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# The Tai Hing Conundrum : Estoppel, Contract or Tort?

## **Abstract**

The purpose of this article is to examine the competing legal principles in the type of situation exemplified in *Tai Hing Cotton Mill Ltd v Liu Chong Hing Bank Ltd and Others* (hereinafter *Tai Hing*). It will be suggested that the outcome of a dispute in a *Tai Hing* situation turns on the application of the principle that is ultimately applied. The search for this principle should commence with an analysis of the principal cases in this area.

## **Keywords**

Tai Hing Conundrum

# THE TAI HING CONUNDRUM: ESTOPPEL, CONTRACT OR TORT?



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The purpose of this article is to examine the competing legal principles in the type of situation exemplified in *Tai Hing Cotton Mill Ltd v Liu Chong Hing Bank Ltd and Others*<sup>1</sup> (hereinafter *Tai Hing*). It will be suggested that the outcome of a dispute in a *Tai Hing* situation turns on the application of the principle that is ultimately applied. The search for this principle should commence with an analysis of the principal cases in this area.

In *Young v Grote*<sup>2</sup> (hereinafter *Young*), the customer of a group of bankers had signed five blank cheques for his wife to complete in accordance with his business requirements. The customer's wife subsequently directed one of his clerks to complete one of the cheques. The clerk completed the cheque, but left spaces in it which enabled him to raise the amount therein by the fraudulent insertion of words and a figure in them. Thus a cheque for £50 2s 3d was, by the clerk's forgery, raised to £350 2s 3d. After the cheque had been cashed by the clerk, the bankers debited their customer's account for the amount paid out by them, namely, the enlarged amount. The customer objected to this, arguing that the cheque was valid for the unaltered amount only. The Court of Common Pleas found for the bankers. What legal principle did the Court apply? The language of Best CJ points clearly to estoppel:<sup>3</sup>

In the present case, was it not the fault of Young<sup>4</sup> that Grote and Co<sup>5</sup> paid £350 instead of £50? Young leaves a blank cheque in the care of his wife. It is urged, indeed, that the business of merchants requires them to sign cheques in blank, and leave them to be filled up by agents. If that be so, the person selected for the care of such a cheque ought at least to be a person conversant with business as well as trustworthy. But it was not likely that the drawer's wife should be acquainted with business, and she acting as her husband's agent, ought not to have trusted to receive the contents of the cheque, any person with whose character she was not perfectly acquainted . . . . It was by the neglect of these ordinary precautions that Grote and Co. were induced to pay . . . . We decide here on the ground that the banker has been misled by want of proper caution on the part of his customer.

Park J immediately followed by saying:<sup>6</sup>

I am of the same opinion . . . Can any one say that the cheque signed by Young is not a genuine order? I say it is. The cheques left by him to be filled up by his wife, when filled up by her, became his genuine order. However the arbitrator finds expressly that he was guilty of negligence; and I concur in that

1 [1986] 1 AC 80.

2 (1827) 4 Bing 253; 130 ER 764.

3 (1827) 4 Bing 253, at 259-260; 130 ER 764, at 766-767. Emphasis added.

4 The customer.

5 The bankers.

6 (1827) 4 Bing 253, at 260; 130 ER 764, AT 767. Emphasis added.

opinion. He leaves blank cheques in the hands of his wife, who was ignorant of business, but having left them with her to be filled up as the exigency of the moment might require, they become, upon her issuing them, his *genuine* orders.

What did Park J denote by 'negligence'? Was his Lordship describing the tort of negligence, or was he adverting to the customer's lack of care? What did Park J mean by the phrase 'his genuine order'? Did he mean to say that no forgery was involved or, rather, that it was not open to the customer to prove forgery? How could Park J have meant that the cheque was genuine when it was in fact forged? Again, if the cheque was genuine, why did Park J hold that the customer's negligence was relevant? How could Park J be taken to have decided that the customer's tort of negligence worked a transformation of a forged cheque into a genuine one? It is submitted that Park J held negligence to be relevant because, on the facts, nothing but the customer's negligence could have precluded him from asserting that the cheque was a forgery. The legal principle that constrains a person to accept that his forged cheque is genuine is estoppel, not the tort of negligence.

