Bond Law Review

Volume 17 | Issue 2 Article 3

12-1-2005

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Robin Edwards
Monash University

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Recommended Citation
Edwards, Robin (2005) "Exclusion of Cardholder Chargeback Rights," *Bond Law Review*: Vol. 17: Iss. 2, Article 3.
Available at: http://epublications.bond.edu.au/blr/vol17/iss2/3

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Abstract
Cardholder chargeback rights have entered Australia through the back door via credit card scheme operating rules that reflect American legislation. These valuable cardholder rights are now legally recognized by the Australian Code of Banking Practice and Electronic Funds Transfer Code. But can these rights be excluded by the merchant in his contract with the cardholder?

Keywords
credit cards, chargeback rights, exclusion, Australian Code of Banking Practice, Electronic Funds Transfer Code

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EXCLUSION OF CARDHOLDER CHARGEBACK RIGHTS

By Robin Edwards[*]

Cardholder chargeback rights have entered Australia through the back door via credit card scheme operating rules that reflect American legislation. These valuable cardholder rights are now legally recognized by the Australian Code of Banking Practice and Electronic Funds Transfer Code. But can these rights be excluded by the merchant in his contract with the cardholder?

Introduction

A chargeback usually occurs when a buyer asks their bank who has issued a credit card to them to remove a charge from their credit card statement. The issuing bank will ask the buyer to provide an explanation about why they are disputing the charge.

Two common reasons for reversals or chargebacks are:

- A buyer's credit card number is used fraudulently over the phone or on the internet. (The card and cardholder are not present at the time of the transaction.)

- A buyer makes a purchase, but believes that the seller has not fulfilled the terms of the contract; for example, the seller has not shipped goods that comply with the description or the goods are not of merchantable quality. (If it is a point of sale transaction the card and cardholder are present at the point of sale and the cardholder signs the transaction slip. But equally such a dispute might involve mail order or phone or internet using the credit card number where the card and cardholder are not present at the time of the transaction.)

But is it possible in Australia for the vendor to exclude chargeback rights that are conferred in Australia by the Electronic Funds Transfer Code (the EFT code) and the Code of Banking Practice? The following are two different terms of dealing on the

* Associate Professor, Department of Business Law & Tax, Faculty of Business & Economics, Monash University.

internet by US merchants that purport to take away the cardholder's rights to chargeback.[1]

- Payments Buyers who purchase via credit card agree, accept, and understand, irrevocably and without exception and without recourse, to waive all actions, rights, claims, or relationships of agency to any chargeback and/or disputed payment procedure or refund, invoked personally and/or invoked by any financial, banking, and/or any credit card institution personally and/or on your behalf with respect to any purchase initiated at this Web site. As a fair and equitable alternative, you elect any conflict of payment as it relates to goods and/or services purchased via credit card at this Web site be bindingly arbitrated, irrevocably, without exception and without recourse, by Alternate Dispute Quorum. (italics added)(http://www.jamesdeeink.com/)

- Customers paying by credit card agree to all terms/conditions contained herein and agree *to waive all chargeback rights*. If presented with a chargeback, SST reserves the right to pursue legal action against the cardholder.(italics added) (http://www.sunsplashtours.com/documents/TourParticipantNew.pdf)

Cardholder's rights to chargeback in Australia.

Strictly speaking the chargeback is about the bank obtaining a refund from the merchant not about whether the card holder can stop payment, although from a practical point of view the cardholder may see it as amounting to the same. Even with the manual use of a card, once it has been instigated there is no way that payment can be stopped. Typically banks' terms and conditions relating to credit cards point this out.

In some ways, the chargeback provisions detract from the attractiveness of credit card payment from the point of view of the merchant. When credit cards operated without chargeback provisions (or when cardholders were not aware of them) the merchant was assured of payment, all other things being equal. The introduction of chargeback

1 For simplicity's sake, discussion will proceed on the basis that Australian law applies. Of course where it is an internet transaction the issue of what is the applicable law becomes crucial .See Andrew Field, 'Legislation, Electronic Commerce and the Common Law: the Growing Legislative Framework, how it Compares Internationally and its Failings in Australia' in Yew-Kwang Ng, Heling Shi and Guang-Zhen Sun (eds), *The Economics of E-Commerce and Networking Decisions* (2003) 134, 146.

provisions relegates credit card payment to a situation similar to that of payment by cheque: it is not an irrevocable payment if the cardholder can compel the card issuer to invoke the chargeback provision against the merchant.

Therefore chargeback rights imply that payment is conditional. Moreover, the right to payment is arguably more tenuous than payment by cheque. A cheque can always be countermanded by the drawer,[2] but this will not always prevent the drawer from being sued on the cheque, especially if the cheque has been passed onto a holder in due course who will be able to enforce it against the drawer free from any disputes between the drawer and the payee.[3] Even in a legal action by the payee against the drawer a defence by the drawer to the action is not easy to establish.[4] Chargeback rights are more akin to a cheque being paid and then the drawer having the right to unravel the whole payment transaction. Clearly if rights of chargeback can be invoked by the cardholder they are more extensive than those of a drawer of a cheque, since complaints about the quality of the goods and services will suffice to support the chargeback.

In Australia there are two initiatives that relate to chargebacks: the Electronic Funds Transfer Code (the EFT code) and the Australian Code of Banking Practice.

