RETHINKING BANKING LIABILITY IN PAYMENT CARD RELATIONSHIP: THE CASE OF "STOP PAYMENT ORDER" AS AN EXAMPLE

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I. INTRODUCTION

The issue of banking liability regarding faults and defects, which occur during the issuance and use of a payment card,[1] has risen repeatedly in recent decades in different countries.[2] This trend is caused by the increasingly

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1. Interpretation of the term "payment card" varies widely in legal doctrine. ELLINGER'S MODERN BANKING LAW defines "payment cards" as "pieces of plastic fitting in wallet or purse that may be used to obtain goods or services." E.P. ELLINGER ET AL., ELLINGER'S MODERN BANKING LAW 581 (4th ed. 2006). Alternately, CONSUMER CREDIT LAW AND PRACTICE defines the term as "a general expression covering any plastic card which may be used on its own (that is, without a cheque or other instrument) to obtain cash, good or service." R.M. GOODE, CONSUMER CREDIT LAW AND PRACTICE § 2.61LA (2010). My doctoral thesis suggests the following analytical definition: "An unconditional order, addressed by a customer to a bank or an issuer, given by using a card issued to the customer's use, ordering the bank or the issuer to: (1) pay a merchant, at a fixed or determinable future time, a certain sum in money, all or a portion of it, according to a slip or an electronic means of communication, all in regard to a transaction between the merchant and the customer; or (2) to transfer money to the possession of the customer by an electronic mechanism for withdrawal of cash." Liran Haim, The Juridical Nature of the Payment Card Relationship 87-90 (2010) (unpublished Ph.D. thesis, Haifa University) (on file with author).

2. These key issues in bank liability have included the juridical nature of the payment card, card issuer liability for misuse of the card, card issuer liability for breaches committed by the supplier, loss allocation, error correction, and failure of payment. For a discussion regarding these topics in U.S. law, see, e.g., EDWARD L. RUBIN & ROBERT COOTER, THE PAYMENT SYSTEM: CASES, MATERIALS AND ISSUES 606-727 (1989); BARKLEY CLARK, THE LAW OF BANK DEPOSITS, COLLECTIONS AND CREDIT CARDS § 5-5.14 (1999); L. Ali Khan, *A Theoretical Analysis of Payment Systems*, 60 S.C. L. REV. 425 (2008). For a discussion in U.K. law, see, e.g., JOAN WADSLEY & GRAHAM PENN, THE LAW RELATING TO DOMESTIC BANKING 463-94 (2d ed. 2000); ELLINGER ET AL., *supra* note 1, at 581-616; ROSS CRANSTON, PRINCIPLES OF BANKING LAW 266-71 (2d ed. 2009). For a discussion in other European law, see, e.g., Christian Mouly & Pascale Bloch, *European Banking Law in France*, *in* EUROPEAN BANKING LAW: THE BANKER-CUSTOMER RELATIONSHIP 35, 50-54 (Ross Cranston ed., 2d ed. 1999); Simonetta Cotterli, *European Banking Law in Italy*, *in* EUROPEAN BANKING LAW: THE BANKER-CUSTOMER RELATIONSHIP 83, 102-05 (Ross Cranston ed., 2d ed. 1999); Immaculada Barral Vinals, *The Cards as a Payment*

common use of the card around the world and by the banking system's vast and ongoing technological developments. Courts and legal scholars in Israel, where payment cards have been widely accepted only in the last two decades, now debate these issues.[3]

This Article is a based on a section of my doctoral thesis, which analyzes the juridical nature of the relationship formed during the issuance and use of a payment card, as well as the practical consequences of that relationship. The thesis was written in light of significant deficiencies in Israeli law, as the issue has not been thoroughly examined since the 1980s,[4] and also in light of innovative theories in banking law and means-of-payment law, both of which were recently accepted in Israel.[5]

In order to examine the juridical nature of the payment card relationship, the thesis was based upon an analytic and comparative research of the law. Within this framework, I examined the law and the prevailing doctrinal approaches relating to payment cards, mostly in the United States, United

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Method and as a Financial Service in Spain: The Responsibility System, 14 ILSA J. INT'L & COMP. L. 595 (2008).

3. For important Israeli Supreme Court decisions relating to the misuse of payment cards in paperless transactions, see generally CA 8501/04 Ishdar Hamrahet v. Israel Credit Card, Inc. [2005] (Isr.); CA 1620/04 Israel Credit Card, Inc. v. Exec. Travel Agency, Inc. [2009] (Isr.). For a critical overview of these decisions, see Haim, *supra* note 1, at 326-37. Also, in recent years, Israel's lower courts have adopted an approach that protects card issuers by imposing in many cases strict obligations on the customer for safekeeping the card and releasing the issuer from liability. Debit Cards Law, 5746–1986, 40 LSI 193-99 (1986) (Isr.). For a discussion of such cases, see Haim, *supra* note 1, at 302-25; Amir Bahar, *Misuse of Payment Card: The Erosion of Consumer Defense*, 11 HAMISHPAT 321 (2008).

4. Haim, *supra* note 1, at 1-29.

5. The Israeli Debit Cards Law was enacted in 1986 following the conclusions of a special committee appointed by the Israeli Justice Department and headed by Professor Aharon Barak. Debit Cards Law, 5746–1986, 40 LSI 193-99 (1986) (Isr.); *see* ISRAEL JUSTICE DEPARTMENT, THE COMMITTEE FOR EXAMINATION OF CREDIT CARD LEGAL ISSUES (1982) (on file with author). The committee's mandate was to examine the legal issues concerning credit cards and their implications. *Id.* Since the law's enactment, it has been amended four times (in 1994, 1996, 1998, and 2008). Israel's banking law and means-of-payment law have developed rapidly in the last two decades. In two leading cases, the Supreme Court and Standard Contracts Tribunal have adopted the academic work of Professor Ricardo Ben-Oliel. In the first case, CA 5893/91 *Tefahot Mortgage Bank v. Tsabach*, 48(2) PD 573 [1994] (Isr.), the Supreme Court held that a bank owes its customers a general fiduciary duty. For further discussion on this duty, see Ricardo Ben-Oliel, *Safety Boxes: A New Approach for the Definition of the Service and the Terms of Liability of the Banker Towards His Customer*, 37 HAPRAKLIT 76 (1987) [hereinafter Ben-Oliel, *Safety Boxes*]; RICARDO BEN-OLIEL, BANKING LAW (GENERAL PART) 102-03 (1996) [hereinafter BEN-OLIEL, BANKING LAW]; Ruth Plato-Shinar, *An Angel Named "The Bank": The Bank's Fiduciary Duty as the Basic Theory in Israeli Banking Law*, 36 COMM. L. WORLD REV. 27, 31-40 (2007). In the second case, Plea 195/97 *Attorney General v. Bank Leumi*, 2003(1) PM 481 [2004] (Isr.), the Standard Contracts Tribunal held that twenty-eight clauses of a banking contract were void either in part or in full. The Israeli Supreme Court recently adopted important parts of this decision. *See* CA 6916/04 Bank Leumi v. Attorney Gen. [2010] (Isr.); *see also* Ricardo Ben-Oliel, *The Attorney General v. Bank Leumi: A Lengthy Appraisal by an Israeli Court of a Banking Account*, 21 BANKING & FIN. L. REV. 61 (2005) (discussing a recent case regarding bank account contracts).

Kingdom, European Union, and Israel.[6] This comparative research concluded, among other things, that the lack of comprehensive examination of the law regarding payment cards is common not only in Israel but in the aforementioned countries as well. I therefore decided to assemble a harmonious,[7] uniform legal thesis that may provide a meaningful and practical contribution to the evaluation of existing law, as well as a suggestion of alternative arrangements.

The research conclusion, as summarized in the first section of this Article, is that the payment card relationship should be classified as a sui generis arrangement, which includes three elements: (1) a means of payment, (2) a special commercial banking transaction, and (3) an agency relationship.[8] From a practical perspective, this classification influences the bank's and issuer's liability towards the customer and supplier regarding various issues.[9] An example, which is presented in the second section of this Article, concerns the issuer's liability when countermanding a payment order given by the customer. This issue is critically discussed in light of the law in the United States and elsewhere. I argue that the issuer must countermand payment only if the initial transaction (i.e., the transaction between the customer and the supplier) was flawed.[10] Accordingly, I assert that the issuer's duty is to review the transaction in detail and assess whether it was flawed.[11] Moreover, I argue that the issuer also has a disclosure duty to the customer and supplier in various matters regarding the countermand of payment.[12]

In light of the aforementioned research conclusions and methodology, I believe that the underlying thesis and its practical effects shall also prove to be extremely relevant to the legal systems of other countries, particularly to that of the United States.