Burrough J said that the 'legal blame'<sup>7</sup> attached to the customer, and Gaselee J found that the customer had been guilty of 'great negligence'.<sup>8</sup>

None of the four judges who decided the case said that the customer was under an implied contractual duty to take care. Equally, none of their Lordships alluded to the tort of negligence. It seems that the ground of decision was that the customer was estopped by his negligence from proving the fact that the amount appearing in the cheque had been forged. All the judges found that the forgery was facilitated by the customer's negligence, which caused his bankers to believe his forged cheque to be his genuine order. The bankers did not sue their customer in negligence. Their argument, raised in defence against the customer's charge of their wrongful debiting of his account, was that because the customer had been negligent the loss should be made to fall on him,<sup>9</sup> namely, the customer could not rely on his own negligence to prove that the raised cheque was a forgery.

In *Robarts and Others v Tucker*<sup>10</sup> Parke B appeared to adopt the view of Park J in *Young*. Parke B said:<sup>11</sup>

Then reliance is placed on *Young v Grote* (4 Bing 253). In that case the customer had signed blank cheques, and left them with his wife to fill up. She filled them up in such a manner that the holder was enabled to add the amount; and it was held that the bankers who had paid this larger amount might charge their customer with it. This was in truth considering that the customer had by signing a blank cheque given authority to any person in whose hands it was to fill up the cheque in whatever way the blank permitted . . . .

Since that cheque in *Young* was in fact a forgery, the 'authority' to which Parke B referred would have been the product of the estoppel by negligence which operated against the customer.

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<sup>7</sup> (1827) 4 Bing 253, at 260; 130 ER 764, at 767.

<sup>8</sup> (1827) 4 Bing 253, at 261; 130 ER 764, at 767.

<sup>9</sup> (1827) 4 Bing 253, at 256-257; 130 ER 764, at 766; per Serjeant Taddy.

<sup>10</sup> (1851) 16 QB 560; 117 ER 994.

<sup>11</sup> (1851) 16 QB 560, at 579-580; 117 ER 994, at 1001-1002.

Four years later, in *The Governor and Company of the Bank of Ireland v The Trustees of Evans' Charities in Ireland*<sup>12</sup> (hereinafter *Evans' Charities*), Parke B himself lucidly explained *Young* as a decision on estoppel:<sup>13</sup>

... In that case it was held to have been the fault of the drawer of the cheque that he *misled* the banker, on whom it was drawn, *by want of proper caution* in the mode of drawing the cheque, which admitted of easy interpolation, and consequently, that the drawer, having thus *caused* the banker to pay the forged cheque by his own neglect in the mode of drawing the cheque itself, *could not complain* of the payment.

*Evans' Charities* also found Lord Cranworth LC endorsing the view that *Young* was a decision on estoppel:<sup>14</sup>

... I think it has been fairly put, that there must be either something that amounts to an *estoppel*, or something that amounts to a ratification, *in order to make the negligence a good answer*. Now the case of *Young v Grote* went upon that ground (whether correctly arrived at in point of fact is immaterial), that the Plaintiff there was *estopped* from saying that he did not sign the cheque for £350; and if the circumstances are such, *whether arising from negligence*, or from any other cause, that as between the customer and his banker, the customer is *estopped* from saying that he did not sign the cheque for a particular amount, that, as between them, is just the same *as if* he had signed it. Therefore taking that view of the facts, the case may be well sustained, and appears to have been well decided.

Lord Cranworth LC thus established two points:

- (1) *Young* had nothing to do with the tort of negligence; and
- (2) *Young* was a decision on estoppel, and that negligence was only one basis for estoppel.

Advisedly, neither Baron Parke nor Lord Cranworth LC saw fit even to discuss the possibility that *Young* might have been decided on the basis of an implied contractual duty owed, and breached, by the customer to his bankers. It would have been fictitious to explain *Young* as a case in which the bankers had sued their customer for breach of contract. It is one thing to say that the customer could not disown his forged cheque if he had himself negligently caused his bankers to believe it was genuine. However, it is an entirely different thing to say that the customer's inability to rely on the nullity of his forged cheque was founded upon an implied contractual promise by him not to mislead his bankers. Estoppel and implied contract are totally different concepts. Estoppel articulates the principle that one who has caused action or inaction in another by inducing in the latter an assumption of fact with legal consequences cannot, as regards the person in whom he has induced the assumption, seek to disprove that assumption, if it would be unfair or unjust for him to do so.<sup>15</sup> By contrast, implied contract operates to create an unexpressed promise in a contract in order to give the contract business efficacy<sup>16</sup> or to prevent it from being 'inefficacious, futile and

12 (1855) 5 HLC 389; 10 ER 950.

13 (1855) 5 HLC 389; 10 ER 950.

14 (1855) 5 HLC 389, at 413-414; 10 ER 950, at 960.

