IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY
COMMERCIAL LIST

CL 27/00

BETWEEN ALLEN'S ENTERPRISES LIMITED

Plaintiff

AND BANK OF NEW ZEALAND LIMITED

Defendant

Hearing: 8 December 2000

Counsel: G.M. Harrison & T.A. Spinka for Plaintiff
N.S. Geyde & N.M.A. Alley for Defendant

Judgment: 8 December 2000

JUDGMENT OF FISHER J

Solicitors:

Jones Fee, DX CP 18020, Auckland (Attn: C.R. Langstone) for Plaintiff
Bell Gully, DX CP 20509. Auckland for Defendant

Introduction

[1] The plaintiff ("Allen's") claims a refund of $3,026 said to have been wrongly debited to its bank account by the defendant ("BNZ"). Although the sum is small the matter is said to involve a question of principle relating to the use of credit cards. I am grateful to both counsel for the quality of their submissions.

The plaintiff

[2] Allen's was a trader in antiques. Its proprietor, Mr Allen, was an expert in Chinese porcelain. Through his company he sold the antiques to individual purchasers throughout the world. In 1998 he decided to offer his purchasers the option of paying for their purchase by credit card. This required him to enter into a written agreement with his bank, BNZ.

Credit card system

[3] The agreement with BNZ had a background of local and international systems for the payment of merchants from the bank account of purchasers using credit card vouchers issued or authorised by the purchasers. At an international level the system rested on a complex set of standing contracts between banks and a given credit card operator such as Visa or Mastercard. The contracts authorised an elaborate series of agreed regulations, bylaws and rules for the practical implementation of credit card transactions. They stipulated the basis on which the cardholder was to provide the authority to the merchant to draw against the cardholder's account using the credit card. The merchant would present a voucher claim to the merchant's bank. The merchant's bank would communicate the claim to the cardholder's bank using procedures prescribed by the credit card operator. The cardholder's bank would debit its customer's account and remit the funds to the merchant's bank. The merchant's bank would then credit the merchant's account.

[4] The system as a whole rested upon broadly three contractual relationships. The first was between the cardholder and the cardholder's bank. The second was the

set of contracts linking the various banks and the credit card operator. The third was the contract between the merchant and the merchant's bank. The last of these is usually referred to as a "merchant agreement". It is the merchant agreement between Allen's and BNZ which falls for interpretation in the present case.

Merchant agreement between Allen's and BNZ

[5] The present merchant agreement authorised Allen's to operate a credit card charging system using Mastercard and Visa cards. These credit card facilities could be invoked by mail order or telephone order. Under the agreement the bank "authorises the merchant to carry out transactions using credit and/or debit cards accepted by the bank". Pursuant to clss 10.2 to 10.4 the bank agreed:

> 10.2 We must pay to your account the full amount of all valid and acceptable sales and *cash* transactions processed by you.
>
> 10.3 We must charge your account with the full amount of all valid and acceptable refund transactions processed by you.
>
> 10.4 We must give you each month a statement showing the full amount of all transactions processed by us during the previous month.

[6] Those undertakings by BNZ were qualified in certain cases. Some transactions negotiated by the merchant were to be either "invalid" or "not acceptable" under the following provisions:

> 9.1 A transaction for a sale, refund or provision of *cash* is not valid if:
>
> (a) the transaction is illegal; or
>
> (b) the signature on the transaction voucher or authority is forged or unauthorised; or
>
> (c) the nominated card's validity dates are not current; or
>
> (d) the nominated card is listed on a warning bulletin sent to you or we have otherwise told you not to accept the nominated card; or
>
> (e) the nominated card is used without the authority of the cardholder or, in the case of a mail, computer or

telephone order, the transaction is not authorised by the cardholder; or

(f) the particulars on the copy of the transaction voucher given to the cardholder are not identical with the particulars on any other copy; or

(g) the transaction voucher is incomplete or illegible; or

(h) you provide a cardholder with *cash* in a nominated card credit transaction; or

(i) the amount of any transaction or transactions on the same occasion is more than the authorised floor limit unless you had obtained authorisation; or

