

## 14<sup>TH</sup> PROGRAMME OF LAW REFORM

Issued: 30 July 2021

The Fraud Advisory Panel welcomes the opportunity to comment on the Law Commission's consultation on its 14<sup>th</sup> programme of law reform, launched on 24 March 2021, a copy of which is available from this [link](#).

We are very happy to discuss any aspect of our comments and to take part in all further discussions on the issues we've highlighted to the Law Commission.

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## GENERAL COMMENTS

1. The Fraud Advisory Panel welcomes the opportunity to respond to the Law Commission's consultation on its *14th Programme of Law Reform*, launched on 24 March 2021.
2. The Fraud Advisory Panel (the 'Panel') is the UK's leading counter fraud charity. We act as the collective voice of the counter fraud profession and provide practical support to almost 300 corporate and individual members. Our members come from a wide range of professions and sectors who are united in their determination to stop fraud.
3. Our response proposes one area of potential law reform relating to banks' duties to customers. It has been prepared by a small group of our members.

## BANKS DUTIES TO CUSTOMERS

### Question 1

In general terms, what is the problem that requires reform?

4. Fraud is on the rise in the UK. Nearly 40% of all crime is fraud, and most of it is committed online.<sup>1</sup> Government recognises this threat and has recently committed to designing and delivering a comprehensive Fraud Action Plan.<sup>2</sup> It is envisaged this will include activities to support and safeguard victims and to crack down on money mules.<sup>3</sup>
5. Fraudsters use social engineering both online and over the phone to persuade thousands of people to transfer money each year using transactions that are instantaneous. Sometimes life-changing sums are involved. All too often, these criminals are based outside of the UK or can move money via UK-based money mules. The outcome for victims is financial loss and limited recovery.
6. Some progress has been made with respect to Authorised Push Payment fraud (APP fraud) and the introduction of the Contingent Reimbursement Model (CRM). However, only about a quarter of customers are fully reimbursed in APP fraud cases.<sup>4</sup> Approximately 40% of the complaints received by the Financial Ombudsman Service from victims of fraud last year involved authorised push payment fraud and most of these were upheld (73%) with FOS noting that the CRM is being applied inconsistently.<sup>5</sup> It is

<sup>1</sup> Office for National Statistics (13 May 2021). *Crime in England and Wales: year ending December 2020*. <https://www.ons.gov.uk/peoplepopulationandcommunity/crimeandjustice/bulletins/crimeinenglandandwales/yearendingdecember2020>

<sup>2</sup> HM Treasury and Home Office (4 May 2021). *Economic Crime Strategic Board: 17 February 2021 Agenda and Minutes*. <https://www.gov.uk/government/publications/economic-crime-strategic-board-minutes-and-agenda-17-february-2021/economic-crime-strategic-board-17-february-2021-agenda-and-minutes>

<sup>3</sup> Ibid.

<sup>4</sup> Lending Standards Board (January 2021). *Review of the Contingent Reimbursement Model Code for Authorised Push Payment Scams*. <https://lendingstandardsboard.org.uk/wp-content/uploads/2021/01/LSB-review-of-the-CRM-Code-FINAL-January-2021-.pdf>

<sup>5</sup> Financial Ombudsman Service. *Annual complaints data and insight 2020/21*. <https://www.financial-ombudsman.org.uk/data-insight/annual-complaints-data>. Also see Financial Ombudsman Service. (2 October 2020). *Response to Lending Standards Board Review of the Contingent Reimbursement Model Code for Authorised Push Payment Scams*. <https://www.financial-ombudsman.org.uk/files/289009/2020-10-02-LSB-CRM-Code-Review-Financial-Ombudsman-Service-Response.pdf>

also worth noting that the CRM does not protect all customers and does not protect customers in relation to international payments.

7. We agree with FOS that ideally banks would prevent fraud at source by identifying and closing-down fraudsters' accounts before they can be used.<sup>6</sup> Fraudsters use the UK banking system to facilitate APP fraud by persuading victims to transfer money to bank accounts that they use, and then concealing the proceeds through chains of financial transactions. The law has not yet been codified sufficiently to set out what is expected of banks to protect their customers where a transaction appears suspicious for reasons of fraud.
8. Recently there has been a number of cases dealing with the Quincecare duty of care of banks relating to the extent banks ought to be detecting transactions of fraud risk to their customers.
9. One of these recent cases has identified the need for codification of duties of banks to help customers guard against fraud. As a result of the decision in *Phillips v Barclays [2020]* it is quite clear that the courts need legislative guidance on the standard of care to which banks need to be held to account for detecting fraud against their customers. When rejecting the claim in this particular case the Judge, HHJ Russen QC, stated:

