

CREDIT CARDS AND INTERNET PAYMENT: TIME FOR ANOTHER LOOK AT S.75 OF THE CCA 1974

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Patricia Robertson of Fountain Court Chambers explains why the internet will give fresh impetus to creditors who want rid of section 75 of the CCA 1974.

Mr Smith sits at his home computer in Slough and uses a VISA credit card issued by his English bank to buy what is described as an antique wool rug ("handwoven by tribesmen in the remote Tsung province") from a vendor in Outer Mongolia, whose website displays the requisite VISA symbol. The rug is delivered: it smells so strongly of camel that Mr Smith has to exile it to the garden, it is plainly nylon and carries a label stating that it was made in Taiwan. Mr Smith promptly claims against his bank in his local County Court, relying on s.75 of the Consumer Credit Act 1974 ("CCA") to raise against the bank any claims which he has for misrepresentation or breach of contract by the vendor.

Does the Consumer Credit Act 1974 apply?

In this example the credit card agreement itself is a regulated agreement within the scope of the CCA 1974. However, cross-border provision of credit card services may become a reality as the market develops post EMU. We may see scenarios where UK card issuers have issued cards to holders domiciled in other states: Mr Smith in Slough may have a credit card agreement with a German bank or Herr Schmidt in Cologne may have obtained his card from an English bank, depending on where interest rates and other terms are most favourable. At this point difficult issues arise as to the extent to which the CCA 1974 applies to the credit card agreement, if at all. Arguably it does so as part of the proper law of the agreement, if this is shown to be English law. If the jurisdiction of the English court is established, at least some parts of the CCA 1974 may apply as the law of the forum. Under the provisions of the Rome Convention, the protection conferred by the CCA 1974 on consumers may constitute an overriding mandatory rule. For the moment, let us pass from these future complications to the next question.

Does section 75 of the Consumer Credit Act 1974 apply?

S.75 CCA 1974 applies where the transaction giving rise to the claim against the supplier has been financed by "a debtor-creditor-supplier agreement" which is "made by the creditor under pre-existing arrangements, or in contemplation of future arrangements, between himself and the supplier" (s.75(1) and s.12(b)).

Are there "pre-existing arrangements" as between the card-issuing bank in England, the card-holder and the vendor in Outer Mongolia? Plainly not if pre-existing arrangements require the existence of direct contractual arrangements between the bank and the vendor. In the vast majority of internet transactions the merchant acquirer, with whom the vendor has an agreement, is a different entity from the card-issuing bank. Many internet transactions involve a vendor who will have an agreement with a merchant acquirer in the same jurisdiction, whereas the card-holder will be signed up with a card-issuer in another jurisdiction.

This situation also occurs in relation to purely domestic transactions where both the card-holder and vendor each happen to have agreements with different banks.

The trouble with "pre-existing arrangements"...

The CCA 1974 distinguishes, in s.11(1)(a) and (b), two party credit agreements where the supplier is the party giving credit (eg store cards) and three party agreements where the supplier and creditor are different entities. The CCA 1974 does not explicitly address the problem that many credit card transactions are in fact four (or more) party agreements: there is a daisy chain of contracts running from card-holder to vendor, through the card-issuer and merchant-acquirer and the entity or entities with whom they each have settlement arrangements. In such cases as well as no direct contract between vendor and card-issuer, there is likely to be no prior contact of any kind.

Some years ago, Barclaycard sought to argue that s.75 applied only in those domestic transactions where the merchant-acquirer and the card-issuer were one and the same, i.e. in three party transactions. It was contended that only then was there a "pre-existing arrangement" between the card-issuer and the vendor. The Office of Fair Trading objected to this interpretation. In 1991 the matter was resolved by Barclaycard issuing a statement that it would not take the point against card-holders.

Similar arguments were put forward on behalf of card-issuers in discussions with the OFT and the DTI in 1994 and 1995 over the application of s.75 to transactions carried out by card-holders when travelling abroad. In the case of an overseas vendor there is no direct contractual nexus between the UK card-issuer and the foreign vendor, furthermore the chain of intermediate relationships gets longer and more complex. In addition, the influence which the UK card-issuer can bring to bear on the vendor may be minimal. It was also pointed out that there is no express provision to apply a sterling equivalent to a price specified in a foreign currency when

determining whether the transaction falls within the necessary financial limits for s.75 to apply (in contrast to s.9(2) CCA 1974). Moreover, the quid pro quo for assuming liability under s.75 is the right to an indemnity from the supplier and the entitlement, subject to the rules of court, to have him made a party to any proceedings brought against the creditor (see s.75(2) and (5)). It was argued that in practice this right to an indemnity is difficult to enforce against a foreign vendor and the supposed right to bring third party proceedings may be nugatory.