The Electronic Funds Transfer Code was worked out by the banks, consumer groups and the Trade Practices Commission. It was seen initially as an alternative to legislation, which is the path followed by the United States. Although it is described as a Code and as being voluntary, those banks that decide to follow it must reproduce its terms in the contract between the card issuer and the cardholder and, moreover, they must warrant that they have incorporated the code's key features. Failure to comply with this warranty would mean that the issuing bank would breach s 12 DB (1) (G) of the *Australian Investment and Securities Act 2001* (Cth) which is based on s53 (g) of the *Trade Practices Act 1974* (Cth), which prohibits false and misleading representation concerning rights and remedies.[5]

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2 *Cheques Act 1986* (Cth), s 90.

3 *Cheques Act 1986* (Cth), ss 49, 50.

4 The fact that the drawer has a right of set-off or a counterclaim against the payee stemming from the contract of sale will not necessarily provide a defence to a claim on the cheque. Judgement will be entered for the payee but the drawer can pursue his claims against the payee in another legal action. Leave to defend the claim will only be granted if the cheque is affected with fraud, illegality or failure of consideration: see *Nova (Jersey) Knit Ltd v Kammgarn Spinnerei GMbH* [1977] 1 Lloyd's Rep 463.

5 *Australian Investment and Securities Act 2001*(Cth) s 12 BAB provides that a person provides a financial service if they '(b) deal in a *financial product'*. A' *financial product'* is defined in

The EFT code applies to credit cards when they are used electronically, for example, over the phone or on the net but not when a consumer uses a credit card manually, that is, by having the credit card swiped and signing a credit card voucher. In regard to chargebacks the EFT code provides as follows:

> Unauthorised credit card and charge card account transactions
>
> 5.11 Where an account holder complains that there is an unauthorised transaction on a credit card account or a charge card account, the account institution shall not hold the account holder liable for losses under clause 5 for an amount greater than the liability the account holder would have to the account institution if the account institution exercised any relevant rights it had under the rules of the credit card or charge card scheme at the time the complaint was made against other parties to that scheme.
>
> The explanatory endnote 21 to the EFT code says in regard to the above:
>
> Account institutions may be able to resolve unauthorised transaction disputes on credit exercising rights (such as the right to chargeback a transaction) against other parties to credit card or charge card accounts. This clause does not require account institutions to exercise any such rights. However they cannot hold account holders liable under clause 5 for a greater amount than would apply if they had exercised those rights. The relevant rights are those that exist at the time the complaint were made. A delayed complaint may mean the rights have expired by the time of the complaint.

The EFT Code provides consumer will only be liable for unauthorized transactions:[6]

1. where the bank can affirmatively prove the user's fraud or breach of the security requirements in regard to the user's secret code and that this contributed to the loss.

12BAA(c) as being a facility by or thorough which people commonly make non-cash payments.

6 Electronic Funds Transfer Code, see, generally clause 5. There are also obviously situations where it would be unfair to hold the cardholder liable: if, for example, there was fraudulent conduct by employees by account institution -cl 5.2(a); or if a forged, expired or cancelled PIN or card was used - cl 5.2(b); or if the transaction took place before the cardholder received the card, PIN or code – cl 5. 2 (c); or if the merchant incorrectly debited the account more than once- cl 5.2(d); or if the transaction took place after the cardholder has the account institution that the card had been lost or stolen or that someone else may know the PIN or password- cl 5.3; or where it is clear that the cardholder has not contributed to the loss – 5.4.

2. where the bank can affirmatively prove the user delayed notifying loss or theft or breach of security requirements.
   The references to security requirements are that the user must not

   * voluntarily disclose one or more of the Codes to anyone
   * indicate one or more of the Codes on the outside of the access device, or keep a record of one or more of the Codes (without making any reasonable attempt to protect the security of the Code records) so that they are liable to loss or theft simultaneously. Ditto where there is no access device
   * after the adoption of the new EFT Code select a Code that represents the user's birth date or part of the user's name having been warned by the bank not to select such a Code
   * act with extreme carelessness in failing to protect the Codes.

3. Where a secret Code is required and neither 1 nor 2 apply, the user is liable for no more than $150 or at any lower figure set by the bank[7].

Matters must be proved on a balance of probabilities basis. Clause 5.5 is of considerable importance since it provides that the fact that the account has been accessed by the correct PIN does not of itself constitute proof of the cardholder's fraud or breach of security requirements.

This will mean the burden of unauthorised use will effectively be borne by banks. It is only when the cardholder has been extremely careless in failing to protect the security of the Codes or negligent in specific ways or fraudulent that the cardholder has to bear the loss; and, even then, only when the financial institution can affirmatively prove this. In reality this will not happen very frequently.

Therefore, in regard to chargebacks, if there is a dispute as to liability in regard to an unauthorised use of a credit card over the phone, for example, and the bank is able to show that the cardholder has contributed to the loss, then the loss to be borne by the cardholder will be no greater than that which would have been the case had the bank exercised its chargeback rights against the merchant.

Given the wide use of credit card numbers over the phone and the internet s 5.11 of the EFT code is a valuable right given how easy it is for rogues to abuse credit card numbers. The EFT code does not, however, allow any chargeback rights where the

7 Under Electronic Funds Transfer Code the bank is normally liable for any failure of the equipment or system – cl 6.1.

purchase by credit card is authorised but the cardholder is dissatisfied with the goods or services. For this we must turn to the Code of Banking Practice.

