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FRAMING CONTRACTUAL FREEDOM WITHIN THE PRECEPT OF 'HONESTY, RELIABILITY AND INTEGRITY'

Jiang Ou v. EFG Bank AG[1]

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I. Introduction

Might a bank rely on a conclusive evidence clause against a customer when its employee has knowingly entered into unauthorised transactions on the customer's account? This was one of the key issues before the Singapore High Court in *Jiang Ou v. EFG Bank AG*. The issue brought into question the considerations that shape the contours of contractual freedom, and how the law should respond when a conclusive evidence clause is relied upon to defeat the claim that the bank statement is inaccurate by reason of fraud perpetrated by the bank's employee. The decision invoked both the *Unfair Contract Terms Act*,[2] as well as public policy at common law to defeat the bank's reliance on a conclusive evidence clause. While preventing the bank from shifting the consequences of fraud originating from within the banking organisation may be intuitively appealing, the decision carries broader implications for the drafting of conclusive evidence clauses and raises questions about the ambit of the common law prohibition.

From a theoretical perspective, *Jiang Ou* is also fascinating—to the present commentator, it suggests an underlying precept of 'honesty, reliability and integrity' which threads through the obstacles to the enforcement of the conclusive evidence clause.[3] This essay argues that, apart from informing the application of the reasonableness test under the *UCTA*, the precept of 'honesty, reliability and integrity' catalyses the application of the *contra proferentem* rule in contractual interpretation. Moreover, it has also amounted to a norm animating the extension of the scope of

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1 [2011] 4 S.L.R. 246 (H.C.) [*Jiang Ou*].

2 Cap. 396, 1994 Rev. Ed. Sing. [*UCTA*]. The statute is *in pari materia* with the *Unfair Contract Terms Act 1977* (U.K.), 1977, c. 50.

3 See *Jiang Ou*, *supra* note 1 for the discussion of "honesty" at para. 110, "reliability" at para. 1 (citing *Bache & Co (London) Ltd v. Banque Vernes et Commerciale de Paris SA* [1973] 2 Lloyd's L.R. 437 at 440 (C.A.) [*Bache & Co*]), and "integrity" at para. 122.

the prohibition against excluding personal fraud liability to the context of banking organisations.

This precept may be located within the theory of good faith envisioned by Carter and Peden.[4] Insofar as the theory posits that good faith pervades all of contract law and that the scope of 'honesty' plays a key role in determining its content, the precept of 'honesty, reliability and integrity' in the banker-customer relationship fits well within the theory. This essay argues that the outworking of this precept in *Jiang Ou* demonstrates the normative dimension of 'honesty'.

II. The Asymmetric Approach to Fraud at Common Law

Fraus omnia corrumpit—*i.e*. fraud unravels all. However, while there is no doubt that fraud "vitiates judgments, contracts and all transactions" tainted by such fraud,[5] the application of the principle becomes more complex when the fraud is perpetrated by an employee or agent of an organisation. Organisational responsibility for the acts of its human agents is invariably mediated by the concepts of vicarious liability and agency. For torts, the liability of the employer turns on whether the employee's act is so 'closely connected' with his employment that it is fair and just that the employer should be held vicariously liable for the employee's act;[6] if this 'close connection' test is satisfied, the employer is vicariously liable. This test has been applied to determine whether an employer is liable for the fraudulent acts of its employee.[7] For contractual liability, the question is whether the agent has acted within his actual or ostensible authority; if he has, the agent's acts are attributed to the principal.[8] At heart, the issue is whether the employee or agent's fraud can be legally connected to the organization.