(j) the price charged for the goods or services is more than your normal price for them; or

(k) you charged a fee for the provision of *cash* in a transaction; or

(l) it represents the collection or refinancing of an existing debt including, without limitation, the collection of a dishonoured cheque; or

(m) another person is to provide the goods, services or *cash* the subject of the transaction; or

(n) you did not actually supply the goods, services or *cash* or have indicated your intention not to do so as required by the terms of the transaction; or

(o) the goods, services and *cash* were supplied outside New Zealand without our consent; or

(p) the transaction is recorded in a currency other than New Zealand dollars without our consent; or

(q) this agreement was terminated before the date of the transaction; or

(r) except in the case of a mail, computer or telephone order the nominated card was not presented; or

(s) in the case of a mail, computer or telephone order, you did not record reasonable identification details for the cardholder and the validity dates of the nominated card; or

(t) in the case of a transaction, details of which are keyed into a terminal, you did not record on the transaction

voucher reasonable identification details for the cardholder; or

(u) the transaction is made by or for any other merchant; or

(v) you have not complied with the requirements in any of the documents listed in Condition 2.

9.2 A transaction for a sale, refund or provision of *cash*, at our election, is not acceptable if the cardholder:

(a) disputes liability for the transaction for any reason; or

(b) makes a claim for set-off or a counterclaim.

9.3 We may refuse to accept a transaction if it is not valid or not acceptable, or may charge it back to you if we have already processed it as set out in clause 21.1.(d).

...

21.1 You authorise us to withdraw from your nominated account or any account you have with us, including the account maintained under 10.1 without notice:

(a) all fees, charges and costs in connection with the services and any use of a terminal; and

(b) all outstanding amounts arising from refund transactions; and

(c) all over-credits paid by us on sales and *cash* transactions due to errors or omissions; and

(d) all credits paid by us on sales and *cash* transactions which are not valid under this agreement; and

(e) all government charges levied on the services, a terminal we supply, your accounts with us and this agreement; and

(f) any amounts found to be due to us during an audit or check by us; and

(g) any additional fees if you seek telephone authorisation where it was not required under clauses 6(b)(ii) and 6(i) ; and

(h) any charges arising from the early termination of a contract you have with us; and

(i) any interest arising thereon from the date of demand to the date of payment at a rate specified by us; and

(j) all other amounts you owe us under this agreement.

[7] These provisions applied to "a transaction for a sale, refund or provision of cash". Although "sale transaction" was not defined ("transaction" being merely stated to include "the sales transaction, refund transaction and cash transaction") it is common ground that it contemplated the usual sale of goods or services by a merchant in return for which the customer would make a payment using a credit card. A "refund transaction" was a transaction by which the merchant could use the credit card system to effect a refund to a customer. A "cash transaction" involved a merchant's provision of cash in return for payment by credit card.

Sales by internet auction

[8] Having set up a credit card facility, Allen's started selling its pottery by auction on the internet. For this it used a United States based internet auction house known as "eBay". eBay provided a facility for merchants such as Allen's to offer an item at auction on terms which eBay broadcast to potential bidders through the internet. eBay's terms of sale stated "your bid is a contract – place a bid only if you're serious about buying the item. If you are the winning bidder, you will enter into a legally binding contract to purchase the item from the seller." The merchant could also stipulate its own terms of sale. Allen's did so in terms which included a 90 day return warranty in the following terms:

> The guarantee now expires 90 days after the sale end date, and refunds will only be made if any claims in that 90 day period, are supported by written statements which challenge my dating assertions, from either:
>
> (a) Christies or Sotheby's Asian Art specialists, or
>
> (b) A curator of Oriental arts at any major museum, or
>
> (c) A recognised testing laboratory using recognised scientific testing procedures (eg Thermoluminescence).
>
> Refunds are limited to the gross sale price (excluding shipping and insurance), minus Ebay's listing fees and commission.