The Australian Code of Banking Practice was initially drafted by the Australian Bankers Association, albeit using earlier Trade Practice Commission (now called the Australian Competition and Consumer Commission) versions as a working draft. [8] Under the Code subscribing banks warrant they will comply with all relevant laws; so this would therefore cover all Commonwealth, State and Territory legislation and banking practice where it represents the law.[9]

For a number of years prior to the introduction of the new version of the code that came into force in May 2004 it was view of the Australian Banking Industry Ombudsman (now called the Banking and Financial Services Ombudsman) that a good banker should attempt chargeback rights on behalf of its customer. The Ombudsman's submission on the Review of the Code of Banking Practice therefore proposed the inclusion of an obligation on banks to place a stop on a cardholder's account when a customer has disputed the transactions debited by a merchant. The Ombudsman took the view that it would improve and clarify the banker/customer relationship if the Code could be expanded to identify as good banking practice that, in situations where a transaction was disputed, a customer would be offered the option of placing a stop on the account, if the banking system allowed it, similar to the stop effected when a card is reported lost or stolen.[10] This recommendation was not, however, taken up.

The Ombudsman's proposal is interesting in that the proposal seems almost to consider the bank card issuer as the agent; this is dubious if the traditional view of *Re Charge Card* is correct.[11]

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8 A L Tyree *Banking Law in Australia*, 4th ed (Sydney: Butterworth's, 2002) 327.

9 The Australian Code of Banking Practice cl 3.

10 Australian Banking Industry Ombudsman Review of the Code of Banking Practice, Issues Paper, February 2001, 3-5.

11 The traditional view of *Re Charge Card* 1987] Ch 150; [1986] 3 ALL ER 298 is that the bank is not acting as the cardholder's agent in paying the merchant. Rather the merchant accepts payment by the bank (subject to the terms and conditions between the bank and the merchant) in lieu of the cardholder's payment obligation. In other words, *Re Charge Card* establishes that payment by credit card is not like payment with a cheque whereby if the cheque is not paid the debt revives and the drawer is still liable to pay for the goods and services. The merchant accepts payment by credit card in full discharge. This can create a problem if the card issuer becomes insolvent, as was the case in *Re Charge Card.* On the basis of *Re Charge Card*, the traditional view therefore is that with a credit card the bank is not the agent of the cardholder and owes no duty to obtain for the benefit of its customer

The Ombudsman's experience was 'that member banks will attempt to chargeback disputed transactions where they can'.[12] It was the view of the Ombudsman that it is good banking practice and that one of the objectives of the Code is to uphold standards of good practice and service.[13]

The latest version of the Australian Code of Banking Practice provides as follows in regard to chargebacks:

> Chargebacks
>
> We will, in relation to a credit card transaction:
> (a) Claim a chargeback right where one exists and you have disputed the transaction with us within the required time frame;
> (b) Claim the chargeback for the most appropriate reason;
> (c) Not accept a refusal of a chargeback by a merchant's financial institution unless it is consistent with the relevant card scheme rules; and
> (d) Include general information about chargebacks with credit card statements at least once every 12 months.

It is interesting to read a major Australian bank's 'translation' of this into the terms and conditions between the cardholder and the bank:

> Each card scheme's rules allow us to dispute an authorised transaction for you in certain circumstances if we do so within strict time limits. If the credit card scheme's rules allow us to do so, we will claim a refund of a transaction ('chargeback') for you. Usually we can only do this if you tried to get a refund from the merchant first and were unsuccessful.[14] You should tell us if want us to chargeback a transaction for you within 30 days of the statement date so that we do not lose our chargeback rights. If you tell after this time, and we cannot chargeback the transaction, you will continue to be liable for that authorised transaction.[15]

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any advantages of the credit card scheme other than those outlined in the contract between the cardholder and the bank.

12 Australian Banking Industry Ombudsman Review of the Code of Banking Practice, Issues Paper, February 2001, 85.

13 The Australian Code of Banking Practice 1.1.

14 This implies that there must be terms in the operating rules of some cards whereby the bank's right of chargeback is conditional upon the cardholder trying to obtain a refund from the merchant.

15 From the author's contract with the Commonwealth Bank.

The Australian Code of Banking Practice is a voluntary code of conduct. Under cl 3.2 those banks which subscribe to it undertake to comply with the code if it imposes any additional obligation upon it beyond what the law imposes except where doing so would lead to a breach of law (for example, a privacy law). Arguably, facilitating a chargeback is something beyond the law although this is debateable.[16] In addition under cl 39.1(a) (i) the banks warrant that they will be bound by the Code in respect of any banking service that is provided to customers. Thus it would seem any attempt by the issuing banks to take away cardholder's rights to chargeback if they subscribe to the code would be in breach of s 12 DB (1)(G) of the *Australian Investment and Securities Act 2001* (Cth) that makes illegal a false or misleading representation concerning the existence, exclusion or effect of any condition, warranty, guarantee, right or remedy.

Chargebacks with an intermediary

The picture is further complicated by the fact that many consumers use internet-based payment mechanisms in conjunction with a credit card. These mechanisms typically involve the use of a third party.