*'I do not accept that the Quincecare duty can properly be used to impose a higher (or more specific) set of standards which dictate that, in certain defined circumstances, the bank is obliged to question the customer's instructions. It is a duty of care framed by concepts of knowledge (actual or constructive) rather than further negligence in failing to follow the rules of some code. If a bank is to be held to the standards of something equivalent to a code for intervention – for present purposes, in the case of suspected APP fraud – then it needs to know its terms.'*

10. In essence, the Judge stated that if a bank is to be held to account for allowing a customer's instructions to make a payment which resulted in a loss to fraud, then the bank ought to know what that standard (duty) of care is (i.e., it needs to be codified).
11. We believe the key issue of codification into law is a duty upon banks to cause customers to suspend making a transaction that is suspect to fraud or financial crime pending a customer affirming their understanding of the transaction and the counterparty. If a bank could be under a duty to use their transaction monitoring systems to identify transactions at risk of fraud and then:
  - a. temporarily suspend that transaction, and
  - b. inform the customer of the reasons for the suspicion

such that the customer is asked to confirm they remain satisfied to make the payment despite the concerns of the bank and their reasoning.

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<sup>6</sup> Ibid.

12. This would advance the position for customers to have a further degree of protection in that:
  - a. customers would know their bank would at least detect (or be under obligation to detect) suspect transactions (or their bank could be held to account for loss of opportunity to stop a transaction), and
  - b. that the customer would, having been notified by their bank, have the opportunity to re-consider their transaction.
  
13. It would also mean that banks are asked to undertake a task akin to enhanced due diligence on the transaction a customer wishes to make which is likely to be detected if outside of the customer's profile. If the customer wishes to proceed despite being asked to re-consider the transaction, they would then be asked to electronically or physically sign a document confirming that the transaction should proceed.

## Question 2

Can you give us an example of what happens in practice? (i.e., how it affects people)

14. An example of what happens in practice is set out below.
  - a. Person A plans to purchase an off-plan property in a property development investment scheme that is misrepresented as a legitimate property investment scheme by fraudsters (Company A).
  - b. Person A is persuaded to invest through phone calls received from a representative of Company A, namely Person B.
  - c. Payments to acquire an interest in a property offered by Company A are to be made via a large retail bank in England (i.e., the bank providing banking services for Person A). Person A authorises a transaction to a Spanish bank (the off-plan property was said to be in Spain). This is not the typical behaviour or transaction of Person A, but they genuinely believe they are paying a legitimate company for a legitimate transaction, namely Company A.
  - d. As a result of this being an unusual transaction, Person A's bank ask Person A if they are sure they want to make the payment, the bank explain why they are suspicious of the transaction and seek Person A's confirmation that they are comfortable with who they are paying.
  - e. In another example, Person B undertakes exactly the same type of transaction, but is not asked by their bank if they are sure they want to make the payment and that they understand the basis for it.
  - f. Within a few months, Persons A and B start to see returns on their investment in the form of small payments paid every month from a party they think is Company A. Persons A and B start investing more money. Neither bank for Person A or Person B questions them and allows these further transactions to be made to

Company A. Except this time, Company A has asked payments to go to Croatia (the off-plan property was said to be in Croatia).

15. In both the above scenarios, the CRM does not apply because the payments are made to an overseas bank. Persons A and B have no redress as their banks are not obligated or required to help customers assess the legitimacy of transactions they wish to make when these transactions are out of the ordinary.
16. However, it could be said that Person A's bank ought not be liable as they asked questions relating to the first transaction and Person A had a chance to reconsider the transaction and continued. However, Person B's bank ought to perhaps be liable because they did not ask anything. These are the types of cases where the Quincecare duty has been in play (i.e., cases where customers are seeking to hold their banks to account where the bank ought to have been on notice of reasons to be suspect about a transaction but not alerting a customer to those concerns).
17. In *Barclays Bank Plc v Quincecare* [1992] 4 All ER 363 it was established that it is an implied term of the contract between a bank and its customer that the bank owes the customer a duty of care to take reasonable care when making a payment on the instructions of the customer. In that case Steyn J explained the scope of the duty as follows:

