MR GRAY

14 March 1990

JACK COMMITTEE ON BANKING SERVICES LAW AND PRACTICE
DRAFT WHITE PAPER

A Voluntary Code of Practice

The draft White Paper accepts the Jack Committee suggestion that the banks and building societies should devise a code of banking practice for themselves. There is a very broad measure of agreement amongst these institutions about the form which this code should take; and this extends to the consumer organisations which will be consulted. The Jack Committee recommended that the Government should reserve the right to impose a code by statute if it was dissatisfied with what emerged from the industry but that there is no reason to think that Sir George Blunden's Committee will fail to produce a document which will give customers a clear picture of what they can expect and be a proper source of reference for Ombudsmen settling disputes.

The draft White Paper broadly accepts the technical recommendations of the Jack Committee but on two important issues it dissents on changes in the complaints procedure and on the law of confidentiality.

Existing Ombudsmen schemes to be retained

On the question of Ombudsmen, the White Paper rejects the suggestion that the banking ombudsman scheme should be put on the same sort of statutory basis as that of the building societies. The present bank ombudsman scheme provides a perfectly satisfactory mechanism for solving disputes which is already available to almost all individuals who have bank accounts and the Jack Committee overstated the risk of inconsistent decisions being made by the separate bodies. There have been virtually no issues of that sort.

No Codification of Confidentiality Law

The Jack Committee called for the codification of the law on confidentiality. It took the view that there had been a 'massive erosion' of the banker's duty of confidentiality in recent years; in particular, it wanted to redraft the rules which compell disclosure of information by law. Many bankers, for example, have been critical of the proposals in the Criminal Justice (International Co-operation) Bill. The White Paper rejects this suggestion and argues powerfully that the basic framework of the rules established in the Tournier case of 1924 is still valid and that it would create all kinds of uncertainty if it were changed. I believe that view to be widely shared in the banking industry. The White Paper's more limited proposals for giving customers clearer information about the situations in which confidential information can be passed on are, however, acceptable to the consumer organisations, and, importantly, the individual should have the remedy of the Ombudsman under the proposed Code of Practice.

The wider issue - as to the way in which the Government should reconcile its need for information on criminal activities with the legitimate desire of the banks and their customers to preserve confidentiality - need not be an impediment to the Blunden Committee whose prime task is to give the ordinary customer clearer knowledge of the minimum standards which he can expect. It is important to stress that they will only be 'minimum standards'; the overriding aim is not to reduce competition in the standards of service and cost. The White Paper should be widely welcomed.

D A Lewis

PP HOWELL HARRIS HUGHES

RETURN TO C/F

Banking Services Law and Practice

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Foreword

by the Rt Hon John Major MP, Chancellor of the Exchequer

Customer confidence in the law and practice affecting the provision of banking services is fundamental to the financial system. Recent developments in banking make it important to ensure that the framework of law and practice is adapted to maintain this confidence in changing circumstances. For this reason in January 1987, the Government, along with the Bank of England commissioned the Review Committee under the Chairmanship of Professor R B Jack, CBE, to conduct a thorough assessment of the existing legislative framework for banking services. The Committee found that the legislative framework had stood the test of time remarkably well, and there were no major deficiencies or gaps, but they identified a number of areas where banking practice could be improved and where the law could be usefully clarified or tightened up.

We have seen enormous changes in the UK banking system over the past few years, with increased competition and rapid changes in technology which continue apace. This White Paper makes proposals to help meet these new challenges.

The Government wishes to express its appreciation to the Review Committee for their work and to all those who helped during the consultation process.

Banking Services Law and Practice: The Government's Response

The Evolution of Banking Services, Competition and the Consumer

1. This White Paper sets out the Government's response to the report of the Review Committee on Banking Services Law and Practice. The Government's proposals follow the objectives identified by the Review Committee, and are fully consistent with an important principle recognised in their Report: in this rapidly changing area it is necessary to preserve regulatory flexibility, and to ensure that competition and innovation are given room to develop.

2. In the past few years there has been a strong increase in competition in the banking sector, to the benefit of the consumer. Many building societies are now using the additional powers provided to them in the Building Societies Act 1986 to compete in the market for retail banking and other financial services. Competition amongst the major commercial banks and building societies for personal customers has clearly intensified. Interest-bearing current accounts, longer opening hours and a variety of card-based facilities are only a few recent examples of the benefits of competition to the retail customer.

3. Technological innovation has meant that new methods of payment can be offered to customers and this too has led to competition amongst innovators. There is also, for instance, evidence of growing competition for credit card services presented in the recent report of the Monopolies and Mergers Commission on this subject. It would be wrong to introduce legislation which might stifle further valuable developments of this kind.

4. Over recent years, it has been competition within a flexible regulatory framework that has benefited the consumer most and it is from this source that further improvements are most likely to come. This is the primary principle underlying the Government's response to the changes which the Review Committee have proposed.

The Report of the Review Committee

5. The Government, jointly with the Bank of England, commissioned the Review of Banking Services Law and Practice in January 1987. Much of the legal framework for the provision of banking services dates back to the last century and although it appeared to have stood the test of time well, it was not self-evident that it could cope with the rapid changes now being seen. Banking services have changed beyond all recognition since the main statutes were drafted, and it was felt that a full and coherent review of the law would be sensible and timely. The Committee was chaired by Professor R B Jack CBE, and the other members were Mrs Liliana Archibald and Mr G W Taylor.

6. The Review Committee's terms of reference were limited to services directly related to personal and business customers of banks and building societies. The remit therefore included payment and remittance services but excluded taxation, company law affecting banks, and issues related to banking supervision covered by the Banking Act 1987 and the Building Societies Act 1986.

7. The chief objective of the Review was to:

> "examine the law and its practical implications from the points of view of banker, customer and the general public interest in the availability, reliability, security and efficient and effective operation of payment, remittance and other banking services."

8. The Review Committee's Report followed a thorough process of consultation. The Review Committee issued five consultation papers in 1987, reproduced in Appendix A of their Report, and they received extensive comments from interested bodies.

9. The Review Committee recognised in their Report, which was published on 23 February 1989 (Cm 622), that an important constraint on any proposals in the field of banking services is the need to preserve flexibility, and to avoid cramping competition and innovation by excessive regulation. Against that background they considered that changes, where they are needed at all, should give priority to four objectives. They should aim:-

- to achieve fairness and transparency in the banker-customer relationship;

- to maintain confidence in the security of the banking system;

- to promote the efficiency of the banking system;

- and to preserve and consolidate the banker's duty of confidentiality to his customer.

10. To achieve these objectives the Review Committee considered the two main regulatory options, self-regulatory and statutory. It considered as a first and general possibility that there could be reliance on some form of regulation by the industry itself. Only if the industry showed itself unable to produce adequate rules would there be a case for imposing regulation on the industry from outside. Codes of good practice were considered as possible useful measures short of statutory regulation.

11. The Review Committee considered legislative measures might be appropriate in some circumstances, for example, the protection of weaker parties, the clarification of existing case law, or the elimination of confusion and anomaly. In addition, legislative measures might be needed to bring the law up to date with modern developments in banking practice and to provide backing, if necessary for a code of banking practice. The Review Committee found that, in general, banking services law had stood the test of time very well and there were no major deficiencies or gaps. Even so, there were a number of areas where the law could be usefully clarified or tightened up.

12. When the Report was published the Government invited comments on the recommendations set out in it. These recommendations are reproduced at Annex A to this White Paper. A list of those who submitted written comments is at Annex B. The Report was widely welcomed as presenting a clear and comprehensive critique of the present law, but reservations were expressed about some of the recommendations. The Government has carefully considered all these comments and this White Paper sets out its conclusions.

The Government's Response

13. A brief summary of the Government's main proposals is set out below. Annexes 1 to 8 discuss the main issues individually in more detail. The overall approach taken is to build on competition. Where this is not feasible, non-statutory self-regulation is proposed. Legislation has only been considered where it would either aid competition, correct areas where the law is inadequate or out of date, or where it is the only means of ensuring that consumers are protected. But it is worth commenting first on the broad approach taken to each of the Review Committee's four objectives.

14. First, **fairness and transparency**. Competition plays a crucial role in improving the fairness and transparency of banks' and building societies' dealing with their customers. Newspapers as well as specialist publications publish comprehensive and up-to-date comparisons of interest rates on different bank and building society accounts. Customers are therefore better informed of the choice available to them. But other matters, such as bank charges, and the terms and conditions under which the account is operated, are much less transparent. Legislation to increase transparency of bank charges and the operation of accounts would, however, be cumbersome and restrictive and the Government, therefore, proposes that increased transparency should be achieved by non-statutory means, as the Review Committee recommended, through a code of banking practice (the Committee's illustrative draft of which is reproduced at Annex C). The representatives of the banks and building societies have agreed to prepare and promulgate such a code. It was announced on 1 March 1990 that a Committee has been set up under the independent chairmanship of Sir George Blunden to oversee the preparation of the code, the terms of

reference of which include consultation with representatives of the consumer interests. The aim is that the main sections of the code should be ready and in place early in 1991.

15. The question of fairness is to a large extent linked with transparency. If a customer realises that his bank or building society is treating him less favourably than another would, he will consider moving his account. Competition therefore plays a major role. But a code of practice would establish the minimum standards of banking services which a customer could expect, and would provide a benchmark against which to judge banks' performance. At least one bank has already introduced a customer's charter on the lines of such a code; but the principle needs to be more widely extended.

16. One of the main ways to ensure fairness is for banks to provide access to a formal complaints procedure and, if that is exhausted, access to an Ombudsman scheme. Building societies are required to belong to an Ombudsman scheme set up under the framework provided in the Building Societies Act 1986. The major banks formed a voluntary Ombudsman scheme in 1986 which covers, at present, well over 90% of personal accounts. Awards made by the Banking Ombudsman are binding on the bank. The Government believes that this is a satisfactory scheme, and, since many of the Review Committee's recommendations have been adopted voluntarily by the Board of the Banking Ombudsman, it sees great advantage in its retention.

17. There is, however, a difference between the Ombudsman's scheme which applies to the banks and that which applies to the building societies. This difference could be eliminated either by amending the Building Societies scheme to make awards binding on a Building Society (at present a Society can reject an award providing it explains its reasons for doing so publicly); or by weakening the Banking Ombudsman's powers. On balance, the Government believes that it is sensible to leave the present arrangements as they are, rather than change two schemes both of which are working well. Steps are, however, being taken by the Board of the Banking Ombudsman to encourage more banks offering retail deposit accounts to join the Ombudsman scheme.

18. The Review Committee's second objective was to **maintain confidence in the security of the banking system.** There are a number of areas in which the Government agrees that confidence could be improved by legislation.

19. The Review Committee explained the advantages of a secure, non-transferable form of cheque, and recommended that this be achieved by introducing a new "bank payment order". That proposal has received little support during the consultation process. Those who have commented have argued that it would only add to the present confusion, rather than reduce it. The Government does not therefore propose to introduce such an instrument. But the present confusion over the status of crossings on a cheque and the meaning of terms such as "account payee only" is unsatisfactory and legislation will be introduced in due course to clarify the position and give legal force to those words.

20. The Review Committee also indicated the need to clarify the law on when precisely a payment is complete. While accepting the need for clarification, the Government is not persuaded that it should legislate immediately. A number of international initiatives in this area are currently under way and those who have commented have argued that it would be premature to enact legislation for the UK which could be overtaken by international developments.

21. Existing legislation in a number of other areas has stood the test of time and is familiar to practitioners. One example is the Bills of Exchange Act 1882 which, although more than 100 years old, continues to work well. The Government sees no need to revise this Act completely, as the Review Committee recommended, but proposes instead to make a number of changes to update it.

22. The third objective, of **promoting the efficiency of the banking system,** must largely be a matter for the banks themselves. But there are a number of areas where changes in legislation can help this process and these will be implemented in due course. For example, the introduction of legislation to permit the "truncation" of cheques (a process which replaces physical presentation with an electronic

message) would enable banks to make greater use of electronic means of data transfer and reduce the need to transport large numbers of cheques around the country to paying banks every day.

23. The fourth objective of the Review Committee was to **preserve and consolidate the banker's duty of confidentiality to his customer.** A banker has a primary duty of confidentiality to his customer except in certain defined cases. The exceptions were set by Lord Justice Bankes in his judgment in the celebrated case of Tournier v National Provincial and Union Bank of England (1924). The Government has been impressed by the evidence given during the consultation by those who have argued that the so called "Tournier rules" are clear, have worked well, and are widely understood by bankers, and that any attempt to codify them in legislation would be at best unnecessary and at worst likely to introduce new difficulties and confusion. The Government is persuaded, therefore that it should not codify the Tournier rules in statute solely for the sake of giving them legislative backing.

24. It is however clear that few customers are aware of the Tournier rules and the considerable protection they afford, and the Government believes that it would be desirable if bankers explained the effect of them in clear and simple terms. The code should contain an explanation of the general effect of the Tournier rules in order to clarify for personal customers the protection they already provide. It would not aim to set out the rules in great detail nor would it need to cover how they apply to corporate customers.

25. The Government shares the Review Committee's concern that confidential information about customers may be passed within a banking group for marketing purposes, and it is also aware that there is growing concern that information may be passed to credit reference agencies without the customer's knowledge or consent. The Data Protection Act 1984 requires that any information passed is obtained fairly, but any further legislation on such issues would inevitably be complex and inflexible and the Government believes that both matters would be more appropriately dealt with through the code of practice.

26. The Government does not accept the Review Committee's suggestion that there has been a "massive" erosion of the banker's duty of

confidentiality through the various statutory exceptions to the general duty of confidentiality such as those in the Drug Trafficking Offences Act 1986. These exceptions affect only the very small number of customers who use the banking system for dishonest purposes. They have no impact on the vast majority of honest customers. Before enacting such exceptions the Government always considers with great care the implications, including the impact on banking confidentiality. The Government only enacts such exceptions where the benefits outweigh any possible disadvantages.

Summary of Proposals

27. In summary, the approach favoured by the Government is to build, wherever possible, on competition for banking services, buttressing that, where necessary, with a voluntary and not a statutory code of banking practice. It believes that a voluntary code of practice is the best means toward that end. Where existing legislation or case law has worked well and is not in doubt, no changes are proposed. But legislation will be presented when other pressures on the legislative timetable permit to clarify and update the law in a number of areas.

28. In brief, therefore:

- The Government fully endorses the recommendation (16(1)) that representatives of the banks and building societies should draw up and promulgate a non-statutory statement of best practice covering broadly the areas in Appendix L of the Review Committee's Report; and it welcomes the steps that are already in hand to prepare it. The Government thinks it desirable that the code should specify that customers will be given information in clear and simple language about the terms of their contract with the banker and the rights and obligations that apply on both sides; customers should be told of the rights to privacy which the law already affords and the very limited circumstances in which any information about their personal finances may be passed on; how to lodge a complaint if it proves necessary, how such complaints will be dealt with, and how matters may be referred to the relevant Ombudsman; they should be told

what banking charges may be levied in what circumstances; and they should be given a simple explanation of the timing of the clearing cycle and when they could normally expect a cheque to be cleared. (Annex 1).

- The Government sees no need to codify the present rules on confidentiality in statute, but thinks it desirable that the code of banking practice should inform banks' customers of the rules' existence. The Government also thinks it is desirable that the code should lay down good practice on the use of information for marketing purposes and the procedures for passing information to credit reference agencies. (Annex 2).

- The Government proposes to leave the present Ombudsman schemes as they are, but steps are being taken by the Board of the Banking Ombudsman to encourage more banks to join the Banking Ombudsman scheme. (Annex 3).

- The Government will legislate in due course to extend to all payment cards the current £50 limit on customer liability for losses, which at present applies only to credit cards, and to ban the unsolicited mailing of cards and PIN numbers. (Annex 4).

- The Government sees no need to introduce a new "bank payment order" but will legislate in due course to clarify the present unsatisfactory position of crossings and markings on cheques. (Annex 5).