15 *Grundt and Others v The Great Boulder Proprietary Gold Mines Limited* (1937) 59 CLR 641, at 674-676, per Dixon J. This article is not concerned with the doctrine of promissory estoppel.

16 *Liverpool City Council v Irwin and Another* [1977] AC 239; *Edelfa Construction Proprietary Limited v State Rail Authority of New South Wales* (1982) 149 CLR 337.

absurd'.<sup>17</sup> There is no promise involved in estoppel by representation of fact, whereas the promise is the essence of the implied contractual term.

However, it should be noted that in *Swan v The North British Australasian Company (Limited)*,<sup>18</sup> Cockburn CJ rejected the view that *Young* was a decision on estoppel, and inclined to the view that it was based on the tort of negligence, saying:<sup>19</sup>

It was held, *not* that the customer was *estopped* from denying that the cheque was a forgery, but that, as the loss which would otherwise fall on the banker, who had paid on a bad cheque, had been brought about by the negligence of the customer, the latter must sustain the loss. As the question arose on an account submitted to arbitration, the matter was decided without reference to any technicality; but I am disposed to think that, technically looked at, the matter would stand thus: the customer would be entitled to recover from the banker the amount paid on such a cheque, the banker having no voucher to justify the payment; *the banker, on the other hand, would be entitled to recover against the customer for the loss sustained through the negligence of the latter.*

Possibly, *to prevent circuity of action*, the right of the banker to immunity in respect of the loss so brought about would afford him a defence in an action by the customer to recover the amount. . . .

With respect, Cockburn CJ appeared to invent two separate, sequential actions: an action by the customer against his bankers for payment from the account without the customer's authority, to be followed by an action by the bankers against the customer for the latter's negligence in misleading the bankers into making the payment. Then, 'to prevent circuity of action', the bankers' action in negligence would be brought forward in time to provide an effective defence against the customer's action for the wrongful debiting of his account. But there is a logical difficulty in Cockburn CJ's exposition. There would have been no cause of action by the bankers unless they had suffered loss. There would have been no such loss unless the customer had succeeded in his action against the bankers. But if the customer had succeeded, then the bankers would have breached their contract with their customer. Their loss would flow from their own breach of contract. It would be a self-contradiction to say that the bankers' loss flowed from their breach of contract as well as from the customer's tort of negligence against them. The issue of whose fault it was must logically be resolved in the customer's action against his bankers for breach of contract. The parties in *Young* were not consecutively at fault. Thus, it was incongruous for Cockburn CJ to state, in effect, that the customer in *Young* was liable in tort to his bankers for negligently causing the latter to breach their contract with him. It was incongruous because the court would have had to hold that the innocent party in a breach of contract was himself liable to the guilty party for the very breach which, *ex hypothesi*, would have had to have been caused by the guilty party. In relation to the one and the same act, namely, the payment of the forged cheque, the bankers could not have been at fault if their action had been negligently caused by their customer (as was in fact the case). In *Young*, therefore, the bankers had not breached their contract. Consequently, the circuity of action, supposed

<sup>17</sup> *Liverpool City Council v Irwin and Another* [1977] AC 239, at 262, per Lord Salmon.

<sup>18</sup> (1863) 2 HLC 175; 159 ER 73.

<sup>19</sup> (1863) 2 HLC 175, at 189-190; 159 ER 73, at 79. Emphasis added.

by Cockburn CJ to exist, and which he was so determined to prevent, could never have existed. The bankers had not made an unauthorized payment, namely, they had not breached their contract because their customer was precluded by his own negligent inducement from proving that the payment was unauthorized. Nonetheless, Cockburn CJ had introduced a germ of doubt into the true principle in *Young*, which otherwise would have remained a simple case of estoppel. Notwithstanding Cockburn CJ's opinion, in *Arnold and Others v The Cheque Bank*,<sup>20</sup> Lord Coleridge CJ strongly supported the view that *Young* was a case on estoppel.<sup>21</sup>

In *Scholfield v The Earl of Londesborough*<sup>22</sup> (hereinafter *Scholfield*) the House of Lords refused to extend the principle in *Young* to make the acceptor of a bill of exchange liable to future indorsees of the bill. However, their Lordships made some observations on *Young*.

Lord Halsbury LC, after lamenting that *Young* was a case of 'inextricable confusion',<sup>23</sup> was prepared to regard with an open mind the suggestion that it might have been a decision on estoppel, saying:<sup>24</sup>

. . . If, to use Lord Cranworth's<sup>25</sup> phraseology, the customer by any act of his has induced the banker to act upon the document by his act or neglect of some act usual in the course of dealing between them, it is quite intelligible that he should not be permitted to set up his own act or neglect to the prejudice of the banker whom he has thus misled, or by neglect permitted to be misled.