BPAY is a popular electronic way of making payments in Australia, especially to utilities. This is basically a simple electronic giro whereby the consumer 'pushes' a payment to the payee. Can there be a chargeback with this? This would seem to depend on common law principles applicable to payment systems, the application of various codes, and the various contracts between the parties. The key issue here would appear to be this: is the BPAY payment conclusive, leaving only settlement arrangements, or does the use of a credit card in conjunction with BPAY, make the credit card dominant, with the possibility of there being a chargeback? The issue is far from clear.[17] One major Australian bank provides that 'When a credit card is used to pay a bill through the BPAY Scheme, the X bank treats that payment as a credit card purchase transaction'.[18] Now, the same bank's Credit Card Terms and Conditions in

16 In relation to cheques it has been held that the bank is entitled to obtain for the benefit of its customer any advantages under the clearing house rules: *Riedell v Commercial Bank of Australia Ltd* [1931] VLR 382; and that therefore the card issuing bank is like an agent of the cardholder. But this decision seems to rest on the idea that banks in both paying and collecting cheques act as agents; and, as such, owe their principals, the customers, a duty always to act in their best interests; on this argument see A L Tyree 'Riedell gets a credit card' (2002) 13 *Journal of Banking and Finance Law and Practice* 301 and 'Payment by credit card' by the same author at http://austlii.edu.au/~alan/payment-by-credit-card.html.

17 See R.R Edwards 'Electronic Payments and the pull back' *Insolvency Law Journal* vol 12 no 2, 81 – 94.

18 This seems to echo the US position where quality chargebacks can only be used where the credit card is used as an extension of credit rather than as a convenient substitute for cash.

the General Explanatory Information set out the card holder's rights in regard to chargeback. This supports the notion that chargeback is still available despite the fact that BPAY says that payment is final.

Another extremely popular way to make payments both to businesses and to other payments is PayPal. If a merchant cannot afford a merchant account then this offers a cheaper alternative. The seller, for example, a merchant has to be registered with PayPal. The buyer logs onto the PayPal website and enters details about the purchase and the amount and the e-mail address of the seller. The amount is taken out of the buyer's account with PayPal or the buyer may charge the amount to a credit card account. Can the buyer, if he uses the latter method, use chargeback procedures? The position in America, at least, seems to be that if the issuing bank classifies the transaction as a credit card purchase, then the US chargeback procedures are available.[19]

Merchants' rights to exclude chargeback

Before exploring this, where the merchant fits into the web of contracts needs to be clarified.

To use a simple example with a credit card, there are at least three agreements. First, there is an agreement between the consumer and the bank setting out the terms and conditions for use of the credit card. Secondly, there is an agreement between the merchant and the bank detailing the merchant's responsibilities in terms of obtaining payment from the bank. Third, there is the agreement between the consumer and the merchant for the purchase of goods and services with the credit card.

In practice it is more likely that the card issuing bank will be Bank A (the cardholder's bank) and the merchant's bank will be Bank B[20] rather than the cardholder and the merchant having the same bank. Therefore there will be four contracts. Diagrammatically it is thus:

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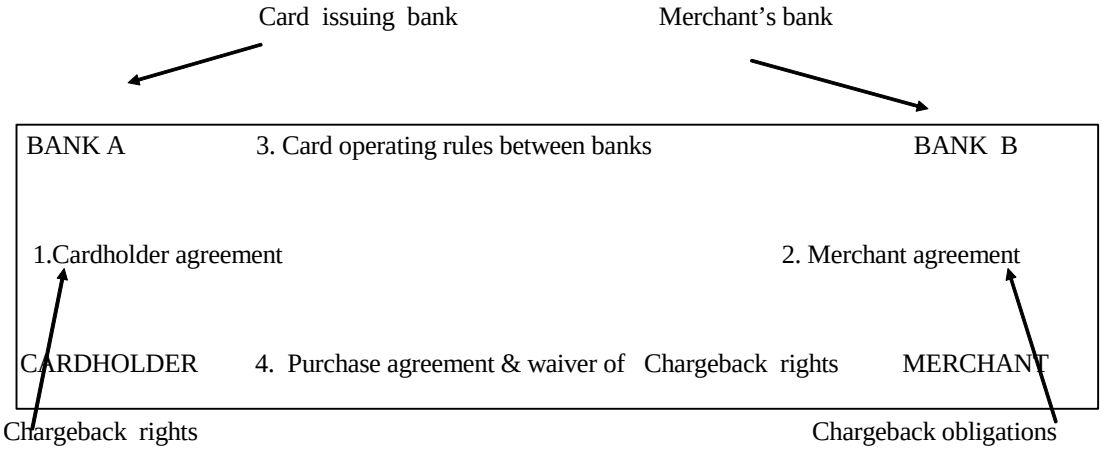
19 https://www.paypal.com/cgi-bin/webscr?cmd=xpt/seller/ChargebackRisk-outside#Q1.

20 This may pose a problem for the argument that chargeback is a legal right that derives from the fact that the issuing bank is the agent of the cardholder. It is hardly credible that Bank B could be viewed as the agent of the cardholder. Bank B has liability to pay the merchant if the merchant provides Bank A vouchers, but this liability is an independent liability. But could Bank B be viewed as the agent of Bank A to receive reimbursement from Bank A? The rules of credit card schemes are not totally in the public domain (snippets can be gleaned from cases) so it is not possible to answer this with any degree of certainty.



It is clear that the rights and obligations of the merchant are found in his contract with Bank B including the possibility that money paid to the merchant can be pulled back from the merchant (chargeback).The cardholder's rights and obligations are found in the contract with Bank A supplemented by the EFT code (if applicable) and the Australian Code of Banking Practice, conferring chargeback rights. Provisions in the *Australian Investment and Securities Act 2001* (Cth), referred to already, undoubtedly prevent the issuing bank from excluding, restricting or limiting the cardholder's chargeback rights deriving from the issuing bank- cardholder contract.

Is there anything in the merchant's card agreement with bank B that prevents the merchant from excluding, restricting or limiting the cardholder's chargeback rights?