II. THE JURIDICAL NATURE OF PAYMENT CARD RELATIONSHIP

Case law and legal doctrine introduce various approaches concerning the

6. Haim, *supra* note 1, at 1-29.

7. The prevailing approach in legal doctrine to the legal definition of payment cards is to define each type of card separately from the others rather than assuming a comprehensive harmonic model for all types of cards. *See infra* Part II. For a discussion of the importance of a harmonious legal model for payment cards, see CRANSTON, *supra* note 2, at 266-68; GOODE, *supra* note 1, § 3.63LA.

8. *See infra* Part II.

9. The main practical result is an increase of issuer liability upon the occurrence of stop payment order, *see infra* Part IV, misuse of the card, Haim, *supra* note 1, at 302-25, distant selling, Haim, *supra* note 1, at 326-37, or supply of credit, Haim, *supra* note 1, at 183-85. Issuer duty to provide effective explanations on the nature of each card service also increases. Haim, *supra* note 1, at 187-88.

10. *See infra* Part III.

11. *See infra* Part IV.

12. *See infra* Part IV.

juridical nature of payment card relationship.[13] There is general acceptance that the two kinds of payment cards, credit and debit, differ in juridical nature. Credit cards are commonly defined as a relationship of assignments[14] or that of direct obligation theory;[15] debit cards are commonly defined as a relationship intended to initiate an electronic funds transfer.[16] This Article will not include a lengthy discussion of the aforementioned approaches and their criticisms. I have discussed that issue critically elsewhere.[17] Therefore, I note only that, in my opinion, these approaches ignore the close connection between the issuance and use of the payment card and the banking system's role therein. They also disregard the payment card's unique nature as a means of payment, as well as the issuer's role in performing payment orders on behalf of the customer and the supplier. In disregarding these elements and their practical legal results, the issuer's increased liability also remains unanalyzed. Furthermore, the prevailing approaches methodologically support a different legal definition for each type of card. I argue, on the other hand, that we must find a comprehensive definition that supports the creation of similar legal arrangements for all such cards.[18]

Rejecting the aforementioned approaches, I contend that the relationship created as a result of the issuance and use of a payment card cannot be defined within the framework of an acknowledged legal model and must therefore be classified as a *sui generis* arrangement. This arrangement consists of three main elements: first, the payment card as a means of

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13. The prevailing approaches to classifying the juridical nature of the payment card relationship are assignment theory, direct obligation theory, and negotiable instruments theory. For a discussion of assignment theory, see John Higgs et al., *Bank Credit Cards: Problems Under Regulation Z and Possible Problems as a Result of Future Developments Under Proposed Consumer Legislation*, 27 BUS. LAW. 111, 111-12 (1971); Donald H. Maffly & Alex C. McDonald, *The Tripartite Credit Card: A Legal Infant*, 48 CALIF. L. REV. 459, 473-74 (1960); Roland E. Brandel & Carl A. Leonard, *Bank Charge Cards: New Cash or New Credit*, 69 MICH. L. REV. 1033, 1046-47 (1970-1971); Jerry G. South, *Credit Card: A Primer*, 23 BUS. LAW. 327, 331-33 (1968). For a discussion of direct obligation theory, see *In re* Charge Card Servs. Ltd., [1986] 2 B.C.C. 99373 (H.L.) 99379-81 (appeal taken from B.C.C.); *In re* Charge Card Servs. Ltd., [1988] 3 W.L.R. 497 (Eng.); A. Paul Dobson, *Credit Cards: Re Charge Card Services*, 1989 J. BUS. L. 339, 341-42 (1989); Maffly & McDonald, *supra*, at 472-73. For a discussion of negotiable instrument theory, see Franklin Nat'l Bank v. Kass, 184 N.Y.S.2d 783 (N.Y. Sup. Ct. 1959); *In re* Brendle's Stores, 165 B.R. 811, 814 (M.D.N.C. 1993); Edwin E. Smith, *A Summary of the Provisions of Revised U.C.C. Article 9*, *in* ASSET BASED FINANCING 2006 133, 143-45 (2006).

14. Higgs et al., *supra* note 13, at 111-12; Maffly & McDonald, *supra* note 13, at 473-74; Brandel & Leonard, *supra* note 13, at 1046-47; South, *supra* note 13, at 331-33.

15. *In re* Charge Card Servs. Ltd., [1986] 2 B.C.C. 99379; *In re* Charge Card Servs. Ltd. [1988] 3 W.L.R. 497; Dobson, *supra* note 13, at 341-42; Maffly & McDonald, *supra* note 13, at 472-73.

16. ELLINGER ET AL., *supra* note 1, at 593-94; Marcus Smith & Patricia Robertson, *Plastic Money*, *in* LAW OF BANK PAYMENTS 187, 197-214 (Michael Brindle & Raymond Cox eds., 3d ed. 2004); M.H. OGILVIE, BANK AND CUSTOMER LAW IN CANADA 350-56 (2007).

17. Haim, *supra* note 1, at 49-81.

18. For a similar approach, see CRANSTON, *supra* note 2, at 266-68; GOODE, *supra* note 1, § 3.63LA.

payment; second, the payment card relationship as a unique commercial banking transaction; third, when the relationship involves a tripartite card, as an agency relationship.[19] I briefly elaborate on the basis and importance of these elements.[20]

A. The Payment Card as a Means of Payment

The definition of the payment card as a "means of payment" derives primarily from two main functions of the card: (1) withdrawal of funds from automatic teller machines (ATMs), and (2) payment for the supply of goods or services by various suppliers.[21] The first function allows the customer to use the card to receive from the bank an amount of money from an account. The role of the issuer and the bank in this case is to create a mechanism to (1) debit the customer's account for the sum withdrawn and (2) hand over this sum to the customer. The second function allows the customer to pay for goods or services from a supplier without using cash. In this case, the issuer absolutely discharges the customer's debt to the supplier in accordance with the initial transaction. The payment by the card constitutes only a conditional discharge of the customer's debt to the supplier. This discharge becomes absolute only upon execution of the issuer's role— the absolute discharge of the initial transaction.[22]

In perceiving payments by card as conditional discharges, I bring the payment card legal arrangement closer to not only bills of exchanges and negotiable instruments, but also to other means of payment.[23] Thus, I have

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19. *See* Haim, *supra* note 1, at 87-90.

20. This Article suggests a global thesis for the different types of cards than for tripartite cards only.

21. Notably, in addition to these functions, the card is used for receiving other bank services. *See infra* Part II.B (providing details regarding the implications of these other bank services on the juridical nature payment cards).

22. *See* CA 47/75 Ben-Yehuda v. E.T.S. 29(2) PD 637 [1975] (Isr.) (indicating that a conditional discharge becomes absolute upon execution of the issuer's role); *see also In re* Charge Card Servs. Ltd., [1986] 2 B.C.C. 99373 (H.L.) (appeal taken from B.C.C.) (noting differences between conditional payment approach and prevailing absolute payment approaches); WADSLEY & PENN, *supra* note 2 (highlighting differences between conditional payment approach and absolute payment approach).

23. It is accepted that a payment by check constitutes a conditional payment. *See* RUBIN & COOTER, *supra* note 2, at 121-22 (discussing several conditions where a check as a payment instrument will not result in the payee receiving funds from the payor's bank or financial institution). The conditional payment becomes absolute only when the check is paid by the drawee bank. *See id.* at 297 (explaining the process by which the drawee bank effects payment and the change legal status of the check). It appears that a conditional payment approach can also be acknowledged regarding banking transfers (Bank Giro). *See id.* at 9 (describing the electronic payment mechanism, called the Giro system in Europe, where a person transmits instructions to their bank or financial institution which would then pay the merchant); *cf.* Ricardo Ben-Oliel, *Payments by Banking Transfers in Practice and in Legal Theory*, *in* DEVELOPMENTS IN AUSTRIAN AND ISRAELI PRIVATE LAW 81, 86-92 (Herbert Hausmaninger et al. eds., 1999) [hereinafter Ben-Oliel, *Payments by Banking Transfers*]

also contributed to the creation of legal harmony in the means of payment market, an outcome that reflects legal policy aimed to properly protect customers.[24] In taking that position, I move away from the perception classifying the credit card in accordance with the direct obligations theory, whereby payment by card is commonly perceived as an absolute discharge of the initial transaction.[25]

From a practical perspective, the definition of the card as a means of payment justifies similar interpretations and drawing of analogies between other laws governing means of payment and the payment card.[26] The main arrangement that may be used as a source of interpretation or analogy is the one governing checks. Obviously, such an interpretation or analogy can be reached only after drawing a comparison between the payment card and the check.[27] In comparing the elements of a check to those of a payment card, dissimilarities exist regarding the nature of the signature and negotiability.[28] As a rule, one must not apply the check law arrangements governing those elements to the payment card.

B. The Payment Card as a Unique Commercial Banking Transaction

Prof. Ricardo Ben-Oliel proposes three main elements that assist in the characterization of a commercial banking transaction: (1) the socioeconomic finality of the transaction, (2) the role of the banking system and the existence of a special banking mechanism for the transaction, and (3) the level of risk posed by the transaction to the depositor's rights.[29] According to these

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(examining the analogy between the check and the banking transfer).