Lord Watson<sup>26</sup> and Lord Macnaghton<sup>27</sup> were both minded to perceive a dichotomy of approaches in the judgments in *Young*:

- (1) that the customer was *estopped* from proving that the cheque was a forgery; or alternatively,
- (2) that the customer had *actually* authorized the amount in the cheque, *as raised*.

The second alternative is problematical. Since it was not disputed that the clerk in *Young* had no actual authority to raise the original amount in the cheque, the authorization attributed to the customer by the Court in *Young* could have been produced by estoppel only.

Of even greater significance (because of its potential for confusion) is the following statement from Lord Watson:<sup>28</sup>

. . . If, on the other hand, the decision in *Young v Grote* was based upon the ratio that the customer, in filling up the cheque through his wife, whom he had constituted his agent for that purpose, had failed in the duty which he owed to his banker by giving facilities for its fraudulent alteration, I am not prepared to affirm that it cannot be supported by authority. But it does not, in my opinion, necessarily follow that the same rule must be applied between the acceptor of a bill of exchange and a holder acquiring right to it after acceptance. *The duty of the customer arises directly out of the contractual*

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20 (1876) 1 CPD 578.

21 Ibid at 586-587.

22 [1896] AC 514.

23 Ibid at 522.

24 [1896] AC 514, at 523-524.

25 A reference to Lord Cranworth LC's comment on *Young* in *Evans' Charities*. See note 14.

26 [1896] AC 514, at 535-536.

27 [1896] AC 514 at 544-546.

28 [1896] AC 514, at 536-537. Emphasis added.

relation existing at the time between him and the banker, who is his mandatory. There is no such connection between the drawer or acceptor and possible future indorsees of a bill of exchange.

The duty of the customer described by Lord Watson is his duty not to mislead his banker on the mandate which he gives to the latter, this 'duty' being merely a compendious way of stating the principle of estoppel. This duty 'arises directly out of' the contractual relation because the customer's cheque will not mislead the banker who pays it unless the banker happens to be the customer's banker, namely, unless there is a contractual relation between the two parties. But to say this is not to suggest that this duty, for the existence of which the contract clearly supplies the condition precedent, is one which has been created in the contract itself. To suggest that this particular duty of the customer is a contractual term is to propound the inexplicable proposition that estoppel is created by implied contract. Estoppel by representation is designed to prevent unjust departures by persons from assumptions of fact which they have induced in others, whereas implied contract is designed to achieve business efficacy for contracts. Business efficacy is a far more stringent test than that applied to determine the existence of estoppel. It has been declared by the High Court that it is 'absurd'<sup>29</sup> to attempt to prevent estoppel by means of a contractual provision. It would be equally absurd, by parity of reasoning, to attempt to create estoppel by means of a contractual provision (express or implied). Apart from conceptual absurdity, it would restrict the scope of estoppel in a contractual situation to require the party, otherwise entitled to rely on estoppel, to prove additionally that the contract would become 'inefficacious, futile and absurd'<sup>30</sup> unless the duty not to mislead the banker was incorporated as a contractual term—a very heavy burden of proof. Such an additional burden would be very heavy because it would be consistent with the business efficacy of the banker/customer contract not to require the customer to make the promise not to mislead, and the banker would be unable to demonstrate that the contract would be unworkable without such a promise by the customer. However, there is no legal principle which prescribes that the absence of such a term operates to disable the banker from recourse to the law of estoppel. Consequently, Lord Watson should not be understood as stating the view that the liability of the customer in *Young* was found in an implied contractual term. Indeed, only four months before his speech in *Scholfield*, Lord Watson himself, in *Ogilvie v West Australian Mortgage and Agency Corporation, Limited*,<sup>31</sup> had said that estoppel was based on 'the rules of fair dealing between man and man',<sup>32</sup> namely that it was based on the need to avoid unfairness in human conduct, rather than on the need to give business efficacy to a commercial contract.

29 *Craine v The Colonial Mutual Fire Insurance Company Limited and Another* (1920) 28 CLR 305, at 326, per Isaacs J, delivering the judgment of the High Court (Knox C J, Isaacs and Starke JJ).

30 *Liverpool City Council v Irwin and Another* [1977] AC 239, at 262, per Lord Salmon.

31 [1896] AC 257.

32 *Ibid* at 269.