- Legislation will also be introduced, when other pressures on the legislative timetable permit, to allow for truncation of cheques, to amend and update the Bills of Exchange Act and to deal with a number of other detailed points raised by the Committee. (Annex 9 details the legislative proposals).

- Many of the subjects covered by the Review Committee may have implications for Scots law. In implementing the proposals, special consideration will be given to the different legal position in Scotland.

Annex 1. The Code of Practice

1.1 The Review Committee's Report contains twenty four recommendations to banks and building societies concerning standards of banking practice which would be contained in the proposed code. The code would be available to customers, enabling them to know the minimum standard of service to expect. It could be referred to by the Ombudsmen in settling disputes. The illustrative code which is set out in Appendix L to their report is reproduced in Annex C below. The code would not attempt to standardise levels of service. That would be counter-productive. In many areas the code will simply define the information the customer should expect to receive from the banker about the way his account should be run and his business conducted, to enable the customer to make sensible choices. Banks and building societies would continue to compete by offering better terms and conditions than any minimum specified.

1.2 Consultation has shown that there is general acceptance of the idea of a code of banking practice. The representative bodies of the banking industry have agreed to produce a code which would be followed by their members. It was announced on 1 March 1990 that a Committee has been set up under the independent chairmanship of Sir George Blunden to oversee the preparation of a code of banking practice by the British Bankers' Association (BBA), the Building Societies Association (BSA) and the Association for Payment Clearing Services (APACS). The other members of the Committee are Sir Alastair Burnet, Miss Margaret Reid, Mr Denis Child, Mr Malcolm Macaskill and Mr Geoffrey Taylor. Its terms of reference are:

i. To oversee the drafting of a code of banking practice, to be drawn up by the Banks and Building Societies in the light of the recommendations contained in the

Report by the Review Committee on Banking Services: Law and Practice, satisfying itself that consultation has taken place with customer and other interests.

ii. To consider, following discussions with the Bank of England and the Building Societies Commission, the most appropriate arrangements for promulgating the code to banks and building societies.

iii. To consider, following discussions with the Bank of England and Building Societies Commission, the most appropriate arrangements for ensuring adoption of the code and of compliance with its terms by banks and building societies.

iv. To keep the code under periodic review and to propose modifications, where necessary, after consultation with the Banking and Building Societies Ombudsmen.

It is intended that work on the code shall start in the spring in order that the main points of the code shall be in place by early 1991. The Government warmly welcomes this development as an indication of the positive way that the banks and building societies are responding to the challenge.

1.3 The particular areas of banking practice, or the specific recommendations which the Government thinks should be incorporated into a code, are addressed in detail in the remainder of this chapter. In setting out those proposals, the views of consultees have been taken into account. Clearly, some areas of the code will be more important than others.

1.4 The code is intended to be a statement of good practice and it is envisaged that all those offering retail banking services will adopt it. The code will also be available to the Banking and Building Society Ombudsmen who will be able to use it in making decisions. It will represent a standard of service against which a bank's operations can be gauged. If it is widely adopted by those offering retail banking services and its standards are met,

it should meet the concerns indentified by the Review Committee and the issue of statutory backing need not arise.

Contents of the Code of Best Banking Practice

(i) UNDERLYING ASPECTS OF THE BANKER-CUSTOMER RELATIONSHIP

1.5 Identity of customers. The Review Committee recommended (rec 6(2)) that, as an indication of what is required for the banks and building societies to secure the protection of section 4 of the Cheques Act 1957, they should initiate procedures which allow them to establish, to their reasonable satisfaction, the true identity of a person opening an account, so that if subsequently challenged they can refer to the action they took at the time.

1.6 The Government strongly supports this recommendation. It extends further than protecting the interests of the banker under section 4 of the Cheques Act 1957. Customers should be reassured that if a cheque is stolen, positive steps would have been taken by banks and building societies to minimise the chance of a criminal obtaining payment by setting up an account in a false name. Banks and building societies have already been encouraged by their regulators to check the identity of new customers in order to avoid accounts being used for money laundering. Such abuses are not in the interests of deposit taking institutions and they and their trade associations have recognised this. Guidance is normally provided by the trade bodies on methods of verifying the identity of new customers and many banks will follow that guidance. The Government urges those institutions which do not make thorough checks, perhaps because they only operate deposit accounts, to institute them.

1.7 Terms and conditions - communication to customer. The Review Committee recommended (Rec 6(3)) that, when a banker informs a customer of the terms of the contract between them, the banker should ensure that the customer receives a fair and balanced view of those terms, and of the rights and obligations

that exist on each side; and is given reasonable notice of any proposals for varying those terms.

1.8 The Government supports this recommendation and welcomes recent moves by some of the clearing banks to follow this suggestion by giving greater transparency to their charges. Competition should, in time, ensure that all areas of banking services become more transparent to the customer. Providing a fair and balanced view of the terms of a contract which would be both accurate and understandable to every customer may be a difficult task; but a customer who is aware of both his obligations and his rights is more likely to be satisfied with the service provided.

1.9 It is also desirable that reasonable notice should be given on any variation in the contract which a bank wishes to introduce, to enable a customer to choose whether or not to continue holding his account with that institution.

1.10 Complaints procedures. The Review Committee recommended (Rec 15(2)) that banks should establish clearly defined internal procedures for handling customer complaints. They should ensure that customers are informed how to lodge a complaint and how it will be dealt with, including the procedure for access to an Ombudsman if the internal procedure does not resolve a dispute. All building societies and many banks already have complaints procedures. The Government thinks it would be desirable if all personal customers were covered by these schemes. A number of banks and building societies advertise their membership of an Ombudsman scheme. The Government believes more widespread publication would benefit both the customer and the member banks. The code of banking practice should require a bank to tell its customers that it is, or is not, a member of the Banking Ombudsman scheme, Building Society Ombudsman scheme or the Finance Houses arbitration scheme.

1.11 Duty of confidentiality. The Review Committee recommended (Rec 5(2)) that the code of banking practice should also explain the rules surrounding the banker's duty of confidentiality. The

Government agrees with that recommendation. The question of confidentiality is discussed in more detail in Annex 2 which sets out the Government's reasons for rejecting the proposal that the existing "Tournier" rules, established in case law, should be codified in statute. The Government believes that there is merit in the code making the customer aware of the protection the law already affords him and the limited exceptions to it. There are, however, two areas of concern to the public where the Government believes that it would be desirable if the code provided for banks to restrict their existing practice in passing information. These are where the information is used for marketing purposes, and where "white" information is passed to credit reference agencies, without the customer's consent. ("White" information means credit information about customers who are not in default as distinct from "black" information which is about customers who are.)

1.12 The Review Committee recommended (Rec 13(4)) that banks and building societies and their subsidiary companies should exercise restraint in the direct marketing of their services. The Government supports this recommendation. The Government therefore proposes that the code of banking practice should contain a provision which will ensure that the customer is made aware that his personal information may be used by a bank for direct marketing purposes and may be passed to credit reference agencies. The customer should be given the opportunity to object. Any objections the customer makes to the use of personal information should be respected. The customer should be informed of the bank's practice in this area when an account is opened, and whenever the banker seeks to vary the terms of that account.

1.13 The Government urges banks to ensure that information relating to minors' accounts is handled with particular care. Credit marketing addressed to minors is prohibited by law. The code of banking practice should include a reassurance to customers that banks will take all reasonable precautions to ensure that marketing material is not inadvertently sent to customers who are minors.

1.14 The Government also supports the Review Committee's recommendation (Rec 5(2)) that banks should explain to their customers that they have right of access, under the Data Protection Act 1984, to their personal records held on computer files by banks and building societies.

1.15 Bankers' opinions. The Review Committee recommended (Rec 6(4)) that bankers should give customers a clear explanation of how the system of bankers' opinions works and invite them to give or withhold a general consent for the bank to supply opinions on them to other bankers in response to status enquiries.

1.16 The Review Committee found no evidence that the present arrangements were working against the customer's interest but they thought that the customer should be better informed. The Government believes that further protection to customers in this area is not needed, but the code should make it clear that if a customer requests information on how the system of bankers' opinions works, the banker should provide an explanation.

(ii) RULES APPLYING GENERALLY TO THE CUSTOMER'S ACCOUNT

1.17 Availability of funds. The Review Committee recommended (Rec 13(1)) that the code of banking practice should provide for banks and building societies to give their customers a simple explanation of the timing of the clearing cycle and the concept of cleared balances; that when a banker applies a "hold" period on cheques, that should also be explained; and that the banker should explain in what circumstances the bank has the right of reversal if a cheque is later returned unpaid.

1.18 There is undoubtedly demand from customers to be given a clear idea of their current, cleared balance, particularly when they would incur charges for an account being overdrawn. The Government accepts the arguments, in favour of the provision of more information, made by consultees. However, consultation also revealed a difficulty with this approach. Although it would be technically possible to show both cleared and uncleared amounts on

bank statements, it may risk confusing the customer. Statements would need to show changes in the cleared balance on days when no other transaction had taken place. To the financially sophisticated this may make sense, but many customers may see lengthier and more complex statements as unnecessarily bureaucratic. There may also be difficulty in providing both balances on ATM enquiries.

1.19 A compromise may be available which would enable the customer to determine the balance available to him, with minimum risk of confusion. A bank providing an uncleared balance could enable the customer to calculate a cleared balance by providing the information about the normal timing of the clearing cycle and the hold period put on cheques by the banker. This supports the intention that banks and building societies should give some clear explanation to their customers as to how they operate the account (that is, on the normal clearing cycle for credits and debits, the banker's hold time, and the reasons for a cheque to be returned); and it reinforces the case for including the provision of such information in the code of banking practice. The Government expects that the clearing time, particularly for debit card items, will be subject to some competition and would not wish to constrain this by specifying fixed times.

1.20 Truncation of cheques. The Review Committee recommended that banks should be permitted to truncate cheques. This would mean that cheques would no longer need to be returned to the paying branch; the information would be transmitted electronically from the receiving bank. The Government proposes to introduce legislation to allow truncation in due course. (The details of the proposals are covered in paragraphs 5.11-5.13 below.) The Government believes that it is important that the customer should have confidence in a system of cheque truncation if the banks wish to adopt it, and it is likely that this confidence would be enhanced if the customer knows that in the event of a disputed transaction, the banker would speedily resolve the problem or re-credit his account. The Review Committee recommended (Rec 7(14)) that, in the event of a dispute regarding a truncated cheque the bank should be given three working days to resolve the

dispute or re-credit the customer's account pending final resolution. Comments received during the consultation period suggest that a period of three working days from the complaint is too short for an absolute limit. The banks themselves should either suggest a single feasible period in the code of banking practice or make it clear in the code that the period would be notified to customers by their bank; the actual period being determined by the individual banks.

1.21 Validity of cheques. The Review Committee recommended (Rec 7(15)) that banks should not return a cheque within six months from the date of issue on the grounds that it was out of date. Existing legislation sets no specific time limit on returning cheques, referring instead to "payment within a reasonable time of its issue".

1.22 One major purpose of a code is to increase transparency and to improve the customer's understanding of how his account operates. It would be sensible to include this recommendation in the code of banking practice. Banks could specify a minimum time period for cheques and possibly a shorter time period for other forms of payment (for example girocheques). They would of course be free to exceed those minimum periods and make payment on a cheque on a date later than that specified.

1.23 Bank Giro Credits. The Review Committee recommended (Rec 7(16)) that banks should make available to their customer an explanation of the rights and obligations of the banker and customer in regard to transactions effected by bank giro credits. A bank giro credit is not defined in statute and conditions may therefore vary from bank to bank. However, the Government believes that any contractual arrangement between the banker and his customer should provide a clear explanation of the terms. This recommendation could therefore be subsumed in the general recommendation that the terms of operation of an account should be clearly stated.

1.24 Multi-function cards. Multi-function payment cards are now used extensively in the United Kingdom and as technology develops

they are likely to offer even more functions. The Review Committee recommended (Rec 11(2)) that banks should include three requirements in the code of banking practice concerning multi-function payment cards: customers should be free to select individual functions; other functions should be blocked off; and no liability should be borne by the customer for fraudulent use (other than on his own part) of the unauthorised functions.

1.25 The Government thinks it desirable that customers be given the choice to refuse to accept certain functions on the card. If so, it is reasonable that they should not bear any liability for those unused functions. If the banks are unable to block off particular functions then they should accept liability for the unused functions and, where relevant, should not issue personal identification numbers (PINs). These points should be covered in the code of banking practice.

1.26 Card notification organisations. The Review Committee raised a concern about card notification organisations. There is a possibility that a customer might believe that the organisation will be able to inform all the respective parties, even though one or more card-issuer may not recognise the card notification organisation and so would not accept notification of a loss of a card from that organisation.

1.27 Although this recommendation (Rec 11(4)) was generally accepted by consultees, the Government is not aware of any particular difficulties with card notification organisations. It believes that it is important for a customer, who accepts a contract with a card notification organisation, to be sure that the organisation will be able to carry out the service that he requires. The Government is not convinced that this issue should best be dealt with in the code of banking practice. It should be left for the terms and conditions of the contract between the cardholder, card notification organisation and the card issuer.

1.28 Countermand. The Review Committee recommended (Rec 12(1)) that the code of banking practice should include a provision which makes customers aware of the different countermand rules applying to payment systems. Countermand is an order to a banker to stop payment of a cheque, direct debit or other payment instruction which the customer has issued. A cheque backed by a cheque guarantee card may not be countermanded.

1.29 The Government believes that bankers should explain, through the code of banking practice, the circumstances when they could stop payment in the various clearing systems. They may also wish to explain to customers the fact that countermand does not cancel a debt. However, the Government would not support changes to the rules of payment systems to encourage an artificial period specifically to allow countermand. The customer, depending on the terms of the contract, may have a right to countermand, but that right is limited and should be exercised rarely (for example, where a cheque has gone missing and may have been stolen). It is usually the case that although a banker will attempt to countermand a cheque, that may not always be possible because the cheque has already been paid. In electronic payment systems the opportunity for countermand is further reduced because of the greater speed with which transactions are processed.

1.30 Charges. The Review Committee recommended (Rec 13(2)) that banks should explain to their customers the basis of charging for the normal operation of the account, including informing the customer about the charges which will be incurred with overdraft arrangements.

1.31 The Government strongly supports this recommendation. There is widespread support for greater transparency of bank charges. Many banks now routinely explain the basic charges for the operation of an account; and the recent moves towards publishing a full list of charges by major banks has been widely welcomed. The lists are to be sent to customers, displayed in branches and will

be regularly updated. The Government warmly welcomes this development. It is clearly desirable that customers should be made aware of charges they are likely to incur and, as far as possible, when they will be levied. Banks should not debit charges from a customer's account without prior warning of the amount, and that should be provided for in the code.

1.32 Foreign exchange transactions. The Review Committee's recommendation (Rec 13(3)) concerning foreign exchange transactions has already been accepted by banks and building societies. They advise customers of the relevant exchange rate and commission charge whenever possible. When the transaction requires a bank outside the UK to handle it or the customer orders currency to be collected at a later date it will not always be possible to offer anything other than an indication as to what the actual exchange rate or amount of commission might be.

1.33 Guarantees by individuals. The Review Committee recommended (Rec 13(5)) that bankers ensure that prospective guarantors, whether or not they are customers, are adequately warned about the legal effects and possible consequences of their guarantee, and about the importance of receiving independent advice.

1.34 The Government does not believe it is appropriate for bankers to be required to explain the legal effects and possible consequences resulting from an individual acting as a guarantor. That is a matter where proper legal advice should be sought. However it is important that bankers should advise prospective guarantors that they should seek independent legal advice before acting as a guarantor. The Government does not suggest that this recommendation need be included in the code of banking practice.

(iii) RULES SPECIFIC TO ELECTRONIC FUNDS TRANSFER

1.35 Authentication of customers' instructions. The Review Committee recommended (Rec 10(1)) that in the context of customer-activated EFT systems, the bank's principal and general duty should be to observe its customer's mandate. Therefore banks should adopt the principle that an EFT system should meet certain minimum standards of security in its authorisation procedures, so as to provide an acceptable degree of protection for the customer against the consequences of an unauthorised instruction.