24. For an approach considering the payment by credit card as a conditional payment, see DENIS V. COWEN & LEONARD GERING, THE LAW OF NEGOTIABLE INSTRUMENTS IN SOUTH AFRICA 270 (5th ed. 1985). For similar considerations, see RUBIN & COOTER, *supra* note 2, at 121-22, 297; Ben-Oliel, *Payments by Banking Transfers*, *supra* note 23, at 90; CRANSTON, *supra* note 2, at 266-68.

25. *See In re* Charge Card Servs. Ltd., [1988] 3 W.L.R. 497, 517 (Eng.) (stating a card holders obligation of payment is absolute and not conditional).

26. For a similar approach concerning banking transfer, see Ben-Oliel, *Payments by Banking Transfers*, *supra* note 23, at 89-90 (discussing the laws governing checks being applicable to bank transfers).

27. It should be noted that an analogy must consider all aspects of the check and the payment card (similar and different legal elements). For these kinds of considerations, see Haim, *supra* note 1, at 93-103.

28. The question concerning the juridical classification of credit cards has been an issue for discussion in the U.S. courts. *See, e.g.*, *In re* Brendle's Stores, 165 B.R. 811, 814 (M.D.N.C. 1993) (discussing the confusion with classifying credit card receivables because of attributes of insturments such as a writing alone not being sufficient to receive payment); Smith, *supra* note 13, at 143-45 (referencing Uniform Commerical Code Article 9 defintions of semi-intangibles which are treated as conventional tangible embodiments of intanbile rights of the debtor). For a broader discussion on the term "payment card" in comparison with the legal elements of a check, see Haim, *supra* note 1, at 87-90, 94-103.

29. Ricardo Ben-Oliel, *Elements for a Legal Definition of Commercial Banking: A Comparative View*, 16 ISR. L. REV. 499, 510-11 (1981) [hereinafter Ben-Oliel, *Elements for a Legal Definition of Commercial Banking*]. It should be noted that Ben-Oliel's initial

characteristics, the payment card is a banking transaction that includes unique elements. From a socioeconomic perspective, the card allows the parties to receive funds they deposited in the bank. In addition, the banking system is the initiator of the payment card scheme and the operator of its mechanism. However, the card provides additional, peripheral services from the bank that are not considered "classic banking services." These additional services demonstrate the special nature of the payment card.[30]

With regard to the socioeconomic nature of the transaction, from the customer's perspective, the card constitutes a central device to receive money from the bank funds he deposited in his account. This is accomplished by withdrawing funds through ATMs or by giving instructions to the bank to pay from the account to third parties, such as suppliers. In addition, the customer may also receive, within the framework of the relationship, additional banking services, the most common of which is the granting of credit.[31]

As for the socioeconomic nature of the transaction from the supplier's perspective, the card chiefly serves to enable the completion of transactions with customers holding a card as a substitute for cash, i.e., in order to receive payment for supplying goods or services in the supplier's place of business.[32] The supplier assumes that, by participating in the issuer's scheme, he increases the certainty of the absolute discharge of transactions.[33] To conclude this point, the socioeconomic nature of the card is to allow the management of the customer's bank account and the collection of payments for the supplier.[34]

As for the socioeconomic nature of the transaction from the bank's or issuer's point of view, it appears that through issuing payment cards they significantly increase their profit.[35] This is made possible as a result of the special mandate the two receive from the general public, which leads both the customer and the supplier to require the unique services provided by the card— the customer for the purpose of managing a bank account and the supplier for the purpose of managing a business.

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suggestion is that a banking business is a "credit transaction." *Id.* at 510.

30. For a broader discussion of that issue, see Haim, *supra* note 1, at 109-13.

31. Besides the receiving of credit, the payment card is used to receive a variety of services, including, for example, selling discounts, gifts, insurance services, customers club membership, etc. *See* Brandel & Leonard, *supra* note 13, at 1035, 1039-40. On the issuer's liability in supplying these services, see Haim, *supra* note 1, at 260-63.

32. *See* WADSLEY & PENN, *supra* note 2, at 471 (explaining cards work like cash whereas the retailer will claim payment against the card issuer).

33. See *id.* (referencing *In re* Charge Card Servs. Ltd., [1988] 3 W.L.R. 497 (Eng.), holding payment by the customer by credit card was absolute payment).

34. *See* Brandel & Leonard, *supra* note 13, at 1040 (describing benefits merchants receive from allowing customers to pay with charge cards).

35. *See* Margaret Howard, *Shifting Risk and Fixing Blame: The Vexing Problem of Credit Card Obligations in Bankruptcy*, 75 AM. BANKR. L.J. 63, 134 (2001) (discussing the highly lucrative profits financial institutions earn from credit cards).

The banking system plays the role of the initiator of the payment card scheme the majority of the time.[36] The banking system constantly floods the public with intense advertising campaigns regarding the need and possibilities of using payment cards.[37] A concrete proposal to issue the card is conveyed to the customer, at the latest, upon creation of the most basic connection between the customer and the bank—the opening of a current account.[38] The payment card is proposed to the customer alongside other means of payment, primarily the check. In fact, it would be extremely difficult for a customer in the modernized world to manage his or her bank account without a payment card.[39] In addition, the banking system plays a major role in the initiation of the transaction vis-à-vis the supplier. Unlike the customer, who needs the card upon opening a bank account, the supplier needs the card daily to sustain the supplier's business and in connection to the issuer's advertisements. In order to sustain business (especially a business providing day-to-day consumer services), the supplier receives collection and clearing services from the bank or the issuer.[40] The supplier is also guaranteed that the certainty of payment for transactions completed by using the card shall increase significantly (in comparison to, e.g., a check).[41] Notably, the supplier views the card as a safer means of payment mainly based on confidence and trust in the bank and the issuer.[42] As a result, the supplier regularly pays high fees in addition to payments as a percentage of each transaction.[43] In such light, the supplier also appears to be a "customer" of the bank or issuer entitled to special protection based on such a relationship.[44] Alternatively, the supplier is a person receiving a service from the bank or issuer entitled to a protection similar to that entitled to the customer.[45]

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36. *See id.* at 65-68 (discussing the process of a customer opening a credit card account beginning with the card issuer mailing a preapproved offer mailed to the customer).

37. *See id.* at 63 n.1 (referring to the three to four billion credit card solicitations mailed each year in America).

38. *See* Ricardo Ben-Oliel, *Bankers Liability in the Bank Deposit Relationship*, 14 ISR. L. REV. 164, 178 (1979) (describing the *sui generis* nature of the bank deposit relationship).

39. BEN-OLIEL, BANKING LAW, *supra* note 5, at 102-03.

40. *See* RUBIN & COOTER, *supra* note 2, at 756-57 (discussing collection and clearing functions the issuer performs for merchants).

41. *See* Brandel & Leonard, *supra* note 13, at 1040 (discussing how merchant agreements with suppliers protect the supplier as compared to receiving payment in other noncash forms).

42. *See id.* (referencing several benefits associated with utilizing a bank's charge card as a form of receiving payment as opposed to other means).

43. *See* RUBIN & COOTER, *supra* note 2, at 760 (explaining the collection fees charged by the issuers).

44. *See* ELLINGER ET AL., *supra* note 1, at 118-22 (discussing the services a customer receives from a bank).

45. For an interpretation of the term "customer," see *id.* at 118-21 (discussing the services a customer receives from a bank). For a wider interpretation, see CRANSTON, *supra* note 2, at 129-33. It should be noted that the Israeli Banking Law (Service to the Customer), 1981, has adopted a rather broad approach viewing as a customer anyone who acquires services from the bank. *Banking (Service to Customers) Law – 1981*, LEVITAN SHARON & CO.

In executing the transaction, the banking system makes use of a unique mechanism available to it, i.e., the clearing mechanism.[46] This mechanism allows the banking system quick and simple access to the public's bank accounts, thus enabling management of payment schemes from these accounts.[47] The mechanism is used in payment card transactions to debit the customer the sum of transactions and to credit the supplier the same sum, in accordance with the presenting of a slip—even when neither the customer nor the supplier are customers of that bank or issuer.[48] It is clear that without management of the clearing mechanism, the banking system would struggle to provide service to both customer and supplier, thus creating an ineffective and unwelcome arrangement for both.[49]

In spite of these distinctive banking characteristics, the payment card scheme also opens the door to a variety of different and changing services.[50] Some of these services do not have the distinctive banking characteristics previously mentioned and occasionally require other mechanisms, which are not necessarily unique to the banking system.[51] Therefore, I argue this is a unique banking transaction.