One of the landmarks in this area of the law is *The Kepitigalla Rubber Estates Limited v The National Bank of India, Limited*<sup>33</sup> (hereinafter *Kepitigalla*). In this case the customer's secretary had forged seven of its cheques totalling £2,400. The bank having debited its customer for this amount, the latter sued for its recovery in an action for money had and received, on the ground that the cheques had been paid from the customer's account without his authority. The bank replied that the customer was estopped from proving that the cheques were forged because it had failed to supervise its secretary properly, and that it had also failed to examine properly its pass-book thereby causing the bank to be misled into believing the cheques to be genuine. Senior counsel for both the customer (J A Simon KC) and the bank (Scrutton KC) made their respective submissions on the basis that estoppel<sup>34</sup> was the sole issue between the parties. It was therefore something of a surprise to find that the judge in the case, Bray J, delivered a judgment in which there was no reference to estoppel. It is submitted that the following passage in Bray J's judgment shows that his Lordship fundamentally misunderstood the bank's submission:<sup>35</sup>

... It amounts to a contention on the part of the bank that its customers impliedly agreed to take precautions in the general course of carrying on their business to prevent forgeries on the part of their servants. Upon what is that based? It cannot be said to be necessary to make the contract effective. It cannot be said to have really been in the mind of the customer, or, indeed, of the bank, when the relationship of banker and customer was created. What is to be the standard of the extent or number of the precautions to be taken? Applying it to this case, can it be said to have been in the minds of the directors of the company that they were promising to have the pass-book and the cash-book examined at every board meeting, and to have a sufficient number of board meetings to prevent forgeries, or that the secretary should be supervised or watched by the chairman? If the bank desire that their customers should make these promises they must expressly stipulate that they shall.

At no stage did counsel for the bank even remotely suggest that the obligation of the customer not to mislead the bank into believing the forged cheques to be genuine was to be found in an implied term in their contract. Furthermore, counsel for the customer did not find it necessary to submit that there was no such implied term. This was because implied contract was not an issue between the parties: the customer was concerned to argue that it was not estopped whilst the bank argued that the customer was estopped. Bray J found in favour of the customer, but not on the ground that it had not been estopped. His Lordship found that the ground on which the customer succeeded was that the business efficacy of the contract did not require the customer to promise that it would not mislead the bank into the belief that its forged cheques were genuine.

The defect in Bray J's decision is that his Lordship failed to notice the issue of estoppel, and therefore omitted to discuss it. Because the issue in the case was erroneously identified by him as one of implied contract, and not as one of estoppel, *Kepitigalla* now stands as a

33 [1909] 2 KB 1010. *Kepitigalla* was followed by the Court of Appeal of New Zealand in *National Bank of New Zealand Ltd v Walpole and Patterson Ltd* [1975] 2 NZLR 7.

34 Ibid at 1017-1020.

35 [1909] 2 KB 1010.

monumental obstruction to the rational development of the law of estoppel regarding the customer's conduct towards his bank.<sup>36</sup>

Apart from an examination of (the wrong) principle, Bray J also ruled that there was no authority for the proposition that a customer must, in the course of carrying on his business, take reasonable precautions to prevent his servants from forging his signature.<sup>37</sup> It is, of course, true that there was no authority expressed in such specific terms. However, there was no reason why the law of estoppel should have been, in effect, arbitrarily restricted by Bray J to the customer's negligence in the mode of *drawing* his cheque, and not be allowed to apply to his *other* forms of negligence, in relation to his duty to conduct himself in such a way as to avoid misleading his bank into believing his forged cheques to be genuine.

No examination of this area of the law could omit an appraisal of *London Joint Bank Limited v Macmillan and Arthur*<sup>38</sup> (hereinafter *Macmillan*). This was a case in which the customers' clerk fraudulently raised the value of the customers' cheque from £2 to £120 by inserting additional words and figures in spaces left in the cheque by the customers. The bank debited the customer's account for £120, whereupon the customers sought a declaration that the bank was entitled to debit their account for £2 only, and not the fraudulently raised sum of £120. Given that the facts in *Macmillan* were so strikingly similar to those in *Young*, the issue became whether *Young* had been correctly decided. Both Sankey J and the Court of Appeal had held that *Young* had been wrongly decided.<sup>39</sup> The House of Lords unanimously reversed the decision of the Court of Appeal, by approving and applying *Young* to find in favour of the bank. Nevertheless, although it was quite unnecessary for their decision, both Lord Finlay LC<sup>40</sup> and Viscount Haldane<sup>41</sup> expressed their approval of Bray J's decision in *Kepitigalla*. The other two members of the House in the case, Lord Shaw of Dunfermline and Lord Parmoor, made no reference to that case. The incongruity of restricting the customer's duty, not to mislead his banker on his mandate, to the mode of issuing that mandate may be noticed in the following illustration of Lord Finlay himself:<sup>42</sup>

... If the door of a warehouse is left unlocked at night, the goods may be stolen, and if a cheque *is drawn* with neglect of all usual precautions to prevent falsification, the cheque may be falsified. The loss in each case is the result of the omission of ordinary and reasonable precaution. ...