Visa and Master card merchant agreements do allow for local variations but most of them allow chargeback in certain circumstances. The following from a major Asian bank is typical of such clauses:

> The Company (the bank) shall have the right at any time without notice *to charge the merchant's account, to withhold payment on any sales draft* (credit vouchers) presented to the company by the merchant at any time or to bill such bill to be payable on receipt thereof for the total value face amount of all sales drafts where
> ……
> (f) The cardholder *disputes the sale quality or delivery of the merchandise or the performance quality of services* in relation to such sales drafts;
> (g) Such sales draft was drawn by or credit given to the merchant in circumstances constituting a breach of any term, condition, representation, warranty or duty of the merchant hereunder;

(h) Sales of merchandise performance of services or use of the credit card involve a violation of law or the rules or regulations of any governmental agency local or otherwise. (Italics added.)

The following from a major Australian bank-merchant agreement seems to indicate that there are almost no limits to chargebacks:

> At our election, a transaction for sale, refund or provision of cash is not acceptable if:
> (a) *the cardholder disputes liability for the transaction for any reason or makes a claim for set-off or a counterclaim*; or
> (b) it is a class which we decide, at our discretion, is not acceptable.
>
> We may refuse to accept a transaction if it is invalid or unacceptable, or may *charge it back to you if we have already processed it even if we have given you an authorisation* (either electronically or by telephone). (Italics added.)

Another major Australian bank-merchant agreement has the following in regard to chargebacks:

> If a Transaction is an Invalid Transaction or an Unacceptable Transaction the Bank may at its sole discretion:
> (a) refuse to accept the transaction; or
> (b) if the Transaction has been processed, at any time within 12 months of the date of the Transaction *charge that Transaction back to the Merchant by debiting the Merchant Account* or otherwise exercising its rights under the agreement.(Italics added.)

An 'Invalid Transaction' is defined to include, amongst other things, an unauthorized transaction, including mail, telephone or Internet orders. An 'Unacceptable Transaction' is defined in the agreement in the following terms:

> A Transaction is not an acceptable Transaction if in the bank's reasonable opinion the cardholder justifiably:
> (i) *disputes liability for the Transaction for any reason*; or
> (ii) makes a claim for set off or counter claim in respect of the Transaction against the bank. (Italics added.)

Again, there seems to be almost no limits to chargebacks. There does not even have to be a legal reason for disputing liability so long as the bank reasonably thinks it is justified. This seems at odds with the very same bank's advice to customers on disputing a credit card transaction which says, in part, 'If you're not happy about the quality, value or price of the product or service but you have authorized the

transaction, you need to deal direct with the merchant'.[21] The latter part of the definition of an 'Unacceptable Transaction'seems to countenance the idea that there is an assignment of the debt between the cardholder and the merchant and that, therefore, the debtor, the cardholder, can set up against the assignee, the bank, any counterclaims or set offs arising from the underlying transaction.

The chargeback provisions relating to telephone sales in the merchant agreement are well documented in *Cosmedia Productions Pty Ltd v Australia and New Zealand Banking Group Ltd;*[22] but nothing in this agreement which had a provision allowing chargeback, would prevent a merchant from agreeing to payment by a cardholder on the basis that the cardholder waive his or her rights to chargeback.

In the Australian merchant credit card agreements above there is nothing that expressly prevents the merchants from accepting payment from the cardholder on the basis of a waiver of chargeback rights by the card holder in the cardholder–issuing bank contract. However, they do provide that the merchant's website has to be approved by the bank and this might possibly be used to stop an exclusion or waiver of chargeback rights. One major bank also provides that the merchant must give 'details of your return and refund policy including how a transaction can be cancelled by a cardholder'. This might arguably be used to prevent exclusion or waiver of chargeback rights, although it would not be difficult to craft a policy that complies with this yet still allows exclusion or waiver of chargeback rights.

In America credit cards are in the main regulated by the *Truth-in-Lending Act*[23] and the Federal Reserve Board's implementation of Regulation Z.[24] This provides for a bill error system which allows cardholders to dispute a bill that has a charge for goods or services not accepted by the cardholder or not delivered. The card issuer then has to credit the cardholder's account with the disputed amount and the card issuer will subsequently chargeback the amount to the merchant. It also provides as follows:

> When a person who honors a credit card fails to resolve satisfactorily a dispute as to property or services purchased with the credit card in a consumer credit transaction, the cardholder may assert against the card issuer all claims (other than tort claims) and defenses arising out of the transaction and relating to the failure to resolve the dispute. The cardholder may withhold payment up to the

21 http://www.anz.com/australia/persbnk/prdsrv/credit/PDF/Disputing_a_Credit_Card_transaction.PDF.

22 (1996) ATPR (Digest) 46-155; (unrep, 5/6/1996, Fed Ct Sheppard J, NG 892 of 1993).

23 Title 1 of the *Consumer Credit Protection Act* of 1968, 15 USC §§ 1601-1667f.

24 12 CFR part 226 (1999).

> amount of credit outstanding for the property or services that gave rise to the dispute and any finance or other charges imposed on that amount.[25]

The right to dispute raises defences or claims arising out of the underlying contract against the card issuer is, however, limited to transactions that take place within the cardholder's state or within 100 miles of the cardholder's address.[26] In addition, the amount of the transaction must exceed $100.