Allen-Tang dealings

[9] In January 2000 Allen's listed an antique pottery horse for sale by auction through eBay. It attracted mounting electronic bids in the usual way. The successful bidder was a Mr Tang of the USA who purchased the horse for NZ $4,845. Mr Tang authorised Allen's to charge the purchase price against his Visa card. He provided the necessary particulars to Allen's for this purpose. Allen's sent Mr Tang an invoice for NZ $4,845 and made a Visa claim to its bank, BNZ. On the strength of those arrangements Allen's despatched the horse by mail to Mr Tang in the USA. Through conventional banking circles BNZ presented that claim to Mr Tang's bank, Citibank, in the USA. Citibank recognised the claim and remitted the necessary funds to BNZ. BNZ credited Allen's account with NZ $4,845.

[10] All of that took place in January 2000. By that stage Mr Tang had his horse, Allen's had the money, and it appeared that the whole matter was at an end. Two months later, however, Mr Tang advised Allen's that he was returning the horse. He claimed that it was a fake. Correspondence followed between Allen's and Mr Tang. Allen's pointed out that Mr Tang would be entitled to a refund if, but only if, he pursued one of the avenues which had been contractually specified. Mr Tang declined to have the horse tested or to provide documentary evidence as to lack of authenticity. Instead, he unilaterally posted the horse back to Allen's, claiming a full refund.

[11] Mr Allen feared that the horse would be damaged if he did not collect it from the post office. He did so and sent it off to an independent expert in Hong Kong. The expert provided a certificate confirming the horse's authenticity. Allen's advised Mr Tang of this in an e-mail of 19 March 2000. Allen's gave Mr Tang the options of having the horse returned to him less costs or alternatively having Allen's resell the horse and forwarding Mr Tang his net proceeds. When Mr Tang made no response Allen's resold the horse at auction on his behalf. It did not fetch as much this time. Allen's used the Visa account system to credit Mr Tang's account with the net proceeds of NZ $1,819 after deducting the costs of the resale and certification.

[12] In May Citibank claimed a refund from BNZ. On 23 May 2000 BNZ wrote to Allen's pointing out that the horse had been returned and asking why Mr Tang had not been given a full refund. Allen's explained why the refund had been partial only. After further correspondence with Citibank, BNZ accepted Citibank's argument that a full refund was due. It made a full refund, debiting Allen's account for the purpose.

[13] Although nothing turns on the point, it is difficult to see why BNZ agreed to the full refund. The contract had been fully executed. The price was paid. Mr Tang received his horse. He had the sole property in the horse. He had no right to rescind the contract. It was Mr Tang's decision to send his own horse to Allen's. Allen's said and did nothing to indicate that it was abrogating the original contract. It must be at least arguable that all it was doing was reselling Mr Tang's horse on his behalf to reduce his own losses.

Issues

[14] When BNZ declined to reverse the debit it had made from Allen's bank account Allen's brought these proceedings. It claims damages for breach of contract. Although no formal statement of defence has been filed, it is agreed that all of the allegations pleaded by the plaintiff are admitted with the exceptions of paragraphs 11, 12 and 13. They allege that in debiting the plaintiff's account BNZ was acting in breach of its contract and that BNZ had no right to debit the account. Those allegations are denied.

[15] It is common ground that the relationship between Allen's and the bank is governed by the merchant agreement of August 1998. There is no suggestion that Allen's was ever a party to the contractual arrangements between the various banks and/or the credit card operator, nor of course a party to the contractual arrangements between Citibank and Mr Tang. It is true that in cl 2(a) of the Allen's-BNZ merchant agreement there is a stipulation that Allen's had to comply with all requirements applicable in current regulations, bylaws and rules of a nominated card scheme provided by the bank to Allen's. However it is not suggested that any such documents were provided to Allen's or that Allen's were in breach of them.

