

BETWEEN WESTPAC BANKING
CORPORATION

FIRST APPELLANT

AND ANZ BANKING GROUP (NEW
ZEALAND) LIMITED

SECOND APPELLANT

AND M M KEMBLA NEW ZEALAND
LIMITED

RESPONDENT

HEARING: 2 MAY 2000

CORAM: ELIAS CJ
THOMAS J
KEITH J

APPEARANCES: F MILLER AND C BLOOMFIELD FOR WESTPAC
C F FINLAYSON AND M G COLSON FOR ANZ
G S A MACDONALD FOR M M KEMBLA

JUDGMENT: 9 NOVEMBER 2000

JUDGMENT OF THE COURT DELIVERED BY ELIAS CJ

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[1] The appeal is brought by the appellant banks against the refusal of Master Kennedy-Grant to enter summary judgment for them as defendants in proceedings brought in the High Court by the respondent as plaintiff. They do not appeal against the Master's refusal to strike out certain causes of action against them.

[2] The claim by the respondent raises novel points about the standard of care of a paying bank and the knowledge to be imputed to a receiving bank where banking transactions are conducted by electronic transfer of funds. The appeal also requires consideration by this Court for the first time of the defendants' summary judgment procedure provided by a 1998 amendment to the High Court Rules.

Background and pleadings

[3] The background facts as pleaded in the statement of claim can be shortly stated. The plaintiff, MM Kembla New Zealand Limited (Kembla), banked with the first defendant, the ANZ Banking Group (New Zealand) Limited (ANZ). From 1991 it paid its creditors by electronic funds transfer through two systems operated by ANZ. It was a security feature of the electronic funds transfer system that it could be operated on behalf of the company only by two authorised user employees, each of whom was required to use a personal identification number (PIN) allocated by ANZ. The authority to the bank to draw on the company's accounts was communicated electronically with no teller intervention and without authority other than the two PIN numbers.

[4] From April 1992 until April 1997 one of the employees of Kembla authorised to operate the company accounts and to whom a PIN was assigned was Jacqueline Chilcott. As the Kembla accountant she was also the person designated by Kembla to receive all communications about the operation of the accounts from ANZ. From September 1992 to March 1997 Ms Chilcott stole more than \$2 million from Kembla. The thefts were effected by electronic transfer of funds from the ANZ accounts operated by Kembla to accounts maintained by Ms Chilcott

or interests associated with her with the three collecting banks, ANZ, Westpac Banking Group (New Zealand) Limited (Westpac) (the second defendant), and the Bank of New Zealand (BNZ) (the third defendant which did not proceed with its application for summary judgment).

[5] The thefts were accomplished by Ms Chilcott in two ways. In some transactions she obtained the necessary second PIN through deception of other employees who were authorised users. In others she herself used, in addition to her own PIN, the PIN of another authorised user. This second PIN is said in the pleadings to have been sent by ANZ to Ms Chilcott as the employee designated as “System Administrator” to receive communications from ANZ on behalf of Kembla.

[6] Transaction reports confirming all electronic funds transfers were automatically generated by ANZ and sent to Kembla. But they were concealed by Ms Chilcott who was also the person nominated by Kembla to receive the reports on its behalf. It is claimed that Kembla believed the amounts transferred out of its accounts were paid to genuine creditors because of an elaborate system of concealment set up by Ms Chilcott.

[7] Against ANZ as paying bank Kembla claims damages of \$2,016,232.30 together with interest and costs for breach of a duty of care “whether contractual or tortious” to advise the plaintiff “that there was a real possibility that Ms Chilcott was defrauding the plaintiff”. Kembla acknowledges in the pleadings that such duty of care arises only “if a reasonable and honest banker in the stead of the first defendant would have considered there to be such a real possibility”. There is no allegation of dishonesty or bad faith made against ANZ. By letter of 15 June 1999 Kembla confirmed that it alleges that an honest and reasonable banker in the place of ANZ would have considered there to be a real possibility that Ms Chilcott was defrauding Kembla. The allegation was particularised as follows:

- (i) The EFT system created greater risk for misappropriation than, for example, payment by cheque, because a signature was not required to authorise payment.
- (ii) The ANZ sent to Ms Chilcott, as MM Kembla’s ANZ direct system administrator, all relevant information, including the

PIN numbers of other authorised signatories.

[8] ANZ by its statement of defence pleads, in addition to denial of liability, three affirmative defences:

- [a] It claims first that any liability it might have arising out of the operation of the electronic transaction system operated by Kembla is excluded by the terms of the contract between it and Kembla including Kembla's agreement to indemnify ANZ for any losses due to ANZ accepting in good faith an apparently authorised application except in the case of fraud by ANZ's employees. There is no suggestion of fraud on the part of ANZ or its employees.
- [b] It pleads that by reason of the contractual terms the plaintiff is estopped from claiming that the transactions authorised by Ms Chilcott were not valid requests.
- [c] It claims that any liability should be reduced or extinguished by reason of the contributory negligence or other fault of the plaintiff or its employees or agents.

[9] ANZ also pleads a set off in terms of its contract with the plaintiff by which the plaintiff undertook to indemnify ANZ against all losses, actions and claims.

[10] Against the defendants as collecting banks, Kembla claimed the amounts paid to each on three bases: as money had and received; in conversion; and for knowing receipt. The Master struck out the claims based upon money had and received and conversion. Since no appeal has been brought by Kembla against that determination these causes of action need not be considered further.

[11] The claim for knowing receipt is based upon the pleading that funds belonging to Kembla were received by the collecting banks:

in circumstances that an honest and reasonable banker in the stead of each of the defendants would have been put on enquiry that the funds so received by each of them did not properly belong to Ms Chilcott and/or her interests.

[12] By way of further particulars supplied at its request to ANZ (and reserving the right to reassess particulars in the light of discovery), Kembla indicated by letter of 15 June 1999 that:

- (i) The ANZ knew that in the period late 1991 to early February 1993 Ms Chilcott was in financial difficulties (Ms Chilcott was in receipt of a Department of Social Welfare benefit, her account was consistently in overdraft, and there were automatic payments to a debt collection agency);
- (ii) From early 1993 there was a noticeable change in the behaviour of Ms Chilcott's accounts as the monthly balances were in credit rather than debit and significant electronic deposits were made into Ms Chilcott's accounts which were clearly identified in the bank statements as originating from MM Kembla.