1.36 The Government is not aware of any evidence of security shortcomings in existing technology. While identification of the customer is based only on a card and PIN there may be problems if the PIN becomes available to others. But that is a matter of customer practice rather than technology. It is in the banks' own interest to ensure that adequate standards exist. Banks have introduced more secure systems as new technology has become available and existing equipment is replaced. It is fundamental to all EFT systems operated by banks and building societies that the security and the protection of the interests of both the banker and the customer are paramount. Banks and building societies may wish to include a provision in the code of banking practice to state that they will continue to maintain minimum standards of security in their present and future EFT systems.

1.37 Issuing of cards and PINs. The Review Committee recommended (Rec 10(3)) that bankers take reasonable care when issuing cards and PINs to their customers. The unsolicited mailing of PINs should be banned and before a customer is able to make use of the service he should be required to acknowledge receipt of both card and PIN in writing.

1.38 It is clear both that the customer needs to take care of his card and protect his PIN number and that card issuers have an obligation to take reasonable care when issuing cards and PINs. The Government proposes (para 4.5 below) that legislation will be introduced in due course to ban the unsolicited mailing of all payment cards and PINs. In the case of the initial issue of a card which is requested, (for example when the customer opens an account or if he requests a new function or banking service) it is reasonable to expect the customer to acknowledge receipt of both card and PIN; but it does not seem necessary to extend that acknowledgement to the renewal of existing cards, where the existing PIN can be assumed to have reached the correct recipient. If that was required there would be a period between despatch of a new card and receipt of its acknowledgement when customers would be unable to use the card facilities. This would cause inconvenience to customers and impose unnecessary costs on the card-issuer.

1.39 Privacy when customers use EFT systems. The Review Committee recommended (Rec 10(4)) that banks ensure that maximum privacy is available to customers when they access EFT systems. The Government is satisfied that the banks already take steps to ensure that privacy is built into terminal design and that manufacturers will continue to develop better designs.

1.40 Monitoring of ATM withdrawals. The Review Committee recommended (Rec 10(7)) that banks and building societies should introduce systematic arrangements to monitor the patterns of automated teller machine (ATM) withdrawals. This recommendation arises from some well publicised cases where cash was illicitly removed using ATMs.

1.41 It is not clear that continuous monitoring would solve this problem. It is possible that it could reduce the occurrence of blatant fraud. But there is a danger in monitoring ATM usage that legitimate transactions could be stopped accidentally. Customers would suffer inconvenience if their transactions were stopped without warning and the banker could become liable for damages. Nevertheless banks may wish to introduce, subject to normal data protection arrangements, systematic monitoring of ATM withdrawals, which they would then include in their contract with the customer.

1.42 Rights to have a written record of ATM withdrawals. The Review Committee drew attention to the customer's entitlement, under the Data Protection Act 1984, to demand a written record of an EFT transaction which must be supplied within 40 days. The option of a written record at the time of the electronic funds transfer is already the existing practice with the majority of transactions. But it is not always possible to ensure that a written record will be immediately available if the machine runs out of paper.

1.43 The Government believes that this recommendation (Rec 10(8)) should be reflected in the code of banking practice on the basis that a written record should normally be available if the customer wishes it, at the time of an EFT transaction. This record would

be in addition to the written record which must be supplied in response to a customer's request under the Data Protection Act 1984.

1.44 Customer's right of action in disputed EFT transactions. The Review Committee recommended (Rec 10(9)) that the code of banking practice should detail the customer's right of action in the case of a disputed EFT transaction. The bank should acknowledge, as card issuer, that it would deal with its own customer, as card holder, in the cases of any complaint.

1.45 In disputed EFT transactions which involve more than one party, (for example, if the customer uses an ATM machine which does not belong to the bank which issued his card, and experiences difficulty) the customer may be left unsure as to whom to address his complaint. The Review Committee believed that it was sensible for the customer to complain initially to the institution that issued the card. It should be for them to ensure that steps are taken to consider the customer's complaint.

1.46 The Government understands from consultation that there are difficulties in implementing this specific recommendation (Rec 10(9)) in the code of banking practice. It nevertheless suggests that banks and building societies should include in the code of banking practice the principle that a customer should be made aware of who would deal with any complaint.

1.47 Apportionment of loss in disputed EFT transactions. The Review Committee recommended (Rec 10(13)) that the code of banking practice should make clear to customers the rules concerning apportionment of loss arising from a disputed EFT transaction. The general question of apportionment of loss is covered in paras 4.8-11 below.

Annex 2. Confidentiality and the disclosure of information

2.1 It is a long established legal principle that a banker owes a duty to his customer not to disclose to any third party information about the customer's personal affairs. That principle is subject to qualification only in certain circumstances.

2.2 The law which governs the bankers' duty of confidentiality was established in the case of Tournier v National Provincial and Union Bank of England in 1924. The judgment of Lord Justice Bankes in this case set out four exceptions under which a bank could legally disclose information about its customer: (a) where disclosure is under compulsion by law; (b) where there is a duty to the public to disclose; (c) where the interests of the bank require disclosure; (d) where disclosure is made by the express or implied consent of the customer.

The Committee's Proposals

2.3 The Review Committee stated that all their consultees agreed that the duty and the stated exceptions are still relevant to present day circumstances. But there was some concern among consultees that the exceptions were not closely enough defined for today's conditions, and so might be open to abuse. The Review Committee therefore recommended (Rec 5(1)) codification of the Tournier rules in statute and proposed that the exceptions should be redefined to reflect those concerns.

2.4 The concerns can best be summarised by grouping the four exceptions into pairs, as in the Report. The first pair of exceptions (a and b above) relates to disclosure under compulsion by law, and where there is a duty to the public. The Review Committee was concerned that, although individually worthy, the

cumulative effect of recent statutory exemptions constituted a serious inroad into the whole principle of customer confidentiality. The extent of the obligations under law led the Review Committee to question the need for the second exception: where there is a duty to the public.

2.5 The Review Committee therefore proposed that on codifying the duty of confidentiality, the first exception, where disclosure is under compulsion by law, should be redrafted. All existing statutory exemptions should be consolidated in new legislation and any future statutory exemptions should be made by reference to this new provision. The second exception, where there is a duty to the public to disclose, should be abolished. The legislation should make clear that no general disclosure provision exists.

2.6 The second area of concern which the Review Committee identified relates to commercial matters and is covered by the two exceptions (c and d above) which deal with circumstances in which disclosure is made "in the interests of the banker" or with the express or implied consent of the customer.

2.7 The Review Committee considered that there are two areas where banking practice has changed since the time of the Tournier judgment. Firstly, banks are now much more likely to be part of a group which includes non-banking subsidiaries such as estate agents or insurance companies and there is growing concern that information is being passed within a banking group for the benefit of the group's marketing activities, using the third of the Tournier exceptions. The Review Committee recommended that the third exception (where the interests of the bank require disclosure) should be limited. It should only allow disclosure between banking companies within the same group, of information that was necessary for the specific purpose of protecting the bank and its banking subsidiaries against loss, in relation to the provision of normal banking services.

2.8 The second area of concern was with the growing use of credit reference agencies and the release of information to them. The Report accepts that it should be possible for negative or

"black" credit information to be released where the interests of the bank require disclosure. But the Review Committee believe it is unclear what view the courts might expect to take on whether banks would be able to release positive or "white" information to agencies without the consent of the customer. (White information is credit information about customers who are not in default, whereas black information concerns customers who are in default).

2.9 The Report does not suggest that consumers are greatly concerned over the question of credit reference agencies as such. It acknowledges that the Director General of Fair Trading has, in practice, adequate powers to ensure that the agencies transmit credit information about individuals strictly for the purpose intended, and not for their subscribers' marketing purposes; and that they are always careful to check that their subscribers are bona fide operators. The Review Committee also recognised that there is considerable support within Government for the provision of information to agencies, to protect imprudent customers from overstretching themselves financially and taking on multiple debts which they cannot repay.

2.10 The Review Committee made two recommendations which would affect information being provided to credit reference agencies. It recommended that the fourth Tournier exception should be altered to require the express consent of the customer (that is, no longer ".... express or implied consent"). Express consent should be given in writing and state the purpose for which it is given. It also recommended that a new exception should be added. This would operate where there has been a breakdown of the banker-customer relationship arising through customer default. The effect of these two changes would be to allow the provision of "black" information to credit reference agencies, but not "white" information without the consent of the customer.

2.11 The Review Committee also believed that legislation should provide for damages for a breach of confidentiality and should include compensation for distress, embarrassment or inconvenience, regardless of whether financial loss could be proved.

The Government Response

2.12 The Government has considered very carefully the arguments put by the Review Committee and by those who have submitted comments during the consultation period. Several of those consulted argued that the present Tournier rules are very clear as they stand, they have worked well and they are well understood by bankers; it is unnecessary to codify them in statute, and any attempt to do so, or to refine them, risks introducing unwelcome and unintended difficulties and confusion. The Government finds these arguments persuasive. The particular concerns which have been expressed relate to specific, narrow areas of banking confidentiality rather than to the basic framework. That framework has worked well since the Tournier judgment and the Government is reluctant to interfere with an area of law which is long-established and familiar to practitioners. It does not therefore propose to codify the Tournier judgment in statute. However, a number of measures are proposed to tackle the specific concerns raised in the light of changes in banking practice.

2.13 The Government does not accept the Review Committee's view that there has been a "massive" erosion of the banker's duty of confidentiality over recent years through the various statutory exemptions from the general duty of confidentiality, such as those in the Drug Trafficking Offences Act 1986 and the Prevention of Terrorism Act 1989. These require bankers to disclose on suspicion, the location of funds which might be used for, or derived from, possible offences under the Acts. These and other similar statutory exemptions from the general duty are only enacted after the most careful consideration of all the implications. These are measures which would not apply to the vast majority of customers. In framing all such legislation, the effect on the normal confidential relationship between banker and customer is taken fully into account. These are, however, areas in which broader public policy will override the need to preserve that confidentiality.

2.14 The Government also believes that there is still a need for the second of the Tournier exceptions, where there is a duty to

the public to disclose. This exception gives a banker a safeguard if he believes that he must disclose information in the public interest. The statutory route requires information from the banker; this exception permits him to disclose. The increasing sophistication of financial crime means that there may well be cases in which a banker wishes to disclose information in the public interest, but he may be uncertain whether there is a specific statutory gateway for him to do so. The public interest gateway also allows a banker to disclose information to a supervisory authority (for example the Bank of England or the Building Societies Commission) where he considers that this would enable or assist that authority to discharge its supervisory functions even though the authority has not required the information to be provided under its powers.

2.15 The Government does, however, accept that changes in banking practice since the Tournier judgment may have affected the use of the third and fourth exceptions, namely where disclosure is in the interest of the bank, and with the consent of the customer. It believes that modifications to banking practice, rather than legislation, which might prove unnecessarily restrictive, would provide the most effective remedy. These changes should be reflected in the code of banking practice (discussed in Annex 1), and would therefore, be available to the Ombudsmen in dealing with complaints about use of confidential information.

2.16 The Government believes that disclosure between companies within the same banking group should continue to be allowed where the purpose of the disclosure is to protect the bank and its banking subsidiaries against loss. The Government believes, however, that banks should not pass confidential financial information outside banking companies in the same group for marketing purposes. In particular banks should not pass on edited information which implicitly reveals the financial status of the customer, such as a list of customers with "gold" credit cards. If a banker wishes to pass on confidential financial information for marketing purposes or to parties other than companies within the banking group, he should seek the consent of the customer.

2.17 Bankers must also continue to be able to pass "black" information to credit reference agencies. The Review Committee noted in their report that the Government favours the fullest possible transfer of credit information to agencies, subject to confidentiality considerations. They provide the best means of ensuring that potential borrowers are creditworthy. This is to the benefit of most consumers who would otherwise have to bear the cost of bad debts through higher charges.

2.18 The fourth of the Tournier exceptions, where the disclosure is made with the express or implied consent of the customer, is also relevant to information provided to credit reference agencies. It is possible that a banker may use the implied consent of the customer to provide "white" information about a customer to a credit reference agency. As the Review Committee point out, it is uncertain what view the courts may take of this. Consultation has shown that those representing consumer interests see this as an important issue. They would like banks to be required to seek the customer's consent and to ensure that the customer is fully aware of the bank's practice on passing information. However there is also general concern about consumer indebtedness, and the Government would not want to discourage the sharing of credit information where it contributes to responsible lending.

2.19 The Government therefore proposes that the code should require that where a bank intends to release to credit reference agencies confidential financial information which goes beyond the "black" information normally passed to such agencies, it should seek its customers consent. It should also explain why this is being done and give the customer a clear opportunity to object. If the customer decides to object to this information being passed, the bank should explain the possible consequences of such a decision. The customer should be informed of the bank's practice in this area, when he first opens his account with the bank, and existing customers should be reminded of the procedures when the terms of the account are varied.

2.20 This approach may not go quite as far as the Review Committee wished. However, the Government is persuaded that a system which required the specific consent of the customer every time information was passed would be impractical. It could result in information being passed much more slowly and possibly reduce the choice of credit to the consumer.

2.21 The Government believes that these changes are most sensibly implemented through the Code of Banking Practice. If they are included in that code, complaints about breach of confidentiality could be dealt with by the Ombudsmen, and the Government believes that that would generally provide a satisfactory means of redress for the customer.

Annex 3. Procedures for resolving disputes

3.1 The Government agrees with the Review Committee's desire to ensure that there is a satisfactory and comprehensive framework for resolving disputes between bankers and their customers.

3.2 The Review Committee recommended (Rec 15(1)) that all banks, except those with only a small number of customers, should be required by law to be a member of one or more recognised Ombudsman schemes, much on the lines of the arrangements for building societies. Building societies are already required by the Building Societies Act 1986 to belong to a recognised Ombudsman scheme which meets the minimum criteria set out in that Act and is approved by the Building Societies Commission.

3.3 At present the great majority of banks' personal customers are covered by a voluntary scheme. This was set up in 1986 by the banks and appears to enjoy the goodwill of both the member banks and the consumer bodies. Awards made by the Banking Ombudsman under this scheme are binding on the member banks.

3.4 The Banking Ombudsman scheme has recently been modified to take account of many of the concerns raised by the Review Committee. The revised terms of reference of the scheme are now based on similar lines to the statutory scheme for building societies, the only major difference being that the Building Societies Ombudsman's awards are not binding on the society: exceptionally, building societies can reject an award against them if they give their reasons for doing so publicly. The Government welcomes the changes made to the Banking Ombudsman scheme and views them as a further demonstration of the goodwill behind that scheme.

3.5 The scheme allows any deposit-taking business authorised by the Bank of England to apply for membership, subject to the approval of the Board. The present scheme covers 20 member banks (and a number of their associates) and includes all the major banks. It is noted in the 1989 Annual Report of the Banking Ombudsman that an independent market research survey commissioned by APACS shows that in the year ending June 1989 of all people who had bank accounts of any kind 99 per cent had their accounts with the banks which are members of the Ombudsman's scheme. As the Review Committee noted, there are a number of authorised banks for whom membership of the Ombudsman scheme is not appropriate, for example, merchant banks and banks with few, if any, personal customers. Other banks whose business is mainly providing credit are members of the Finance Houses arbitration scheme though at present this is limited to credit or hire agreements and does not cover other retail banking services provided by its members. There are also some smaller banks, with a branch network offering retail services, and some subsidiaries of the larger banks which are not members of any Ombudsman or arbitration scheme.

3.6 There are good arguments, which the Review Committee set out in their report, for seeking further consistency and convergence between the two Ombudsmen's schemes (Rec 15(3)). In theory, though probably not in practice, it may be confusing to customers that there should be different schemes applying to the provision of the same banking services by different institutions; and in theory it could lead to inconsistent decisions about the merits of similar cases, though again there is no evidence there that is a real problem in practice. Full consistency between the schemes could only be achieved, however, by removing from the Building Society Ombudsman scheme the option of rejecting an award and explaining publically the reasons for doing so, or by weakening the Banking Ombudsman's powers to make binding awards.

