts, this does not provide the customer with a cause of action should the bank fail to do so. An Israeli court would have ruled otherwise

Israel Banking System --- A Further Examination", 33 *Quarterly Banking Review*, 1995, issue 130, 62.

⁵³ In this matter see: Plato-Shinar, Ruth, "The Banks' Duty of Disclosure - towards a New Model", 27 *B. F. L. R.*, 2012, 427.

⁵⁴ 1999, 1 All E.R. (Comm.) 612.

on the basis of the fiduciary duty, which obliges the bank to protect and to further the interest of the customer.

Another example deals with the obligation to provide explanations.⁵⁵ In the Israeli case of *Hershko* mentioned above,⁵⁶ it was ruled that the bank breached its fiduciary duty to a customer that received a complicated loan, by failing to provide the customer with the full explanation that was required, even though the customer had received independent advice from his attorney. Under English law, it is doubtful that the customer would have succeeded in his claim because, under normal circumstances, a customer that relies on private professional advice is not deemed to be one who has relied on the bank's advice, and, without such reliance, a fiduciary relationship is not usually recognized.⁵⁷

In the Israeli case of *Turgeman*,⁵⁸ the issue at hand concerned a tax credit that was received in respect of the *Turgeman* couple at a branch of the bank. The couple had previously run a joint account at the branch; however, when they got divorced the account was closed. An account existed at the branch in the name of the husband alone which was in overdraft. The bank deposited the tax credit in the husband's account. The woman sued the bank, *inter alia*, in respect of a breach of the fiduciary duty towards her. The court accepted the claim and held that the fiduciary duty to the customer continues even after closure of the account. Hence, the bank owed a duty of trust to the woman even after closure of the joint account and it was prohibited from depositing the tax credit in a separate account belonging to the husband, without her consent. However, under English law, a claim based on the fiduciary duty would have been dismissed. We have seen that the bank—customer relationship, *per se*, does not create a fiduciary duty; and, according to English law, even if a fiduciary duty exists at the time of closure of the account, the bank—customer relationship comes to an end, and the bank owes no duty to the customer, except for the duty of confidentiality.

These and other examples illustrate the huge difference between Israeli law and English law regarding the implementation of the concept of the

⁵⁵ Plato-Shinar, *supra* note 53, at p. 437-439.

⁵⁶ *Israel Mortgage Bank Ltd v Hershko*, *supra* note 23.

⁵⁷ This is aside from the doctrine of undue influence, according to which, also, the bank would bear no responsibility if the obligor (mostly surety) received independent legal advice. See: Ellinger Lomnicka *et al.*, *supra* note 5, at p. 139–53; Mark Hapgood, general ed., *Paget's Law of Banking*, 13th ed., London, LexisNexis Butterworths, 2007, 689–700.

⁵⁸ *Turgeman v Bank Leumi Le-Israel Ltd*, *supra* note 38.

bank's fiduciary duty. Naturally, differences exist in relation to other legal systems that impose other models of the fiduciary duty on the banks.

These differences are, apparently, a source of problem. The banking business has become truly global. Yet, legal rules and doctrines are still very much based on national frameworks. The result is that obligations of banks depend on the place of the executed business transactions, and for global banks it makes the compliance with applicable rules difficult. Since many banks are prominently represented in different jurisdictions, the impression exists that not enough consideration is given to the different concepts of the fiduciary duty of banks vis-à-vis their customers in the real world. Obviously, the described legal differences are obstacles to the global banking business. The harmonization of some basic rules would improve the legal certainty without jeopardizing the flexibility of the banks to a substantial extent. It would seem to be worthwhile to give greater attention to the possibilities of a certain harmonization of rules that implement the doctrine of the bank's fiduciary duty.⁵⁹

Alongside the call for harmonization in the implementation of the case law doctrine of the bank's fiduciary duty, an interesting trend of recent years should be noted, which may reduce the gaps between the different legal systems. Under banking regulation that is on the rise in many countries, various behavioral rules are imposed on the banks by legislation or by the regulator. These rules are, in effect, expressions of the fiduciary duty.

This is, for example, the situation in England, where the courts are reluctant to impose a fiduciary duty on the banks.⁶⁰ However, the duty has gained significant strength through the entrenchment of its various components in the binding principles of the Financial Services Authority (FSA).⁶¹ These principles bind the bank to conduct its business with integrity;⁶² to pay due regard to the interests of its customers and treat them fairly;⁶³ to manage conflicts of interest fairly, both between itself and its customers and between a customer and another customer;⁶⁴ and to take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.⁶⁵ In the investment field, English

⁵⁹ Plato-Shinar and Weber, *supra* note 6, at p. 433.

⁶⁰ See chapter B, above.

⁶¹ FSA Handbook: High Levels Standards, Principles for Businesses, PRIN 2.1 -The Principles, Available at <http://fsahandbook.info/FSA/html/handbook/PRIN/2/1>.

⁶² PRIN 2.1.1(1).

⁶³ PRIN 2.1.1(6).

⁶⁴ PRIN 2.1.1(8).

⁶⁵ PRIN 2.1.1(9).

banks are subject to the “client’s best interests rule”. This rule determines that “*a firm must act honestly, fairly and professionally in accordance with the best interests of its client*”.⁶⁶ As discussed above, this is precisely the core meaning of the fiduciary duty.⁶⁷

These and other similar provisions actually reduce the existing gap between the different legal systems regarding the method of implementation of the bank’s fiduciary duty. If this trend continues, then despite the different approaches of the courts in the different jurisdictions, harmonization could be achieved in practice after all.

⁶⁶ FSA Handbook: Business Standards, Conduct of Business Sourcebook, Conduct of Business Obligations, COBS 2.1.1, available at <http://fsahandbook.info/FSA/html/handbook/COBS/2/1>. The rule is an implementation of section 19(1) of the European Council Directive 2004/39 Markets in Financial Instruments (MiFID), 2004 O.J. (L 145), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CONSLEG:2004L0039:20070921>, en PDF.

⁶⁷ In Chapter A, *supra*.