In practical terms, defining the payment card relationship as a unique commercial banking transaction imposes strict liability on the bank and issuer vis-à-vis the customer and supplier relationship, which stems from banking law. This liability takes effect in spite of the transaction's unique nature and particularly in light of its socioeconomic characteristics and the bank's dominance in initiating the transaction and marketing it to the general public. The main duty establishing banking liability, on which I focus in this article, is the bank's fiduciary duty, which was singularly developed in Israeli doctrine and case law.[52]

C. The Payment Card as an Agency Relationship

In addition to defining the card as a means of payment and as a unique

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ADVOCATES & NOTARIES, http://www.israelinsurancelaw.com/insurance-law/banking-service-to-customers-law-1981.html (last visited Oct. 29, 2011).

46. For the unique characteristics of the clearing mechanism in defining the banking business, *see* Ben-Oliel, *Elements for a Legal Definition of Commercial Banking*, *supra* note 29, at 515.

47. *See id.* (explaining how the clearing mechanism facilitates the business of credit cards).

48. *See* RUBIN & COOTER, *supra* note 2, at 757-58 (describing the clearing mechanism process and parties involved).

49. On this special cartelistic nature of the payment card market, see Timothy J. Muris, *Payment Card Regulation and the (Mis)Application of the Economics of Two-Sided Market*, COLUM. BUS. L. REV. 515, 520-21 (2005).

50. *See* Brandel & Leonard, *supra* note 13, at 1033-37.

51. *Id.*

52. See *infra* Part IV.B.2 for discussion of the development of a bank's fiduciary duty in Israel.

commercial banking transaction, I argue that in the case of a tripartite payment card the relationship between the parties also constitutes an agency relationship, wherein the issuer is an agent.[53] From the customer's perspective, the issuer acts on behalf of the customer when the purpose of the agency is to bring about the absolute discharge of his debt to the supplier.[54] From the supplier's perspective, the issuer acts on behalf of the supplier when the purpose of the agency is the collection of the customer's debt to the supplier.[55] In actuality, the issuer acts within the legal sphere that exists between the customer and the supplier. As will be shown, this has implications on the analysis of the relationship between the parties.

In both cases described above (acting on behalf of the customer or on behalf of the supplier), the customer and supplier vested in the issuer a power to execute the act of payment or collection, and, in so doing, altered their legal relationship. This conclusion is based primarily on the fact that, after the execution of the payment, the issuer exits the legal relationship, and the payment and collection of the debt is attributed to the customer and supplier, respectively. No additional legal action is required from the customer or the supplier in order to attribute to them the actions preformed by the issuer.

In practical terms, one must, as much as possible, analyze the issuer-customer relationship separately from the issuer-supplier relationship, as two separate agencies from the perspective of each principal party.[56] In other words, in considering a legal issue within the issuer-customer framework, the relationship should be analyzed whereby the customer is the principal, the issuer is the agent, and the supplier is the third party. On the same note, in considering a legal issue within the issuer-supplier framework, the relationship should be analyzed in a manner whereby the supplier is the principal, the issuer is the agent and the customer is the third party. Nevertheless, the analysis changes when a question arises within the tripartite framework, i.e., between the supplier and customer as joint principals and the issuer as an agent. When dealing with this issue, a separate analysis of the relationships—as two separate agencies—is impossible because this situation does not legally express the identical status (of the principals) of both the customer and the supplier towards the issuer. Such a status has implications in examining the parties' respective liabilities. The appropriate legal analysis in this case requires the employment of the laws relating to multiple principals, and particularly those relating to an agent who acts between or among more than one principal in a transaction.[57] In such a

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53. *See* Maffly & McDonald, *supra* note 13, at 463-65 (discussing agency relationships of issuer in tripartite payment card transactions).

54. *Id.*

55. *Id.*

56. Traditional concepts of legal doctrine maintain that agency is a bilateral relationship. *See generally* G.H.L. FRIDMAN, FRIDMAN'S LAW OF AGENCY 11-21 (7th ed. 1996) (defining "agency"); FRANCIS M.B. REYNOLDS, BOWSTEAD AND REYNOLDS ON AGENCY 1-4 (18th ed. 2006) (same).

57. HAROLD GILL REUSCHLEIN & WILLIAM A. GREGORY, THE LAW OF AGENCY AND PARTNERSHIP

case, I argue that the agent's duty to the individual principal becomes incidental to his duty to perform the authorization granted to him by both principals.[58]

One may also use the agency framework to analyze other relationships that diverge from the core relationship between the customer, the issuer, and the supplier. Thus, for example, collecting and clearing entities should constitute subagents, thereby imposing on the issuer liability relevant to their actions. Moreover, the aforementioned thesis also justifies the imposition of stringent duties on the issuer when providing additional services to the parties.[59]

To conclude this point, it is important to note that, despite the description of the relationship as that of agency, the issuer is indisputably not a classic agent. Rather, the issuer is a unique agent because the issuer is the dominant party and is the initiator of the payment card scheme. Moreover, the issuer is the primary beneficiary of the payment card relationship.[60]

III. COUNTERMAND OF PAYMENT

A. Brief Description of the Issue

A tripartite payment card serves the customer, inter alia, in completing transactions with suppliers. Usually, the customer turns to the supplier's business, seeking to purchase a product or a service. Following the purchase of the product or service, the customer wishes to pay for the transaction by using a tripartite payment card.[61] On some occasions, after paying for the transaction with the card, the customer wants the issuer to countermand the payment or to re-debit the supplier when a payment was already executed (sometimes in the manner of an offset). In most cases, customers make such requests due to faults or defects that occurred during the transaction. The aforementioned situations raise the question of the issuer's duty while being given an order for countermand of a payment. Should the issuer act according to the customer's wishes and countermand the payment order, or should the issuer act according to the supplier's likely wishes to honor it?

256-57 (2d ed. 1990); REYNOLDS, *supra* note 56, at 57-59; Arthur B. Laby, *Resolving Conflicts of Duty in Fiduciary Relationships*, 54 AM. U. L. REV 75, 80-89 (2004) (discussing conflicts of interest and duty when agents act on behalf of more than one principal in the same transaction).

58. Laby, *supra* note 57, at 80-83.

59. *Id.*

60. Maffly & McDonald, *supra* note 13, at 463-65.

61. In order for the customer to pay the supplier by a tripartite card, the supplier must be connected with the issuer of the customer's card, either in a direct contract or by an indirect clearing contract (to be a member of a scheme conducted by an issuer who has a clearing arrangement with the issuer of the customer's card). *See* Brandel & Leonard, *supra* note 13, at 1034-37.

B. Existing Law - A Critical Review

American legislation, as a rule, does not require the issuer to countermand a payment order given using a tripartite payment card.[62] Similarly, such a legal duty does not apply, as a rule, in the United Kingdom and under the directives of the European Union.[63] It should be noted, however, that legislators in these countries have granted some protection to customers in cases where faults occur in the initial transaction with the supplier. For example, under certain circumstances in a credit card transaction, the law allows the customer to assert claims and defenses he may have regarding the initial transaction towards the issuer.[64] The purpose behind such provisions is to provide the customer with another entity liable to faults occurring in the transaction.[65] It would seem that these provisions are based on the issuer's liability for granting credit for the execution of the transaction.[66]

Although the concept of customer protection against faults occurring in transactions completed by using a credit card is a worthy one, its implementation through the aforesaid arrangements is not without substantial critique. First, the arrangement only protects the customer with regard to transactions completed using a credit card, although the juridical nature of the relationship leads to the conclusion that the customer should also be protected in transactions completed using debit card. This conclusion is drawn, inter alia, from the nature of the payment by the card (of all various kinds) as a conditional discharge of the transaction and therefore the customer's right to revoke the payment order.

Second, the aforementioned arrangement creates an unjustifiable juridical disharmony on two levels: (1) a disharmony in the payment card market itself, whereby the customer is entitled to certain protections when completing a transaction by using a credit card and to others when completing a transaction by using a debit card, and (2) a disharmony in the means of the payment market in general, as there is no recognition of banking liability for faults occurring in the initial transaction while completing it with

62. Legislation does, however, allow the customer to give a stop payment order in case of a preauthorized transfer. 15 U.S.C. § 1693e(a) (2006).

63. *See, e.g.*, Consumer Credit Act, 1974 c. 39, § 75 (Eng.). On the other hand, the Israeli legislature adopted last year a special arrangement which obligates the issuer to stop the customer's payment order under certain circumstances, primarily when the supplier breaches the transaction he made with the customer. *See* Haim, *supra* note 1, at 274-80, 292-99.

64. *See, e.g.*, 15 U.S.C. § 1666i (2006); Consumer Credit Act § 75.

65. The subject has been an issue for extensive comparative writing. *See, e.g.*, Brandel & Leonard, *supra* note 13, at 1041-55; Christopher Hare, *Your Flexible Friend?*, 64 CAMBRIDGE L.J. 287 (2005) (discussing the application of section 75 of the Consumer Credit Act for lender liability); Higgs et al., *supra* note 13, at 111-14; Maffly & McDonald, *supra* note 13, at 471-79; Note, *Preserving Consumer Defenses in Credit Card Transactions*, 81 YALE L.J. 287, 294-97 (1971).