If, as Lord Finlay is at pains to assert, it is negligent to leave the door of a warehouse unlocked at night because this may lead to the theft of the goods therein, why would it not be equally negligent to leave a cheque book on a table in an open office so that cheque forms may be stolen from it and the customer's signature forged thereon? Would it not

36 It should be noted that Bray J said, *Obiter*, that even if there had been a duty on the customer to take reasonable precautions to prevent the bank from being misled, such precautions had been taken by the customer in this case: [1909] 2 KB 1010, at 1026.

37 [1918] AC 777.

38 [1918] AC 777.

39 *Ibid* at 787.

40 [1918] AC 777 at 801.

41 [1918] AC 777 at 815-816.

42 [1918] AC 777 at 794. *Emphasis added*.

constitute "the omission of ordinary and reasonable precaution"<sup>43</sup> for the customer to leave his cheque forms so easily accessible to such rogues as may be disposed to misuse them? What legal principle is there to support the view that a customer who carelessly permitted his signature to be forged on his cheque form ought to be placed in a more favourable position than one who signed his cheque form but carelessly permitted another to fill in the resulting blank cheque? None. Yet Lord Finlay LC<sup>44</sup> and Viscount Haldane<sup>45</sup> would, as regards the customer, exclude the law of estoppel from the customer's conduct in the case of the forged signature on the cheque, only to apply the same law against him in the case of the forged amount on the cheque. To quote Viscount Haldane:<sup>46</sup>

... Thus a man may be imprudent in leaving his cheque-book and pass-book in the hands of his clerk, who is thereby enabled to forge a cheque. But he is not liable, for this reason, that the direct and real cause of the loss is *the intervention of an act of wickedness* on the part of the clerk, which the law does not call on him to anticipate in the absence of obvious ground for suspicion. . . .

With respect, Viscount Haldane's explanation proves too much. If 'the intervention of an act of wickedness on the part of the clerk'<sup>47</sup> was sufficient to protect the customer from liability in estoppel, then *Macmillan* itself would have been decided the other way, because the fraudulent alteration of the customer's cheque by their clerk was a perfect example of 'the intervention of an act of wickedness on the part of the clerk'.<sup>48</sup> Moreover, Viscount Haldane's illustration was specifically contradicted by Lord Finlay LC, who said:<sup>49</sup>

... [I]f a customer in drawing a cheque neglects reasonable precautions against forgery and forgery ensues, he is liable to make good the loss to the banker, and that *the fact that a crime has to intervene* to cause the loss does *not* make it too remote. *Indeed, forgery is the very thing against which the customer is bound to take reasonable precaution.* . . .

It is rather difficult to follow how Lord Finlay, who declared that forgery was the 'very thing'<sup>50</sup> against which the customer was bound to take reasonable precaution, could, without inconsistency, have also declared in the same speech that the customer had no duty to take reasonable precaution against the forgery of his signature on his cheque forms.<sup>51</sup> Why would it be culpably careless for the customer to facilitate the forgery of the amount in his cheque, but, by contrast, be permissibly careless for him to facilitate the forgery of his signature on his cheque form? It is submitted that this forced dichotomy in *Macmillan*, supported by Lord Finlay LC and Viscount Haldane, is conceptually inexplicable. This dichotomy cannot be more poignantly lamented than in the following words of Lord Devlin, uttered in a rather different context:<sup>52</sup>

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43 Ibid.

44 [1918] AC 777 at 795.

45 [1918] AC 777 at 815-816.

46 Ibid. Emphasis added.

47 Ibid.

48 Ibid.

49 [1918] AC 777 at 810-811.

50 Ibid.

51 [1918] AC 777 at 795.

52 *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 465, at 517.