*'...a banker must refrain from executing an order if and for as long as the banker is 'put on enquiry' in the sense that he has reasonable grounds for believing that the order is an attempt to misappropriate the funds of the company...'*
18. Since then, cases have evolved where the Court has stated a bank has a duty to be on watch, so to speak, to ensure a customer is not defrauded but most recently the cases show there needs to be some information a bank has that causes them to be '*on inquiry*' such that the Quincecare duty could come into play. Even then, this leads to an arduous factual enquiry that is both expensive and heavily weighted against the customer, namely as:
  - a. they are already financially challenged due to having lost money to fraud, and
  - b. the banks have more resources to argue that they did not have a reason to be '*on inquiry*'.
19. Customers are now expected to be as vigilant as possible, but these fraud schemes can sometimes be so convincing as to appear legitimate and draw victims in through advertisements on well-known search engine sites.
20. Banks do have the ability to check the details of payment recipients, to impose restrictions on transactions, and to ask questions of their customers (keeping a record to show that they have tried to protect them when a transaction is out-of-the-ordinary and/or displays other red flags).
21. For banks to check details of payment recipients, they need to know what it is they should/must do. Otherwise, they are left in limbo between the uncertainty of interpretation of whether a bank is liable under the Quincecare duty or not. Banks want

to help their customers but as matters stand, if they try to help but do not do enough, it appears that the bank assumed a responsibility to prevent fraud as that could be argued to be consistent with their actions. Therefore, it is now almost more of an incentive for banks to not imply what their duty is by not taking any steps. The loser is the consumer (individuals and businesses).

22. The only existing guidance banks can look to beyond case law (as to banks duties owed to customers) is the British Standard Institution (BSI) PAS 17271:2019 code of practice for financial institutions on '[protecting customers from financial harm as result of fraud or financial abuse](#)' (published October 2017). Amongst other things it encourages banks to take a proactive approach to minimising risk and provides examples of potentially suspicious activities on customers' accounts.
23. However, like the CRM for APP fraud, this is simply best practice guidance and is not a legislative requirement which compels a minimum standard of care to customers irrespective of their type (i.e., personal or business). In our view legislation is needed to make clear what a customer can expect from their bank.

### Question 3

To which area(s) of the law does the problem relate?

24. The problem relates to the following areas of law: consumer law, commercial or contract law, and regulator law.

### Question 4

We will be looking into the existing law that relates to the problem you have described. Please tell us about any court/tribunal cases, legislation, books or journal articles which relate to this problem.

25. We refer the Law Commission to two articles written by Tenet Compliance & Litigation (a corporate member of the Fraud Advisory Panel) which summarise the law and the BSI protocol. These are:
  - a. '[Quincecare duty: a review of developments](#)' (dated 29 January 2021), and
  - b. '[The Banking Protocol and financial harm](#)' (dated 12 January 2021).

### Question 5

Can you give us information about how the problem is approached in other legal systems?

26. No.

### Question 6

Within the UK, does the problem occur in any or all of England, Wales, Scotland or Northern Ireland?

27. The problem occurs in all four countries of the United Kingdom: England, Wales, Scotland and Northern Ireland.

### Question 7

What do you think needs to be done to resolve the problem?

28. We believe that legislation is required to impose a duty of care upon banks and building societies dealing with customers who use their services for the transfer of money. This legislation would ideally need to prescribe the following.
- a. Which types of customers the proposed legislation applies to (if not all customers).
  - b. Which types of transactions it applies to (for example, not to pre-existing payees).
  - c. The need for banks to identify and monitor transactions of suspicion of fraud or financial crime where a customer is seeking to make a payment which is out-of-the-ordinary. Out-of-the-ordinary could be defined, for example, as not having been made before, to a jurisdiction outside of the UK etc.
29. In the event a customer makes a transaction, and their bank does not make checks which, had those checks been made the customer would not have lost money to a fraudulent scheme, the proposed legislation would then set out the consequences of the bank's failure including liability to the customer and/or regulatory penalty.

### Question 8

What is the scale of the problem?

30. According to UK Finance, in 2020 APP fraud increased in both volume and value to just under 150,000 cases with losses of £479m. Most cases (95%) were related to personal accounts. Since the CRM code was introduced in 2019 there have been 139,104 cases assessed and closed worth £311.8m. £188.3m has been reimbursed to customers.<sup>7</sup>
31. The Financial Ombudsman Service (FOS) reported a significant increase in fraud and scam complaints in 2020/21 (18,000) compared to 2019/20 (11,000). About 40% of

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<sup>7</sup> UK Finance (2021). Fraud The Facts 2021: The definitive overview of payment industry fraud. <https://www.ukfinance.org.uk/policy-and-guidance/reports-publications/fraud-facts-2021> <https://www.ukfinance.org.uk/policy-and-guidance/reports-publications/fraud-facts-2021>

complaints in 2020/21 involved push payment fraud with two-thirds of these cases upheld by them.<sup>8</sup>

### Question 9

What would be the positive impacts of reform? Benefits derived from law reform can include the following.