[16] It is agreed that the dispute turns on the proper interpretation of clss 9.2 and 9.3 interpreted, of course, in the context of the agreement as a whole and that factual matrix which had been in the mutual contemplation of the parties when they entered into the agreement. At one point in these proceedings BNZ raised the possibility of other defences arising from potential invalidity under other provisions in cl 9.1. At the hearing before me those arguments were abandoned. Everything turns on the interpretation of clss 9.2 and 9.3

BNZ's right to decline collection where cardholder disputes liability

[17] It will be seen that in the merchant agreement clause 9.1 specifies a series of situations in which the relevant transaction will be held "not valid". By way of contrast, cl 9.2 deals with a different category of transaction which attract the lesser epithet "not acceptable". Clause 9.2 gives the bank the right to classify a transaction as "not acceptable" if the cardholder disputes liability for the transaction for any reason or claims a set off or counter-claim. Where the cardholder disputes the transaction in that way the bank has the option of accepting or rejecting the transaction forwarded to it by the merchant for collection.

[18] It is clear that in this case Mr Tang did dispute liability for the transaction. I can see no ground for implying into cl 9.2(a) a term of the kind suggested by Mr Harrison that the challenge advanced by the cardholder must be legally justified. The wording of cl 9.2(a) is plain on its face. People "dispute liability" under a contract as soon as they argue that they are not liable under it. There is nothing to suggest that their stance must have some foundation in law. It follows that in the present case there was a transaction which was capable of falling within cl 9.2(a). However, it is the consequence of that classification which matters. For this one must turn to cl 9.3.

[19] Clause 9.3 gives the bank two options. They are merely options because of the word "may" in each case. The first is to "refuse to accept a transaction". It is common ground that this referred to the right of the bank to decline to collect upon a transaction submitted to it by the merchant. That is plain both from the words "refuse

to accept" and also the deliberate contrast with the later words "may charge it back to you if we have already processed it".

[20] The first of the two options under cl 9.3 gives the bank the opportunity to decline to process the transaction in the first place. That would of course result in the merchant never receiving any credit into the merchant's account. There is some similarity with a collecting bank refusing to assist in the collection process where a cheque has been stopped before the credit has reached the payee's account. It is not suggested that in the present case the first limb under cl 9.3 could now be availed of by BNZ. By the time Mr Tang disputed liability BNZ had already processed the transaction and credited Allen's account. Only the second option, if available, could now help the bank.

Bank's right to reverse a credit where cardholder later disputes liability

[21] Once a sale has been implemented by the passing of property and possession, and receipt of payment by the vendor, the transaction is prima facie at an end. So is the processing associated with the credit card once the funds have been credited to the merchant's account. For example the merchant would be entitled to withdraw and spend the funds at that point.

[22] BNZ accepts that after a credit card transaction has been executed in that sense it could withdraw the funds from the merchant's account, and refund them to the cardholder's bank, only if it can point to a positive contractual right to do so. The only candidate in that respect is the second limb of cl 9.3. If applicable, the second limb gives the bank the right to "charge it back to him if we have already processed it as set out in clause 21.1.(d)".

[23] On the face of it the difficulty for the bank is that cl 21.1(d) is limited to "all credits paid by us on sales and cash transactions which are not *valid* under this agreement". If language is consistently used in this contract, the word "valid" could refer only to transactions falling within cl 9.1 (described as "not valid") and not those falling within cl 9.2 (described as "not acceptable"). On the face of it, therefore, if the sole challenge to a transaction comes under cl 9.2 rather than cl 9.1,

the bank's contractual remedy is confined to the first limb of cl 9.3. It does not give rise to any option to charge the transaction back to the merchant.

[24] That interpretation stems from the plain language of those clauses. It is reinforced to some degree by the use of the expression "not acceptable" in cl 9.2. That phrase seems to place the emphasis upon the notion of acceptance or refusal to accept the transaction for processing, as distinct from revisiting the transaction for chargeback purposes.. The phrase may be contrasted with such expressions as "invalid", "void" or "ineffective" denoting a purported transaction which is inherently incapable of being recognised for processing purposes. There is some reinforcement for that view in the association between the word "acceptable" in cl 9.2 and use of the same word root a few lines later in the first limb of cl 9.3. There is no equivalent connection with the second limb in cl 9.3

[25] Because of that apparent meaning on the face of the words themselves, and the lack of any obvious ambiguity, I do not think it necessary to proceed on to the contra proferentium argument advanced by Mr Harrison. Prima facie the contract supports the arguments advanced for Allen's. It remains to consider, however, the bank's arguments to the contrary.