3.7 Opinions among the consultees were divided on this and the decision is a fine one. But on balance the Government believes that it is not worth disrupting two schemes which are working well, and proposes to leave the present arrangements as they are

for now. The Board of the Banking Ombudsman is taking steps to encourage more banks to join the scheme. Those who are members are encouraged to inform their customers and display notices prominently in their branches stating that they are members of the scheme. The Government will keep the situation under review and discuss with the representatives of the banks and building societies whether any further steps can be usefully made in the longer term to bring the two schemes closer together.

3.8 The Review Committee recommended that the Banking Ombudsman scheme should be extended to cover small businesses. The current schemes already deal with a very large number of complaints from unincorporated businesses including partnerships. The Government does not support any extension of the scheme to cover incorporated businesses. Ombudsmen are set up to give an individual the means of redress on a complaint without recourse to the courts. It is normally assumed that companies will be in a better position to take legal action through the courts.

3.9 Finally, the Review Committee suggested (Rec 15(2)) that banks should establish internal complaints procedures and inform customers of those procedures and of the existence of the Ombudsman scheme. The Banking Ombudsman contained the same proposals in his annual report for 1987/88. It is proposed that this should be covered in the code of banking practice which should also require banks to tell their customers whether they are, or are not, members of one of the Ombudsman schemes or the Finance Houses arbitration scheme.

Annex 4. Electronic Funds Transfer

4.1 In recent years, advances in technology have revolutionised banking services through the introduction of electronic funds transfer (EFT). This has led to more convenient banking for many customers at a lower cost than would otherwise have been possible. If such desirable innovation is to realise its full potential, it is important that the various problems that have arisen so far should be dealt with to reinforce consumer confidence but without imposing unnecessary restrictions on future developments.

4.2 The Review Committee recognised that flexibility is necessary but concluded that some steps should be taken to offer protection to consumers when using customer activated EFT systems. The Government accepts that limited legislation would be helpful.

Unsolicited Mailing of Cards and Financial Limits on Liability

4.3 The Consumer Credit Act 1974 provides protection to the consumer when taking credit. As a result of this legislation credit cards and certain other similar credit facilities are subject to a number of consumer protection measures.

4.4 The Review Committee recommended (Rec 10(2)) that section 51 of the Consumer Credit Act should be extended to cover the unsolicited mailing of all payment cards and (Rec 10(10)) that sections 83 and 84 which set the limits of legal liability should also be extended to cover all payment cards.

4.5 Section 51 of the Consumer Credit Act bans the unsolicited mailing of credit cards and certain other similar credit facilities. The Government intends to introduce legislation in due course to ban the unsolicited mailing of all payment cards

including ATM and cheque guarantee cards. This would not apply to renewal cards for existing customers.

4.6 Sections 83 and 84 of the Consumer Credit Act 1974 provide that the customer is only liable for any losses incurred as a result of the loss or theft of the card up to the point where he notifies the card issuer, subject to a financial limit which is currently fixed at £50. Again, the Act only applies to credit cards and certain other similar credit facilities. The Government intends to introduce legislation in due course to provide the same protection in respect of all payment cards. The card issuer will be liable for any losses incurred after notification, but will have a right of redress against a third party who can be shown to have contributed to the loss by fraudently using any EFT system. The card issuer should not be liable in cases where negligence on the customer's part enables a person to find out the PIN applicable to the card, for example where the number has been written on the card.

Liability in Event of Failure of EFT Equipment

4.7 The Review Committee recommended (Rec 10(11)) that customers should be compensated for any direct, or clearly consequential, loss due to the failure of customer-activated EFT equipment. Under current law a bank which undertook to transfer funds by means of an EFT system would be contractually liable for any failure in that system, except to the extent that it excluded the liability under contract. In the absence of any exclusion, damages will be awarded for any losses that were reasonably forseeable or were specifically contemplated by the bank and the customer. At present banks can exclude such liability in their contracts subject to the Unfair Contract Terms Act 1977. The Government proposes that, in the case of customer activated EFT systems, banks should not be permitted to exclude their liability by contract. Legislation will be introduced in due course which will enable an individual customer to be compensated for forseeable losses (and specifically contemplated losses) due to the failure of customer-activated EFT equipment despite any contract terms which restrict the bank's liability.

Disputed EFT transactions

4.8 Disputed EFT transactions are a matter which has caused some public concern. One of the recommendations put forward by the Review Committee (Rec 10(12)) was that there should be apportionment of loss in these cases. At present the terms and conditions imposed by the card issuers generally put the burden of proof on the customer. The evidence relating to disputed transactions taken to the Ombudsmen in the past indicates that many of them occur because a card has been used without the customer's knowledge or consent by a member of the family, a close personal friend or a colleague at work. Generally, the card and PIN were used at an ATM close to the complainant's home or place of work. Frequently, however, the customer asserts that he protected his card and PIN but bank records show a debit using that card and PIN, and that money was paid out by the ATM with no evidence of difficulty or malfunction.

4.9 Questions about disputed transactions which cannot be resolved at branch level or by senior bank management can and often are taken by the customer to the relevant Ombudsman who will have to take into account all the circumstances of the case. After consulting the Banking and Building Society Ombudsmen the Government has concluded that there are practical difficulties in accepting the Review Committee's recommendation.

4.10 When a complaint is made to one of the Ombudsmen about a disputed customer activated EFT transaction he first considers whether there is a case to answer; all that is necessary is for the customer to show that there is a problem. The burden of proof then effectively falls on the card issuer (bank or building society) to show that the card and PIN have been used to make the disputed transaction and that this was not affected by any technical breakdown or other deficiency. This is done by producing copies of the relevant records generated by the use of the ATM system in question. Once the Ombudsman is satisfied that the card and PIN were used, the burden of proof effectively falls on the card holder (the customer) to show that his card and PIN

could not have been used. The Ombudsman will then consider the evidence supplied by both parties.

4.11 A power to apportion loss as recommended by the Review Committee would not be applicable in most cases because the evidence before the Ombudsmen will be sufficient to enable them to establish the facts of the case. The cases where the Ombudsmen might be expected to use their discretion to take the factors identified by the Review Committee into account will be rare. In these cases the Ombudsmen will be confronted by conflicting evidence and, as in a court, will have to decide in favour of one party or the other. The Government, in not accepting apportionment of liability, believes that although it is ultimately for the customer to establish his case, he has ample opportunity to do so.

Forgery and Counterfeiting Act 1981

4.12 The Review Committee highlighted in their Report the problem of the counterfeiting of payment cards. Provisions in the Forgery and Counterfeiting Act 1981 make it illegal to counterfeit payment cards. However section 5(5) which deals with offences relating to the control or custody of instruments which a person knows, or believes to be, false does not explicitly apply to payment cards.

4.13 The Review Committee recommended (Rec 11(5)) that section 5 should be extended to include all payment cards. The Government accepts that, for the avoidance of doubt, section 5(5) should be so amended.

4.14 The Review Committee also recommended (Rec 11(6)) that the Forgery and Counterfeiting Act should be amended to include a provision which would make it a specific offence to possess, or to sell, information that could be used in the manufacture of counterfeit cards, with the intent to defraud. Whilst agreeing in principle, the Government has concluded that this recommendation would require a wider consideration of criminal law and does not at present propose to accept it.

4.15 In Scotland neither the Theft Act 1968 nor the relevant provisions of the Forgery and Counterfeiting Act apply. Instead common law principles relating to fraud and forgery apply. The Review Committee have recommended (Rec 11(7)) that consideration should be given to the creation of statutory offences for forgery and counterfeiting under Scottish law, similar to those contained in the Forgery and Counterfeiting Act 1981. The Government is not aware that the absence of specific provisions in Scottish law has any adverse consequences in Scotland and so no need is seen to legislate on this issue.

Annex 5. Cheques and payment orders

5.1 The present use of cheques is governed largely by the Bills of Exchange Act 1882. The only significant amendment since then has been the Cheques Act 1957. Although the cheques legislation was enacted when few people had bank accounts, and cheque usage was relatively low, the provisions have subsequently worked well. The Review Committee recommended a number of changes to bring the law up to date, which they proposed be enacted in a new separate Cheques and Bank Payment Orders Act.

5.2 The Government does not accept that there is a need for a new Act (Rec 7(1)) but proposes that many of the changes recommended by the Review Committee should be enacted through amending legislation to existing statutes.

Non Transferable Instrument

5.3 The Review Committee identified a number of areas where problems arise in the use of cheques. These include the fraudulent cashing of stolen cheques, and the confusion that exists, in both the public mind and in the law, as to the significance of various markings often put on cheques, particularly crossings on cheques. It examined two ways of resolving these problems. The first was to introduce a new instrument, the bank payment order, which would operate alongside the cheque and would be non-transferable, that is it could not be paid into an account other than that of the payee named on the instrument. The second was to clarify the effect of the existing markings and crossings on cheques. The Review Committee recommended the first alternative (Rec 7(7)).

5.4 The Government accepts that there is a need for a non-transferable instrument with a clearly established legal status and that the increased use of such an instrument should help to reduce the opportunities for fraud. It is also evident that the present legal status of the various markings and crossings is unclear and that customers believe they afford a greater measure of protection than is in fact the case. However, after detailed consultation the Government found that there was little support for the introduction of a new "bank payment order", largely because its introduction might well result in even greater confusion in the public mind about the use of cheques. On balance therefore, it has decided to tackle the problems identified by the Committee by measures designed to clarify the existing law relating to cheques.

Cheque Crossings

5.5 In general, customers have a reasonable understanding of the effect of crossing a cheque with two parallel lines. The 1882 Act gave statutory force to the general crossing of two transverse parallel lines, (with or without "and Co"), indicating that payment must be made through a bank. Although the Act recognises the use of the words "not negotiable"; this expression is not generally understood. "Not negotiable" does not mean a cheque cannot be transferred; it means only that if it is transferred, the holder will not get better rights of ownership than the person from whom he received it had, so that if, for example, he received it from a thief (in good faith) it will prove worthless. The Committee recommended (Rec 7(4)) that in order to clarify this complex area, statute should recognise only one form of cheque-crossing, consisting of two transverse parallel lines, and that the effect of this crossing would be to ensure both that the cheque must be paid through a bank, and that it would be "not negotiable" in the sense explained above. As at present the crossing might be pre-printed on cheques, with or without the words "not negotiable"; either way it would be not negotiable in law. The use of words such as "and Co" or "and Company" would continue to be optional though they have no special effect in law. The Government accepts this recommendation as a useful clarifying

measure and will introduce legislation in due course to effect it. It also accepts the recommendation (7(3)), that the special crossing, which identifies the banker or branch to whom payment should be made, is no longer necessary and should be repealed.

Non-Transferable Cheques

5.6 The Government agrees that there is a need for a clear method of making cheques non-transferable and proposes that this should be met by giving legal status to the words "account payee" or "a/c payee", with or without "only", written on the face of a cheque. A customer who writes these words on a cheque will make it "non-transferable" so ensuring that the cheque can only be paid into the bank account of the named payee. If a collecting bank credited the proceeds of a non-transferable cheque to the wrong account it would be unambiguously liable to the payee named on the cheque; the paying bank would not be liable. The paying bank would not know whether the cheque had been paid into the account of the named payee. The collecting bank would, however, have a defence if it could show that it had acted in good faith and without negligence, where for example, the account name was indistinguishable from that of the payee on the cheque and it had taken steps to establish the identity of the customer to whose account the proceeds of the cheque had been credited (following Recommendation 6(2)). These proposals will not preclude the use of the existing methods of making cheques non-transferable, namely writing "pay John Smith only", together with the deletion of "or order" from pre-printed cheques; or adding the words "not transferable". These are not however often used at present and the Government expects that these expressions will be used even less frequently when clear statutory backing is given to the words "account payee".

5.7 The Review Committee suggested that giving legal status to "account payee" might be unduly onerous to the banks, but their response to the consultation exercise indicated that on balance they would prefer that to a new payment order.

5.8 It is clear that bank customers will need to be made aware of these measures. The effect of the words "account payee" and the general crossing will have to be explained so that customers can understand the purpose of a "non-transferable" cheque on the one hand, and of a cheque that is simply crossed (that is "not negotiable") on the other. Banks may feel it is sensible to inform their customers through the code of practice or in cheque books. The use of open cheques will, however, still be possible for payments to individuals with neither a bank nor a building society account, despite the attendant risk of fraud.

Protection for Banks and Building Societies

5.9 The Review Committee recommended two changes to the law which offers protection for banks. The first (Rec 7(5)) is that the various statutory protections available to the paying bank would be made subject to the condition that the bank had acted "in good faith and without negligence", currently expressed in a slightly different form in each of the relevant statutory provisions. The existing sections 60 and 80 of the 1882 Act, section 1 of the 1957 Act and section 19 of the Stamp Act 1853, would be repealed. This recommendation is designed to clarify several inconsistencies in earlier legislation whilst retaining the spirit of the existing provisions. The Government accepts the recommendation.

5.10 The Review Committee also recommended (Rec 7(6)) bringing the law in Scotland into line with that in England for section 4 of the Cheques Act. In Scotland the law does not recognise the tort of conversion and common law appears to provide a defence unless there has been bad faith; however the Government is not convinced that banks in Scotland have significant additional protection. The Review Committee's report offers no evidence that the different law in Scotland is causing problems. Accordingly no need is currently seen for legislation on this point; instead the Government proposes to refer the question of the banks' protection in Scotland to the Scottish Law Commission for consideration.

Cheque Truncation

5.11 The banks have for some years been pressing for an amendment to the 1882 Act to facilitate the truncation of cheques. The Review Committee recommended (Rec 7(8)) legislation, which would be permissive and allow the truncation of cheques. Banks would be able to obtain payment by presentation of electronic information rather than the paper cheque itself, as currently required by the 1882 Act. A photocopy or some other reproduction in legible form, suitably marked and authenticated, would also be accorded the status of "evidence of the receipt by the payee of the sum payable by the cheque".

5.12 The truncation of cheques would eliminate the transportation of millions of cheques around the country each day. The pieces of paper would remain at the bank branch at which they were paid in (or local clearing point) and the relevant information to permit the debiting of accounts would be transmitted electronically. Some European countries already have systems of truncation in place.

5.13 The Government accepts the Review Committee's recommendation and will introduce the necessary legislation in due course. If banks introduce cheque truncation, however, it is important for there to be safeguards to ensure that the customer does not suffer as a result of this innovation. The Government proposes that there should be a provision in the code of banking practice that, unless the evidence to resolve a dispute about a truncated cheque is produced within a specific number of working days of the complaint, the bank should re-credit the customer's account that has been debited. The code should either suggest a single feasible period or make it clear that the period would be notified to customers by their bank, with the actual period being determined by the individual banks. Customers should also have the right under the code to receive, within a reasonable time, a photocopy (or the original) of any cheque which has been truncated. Banks should be required to keep the original cheques for a reasonable period.

Determination of the Amount Payable on a Cheque

5.14 The Review Committee recommended (Rec 7(9)) that precedence should continue to be given to the amount in words over that in figures on a cheque. The Government believes the existing practice is working well and supports the Review Committee's view that the law should not be amended.

Attachment of Funds in Scotland

5.15 The Review Committee recommended (Rec 7(10)) that the "funds attached principle" in Scottish law should be abolished except in relation to negotiable instruments other than cheques. Under section 53(2) of the 1882 Act (which only applies to Scotland) where the drawer of a cheque has insufficient funds to meet a cheque, the bank must "attach" any available funds in the account. The available balance is transferred to a suspense account where it can be released only when the cheque is re-presented and met, or with the payee's consent, or after five years, or after a judicial settlement. Once attached the funds cannot be used to meet other cheques drawn by the customer.

5.16 The Review Committee took the view that this provision is expensive to administer for the banks; causes inconvenience and sometimes hardship for their customers; and does not give significantly more protection to payees than is available in English law. Their recommendation would, for cheques, bring the law in Scotland into line with that in England.

