

## Notice of Undertaking

### Introduction

As a qualifying body under the Unfair Terms in Consumer Contracts Regulations 1999 (the Regulations) we can challenge firms that are using terms which we consider unfair. We review contract terms referred to us by, among others, consumers, enforcement bodies and consumer organisations. Our review of terms and conditions used in the RBS Group has led to The Royal Bank of Scotland plc, National Westminster Bank plc, Ulster Bank Limited, Coutts & Co and Adam & Company plc undertaking not to use certain terms that we consider unfair.

Under the Regulations we must notify the Office of Fair Trading (OFT) of the undertakings we receive. The OFT has a duty to publish details of these undertakings, which then appear on its Consumer Regulation website. We also publish a notice of these undertakings on our website. Both publications name the firms, identify the specific terms and explain why we thought they were unfair under the Regulations.

Even if firms have not given an undertaking or been subject to a court decision under the Regulations, they should remain alert to undertakings or court decisions concerning other firms as part of their risk management. These will be of potential value in showing the likely attitude of the courts, the FSA, the OFT or other qualifying bodies to similar terms or terms with a similar effect. Ultimately only a court can determine the fairness of a term and, therefore, we do not recommend terms that have been revised by a firm to address our concerns as being definitely fair. We cannot approve terms for the purposes of the Regulations; it is for firms to make an assessment of the fairness of their terms and conditions under the Regulations and in the context of the product or service in question. It is important to bear in mind that wording that is fair in one particular agreement is not necessarily fair in another. Where we accept an undertaking given to us from a firm to revise a term, this means that, on the evidence available at the time, we consider the term to be improved enough so that further regulatory action is not required.

### Undertaking in relation to certain terms and conditions in consumer contracts of certain members of the RBS Group

<b>Name of businesses</b>	The Royal Bank of Scotland plc (RBS) National Westminster Bank plc (NatWest) Ulster Bank Limited (Ulster Bank) Coutts & Co (Coutts)	<b>Lead organisation</b>	FSA
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	Adam & Company plc (Adam)		
<b>Trading sector</b>	Banking	<b>Contract identifier</b>	Phone and fax indemnity – Personal and Private Banking

**Original terms in use by RBS, NatWest and Ulster Bank**

*'1. In consideration of [the bank] agreeing (at [the bank's] discretion) to accept payment and transfer Instructions to or from any accounts in the account holder's name upon receipt of messages by telephone or facsimile ('Instructions'),*

*2. It is agreed that the account holder will keep [the bank] indemnified from and against all actions, proceedings, claims and demands which may be brought or made against [the bank] and all losses, costs, charges, damages and expenses which [the bank] may incur or sustain or for which [the bank] may thereby become liable, provided that:*

*a) such facsimile Instructions reasonably appear to be signed by the account holder, or where applicable in accordance with any third party mandate to the Bank for the time being,*

*b) such telephone Instructions reasonably appear to be given by the account holder, or alternatively in accordance with the Letter of Authority referred to below; and*

*c) the Instructions are checked, as to the total amount and the payee, by a return telephone call made by a Bank employee to a telephone number specified by the account holder, or alternatively in the Letter of Authority provided by and signed by the account holder and such number reasonably appears to have been answered by the account holder, or any person specified in the said Letter of Authority.*

*It is further agreed that:*

*3. The Bank shall be entitled to treat all Instructions as being duly authorised by the account holder and the account holder agrees that it will unconditionally ratify the Bank's actions taken in accordance with any Instructions.*

*4. The account holder hereby gives [the bank] its irrevocable authority to debit its account(s), (whether or not an overdraft is so created or increased) in accordance with any Instructions (and with any sums due under this Indemnity).'*

**Coutts and Adam used wording which was similar to the above terms in their respective consumer contracts concerning phone and/or fax instructions.**

**Application of the Regulations**

Terms are regarded as unfair under Regulation 5 of the Regulations if, contrary to the requirement of good faith, they cause a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer. In our view, the terms set out above were likely to be unfair under Regulation 5 of the Regulations.

*Significant imbalance*

In our view, the terms created a significant imbalance in the parties' rights and obligations arising under the contract because the terms had the potential to (i) be too broad in effect; (ii) provide the firm with too wide a discretion; (iii) absolve the firm of responsibility; and (iv) deprive consumers of protection afforded to them by law, namely under the Payment Services Regulations 2009 (PSRs).

i) Broad effect of the terms

We considered that the terms set out above were drafted so broadly that they had the potential to

hold consumers responsible for all actions, proceedings, claims and demands (Claims) brought or made against the firm and for all losses, costs, charges, damages and expenses (Losses) the firm incurred including where the Claims or Losses were directly attributable to the firm's own actions or negligence or were otherwise not properly incurred or were unreasonable and regardless of whether, for instance, Claims were resolved in favour of consumers.

The OFT, in its role as primary enforcer of the Regulations, issued guidance in February 2001 (reissued in September 2008) (OFT 311) on its interpretation of the Regulations, which supported our view. Paragraph 18.2.7 explains that 'terms under which the supplier must be 'indemnified' for costs which could arise through no fault of the consumer's are open to ... objections, particularly where the supplier could himself be at fault.'

#### ii) Wide discretion

We considered that the terms had the potential to provide the firm with too wide a discretion. For example, the terms provided the firm with a wide discretion to decide whether the payment instruction was valid by reference to criteria that we considered to be too vague.