[13] Kembla claims for knowing receipt:

- [a] \$887,977.99 from ANZ as collecting bank;
- [b] \$684,802.45 from Westpac;
- [c] \$443,451.93 from BNZ;

together with interest and costs.

The summary judgment application

[14] The defendants applied for summary judgment against the plaintiff on the grounds that "none of the causes of action against them can succeed". The applications were opposed. The notice of opposition, in addition to asserting that the claims can succeed, claimed that discovery and other interlocutory proceedings were required to establish the facts and that expert evidence would be required as to whether the defendants acted as honest and reasonable bankers.

[15] The defendants filed affidavit evidence. The plaintiff filed affidavit evidence in reply. Further affidavit evidence in response was then filed by the defendants. None of the parties to the present appeal filed expert evidence concerning banking practice. We were advised that such evidence had been filed in relation to the third defendant, BNZ and that in consequence BNZ withdrew its application for summary judgment. The only applications for summary judgment to proceed to hearing before the Master were those made by ANZ and Westpac, the two appellants.

[16] For ANZ, affidavit evidence was provided by the Operating Loss Manager. He described the ANZ electronic transfer system used in the thefts from Kembla. Using PINs and passwords, authorised users effect the transactions without bank involvement. On the following day after each transaction is carried out, a report is automatically generated and sent to the person nominated by the customer to receive it so that the conditions of use can be checked by the customer. Under the Conditions of Use which govern the contractual arrangements between customer and bank, responsibility for ensuring that transactions are properly carried out “lies with the customer rather than ANZ, which is not in a position to check these matters”. The arrangements are the same where ANZ is both paying and collecting bank. Such transactions would not come to the attention of staff. It was said that it is not a viable option to provide that electronic payments cannot be made into the account of an authorised user of the system both for practical reasons and because payment of salaries (including to employees who are authorised users) is one of the most common uses of the electronic banking system. Progress in providing better security

depends upon banks not being potentially liable for unauthorised transactions carried out by authorised users who are given full authority to use the system by the customer”. ... If banks were to be held potentially liable for such abuse by authorised users, despite the deliberate breadth of the contractual liability-exclusion terms in place between ANZ and its customers, then the potential losses to banks in the future would be so great that it would not be a commercially viable (or even insurable) option to continue offering electronic banking services. The increase in account or transaction fees which would be necessary to provide for the increased financial risk would rule out continuation of electronic banking by ANZ in this country. (original emphasis)

[17] The affidavit annexed the applications for use completed on behalf of Kembla identifying Ms Chilcott as contact name and System Administrator for Kembla and her position as user. She accordingly received an ANZ user ID, user password, log on password, Racal unit, Racal watch word PIN, test challenge and test response.

[18] The documents for both the ANZCASH system and the ANZ Direct system which replaced it in 1995 were annexed to the affidavit on behalf of ANZ. The Conditions of Use for both limited ANZ’s liability. The ANZCASH application for

use contained an indemnity whereby Kembla agreed to indemnify the Bank:

from and against all actions and claims demands losses damages injury costs and expenses for which the Bank its employees agents and independent contractors shall or may become liable in respect of or arising directly or indirectly from or as a consequence of:

- (a) any use of ANZCASH (whether authorised or not) and any reliance on the information derived therefrom or any transactions effected thereby;
- (b) my/our inability to use ANZCASH at any time or for any reason.

[19] The ANZCASH Conditions of Use required the customer and each user to take all actions necessary to prevent unauthorised use of ANZCASH. The Customer and each user agreed to be responsible for any liability “incurred by it or by the Bank” on a full indemnity basis due to the unauthorised access to ANZCASH by any person “save and except for the fraud of the employees of the Bank”. The Customer acknowledged that any instructions made or purportedly made by it by use of ANZCASH would operate as a request to the Bank to act on the instructions and the Bank would not be responsible in respect of any unauthorised instructions.

[20] The documents relating to the new ANZ Direct, though in different form, were to similar effect. Kembla acknowledged that it would be responsible for any liability incurred by it or by the Bank on a full indemnity basis due to unauthorised access to ANZ Direct by any person by any means “except in the case of fraud by the Bank’s employees”. Kembla acknowledged that any application appearing to be made by it would operate as a request to the Bank to act on the application and that the Bank would not be responsible or liable for any loss by Kembla or any other party and would indemnify the Bank for any such loss due to “the Bank accepting in good faith an unauthorised Application . . . appearing to be authorised by me/us or any other person purporting to act on my/our behalf (except in the case of fraud by the Bank’s employees)...”.

[21] Westpac’s affidavit evidence dealt with the nine Westpac accounts detailed in the statement of claim as having received funds stolen from Kembla on behalf of Ms Chilcott or her associate. Six accounts were maintained until March 1996 at a

Papakura Branch of Westpac. They were closed in 1996 when three further accounts were opened at the Pukekohe branch. Westpac annexed copies of bank statements for all accounts. Its deponent, Ms Friedrich (at the relevant time the manager of the Pukekohe branch and now the manager of the Manukau branch) explained that, although a branch bank officer is “nominally” assigned to a retail account, bank statements are produced by computer centrally and do not require human intervention. The accounts are not reviewed unless bank officers are alerted to default or irregularity by computer generated warning or when the customer raises a query. Electronic deposits are not reviewed by a bank officer. The Westpac deponent confirmed that the electronic transfer system operated by Westpac is similar to that operated by ANZ and that in particular the branches do not track deposits made electronically into Westpac accounts. The history sheets maintained by the Bank record two housing loans and a business loan to the customers secured by mortgage and the declining of an application for further borrowing. A telegraphic transfer of money in December 1994 to a US bank at the request of Ms Chilcott was made to the wrong bank. Correspondence was returned at one stage and an updated address from the customers was sought. No other inquiries were noted and no review of the accounts was undertaken at any stage. Although the bank statements record some instances when the accounts were overdrawn and direct debits were automatically reversed by the computer system, no further action was taken by the bank officers. The direct debit reversals were made in respect of debits made by WestpacTrust Card Services to cover payments for credit card transactions.

