Feature

KEY POINTS

- The decision in *Philipp v Barclays Bank UK Plc* [2021] EWHC 10 (Comm) and the Lending Standards Board Review of the Contingent Reimbursement Model Code (CRM Code) have brought into sharp focus a bank's duty of care as established in *Barclays Bank plc v Quincecare Ltd* [1992] 4 All E.R. 363.
- A bank's Quincecare duty, which is subsidiary to its primary duty to execute its customer's mandate, is limited to cases of attempted misappropriation by an agent of the customer.
- With the legal landscape uncertain, fraudsters becoming ever more sophisticated, and the Quincecare duty itself arguably misplaced; is it now time for regulation?

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When is a duty to pay not a duty to pay?

Frauds may be unauthorised (credit card fraud, phishing, for example) or authorised. Authorised frauds may be "pull" frauds, where the fraudster is given the victim's account details and authorised to pull the funds from their account, or "push" frauds (APP), where the victim instructs its bank to send money to the fraudster's account.

If society is serious about combatting fraud, the Quincecare duty should be recognised as incongruous. Where the threshold is crossed, transactions should be referred to the authorities, akin to a Suspicious Activity Report (SAR) notification. The decision whether to comply with the customer's instructions should be that of those best placed to investigate.

THE BACKGROUND TO *PHILIPP v BARCLAYS BANK UK PLC*

"Money never made a man happy yet, nor will it. The more a man has, the more he wants. Instead of filling a vacuum, it makes one." (Benjamin Franklin)

And where there is money, an opportunity and a vacuum in legal liability, fraudsters will lurk:

- Levels of APP fraud rose by 29% to £455.8m in the UK in 2019 (UK Finance: Fraud: The Facts 2020 (June 2020)).
- The Lending Standards Board Review found that between 28 May 2019 and 1 July 2020, firms participating in the Contingent Reimbursement Model Code (CRM Code) recorded 123,066 cases under the CRM Code.

Victims of fraud almost inevitably realise too late to secure the funds via the receiving bank, and once paid, there is little prospect of recovering them from the fraudster. This begs the contentious question: who bears the resultant loss?

The recent case of *Philipp v Barclays Bank UK Plc* (handed down on 18 January 2021, with permission to appeal granted on 22 February) concerned a sophisticated authorised push payment fraud and is a "classic" example of the techniques employed by fraudsters. In March 2018, the claimant, (Mrs Philipp), became embroiled in a fraud after her husband, Dr Philipp, was approached by a man calling himself "Jonathan Watts". She lost £700,000. Like many victims in her position, unable to recover her funds from the fraudster, she turned to the defendant (the Bank).

Mr Watts persuaded Dr Philipp that he worked for the Financial Conduct Authority (FCA), and that Dr Philipp was a critical part of an investigation by the FCA and National Crime Agency into fraud being perpetrated by HSBC staff. First, he transferred funds to Mr Watts from his HSBC account. Then, on instruction from the fraudster, Mrs and Dr Philipp actively declined the involvement of police officers who visited their home on two separate occasions. On the first visit they were expressly warned that "[the police] believed they had been the victims of a fraud".

Hours later, Dr Philipp transferred £950,000 from his savings with Tilney Financial Services. Mrs Philipp then made two in person, in branch transfers to the UAE, of £400,000 and £300,000 respectively. Dr Philipp attended on both occasions; when the first instructions were given on 10 March 2018, he volunteered to the Bank that they had had previous dealings with the payee. It was not disputed that both times the Bank later telephoned Mrs Philipp to verify her identity and her instructions, and she had confirmed she wished to make the payments. Mrs Philipp also accepted that she had provided Mr Watts with her identity documents, her telephone banking code and her mother's maiden name.

The police visited again on 15 March 2018; four days later Mrs Philipp requested a further payment of £250,000 which was blocked by the Bank. The fraud only unravelled when Dr Philipp's friends made contact with Tilney, HSBC, the Bank and the police. Together, they finally persuaded the Philipps that they had been conned.