66. CROWTHER COMMITTEE, REPORT ON CONSUMER CREDIT, 1971, Cmnd. 4596 (U.K.).

other means of payment (e.g., the check).[67] In such a state of affairs, each customer must consider his legal options and relevant protection that each means of payment grants him every time he wants to complete a transaction without the use of cash. This demand contradicts public policy and common fairness since many customers are understandably unaware of the different legal arrangements that apply to each different means of payment.

Third, the said state of affairs may encourage the customer to execute more credit transactions in cases where he has no need to do so. This will be done because the customer is able to obtain certain protections in cases where faults occur in the initial transaction.[68]

Fourth, in order to be granted protection due to faults occurring in the initial transaction, the customer is required to take legal action against the supplier and issuer, often relating to daily transactions at a relatively small sum. It is only reasonable to assume that in such cases the customer would not always opt for the legal action (since it could be longer and more expensive than the sum of the transaction). In such cases the remedy granted to the customer by the aforementioned legal arrangement proves to be ineffective.

Fifth, the aforementioned arrangement is unbalanced with regard to the issuers and suppliers. From the suppliers' perspective, the issuers may include a provision in their contract that allows them to re-debit the supplier at the sum of the transaction in case of claims made by the customer. This is likely due to issuers' concerns for the customer's right to assert claims regarding faults in the initial transaction against him. In such a state of affairs, in order to prevent possible damage to themselves, the issuers would countermand the payment order and return the funds to the customer. It should be noted that this state of affairs is also undesirable, as the supplier may suffer a financial disadvantage, especially if it eventually turns out that the customer's claims were unfounded. It is important to note in that regard that the supplier is also a "customer" requiring legal protection vis-à-vis the issuer.[69] From the issuer's perspective, its legal status is also unclear. The issuer would attempt to minimize its own damages due to the concern of being sued by the customer. On the other hand, if the issuer withholds payment to the supplier, then the issuer takes the risk of the customer's claim being unfounded and subsequently being exposed to a possible suit by the supplier.

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67. U.C.C. § 4-403 (1977); Bills of Exchange Act, 1882, 45 & 46 Vict., c. 61 § 75 (Eng.).

68. On the financial risk of credit transaction, see Teri Rebecca Daniel, Note, *Improvident Extension of Credit as an Extension of Unconscionability: Discover Bank v. Owens and a Debtor's Rights Against Credit Card Companies*, 54 CLEV. ST. L. REV 435, 436-37 (2006); Angela Littwin, *Beyond Usury: A Study of Credit-Card Use and Preference Among Low-Income Consumers*, 86 TEX. L. REV 451, 453-56 (2007-2008).

69. According to my doctoral thesis, the issuer also has strict liability towards the supplier. Haim, *supra* note 1, at 209-24.

Finally, it is improper to impose such broad liability on the issuer for the damage derived from the initial transaction itself, as distinguishable from the duty to only countermand the payment order in proper cases.

In light of the above critique, it is reasonable to doubt both the effectiveness and justification of the aforementioned legal arrangement. Rather, the analysis of the juridical nature of the payment card relationship, as presented above, should lead to a different conclusion. As I argue, it indicates that the issuer has a duty to countermand the payment order if the initial transaction was flawed. The duty to ascertain whether such a fault occurred lies with the issuer. I shall hereafter elaborate on these matters.

IV. COUNTERMAND OF PAYMENT AND ISSUER LIABILITY IN LIGHT OF THE PROPOSED THESIS

A. General

In this Section, I examine the issuer's duty to countermand a payment order given by the customer with regard to a transaction completed by a tripartite payment card, in light of my aforementioned thesis. The discussion of this issue is divided into two main questions: first, whether, as a rule, the issuer has a duty to countermand a payment order given by the customer; second, in cases where such a duty exists, what are its boundaries?

I argue that according to the juridical nature of the relationship, the issuer has a duty to countermand the payment order given by the customer. As for the boundaries of this duty, I contend that it is not an absolute duty and that it applies only in cases where the initial transaction was flawed. Thus, and in accordance with the juridical nature of the relationship, the issuer's main duty in such cases should be to examine the initial transaction in detail and reach a legal conclusion as to whether it was flawed. I also argue that a disclosure duty applies to the issuer with regard to the policy it employs in case of such countermand requests. In light of these conclusions, I offer several practical suggestions for the issuer to decrease its liability towards the customer and supplier.

B. Considerations and Suggestions on the Issue in Light of the Proposed Thesis

1. My proposals in light of the bills of exchange laws

Bills of exchange laws acknowledge the customer's right to countermand a payment order he gave to the bank by a check.[70] The rule established by the Uniform Commercial Code ("U.C.C.") is that a banker's authority to pay a check drawn by the customer is revoked upon the countermand of payment by the customer, provided that the countermand notice was given in circumstances

70. U.C.C. § 4-403; Bills of Exchange Act § 75(1).

allowing the bank to execute it.[71] Hence, it can be asserted that following the countermanding of payment the bank owes his customer a positive duty to refuse payment of the check.[72] This principle is also accepted in the United Kingdom and European Union[73]

As discussed, it is my view that bills of exchange laws provide an appropriate analogy to the payment card relationship. The applicability of this analogy should be determined on a case-by-case basis, according to the level of similarity or dissimilarity between the bills of exchange characteristics relevant to the legal issue at hand and those of the payment card.[74]

I contend that the law governing checks requires some adaptation in order to be employed with regard to the tripartite payment card relationship. In my view, a certain dissimilarity exists between the characteristics of the tripartite payment card relationship and those of the check. As noted above, both the check and the payment card are intended, as a rule, to serve in the completion of various initial transactions.[75] However, while checks require only the establishment of one contractual relationship—that between the customer and the bank—the payment card transaction requires the establishment of a tripartite contractual relationship between the customer, issuer, and supplier.[76]

As a result, the duties of the bank or the issuer toward the various parties change accordingly. When analyzing the countermand of payment by check, the bank's only duty is to act in accordance with the customer's order and refuse to pay the check if the payment order was countermanded. Conversely, when dealing with a countermand payment order in a tripartite payment card relationship, the issuer's duty is to not only act in accordance with the customer's instructions, but also with those of the supplier. Thus, the bank has a unilateral duty toward the drawing customer when dealing with the countermanding of payment by check and a bilateral duty toward the customer and the supplier when dealing with the countermanding of a payment by a tripartite payment card.

It would therefore seem that the correct application of the check law in this case would not lead to a countermand of payment only according to the customer's instructions, but must take the supplier interest into account as well. Correct application of the check law in such a case leads to the conclusion that such a countermand depends on another question: whether the transaction between the customer and the supplier was flawed. If the

71. U.C.C. § 4-403.

72. BEN-OLIEL, BANKING LAW, *supra* note 5, at 329; COWEN & GERING, *supra* note 24, at 416.

73. Bills of Exchange Act, § 75(1).

74. *See supra* Part II.A.

75. *Id.*

76. See Haim, *supra* note 1, at 87-90, for a broader discussion of the term "payment card" and its comparison to the check.

transaction was flawed, then no harm came to the supplier, and the payment order given by the customer must be countermanded in accordance with his request. In such a case, we come closer to applying the law governing the check. However, if the transaction was not flawed, the issuer must comply with the supplier's instructions and not countermand the payment order. Such a situation differs from the one governing the check.

It should also be noted that, unlike a countermand of payment by check where the bank may have difficulties in recovering payment from the supplier if the countermand notice arrives too late, the bank would usually be able to offset the transaction and re-debit the supplier in the case of a countermand on a payment card.[77]

The application of the law governing checks should lead to the conclusion that in order for the issuer to dispose of its duty when countermanding a payment order given by the customer, it must examine the initial transaction in detail and determine whether it was flawed. Only an unequivocal answer to that question can lead to an outcome whereby the issuer meets its duties toward both parties. In the absence of such an answer, the issuer is exposed to strict liability.[78]

Assuming my assertions are correct, two additional questions arise. The first relates to the nature of the examination the issuer must complete in order to dispose of his duty with regard to the countermand of the payment.[79] This matter shall be clarified below. The second question pertains to the issuer's duty while the examination and determination as to the breach of the transaction is pending. In answering this question, I contend that it is inevitable that until the issuer disposes of its said duty and reaches a final legal conclusion regarding the breach of the transaction, it must bear the burden of payment to both parties. In other words, it must repay funds to the customer but also incur the payment of that sum to the supplier. After the dispute has been resolved, the issuer may once again debit the party who received funds unlawfully. The issuer's practical possibilities of resolving this strict burden shall be discussed in Section IV.C of this Article.[80]

2. My proposals in light of the fiduciary duty

According to American law, the banks owe, under certain circumstances, a fiduciary duty to their customers.[81] This approach is also accepted in other

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77. U.C.C. § 4-403 cmt. 1.