5.17 This issue was last addressed by Parliament in the 1984/85 session when the decision was taken to retain attachment in the case of returned cheques. The law was changed in 1985 to remove attachment when the drawer countermands payment.

5.18 Abolition of the "funds attached principle" would have implications for certain long-established principles of Scottish law and the Government would not wish to proceed with it unless there was clear evidence that a change in the law was necessary and desirable. Accordingly, the Government proposes to consult

interested parties in Scotland on this recommendation and will take account of their views in reaching a conclusion.

Payable Orders

5.19 Payable orders, or warrants, are documents issued mainly (but not exclusively) by one Government department to be drawn on the same or another Government department, such as a National Savings warrant. They are treated as cheques by banks and their customers though they are not cheques as defined in the 1882 Act. The rules of negotiability therefore do not apply. The Review Committee recommended (Rec 7(11), 7(12)) that legislation should be enacted to equate Government payable orders and warrants, (for the payment of interest or dividends, or for repayment of capital) with cheques.

5.20 The Review Committee's proposals are a useful tidying up of the law which would state unambigiously that such instruments are to be treated as cheques for all purposes. The Government accepts the Review Committee's recommendations on payable orders and legislation will be introduced in due course.

Bank Giro Credits

5.21 The Review Committee have also recommended (Rec 7(13)), for the avoidance of doubt, that legislation should make it clear that a transfer instruction by Bank Giro Credit does not constitute a legal assignment of the funds involved.

5.22 The Bank Giro Credit has been developed by the banks over the last twenty years but, unlike cheques, is not governed by any legislation. Apart from this one point of clarification the Review Committee considered that legislation was unnecessary. The majority of legal authorities share the Review Committee's view that a Bank Giro Credit is not a legal assignment, but is merely an instruction to the bank. However, the Government proposes to introduce into legislation a clarifying provision to avoid future uncertainty.

Annex 6. Negotiable Instruments

6.1 Negotiable instruments (other than cheques) include bills of exchange, Treasury bills, certificates of deposit and bearer shares. The law relating to such instruments is of interest and importance to a comparatively small number of companies, traders and banks who deal in these instruments. It does not normally affect personal customers. The Review Committee made a number of recommendations this area. In particular, it proposed a new Negotiable Instruments Act. Much of this would be a consolidation and codification of existing statute and case law. The Government does not believe that such an exercise would be warranted and this chapter makes proposals only where the Government believes that some change in the law would be positively helpful.

6.2 The main existing legislation governing negotiable instruments is the Bills of Exchange Act 1882. That Act has worked well but some limited changes are necessary to bring the law up to date with modern circumstances. The Review Committee believed that the structure and language of the 1882 Act should be preserved (Rec 8(2)), and the Government supports that view. Changes to the law will therefore be achieved by amending the 1882 Act, when other pressures on the legislative timetable permit.

DETAILED PROPOSALS

6.3 The Review Committee recommended (Rec 8(3)) that there should be a statutory test of negotiability under the new Act covering not only bills of exchange and promissory notes but other instruments as well. The Government does not intend to extend the 1882 Act to embrace other instruments at present, and so it does not accept this recommendation. Other instruments, of course, are

negotiable at common law and the Government does not propose to change this.

6.4 The Government accepts the Review Committee's recommendation (Rec 8(5)) that the sum payable on a negotiable instrument should no longer have to be certain at the date of issue provided it is "certain or ordinarily determinable" in accordance with provisions which will be set out in amending legislation. This proposal aims to facilitate the use of instruments denominated in units of account like the ECU. The 1882 Act will therefore be modified so that the amount of a bill instead of being "a sum certain in money" will be "a certain or ordinarily determinable sum" which would be defined to include "a monetary unit of account established by an inter-governmental institution". The Government is aware that there may be technical difficulties involved in defining a sum as "ordinarily determinable". The sum payable will need to be objectively ascertainable and not dependent on private standards peculiar to the parties. Even then there may be some residual uncertainty, for example there may be a variation in rate during the day on which an instrument is payable. However the Government believes that it should be possible to overcome such difficulties.

6.5 In the context of discussing Recommendation (8(5)), the Review Committee raised the question of whether floating rate instruments, where the rate of interest rather than the currency is the problem area, should be brought into the 1882 Act. Most bills are drawn for 90 days or less and are traded at a discount; bills including interest are very rare. The Government has therefore concluded that there is no need at present to make special provision for floating rate instruments.

6.6 Noting and protest are procedures for providing formal proof that a bill of exchange has been presented and dishonoured. Protesting is mandatory under the 1882 Act for foreign bills because some overseas courts will not otherwise accept that a bill has been dishonoured.

6.7 The Government proposes to abolish the mandatory requirement for noting and protesting a dishonoured foreign bill. However this procedure would be retained in a slightly modified form for use on a voluntary basis. Anyone entitled to take an oath would be able to give a simple certificate of the facts in order to fulfil the requirements in those countries where noting and protesting are still necessary.

6.8 The Review Committee mentioned giving recognition to the "aval" in para 8.16 of their report. The Government intends to give legal recognition to the "aval". An "aval" is where a third person guarantees the payment of a bill by signing it. It is a common practice on the Continent which has received only limited recognition so far under English law. The Government proposes to amend the 1882 Act to recognise a guarantee given by way of an aval.

6.9 The Review Committee recommended (Rec 8(9)) legislation to provide a clearer statutory basis for the transfer of negotiable instruments by electronic means in screen-based or book-entry depository systems. The purpose of this recommendation is to facilitate the development in the City of London of a system (or systems) for the electronic transfer of negotiable money market instruments (for example, bills of exchange, Treasury bills, certificates of deposit), which are at present walked around the streets of London.

6.10 The Government believes that such a system will provide a more efficient method of trading in these instruments. The Bank of England has already announced its intention to provide a service for screen-based settlement of negotiable instruments through the setting up of the Central Moneymarkets Office (CMO). In its initial phase the CMO will provide screen-based transfers for money market instruments held in paper form in a central depository, which will operate within existing legislation. There would be considerable gains in efficiency if such instruments could be "dematerialised" (that is to say issued and traded in purely electronic form). However the absence of a physical instrument would mean that the rules on negotiable instruments

would not necessarily apply. The Government intends to legislate, when other pressures on the Parliamentary timetable permit, to give transactions in dematerialised instruments the same status as transactions in negotiable instruments generally.

6.11 The Review Committee have recommended, (Rec 8(10)), the adoption of a further 40 technical changes to the 1882 Act. (Appendix N of the Review Committee's report.) Many of these recommendations would be sensible if the 1882 Act were to be completely rewritten. However, since the Government does not envisage introducing a new Act at this stage, it proposes instead to amend existing legislation to include only Technical Recommendation 36, which would allow notice of dishonour to be given by electronic communication or by telecommunication.

Annex 7. Other Aspects of Banking Law

7.1 This annex considers the remaining aspects of banking law on which the Review Committee have made recommendations. The Review Committee have recommended amendments to the Bankers' Books Evidence Act 1879, and the Statute of Frauds Amendment Act 1828 and have made proposals for new legislation on completion of payment and contributory negligence.

Bankers' Books Evidence Act 1879

7.2 The original purpose of the Bankers' Books Evidence Act was to overcome the difficulties faced by bankers in having to produce their books of account during court proceedings to which they were not a party. The 1879 Act allowed properly authenticated copies of entries to be admitted as evidence in court and gave courts the power to make orders for inspection and copying of relevant entries in certain circumstances.

7.3 The Review Committee considered whether various sections of the 1879 Act need to be altered or updated. As a result they have made five recommendations. These would repeal the sections specially providing for the admission of copies of physical book entries; allow inspection orders prior to the start of legal proceedings; extend the definition of "bankers' books" to include credit slips and paid cheques; include the Bank of England in the definition of a "bank" and provide for the discretion to permit reimbursement of banks for the cost of complying with court inspection orders.

7.4 Sections 3 to 5 of the 1879 Act contain special provisions for the admissibility in court of copy evidence, and for the verification of entries in bankers' books. The Review Committee

concluded that banks, like other businesses of a reasonable size, no longer keep the majority of their records in physical form. The banks can therefore be treated in the same way as other businesses, and so it is no longer necessary to have special provisions relating solely to bankers' books.

7.5 Section 6(1) of the Civil Evidence Act 1968 applies to all documentary evidence relating to civil proceedings. It is sufficient to cover the records of banks and other businesses, both those held in physical form and on computer. It also expressly refers to the production of copies. Sections 24 and 27 of the Criminal Justice Act 1987 apply in a similar way to criminal proceedings. The Government therefore accepts the Review Committee's recommendation (13(6)) that section 3 of the Bankers Books Evidence Act should be repealed as it is no longer required, though legislation on this is not urgent. This proposal is subject to the findings of the Scottish Law Commission which is currently considering the subject of criminal evidence.

7.6 The Review Committee recommended (Rec 13(7)) that the 1879 Act should be amended so as to permit a court to make an order for inspection and copying of entries in bankers' books if it thinks fit, whether or not legal proceedings had formally begun. The order would only be granted in circumstances where the court was satisfied that a double criterion was met. Proceedings would have to be seriously contemplated and there would have to be grounds to support a prosecution or an action over and above what might be discovered as a result of the order.

7.7 Following the publication of the Review Committee's report those consulted expressed strong reservations about this recommendation despite the safeguard against "fishing expeditions" that it contained. The Government shares those concerns. In view of the important principle of banking confidentiality which is involved, the Government would require clear evidence of the need for this amendment in defined circumstances before supporting a change in legislation.

7.8 The current definition of "bankers' books" under section 9 of the 1879 Act encompasses ledgers, day books, cash books, accounts books and all other records used in the ordinary course of business of the bank, whether in written form or kept on microfilm, magnetic tape or any other form of mechanical or electronic medium. The Review Committee recommended (Rec 13(8)) that this section be extended to include credit slips and paid cheques where this is necessary to identify, confirm or provide necessary detail of book entries, thus taking account of changes in banking accounting practices over recent years. The Government believes that a wider definition of section 9 would be helpful and will propose legislation accordingly, in due course.

7.9 The Government also proposes to take a legislative opportunity to include the Bank of England in the definition of a "bank" or "banker" in section 9 of the 1879 Act (Rec 13(9)).

7.10 The Review Committee also recommended (Rec 13(10)) that the 1879 Act should be amended so as to give a court discretion to order payment of a fee to the bank against which an order under section 7 of the Act is made, in order to reimburse the bank for the cost of compliance.

7.11 Currently, banks are unable to seek recompense for complying with section 7 orders where they are not a party to the litigation, despite the cost imposed upon them. The Government supports the Review Committee's recommendation to give a court discretion to order payment of a fee to the bank against which an order under section 7 of the 1879 Act is made (as amended above) and will seek to amend the law accordingly.

Statute of Frauds Amendment Act 1828

7.12 The Review Committee recommended that section 6 of the Statute of Frauds Amendment Act 1828 should be repealed. The assumption underlying this recommendation was that section 6, the only section of the 1828 Act which has not been repealed, was no longer used. However consultation has shown that this assumption

is not correct. The Government does not therefore propose to repeal that Act.

Completion of Payment

7.13 The Review Committee recommended (Rec 12(2)) new legislation to define when a payment is complete. The few cases there have been on completion of payment leave the law unclear in a number of areas. The Review Committee's case for a statutory definition is based on the perceived need to provide more certainty about the legal consequences of a transfer of funds in the event of a bank failure.

7.14 The Government agrees that it would be desirable to have greater legal certainty in this area. It is an important issue which is currently exercising bankers and others around the world. Current initiatives include the United Nations Commission on International Trade Law Working Group on International Payments which is drafting a model law on international credit transfers. There is also a major study of payment netting schemes and cross-border payment systems being conducted by major central banks and the Bank for International Settlements.

7.15 The Review Committee offered a definition which is intended to be a codification of existing English case law. The Government has a number of doubts about the proposed definition. Some of those consulted questioned whether the proposed definition did indeed reflect existing law. Furthermore, the Committee analysed payment completion solely in terms of bank failure. There are many other more commonplace situations in which payment completion is important; for example, death or insolvency of a customer, court orders, system error and fraud. In view of the importance of this subject, recognised by the Review Committee and others who have commented on their recommendations, the Government believes that there would be dangers in the premature adoption in statute of a provision based on the Review Committee's definition.

7.16 The Review Committee also recommended (Rec 12(3)) that the Bank of England should convene a working group of interested

parties to consider and report on the operational implications of their definition of payment completion. The Government proposes that this working group should not be convened until the international initiatives mentioned above (para 7.14) become clearer. When the various domestic and international developments have been considered further, the Government will review the need for legislation on completion of payment and decide whether a working group convened by the Bank of England would be helpful.

Contributory Negligence

7.17 The Review Committee recommended (Rec 6(1)) that there should be a statutory provision whereby, in an action against a bank in debt or for damages arising from an unauthorised payment, contributory negligence may be raised as a defence if the court is satisfied that the degree of negligence shown by the plaintiff is sufficiently serious for it to be inequitable that the bank should be liable for the whole amount of the debt or damages.

7.18 At present, if a bank makes an unauthorised payment (for example, pays a forged cheque), the bank is liable for the loss regardless of whether the negligence of a customer contributed to the loss. Following a 1985 case (Tai Hing Cotton Mill Ltd v Liu Chong Hing Bank and others) banks and others have expressed concern that the law is unfair and should be changed to redress the balance in cases of unauthorised payments.

7.19 The Government agrees that the law at present is unfair to banks and is disposed to make it more evenly balanced between banks and their customers. The subject of contributory negligence was examined by the Law Commission which published a consultation paper entitled "Contributory negligence as a defence in contract" in January 1990. The paper considers how the concept could be applied as a defence in legal cases involving banks as well as in many other areas. When it has considered the responses to this consultation the Commission will submit a final report. It would be premature for the Government to propose revisions of the laws affecting banks to allow the defence of contributory negligence, when a much wider revision may be necessary. The Government will therefore make its proposals to change the law in this area when it has received and considered the Law Commission's final advice.

Annex 8. Wider Banking Issues

8.1 In preparing their report, the Review Committee have commented on a number of issues which went wider than their terms of reference. These matters all have a banking dimension, but the Review Committee were only able to offer comments on the banking implications of these particular issues. Their recommendations generally suggest that further work and consultation is needed before the banking problems identified by them can be considered in depth.

Consistency Across the Field of Payment Cards

8.2 The Review Committee were sympathetic to the need to ensure consistency of legal treatment in the use of payment cards. They took the view that it was unreasonable and confusing to customers if their rights and obligations differed greatly depending on which card they used. The Review Committee therefore recommended (Rec 11(1)) that the Government should consider how consistency of law and practice, across the field of payment cards generally, can be best achieved in the case of payment cards issued by retailers and other non-bank institutions.

8.3 The Government accepts that consistency of law and practice across the field of payment cards generally is an issue on which further work may be necessary. This White Paper includes proposals which will have the effect of achieving consistency in the main areas where unjustifiable differences of treatment have been identified. Of course, in some areas differences of treatment may be appropriate, for example, if cards offer different facilities. Some payment cards offer credit whereas others are purely debit cards. The Government will keep the area under general review, in the light of developments in the banks'

code of practice, and will give careful consideration to any representations it receives about unjustified inconsistencies.

Connected Lender Liability

8.4 The concept of connected lender liability was introduced by section 75 of the Consumer Credit Act 1974. The rationale behind the rules of connected lender liability is that the connected lender and the seller are in effect engaged in a joint venture to their mutual advantage and their respective roles cannot be isolated. The 1974 Act provides that purchases made using a credit card are to be covered by the provisions of section 75. The Review Committee were impressed by the arguments put forward by the banks that the connected lender liability should be removed from credit cards.

8.5 The Government's recent review of the Consumer Credit Act confirmed the general rationale for connected lender liability. Since issuers of credit cards benefit from the purchases made with their cards the Government does not accept the Review Committee's recommendation (Rec 14(1)) that there should be an exemption from the connected lender liability provisions of the Consumer Credit Act for purchases financed by the use of credit cards.