. . . I am bound to say, my Lords, that I think this to be nonsense. It is not the sort of nonsense that can arise even in the best system of law out of the need to draw nice distinctions between borderline cases. It arises, if it is the law, simply out of a refusal to make sense. The line is not drawn on any intelligible principle. . . .<sup>53</sup>

The nonsense is easily illustrated. An employer signs a blank cheque, intending to deliver it to a trusted employee. In tearing off this (signed) blank cheque he accidentally also removes a cheque form, without noticing that he has done the latter. Thinking that he has only the blank cheque in his hand, but in fact holding both the blank cheque *and* the cheque form, he delivers to his trusted employee these two documents in the belief that he was delivering the blank cheque only. Subsequently, the employee fills in the blank cheque for an unauthorized amount, and forges the employer's signature on the cheque form for the payment of a sum of money. The two 'cheques' are made payable to the employee or bearer. The employee cashes the 'cheques' and absconds with the proceeds. Assume that the amount payable on each 'cheque' was \$10,000. The employer's bank debits his account for \$20,000. Now, if *Keptigalla* is good law, and the duty not to mislead is thus restricted to the drawing of cheques by the customer, then the employer will bear the loss for the \$10,000 stolen through the forged amount in the blank cheque, because he was negligent in his mode of drawing it, but, in respect of the \$10,000 stolen through the forgery of the employer's signature on the cheque form, this loss will have to be borne by the bank, because the employer (customer) was not negligent in any mode of drawing the cheque form, he not having drawn the second 'cheque'.

A decision of major importance which demonstrates that the duty of the customer not to mislead his bank on the matter of his mandate is not restricted to the mode of issuing that mandate is *Greenwood v Martins Bank Limited*<sup>54</sup> (hereinafter *Greenwood*). The customer's wife had forged forty-four of the customer's cheques totally £410.6s. After the bank debited his account for this sum, the customer sought a declaration that he was entitled to be credited in his account with this sum because the bank, in paying the cheques, had acted without his authority. The customer had known about the withdrawals made under these forgeries because his wife had told him about them, giving him a false explanation as to why she had perpetrated them, and asking him not to apprise the bank of these forgeries. The customer complied with his wife's request, and did not tell the bank about these forgeries until after his wife's suicide, when, as the law of England then stood,<sup>55</sup> the bank lost its right to sue the customer's wife as well as the customer himself for his wife's tort.

The sole issue<sup>56</sup> before the House of Lords was whether or not the customer was estopped by his conduct from relying on the fact that his cheques had been forged. The House held that he was so estopped.

53 In *Commonwealth Trading Bank of Australia v Sydney Wide Stores Pty Ltd and Another* (1981) 55 ALJR 574, the High Court followed the ratio decidendi in *Macmillan* (namely, its approval of Young), but made no allusion to the principle established in *Keptigalla*.

54 [1933] AC 51.

55 A husband's liability for his wife's tort has been generally abolished by statute. Thus, today the customer in *Greenwood* would not be liable for his wife's tort: *Law Reform (Married Women and Tortfeasors) Act 1935* (UK), Section 3.

56 [1933] AC 51 at 57.

Lord Tomlin, in whose speech the other law lords concurred, said:<sup>57</sup>

The appellant's silence, therefore, was deliberate and intended to produce the effect which it in fact produced—namely, the leaving of the respondents in ignorance of the true facts so that no action might be taken by them against the appellant's wife. The deliberate abstention from speaking in those circumstances seems to me to amount to a representation to the respondents that the forged cheques were in fact in order, and assuming that detriment to the respondents followed there were, it seems to me, present all the elements essential to estoppel. . . .

Thus the House simply applied the law of estoppel. The House did not thereby merely add another specific limited duty to the supposedly limited duty of the customer to exercise care when drawing his cheques, the latter being the view of Lord Finlay LC and Viscount Haldane in *Macmillan*. Rather than regard *Macmillan and Greenwood* as two discrete duties imposed on the customer, each with its own factual limitation, these 'two' duties are conceptually no more than particular illustrations of the principle of estoppel, a principle thus expounded by Dixon J:<sup>58</sup>

. . . The principle upon which estoppel *in pais* is founded is that the law should not permit an unjust departure by a party from an assumption of fact which he has caused another party to adopt or accept for the purpose of their legal relations. . . .

If it can be established that a customer has caused his bank to pay a forged cheque in the belief that it was his genuine order, then, the law of estoppel will preclude the customer from asserting the forgery. It is irrelevant whether that belief was caused by a cheque with a forged signature or by one with a genuine signature but a forged amount. This view appears to be entirely consistent with the position taken by Scrutton LJ in the Court of Appeal<sup>59</sup> in *Greenwood*, where his Lordship said:<sup>60</sup>

. . . the customer is held bound to use reasonable care in drawing the cheque so that the banker may not be misled. But the relation does not merely refer to one cheque; it is a continuing relation in which the customer may draw cheques from time to time, and the banker is under a continuing duty to honour mandates. This, in my view, involves a *continuing duty* on either side to act with reasonable care to ensure the proper working of the account . . .