78. Haim, *supra* note 1, at 87-90.

79. *See* RUBIN & COOTER, *supra* note 2, at 781 (explaining that the issuer must obtain a copy of the charge slip from the supplier to determine what the problem is before countermanding payment).

80. *See infra* Part IV.C.

81. *See, e.g.*, Denison State Bank v. Madeira, 640 P.2d 1235 (Kan. 1982) (holding that a fiduciary relationship between a bank and a customer depends on the circumstances and facts of each individual case); Bank of Red Bay v. King, 482 So. 2d 274 (Ala. 1985) (finding a fiduciary duty exists when a customer relies on a bank for financial advice); Garrett v.

countries.[82] The Israeli Supreme Court of the mid-nineties took a different approach.[83] In the *Tsabach* case, the Israeli Supreme Court adopted the approach suggested by Professor Ben-Oliel,[84] whereby the bank's fiduciary duty to its customers is a general duty whose existence does not depend on certain services or circumstances.[85] This general fiduciary duty needs concretizing at each and every separate banking service.[86]

This Article does not discuss the different approaches to the application of the bank's fiduciary duty. I would note, however, that in my thesis I have adopted Professor Ben-Oliel's approach, which was also adopted by the Israeli Supreme Court.[87] This approach can be summarized as follows: in light of the juridical nature of the bank deposit relations, the substantial power granted to the bank, its public standing, the psychological aspects of the banking services and the customer's inferiority, the bank owes a general fiduciary duty to the customer. The banks general fiduciary duty (as opposed to its concretizing) is independent of any specific service or circumstances.[88] It is my view that espousal of this approach brings about the imposition of appropriate duties on the banking system and eventually contributes to its validity and solidity. However, even if we assume that the bank's fiduciary duty depends on a certain service and special circumstances—as is accepted in the laws of

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Bankwest, Inc., 459 N.W.2d 833 (S.D. 1990) (finding that a fiduciary relationship between a bank and a customer can arise if customers faith or trust in bank results in the banks control or influence over the customers affairs); Waddell v. Dewey Cnty. Bank, 471 N.W.2d 591 (S.D. 1991) (finding that typically a bank owes no fiduciary duty to a customer unless the customer puts faith in the bank, is in a dependent position, and the bank exercises control over the customers affairs).

82. *See, e.g.*, Woods v. Martins Bank, [1959] 1 Q.B. 55 (Eng.) (holding that bank owed duty to customer to take reasonable care and skill when providing financial advice); Lloyds Bank Ltd. v. Bundy, [1975] Q.B. 326, 336-39 (Eng.) (outlining the categories in which a fiduciary relationship between a customer and a bank can develop); Nat'l Westminster Bank Plc v. Morgan, [1985] A.C. 686, 707 (Eng.) (finding that a fiduciary relationship can form if the bank has a dominating influence over the customer); Bertolo v. Bank of Montreal (1986), 33 D.L.R. 4th 610 (Can. Ont. C.A.) (noting that a fiduciary relationship can exist between a customer and a bank in special circumstances); Vita Health Co. (1985) Ltd. v. Toronto-Dominion Bank (1994), 118 D.L.R. 4th 289 (Can. Man. C.A.) (holding that the relationship between a bank and a customer is not normally fiduciary, but there are exceptions); ELLINGER ET AL., *supra* note 1, at 128-29 (explaining that a bank's duty to follow a customer's instructions is subject to limitations).

83. CA 5893/91 Tefahot Mortgage Bank v. Tsabach, 48(2) PD 573 [1994] (Isr.).

84. Ben-Oliel, *Safety Boxes*, *supra* note 5, at 85.

85. *Id.* at 83-88.

86. *Tsabach*, 48(2) PD at 595; *see also* Plato-Shinar, *supra* note 5, at 32-40 (discussing the fiduciary duties of banks in Israel).

87. See Kevin Rogers, Note, *Trust and Confidence and the Fiduciary Duty of Banks in Iowa*, 35 DRAKE L. REV. 611 (1985-1986), for similar approaches to fiduciary duties in the United States. *Cf.* Kurth v. Van Horn, 380 N.W.2d 693, 697-98 (Iowa 1986) ("[I]t is difficult to categorize cases because of the diverse nature of **fiduciary** duties and the general principle that each case must be decided on its own facts.").

88. BEN-OLIEL, BANKING LAW, *supra* note 5, at 102-03.

various countries—it nevertheless remains that when faced with the countermand of payment made by using a payment card, such a duty must be imposed on the bank vis-à-vis the customer and the supplier, for a number of reasons.

First, when a bank supplies the service of a tripartite payment card, it ultimately and knowingly supplies a specific service to two of its customers who may, under certain circumstances of using the service, find themselves on opposing sides of a dispute. Thus, not only does the bank risk creating a conflict of interest between its own interests and those of its customer, but also—and more severely—it risks entering into a conflict of interests between its two customers. The latter conflict of interests risk becomes very real when the bank receives an order to countermand a payment from the cardholder. In this situation, the bank finds itself in the legal sphere between the interest of the customer and the interest of the supplier. It will probably receive contradicting orders from both and will have no choice but to decide in favor of one or the other (the interest of the customer or the interest of the supplier). This conflict of interests is more severe than in the majority of other banking services and therefore justifies the imposition of a high standard of conduct on the bank and the issuer.[89]

Second, and on a more general note, the use of payment cards distorts the customer's discretion with regard to buying capabilities. This is common in cases where credit is granted to the customer, but is also common where transactions are made by using the card without the actual granting of credit (e.g., debit cards). In both situations, the customer might be tempted to make purchases which the customer would not have necessarily made had the transaction been executed in cash. This stems from the sense of "security" provided by the card—as it promotes the illusion that the customer is not actually spending money—and from the level of trust the customer places in the bank. From a legal point of view, we can note that in similar situations where credit is granted, courts have decided that the bank may be bound by a fiduciary duty to its customers, inter alia, because of duties imposed on it by the legislature.[90] This should also apply to the issue of a countermand of payment order given by a customer using a payment card. In both cases—executing transactions by credit or executing transactions by using a card—the "temptation" to execute more transactions is well acknowledged. This

89. *See* CRANSTON, *supra* note 2, at 191(differentiating between the existence of a fiduciary duty in the bank-depositor area and the contractual relationship in commercial lending situations). A similar conflict occurs when the bank advises a customer about stock investment. In these cases the British and Canadian courts acknowledged the bank's fiduciary duty. *See, e.g.*, Woods v. Martins Bank, [1958] 1 W.L.R. 1018 (Eng.); Standard Invs. Ltd. v. Canadian Imperial Bank of Commerce (1985), 22 D.L.R. 4th 410 (Can. Ont. Sup. Ct. J.).

90. For example, in *Stone v. Davis*, 419 N.E.2d 1094, 1097-99 (Ohio 1981), the court addressed the issue by applying the principles of the Truth in Lending Act, 15 U.S.C. §§ 1601-67 (1968). *See also* Commonwealth Bank of Australia v. Smith, (1991) 42 FCR 390, 392-394 (Austl.) (finding a fiduciary relationship existed because the bank was dealing with two customers).

temptation increases the risk of faults occurring in these transactions and can therefore justify the issuer's liability for countermand of payment in the proper circumstances.

Third, the tripartite payment card relationship constitutes that of agency. It is well known that the duty of such a relationship is a fiduciary duty of the agent to its principals.[91] For that reason, the bank should have a fiduciary duty to the customer and the supplier within the framework of the payment card relationship, particularly in the case of a countermand of payment, wherein the bank faces a conflict of interests between its principals. This is further clarified below.[92]

If my assertions are accepted, then a question also arises as to how the fiduciary duty should be made concrete regarding the case of countermand of payment in payment card relationships. In my view, there are three central aspects to a bank's fiduciary duty in a case of countermand of payment made by a customer using a payment card. First, the issuer has a duty, in certain circumstances, to execute the customer's order to countermand the payment. This stems directly from its duty to act competently and professionally in providing its services. Second, the issuer has a duty to examine the initial transaction in detail and to reach a legal conclusion as to whether that transaction was faulty. For that purpose, the issuer must establish a neutral mechanism to resolve the dispute relating to the transaction. Third, the issuer has a duty to disclose certain details of its policy while being ordered to countermand a payment. I shall elaborate on these aspects.

A fiduciary duty is intended to protect a legitimate interest of the bank's customers.[93] In the matter at hand, we must consider the legitimate interest of the customer (the cardholder) and the supplier when the customer orders the issuer to countermand a payment. The legitimate interest of the customer in such a case is that the issuer assists him by not paying the supplier in case he learns that the transaction was flawed.[94] The customer's expectation stems from the great confidence the customer has in the issuer, from the close relationship between the two—deriving from the deposit of the customer's money in the bank—and also from the issuer's liability to the deposited funds.[95] This relationship gives the customer a strong sense of security and

91. RESTATEMENT (THIRD) OF AGENCY § 1 (2006); REYNOLDS, *supra* note 56, at 181-206; *see also* CRANSTON, *supra* note 2, at 188-89 (viewing the bank as a fiduciary based on its role as an agent).