The Banking Ombudsman had lent this stance some support in his report for 1989-90, in which he expressed the view that Parliament had not intended s.75 to apply to overseas transactions. The OFT, however, rejected these contentions and expressed the view that s.75 does plainly apply to overseas transactions. The DTI published a consultation document in December 1995 to test the seriousness of the burden placed on industry by such an interpretation. Following the consultation, the DTI announced that there was to be no change to s.75. In essence, the line taken by the OFT and the DTI was that credit-card companies had chosen to market their product specifically on the basis of its suitability for making payment when overseas, portraying the whole world as one big happy VISA-or-Access-accepting family: they could not then turn round and ask to be treated as wholly unconnected parties when it came to the application of s.75.

A question of construction

There is some basis for banks' opposition to the construction of CCA 1974. An agreement is entered into under pre-existing arrangements if it is entered into in accordance with, or in furtherance of, arrangements previously made between any of the following:

- (a) the creditor and the supplier;
- (b) one of them and an associate of the other's; or
- (c) an associate of one and an associate of the other's (s.187(1) and (4)).

The test of whether companies are associates is defined in terms of common control: is there a person or associated persons in control of both companies (s.189(1) and s.184(1))?

The use of the term "arrangements" rather than "agreement" strongly suggests that something short of contractual relations will suffice. However, on the face of it, these arrangements must at least be between the creditor and supplier themselves or their respective associates. In the sort of transaction we are looking at, none of the individual contractual links in the daisy chain between supplier and creditor could be said to constitute an arrangement between those parties or their associates, in the required sense of companies sharing common control.

Most commentators, Goode at their head, have taken the view that overseas transactions are covered by s.75. If, instead of looking at the individual links in the chain, one stands back and looks at the network of contractual relationships as a whole, it can be argued that this constitutes an arrangement between the supplier and the creditor made by virtue of their membership of the VISA network. An analogy might be found in the approach taken by English courts to clubs where membership has been found to give rise to a contract between two individual members, the terms of which are based upon the rules of the club (*The Satanita* [1895] P 248). Here, however, the court need not even go so far as to find a contract between the members, since a mere arrangement is enough.

The position has never been tested in the higher courts - perhaps deliberately so. Card-issuers fear an adverse reaction from judges keen to defend consumers' rights. The decision of the Court of Appeal in *Jarrett v Barclays Bank* [1997] 3 WLR 654 demonstrates that this fear is justified. The Court of Appeal gave short shrift to a jurisdictional argument which would have had the effect of booting all s.75 claims out of this jurisdiction where the underlying contract breached was for the transfer of an interest in immovable property. That argument had been accepted by a number of County Court judges. By a robust, some would say wrong-headed, interpretation of the relevant European case law, the Court of Appeal found there to be jurisdiction to bring such claims here, thereby saving the card-holder from the prospect of having to litigate claims in the jurisdiction where the property in question was located. The argument that no s.75 claim was available in any event does not appear to have been advanced in any of the cases under appeal and one suspects it would have got equally short shrift. History does not relate what became of these cases once remitted to the County Courts for hearing.

So what is new: does the internet make a difference?

The internet makes the problem presented by s.75 more compelling because it will multiply the occasions when a given card-holder generates transactions involving overseas vendors: not just when on his summer holiday, but when buying books from Amazon on a weekday evening.

Furthermore, it is reasonable to anticipate that the growth of internet commerce will encourage recruitment of vendors into the VISA and Access networks in jurisdictions where, up to now, there has been little penetration by credit cards. The vendor will not have to wait until enough foreign tourists are coming to his town to make it worth his while signing up as a merchant. If he has access to a server and suitable software (which are getting cheaper all the time), he can set up a website accessible by customers all over the world, who will expect to be able to pay by credit card. Merchant acquirers keen to recruit merchants in these jurisdictions may be inclined

to apply lower criteria for admission to the network in order to reach a critical mass more quickly. There is therefore a real risk that card-issuers in the UK will end up paying the price for this expansion, in terms of footing the bill for sub-standard suppliers recruited by merchant acquirers over whom the card-issuers have no direct control.

Unfortunately for card-issuers, the arguments against s.75 liability look no more attractive when advanced in relation to the internet than they do in relation to transactions undertaken when the card-holder is abroad.