#### iii) Absolving the firm of responsibility

We considered that the terms had the potential to allow the firm to absolve itself of all responsibility concerning payment instructions even if it did not carry out the validation steps contained in clause 2(a) to (c). Clause 3 allowed the firm to exclude itself from accepting any responsibility for any instructions on the account, as all instructions were deemed to be authorised by the consumer. In our view, this term was similar in effect to paragraph 1(b) of Schedule 2 to the Regulations, which states that a term is indicative of being unfair if it 'inappropriately exclude[s] or limit[s] the legal rights of the consumer vis-à-vis the seller or supplier ... in the event of total or partial non-performance or inadequate performance by the seller or supplier of any of the contractual obligations...'

#### iv) Depriving consumers of protection under law

We considered that clauses 1 to 4 had the object or potential effect of depriving consumers of protection under law, namely under the PSRs. Part 6 of the PSRs, among other things, provides protection for customers of payment service providers (which includes consumers) in relation to unauthorised payment transactions. In particular:

- Regulations 61 and 62 relate to the incidence of liability for payment transactions that were not properly authorised by the customer. The general principle is that, unless the payment service provider can prove that the customer authorised the payment transaction, or that he has acted fraudulently or failed, with intent or gross negligence, to meet his obligation in respect of the security of the payment instrument, the payment service provider must provide a refund to the payer.
- Regulation 60 (evidence on authentication and execution of payment transactions) provides that, where a customer denies having authorised a payment, the use of a payment instrument (for example, following the agreed set of procedures for giving instructions by fax or telephone) is not in itself necessarily sufficient to prove that the customer either authorised the payment or is at fault. Terms to the effect that the use of the payment instrument will be taken as proper authorisation in all circumstances are not, therefore, compatible with the PSRs.
- Regulation 62(3) provides that, except where the customer has acted fraudulently, he is not liable for any losses in relation to unauthorised payments arising after he notified the payment service provider of the misappropriation of the procedures for giving phone or fax

payment instructions.

- Regulation 66 addresses the circumstances in which a payment service provider may refuse to execute an authorised payment order.

Clauses 1 to 4 of the terms were inconsistent with these protections because they purported to allow the firm to refuse to execute an authorised payment order (Clause 1) and they require customers to:

- unconditionally ratify all payment transactions (Clause 3);
- give irrevocable authority to debit the account (Clause 4);
- keep the firm indemnified against losses in relation to unauthorised payment transactions where the use of the payment instrument was recorded (Clauses 1 and 2); and
- had the potential effect of transferring liability for unauthorised payment transactions and the risk of fraudulent behaviour by third parties to the customer in unduly broad circumstances (Clauses 2, 3 and 4).

The OFT guidance (referred to above) states at paragraph 18.6.1 that ‘any contract wording which could have the effect of depriving consumers of protection normally afforded to them under the law is open to suspicion of unfairness. The Regulations indicate specifically that terms excluding rights to redress for breach of contract may be unfair ... [and that] consumers also enjoy protection under legislation that operates separately from contract law’ such as the PSRs.

#### *Good faith and detriment*

In our view, the terms were contrary to the requirement of good faith as they had the effect of ‘contracting out’ of the protection offered to consumers by law under the PSRs. The terms had the potential to operate to the detriment of the consumer in that they allocated liability for potentially significant losses to the consumer that the PSRs place on the payment service provider. They could also have acted as a disincentive to consumers seeking to challenge the authenticity of payment instructions and making valid claims for refunds.

#### *Legal jargon – ‘indemnity’*

Regulation 7 states that ‘A seller or supplier shall ensure that any written term of a contract is expressed in plain, intelligible language’. We consider terms using the word ‘indemnify’ or ‘indemnity’ to not be expressed in plain and intelligible language, contrary to Regulation 7. We note that the OFT’s guidance (referred to above) indicates similar concerns regarding the use of terms requiring consumers to ‘indemnify’ firms. Paragraph 18.2.7 states ‘the word ‘indemnify’ itself is legal jargon which, if understood at all, is liable to be taken as a threat to pass on legal and other costs incurred without regard to reasonableness’.

**How the terms have changed**

The terms were redrafted to (i) remove the terms relating to payment instructions received by fax or telephone operating to and from consumer bank accounts that we were concerned were too broad; (ii) remove the legal terminology that we were concerned consumers may not understand; (iii) not set aside the provisions of the PSRs and not include terms that are inconsistent with the provisions of the PSRs; and (iv) more accurately reflect the intention behind the original terms, namely the verification of payment instructions to protect the firm and its customers against fraud.

**New terms for RBS, NatWest and Ulster Bank**

‘The payment instructions, whether received from you by phone or fax, will be verified by a return telephone call made by a Bank employee to a telephone number we currently hold on our records for you. During this call, we verify your identity (or that of your agent) and confirm you have instructed the payment. Please note we will not call you back on any new number provided with the payment request. If we are unable to contact you by telephone to verify the instructions, the payment may be delayed or not made.’

**Coutts and Adam undertook to include new or amended wording in their contracts that is the same or similar to the wording outlined above.**

**Other information**

Each firm was fully cooperative in providing the undertaking summarised above to us.

Coutts and Adam are or have amended their existing terms and RBS, NatWest and Ulster will use new terms in a stand alone document with consumers. RBS, NatWest and Ulster are in the process of changing each of their account terms and conditions to include terms that are similar to the new terms. They will then remove the standalone document as an unnecessary process once the revised terms and conditions become effective.

Each firm has agreed that in relation to payment instructions by phone and/or fax operating to and from consumer bank accounts it will not rely on the original (or any similar) terms. Each of them has also advised that it will treat any former or existing consumers as though they were subject to the new terms.

**Undertaking published 8<sup>th</sup> March 2011.**