92. *See infra* Part IV.B.3.

93. BEN-OLIEL, BANKING LAW, *supra* note 5, at 102-06. *See also* Rogers, *supra* note 86, at 612-15 (discussing the recognition of a fiduciary duty in situations where a customer places trust and confidence in a bank); Kurth v. Van Horn, 380 N.W.2d 693, 698 (Iowa 1986) (failing to find a fiduciary relationship when the customer has not demonstrated a risk to a significant interest).

94. *See* Brandel & Leonard, *supra* note 13, at 1041-42 (listing possible flaws in the customer-supplier transaction).

95. *See supra* Part II.A.

reliability regarding the nature of the initial transaction, as well as with regard to the "protection" the issuer is supposed to provide the customer in case the initial transaction was flawed. Conversely, the legitimate interest of the supplier is to have a high level of certainty that the issuer will collect the customer's debt relating to the transaction. The supplier relies on the fact that it is paying a steep fee to the issuer for its services and that the issuer guarantees, in return for that fee, a high level of certainty with regard to collection of the customer's debt.[96] Thus, like the customer, the supplier also believes that completion of the transaction by way of a tripartite payment card provides it with, in and of itself, a high level of certainty with regard to the customer's payment by the issuer.[97] Like the customer, the supplier also acts with the same sense of "confidence" provided to it by the issuer, and under the assumption that the issuer shall collect for the supplier the customer's debt in case the supplier finds that the transaction was lawfully executed.

The aforementioned interest of the parties is far from negligible. Thus, as a result of the issuer's public mandate and the confidence induced by the completion of the transaction by using a payment card, the parties might take risks which they would not have taken had the transaction been executed in cash. For example, the customer might pay for the transaction with the card prior to even receiving the product because they are under the assumption that the issuer will not pay the customer's debt to the supplier if the product is not supplied. The customer will, in many cases, only be charged for the transaction at a later date. This may reinforce the illusion that the money is not transferred to the supplier at the time of the transaction. Similarly, on the other side of the transaction, the supplier might take the risk of engaging with a "problematic" customer under the assumption that the issuer will transfer the amount of the payment even if the customer refutes, possibly incorrectly, the transaction.

It appears that the legitimate interest of the parties is additionally based on the close connection between the issuer and the initial transaction. It is well known that the issuer receives fees as a percentage of the transactions executed by using the card. The issuer therefore constantly seeks to increase the number of transactions completed using the card.[98] In order to accomplish that goal, the customer is guaranteed a safe mechanism and a very high level of service, and the supplier is guaranteed a high level of payment certainty. Moreover, the close connection between the issuer and the transaction stems from the technical nature of the transaction. As a result of services and benefits granted by the issuer through the card, customers will increase their use of it in order to enjoy such services and benefits.[99]

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96. *See supra* Part II.B.

97. *Id.*

98. *See* Muris, *supra* note 49, at 522 (describing one of the issuers streams of revenue as the interchange fee that is paid whenever the card is used).

99. *See generally id.*

Thus, it is purely rational for both the customer and the supplier to expect the quality of the services they receive from the issuer or bank to be extremely high. Similarly, the customer and supplier can expect the issuer or bank to fulfill the former's legitimate expectation and protect the interests of each. As a result, and under the assumption that the concretized fiduciary duty must lead to the protection of the legitimate interest and expectation of each party, the issuer's duties must also be determined in a manner that fulfills them all.

I contend that the issuer can only protect the legitimate interests of all the parties by examining the initial transaction in detail to determine whether it was flawed. In my opinion, the only way the issuer can perform this duty in a reliable, professional, and effective manner is to establish a mechanism of legal authority through which the issuer may resolve the question of flaws in the transaction. Moreover, because the issuer places itself in a conflict of interests between the customer and the supplier, it is inappropriate for the issuer to decide the dispute. Rather, the decision should be made by a neutral third party (who is appointed by the issuer and accepted by the customer and supplier). Such a state of affairs could also assist to reinforce the trust and confidence that exists between the parties, which might be undermined if the issuer were the deciding party. The nature of this mechanism, particularly in light of the juridical nature of the payment card relationship, will be discussed below.[100]

In light of my conclusions, , the issuer's duties in the face of current legislation should also be further discussed. As described, the U.C.C. grants the customer a legal cause of action against the issuer in case of flaws in the initial transaction.[101] However, the U.C.C. does not address the issuer's duty while countermanding a payment. This duty derives from case law and legal doctrine.[102] Nevertheless, I argue that an issuer choosing to take a legal risk by not acting in accordance with his fiduciary duty and examining the initial transaction in detail is still obliged by the same fiduciary duty, to explicitly disclose to the customer and supplier certain details regarding his countermanding of payment policy. Specifically, the issuer must disclose to the parties its policy in cases of customer claims of flaws in the initial transaction and a subsequent request to countermand a payment. That is, the issuer must clarify to the parties either that it is not protecting their legitimate interests or that it is doing so in a manner different from the previously suggested method of using a third-party dispute resolution program.[103] Such a disclosure duty constitutes the minimal obligation of the issuer in that regard.

100. *See infra* Part IV.C.

101. *See supra* text accompanying notes 53-55.

102. U.C.C. § 4-403 (1977).

103. *See* Vinals, *supra* note 2, at 601-02 (discussing a similar approach); *see also* Lloyd's Bank v. Bundy, [1974] 3 All E.R. 757 (H.L.) 767-73 (appeal taken from Eng.); ELLINGER ET AL., *supra* note 1, at 82-85 (examining a bank's fiduciary duties).

The exact definition and boundaries of the issuer's disclosure duty in this matter shall be elaborated later in this Article.[104]

Finally, it seems that a conclusion similar to that arising from the application of the bills of exchange laws is called for in light of the issuer's fiduciary duty.[105] Meaning that the issuer should bear the burden of payment (that of the customer's debt and the supplier's payment) to both parties, pending resolution of the dispute and the subsequent determination whether to countermand the payment. This obligation is, of course, subject to the issuer's right to restitution of the payment from the relevant party after the dispute is finally resolved.

3. My proposals in light of agency laws

As discussed, I argue that the tripartite payment card scheme constitutes a relationship of agency.[106] Consequently, the issue of the countermand of payment should be regulated in accordance with the laws pertaining to multiple principals, particularly those pertaining to an agent who acts for more than one principal in a transaction between or among them.[107]

The Third Restatement of Agency provides that two principals may authorize an agent to act between them in a certain matter.[108] The Restatement emphasizes that in such a case the agent must act in good faith vis-à-vis his principals, to disclose to them that it is acting on behalf of them both, as well as any other fact that might influence their discretion.[109] I accept the Restatement's approach here with regard to a payment card relationship. It therefore appears that the issuer must disclose to both parties—before entering a contract between them—the various risks involved, including the policy the issuer employs in cases of a countermand of payment order because such details might indisputably influence the principals' discretion. In addition, and even if the issuer disposes of its said duty, it is my opinion that this does not exempt the issuer from acting further in accordance with the authorization given to the issuer by the two principals. This is so even if that authorization and consent for the issuer to act on behalf of both principals were made with full disclosure. I therefore contend that alongside the said disclosure duty, the issuer is still bound to execute its role according to the authorization given to it by the two principals.[110]

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104. *See infra* Part IV.B.3

105. *See supra* Part IV.B.1.

106. *See supra* Part III.C.

107. The concept of multiple principals is a relatively new term. The legal writing on this issue is relatively limited. *See* REYNOLDS, *supra* note 56, at 59 (examining co-principals); *see generally* Haim, *supra* note 1, at 225-44.

108. RESTATEMENT (THIRD) OF AGENCY §§ 3.16; *see also id.* § 8.06.

109. *Id.* § 8.06.

110. *See* Haim, *supra* note 1, at 229-30 (arguing that the principal's consent does not give the agent the power to breach his fiduciary duty towards them; rather, it provides the agent with a defense from the principal's possible later claim that by consenting to act as a multiple agent the agent breaches his fiduciary duty).

As explained above, the issuer's authorization stems from the tripartite payment card relationship, which constitutes a tripartite agreement between the parties whereby the issuer would only execute payment from the customer to the supplier if the initial transaction was lawfully executed and not flawed.[111] Hence, in case of a countermand payment, the issuer should be bound by the duty to pay only if the transaction was not flawed.[112] In addition, the duty to reach a conclusion as to whether the transaction was flawed or not should apply to the issuer as the one undertaking the agency, initiating the relationship and presenting itself as an agent competent and equipped to execute it.[113] It would therefore be difficult for the issuer to relieve itself of liability in situations where it pays the customer's debt when the initial transaction was flawed, or conversely, if it refuses payment of the customer's debt when the initial transaction was lawfully executed.