From the risk-allocation perspective, the common law has not taken the simple position that an organisation is legally responsible for the fraud of its employees merely because the employer is the least cost avoider of the risk in question. This is demonstrated by the asymmetric treatment of fraud occurring in the bank-customer's organisation as contrasted to fraud by the bank's employees. Indeed, the advent of conclusive evidence clauses stems in part from the desire of banks to make their customers take responsibility for internal controls over their financial affairs. The imperative for the reallocation of such fraud risks is starkly demonstrated in *Tai Hing Cotton Mill Ltd v. Liu Chong Hing Bank Ltd,*[9] a decision of the Privy Council on appeal from Hong Kong. A clerk in Tai Hing Cotton Mill had forged the signature of the General Manager on the company's cheques. The company's internal controls were weak; it was found as a fact that the weakness in the controls facilitated the

4 J.W. Carter & Elisabeth Peden, "Good Faith in Australian Contract Law" (2003) 19 Journal of Contract Law 155 [Carter and Peden].

5 *Lazarus Estates Ltd v. Beasley* [1956] 1 Q.B. 702 at 712 (C.A.), Denning L.J.

6 *Skandinaviska Enskilda Banken AB (Publ), Singapore Branch v. Asia Pacific Breweries (Singapore) Pte Ltd* [2011] 3 S.L.R. 540 at para. 86 (C.A.) [*Skandinaviska*] adopts the 'close connection' test in *Bazley v. Curry* [1999] 2 S.C.R. 534, *Lister v. Hesley Hall Ltd* [2002] 1 A.C. 215 (H.L.), and *The Ming An Insurance Co (HK) Ltd v. The Ritz-Carlton Ltd* [2002] 3 Hong Kong Law Reports and Digest 844 (Court of Final Appeal).

7 *Skandinaviska, ibid.* at para. 86.

8 *Armagas Ltd v. Mundogas SA* [1986] A.C. 717 (H.L.).

9 [1986] A.C. 80 [*Tai Hing Cotton Mill*].

fraud. While the High Court and the Court of Appeal of Hong Kong found that the company was in breach of duties of care owed to the bank both in contract and tort, the Privy Council held otherwise. The Privy Council reiterated that 'mandate' is the key to discharging the bank's payment obligation.[10] A bank discharges its indebtedness to the customer by making payments within its mandate. Instructions issued by a fraudster lack a mandate. The risk of making payments pursuant to such fraudulent instructions lies with the bank. The Privy Council repudiated the notion that a customer owes a duty to the bank to have in place businesses practices which prevent the perpetration of fraud. Apart from determining the absence of a common law duty on the part of the customer towards the bank, the Privy Council noted that the employee's fraud was not attributable to the company.

Where a bank's employee fraudulently executes transactions on a customer's account, the absence of a mandate would necessarily mean that the bank is obliged to restore the accounts to the state before the fraudulent transactions. Without a mandate to carry out the transaction, the bank's obligation to the customer remains unaltered by the unauthorised transaction. The bank will therefore have to bear the consequences of its employee's fraud. As can be seen, the outworking of 'mandate' in the banker-customer relationship results in an asymmetric approach to fraud arising from the bank's employees, as contrasted to fraud arising from the customer's employees.

The interesting question which *Jiang Ou* presents is whether a bank may, by a conclusive evidence clause, prevent its customer from questioning inaccuracies, whatever their origins. That is, may a bank be absolved from all liability for inaccuracies—regardless of the cause of these inaccuracies—by arguing that its customer has agreed to the conclusiveness of a statement of account upon the lapse of the agreed period?[11]

A conclusive evidence clause typically encompasses two duties. First, the customer assumes contractual responsibility for examining and verifying the statements sent by the bank. Second, the customer agrees to notify the bank of any errors or inaccuracies in the statements.[12] Upon the expiry of the contractually stipulated period for raising inaccuracies with the bank, the conclusive evidence clause renders the statement conclusive of the amounts owing between the bank and its customer. Importantly, the customer is precluded from raising questions relating to inaccuracies in the statements.

It should be immediately obvious how such a conclusive evidence clause reverses not only the common law rule set out in *Tai Hing Cotton Mill*, but also changes the incentives for the customer. A conclusive evidence clause provides a very strong inducement for a customer to carry out periodic internal audits of its finances. Indeed, it must carry out checks on its accounts *within the time period* set out in the conclusive

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[10] *Ibid.* at 103, 104.