THE DECISION

As HHJ Russen QC affirmed in this case, a bank's obligation is to effect payment in accordance with its instructions; to comply with its customer's mandate.[1]

It goes too far to say that the duty to follow instructions is strict[2] but it is true to say that a bank has no duty to advise its customer of the commercial wisdom (or otherwise) of its proposed transaction, or of tax repercussions.[3] In that respect, a bank's duty does mirror that of a strict agent, as summarised in *Bowstead & Reynolds on Agency*[4] "… even if the principal's instructions are foolhardy, the agent must carry out what has been instructed".

HHJ Russen QC applied the decision of Steyn J in *Quincecare*, at 376, that any duty to exercise reasonable care and skill in executing a customer's instruction "must generally speaking be subordinate to the bank's other conflicting contractual duties. *Ex hypothesi* one is considering a case where the bank received a valid and proper order which it is prima facie bound to execute promptly on pain of incurring liability for consequential loss to the customer".

Steyn J had continued that a "banker must refrain from executing an order if and for as long as the banker is 'put on inquiry' in the sense that he has reasonable grounds (although not necessarily proof) for believing that the order is an attempt to misappropriate the funds of the company".

That begged the question, what of a customer who is not a company? The Bank contended that the Quincecare duty was inapplicable. HHJ Russen QC agreed: the existing authorities confine "the duty to cases of attempted misappropriate by an agent of the customer".[5] Nor was there any proper basis for expanding that duty.[6] Such a conclusion, is, it is submitted, the inevitable consequence of a proper examination of the legal position:

- The *dicta* of Lady Hale in *Singularis Holdings Ltd v Daiwa Capital Markets Europe Ltd* [2019] UKSC 50 about the purpose of the Quincecare duty "have no resonance where the cause of the customer's own loss is her desire to make the payments to their intended recipients" (at [161]);
- Mrs Philipp sought to impose liability upon the Bank for alleged omissions which "really relate to testing the genuineness of the recipient of the monies rather than the genuineness of the instruction to pay the monies" (at [174]);
- Mrs Philipp gave the instructions herself. It is trite law to say she cannot misappropriate (steal) her own funds. Thus, the Bank could have no real cause to question the genuineness of the payment instruction or her authority;
- In *Philipp*, the payment instruction was not only valid as between her and the Bank but was valid in passing legal title to the monies from her to the fraudster. That is not the case where a bank's customer's agent misappropriates the customer's money.

Moreover, the judge held, the proposed expansion would elevate the duty (which is, and should remain, subordinate to the primary obligation to obey the customer's instruction) to a level where too much doubt would arise over the effectiveness of those instructions.

HHJ Russen QC was unpersuaded when asked to extend the duty:

- "there is no clear framework of rules by reference to which the duty, as extended, might sensibly operate … where the duty is said to involve second-guessing the customer's own outwardly genuine instruction, [it] would have to be supported by some form of clearly recognised banking code defining the circumstances in which the need for such questions would be considered" (at [159]);
- "the existence of such a duty would involve the triumph of unduly onerous and commercially unrealistic policing obligations over the bank's basic obligation to act upon its customer's instructions";
- "It is because the Bank cannot be expected to carry out such urgent detective work, or [be] treated as a gatekeeper or guardian …" (at [171]).

These observations were framed by the high hurdle set in *Quincecare*, applying *Lipkin Gorman (a firm) v Karpnale Ltd* [1987] 1 WLR 987, 1006 where Alliott J held that:

> "(3) it follows that, if a bank does not have reasonable grounds for believing that there is fraud, it must pay; (4) mere suspicion or unease do not constitute reasonable grounds and are not enough to justify a bank in failing to act in accordance with a mandate; and (5) a bank is not required to act as an amateur detective."