It should be noted following my postulation of the authorization given to the issuer and the issuer's fiduciary duty, if the issuer neglects to implement a procedure to ascertain whether the initial transaction was flawed then the issuer has violated its fiduciary duty to the parties even if it turns out that payment order was lawfully countermanded or executed. This is because the nature of the fiduciary duty allows the duty to be violated even in the absence of any real damage.[114] Consequently, regardless of whether or not the initial transaction was flawed, the issuer violates its fiduciary duty when it does not act in accordance with its authorization, which requires the issuer to examine the initial transaction in detail to determine whether it was flawed. Thus, it is the issuer's responsibility, pending the said examination and resolution of the initial transaction, to bear the burden of payment to both parties.[115]

C. Practical Recommendations

As I have identified what the issuer's duties should be, I now examine how the issuer can fulfill those duties. I have stated that the issuer's main duty is to examine in detail the initial transaction. Meaning, the issuer must ascertain whether the transaction was flawed or not. But how should the issuer fulfill this duty?

First, it appears that the issuer must not perform the examination itself. This is so for two reasons. First, the issuer does not possess the skills or authority to reach a legally binding conclusion, thereby creating the

111. *See supra* Part IV.B.2.

112. *See* Haim, *supra* note 1, at 233-35 (explaining that the content of contracts obligates the issuer to pay only when the sale was conducted legally).

113. Laby, *supra* note 57, at 125-48 (explaining the agent's duty when he causes a potential conflict of interest between his principles).

114. *See* REYNOLDS, *supra* note 56, at 212-13 (explaining the agents duty to the principal).

115. *See* RESTATEMENT (THIRD) OF AGENCY § 3.16 (declaring that an agent may have co-principals, from which it follows that the agent has equal duties to each).

possibility that a court of law would reach a different decision than the one made by the issuer, even if the issuer acts to the best of its ability. Thus, and especially in light of the strict nature of the fiduciary duty, the issuer might be liable for damages as the one unlawfully countermanding the payment. The second reason is rooted in the conflict of interests in which the issuer is placed within the framework of countermanding payment in a tripartite payment card relationship. In fact, due to the issuer's significant interest in the execution of initial transactions by using the card, the issuer constantly faces the temptation of favoring one party over the other.[116] Either way, any path taken by the issuer might also undermine the trust between it and the party against whom it decided. Additionally, the issuer is also the one driving the parties into the problematic situation because on the one hand, the issuer is obliged to examine the transaction in detail and ascertain whether it was flawed, and on the other hand, the issuer does not possess the legal skills to do so. It is illogical that the issuer would resolve the conflict it had, at the very least, a hand in creating. This is also not possible under agency law—specifically the law that governs an agent's responsibilities where that agent caused the violation of its own agency.[117]

Second, because the issuer cannot itself resolve the dispute between the parties, I contend that it must turn to a neutral third party to do so.[118] The use of a third party eliminates the conflict of interest facing the issuer and allows the issuer to fulfill its duties without apprehension. Nevertheless, the assistance of a third party may be of use to the issuer only under two conditions: first, when the third party is legally authorized to make a decision that is legally binding on the parties; second, when the issuer bears the burden of the "double payment" to the customer and supplier pending the decision of the third party. To successfully use a third party, the issuer may initiate an arrangement in which the parties agree to a legally binding alternative dispute resolution mechanism that may bring about a swift resolution concerning the supposed flaws of the initial transaction.[119]

An issuer appointing a third party to examine the initial transaction serves to significantly reduce the risk of erroneously countermanding a

116. *See generally* Muris, *supra* note 49 (discussing the revenue streams of the issuer).

117. Arthur B. Laby, *Resolving Conflict of Duty in Fiduciary Relationship*, 54 AM. U. L. REV. 75, 91-92 (2004).

118. Haim, *supra* note 1, at 97-98.

119. This can be achieved by the arbitration mechanism, for example. In my opinion, there is no prevention for the arbitrator to be appointed by the issuer, as long as he remains neutral, impartial, and possesses the legal knowledge regarding the situation. This arbitration arrangement should be financed by the issuer since it is within his interest and his legal duty to resolve the aforementioned conflict. The advantage of the arbitration arrangement is that it should resolve the issuer's conflict quickly and justly. Therefore it will give the issuer the certainty he needs to stop (or not stop) the customer's payment order. In the context of the issue, the arbitration should be, in most cases, a short procedure (a few sessions at most), since payment card transactions are mostly small ones. The issuer still remains obligated to disclose to the parties the existence and nature of this mechanism before issuing a payment card.

payment. In fact, by employing such a mechanism the issuer complies not only with the personal expectation of each party that the payment order will only be countermanded in case the initial transaction was flawed, but also with its duty according to the proposed legal arrangement and to the authorization it received from both parties. Moreover, due to the inherent conflict of interests created by the issuer in this state of affairs, the use of a third party may reinforce the confidence and trust already existing between the parties and may also, ultimately, even encourage the use of the card as an effective means of payment.

Finally, in order not to relieve the issuer from its duties prior to the said final resolution, the issuer bears the burden of payment to both customer and supplier until the examination ends and the duty to ascertain whether to countermand the payment order is fulfilled.

As for the issuer's disclosure duty, I suggest that the issuer must strictly uphold several important points. First, the issuer must disclose to the parties that within the framework of the tripartite payment card relationship, the issuer has a double duty to both customer and supplier.[120] This means that the issuer is not unequivocally obliged to accept the position of a certain party, but rather, the issuer is to examine—through a neutral lens—the scope and manner of the transaction. This is not plainly clear and therefore disclosing this explicitly, prior to the creation of a relationship between the parties, is essential in order to inform the parties of the true nature of the service and to reinforce confidence and trust between all parties.

Second, as different issuers might adopt different policies in the said situation, the issuer must disclose to the parties the policy it employs in case of a countermand of payment order. Such disclosure should include the circumstances under which countermanding is made possible, and the manner of examination the issuer conducts with regard to the initial transaction. In employing such disclosure, the issuer may decrease the chance that the customer and supplier will rely on a policy the issuer does not in fact employ.

Third, I contend that it does not suffice for the issuer to disclose these details in the contracts. The parties must receive the disclosure through a document in language which is clearer and more readily understood than the language in a typical contract. Moreover, the identity of the customer may also dictate a duty of the issuer to explain the content of the policy orally, in clear, plain language, to ensure that the customer understands the issues and the available alternatives.[121] An issuer acting in this manner also increases the

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120. *See* National Westminster Bank Ltd. v. Morgan, [1985] A.C. 686 (H.L.) 707 (appeal taken from Eng.) (discussing duty to disclose potential conflict of interest); Woods v. Martins Bank, [1958] 1 W.L.R. 1018, 1019 (Eng.) (explaining the duty of disclosure).

121. *See* Commonwealth Bank of Australia v. Smith (1991) 42 FCR 390, 392-94 (Austl.) (discussing disclosure duty); Ricardo Ben-Oliel, *A Bank Mortgage in General and a Bank Mortgage for Housing in Part: A Critical Review*, 5 DIN UDVARIM 1, 55-59 (same).

customer's ability to make use of, in appropriate cases, alternative means of payment. Such alternatives may be, for instance, payment with a check or a banking transfer, in which the payment order by a check can be utterly countermanded and the issuer is not placed in the situation of having double duties to the parties.[122]

V. CONCLUSION

In recent years, payment cards have been a source of various risks and mishaps. In an attempt to address these, I have proposed a thesis that would assist to uniformly and comprehensively define the liability of the parties using various payment cards.

The proposed thesis reflects the main characteristics of payment cards. Its adoption would lead to a relationship that is more equal, fair, and just for all parties involved, and is sufficiently flexible so that it may adapt to future developments in the payment card market. The adaptation of the thesis would also bring the arrangement of payment cards closer to those pertaining to other means of payment—a state of affairs that is essential to maintain fairness vis-à-vis the general public of banking customers.

This Article focuses on the issue of countermand of payment. It appears that the issuer cannot be easily relieved from the duty to examine the initial transaction in detail and ascertain whether it was flawed, and consequently decide whether to countermand the payment order given by the customer. This outcome differs from the current law in the United States and other countries by imposing on the issuer liability regarding whether the initial transaction was flawed, as opposed to imposing personal liability for the actual flaws themselves.

It should be noted that despite the importance of the issue pertaining to the countermand of payment, the arrangement regarding other important questions would also change according to the proposed thesis. This is particularly true with regard to misuse of cards, a "card not present" transaction, the nature and scope of granting credit by the card, and the issuer's liability in providing peripheral services to the customer.[123] However, presenting the thesis's practical effects on those issues is beyond this Article's scope.

In sum, the model and practical outcome presented in this Article, as well as other effects its proposals would induce, would bring about a fairer and more equitable framework for all parties involved in a payment card relationship.

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122. See *supra* Part IV.B.1 (discussing the bank's duty to stop the payment order given by a check).

123. *See generally* Haim, *supra* note 1.