[11] Where the lack of mandate originates in fraud external to the bank, there has been no issue with the reasonableness or legality of the conclusive evidence clause: see *Jiang Ou*, *supra* note 1 at para. 103, examining *Consmat Singapore (Pte) Ltd v. Bank of America National Trust & Savings Association* [1992] 2 S.L.R.(R.) 195 (H.C.) [*Consmat*], *Stephan Machinery Singapore Pte Ltd v. Oversea-Chinese Banking Corp Ltd* [1999] 2 S.L.R.(R.) 518 (H.C.), *Tjoa Elis v. United Overseas Bank Ltd* [2003] 1 S.L.R.(R.) 747 (H.C.) [*Tjoa Elis*], and *Pertamina Energy Trading Limited v. Credit Suisse* [2006] 4 S.L.R.(R.) 273 (C.A.) [*Pertamina*].

[12] *Pertamina*, *ibid.* at para. 68; *Jiang Ou*, *ibid.* at para. 60.

evidence clause. Otherwise, a lapse in checking the accuracy of the bank statements could result in very real financial losses.

However, conclusive evidence clauses are framed broadly to cover errors in general, without distinguishing whether the errors originate from fraud by the customer's employees, or whether the errors originate from the bank. The problem posed in *Jiang Ou* was a more extreme form of an error from within the bank. The transactions were not only unauthorised, but were also fraudulently effected by the bank's employee. Can the conclusive evidence clause nonetheless be employed to enable the bank to assert the conclusiveness of the bank statement regarding debts owing between the parties?

III. 'Reasonableness' under the *UCTA*

As the conclusive evidence clause is a standard term of contract inserted by the bank to restrict its business liability, s. 3 of the *UCTA* applies and subjects the term to the 'reasonableness' test.[13] On this, Steven Chong J. held that:[14]

> [I]t is plainly unreasonable that a bank should be able to shift the risk of unauthorised transactions by a fraudulent employee (within its own sphere of control) to an innocent customer by way of a conclusive evidence clause.

The conclusion proceeds from an analysis of what constitutes fair allocation of an organisation's operational risks. Courts have been willing to uphold conclusive evidence clauses because they:[15]

> [E]nable banks to contractually allocate risks which were better managed by customers, brought about by tainted transactions outside the purview of the bank.
> …
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> However, the converse must be true as regards transactions executed fraudulently by banks' employees. Allocation of the risk of fraud or wilful misconduct of banks' employees to the customers by way of conclusive evidence clauses is contrary to the somewhat compelling rationale underpinning the genesis of such clauses in that banks rather than the customers would be in a better position to effectively detect the fraud of its own employees.

Chong J. had earlier determined that, on a true construction of the contract, the clauses did not "exclude liability caused by the fraud or wilful misconduct of [the bank's] employees."[16] Accordingly, "there was strictly no necessity for [him] to examine the issue of whether the clauses should be upheld in the case of an individual."[17] The

[13] Thean J.'s doubts in *Consmat*, *supra* note 11 at para. 21 regarding the applicability of the *UCTA*, *supra* note 2 were made before the Singapore Parliament expressly enacted the *UCTA* in 1994. Since its enactment, there can now be no doubt that that the *UCTA* may be applied to scrutinise the reasonableness of conclusive evidence clauses found in banking contracts: see *e.g.*, *Pertamina*, *ibid.* at paras. 59-63; *Tjoa Elis*, *supra* note 11 at paras. 92, 93.

[14] *Jiang Ou*, *supra* note 1 at para. 118.

[15] *Ibid*. at paras. 118, 119.

[16] *Ibid*. at para. 107.

[17] *Ibid*. at para. 117.

holding, constituting as it does one of the grounds of decision, nonetheless has undeniable precedential value. Although the Singapore Court of Appeal has articulated similarly strong sentiments in *Pertamina*,[18] the facts there did not involve fraud on the part of the bank's employees.[19] *Jiang Ou* is the first Singapore decision—indeed it might be the first reported decision in the Commonwealth—holding unreasonable a term which seeks to shift onto a customer the consequences of fraud perpetrated by a bank's employees.