Constructive Trust

8.6 The Review Committee drew attention in their report to the concept of the constructive trust, which arises when a person who has not been appointed to act as a trustee becomes involved in the affairs of a trust (for example providing banking services to trustees) as a result of which the liabilities of a trustee are imposed upon him. This concept has particular implications for banks since a bank can become subject to a constructive trust, for example, when it honours a cheque which it knows or ought reasonably to know is a misapplication of trust money. The Review Committee were concerned about the uncertainties surrounding the present state of the law and how it might evolve by judicial decision in the future. Therefore they recommended (Rec 14(2))

that the concept of constructive trust should be examined in depth by the Law Commission.

8.7 The concept of constructive trust extends to many areas of law and is not confined to banking. The Government will in due course determine with the Law Commission whether a general review of this topic would be of use. It is meanwhile considering with the Law Commission an examination of one aspect of this topic: the interrelationship of fiduciary duties and regulatory rules.

Set-off

8.8 The Review Committee identified a concern with the law of set-off. This was that section 323 of the Insolvency Act 1986 might have excluded contingent liabilities which are not due and payable at the commencement of the bankruptcy from being taken into account. This was thought to cast doubts on a banker's ability to set-off contingent liabilities which become actual liabilities after notification of insolvency.

8.9 The Government proposed an amendment in the Companies Bill to deal with the perceived doubt. However, on further consideration, the amendment whilst clarifying the position of some contingent claims, unacceptably widened the potential scope of those claims capable of inclusion in the set-off. The amendment was not therefore pursued.

8.10 Another concern identified by the Review Committee relates to the judgment of Mr Justice Millett in the case of Re Charge Card Services Limited (1986). He found that a creditor (eg a bank) cannot validly take a charge over a debtor's (eg a customer's) credit balance with the creditor as security for a loan made to that debtor. However, this form of security has in practice been used by the banks in order to obtain wider rights over a customer's credit balance than that available under statutory set-off and the judgment was therefore of great concern to them. The Review Committee recommended that the Government should institute a process of consultation with a view to removing the uncertainty surrounding Mr Justice Millett's judgment.

8.11 The Review Committee's concern relating to the validity of a charge over a credit balance in favour of the person with whom the balance is held involves complex issues. The Government is giving the matter further consideration to establish whether a solution can be found that is acceptable to all interested parties.

Bank Holidays

8.12 The Review Committee examined the banking implications of the mismatch of bank holiday dates as between England and Wales on the one hand, and Scotland on the other. There is also a mismatch with two dates in Northern Ireland. The problem for banks, particularly in Scotland, relates mainly to transactions passing through the electronic clearings and stems from the fact that settlement of these inter-bank transactions for the whole of the United Kingdom takes place in London. Thus when London is closed there is no settlement, whilst settlement does take place on days when there is a Scotland-only bank holiday. This can lead to extra costs for Scottish banks, and may give rise to confusion and complaint on the part of their customers.

8.13 The Government notes the Review Committee's concerns about the banking problems associated with the mismatch of bank holiday dates as between England and Wales, and Scotland. The Government does not propose to harmonise dates within the United Kingdom (Rec 14(4)) and believes that it is for the banks themselves to resolve this difficulty by contract or administrative procedures.

A Minor's Capacity to Contract

8.14 The Review Committee did not formally consult on the question of banking for minors but their attention was drawn to concerns that parents have expressed regarding banks' insensitivity about the banking activities of their minor children and the use made of information about minors with bank accounts. Bankers clearly face a dilemma arising out of the conflict between the rights and duties of a parent or guardian, and the bank's relationship with a young person for whom the parent or guardian

is responsible. The general legal principle is that during minority, the capacity to contract is severely limited and the minor is protected to the extent that many obligations incurred are not in fact enforceable. If a bank allows, or permits by accident, an overdraft on a minor's account, then the bank faces the delicate decision regarding parental involvement in obtaining repayment. In addition, credit marketing to minors is prohibited by law. The Government is concerned that banks should exercise particular care to ensure that information held on minors with bank accounts is not used for marketing purposes.

8.15 The Scottish Law Commission have recently examined the question of a minor's capacity to contract and the Review Committee have recommended that the Government should consider introducing into legislation the recommendations of that Commission. In addition the Review Committee recommended (Rec 14(5)) that the Government should consider instituting a similar review of the English law dealing with a minor's capacity to contract.

8.16 The Review Committee's concerns about the English law dealing with a minor's capacity to contract have been noted (Rec 14(5)). The Government has accepted the Scottish Law Commission's recommendations, which were included in a Private Members Bill in the last session of Parliament; unfortunately, this failed to make progress, but the Government remains committed to the principle of legislation. A similar review for England and Wales was undertaken by the Law Commission in 1984 which led to the passing of the Minors' Contracts Act 1987 and the Government does not believe that a further review in England is necessary at this time.

Evidential Requirements of the Criminal Law

8.17 The subject of the admissibility of computer produced evidence in court has been raised by the Review Committee in the context of fraud through EFT systems, though they recognised that it has much wider implications. The Review Committee concluded that if current evidential requirements hinder the conviction of

fraudsters then those requirements should be reviewed. Therefore they recommended that consideration should be given to a review of those requirements, insofar as they relate to the corroboration of computer-produced evidence in cases of fraud.

8.18 The Government would be ready to review the evidential requirements for computer produced evidence if it were shown that they were in practice hindering the prosecution and conviction of fraudsters.

Computer Hacking

8.19 The Review Committee recommended (Rec 14(7)) that action should be taken to make it a criminal offence to obtain unauthorised access to a computer by "hacking", as recommended by the Scottish Law Commission and to introduce "viruses" into computer programs.

8.20 The English Law Commission have also published a report on computer misuse, in which they recommend the creation of three new offences. These would cover the types of misuse identified by the Review Committee. In his response to the report, the Secretary of State for Trade and Industry stated that he was inclined to accept the recommendations. A Private Members' Bill was introduced into the House of Commons on 20 December 1989 to give effect, with modifications, to these recommendations. The Bill also takes into account earlier recommendations made in the Scottish Law Commission report referred to above.

Customer Choice in the Means of Payment

8.21 The Review Committee have recommended that the Government keep under periodic review the scope for customer choice as between different payment systems, and the related question of the acceptability of legal tender, to ensure that there is no unfair discrimination through contractual arrangements, charging or financial incentives (Rec 14(8)). In this recommendation the Review Committee were highlighting a general concern that as

payment systems develop, a customer's choice of payment method may be restricted.

8.22 It is of course important to bear in mind the needs of the those who do not have bank or building society accounts and who should be able to continue to tender with cash. At present in the United Kingdom although cash is legal tender, it is open to a person to refuse to enter into a transaction with another person who is only willing to pay in cash. A shopkeeper, for example, is not obliged to sell any of his goods simply because they are on display, and could, for instance, refuse to sell them except to someone who is prepared to pay for them by means of a cheque. If he has already entered into a transaction however, and is owed money for the goods sold, he cannot successfully pursue that person in the courts if offered legal tender in settlement. Discrimination in favour of one payment system or against another, whether through contractual agreement, charging or the use of financial incentives, might, in some circumstances, give rise to concern, particularly if the effect were anti-competitive. However the Government recognises that different payment systems incur different costs. The Government therefore accepts the principle behind the Review Committee's recommendations for periodic considerations of the scope for customer choice as between different payment systems (Rec 14(8)).

Future Review of Banking Services Law and Practice

8.23 The Review Committee concentrated on those areas of banking services law and practice which at the present time appear to them to require priority. Whilst they have done their best to allow for future developments they have emphasised that the development of electronic banking is expanding at an increasing rate. Therefore priorities will change with time and the Government should keep under review the possible need for further studies to deal with the rapid change in banking services. The Government accepts the need for further studies (Rec 17(1)) to deal with the priorities as and when they emerge in the field of banking services law and practice.

Annex 9. Scope of the Proposed Legislation

Legislation will be introduced, when other pressures on the legislative timetable permit, for the following purposes:

(a) banning the unsolicited mailing of all payment cards (Committee recommendation 10(2)/paras 4.4-5);

(b) restricting a customer's liability for loss in the case of payment cards (recommendation 10(10)/paras 4.6;

(c) imposing on banks liability for the failure of electronic funds transfer equipment (recommendation 10(11)/paras 4.7);

(d) clarifying the meaning of crossings on cheques and giving statutory recognition to the words "account payee" (recommendation 7(2), 7(4)/paras 5.6);

(e) permitting the truncation of cheques (recommendation 7(8)/paras 5.11-13);

(f) clarifying the status of payable orders and bank giro credits (recommendations 7(11),(12),(13)/paras 5.19-22);

(g) extending section 5(5) of the Forgery and Counterfeiting Act 1981 to apply to all payment cards (recommendation 11(5)/paras 4.12-13);

(h) repealing sections 3 to 5 of Bankers' Books Evidence Act 1879 (which relate to the admissibility in evidence of copies of entries in bankers' books) (recommendation 13(6)/paras 7.2-7.5);

(i) amending the Bankers' Books Evidence Act 1879:-

i. to extend the definition of "bankers' books" in section 9 to include cheques and credit slips (recommendation 13(8)/para 7.8);

ii. to extend the definition of "bank" and "banker" in section 9 to include the Bank of England (recommendation 13(9)/para 7.9); and

iii. to give a court discretion when making an order under section 7 to order payment of a fee to reimburse the bank for the cost of compliance (recommendation 13(10)/para 7.11);

(j) restructuring the various statutory protections available to the paying bank under the Cheques Act 1957, the Bills of Exchange Act 1882 and the Stamp Act 1853 (recommendation 7(5)/para 5.9);

(k) updating the Bills of Exchange Act 1882:-

i. to provide that the sum payable on a negotiable instrument will no longer have to be certain at the date of issue if it is "certain or ordinarily determinable" in accordance with the provisions set out in the Act (recommendation 8(5)/para 6.4);

ii. to remove the mandatory requirement for noting a protest of a dishonoured foreign bill, while retaining the procedure for use on a voluntary basis (recommendation 8(8)/ para 6.6-7);

iii. to permit transactions by way of screen based or book entry depository systems operated by an approved depository including transactions in "dematerialised" instruments (recommendation 8(9)/paras 6.9-10); and

iv. to allow notice of dishonour to be given by electronic communication or by telecommunication (Technical Recommendation 36) (recommendation 8(10)/para 6.11).

Annex A: Review Committee's recommendations

The Review Committee made 83 recommendations, 26 addressed to banks and building societies and the remainder to Government. The Government's response to individual recommendations (reproduced below) can be found in the following Annexes to the White Paper.

Annex 1: The Code of Practice

Recommendation 16(1): Banks should promulgate a Code of Banking Practice on matters that are the subject of Recommendations in this Report on standards of best practice addressed to banks, giving priority to the EFT area. If in any particular respects they can see good reason for departing significantly from the terms of the illustrative Code at Appendix L, they should consult consumer and other interests.

Recommendation 6(2): As an indication of what is required for banks to secure the protection of Section 4 of the Cheques Act 1957 (under the current legislation), they should initiate procedures which allow them to establish, to their reasonable satisfaction, the identity of a person opening an account, so that if subsequently challenged they can refer to the action they took at the time.

Recommendation 6(3): A standard of best practice should require a bank, in any communications to its customer of the terms of the banker-customer contract, to ensure he is given a fair and balanced view of those terms, and of the rights and obligations that exist on each side; and to give him reasonable notice of any proposals for variation of those terms.

Recommendation 15(2): A standard of best practice should require banks to establish clearly defined internal procedures for handling customer complaints; to ensure in some appropriate way that customers are told how to lodge a complaint, and how it would be dealt with; and to ensure that, as and when a complaint arises, the customer is made personally aware of the existence of the bank's internal procedures, and of the relevant procedures of the Banking or Building Societies Ombudsman, as appropriate.

Recommendation 5(2): A standard of best practice should enjoin banks to explain clearly to all their customers the rules on the banker's duty of confidentiality, once codified in statute law. It should require banks to remind customers of their right of access, under the Data Protection Act 1984, to computer records about themselves held by banks. It should state that express consent, in whatever form, should not be sought in such a way as puts the customer under pressure to give it. In the case of express consent to be obtained in tacit form for the giving of bankers' opinions, a letter should be sent personally by the bank to its customer, seeking his consent for this specific purpose(s).

Recommendation 6(4): A standard of best practice should require a bank to give all its customers a clear explanation of how the system of bankers' opinions works, and to invite them to give or withhold a general express consent for the bank to supply opinions on them in response to status enquiries.

Recommendation 13(4): A standard of best practice should require banks, in the direct marketing of their services, to exercise restraint, and in particular:

- to ensure that customers are aware of the marketing purpose for which they are being approached, and

- to respect any customer's objections to the use of personal information for marketing purposes, and to desist from such activity on request.

Recommendation 13(1): A standard of best practice should require banks to give all their customers a simple explanation of the timing of the clearing cycle, and the concept of cleared balances. This would deal, especially, with the normal time taken to clear cheques and bank payment orders, should specify the "hold" period the bank is applying, and should say whether the bank has a right of reversal if the cheque or bank payment order is later returned unpaid. But it would cover other payment systems as appropriate, including the timing of direct debit procedures, and the customer's right of reversal under that system. Where needed, an explanation should be given of the system of truncation of cheques and bank payment orders, and of resulting changes, if any, in the timing of the clearing cycle. Banks should consider how their customers could usefully be given more information, in periodic statements of account and in ATM slips, about cleared as well as uncleared balances on their account.

Recommendation 7(14): It should be a standard of best practice that, if the necessary evidence to resolve a dispute regarding a truncated cheque or bank payment order is not produced within three working days, the customer's account should be re-credited pending final resolution.

Recommendation 7(15): There should be a standard of best practice to the effect that a bank should not return, within six months from the date of issue, an instrument covered by the new Cheques and Bank Payment Orders Act on the grounds that it was out of date.

Recommendation 7(16): A standard of best practice should require banks to make available in a leaflet, or by other suitable means, an explanation of the rights and obligations of bank and customer in regard to transactions effected by BGC including the rules on countermand.

Recommendation 11(2): A standard of best practice on multi-function cards should establish that:

- a customer should be free to choose which of the functions on his card should be available for use; a bank should not be at liberty to refuse a card for a single function if its customer does not require more;

- functions that the customer does not require should be blocked off, so that the card cannot be used for those purposes in a machine;

- if for whatever reason the card is nonetheless compromised, the customer should (fraud on his part excepted) have no liability on all functions that he has not authorised.

Recommendation 11(4): All banks as card-issuers should, as a matter of best practice, inform all customers as cardholders:

- whether or not they themselves will accept notification of loss or theft of a payment card from a third party, presumably a card notification organisation;

- if so, the terms in which they would require cardholders to notify them, by a standard form of notice acceptable to card-issuers and signed by cardholders, of the appointment of an agent for this purpose;

- the effect, if any, on the cardholder's liability if an agent is appointed, especially the matter of whether notification to the agent discharges the cardholder's obligation to the card-issuer.

Recommendation 11(3): Legislation should be introduced requiring card notification organisations to be licensed by the Director-General of Fair Trading. It should include a power by which the Director-General, if he saw fit, could impose on such organisations a requirement to take out a fidelity bond, and an errors and omissions policy in a suitable sum, as a condition of the grant or continuance of a licence.

Recommendation 12(1): A standard of banking practice should require banks, when establishing countermand rules for individual payment systems, to allow customers a period of time for countermand wherever possible, only eliminating it where that is necessary for the efficient working of the system. Banks should take steps to make customers aware of the different countermand rules applying to different payment systems.

Recommendation 13(2): A standard of best practice should require banks to explain to their customers the basis of charging for the normal operation of the account. Where an overdraft arrangement has been agreed in advance, a bank should ensure that its customer is aware, both in advance and as and when a change occurs, of the rate over base rate that will be charged, and of the timing of the debiting of interest. The customer should also be given full details of the method of calculation of fees and charges, when these are applied to his account, including charges applied where an overdraft occurs without prior agreement. The customer should also be told of any services other than lending for which he will be charged (stopping cheques, correspondence etc).