Indeed the Court of Appeal in *Singularis* believed it was the first finding against a bank for a breach of the Quincecare duty:

> "it will be a rare situation for a bank to be put on inquiry; there is a high threshold" (per Vos C at [98])

Notwithstanding this, on appeal in *Lipkin Gorman v Karpnale Ltd* [1989] 1 W.L.R. 1340, 1377-8, Parker LJ opined that:

> "I would not, however, accept that a bank could always properly pay if it had reasonable grounds for a belief falling short of probability. The question must be whether, if a reasonable and honest banker knew of the relevant facts, he would have considered that there was a serious or real possibility, albeit not amounting to a probability, that its customer might be being defrauded."

That went further than Alliott J at first instance or *Quincecare* itself and does not appear to have been reflected in the ratio of subsequent cases. However, both Rose J and Vos C in *Singularis* cited the text without either apparent disapproval or questioning of the different standard it purported to set. Read against the background of the move towards consumer protection, adopting it would drive the duty closer to requiring banks to turn amateur detective.

It submitted below that HHJ Russen QC's concerns therefore apply equally to the existing scope of the duty.

Consequence of the decision

The decision has been criticised in the previous edition of this journal,[7] where it was said that:

> "HHJ Russen QC's decision in *Philipp v Barclays Bank* leaves personal customers in the anomalous position of being deprived of the limited protection which the Quincecare duty provides to business customers."

In fact, on closer examination, the distinction is not anomalous. It is the perfectly logical consequence of the legal framework within which the duty exists. The critical factor is the *authorised* nature of the transaction. Mrs Philipp (and individuals in her position) have given a valid and proper instruction. The bank is bound to comply with it.

Contrast the situation with a corporate customer (or SME). In such a case, there are two separate legal personalities involved in the transaction. The purpose of the Quincecare duty is to protect a customer from the fraud of its agent, ie to protect one legal personality (the customer) from the unauthorised acts of another (its agent). Thus, there is no anomaly, because in the context of an individual customer, there is no agent from whom protection is required.

It is also wrong to conclude that a corporate customer is better protected against APP fraud than a personal customer. It would be a mistake to assume that where the agent of a business customer falls victim to an APP fraud, the transaction would have been unauthorised. It requires no stretch of the imagination to conceive of a situation where both legal personalities are acting with one mind: the customer's agent is not seeking to defraud the customer and has simply been duped. In those circumstances, Quincecare will be of no assistance to the corporate customer.

Quincecare: an anomaly?

The true position is that the Quincecare duty itself is anomalous. The issue stems from asking, "When is one agent required to disregard the instructions of another, superior, agent?". A corporate customer's employee, director or authorised signatory is its agent and is superior to the bank. As junior agent, the bank would, pursuant to the customer's mandate, ordinarily, and but for Quincecare, be expected to comply with the orders of the customer's agent.

It remains uncertain to what extent a bank is absolved of liability for its customer's losses where it delayed or refused to process a transaction because it had reasonable grounds for believing that the order was an attempt to misappropriate the customer's funds by an agent of the customer. One cannot properly ascertain the appropriateness of imposing a duty until one has considered the counterfactual.

What if a bank, exercising its Quincecare duty, takes the steps required thereunder, and its inquiries establish the honesty of the agent? Surely, the bank should not be liable for losses caused by the delay to the transaction. There is little English authority; however, the decision of the New Zealand Supreme Court in *Westpac Banking Corp v Map Associates* [2011] NZSC 89 suggests otherwise. There, *Quincecare* was relegated to a mere footnote to para [12], with the court holding at [11] that "the starting point for resolving the issue must be that, as a matter of contract, a bank's clear initial duty is to act in terms of its customer's instructions. Too ready or easy an undermining of that obligation would introduce much inconvenience and uncertainty into a fundamental commercial relationship".