The significance of the ruling, however, extends beyond the enforceability of the contractual term at issue in *Jiang Ou*. It puts into issue whether a broadly drafted conclusive evidence clause covering both reasonable and unreasonable exclusions is to be considered unreasonable by reason of the impermissible exclusion. That is, may the bank argue that such a term can be relied upon in scenarios where the exclusion operates reasonably?

The *UCTA* does not, of course, render unreasonable terms void. It operates through the notion of permissible reliance. It prevents a party from relying on a term to exclude or restrict the covered liability "except in so far as… the contract term satisfies the requirement of reasonableness."[20] The regulatory strategy embodied in the 'reasonableness' test is to posit the presumptive impermissibility of relying on a term, except where the person seeking to rely on that term is able to show that the term is reasonable under the parameters set out in s. 11 of the *UCTA*. In other words, where a term is subject to the 'reasonableness' test, the *UCTA disables* reliance on the terms unless the term is shown to be reasonable.
Section 11(1) of the *UCTA* prescribes:

> [T]he requirement of reasonableness… is that the term shall have been a fair and reasonable one to be included having regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made.

The term is thus to be considered as a whole. Moreover, the reasonableness of the term is to be adjudged at the point of contract.[21] Significantly, the statutory test of 'reasonableness' is not to ascertain whether the application of the exclusion or restriction clause is reasonable in the circumstances.[22] Rather, the test is whether it is a "fair and reasonable one to be included".[23] The relevant circumstances are those existing at the point when the contract is concluded. Hence, the nature of the customer—whether it is a commercial organisation, a business savvy individual or an unsophisticated individual—features in the inquiry. However, the actual occasion in

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[18] *Supra* note 11.

[19] *Ibid.* at para. 63: "For example, if a bank attempted to exclude liability for the fraud of its own employees, we would have no hesitation in declaring such a clause unreasonable and invalid."

[20] *UCTA*, *supra* note 2, s. 3(2).

[21] *Thomas Witter Ltd v. TBP Industries Ltd* [1996] 2 All E.R. 573 at 598a (H.C.) [*Thomas Witter*].

[22] *Shearson Lehman Hutton Inc v. Maclaine Watson & Co Ltd* [1989] 2 Lloyd's L.R. 570 at 612 (H.C.); *Stewart Gill Ltd v. Horatio Myer & Co Ltd* [1992] Q.B. 600 (C.A.) [*Stewart Gill*]; *Balmoral Group Ltd v. Borealis UK Ltd* [2006] 2 Lloyd's L.R. 629 at para. 420 (H.C.) [*Balmoral Group*]: "The question is not, as it was under section 55 of the [*Sale of Goods Act, 1893* (U.K.), 56 & 57 Vict., c. 71] whether it would be fair and reasonable to allow *reliance* on the term in the events which have happened" [emphasis in original].

[23] *UCTA*, *supra* note 2, s. 11(1).

which the application of the term is sought does not feature in the statutory parameters for ascertaining 'reasonableness'. Other provisions on the 'reasonableness' test—for example, s. 11(4) and paragraphs (a) to (e) of the Second Schedule to the *UCTA*—refer to circumstances preceding the point of contract. There is therefore no question that the test is of the reasonableness *of the term*, not the reasonableness of the *application* of the term. As Jacob J. pointed out in *Thomas Witter,*[24] when commenting on a similarly worded 'reasonableness' test in the context of an exclusion clause for misrepresentation:[25]

> The [*Misrepresentation Act 1967*][26] calls for consideration of the *term* as such. And it refers to 'any liability' and 'any misrepresentation'. It does not call for consideration of the term so far as it applies to the misrepresentation in question or the kind of misrepresentation in question. The term is not severable: it is either reasonable as a whole or not. So one must consider its every potential effect. The clause does not distinguish between fraudulent, negligent, or innocent misrepresentation. If it excludes liability for one kind of misrepresentation it does so for all. I cannot think it reasonable to exclude liability for fraudulent misrepresentation… since the width of this clause is too great I would have held [that] it failed the requirement of reasonableness and so was of no effect.