[22] An affidavit by Mr Kelly, a manager of Kembla, deals with the question of Westpac’s knowledge. It refers to documents obtained by Kembla from the Serious Fraud Office following its investigation of Ms Chilcott. Westpac records of the loan applications made to it by Ms Chilcott and her partner show that, between the first loan approved in May 1994 and a second approved in March 1996, the assets of Ms Chilcott and her partner had increased by \$105,000 when their personal finance application form showed that they had a combined total gross monthly income of \$7,909. A further loan in May 1996 (when their combined gross monthly income was confirmed at \$7,910) took the borrowings at that date to \$230,000. A third loan, initially declined by Westpac for insufficient information, was approved in August 1996 after an interview. This material was not annexed to the Westpac affidavit.

The third loan took the borrowings from Westpac over six months to \$280,000. Also obtained by Kembla from the Serious Fraud Office were details about Ms Chilcott's credit cards indicating that over the period 12 February 1995 to 13 April 1997 Ms Chilcott charged a total of \$228,271.28 to her Westpac cards and made payments totalling \$209,044.30. During the period covered by the bank statements there are regular payments into Ms Chilcott's accounts from Kembla. Some total thousands of dollars in a single month. Ms Chilcott's salary, also credited to a Westpac account, is separately identified in the bank statements.

[23] A further affidavit by Mr Kelly for Kembla responded to the ANZ affidavit. It annexes material obtained from the Serious Fraud Office (not attached to ANZ's affidavit) suggesting that the user ID and passwords for another user were sent to Ms Chilcott by ANZ. He expresses the view that the security precautions described by ANZ "broke down in this case because the ANZ sent to Ms Chilcott, as the system administrator, the PIN number and other authorised user information for another MM Kembla employee". The affidavit raises questions about ANZ's apparent failure to require receipts for the information and deposes to a similar delivery of another user's PIN to Mr Kelly, when he became the System Administrator. In another affidavit he detailed his own experience of ANZ seeking further authority when a batch limit was exceeded in challenging the claim by ANZ that intervention by the Bank in respect of electronic transfers is not practicable.

[24] Kembla filed an affidavit by a licensed private investigator who had investigated the frauds for Kembla. He deposed to his examination of accounts which revealed that Ms Chilcott and her partner regularly transferred funds from their other accounts (with Westpac, ANZ, BNZ and ASB Bank) to an account maintained with Westpac's Pukekohe Branch in the name of Jekka Toys Limited, a company owned by Ms Chilcott and her partner. He concluded that significant sums of money were applied by Ms Chilcott to the three toy shop businesses operated by Jekka Toys Limited. He also said that Ms Chilcott had a close association with an employee of the Westpac Pukekohe Branch who later was employed as a manager by Jekka Toys.

[25] ANZ responded to the affidavit of Mr Kelly by a further affidavit which

pointed out that the Conditions of Use and the Application for Use required the Bank to deliver documents containing information relating to the use of the electronic transfer system to the System Administrator nominated by the customer. The Conditions of Use provided that:

By acting in the manner described, the Bank shall have discharged any duty of care it may owe to me/us as to the confidentiality of the ANZ Direct Information.

[26] ANZ's evidence claims there was no "breakdown" in delivering the PIN and passwords to Ms Chilcott. ANZ complied with the directions given to it by Kembla. The loss is said to have been caused by Kembla's failure to appoint a trustworthy System Administrator "and an absence of any effective internal safeguards or checks within the plaintiff company".

[27] Westpac filed a further affidavit in reply dealing with the loans made to Ms Chilcott and her partner and Ms Chilcott's credit card use. The deponent, Ms Friedrich, explains the making of the loans by reference to the security provided, the borrowers' income and the normal lending criteria applied by Westpac. Ms Chilcott would have qualified for credit cards under the normal criteria operated by WestpacTrust. The statements are electronically generated and would not have been reviewed by the customer's branch or reviewed by WestpacTrust or Card Services "in the ordinary course". The affidavit also dealt with the relationship between Ms Chilcott and the Westpac employee at the Pukekohe Branch. Ms Friedrich deposed that the friend had access to Westpac's computer system but was not authorised to handle significant customer transactions. She did not have anything to do with the loans to Ms Chilcott.

The judgment in the High Court: the claim against ANZ as paying bank

[28] The Master declined to strike out the claim against ANZ as paying bank. As already mentioned, there is no appeal against the strike out decisions. Rather, the appeal is against the refusals to grant summary judgment.

[29] ANZ argued in support of its application for summary judgment that the

terms of the contract established by the evidence precluded any liability on the part of ANZ. The Master considered that submission upon two bases:

- [a] the duty of care generally pleaded in the statement of claim to advise the plaintiff that there was a real possibility that Ms Chilcott was defrauding Kembla “provided a reasonable and honest banker in the stead of the first defendant would have considered there to be such a possibility”;
- [b] the allegation in the affidavits (not carried through to the pleadings) of a duty of care owed by ANZ to Kembla in the manner of delivery of the intercepted PIN and passwords.

[30] On the first basis of liability, the Master accepted that the contract did not expressly impose a duty of care to advise that there was a real possibility that Ms Chilcott was defrauding the plaintiff. But he considered that an implied duty in such terms “provided a reasonable and honest banker in the stead of the first defendant would have considered there to be such a real possibility” would not be inconsistent with either the express terms of the contract or the contract as a whole:

To impose a duty on the first defendant to advise the plaintiff of a risk of fraud where “a reasonable and honest banker” would have considered there was such a risk is not, in my view, inconsistent with the purpose and structure of electronic funds transfer systems such as ANZCASH and ANZ Direct. It does not detract from the primary responsibility of the customer to ensure the integrity of the system. It does no more than say that, if the paying bank becomes aware of any facts which would cause a reasonable and honest bank in its position to draw those facts to the customer’s attention, then the paying bank has a duty to do so.

[31] On the basis of the evidence filed the Master was not satisfied by ANZ that the plaintiff could not succeed on its cause of action: “the cause of action is arguable”.