The court accepted that "the bank has to anticipate the view a court may later take after a much fuller consideration of the circumstances than is usually possible when the bank is faced with an immediate demand from a customer" but nonetheless held the bank liable for failing to comply with its customer's instructions. This is all the more concerning given the potential overlap between what counsel in *Philipp* termed "red flags" for APP fraud, and possible red flags for misappropriation by an agent, and the risk that red flags that on their face give reasonable grounds for believing an agent is trying to misappropriate its customer's money will not be identified as APP fraud until it is too late for the transaction in question.

Whilst comparisons were drawn by the claimant's counsel in *Philipp* between the Quincecare duty and money laundering regulations, in reality there is a significant difference in how they are handled. If a bank is put on notice of a potential fraud, it has to consider whether it should submit a Suspicious Activity Report (SAR) under the Proceeds of Crime Act 2002 (POCA). In *Shah v HSBC Private Bank (UK) Ltd* [2012] EWHC 1283 (QB), Supperstone J held (at [38]), that "the reporting regime under POCA, necessarily in my view, makes inroads into the contractual duty of bankers to comply with a customer's payment instructions". The consent provisions in ss 327-329 and s 335 POCA provide timescales (initially seven days) during which a bank cannot act, and during which a decision on the SAR is to be expected. The court was satisfied (at [39] onwards), that in such circumstances and where there is no express term, the courts will imply a term that permits a firm to refuse to execute payment instructions in the absence of "appropriate consent".

This is in stark contrast to the position with the Quincecare duty, where it is not clear that a bank would escape liability for losses caused when complying with that duty. Furthermore, once the bank acting under POCA has established the existence of the necessary concerns, it does not have to investigate any further, still less make a decision. It hands the matter over to a centralised public agency. The bank in the same position under Quincecare must take those steps itself.

Quincecare in the modern world

In the context of the comparatively simple question of account details for payments, the Court of Appeal in *Tidal Energy Ltd v Bank of Scotland Plc* [2014] EWCA Civ 1107 observed that "… the evidence was that CHAPS did not operate in such a way that the beneficiary's name formed part of the identifier which determined the destination of the payment. This was because the volume of CHAPS transactions would make manual checking impossible within the short timescale" (at [24]). The same can be said for all electronic payment systems: indeed, the timescale is even shorter for many transfer methods, for example Faster Payments.

Quincecare is a duty from an era where agents misappropriated money by signing cheques, and when banks still largely knew their SMEs. It is not a duty that sits easily with modern day payment mechanisms. What steps, realistically, can a bank take?

The reality is that fraudsters' methodology evolves, and is doing so faster than regulation, or voluntary codes alone can keep pace with. Frauds are increasingly sophisticated and alongside remote transactions, the most effective tool fraudsters have in their kit is that of confidence: the art of the "con".

Herein lies one of the difficulties with the Quincecare duty. Steyn J held that a bank was not required to become an "amateur detective". However, in *JP Morgan Chase Bank NA v Nigeria* [2019] EWHC 347 (Comm) (at [21]), Rose J, following her first instance decision in *Singularis*, held that:

> "In most cases, the reconciliation of the conflicting duties owed by the bank to which Steyn J referred in *Quincecare* will require something more from the bank than simply deciding not to comply with a payment instruction."

Biog box

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There is a very significant difference between asking generalised safeguarding questions ("are you happy this payment request is genuine") and suspending a transaction entirely to investigate.
Two issues arise:

- if questions are to be asked, of whom should the bank ask them; and
- if the questions are only asked of the customer, what is the purpose of them?

First and foremost, there are often issues about who questions can be asked of. In *Singularis* the dishonesty was in the company's sole shareholder and manager (though not sole director). In other cases, the company may be a true "one man band". In *JP Morgan*, the suspected dishonesty extended to the highest levels of the Nigerian state. Often, asking third parties jeopardises the customer's confidentiality. In such cases, one has to ask with whom the bank should (or indeed can) check.