This would mean that a broad term which covers unreasonable exclusions might be adjudged unreasonable even if some aspects which it covers are reasonable. Put another way, the unreasonable exclusions taint the term as a whole and thereby render the term unreasonable. Importantly, whether the term is unreasonable *does not* entail weighing the reasonable aspects of the term against its unreasonable aspects, and determining on balance whether the term is a reasonable one. An important implication for the conclusive evidence clause is that if the term fails to distinguish between bank fraud and other scenarios, the bank bears the risk that the conclusive evidence clause may be declared unreasonable and unenforceable.

The contours of 'reasonableness' of a conclusive evidence clause are shaped by the notion that the party who better controls the risk of fraud should bear the risk. The 'better controller of risk' parameter would also extend to unilateral mistakes originating from an organisation since such operational lapses are, *ex hypothesi*, within its control but not within the control of its counterparty. It is difficult to justify how it is reasonable for a bank to cite a conclusive evidence clause to defeat a customer's claim for rectification of mistakes generated by the bank's own processes. After all, if a bank makes a mistaken debit to a customer's account—whether by

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[24] *Supra* note 21.

[25] *Ibid.* at 598 [emphasis added]. The question whether the doctrine of severance can be applied may yet await a conclusive determination. In *Stewart Gill*, *supra* note 22 at 606, a clause excluding a customer's right to "any payment, credit, set-off [or] counterclaim" (at 604) was held to be unreasonable as a whole and not severable to cover only the right to set-off. One question that arises is whether the words "except in so far as" in s. 2(2) of the *UCTA*, *supra* note 2, permit a court to sever the term, *i.e.* to hold one part reasonable and enforceable while holding the unreasonable part unenforceable. *R W Green v. Cade Bros Farms* [1978] 1 Lloyd's L.R. 602 (H.C.) suggests the possibility of severance on the back of the similarly phrased (though now superseded) s. 55 of the *Sale of Goods Act, 1893*, *supra* note 22 (which had the words "enforceable… to the extent that"). Note, however, the differences: see *Balmoral Group, supra* note 22.

[26] (U.K.), 1967, c. 7.

reason of glitches in its software or by reason of human error—it is difficult see why the customer's failure to notify the bank of such mistakes should render such mistakes unrectifiable.[27] In light of *Jiang Ou*, conclusive evidence clauses that fail to distinguish between unauthorised transactions carried out in the customer's organisation and those carried out in the bank stand the very real risk of being declared unreasonable for shifting to the customer risks which a bank should reasonably bear.

IV. Void as a Matter of Public Policy

Apart from finding the clause unreasonable under the *UCTA*, the conclusive evidence clause in *Jiang Ou* was also found to be "void as a matter of public policy" as:[28]

> Shifting the attendant risk and liability for the fraud or wilful misconduct of employees of banks by way of conclusive evidence clauses, strikes at the very heart of the presumed integrity of the system.

The integrity of the banking system stems from "[p]ublic confidence in the banking system",[29] which in turn is founded upon "mutual trust and a reasonable expectation of honest dealings by employees of banks."[30] Thus, to the extent that a conclusive evidence clause undermines the presumed integrity of the system by seeking to absolve a bank from responsibilities which the public perceives to be foundational, it is void. The reasoning here builds on Lord Denning's oft-quoted dictum that such verification clauses are upheld on the premise that the banks "are known to be honest and reliable men of business who are most unlikely to make a mistake".[31]

The public policy rationale for nullifying the conclusive evidence clause echoes the principle that one may not contract out of liability for one's own fraud.[32] However, the policy rationales underlying the two are distinguishable. In the latter principle, there is no issue that the person subject to the principle perpetrated the fraud. In an organisational or agency context, the additional issue of connecting the organisation to the human agent raises the question of whether the relevant common law rules may be contractually displaced.

