**What the Decision in Kingdom Bank Limited v Alice Wanja (2024) means for Commercial Banks**

***Background***

The High Court recently directed a local bank to reimburse a client who erroneously transferred funds to an account held with it. This decision will have far reaching implications on the duty of care borne by banks and payment service providers.

An individual (the **respondent**) erroneously transferred funds through M-pesa to an account at the bank. Upon discovering the error, she requested Safaricom to reverse the transaction. Safaricom advised her it had notified the bank, who she should follow this up with.

The bank’s response was that by when it was informed of the erroneous transfer, its customer had withdrawn the funds. The account did not have sufficient funds to reimburse the appellant, and the bank could not debit the account without the customer’s consent.

The respondent sued at the Small Claims Court, which ordered the bank to reimburse her. This decision was upheld by the High Court on appeal.

***Findings by the Small Claims Court and the High Court***

The Small Claims Court held that money paid by mistake is repayable, for the following reasons:

* A bank is not entitled to retain money which in common honesty it ought not to.
* Whether the bank will be liable for refunding the erroneous transfer depends on when it was informed and what actions had been taken. If the funds were withdrawn, accounts settled or other action taken before the bank was informed, it is likely to be inequitable to ask the bank to refund.
* Upon being informed of the erroneous transfer, the bank should have acted quickly to freeze the account as it sought clarity from its customer.

The bank understandably aggrieved appealed. The High Court though agreeing there was no contractual relationship between the parties dismissed the appeal. It made the following consequential findings:

* Electronic fund transfers are based on a good faith expectation funds will reach their intended destination and where there is an error, the funds will be recovered.
* Erroneous transactions are inevitable and the question is whether the bank acted in good faith. A bank must demonstrate it did not aid fraud and took steps to recall funds transferred in error.

Key to these findings is the concerned bank did not prove its customer withdrew the funds before it was notified of the erroneous transaction.

***Dealing with Disputed Transactions***

Borrowing from these decisions, and practices in comparative jurisdictions, the best practices for dealing with disputed transactions, are:

* Protect – immediately the bank is notified of a misdirected payment, it should put a hold on an equivalent sum. The customer is entitled to access any uncontested funds so entirely freezing the account is likely to be excessive and lead to claims by the customer against the bank.
* Give Notice – the bank should inform its customer it has put a hold on the funds from the disputed transaction. The beneficiary of a misdirected payment can authorize the bank to debit its account and return the funds. The beneficiary may also dispute the claim.
* Inform – where the beneficiary disputes the claim the funds should be returned, the bank should inform the complainant or his service provider as soon as possible.

***Concerns for the Financial Sector***

These cases did not answer some very important issues which should seriously concern all banks, payment service providers, and electronic wallet providers.

**Firstly**, it was not disputed the erroneous payment was made through M-Pesa which provides opportunity to verify the payee before payment. Therefore, the aggrieved party contributed to the loss of her funds, which does not appear to have been considered by either court. It is therefore unclear whether Kenyan courts will attribute any responsibility for loss of funds to anyone who transacts negligently.

**Secondly**, the decision impacts electronic payments resulting in disproportionate consequences for the banking sector and payment service providers. This is because the court found the bank which was merely a receiving agent was under obligation to undo any transactions it effects to a customer on instruction of the third-party payer. A key benefit of electronic payments is immediately available funds. The obligation to undo such transactions may impact when electronically transferred funds are made available to the beneficiary. This can be a complex and difficult endeavour given the standards for such systems are internationally established.

**Lastly**, the decision does not provide clarity on what the bank ought to do where the beneficiary of a disputed transaction disputes the claim. Financial service providers are not arbiters of truth and are likely not be in a position to definitively distinguish genuine mistakes from fraud or unscrupulous payers acting in bad faith.

***Recommendations***

In an era of increased digital payments, misdirected payments are inevitable. Fortunately, comparative jurisdictions offer guidance on best practices which the Kenyan financial sector may consider adopting.

**Verification of Payee** –payment systems can adopt payee verification as a standard. This modification, similar to what M-pesa provides, allows the payer to verify if the beneficiary is who they intend before they confirm payment instructions.

**Credit Payment Recovery (CPR) Process** – the banking industry in the UK, has adopted a standard process for recovering erroneous payments. The CPR Process sets out how a payee would make their claim, how the institutions involved would respond, and the timelines for doing so.

These interventions which will require industry consensus and effort will go a long way in simplifying resolution of disputed transactions.

DISCLAIMER:

*This alert highlights legal matters, legislative and policy changes for general use only. It does not create an advocate-client relationship between the sender and its receiver/reader. It is not legal advice or legal opinion. You should not act or rely on this briefing without consulting an advocate.*

*Contributors:*

*1. Mugambi Maingi – Partner*

*2. Emmanuel Mueke – Partner*

*3. Bernard Nyaga – Trainee Advocate*