Alternative interpretation of the wording of clause 9.3

[26] Mr Geyde submitted that the word "it" in the second limb of cl 9.3 was a reference back to the whole phrase "a transaction if it is not valid or not acceptable". By that means he argued that when it is said in the second limb that the bank may charge "it" back to you the word "it" embraced both invalid and not acceptable transactions. Mr Geyde submitted that cl 21.1 was a purely procedural or machinery provision and that it ought not to be used as a means of interpreting the more substantial provision in cl 9.3. He categorised the limitation to the words "not valid" in cl 21.1(d) as merely a matter of "loose or unthinking" drafting.

[27] It seems to me, however, that the word "it" in the second limb of cl 9.3 is more likely to refer back to the unadorned noun "transaction", particularly since it is the "transaction" which is charged back to the merchant where the second limb is

operative. It requires, to my mind, a more elaborate, cumbersome and therefore unnecessary interpretation to extend the word "it" to the lengthy phrase referred to by Mr Geyde. I can see no reason why cl 21.1(d) should be relegated in importance as a source of contractual meaning when it has been expressly adopted in cl 9.3 as the means of defining the substance of the bank's option under the second limb. Further, it seems to me that there would have to a compelling reason for departing from the meaning apparent on the face of the plain language used. I can see no compelling reason in the words themselves. However, Mr Geyde went on to advance reasons which in his submission justify that interpretation.

Rejection under cl 9.3 would not have time to operate

[28] Mr Geyde submitted that the opportunity for the cardholder to dispute liability in terms of cl 9.2(a) would nearly always arise for the first time after the credit card transaction had been processed. Thus in most if not all cases there would be no opportunity for the cardholder to dispute liability before the merchant bank had accepted the transaction for processing under the first limb in cl 9.3.

[29] I am not at all sure that I ought to accept that proposition as a question of fact. Certainly for an overseas transaction of the kind involving Mr Tang that is probably correct. It should be borne in mind, however, that the contract is to be interpreted in the light of all of the various transactions which Allen's might enter into and of course these would include local transactions.

[30] The situation here is not very different from that relating to the stopping of cheques. It is not at all unknown for purchasers to stop cheques before they have been processed even where the merchant had parted with possession on the strength of the cheque. If the purchaser is too late to prevent payment to the merchant by that summary means the purchaser has to resort to a direct legal dispute with the merchant which, if necessary, involves the issue of proceedings and resolution through the courts. I cannot see anything inherently unlikely in an intention to treat credit card transactions in the same way. On the face of it I would have thought the converse a good deal more unlikely. It would be odd if, after the matter had been processed through conventional banking systems, the purchaser could, on the

strength of an unsubstantiated protest, and long after the transaction had been implemented, have it unravelled in this way.

Other interpretation arguments.

[31] Another of the Bank's arguments was based on cl 7.3(c) of the contract. In presenting a voucher for a transaction a merchant warrants that the cardholder is not disputing the transaction or making a set-off or counter-claim. Mr Geyde submitted that that demonstrated the intention of the parties that disputes between the merchant and the purchaser should not involve the bank. He supported that submission by the further point that pursuant to cl 26(c) the bank gave no guarantee that a processed transaction was valid or acceptable.

[32] If anything, however, cl 7.3(c) reinforces the notion that liability disputes notified by the cardholder are intended to be taken into account for credit card processing purposes only up to the point that the credit card transaction is processed by the banks. The only opportunity for the merchant to provide a warranty arises when the merchant submits the voucher to the merchant's bank for processing. It would be entirely consistent with the system I have mentioned that the merchant would warrant at that time that the cardholder was not disputing the transaction. That in turn would help the merchant's bank to know whether to accept the transaction in terms of cl 9.3.