Neither is the question merely one of the reasonableness of risk allocation. The dictum quoted at the beginning of this section makes it clear that the clause is at odds with public policy by reason of the clause undermining a foundational expectation that the public holds of the banking industry—'honesty and integrity'. This public policy ground is thus different from the principle against exclusion of liability for one's own fraud. The industry to which the public policy ground applies is a narrow one—the banking sector. While expectations of 'honesty and integrity' might also

[27] See also *Tjoa Elis, supra* note 11 at para. 96.

[28] *Jiang Ou*, *supra* note 1 at para. 122.

[29] *Ibid*.

[30] *Ibid*.

[31] *Bache & Co*, *supra* note 3 at 440, adopted in *RBS Coutts Bank Ltd v. Shishir Tarachand Kothari* [2009] SGHC 273 at para. 8.

[32] *Pearson & Son Ltd v. Dublin Corporation* [1907] A.C. 351 (H.L.) [*Pearson & Son*]; *HIH Casualty and General Insurance Ltd v. Chase Manhattan Bank* [2003] UKHL 6 [*HIH Casualty* (H.L.)].

inhabit other business relationships, the public policy objections to a business organisation excluding liability for the fraud of its employees might not be as compelling as a bank doing the same.[33]

At the same time, insofar as the fundamentality of 'honesty and integrity' in banking operations stands in the way of a bank excluding liability for fraud by its employees, it might also extend to situations where internally-generated mistakes result in the bank effecting an unauthorised transaction on its customer's account. "Reliability", cited by Lord Denning as a fundamental premise underpinning the willingness of courts to uphold conclusive evidence clauses,[34] should join 'honesty and integrity' as foundational norms of the banker-customer relationship. The use of a conclusive evidence clause to prevent a customer from requiring a bank to rectify its own mistake strikes at the fundamental norms of 'honesty and integrity' by which banks are expected to operate. It would also undermine public confidence in the reliability of banks. After all, allowance for the operation of a conclusive evidence clause rests on the critical assumption of 'honesty and reliability'. Where a conclusive evidence clause operates to exclude liability flowing from actions at variance with reliability, it would arguably offend the foundational norms that govern the banker-customer relationship.

The significance of *Jiang Ou* therefore goes beyond laying down a narrow rule of public policy against a bank seeking to shift the risk of bank employee fraud to its customers. The source of this rule of public policy lies in the fundamental assumption that 'honesty, integrity and reliability' go to the root of the banking industry, and carries implications for mistakes that originate in the bank, which are otherwise untainted by fraud.

The public policy ground which nullified the conclusive evidence clause in *Jiang Ou* should therefore be seen as a new public policy ground in the landscape of common law illegality. Despite its apparent novelty, this rule stems from sound fundamental assumptions and norms governing how banks operate. It is from these assumptions that conclusive evidence clauses draw their legitimacy. Furthermore, these fundamental assumptions of 'honesty, integrity and reliability' give rise to the constraints on the liberty of banks to exclude their liability. This new public policy ground should therefore be viewed as fundamentally correct.

V. Interpretation

Although it is uncertain whether the common law generally prohibits a principal from excluding liability for the fraud of its agent,[35] it is well-established that any

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[33] The intriguing question after *Jiang Ou, supra* note 1, is how far beyond the banking context the prohibition against excluding liability for employee fraud extends. Apart from banking relationships involving deposit taking and the giving of loans, financial institutions like insurance companies and private equity funds might conceivably seek to exclude liability for employee fraud through the use of conclusive evidence clauses. The present commentator expects that the intensity of the precept of 'honesty, reliability and integrity' inhabiting the relationship is likely to shape the contours of the prohibition, just as it is likely to affect the application of the 'reasonableness' test under the *UCTA*.

[34] See text accompanying note 31.