[32] To the extent that the plaintiff relied upon a tortious duty of care the Master held:

- [a] There is no absolute bar to the imposing of a tortious duty of care on parties to a contract.
- [b] In judging whether a tortious duty of care should be imposed regard must obviously be had to the terms of the contract

between the parties.

[c] The duty alleged is not inconsistent with those contractual provisions [for the reasons earlier given].

[d] In the light of these findings, the cause of action is arguable.

[33] The Master found that if the allegations in the affidavits that ANZ were in breach of a duty of care in relation to the delivery of the PIN and passwords, the existence of such a duty was not excluded by the Conditions of Use:

[a] The terms of the Conditions of Use are capable of the interpretation that they apply to the initial supply of system information (including User numbers and passwords). (Although it must be noted that the same form was used more than once during the period when the plaintiff was using the ANZCASH system.).

[b] The duty is not excluded by the plaintiff's authorisation of Ms Chilcott as Systems Administrator:

the fact that the first defendant was obliged to act on the nomination of a new user by the Nominated Officer or System Administrator does not mean that the first defendant was obliged to deliver Ms Wallace's user PIN and password to Ms Chilcott rather than to Ms Wallace personally.

[c] It is arguable that the clauses relied upon by ANZ which impose responsibility upon the customer are directed to "external security" ("security vis-à-vis persons not authorised to use the system, rather than to misconduct by persons authorised to use the system").

[34] The Master found that the allegation was therefore arguable as a matter of implied contractual term or in tort. Further, the evidence adduced did not permit the Master to resolve the argument by granting summary judgment to the defendant:

So far as the facts are concerned, the evidence adduced by the parties is limited to the nature of electronic funds transfer systems, the contractual arrangements between the parties and the involvement of Ms Chilcott. Neither party has called expert evidence as to whether there were features which would have caused a reasonable and honest banker in the place of the first defendant to have considered that there was a real possibility Ms Chilcott was defrauding the plaintiff. Nor has either party called evidence as to the reasonableness or otherwise, in the context of the ANZCASH and ANZ Direct systems, of the first defendant delivering the User

and Racial PINs and passwords of a user other than the System Administrator himself or herself to the System Administrator. Given the limitations of the evidence, I hold that the first defendant is not entitled to summary judgment against the plaintiff on the plaintiff's cause of action against it as paying bank.

The judgment in the High Court: the claim against ANZ and Westpac as collecting banks on the basis of knowing receipt

[35] On the "limited evidence" the Master was not prepared to make a finding "one way or another" on the issue of knowing receipt.

[36] Westpac had also argued that, apart from the question of knowledge of Ms Chilcott's fraud, it had not beneficially received any funds by acting as a collecting bank. The Master considered that on the evidence he could not be satisfied that the plaintiff could not succeed:

I am not satisfied that I have sufficient evidence before me to enable me safely to determine the application of the principles in those cases to the question of whether there was beneficial receipt in this case. I think the issue should go to trial.

The appeal

[37] Both ANZ and Westpac appeal the refusal of the Master to enter summary judgment on their applications. They criticise the approach adopted by the Master to the summary judgment jurisdiction. ANZ contends that the Master erred in considering a cause of action not pleaded by Kembla (breach of duty of care in the delivery of user information), but available on its evidence if the pleadings are amended. ANZ submits that on the evidence the plaintiff could not succeed on the claim against it as paying bank because the duties of care pleaded or available on the evidence if the pleadings were amended were excluded by the contract between the parties. Both defendants submit that the claim based upon knowing receipt by each of them as collecting banks could not succeed because the evidence (upon which it is said there was in fact no "conflict of evidence" as the Master thought) does not disclose beneficial receipt and does not disclose their knowledge that the funds

deposited with them were obtained in breach of trust by Ms Chilcott. The Master failed to assess the credibility and weight of the evidence and failed to apply the correct test: “whether the plaintiff has a seriously arguable claim against [the defendants] for knowing receipt”. In addition ANZ submits that by the terms of the contract between it and Kembla any liability it may have had for knowing receipt is excluded. Both defendants contend that summary judgment should have been entered on their applications because none of the causes of action in the plaintiff’s statement of claim can succeed.

Breach of duty of care in the delivery of user PINs and passwords

[38] The statement of claim upon which the summary judgment application was heard did not plead a cause of action relating to negligent delivery of the user information to Kembla by ANZ. Counsel for ANZ submit that the Master erred in considering a cause of action not pleaded by Kembla on the basis of reference to it in the evidence. At the appeal we were advised that an amended statement of claim now pleads the additional cause of action. But Mr Finlayson submits that on its summary judgment application the defendant was entitled to proceed on the basis of the pleadings as at the time of the hearing. Rule 136(2) requires the defendant to satisfy the court that “none of the causes of action in the plaintiff’s statement of claim can succeed”. The focus is thus on the claim “as pleaded”. The Master had acknowledged that the allegation in the affidavits was “not carried through to the pleadings”. Although ANZ had notice of the claim in the evidence filed by Kembla, Mr Finlayson submitted that “a defendant cannot be expected to search through the plaintiff’s evidence for possible implied causes of action”:

Rule 136(2) does not require a defendant to go beyond satisfying the Court that “none of the causes of action in the plaintiff’s statement of claim can succeed”. If the drafters of the High Court Rules had intended otherwise, they could have phrased the rule so as not to refer to the statement of claim. To require a defendant to look for implied causes of action would have the effect of deterring defendant’s summary judgment applications because of the uncertainty that would be involved.

[39] It is submitted on behalf of ANZ that summary judgment application is different from strike out applications where the Court will “almost invariably” allow

amendment to pleadings. The submission is acknowledged to be contrary to the view expressed by Master Thomson in *Eatwell Livestock Ltd v Bank of New Zealand* (2000) 13 PRNZ 671. But it is contended that, because affidavit evidence is filed by the defendant to refute the claim as pleaded, amendment prejudices a defendant whose evidence will be filed before the potential claim is identified in the plaintiff's affidavit evidence in reply.

[40] On behalf of Kembla, Mr Macdonald points out that the “unpleaded allegation” concerning the provision of the user identification information was argued at the hearing before the Master without objection. It was not suggested that ANZ was prejudiced in any way. Because no objection was taken, no formal amendment was sought at the hearing. The allegation is now incorporated in the amended statement of claim which has been filed.