[33] Once the transaction has been accepted by the bank, however, there is no obvious further opportunity for the merchant to give the bank a warranty. There would be no affirmative communication from the merchant such as the provision of a voucher. Any dispute which might later arise between the cardholder and the merchant could certainly give rise to litigation between them direct. However the occasion for a warranty to the bank on that subject could scarcely arise earlier than notice to the merchant that there is in fact a dispute.

[34] Nor does cl 26 seem to assist. In cl 26 the bank refutes any guarantee as to the validity or acceptability of the transaction. But this involves the question whether the bank had the positive right to make a chargeback, not the question whether the

merchant might otherwise have made a claim against the bank based on some form of guarantee.

No commercial sense

[35] Mr Geyde submitted that the interpretation contended for by the plaintiff would make no commercial sense given the anomalous position in which the bank would be left. The argument is that the bank might be forced to make a refund without recourse to the merchant.

[36] I do not see anything in the merchant agreement creating a risk of that outcome. For example there is nothing there to suggest that after the merchant bank had processed the transaction and credited the merchant's account a cardholder or the cardholder's bank could, on the strength of an unsubstantiated allegation by the cardholder, make a mandatory recovery from the merchant's bank. Mr Geyde's argument to that effect really had to turn upon the broader relationship between banks and the credit card operator. There are several difficulties in that respect.

[37] First, there is no justification for resorting to a wider factual matrix if the words of cl 9.3 and its associated provisions are plain on their face.

[38] Secondly, the only factual matrix which could be relevant is that which was within the mutual contemplation of both parties at the time the contract was entered into. The bank cannot impute to Allen's a knowledge of the systems and practices within the banking world unknown to its customers. As I mentioned earlier, cl 2(a) makes reference to wider documentation but that was only such regulations, bylaws and rules as might be provided by the BNZ to Allen's. There is no evidence that such additional documents were provided. There are other documents referred to in cl 2 but there is no evidence before me as to which of these documents were provided to Allen's and, more particularly, whether they contained anything which would demonstrate that on the interpretation which the plaintiff favours the merchant bank could be left in a position of needing to pay a chargeback to the cardholder's bank without opportunity for recourse to its own merchant customer.

[39] Thirdly, if one were to look at the system which operates between the various banks (and I emphasise that for the reasons I have mentioned I do not think that this is a permissible aid to interpretation in this case) I am not at all sure that the anomaly would arise. It seems that under that wider system, "Reason code 53" dictated that a chargeback could take place if "cardholder returns merchandise or cancelled services that did not match those described on the transaction receipt or other documentation presented at the time of purchase". Of course that would require that as a matter of fact the cardholder would have to have received non-complying goods. As I interpret code 53, there is no obligation on the merchant bank to recognise a chargeback claim unless a disparity between goods and contract is established as a matter of fact. There is provision for arbitration to deal with disputes between the merchant's bank and the cardholder's bank. I do not doubt that the merchant bank would wish to avoid being drawn into a dispute of that nature but there is at least apparently some avenue for checking the substance of the claim. The mere fact that the cardholder disputes liability is not of itself sufficient. And if the merchant is in fact liable to make the refund it will almost certainly be liable to indemnify a third party such as the bank for making the refund on the merchant's behalf.

[40] As I commented earlier, the bank in this case was much too quick to capitulate to the chargeback claim which was made. There was no reason for thinking that the pottery horse "did not match those described on the transaction receipt or other documentation presented at the time of purchase". However that is beside the point. The matter falls for interpretation in the light of the merchant agreement between Allen's and BNZ alone, not the systems and contracts prevailing in the wider banking world. Under that agreement there was no justification for making the deduction from Allen's account.

Result

[41] There will be judgment for the plaintiff Allen's in the sum of $3,026 together with interest at the rate of 8 percent per annum from 28 August 2000 to the date of this judgment.

[42] I have now heard from both counsel as to costs. Both parties treated this as a test case. Notwithstanding the sum involved it was appropriate that it be dealt with in the High Court in the first instance to save hearing it initially in the District Court and then coming to this court on appeal. The defendant must pay the plaintiff's costs which I award on a 2B basis.

RL Fisher J