Recommendation 13(3): A standard of best practice should require a bank, when undertaking a foreign exchange transaction for its customer, to ensure that he is made aware of the basis of the exchange rate to be applied, and of any associated charges.

Recommendation 13(5): A standard of best practice should require banks to ensure that prospective guarantors, whether or not they are not customers, are adequately warned about the legal effects and possible consequences of guarantees, and about the importance of receiving independent advice.

Recommendation 10(1): A standard of best practice should translate into the context of customer-activated EFT systems a bank's principal and general duty to observe its customer's mandate. Banks should therefore adopt the principle that an EFT system must meet certain minimum standards of security in its authorisation procedures, so as to provide an acceptable degree of

protection for the customer against the consequences of unauthorised instructions. In furtherance of that principle, they should accept a continuing commitment to upgrade their systems by the introduction, so far as practicable, of new technology based on the recognition of a signature or other personal characteristic.

Recommendation 10(3): A standard of best practice should require banks to take every reasonable care when issuing cards and PIN's to their customers. It should state that that obligation should be undertaken by banks on the explicit assumption that customers for their part will take every reasonable care at all times in handling their cards and PIN's. It should also ban the unsolicited mailing of PIN's by banks to customers, following the principle proposed for legislation in respect of the mailing of payment cards. A customer should be required to acknowledge receipt of both card and PIN, before he can avail himself of the service for which they are needed.

Recommendation 10(4): A standard of best practice should require banks to ensure the maximum privacy that is reasonably possible in customers' access to EFT systems. In particular banks should aim to ensure that it is physically impossible for a customer's PIN to be read by anybody else when he is keying it in.

Recommendation 10(7): A standard of best practice should require banks to introduce systematic arrangements where they have not done so already, to monitor patterns of ATM withdrawals, such as might give rise to suspicion of fraudulent misuse of the system.

Recommendation 10(8): A standard of best practice should draw attention to customers' entitlement, under the Data Protection Act 1984, to demand a written record of an EFT transaction if they wish to have it; and should require banks to interpret this in the sense that customers are given the option of a written record at the time of the transaction, rather than in due course.

Recommendation 10(9): A standard of best practice should require a bank, as card-issuer, to deal with its own customer, as

cardholder, in case of any complaint or claim arising on the customer's part from a dispute over a banking service provided through an EFT payment system. It should be for the card-issuer to take action against any other party involved, for example in an EFT-POS system or shared ATM network.

Recommendation 10(13): A standard of best practice should require banks to make customers who use the relevant services aware of this rule in Recommendation 10(12) on apportionment of loss arising from a disputed EFT.

Annex 2: Confidentially and the Disclosure of Information

Recommendation 5(1): The Tournier rules on the banker's duty of confidentiality, suitably updated to comply with modern conditions, should be codified in statute law.

Recommendation 5(3): The Government should not further extend the statutory exceptions to the duty of confidentiality, without taking full account of the consequences for the banker-customer relationship.

Annex 3: Procedures for Resolving Disputes

Recommendation 15(1): Statutory provision should be made for comprehensive coverage of authorised banks, except those with less than a given (small) number of customers, by one or more recognised Ombudsman schemes. Statutory responsibility for granting recognition to such a statutory scheme (or schemes), and for withdrawing any recognition it has granted, should be placed on the Bank of England. The statute should lay down matters to be provided for in a statutory scheme (or schemes) and the requirements for recognised schemes as regards matters of complaint, grounds of complaint, functions of the Ombudsman, etc. There should be statutory provision for periodic review and amendment of the terms of the scheme (or schemes).

The Review Committee's preference is for a single Scheme for authorised banks based on the present Banking Ombudsman Scheme,

except that responsibility for approving the Ombudsman's terms of reference, for appointing independent members of the Council, and for approving the appointment of the Ombudsman himself, or its renewal or termination, would pass from the Board to the Bank of England. The Board would remain responsible for finance. The membership of the Council should be increased to eight by the addition of one more independent member. Any individual should be precluded from serving on both the Board and Council of such a Scheme. A bank rejecting a non-mandatory award under such a Scheme should be required to publish its reasons for doing so. It should be considered whether a suitable eligibility criterion could be devised which would allow small businesses to be brought within the ambit of such a Scheme.

Under such a Scheme, the following specific amendments should be made to the Banking Ombudsman's terms of reference:

- The Ombudsman should be required, if a complaint has not been resolved in some other way, to make a determination by reference to what is, in his opinion, fair in all the circumstances.

- The Ombudsman should be given a power to compel production by a bank of any relevant documents or information.

- The power whereby a bank may withdraw from the Ombudsman's jurisdiction any complaint which has wide ramifications, or raises important legal issues (the "test cases provision"), should be exercised only with the concurrence of the Ombudsman.

- The Ombudsman should be allowed to publish information about a complaint if the customer consents.

- The present requirement that complaints must in all cases be made by "all beneficiaries" should be dropped.

- Banking services for bank employees and their dependants should be included within the scope of the Scheme, unless there is a disciplinary issue involved.

Recommendation 15(3): The Government should consider the scope for rationalisation, in some form, between a statutory Banking Ombudsman Scheme and the Building Societies Ombudsman Scheme, to cover at least the banking services area; and for any limited convergence as between the two Schemes that could usefully be achieved meanwhile.

Annex 4: Electronic Funds Transfer

Recommendation 10(2): A provision in statute law should ban the unsolicited mailing of all payment cards by banks to their customers, apart from credit cards already covered by Section 51 of the Consumer Credit Act 1974.

Recommendation 10(10): A provision in statute law, applicable to any customer-activated EFT system, should set the limits of legal liability for loss due to fraud on the principles established in Sections 83 and 84 of the Consumer Credit Act 1974. The main provisions are that a customer should normally be liable for any losses incurred up to the point where he notifies his bank, subject to a financial limit currently fixed at £50; the bank should be liable for any losses incurred thereafter. Where gross negligence on the part of either party could be demonstrated, that party should be liable for any amount up to the full amount of the loss. The bank's duty should be in any event to its customer, but the bank should have a right of relief against a third party who could be shown to have contributed to loss by fraud through an EFT system.

Recommendation 10(11): A provision in statute law, applicable to any EFT system, should make the bank normally liable to the customer for any direct, or clearly consequential, loss due to the failure of EFT equipment to complete a transaction, notwithstanding the terms of any contract to the contrary. Compensation may be reduced if the failure is due to causes beyond

the bank's control, of if intent or gross negligence on the customer's part has contributed to the fault. If, in the case of a customer-activated system, the customer should have been aware that the equipment was unavailable for use or malfunctioning, the bank's liabilities should be limited to the correction of any errors on the customer's account, and the refund of any charges or fees imposed on him as a result. It should be for the bank to resolve with third parties any question of liability on their part.

Recommendation 10(12): A provision in statute law should apply, notwithstanding the terms of any contract to the contrary, to the apportionment of any loss arising from a transaction carried out through a customer-activated EFT, where it is in dispute whether or not that transaction was authorised. It should require that loss to be apportioned on an equitable basis, by reference to the extent to which the acts or omissions of the parties have contributed to the loss. Apportionment of the loss should take into account such factors as (i) the steps taken by the customer to protect the security of his card and PIN, (ii) the extent to which the system provided by the bank protects the customer against unauthorised transactions on his account, and (iii) the relative weight of the evidence adduced by the parties in support of their respective contentions that the transaction was, or was not, authorised.

Recommendation 11(5): Section 5(5) of the Forgery and Counterfeiting Act 1981 should be made applicable, through amending legislation, to all payment cards generically.

Recommendation 11(6): A provision should be inserted in the Forgery and Counterfeiting Act 1981 to make it a specific offence to possess, or to sell, information that could be used in the manufacture of counterfeit cards, with intent to defraud.

Recommendation 11(7): Consideration should be given to the creation under Scots law of statutory offences in relation to card counterfeiting on the lines provided under 1981 Act, amended as under Recommendations 11(5) and 11(6).

Annex 5: Cheques and Payment Orders

Recommendation 7(1): The law relating to cheques should be re-enacted in a new Act, to be called the "Cheques and Bank Payment Orders Act". It should incorporate amendments recommended in [Chapter Seven of the Review Committee's report].

Recommendation 7(7): The new Act should include provisions permitting the introduction of a new non-transferable instrument (the "bank payment order") the proceeds of which could be collected only by a bank and solely for account of the named payee.

Recommendation 7(2): The new Act should contain a provision to the effect that nothing written on any cheque can take away the right to transfer it; this would deny legal effect to any annotation such as "Account Payee".

Recommendation 7(3): The new Act should provide for the special crossing, though banks should continue to be permitted to stamp their name and address on the face of cheques for collection purposes.

Recommendation 7(4): The new Act should recognise only one cheque crossing. It should consist of two transverse parallel lines as now, the effect of which would be to make the cheque "not negotiable" in addition to requiring payment only to a bank.

Recommendation 7(5): The new Act should bring together the various statutory protections available to the paying bank and each should be made subject to the condition that the bank had acted "in good faith and without negligence". The existing Sections 60 and 80 of the 1882 Act and Section 1 of the 1957 Act should be repealed.

Recommendation 7(6): The new Act should contain a provision restricting, for Scotland, the banks' protection to that given for the rest of the UK in Section 4 of the 1957 Act.

Recommendation 7(8): The new Act should amend the law, so far as cheques are concerned, to permit banks to obtain payment by presentment of electronic information rather than the instrument itself (as currently required by Section 45 of the 1882 Act). It should also accord to a photocopy, or some other reproduction in legible form, of a cheque, suitably marked as paid and authenticated by the collecting bank, the status of "evidence of the receipt by the payee of the sum payable by the cheque" (cf Section 3 of the 1957 Act).

Recommendation 7(9): In determining the amount payable on an instrument covered by the new Act, precedence should continue to be given to the amount in words over that in figures.

Recommendation 7(10): The "funds attached principle" in Scots law should be abolished except in relation to negotiable instruments other than cheques. The new Act should therefore provide that presentment would not operate as an assignation of the sum for which it is drawn, in relation to any instrument covered by the new Act, to any order to pay addressed to a bank otherwise than in writing, or to any such order to pay presented to the drawee otherwise than in writing.

Recommendation 7(11): The definitions of a cheque and of a bank payment order should be drawn to include warrants for payment of interest or dividend or for repayment of capital and to include bankers' drafts.

Recommendation 7(12): The new Act should specify that its provisions as to cheque or bank payment orders, as appropriate, extend to payable orders. "Payable Order" should be defined as "any document issued by a government department and drawn on the same or another government department, or issued by and drawn on one of the persons or bodies specified in [a Schedule] which, not being a cheque or bank payment order, is intended to enable a

person to obtain payment from the department or body on which it is drawn of the sum mentioned in the document".

Recommendation 7(13): For the avoidance of doubt, the new Act should make it clear that a transfer instruction by BGC (Bank Giro Credit) does not constitute a legal assignment of the funds involved.

Annex 6: Negotiable Instruments

Recommendation 8(1): There should be a new Negotiable Instruments Act covering not only bills of exchange and promissory notes, but also, insofar as their negotiability is concerned, all other negotiable instruments.

Recommendation 8(2): The language and style of the 1882 Act should be retained in the new Act since it is clear, concise and well understood.

Recommendation 8(3): An instrument should be negotiable if

(a) it is a bill of exchange or promissory note as defined in the new Act, or
(b) it falls into one of the categories set out in (ii)-(v). of [paragraph 8.09 of the Review Committee's report].

Recommendation 8(4): The need for consideration as a test of negotiability should be abolished.

Recommendation 8(5): The sum payable on a negotiable instrument should no longer have to be certain at the date of issue provided it is "certain or ordinarily determinable" in accordance with rules to be set out in the Act.

Recommendation 8(6): The drawer or maker of an instrument should be permitted to choose which law is to govern the instrument he draws or makes and any subsequent variation should

be ignored. If no choice is made, the instrument should be governed by the law of the place of payment, as defined.

Recommendation 8(7): A protective rule in favour of other parties should be provided in relation to (a) forged drawers' or acceptors' signatures and (b) forged or unauthorised indorsements. That rule could be varied by contractual agreement.

Recommendation 8(8): The mandatory requirement for noting and protest of a dishonoured foreign bill should be abolished but the procedure should be retained, slightly modified for use on a voluntary basis.

Recommendation 8(9): The new Act should contain provisions giving to transactions taking place in a screen based or book entry depositary (or dematerialised) system operated by an Approved Depositary, and satisfying certain basic statutory requirements, the same status as equivalent transactions in negotiable instruments generally.

Recommendation 8(10): We also endorse a further 40 suggestions of a technical nature recommended by Professor Shea in his Report. These are set out at Appendix N.

Annex 7: Other Aspects of Banking Law

Recommendation 13(6): The provision of the Bankers' Books Evidence Act 1879 relating to the admissibility in evidence of copies of entries in bankers' books should be repealed.

Recommendation 13(7): Section 7 of the 1879 Act should be amended so as to permit a court to make an order for inspection and copying of entries in a banker's book if it thinks fit, whether or not legal proceedings have formally commenced. An order should be granted in such circumstances only where the court is satisfied (i) that proceedings are in serious contemplation, and (ii) that there are other grounds to support a prosecution or an action over and above what might be discovered as a result of the order.

Recommendation 13(8): The definition of "bankers' books" in Section 9 of the 1879 Act should be extended to include items such as credit slips and paid cheques (but not internal reference notes), insofar as they are required to substantiate and identify a transaction recorded in those books.

Recommendation 13(9): The Bank of England should be included in the definition of "bank" and "banker" in Section 9 of the 1879 Act.

Recommendation 13(10): The 1879 Act should be amended so as to give a court discretion to order payment of a fee to the bank against which an order under Section 7 of the Act is made, in order to reimburse the bank for the costs of compliance.

Recommendation 6(5): Section 6 of the Statute of Frauds Amendment Act 1828 should be repealed.

Recommendation 12(2): Rules to define completion of payment should be enacted in primary legislation. They should provide (a) that payment is to be regarded as complete at the point where the payee's bank (or its agent in the clearing), having actual or ostensible authority to accept payment on behalf of the payee, accepts a transfer of funds from the paying bank (or its agent in the clearing) for the payee's account- provided that the transfer is or has become unconditional; and (b) that, where the transfer is between two accounts at the same bank, payment should be regarded as complete when the bank has taken the decision to treat the instructions for transfer as irrevocable. The rules should be subject to modification by contractual arrangement, among parties to a contract governing a payment system.

Recommendation 12(3): The Bank of England should convene a working group of interested parties to consider and report on the operational implications of the completion of payment rules which we have recommended (Recommendation 12(2)), before they are enacted.

Recommendation 6(1): There should be a statutory provision whereby, in an action against a bank in debt or for damages, arising from an unauthorised payment, contributory negligence may be raised as a defence, but only if the court is satisfied that the degree of negligence shown by the plaintiff is sufficiently serious for it to be inequitable that the bank should be liable for the whole amount of the debt or damages.

Annex 8: Wider Banking Issues

Recommendation 14(1): The current review of the Consumer Credit Act 1974 should cover the desirability of an exemption from the connected lender liability provisions of that Act for purchases financed by the use of credit cards.

Recommendation 14(2): The concept of constructive trust should be examined in depth and in its proper context, perhaps by the Law Commission.

Recommendation 14(3): The Government should institute a process of consultation with a view to introducing legislation to clarify the right of set-off, and the validity of a charge over a credit balance in favour of the person with whom the balance is held.

Recommendation 14(4): The Government should consider options for eliminating, at least for banking purposes, the two mismatches between Bank Holiday dates in Scotland on the one hand, and England, Wales and Northern Ireland on the other. Of four options discussed in Chapter Fourteen, that favoured from the standpoint of the operational efficiency of the banking system is to harmonise dates when banks north and south of the border are open for business.