Breach of duty of care of ANZ as paying bank

[41] ANZ submits that it adduced sufficient evidence to have shifted the evidential onus to Kembla to demonstrate negligence on the part of ANZ “such as to prevent the ANZ from relying on the exclusion of liability and indemnity clauses in the ANZCASH and ANZ Direct conditions of use”. No such evidence, it is suggested, was put forward by Kembla at the time of the summary judgment application.

[42] It is contended that the Master failed to assess the evidence. If properly considered, the claim could not succeed because:

[a] There is no express contractual duty of care.

[b] No duties of care to advise Kembla that there was a real possibility that Kembla was being defrauded by Ms Chilcott or (if the pleadings were amended) in respect of the delivery of user information can be implied, following the test adopted in *BP Refinery (Westernport) Pty v Shire of Hastings* (1977) 16 ALR 363, 376. In particular, the alleged duties of care are inconsistent with the terms of the contract which exclude

liability by ANZ.

- [c] The indemnities pleaded as an affirmative defence by way of set off are an entire answer to the claim.
- [d] No tortious duty may be imposed to overcome a contractual exclusion clause (*Henderson v Merrett Syndicates* [1995] 2 AC 145, 194 per Lord Goff). The clauses excluding ANZ's liability prevent the imposition of a duty of care.
- [e] If a tortious claim is available, that pleaded amounts to a claim for negligent misstatement by omission causing economic loss. Kembla has not adduced evidence of assumption of responsibility by the defendant, reliance upon the advice or that such reliance was reasonably foreseeable (*Fleming v Securities Commission* [1995] 2 NZLR 514; *White v Jones* [1995] 2 AC 207, 274; *Brownie Wills v Shrimpton* [1998] 2 NZLR 320, 324). It is not sufficient for a plaintiff faced with a summary judgment application to say that more evidence will be available at trial; it must put up sufficient evidence to discharge the evidential onus "now" (*Pizza Pizza Ltd v Gillespie* (1990) 45 CPC (2d) 168).

[43] On behalf of Kembla, Mr Macdonald argues that the contractual provisions relied upon by ANZ, as clauses which exclude liability, must be clearly and unambiguously applicable and construed contra proferentem. He contends they must be fairly drawn to the attention of the other party to be part of the contract (*Livingstone v Roskilly* [1992] 3 NZLR 230 per Thomas J). And there is a presumption that such clauses are not to be construed to afford protection against the indemnified person's own negligence without clear words (*Smith v South Wales Switchgear Ltd* [1978] 1 All ER 18, [1978] 1 WLR 165 (HL); *E E Caledonia Ltd v Orbit Valve Co Europe* [1993] 4 All ER 165).

[44] Since none of the provisions relied upon by ANZ expressly exclude liability for ANZ's negligence or indemnify ANZ for liability arising out of such negligence,

Kembla maintains ANZ cannot exclude the plaintiff's claim on summary application.

[45] In addition to these contentions, Mr Macdonald argues in relation to the unpleaded claim that the conditions must be read in context. Since the operation of the system depended upon what ANZ has described as rigid security and since the conditions are predicated upon the user password being known only to the authorised user and ANZ, disclosure of the user PIN of another person to Ms Chilcott had the potential to defeat the security of the system. In those circumstances the exclusion clause could not be construed to exclude liability for breach of a duty of care in the disclosure. The clause is, moreover, (as the Master held) capable of the interpretation that it applied to the initial supply of systems information only. The Master was correct to hold that nothing in the conditions obliged ANZ to deliver the PIN to Ms Chilcott rather than the designated user. In addition, the Master was correct to hold that it was arguable that the obligations imposed upon the customer under the conditions are directed to external security matters and do not apply to the present case.

Knowing receipt

[46] Both appellants contend that the pleadings and evidence are insufficient foundation for a tenable claim based on knowing receipt. The knowledge alleged is insufficient for liability. And the facts do not disclose any sufficient benefit to the collecting banks in the receipt of the funds obtained by Ms Chilcott's fraud.

[47] Both appellants acknowledge that the extent of knowledge required to make a bank a constructive trustee is not settled on the authorities. They submit that New Zealand authorities such as *Westpac Banking v Savin* [1985] 2 NZLR 41, *Powell v Thompson* [1991] 1 NZLR 597 and *Equiticorp Industries Ltd v Hawkins* [1991] 3 NZLR 700 may require reassessment in the light of English authorities such as *Agip (Africa) Ltd v Jackson* [1990] Ch 265 and *Westdeutsche Bank v Islington* [1996] AC 669. But in any event they contend that the knowledge pleaded by Kembla amounts to knowledge to be imputed from negligence only, equivalent to that proposed in the fourth and fifth categories identified by Peter Gibson J in *Baden v Societe Generale pour Favoriser le Developpement du Commerce et de l'Industrie en France SA*

[1992] 4 All ER 161.

[48] The appellants take different lines on this issue. ANZ maintains that the knowledge pleaded by Kembla is insufficient as a matter of law and that the plaintiff's claim is untenable. Westpac was content to accept for the purposes of summary judgment that the basis for imputed knowledge pleaded is sufficient but argued that the evidence does not bring Westpac within it.

[49] ANZ submits that no New Zealand case has imposed liability in trust upon the basis alleged in the statement of claim that the funds were received "in circumstances that an honest and reasonable banker in the stead of each of the defendants would have been put on enquiry that the funds so received by each of them did not properly belong to Ms Chilcott and/or her interests". Those cases where banks have been held liable as constructive trustees have arisen where the banks have known of the fiduciary capacity in which their customer dealt with funds banked to its account (see, for example, *Westpac v Savin*; *Westpac Banking Corporation v Ancell* (1993) 4 NZBLC 103,259). The knowledge alleged here, it is submitted, is insufficient for liability.