The issue is brought into sharper focus when one considers personal account holders. Mrs Philipp was described as being under the "spell" of Mr Watts. Assistance from the police, and friends had been rejected. It is hard to imagine what the Bank could have done to dissuade them, or whom the Bank could have made enquiries of. Mrs Philipp argued the Bank should have gone to the police and Tilney, amongst others, but even if the police had capacity to assist, as with corporate customers, many such enquiries would place a bank in breach of its duty of confidence.

Secondly, customer fatigue is a well-established phenomenon. Once the customer has confidence in the fraudster, is it really likely that they will be dissuaded from payment by the need to electronically tick the same warning box they have ticked umpteen times before? The reality is that the more used to seeing warnings customers become, the more blind to them they will be.

To pretend that banks can do anything other than offer automated questions risks jeopardising this country's reputation as one of the world's leading commercial jurisdictions. Anything more than basic questions is unduly burdensome and will prejudice the speed of payment that commerce relies upon, and to pretend that automatic questions alone can combat the tidal wave of frauds is similarly unrealistic.

Simply put, Quincecare is fundamentally unsuited to situations of APP fraud. Moreover, where a customer falls victim to a fraud, a claim against the bank will be time consuming and costly, and inherently uncertain. It will rest upon not just the determination of a duty of care, but also the standard of that care – with expert evidence and heated debate. That is not necessarily in a consumer's interests.

CONCLUSION

The decision in *Philipp* confining Quincecare to its existing scope is a welcome one, but it does not resolve the underlying tensions between the financial and public harms of burgeoning fraud, and the role of private institutions. The PSR (Payment Systems Regulator) and CRM (Contingent Reimbursement Model) Code assert that banks are best placed to combat fraud: on the contrary, this is society's problem and it is not the function of the banks or the courts to resolve.

It is unclear why banks should step in as insurers of last resort for decisions which customers with hindsight come to regret. The institutional cost (of the investigatory and procedural steps, and liability if a breach of duty is found) filters through to investors, borrowers and savers, all of whom ultimately bear the additional costs that arise wherever there is liability. One might well ask why such costs fall to private entities.

It is even less clear why banks should also bear the risk of the counterfactual, namely, that if they block or suspend a legitimate transaction, they will be held in breach of mandate, and found liable for the customer's consequential losses.

Banks are not necessarily best placed to identify and prevent fraud. The time has come to expand the SAR system or introduce an equivalent for fraud. Where transactions meet the specified threshold, a bank's obligation would be to report it to a centralised, public body, tasked with investigating suspected frauds.
The accumulation of evidence by a public agency would provide substantially increased insight into patterns of frauds, and an improved prospect of identifying organised crime. It would absolve banks of the inherent conflict of duty that currently exists and enable investigations that are presently precluded by reason of a banker's duty of confidentiality. Where the criteria for a report were met, a bank would, as in *Shah*, have a defence to a claim of breach of mandate. In addition, the statutory timeframe for the return of a decision would remove uncertainty for customers and ensure minimal interruption to trade. Banks would have a greater confidence in delaying transactions, and commercial certainty would be better protected. ■

1 *Paget's Law of Banking*, 15th Edition, §22.51.
2 *The Quincecare Duty: Misconceived and Misdelivered*, Watts QC J.B.L. 2020, 5, 403, 404.
3 Paget, §4.25.
4 22nd Edition, §6-003.
5 [2021] EWHC 10 (Comm) [133].
6 [2021] EWHC 10 (Comm) [156].
7 (2021) 3 JIBFL 172.

Further Reading:

- Prospects for bankers' liability for authorised push payment fraud (2021) 3 JIBFL 172.
- Quincecare and the Proceeds of Crime Act: connected duties or different worlds? (2020) 3 JIBFL 187.
- LexisPSL: Banking & Finance: Drawing the boundaries of the Quincecare duty in cases of fraud (*Philipp v Barclays Bank*).