[35] The Court of Appeal in *HIH Casualty and General Insurance Ltd v. Chase Manhattan Bank* [2001] 2 Lloyd's L.R. 483 held that a principal can protect himself against fraud by his agent by making clear the limitations on the agent's authority (at para. 103). A majority of the House of Lords in *HIH Casualty*

such exclusion must be expressly referred to and manifestly clear from the wording of the contract. Lord Bingham's dictum in *HIH Casualty and General Insurance Ltd v. Chase Manhattan Bank*, articulated in the context of a contract induced by fraud, applies equally to the exclusion of fraud in the performance of a contract:[36]

> For it is in my opinion plain beyond argument that if a party to a written contract seeks to exclude the ordinary consequences of fraudulent or dishonest misrepresentation or deceit by his agent, acting as such, inducing the making of the contract, such intention must be expressed in clear and unmistakable terms on the face of the contract… *General words, however comprehensive the legal analyst might find them to be, will not serve: the language used must be such as will alert a commercial party to the extraordinary bargain he is invited to make*.

As put succinctly by Chong J. in *Jiang Ou*:[37]

> The risk of fraud by the bank's employee is a unique risk that typically resides with the bank… nothing short of express reference in the relevant clause to such a risk [*i.e*. that the bank is shifting onto the customer the risk of bank-employee fraud] would have sufficed.

Such an interpretative approach not only has the benefit of laying bare the unusual risk that the other is made to bear, but also subjects the party seeking the benefit of such an exclusion to the embarrassment of having to explain why he insists on the inclusion of such a clause. Indeed, the 'laying bare' regulatory strategy embedded in this interpretative approach raises questions in the mind of the counterparty of the reliability of the party seeking such an exclusion. If the latter is an organisation, it puts into question the state of internal controls within the organisation. Apart from the embarrassment entailed in explaining the need for such an exclusion clause, its very inclusion is a cause for embarrassment. It is not only fair in forcing the disclosure of unusual risks which the counterparty is expected to assume, but also has the salutary effect of putting at risk the reputation and goodwill of the party seeking such exclusion.

VI. Theoretical Implications

From a theoretical perspective, the interpretative stance taken in the banker-customer context may be seen as being framed by the precept of 'honesty, reliability and integrity', which conditions the intensity with which the former is applied. This notion may be illustrated through a non-banking example. A vendor of property, who confers on an auctioneer the authority to knock down the property to the highest bidder, may at the same time exclude any authority on the part of the auctioneer to make representations on its behalf.[38] One would venture to suggest that this rule applies regardless of whether the auctioneer made the representations fraudulently or

(H.L.), *supra* note 32, left the question open: see Lord Bingham at para. 16, Lord Steyn at para. 24 (agreeing with Lord Bingham), and Lord Hoffmann at para. 80. Handley forcefully argues that the Court of Appeal is wrong: K.R. Handley, "Exclusion clauses for fraud" (2003) 119 Law Q. Rev. 537.

36 *HIH Casualty* (H.L.), *ibid.* at para. 16 [emphasis added].

37 *Supra* note 1 at para. 108.

38 *Overbrooke Estates Ltd v. Glencombe Properties Ltd* [1974] 1 W.L.R. 1335 (Ch.).

innocently. The reason why the attribution rules might be excluded lies in the absence of an overriding principle which renders unseverable the link between the agent's fraud and the principal. This is to be contrasted with the banker-customer context, where the notion of 'honesty, reliability and integrity' is closely identified with the nature of the banking business. This, in turn, binds the banking entity to the actions of its constituent parts, such that it is impermissible to exclude the liability of such constituent parts. In a similar fashion, this overriding precept of 'honesty, reliability and integrity' catalyses the intensity with which the 'clear stipulation' principle is applied. This might, for example, result in requiring specificity in stipulating the types of fraud covered.

At the same time, the precept of 'honesty, reliability and integrity' in the bank's operations might intensify the *contra proferentem* rule, such that unauthorised debits originating in the bank might be interpreted as falling outside a broadly worded conclusive evidence clause, unless the particular liability is covered by clear and unmistakable wording. The notion that the precept of 'honesty, reliability and integrity' inhabits the banker-customer relationship might bring to mind echoes of the implied duty of trust and confidence between an employer and an employee.[39] However, the precept here is more foundational. It is a fundamental premise of the bank-customer relationship, and has ramifications for interpretation, determination of 'reasonableness' under the *UCTA*, as well as public policy on risk shifting. Thus, it reaches into rules susceptible to modification by contract, as well as mandatory norms. It is at the same time more far reaching and more deeply embedded than implied terms, which are susceptible to contractual exclusion and modification.