[50] Both appellants also maintain that, irrespective of the proper standard of knowledge, there is no evidence upon which it could be argued that they fell even within the fourth and fifth categories identified in the *Baden* case. Mr Miller for Westpac submits that the question for the Master was whether he could be satisfied "on the evidence that, at least arguably, a reasonable and honest banker in Westpac's position would at the time (and not with the benefit of hindsight) have been put on inquiry as to the source of the funds in the accounts". He suggests that the starting point, in reliance upon *Westpac v Savin*, is that "in ordinary circumstances banks need not inquire into the source of funds paid by customers into their accounts". He acknowledges that the Court must look at all the circumstances at the time of the acts complained of. Here there were no circumstances to put the Bank on notice:

[a] Bank personnel do not have cause to peruse the transaction history of particular accounts, including the volume of transactions and source of funds. The Bank's computer alerts

it only if the account goes into overdraft or exceeds any agreed overdraft level.

- [b] The banking transactions were electronic. It is standard Westpac practice that checks are not made and Kembla has not presented any expert evidence to suggest that such inquiries would be feasible or would be considered normal and prudent banking practice.
- [c] The loans were in accordance with the Bank's lending practices.
- [d] Ms Chilcott's credit card transactions would not normally come to the attention of the Bank.
- [e] The evidence about Ms Chilcott's friendship with a member of Westpac's staff is speculative and in any event any knowledge of the friend could not be imputed to Westpac.

[51] Mr Miller submitted that, contrary to the suggestion of the Master, there is no dispute in relation to material facts:

There is no evidence to contradict that of Westpac in relation to the operation of the accounts. Kembla has had the opportunity to file such evidence. It has had access to all bank documents relevant to its claim, but has not pleaded one act or omission on the part of the bank as a basis for that claim. It has had the opportunity to file expert evidence, but has not done so.

[52] In the absence of credible evidence to the contrary, the appellants submit that the Court may infer that their conduct was consistent with the accepted practice of careful bankers.

[53] Even if the question of knowledge cannot be conclusively resolved on the summary judgment application, the appellants argue that there is no evidence of sufficient beneficial receipt of the funds collected to justify imposition of a constructive trust. (Without such receipt, liability could only arise in knowing assistance for which dishonesty on the part of the Bank would be required and which

is not suggested here.) Mr Miller (who carried the burden of the argument for both appellants on this point) submitted that, where a bank credits a customer's account with funds and the account is in credit, the funds are not received for the benefit of the bank. Even where an account is in overdraft, he submits that it is doubtful whether receipt will amount to beneficial receipt. On the evidence, some accounts did become overdrawn from time to time but the overdrawings were always cleared within a few days without the necessity for the Bank to take action. In many cases when an account was in overdraft, Ms Chilcott was in credit in another account. Therefore, he submits, the case is to be contrasted with *Westpac v Savin*, *Westpac v Ancell* and other New Zealand authorities where the banks were pressing for reduction of a customer's debt and consciously applied the funds received in reduction of it.

[54] In addition to the contentions common to both appellants, ANZ maintain that, even if liable in constructive trust, the indemnity contained in the contract with Kembla is not restricted to its conduct as a paying bank and is a "complete answer" to the claim. Counsel did not cite authority in support of this bald assertion.

[55] Mr Macdonald, for Kembla, argues in response to Westpac on the knowing receipt argument that the Master was correct not to embark on a detailed inquiry into the issue of whether the Bank had constructive knowledge of the breach of trust. It could not be resolved on summary judgment. The factual issues known to the plaintiff before discovery include:

- [a] Deposits totalling \$584,802.45 into 9 accounts over a period of 4½ years;
- [b] Credit card activity totalling approximately \$300,000 between December 1993 and April 1997;
- [c] Borrowings totalling \$280,000 between March and August 1996; and
- [d] Ms Chilcott's relationship with an employee of Westpac.

[56] Kembla does not accept that the affidavits filed by the banks disclose all

records. It requires discovery.

[57] Mr Macdonald argues that on the knowing receipt cause of action the question of constructive knowledge cannot be divorced from the standard of compliance with banking practice. It is for the defendants seeking summary judgment to exclude an arguable case. Westpac has not sought to lead expert evidence of banking practice but has relied on the evidence of its Pukekohe branch manager as to Westpac's practice. ANZ similarly did not put forward expert evidence but rather described its own procedures. Such evidence (which included opinion evidence) was, it is submitted, inadequate to discharge the burden on a defendant bank seeking summary judgment.

Decision

[58] The applications for summary judgment were made under Rule 136(2) of the High Court Rules which permits the Court to give judgment against the plaintiff "if the defendant satisfies the Court that none of the causes of action in the plaintiff's statement of claim can succeed".

[59] Since Rule 136(2) permits summary judgment only where a defendant satisfies the Court that the plaintiff cannot succeed on any of its causes of action, the procedure is not directly equivalent to the plaintiff's summary judgment provided by Rule 136(1).

[60] Where a claim is untenable on the pleadings as a matter of law, it will not usually be necessary to have recourse to the summary judgment procedure because a defendant can apply to strike out the claim under Rule 186. Rather Rule 136(2) permits a defendant who has a clear answer to the plaintiff which cannot be contradicted to put up the evidence which constitutes the answer so that the proceedings can be summarily dismissed. The difference between an application to strike out the claim and summary judgment is that strike out is usually determined on the pleadings alone whereas summary judgment requires evidence. Summary judgment is a judgment between the parties on the dispute which operates as issue estoppel, whereas if a pleading is struck out as untenable as a matter of law the

plaintiff is not precluded from bringing a further properly constituted claim.

[61] The defendant has the onus of proving on the balance of probabilities that the plaintiff cannot succeed. Usually summary judgment for a defendant will arise where the defendant can offer evidence which is a complete defence to the plaintiff's claim. Examples, cited in *McGechan on Procedure* at HR 136.09A, are where the wrong party has proceeded or where the claim is clearly met by qualified privilege.

[62] Application for summary judgment will be inappropriate where there are disputed issues of material fact or where material facts need to be ascertained by the Court and cannot confidently be concluded from affidavits. It may also be inappropriate where ultimate determination turns on a judgment only able to be properly arrived at after a full hearing of the evidence. Summary judgment is suitable for cases where abbreviated procedure and affidavit evidence will sufficiently expose the facts and the legal issues. Although a legal point may be as well decided on summary judgment application as at trial if sufficiently clear (*Pemberton v Chappell* [1987] 1 NZLR 1), novel or developing points of law may require the context provided by trial to provide the Court with sufficient perspective.