If anything, it becomes more anomalous to contend that a card-holder who is sitting at his computer should be able to rely on s.75 when he buys from a vendor who happens to be physically located in the same jurisdiction but not when he buys from a vendor located abroad. The real location of the vendor may be a matter of supreme indifference to the card-holder as he searches the web for someone who can supply, for example, a particular software upgrade. He can download it as easily from a vendor in Japan as from a vendor in this country and paying with his credit card immediately solves any currency conversion problem.

There can be little doubt that an English court will be inclined to apply s.75 unless the case for a contrary construction is compelling. As we have seen, it is not.

The likelihood, therefore, is that our Mr Smith will be able to bring a claim for damages against his card-issuer under s.75 in respect of misrepresentation and breach of contract by the Outer Mongolian carpet vendor. Outer Mongolian law probably applies to that contract and may or may not have the effect that Mr Smith has a good claim. However, the English court will assume that Outer Mongolian law is the same as English law unless one of the parties pleads an express case to the contrary. The card-issuer will have to go to the trouble of finding experts on Outer Mongolian law to say that a strict rule of caveat emptor invariably applies and that an odour of camel is regarded as indispensable in any tribal rug worth the name or, alternatively, just accept a ruling based on English law.

Could it get any worse?

Well, yes. Supposing our Outer Mongolian vendor, once armed with Mr Smith's credit card details as a result of the rug purchase, then uses those details to pay over the internet for further stocks of rugs from Taiwan. These will appear to be legitimate credit-card transactions, until Mr Smith challenges the entry on his statement a month or so later. Fear of this sort of fraud is driving the search for credit card payment protocols which not only use encryption to protect the

card details from unauthorised third parties, but even avoid the details themselves being released to the vendor.

Article 8 of the Distance Contracts Directive (Directive 97/7/EC of 20 May 1997, published in the Official Journal No L 144/19) requires Member States to ensure that measures exist to allow consumers to be recredited with the sum debited to a card in the event of fraudulent use of a payment card in connection with a distance contract, which will include contracts entered into over the internet.

This would appear to go further than the present ceiling on liability of £50, with an exemption from liability once notice of theft or loss is given (provided for in relation to credit cards by the CCA 1974 and in relation to debit cards by the Banking Code and other codes of practice). The Directive would seem to require all sums to be recredited whether or not notice had been given to the card-issuer of the fraud at the time the sum was debited.

The possibility that the Directive may lead to the whole of the liability for fraudulent transactions falling on the card-issuers is an additional incentive in the search for the ultimate secure payment protocol. However, the problem is that it is the merchant acquirer, rather than the card-issuer, who is in a position to influence selection of vendors and merchant terms and conditions, including those relating to cryptography and access to keys. The card-issuer's agenda will only influence the solutions that are adopted if, and to the extent that, card-issuers can pass their liability back down the line to the merchant acquirer.

What can be done?

A challenge in the courts to the application of s.75 would be a high risk strategy. In practical terms, a large part of the answer must lie in ensuring that liability can be passed down the line to the merchant acquirer, through however many intermediate links. This would give merchant acquirers some incentive to police their vendors and remove persistent offenders from their networks.

The difficulty is that the UK is out of line with other jurisdictions in providing such a high level of protection for consumers who use credit cards to pay for transactions. Elsewhere in Europe, the liability of the issuer in the case of breach by the supplier has generally been limited to re-crediting the sum charged to the card, in line with the Consumer Credit Directive, rather than extending to consequential damages. Elsewhere in the world, the protection accorded to

consumers is even more limited. English card-issuers are therefore seeking to pass on liability in circumstances where there may not be reciprocity.

Presumably credit card issuers, merchant acquirers and their intermediaries have already had to reach, in the terms of their agreements inter se, compromises as to how this liability is to be allocated. (These agreements are not in the public domain.) If there was to be a massive surge in the number of s.75 claims as a result of growth in internet commerce, those compromises may be put under some strain.

Consultations carried out by the DTI in 1995-6 did not deal with the effect of internet commerce on s.75 liability and vice versa, no doubt because at the time this accounted for a small proportion of transactions. If card issuers wish to have another go at persuading the Government of the need for a change to s.75 to bring it into line with the Consumer Credit Directive, it would be worth making internet commerce the focus and carrying out a cost assessment based on projected levels of internet transactions, as well as overseas transactions. The results may make the case for change more compelling than the DTI judged it to be when it last looked at the issue in 1996.