32. We believe the following benefits would be derived from law reform in this area.
- a. Costs of seeking redress for consumers are likely to be reduced by legislatively holding banks to account. For example, if legislation prescribed when a bank should ask enhanced due diligence questions about a proposed transaction, this would make it clear if a bank had or had not done so and what the consequences of inaction are.
  - b. The reputations of banks would likely be enhanced through providing preventative information and helping their customers when they have become victims of fraud.
  - c. Such change will also see banks improving their current checks to approve bank accounts reducing the number of bank accounts held by fraudsters.
  - d. Fairness. New legislation of this nature would result in consumers being able to understand far earlier if they are likely to succeed in a claim against their bank (rather than waiting for a judicial decision in cases involving the Quincecare duty).

### Question 10

If this area of law is reformed, can you identify what the costs or other negative impacts of reform might be?

33. We believe the possible downsides from law reform in this area might include the following.
- a. An increased cost of banking to consumers (banks having to increase charges to allow for a fund to exist to meet payments where the bank was held liable considering the proposed legislation).
  - b. Delays for consumers on legitimate transactions deemed suspicious by their bank which may lead to loss for a consumer. However, we believe there are very limited circumstances in which an instant payment is necessary. The remedy for this type of issue is customer education so they know transactions may be halted.
  - c. It may be said by banks that if a customer is convinced that they are dealing with a legitimate party when the customer wishes to make the transaction, the customer will approve the transaction despite warnings or caution being urged by their bank.

<sup>8</sup> Financial Ombudsman Service (2020) *Annual report and accounts for the year ended 31 March 2020*. Available from <https://www.financial-ombudsman.org.uk/files/287580/Annual-Report-and-Accounts-for-the-year-ended-31-March-2020.pdf>

That may well be the case, but for some it will stop them being defrauded of large sums of money.

- d. If banks are made liable to pay damages and/or refund losses to customers in these wider circumstances, it may make APP fraud a more attractive fraud type for criminals. However, it may also incentivise banks to improve their due diligence checks when opening new bank accounts and encourage greater information sharing between banks on fraud schemes that are identified.

#### **Question 11**

Does the problem adversely impact equality, diversity and inclusion by affecting certain groups in society, or particular areas of the country, more than others? If so, what are those groups or areas?

34. No, not as far as we are aware.

#### **Question 12**

In your view, why is the independent, non-political, Law Commission the appropriate body to undertake this work, as opposed to, for example, a Government department, Parliamentary committee, or a non-Governmental organisation?

35. We believe the problem requires consideration by an independent, non-political body such as the Law Commission because of its unique ability to:
  - a. build consensus on sensitive issues across a broad range of different stakeholders including regulators, industry bodies and consumer groups, and
  - b. consider technically complex areas of the law which may not be an immediate priority for government. In our view, this issue has a great significance to, and impact on, the victims of fraud including individuals, businesses and not-for-profit organisations.

#### **Question 13**

Have you been in touch with any part of the Government (either central or local) about this problem? What did they say?

36. No, we have not.

#### **Question 14**

Is any other organisation such as the Government or a non-Governmental group currently considering this problem? Have they considered it recently? If so, please give us the details of their investigation on this issue, and why you think the Law Commission should also look into the problem.

37. The Financial Conduct Authority (FCA) is currently consulting on banks' duty of care to consumers. It proposes setting a higher level of consumer protection in the retail financial markets to enable consumers to get good outcomes.<sup>9</sup> Although the consultation does not specially consider fraud, its aims very much align with our own in respect of the Quincecare duty of care to tackle harms and their causes and to 'help consumers make good choices and be confident that they will receive good customer service'<sup>10</sup>.

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<sup>9</sup> Financial Conduct Authority (May 2021). *A new Consumer Duty: Consultation Paper CP21/13*\*\*\*

<https://www.fca.org.uk/publication/consultation/cp21-13.pdf>

<sup>10</sup> Financial Conduct Authority (2021). *FCA proposes stronger protection for consumers in financial markets*, press release, 14 May. <https://www.fca.org.uk/news/press-releases/fca-proposes-stronger-protection-consumers-financial-markets>