[63] Except in clear cases, such as a claim upon a simple debt where it is reasonable to expect proof to be immediately available, it will not be appropriate to decide by summary procedure the sufficiency of the proof of the plaintiff's claim. That would permit a defendant, perhaps more in possession of the facts than the plaintiff (as is not uncommon where a plaintiff is the victim of deceit), to force on the plaintiff's case prematurely before completion of discovery or other interlocutory steps and before the plaintiff's evidence can reasonably be assembled.

[64] The defendant bears the onus of satisfying the Court that none of the claims can succeed. It is not necessary for the plaintiff to put up evidence at all although, if the defendant supplies evidence which would satisfy the Court that the claim cannot succeed, a plaintiff will usually have to respond with credible evidence of its own. Even then it is perhaps unhelpful to describe the effect as one where an onus is transferred. At the end of the day, the Court must be satisfied that none of the claims can succeed. It is not enough that they are shown to have weaknesses. The

assessment made by the Court on interlocutory application is not one to be arrived at on a fine balance of the available evidence, such as is appropriate at trial.

[65] Applying these general principles, we are of the view that it was appropriate for the Master to consider the evidence as to delivery of the PIN and passwords even though negligence in such delivery was not distinctly pleaded. The starting point is Rule 187 which permits a party “at any time before trial” to file an amended pleading. Leave of the Court is required after a proceeding has been set down for trial. But no such leave is necessary before then.

[66] Although Rule 136 refers to the causes of action “in the plaintiff’s statement of claim”, Rule 186 (which permits the Court to strike out a cause of action) similarly is based upon “the pleading”. Under Rule 186 the Court does not strike out pleadings where a defect can be cured by amendment which the party is willing to make. Similarly, the residual discretion of the Court under Rule 136 to refuse summary judgment would be properly invoked to avoid the oppression which would otherwise result if an application by a defendant for summary judgment would preempt a plaintiff exercising the right to amend the pleadings in terms of Rule 187. Indeed, use of the discretion to enable amendment is arguably more necessary in the interests of justice in the case of summary judgment than in the case of strike out because summary judgment results in issue estoppel.

[67] The Master did not need to decline summary judgment on this ground, since he was of the view that Westpac had not discharged the burden of showing that the plaintiff could not succeed on the other causes of action (and it is necessary under Rule 136 to show that no cause of action could succeed). But had it been necessary for him to do so, we are of the view that it would have been open to the Master to refuse summary judgment on the ground that an amendment to the statement of claim which the plaintiff was prepared to make raised a cause of action upon which he was not satisfied the plaintiff could not succeed.

[68] The wording of Rule 136 is consistent with the wording of Rule 186 and is subject to the same residual discretion to avoid oppression. Such an approach ensures that the plaintiff is not deprived of the benefit of the power to amend in Rule

187. Any real prejudice to a defendant through surprise can be adequately met by allowing him time to respond to the evidence. Mr Finlayson did not suggest that there were any such difficulties in the present case. The suggestion that the risk of precipitating an amendment will deter defendants from applying for summary judgment (referred to by Mr Finlayson in the argument set out in para [38] above) is not persuasive. Summary judgment should not be applied for by plaintiff or defendant unless the substantive merits of the case are clear and capable of summary disposal. If defendants are discouraged from applying for summary judgment opportunistically when correctable error by the plaintiff is identified, that seems to us a result which serves the ends identified by Rule 4 of just, speedy and inexpensive determination of proceedings and interlocutory applications.

[69] The claims that ANZ breached duties of care to advise Kembla of the risk that Kembla was being defrauded by Ms Chilcott and in the delivery of the user PIN and passwords are put forward alternatively in contract (by implied term) and in tort (in which case the scope of the contractual obligation and any limitation of it is critical). On both bases therefore, construction of the contract entered into between the parties is necessary. The key clauses relied upon by ANZ are the clauses which exclude its liability and which require Kembla to indemnify it for loss. These exclusion clauses fall to be construed *contra proferentem* (*Smith v South Wales Switchgear Ltd* [1978] 1 All ER 18, [1978] 1 WLR 165). An exclusion clause apt to exclude other liability and not expressly referring to negligence may be held not to exclude liability for negligence (*White v John Warrick & Co Ltd* [1953] 2 All ER 1021, [1953] 1 WLR 1285; *Producer Meats Ltd v Thomas Borthwick & Sons Ltd* [1964] NZLR 700). Whether the clauses relied upon by ANZ are effective to exclude liability for any negligence of ANZ to Kembla (assessed by the standard of care of the reasonable and honest banker), or whether they require Kembla to indemnify ANZ for ANZ's liability for such negligence to Kembla, depend upon the expectations of the parties as objectively assessed from the terms of the agreement, its purpose, and the factual setting as it existed at the time (*Vickery v Waitaki International Ltd* [1992] 2 NZLR 58).

[70] As the Master held, the express terms of the contract do not clearly exclude ANZ's liability for its own negligence to Kembla in failing to warn Kembla if an

honest and reasonable banker in its position would have appreciated the risk that Kembla was being defrauded. The exclusion of liability is concerned with liability arising from unauthorised applications, not failure to warn in circumstances where an honest and reasonable Bank would have been alerted to systematic fraud. Nor do they unambiguously exclude liability for negligence in providing information essential to the security of the electronic funds transfer system in a way which undermines the security of the arrangement. ANZ was not explicitly obliged by the obligations entered into to supply the PIN and passwords for another user to Ms Chilcott as System Administrator, rather than to the user. On the plaintiff's contentions, loss arose through ANZ's breach of a duty of care which preceded the applications and set up the conditions in which the system was insecure and vulnerable.

[71] The proper construction of the contractual exclusion clauses requires consideration of the surrounding facts inappropriate for determination on summary application. If they do not exclude liability for negligence, then we agree with the conclusion of the Master that the scope of the duty of care and whether ANZ has properly discharged it are questions which may well require evidence of banking practice. It is not good enough for ANZ to say that the plaintiff should have put such evidence forward at this stage. It is for the defendant to satisfy the Court that the claim cannot succeed. In the absence of evidence put forward by ANZ that its conduct conformed with banking practice, the Court on summary application is not able to judge the matter.