In the case of *Izraelewitz v Manufacturers Hanover Trust Co*[27] the seller of electronic diagrams had a 'No refund' clause that was clearly written in the 'how to order' part of the catalogue. This was considered fair under American law since it protected the seller from buyers who could just copy the diagrams and then claim a refund. The buyer purchased with a credit card and then tried to claim a chargeback. This failed because of the seller's location. However, even if this was not a hurdle, as between credit card holder and issuing bank, the cardholder remained liable for the disputed debt, because even assuming that the cardholder was able to assert claims and defences from original transaction, any claims or defences the holder chose to assert would only have been as good as and no better than his claim against seller. In short, the merchant had by the 'No refunds' clause effectively prevented the buyer from exercising chargeback rights because the buyer had no legally enforceable claim against the seller. Therefore there was no right to set up against the card issuer.

This case indicates that in America it may be possible for the merchant to exclude chargeback rights. In America 'quality' chargeback rights (for example that the goods are not of merchantable quality) depend on a legally tenable claim against the merchant. This was justifiably excluded by the 'No refunds' clause.[28] American law is

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25 Ibid 226.12[c](1). The rationale seems to be that if a consumer buys goods on credit from the merchant and they are defective, the consumer can set up against the merchant defences stemming from the contract. If it is a third party that is supplying the credit, why should not the consumer be able to set up against that third party credit provider defences he could set up against a direct supplier of credit?

26 The rationale for the geographical limitation being that the supplier of credit will be able to monitor merchants and only have links with reputable ones.

27 465 NYS 2d 486.

28 The US legislation seems to be based on the idea a credit card involves an assignment by the merchant to the bank of 100 cents in the dollar of the debt owed by the consumer to the merchant and the merchant receives a lesser sum in return from the card issuer. With an assignment of a debt the assignee takes subject to defences and counterclaims that could have been raised by the debtor vis a vis the assignor : *Roxburghe v Cox* (1881) 17 Ch D 520; s 134 Property Law Act 1958 (Vic). Others say a credit card is more like a letter of credit. A letter of credit is used to provide sound financial banking to the buyer's undertaking to

a lot clearer on what might give rise to a chargeback right in this context: if the transaction is authorized it must be a right or a defence arising under the original transaction. Australian chargeback rights are not so clear. They seem to depend merely on the cardholder merely disputing the transaction and on the chargeback rights or 'boxes' in the credit card operating rules. These cover such things as: cardholder does not recognise transaction; transaction is a duplicate; goods or services not received /rendered ; recurring transaction/direct debit not authorised; processing error - incorrect amount or paid by other means; credit not processed; incorrect amount; did not authorise or participate in this transaction and so on.[29] Thus also seems to depend on what the credit card scheme's rules allow. The Australian Code of Banking Practice coyly indicates this by saying, 'We will, in relation to a credit card transaction: (a) Claim a chargeback right where *one exists'* (italics added). If the credit card scheme's rules did not allow for chargeback then the card holder would have no rights. The chargeback rights in the Australian Code of Banking Practice seem to have been developed with credit card scheme operating rules in mind. These in turn seem to have been developed to reflect American legislation. Happily credit card scheme's rules usually allow for chargebacks because in the main they seem to have been drawn up with American laws in mind.

In Australian law, would waiver or exclusion of chargeback rights by a merchant be misleading and deceptive within the terms of s 12 DB (1) (G) of the (Cth) on the basis that it is equivalent to saying 'no refunds'? If it is a consumer transaction then the statutory implied terms cannot be excluded and if a breach of these gave rise to a right to a refund, then it could be argued that the waiver or exclusion of chargeback rights by a merchant is misleading and deceptive if payment is made by credit card.[30]

Since merchants commonly have advertising saying they will accept payment by credit card and since rights of chargeback are fairly well known by cardholders, would it mean that continuing such advertising but accepting payment by credit card

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pay. Likewise with a credit card 'supplier and customer have for their mutual convenience each previously arranged to open an account with the same company, and agree that any account between themselves may, if the customer wishes, be settled by crediting the supplier's and debiting the customer's account with that company': *Re Charge Card Services* [1987] Ch 150; [1986] 3 ALL ER 298 at 303. With a letter of credit the thing that triggers liability to pay the beneficiary is the conformity of the documents with the principal's instructions- the applicant cannot interfere with payment if it is an irrevocable letter of credit unless clear fraud is established. Likewise, so it is argued, with a credit card: the vouchers submitted by the merchant give rise to an independent obligation on the card issuer to pay.

29 http://www.anz.com/pacific/merchant/hottopics/chargebacktop10.asp.

30 http://www.accc.gov.au/content/index.phtml/itemId/8818/fromItemId/3669#h3_56.

on the basis of a waiver of chargeback rights be misleading and deceptive? This would hardly be a tenable argument if the exclusion or limitation clause was made clear to the cardholder before the purchase by credit card. If the exclusion clause is prominently displayed, for example, on a website it does not really matter if it is viewed as an invitation to treat or an offer by the seller if the buyer has knowledge of this exclusion or limitation clause by clicking on, for example, the 'I agree' box.[31] It should be noted that the merchant would not be excluding the cardholder's rights in terms of conditions express or implied in the contract of sale relating to the sale of the goods or services but merely restricting a right attaching to the form of payment. By way of comparison it would be somewhat like a merchant agreeing to take payment by cheque on the basis that the drawer does not stop payment.