Recommendation 14(5): The Government should consider instituting a review, similar to that recently concluded by the Scottish Law Commission, of the English law dealing with a minor's capacity to contract. They should also introduce the legislation needed to implement the recommendations of the Scottish Law Commission.

Recommendation 14(6): Consideration should be given to a review of the evidential requirements of the criminal law, insofar as they relate to the corroboration of computer-produced evidence in cases of fraud.

Recommendation 14(7): Urgent action should be taken to make it a criminal offence (i) to obtain unauthorised access to a computer by "hacking", as recommended by the Scottish Law Commission, and (ii) to introduce a "virus" into a computer program.

Recommendation 11(1): The Government should consider how consistency of law and practice, across the field of payment cards generally, can best be achieved in the case of payment cards issued by retailers and other non-bank institutions, which fall outside the strict scope of banking services. Charge cards and store cards are the main types at issue. Where new standards of practice are introduced for such cards, they should be monitored and, by the use of appropriate sanctions, enforced.

Recommendation 14(8): The Government should keep under periodic review the scope for customer choice as between different payment systems, and the related question of the acceptability of legal tender, to ensure that there is no unfair discrimination through contractual arrangement, charging, or financial incentives.

Recommendation 17(1): The Government should keep before them the possible need for further studies to deal with new priorities as and when they emerge, in the field of banking services law and practice.

Other recommendations

The Review Committee also made the following two recommendations to banks and building societies:

Recommendation 10(5): Banks should introduce encryption in customer-activated EFT systems, where this can be operationally justified.

Recommendation 10(6): Banks should make customer-activated EFT systems on-line, where this can be operationally justified.

The Government have also considered the following three recommendations concerning standards of banking practice.

Recommendation 16(2): The Government should assess whether banks' Code of Banking Practice (see Recommendation 16(1)) constitutes an adequate response to the Recommendations of this Report. If so, it should ensure that the statement is formally presented to the Banking and Building Societies Ombudsmen as the impartial guidance on best banking practice of which they should take account in their adjudications.

Recommendation 16(3): Against the possibility that the banks' statement which is the subject of Recommendation 16(1) proves to be inadequate, or is not forthcoming within a reasonable timescale, the Government should consider at what stage to enact enabling legislation (see Appendix S) to support a statutory Code of Banking Practice, and an associated duty on banks to "trade fairly" with their customers.

Recommendation 16(4): The Government should appoint the Bank of England and the Building Societies Commission to monitor the continued observance and updating by banks of their published Code of Banking Practice. In support of these arrangements, the Banking and Building Societies Ombudsmen should be required, in their terms of reference, to comment in their Annual Reports on the extent to which banks are complying with, and, where necessary, keeping up-to-date their own published standards of best practice. (For example, new standards are likely to be needed before home and office banking, or smart/laser cards, come into general use.) If at any time monitoring reveals that these standards are not being complied with or updated as necessary, the Government should consider whether to implement the statutory fallback as in Recommendation 16(3).

Annex B: Consultees who submitted evidence following publication of Review Committees report

Access: The Joint Credit Card Company Limited
Association for Payment Clearing Services
Australian Federal Bureau of Consumer Affairs

The Banking Ombudsman
Mr Geoffrey S Beccle
British Bankers' Association
The British Computer Society
British Merchant Banking and Securities Houses Association
The Building Societies Association
The Building Societies Ombudsman

Clifford Chance
Close Brothers Limited
The Committee of London and Scottish Bankers
The Committee of Scottish Clearing Bankers
Consumer Credit Trade Association
Consumers' Association
Consumers in the European Community Group (UK)
The Council of the Banking Ombudsman
Coopers & Lybrand
Credit Card Sentinel (UK) Ltd
Mr Geoff Crocker

The Data Protection Registrar
The Director General of Fair Trading

Finance Houses Association
The Forum of Private Business

The General Council of the Bar
Girobank plc

Mr C M Johnston

The Law Society
The Law Society of Scotland
Local Authorities Co-ordinating Body on Trading Standards
London Chamber of Commerce

Mr Jeremy Mitchell

National Association of Citizens Advice Bureaux
National Consumer Council
National Council for Civil Liberties
National Westminster Bank plc
Nationwide Anglia Building Society
Northern Ireland Bankers' Association
Norwich and Norfolk Chamber of Commerce and Industry

O.E. Organetic Services Limited
The Office of the Banking Ombudsman

Pensioners' Voice (National Federation of Retirement Pensions Associations)

The Retail Consortium
Retail Credit Group

Scottish Consumer Council
Mr J Shell

Trades Union Congress

Annex C: Review Committee's illustrative code of banking practice

In Appendix L of their report the Review Committee prepared an illustrative non-statutory "Code of banking practice", which is reproduced below. The bold lettering indicates the operational requirements on banking and building societies.

Code of Banking Practice

A UNDERLYING ASPECTS OF THE BANKER-CUSTOMER RELATIONSHIP

A1 *Identity of a person opening an account.*

Banks should initiate procedures which allow them to establish, to their reasonable satisfaction, the identity of a person seeking to open a new account, so that if subsequently challenged they can refer to the action they took at the time. It is intended that this requirement will be an important element in determining the standards of care by which banks are to be assessed, if they are to benefit from the protection of [Section 4 of the Cheque Act 1957 as the legislation currently stands].

A2 *Terms and conditions - communication to the customer*

In any communication by the bank to the customer of the terms of the contract, the bank should ensure that the customer is given a fair and balanced view of those terms, and of the rights and obligations that apply on each side (not, for example, over-stressing the rights of the banker and the obligations of the customer). A customer should be

given reasonable notice of any proposals for variation of those terms.

A3 *Complaints procedures*

Banks should establish internal procedures for handling customer complaints. They should ensure in some appropriate way that customers are told how to lodge a complaint, and how it would be dealt with. They should also ensure that, as and when a complaint arises, the customer is made personally aware of the existence of these individual procedures and of the relevant procedures of the Banking or Building Societies Ombudsman, as appropriate.

A4 *Banker's duty of confidentiality*

The [Banking Services Act] imposes on a bank a duty not to disclose to any third party confidential information about its customers' private affairs. It also recognises four kinds of exception to that general duty. These exceptions call for the following comment:

(a) *Where disclosure is under compulsion by law.* Under the new Act there is no generalised provision obliging, or permitting, banks to disclose in the public interest anything about their customers' private affairs. **Where disclosure is required under the provisions of specific statutes which have been consolidated in the new Act, a court order is still, in some though not all cases, required before confidential information may be disclosed.**

(b) *Where the interests of the bank require disclosure.* The Act specifically limits such disclosure to certain narrowly circumscribed situations: (i) disclosure to a Court in the event of legal action to which the bank is a party, (ii) disclosure as between banking companies within the same group, for the specific purpose of protecting the bank and its banking subsidiaries against loss, in relation to the provision of normal

banking services, and (iii) disclosure for the purposes of, in connection with, and insofar as may be necessary for, the proposed sale of the ownership of the bank itself, or a substantial part of its undertaking. Thus, it does not provide a generalised permission for disclosures in the interests of the bank. The terms of the Act exclude, for example, disclosure of confidential information for any purpose, without express customer consent, to non-banking companies within the bank's group, or disclosure to banking subsidiaries for marketing purposes.

(c) *Where disclosure is made by the express consent of the customer.* The Act provides that, for a consent to qualify as express consent, it must be in writing, and must state the purpose for which it has been given. The only exception is the case of bankers' opinions (see A5 below), where consent in tacit form may be obtained provided a bank can show, first, that the customer has been made clearly aware of the purpose for which consent is required; secondly, that he has been advised that he is free to give or withhold his consent, which will be assumed unless he has, within a reasonable time, notified his bank that he does not wish to give it; and thirdly, that he has not given any such notification.

In addition to those statutory requirements, it should be a requirement of best practice that:

- **express consent, in whatever form, should not be sought in such a way as puts the customer under pressure to give it;**

- **in the case of express consent to be obtained in tacit form for the giving of bankers' opinions, a letter should be sent personally by the bank to its customer, seeking his consent for this specific purpose.**

(d) *Where there has been a breakdown of the banker-customer relationship arising through customer default.* The Act defines what is meant by a breakdown in the relationship: the case where no security has been given, and no satisfactory response has been received from the customer within 28 days of formal demand for repayment. The Act expressly limits disclosure of confidential information, in these circumstances, to approved credit reference agencies. It follows that the customer's express consent is still required for any disclosure of confidential information, even in the event of a breakdown of the relationship, to persons other than approved credit reference agencies or those covered by exceptions (a)-(b) above; and, in circumstances where there has been no breakdown in the relationship, to any persons (including credit reference agencies) other than those covered by exceptions (a)-(b) above.

Banks should explain to their customers the above rules, and exceptions, concerning the duty of confidentiality. They should remind all customers that they have a right of access, under the Data Protection Act 1984, to computer records about themselves held by banks.

A5 *Bankers' opinions*

Banks should give all customers, when they open an account or at the time this Code is first issued, a clear explanation of how the system of bankers' opinion works; and should invite customers to give or withhold a general consent for the bank to supply opinions on them in response to status enquiries, in accordance with the exception (c) to the duty of confidentiality as explained under Section A4 above. In the absence of such authority, the bank would, of course, be quite entitled to respond to the effect that the customer had not authorised it to reply to such enquiries. Failing a general authority, a customer could still give occasional specific authorities for its bank to respond to

particular enquiries, provided he could specify satisfactorily how such enquiries were likely to be framed and the source from which they might be received. But there would be no obligation on a bank to seek directions from a customer if it received an enquiry and had no general authority to respond.

A6 *Direct marketing of services*

Banks should exercise restraint in the direct marketing of their services, and should in particular:

- ensure that customers are aware of the marketing purpose for which they are being approached;

- respect any customer's objections to the use of personal information for marketing purposes, and desist from such activity on request.

B RULES APPLYING GENERALLY TO THE CUSTOMER'S ACCOUNT

B1 *Availability of funds*

Banks should give all their customers a simple explanation of the timing of the clearing cycle, and the concept of cleared balances. This would deal, especially, with the normal time taken to clear cheques and bank payment orders, should specify the "hold" period the bank is applying, and should say whether the bank has a right of reversal if the cheque or bank payment order is later returned unpaid. But it would cover other payment systems as appropriate, including the timing of direct debit procedures, and the customer's right of reversal under the system. Banks should consider how their customers could usefully be given more information, in periodic statements of account and in ATM slips, about cleared as well as uncleared balances on their account.

B2 *Truncation of cheques and bank payment orders*

Banks should give their customers an explanation, where needed, of what is involved in the truncation of cheques and bank payment orders, and of resulting changes, if any, in the timing of the clearing cycle. This should include an assurance that truncation will not detract from the bank's responsibilities, or add to the customer's obligations, in respect of the collection and payment of cheques and bank payment orders. If the necessary evidence to resolve a dispute regarding a truncated cheque or bank payment order is not produced within three working days, the customer's account should be re-credited pending final resolution.

B3 *Out of date cheques and bank payment orders*

A bank should not return, within six months from the date of issue, a cheque or bank payment order on grounds that it is out of date.

B4 *Bank Giro Credits*

Banks should explain the rights of bank and customer in regard to transactions effected by Bank Giro Credit.

B5 *Multifunction cards*

Banks should ensure that their terms and conditions for the use of multi-function cards include the following:

- a customer should be free to choose which of the card's functions he wishes to authorise for his own use; a bank should not be at liberty to refuse a card for a single function if its customer does not require more;

- functions that the customer does not require should be blocked off, so that the card cannot be used for these purposes in a machines;

- if for whatever reason the card is nonetheless compromised, the customer should (fraud on his part excepted) have no liability on any function that he has not authorised.

B6 *Card notification organisations*

Banks as card-issuers should inform all their customers who are cardholders:

- whether or not they themselves will accept notification of loss of theft of a payment card from a third party, presumably a card notification organisation;

- if so, the terms in which they would require cardholders to notify them, by a standard form of notice acceptable to card-issuers and signed by cardholders, of the appointment of an agent for this purpose;

- the effect, if any, on the cardholder's liability if an agent is appointed, especially the matter of whether notification to the agent discharges the cardholder's obligation to the card-issuer.

B7 *Countermand*

A bank should advise its customer of the different rules for each payment system in regard to countermand of instruction or authority. In formulating these rules, a bank should be guided by the principles that a period of time for countermand by the customer should be allowed where possible. It should only be eliminated where that is necessary for the efficient working of the system.

B8 *Bank charges*

A bank should explain to its customer the basis of charging for the normal operation of the account. Where an overdraft arrangement has been agreed in advance, a bank should ensure that its customer is aware, both in advance and as and when a change occurs, of the rate over base rate that will be charged, and of the timing of the debiting of interest. The customer should also be given full details of the method of calculation of fees and charges when these are applied to his account, including charges applied where an overdraft occurs without prior agreement. The customer should also be told of any services other than lending for which he will be charged (stopping cheques, correspondence, etc).

B9 *Foreign exchange transactions*

Where a bank undertakes a foreign exchange transaction for its customer, it should ensure that he is made aware before the transaction is completed of the basis of the exchange rate to be applied, and of any associated charges.

B10 *Guarantees*

Banks should ensure that prospective guarantors, whether customers or not, are adequately warned about the legal effects and possible consequences of guarantees, and about the importance of receiving independent advice.

C RULES SPECIFIC TO ELECTRONIC FUNDS TRANSFER (EFT)

C1 *Authentication of customers' instructions*

(a) *Standards of system security*

The bank's principal and general duty to observe its customer's mandate has special implications for the security of EFT payment systems operated by banks. Banks should therefore adopt the principle that an EFT system must meet

certain minimum standards of security in its authorisation procedures, so as to provide an acceptable degree of protection for the customer against the consequences of unauthorised transactions. In furtherance of that principle, they should accept a continuing commitment to upgrade their systems by the introduction, so far as practicable, of new technology based on the recognition of a signature or other personal characteristic.

(b) Existing systems

In assessing the security of their existing systems for purposes of authenticating a customer's instructions, banks should have regard to or, where appropriate, ask their customers to have regard to, such matters as the following:

- Care of payment cards and Personal Identification Numbers (PIN's). Every reasonable care should be taken by banks when issuing cards and PIN's to their customers; but banks should make clear to their customers that this obligation is only assumed on the assumption that customers for their part will take every reasonable care at all times in handling their cards and PIN's. The Act provides that there should be no unsolicited mailing of payment cards by banks to customers. Banks should observe a similar rule in respect of the mailing of PIN's. A customer should be required to acknowledge receipt of both card and PIN before he can avail himself of the service for which they are needed.

- Privacy. Banks should ensure the maximum privacy that is reasonably possible in customers' access to EFT systems. In particular, banks should aim to ensure that it is physically impossible for a customers' PIN to be read by anybody else when he is keying it in.

- Monitoring suspicious patterns of withdrawals. Banks should introduce systematic arrangements, where they

have not done so already, to monitor patterns of ATM withdrawals, such as might give rise to suspicion of fraudulent misuse of the system.

C2 *Written records*

Customers are entitled, under the Data Protection Act 1984, to demand a written record of an EFT transaction if they wish to have it. Banks should interpret this provision in the sense that customers are given the option of a written record at the time of the transaction, rather than in due course.

C3 *Customer's right of action*

A bank, as card-issuer, should deal with its own customer, as cardholder, in case of any complaint or claim arising on the customer's part from a dispute over a banking service provided through an EFT payment system. It is for the card-issuer to take action against any other party involved. This applies, for example, to EFT-POS systems or to shared ATM networks.

C4 *Apportionment of loss arising from a disputed EFT*

Banks should explain to all customers who use customer-activated EFT services that the Act requires losses, arising from disputed transactions carried out through such systems, to be apportioned on an equitable basis, by reference to the extent to which the acts or omissions of the various parties have contributed to the loss. Apportionment of the loss should take into account such factors as (i) the steps taken by the customer to protect the security of his card and PIN, (ii) the extent to which the system provided by the bank protects the customer against unauthorised transactions on his account, and (iii) the relative weight of the evidence adduced by the parties in support of their respective contentions that the transaction was, or was not, authorised.