[72] Nor do we accept the argument advanced by Mr Finlayson that Kembla has failed to adduce evidence of reliance upon the advice of ANZ. Given the relationship between the parties and ANZ's supply of the system of electronic transfer of funds to its customers, the defendant on summary application has not in our view excluded the reasonable prospect that Kembla may succeed in establishing such reliance, assuming such reliance to be necessary to the claim (a matter upon which we do not find it necessary to express any view).

[73] Mr Finlayson in argument placed considerable reliance upon the Canadian decision in *Pizza Pizza Ltd v Gillespie* (1990) 45 CPC (2d) 168, a decision of the

Ontario Court of Justice based upon Rule 20 of the Ontario Rules of Civil Procedure. The Ontario Rules differ significantly from Rule 136. A party applying for summary judgment does not have the onus of satisfying the Court. A responding party “may not rest on the mere allegations or denials of his or her pleadings, but must set out, in affidavit material or other evidence, specific facts showing that there is a genuine issue for trial”. Given the difference in the Rules, the assistance to be obtained from the Canadian approach is limited. It is not appropriate in New Zealand to regard the occasion for the plaintiff to put up proof as being the summary judgment application. If the claim is shown by the defendant to be patently devoid of merit, then, in the absence of challenge by the plaintiff’s evidence of the evidence relied upon by the defendant, summary judgment will be appropriate. But where, even adopting the “robust” approach required by the New Zealand decisions, the case on the evidence available cannot be dismissed as without realistic prospect of success, summary judgment is not appropriate.

[74] We are in agreement with the Master that the cause of action is arguable and that summary judgment on the application of ANZ in respect of its liability for negligence as paying bank was properly declined.

[75] There is much force in the attractive arguments advanced in particular by Mr Miller as to the beneficial interest in collection which is required before a collecting bank can be held to have “received” funds for the purposes of liability for knowing receipt and the knowledge to be imputed to a collecting bank. Ross Cranston in *Principles of Banking Law* (1997, Clarendon) 207, expresses the view that “the law on whether a bank has received funds beneficially is hopelessly confused and sits ill with legal principle and banking practice”. The cases which have so far risen for consideration in New Zealand are ones where the collecting bank has applied the funds to reduce the customer’s indebtedness to the bank (see, for example, *Westpac v Savin*, although it may be noted that the High Court of Australia has doubted that reduction of a customer’s overdraft is necessarily a benefit obtained by the bank (*Australia and New Zealand Banking Group Ltd v Westpac Banking Corporation* (1988) 164 CLR 662, 681)). Even assuming that the bank did not receive such direct benefit here (and, as indicated below, it is impossible to be confident on the facts as available on summary judgment that is the case), it does not

follow that a receiving bank gains no relevant benefit. The matter has not yet risen squarely for determination in New Zealand. Policy considerations, such as are identified in *Agip (Africa) Ltd v Jackson & Ors* [1992] 4 All ER 385, 404, [1990] Ch 265, 292 will need to be weighed. As will questions of fact concerning the benefits derived by banks from trading operations. The defendants may well be correct that the imposition of liability on a collecting bank will depend upon whether there is some “conscious appropriation”, as Sir Peter Millett suggested in “Tracing the Proceeds of Fraud” (1991) 107 *Law Quarterly Review* 71, 83. On that view, the mere continuation of a running account in overdraft would not be sufficient to make the bank liable without such “conscious appropriation”. A similar suggestion that the liability of banks should be limited to situations of “real benefit” to it, is suggested by Cranston (at 208). Cranston acknowledges that the suggestion does not accord with principle (because the bank receives money as its own and not as agent) but says that it is necessary to bring the law into conformity with banking practice.

[76] This area of law is marked by present confusion. Clarification is not responsibly undertaken on facts put forward in abbreviated form and without discovery. It is to be expected that expert evidence of banking practice will be important if the Court is to be invited to consider the scope of imposition of constructive trust for knowing receipt on the basis that the law should conform with banking practice. It would not be warranted to accept the defendant’s assertions of commercial damage, should the liability of banks be extended by enlargement of concepts of beneficial receipt, without such evidence.

[77] On the facts as presently disclosed, it is not possible to be clear what benefit the banks obtained. The accounts did at times go into overdraft. And in the case of Westpac substantial funds were received to clear credit card indebtedness. Without formal discovery and more analysis than has been provided on the summary judgment application, it is not possible to be confident of the extent to which the banks benefited.

[78] Similarly, if the Court is to be asked to review the circumstances in which knowledge sufficient to attach liability to a receiving bank is to be imputed, a factual basis for the appellants’ claims that the bank cannot be expected to review customer

accounts for patterns which suggest fraud and that such review is not reasonably feasible under electronic transfer systems needs to be addressed by evidence of banking practice. It is not enough for the defendants to describe their own practice. The assertions that banks should not have imposed on them a duty to note suspicious dealings with accounts and cannot reasonably set up systems to check for such suspicious dealings may need to be considered in the light of the statutory obligations imposed by the Financial Transactions Reporting Act 1996. It is necessary for the facts as to the operation of the accounts to be fully ventilated after discovery has been obtained by the plaintiff. It is a relevant factor that the operation of the accounts is a matter within the knowledge of the defendant banks.

Conclusion

[79] For the reasons given, we are of the view that summary judgment was properly declined by the Master. The Master was correct to deal with the foreshadowed claim against ANZ in negligence: to permit amendment to the pleadings is consistent with the Rules and the interests of justice. The claims in negligence and for the knowing receipt are so inherently dependent on evidence and full legal argument based upon such evidence relating to complex and uncertain questions of law that we do not consider an application under Rule 136(2) was at all appropriate. The case was not suitable for summary determination. The appeals are dismissed. The respondent is entitled to costs of \$2,500 from each appellant, together with reasonable disbursements to be fixed by the Registrar and to be paid as to one-half by each appellant.

Solicitors:

Chapman Tripp Sheffield Young, Wellington for Westpac
Bell Gully Buddle Weir, Wellington for ANZ Bank
Phillips Fox, Auckland for Kembla