Could the exclusion or waiver of chargeback rights be attacked as unconscionable? The doctrine of unconscionable dealing articulated by the High Court in cases such as *Blomley v Ryan*,[32] *Commercial Bank v Amadio*,[33] *Louth v Diprose*[34] and *Bridgewater v Leahy* [35] has usually been viewed as applying to transactional unfairness as opposed to substantive unfairness. [36] Provided the process of transacting was fair equity would not interfere with the outcome, even where the outcome was harsh or unreasonable.[37] Sir John Salmond in *Brusewitz v Brown* commented:

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31 See *Mortenson v Timberline Software Corp* 140 Wn.2d;2000 Wash.LEXIS 287 (Supreme Court of Washington, Court of Appeal, 5 May 2000) for a discussion of whether a website approximates a shop display and is therefore an offer to treat or whether there is an offer to sell by the vendor.

32 (1956) 99 CLR 362.

33 (1983) 151 CLR 447.

34 (1992) 175 CLR 621.

35 (1998) 194 CLR 457.

36 The distinction between procedural and substantive unfairness was discussed by Leff A, 'Unconscionability and the Code – The Emperor's New Clause' (1967) 115 *U Pa. L. Rev* 485. See also Duggan A.J., *'Trade Practices Act 1974 (Cth), Section 52A and the Law of Unjust Contracts'*, (1991) 13 *SydLR* 138. In the United States statutory unconscionability (Uniform Commercial Code 2-302) has been interpreted in commercial cases to involve both a procedural and a substantive unfairness: see Priestley L J, 'A Guide to Comparison of Australian and United States Contract Law' (1989) 12 *UNSW LJ* 4 at 15. The doctrine's substantive element is said to trace to inadequate price doctrines such as Roman law's *laesio enormis* (where certain sales for under half price could be rescinded: see Reynolds 'FMB Contract: Codification, Legislation and Judicial Development' (1995) 9 *JCL* 11 at 27) and the usury and just price theories of the Middle Ages: see DiMatteo L, 'Equity's Modification of Contract: An Analysis of the Twentieth Century's Equitable Reformation of Contract Law' (1999) 33 *New Eng L Rev* 265 at 288-9.

37 Equity cases are replete with reminders that 'equity mends no man's bargain': *Maynard v Moseley* (1676) 3 Swanst 651 at 655 per Lord Nottingham. See *Allcard v Skinner* (1887) 36 Ch

> The law in general leaves every man at liberty to make such bargains as he pleases and to dispose of his own property as he chooses. However improvident, unreasonable or unjust such bargains or dispositions may be, they are binding on every party to them unless he can prove affirmatively the existence of one of the recognised invalidating circumstances such as fraud or undue influence.[38]

Under the unwritten law on unconscionability therefore the cardholder would have to show they were under some special disability to be brought into the category of persons who would be deserving of protection. This would cover any condition that 'seriously affects the ability of the innocent party to make a judgment as to his own best interests' is sufficient to put the weaker party under a special disability.[39] Depending on the circumstances of the cardholder it might be possible for the cardholder to argue that exclusion or waiver of chargeback rights is unconscionable.

Section 12CB of *Australian Investment and Securities Act 2001* (Cth) provides for a statutory version of unconscionable conduct in regard to consumers which might also apply and provides a non- exhaustive list of matters that the court may take into consideration in determining whether conduct is unconscionable. Of particular interest are the following

> (a) the relative strengths of the bargaining positions of the supplier and the consumer; and
> (b) whether, as a result of conduct engaged in by the supplier, the consumer was required to comply with conditions that were not reasonably necessary for the protection of the legitimate interests of the supplier; and
> (c) whether the consumer was able to understand any documents relating to the supply or possible supply of the services;
>
> Typically the supplier will be the stronger of the two and the exemption clause will be provided on a 'take it or leave it' basis. Is the suppler who uses an

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D 145 at pp 182-183 per Lindley LJ; *Brusewitz v Brown* [1923] NZLR 1106 at 1110 per Salmond J; *White and Carter (Councils) Limited v McGregor* (1962) AC 413at 445 per Lord Hodson 'It is trite that equity will not rewrite an improvident contract where there is no disability on either side'. *Hart v O'Connor* [1985] App Cas 1000 at 1018 (Privy Council). The common law has long held that whilst consideration must be sufficient it does not have to be adequate. See *Thomas v Thomas* (1842) 2 QB 851; *Chappell & Co v Nestle & Co Ltd* (1960) AC 87 (House of Lords).

38 [1923] NZLR 1106 at 1110.

39 *Commercial Bank of Australia v Amadio* (1983) 151 CLR 447 at 462 per Mason J, at 477 per Deane J, with whom Wilson J agreed. See also *Bridgewater v Leahy* (1998) 194 CLR 457 at 470 per Gleeson CJ and Callinan J; *Blomley v Ryan* (1956) 99 CLR 362 at 392 per McTiernan J, at 415 per Kitto J.

> exemption or waiver clause reasonably protecting his legitimate interests? Merchants frequently complain that chargeback rights are frequently abused by cardholders and that complaints about 'quality' chargebacks are spurious. However, given that exclusion of chargeback rights is not widespread in Australia it perhaps indicates that such an argument is overstated. Whether the consumer understands the significance of the exclusion clause would presumably only be relevant if the consumer had a special disability.But the circumstances where it could be argued that the use of an exclusion or waiver clause in regard to chargeback is unconscionable would seem to be fairly limited.