The notion that the precept of 'honesty, reliability and integrity' pervades the banker-customer relationship is consistent with the theory of good faith postulated by Carter and Peden. In 2003, Carter and Peden argued that good faith is inherent in contract law and informs all aspects of contract law.[40] This includes contractual interpretation and determining the scope of contractual rights. The content of good faith in contract depends on the scope of 'honesty' as a concept.[41] This might include a positive norm,[42] for example, the requirement to communicate the revocation of an offer in order for the revocation to take effect.[43] Alternatively, it might consist of a negative norm,[44] for example, the law on misrepresentation and the requirement to give reasonable notice of onerous terms before they may be incorporated by notice.[45]

The precept of 'honesty, reliability and integrity' that threads through the areas discussed above—interpretation of the scope of an exclusion clause, the public policy prohibition, and the application of 'reasonableness' under the *UCTA*—may be seen as a version of 'honesty' in the context of the banker-customer relationship. Good faith in the interpretation of exclusion clauses would normally require the exclusion of

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[39] *Bliss v. South East Thames Regional Health Authority* [1987] I.C.R. 700 (C.A.); *Malik v. Bank of Credit and Commerce International S.A (Liquidator of)* [1998] A.C. 20 (H.L.).

[40] See Carter & Peden, *supra* note 4 at 156, 158-162.

[41] *Ibid*. at 156, 157.

[42] *Ibid*. at 157.

[43] *Byrne v. Van Tienhoven* (1880) 5 C.P.D. 344.

[44] Carter & Peden, *supra* note 4 at 157.

[45] *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* [1989] Q.B. 433 (C.A.).

liability for fraud of an agent to be explicitly and unmistakably set out; absent a clear and explicit exclusion of such fraud, the clause would not be interpreted to cover such liability. The precept of 'honesty, reliability and integrity' would affirm and indeed intensify the rigour with which it is to be applied.[46] The contextualised version of 'honesty' in the banker-customer relationship also informs how the 'reasonableness' test in the *UCTA* should be applied to a conclusive evidence clause which prevents rectification of errors occasioned by fraud on the part of bank employees.

While Carter and Peden did not illustrate good faith with public policy prohibitions, a well-established example is the common law prohibition against excluding liability for one's own fraud.[47] I would argue that in the banker-customer context, the 'honesty' precept goes further to extend the impermissibility of excluding one's fraud to the impermissibility of excluding liability for fraud perpetrated by its agents within the banking organisation. The latter prohibition may be seen as 'honesty' in banking predicating the impermissibility of thrusting the risk of organisation fraud onto the bank's customer. This contextualised notion of 'honesty' goes further to posit the impermissibility of shifting the risk of errors originating from within the bank to the customer.

While this precept of 'honesty, reliability and integrity' resonates with the implied term of trust and confidence, it is in this context a much more fundamental premise of the banker-customer relationship. For this reason, it informs and shapes the interpretation of the contract, just as it sets the boundaries of permissible contracting. This argument further develops Carter and Peden's theory of good faith by demonstrating how the context can intensify and even extend the contours of liability predicated by general law. In agreeing with Carter and Peden that good faith inhabits all of contract law, I would argue that there also exists a normative dimension to the 'honesty' precept that, in addition to giving content to good faith in contract law, develops such content. To be sure, the normative ramifications have to be worked out circumspectly. While utmost regard should be given to contractual freedom, the 'honesty' precept is nonetheless capable of generating public policy prohibitions in appropriate contexts.

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[46] A good question is whether reliability is at the same level of fundamentality as honesty, such as to be capable of generating a public policy prohibition in a similar manner.

[47] *Pearson & Son*, *supra* note 32; *HIH Casualty* (H.L.), *supra* note 32.