But, in practice, would having the cardholder waive rights to chargeback be effective? Under Australian law the cardholder's rights to chargeback derive from the contract between the issuing bank and the cardholder supplemented by the Electronic Funds Transfer Code (the EFT code) and the Code of Banking Practice. Could the merchant try to stop the cardholder from invoking these rights? This would mean having to notify the issuing bank not to exercise chargeback rights on behalf of the cardholder. This could occur sometime after the purchase is made (under some credit card schemes, chargebacks can be exercised up to 6 months after the sale). What would be the legal basis for such a request, given that the merchant is not a party to the cardholder-issuing bank contract? If the issuing bank facilitated a chargeback would this be tantamount to inducing a breach of contract between the merchant and the cardholder? This would be dubious since the issuing bank would say that by exercising chargeback obligations vis-à-vis the cardholder it was merely complying with the terms between itself and the cardholder.[40] It is really a situation of there being two inconsistent contracts. Just because the issuing bank knows that the cardholder has agreed with the merchant that he will not exercise his rights of chargeback does not mean that if the cardholder does exercise his rights of chargeback with the issuing bank that the latter has induced a breach of contract between the cardholder and the merchant. Conversely, it also would not be tenable that the merchant by entering into a waiver or exemption clause with the cardholder was inducing a breach of the issuing bank-cardholder contract that confers chargeback rights.

The only legally sound basis, if the cardholder exercised rights of chargeback contrary to the agreement with the merchant, would be for the merchant to bring a legal action against the cardholder for breach of the agreement. From a practical point of view this

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40 The tort of inducing a breach of contract has been described by Lord Macnaghten in the following terms 'A violation of legal rights committed knowingly is a cause of action, and it is a violation of legal rights to interfere with contractual relationships recognised by law if there be no sufficient justification fro the interference': *Quinn v Leatham* [1901] AC 495 at 510.

would be fraught with problems, especially where the purchaser lived at a distance to where the merchant was located or when the amount concerned was not substantial.

Excluding chargeback rights, if widespread, might be viewed by banks as detrimental to credit card schemes from which banks derive a great deal of revenue. If the banks concerned decided that they did not want a merchant because of his attitude to chargebacks, could they collectively decide not to deal with the merchant? This would seem to be problematic in terms of either the common law tort of conspiracy or collective refusals to deal under the *Trade Practices Act 1974* (Cth), although the former does allow a defence of protecting trade or vital interests and the latter does provide for authorisation on the basis of public benefits. Would widespread use of exclusion or waiver of chargeback rights by merchants imperil the credit card schemes or defeat the purpose of the chargeback provisions in the Australian Code of Banking Practice and would this be a sufficient justification on a public benefits basis? The bank card scheme operated successfully for many years without chargebacks rights and it was quite common until recent years for cardholder contracts to provide that disputes over goods or services acquired had to be sorted out directly by the cardholder with the merchant.[41] So justification of a boycott by banks of merchants who exclude chargeback rights would not be likely to succeed.

Conclusion

In summary, it seems dubious that bank- merchant agreements prevent exclusion of chargeback rights by the merchant. There does not seem to be any explicit clauses preventing exclusion or waiver by merchants of cardholders' chargeback rights.

A waiver or exclusion of chargeback rights might amount to misleading or deceptive conduct if it is a consumer transaction but this would depend on the wording. It is unlikely that it would be considered unconscionable but again this would depend on the circumstances.

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41 The Royal Bank's VISA cardholder agreement (Canada) is typical. It provides that the cardholder is liable to Royal Bank 'for all Debt charged to the Account no matter how it is incurred or who has incurred it....' and goes on to state: 'Problems with a Purchase**:** You [Royal Bank] will not be responsible for any problem I [cardholder] have with any Purchase. If I have a problem or dispute with a merchant regarding a Purchase, I must still pay all Debt as required by this Agreement and settle the problem or dispute directly with the merchant. You will also not be responsible if my Card is not honoured by a merchant at any time and for any other problem or dispute I may have with the merchant.'

The right of chargeback is a valuable right of credit cardholder that is expressly conferred by the both the Code of Banking Practice and the EFT code. If merchants can effectively take away this right by exclusion clauses or waivers, even if they only operate in terrorem, it defeats the purpose of the Code of Banking Practice. Given that the EFT code only applies to unauthorised use electronically, an exclusion or waiver clause would not be effective here since the legitimate cardholder would not be the person who has agreed to the exclusion or waiver clause.[42] It is therefore principally in regard to 'quality' chargebacks under the Code of Banking Practice that exclusion or waiver would have the most impact. However, this is an area where merchants are frequently disgruntled judging from websites.[43]

If one of the reasons why merchants try to exclude or have the cardholder waive chargebacks rights is abuse by cardholders of these rights them some amelioration to the right of chargeback might be worthwhile.

The provisions in the Australian Code of Banking Practice do not expressly provide that the cardholder has to try and resolve the dispute and send back the goods before asking the issuing bank to facilitate a chargeback. Such a precondition to the exercise of chargebacks rights in regard to 'quality' disputes seems sensible: the vendor gets back his goods and the cardholder gets back his money.

Australian cardholder chargeback rights are derived from the EFT code and the Australian Code of Banking Practice. The latter, in regard to chargeback rights, depends upon credit card scheme operating rules that reflect American chargeback rights. Chargeback rights have come to us through the backdoor. If chargeback rights were enshrined in an Australian statute that reflected a clear rationale for such rights, then the problem of exclusion by merchants of these rights could be properly addressed.

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42 Unauthorised transactions over the internet are another major problem. Many merchant agreements provide for bank authentication where online transactions are verified by Visa or Mastercard - this shifts the liability from the merchant to the issuing bank.

43 http://site.yahoo.com/bank1/chargebacks.html
http://www.merchantseek.com/article8.htm;
http://www.vindicia.com/pdf/VindiciaDataSheet-1.1.pdf;
http://www.merchant911.org/