It is submitted that Scrutton LJ's view is inconsistent with the restricted scope given to the customer's duty in *Kepitigalla*. Indeed, in his role as senior counsel for the bank in *Kepitigalla*, Scrutton KC (as Scrutton LJ then was) had put the same view to Bray J, who rejected it. Hence the inconsistency, except that the balance of authority was later reversed by Scrutton LJ. In *Kepitigalla*, Scrutton KC had unsuccessfully argued:<sup>61</sup>

. . . It is also the duty of a customer to his banker to take reasonable care in the carrying out of his business relating to the issuing of mandates. The mandate is a *continuing mandate*, namely, to pay the sums for which cheques are drawn from time to time, and care must be taken during the whole time. The duty of the customer is to take reasonable care to prevent the banker from being misled on each occasion. . . .

57 [1933] AC 51 at 58.

58 *Grundt and Others v The Great Boulder Proprietary Gold Mines Limited* (1937) 59 CLR 641, at 674. Emphasis added.

59 [1932] 1 KB 371.

60 *Ibid.*, at 380-381. Emphasis added.

61 [1909] 2 KB 1010, at 1017. Emphasis added.

This conflict between the judgment of Scrutton LJ in *Greenwood* and that of Bray J in *Kepitigalla* should be resolved in favour of Scrutton LJ, on both authority and principle. The acceptance of Scrutton LJ's view would allow estoppel to become recognized as the focus of the law in this area.

It is time to analyse the conundrum itself: *Tai Hing Cotton Mill Ltd v Liu Chong Hing Bank Ltd and Others*<sup>62</sup> (hereinafter *Tai Hing*). The customer (a company) had a current account with each of three banks. One of the persons authorized to sign for the customer was its managing director. An accounts clerk employed by the customer forged its managing director's signature on about three hundred cheques totalling HK\$5.5 million, which the banks paid and for which they debited the customer's accounts. The customer sought declarations that the banks were not entitled to debit its accounts in respect of the forged cheques. The banks replied in a rather curious way. Although they alleged that the customer was estopped by its misleading conduct towards the banks from relying on the fact that the cheques were forgeries, they further submitted that there was imposed on the customer a 'duty of care'<sup>63</sup> not to mislead the banks on its mandates, a duty which was imposed by an implied term in its respective contracts with the banks 'as well as'<sup>64</sup> by the law of tort. This contractual/tortious 'duty of care' was submitted to be either the wider duty of taking reasonable care to ensure that only properly drawn cheques were presented to the banks for payment or, at least, the narrower duty to check the periodic bank statements with reasonable care.<sup>65</sup> The banks also relied on an express term, in their respective contracts with the customer, which purported to bind the customer to the accuracy of such bank statements as it chose not to query. This last argument was rejected by the Privy Council on the ground that the express term in question was not 'clear and unambiguous'.<sup>66</sup>

The banks' submission on estoppel is curious because it had the effect of erecting the alleged contractual/tortious duty of care into an alternative remedy which was presented to be superior in scope to estoppel. Indeed, the gist of the banks' argument was that the alleged contractual/tortious duty of the customer, in contradistinction to the law of estoppel, supplied the banks with the dispensation from having to prove proximate cause between the customer's conduct and the banks' loss.<sup>67</sup> It will be no small undertaking to discover where the banks located their authority for saying:<sup>68</sup>

... proximate cause was required for estoppel, *which is still the law*, and also that proximate cause was required for negligence, *which is not now the law*. .

Thus the banks not only discarded the true basis of their remedy, namely, estoppel of the customer, but discarded it on the false basis that it would have been disadvantageous for them to have relied principally on it. With respect, there is no authority to support the view that a

62 [1986] 1 AC 80.

63 Ibid at 93.

64 Ibid.

65 [1986] 1 AC 80, at 92.

66 [1986] 1 AC 80 at 110.

67 [1986] 1 AC 80 at 91.

68 Ibid. Emphasis added.

customer who is blameless in his conduct towards the bank in the law of estoppel may, by dint of judicious pleading, nonetheless be drawn within the bounds of culpability by the bank. The bank cannot say to its customer : you have not been negligent in the law of estoppel and therefore you are not estopped from asserting that we debited your account without your authority, but although you have not been negligent in the law of estoppel, you have been negligent in the law of tort, and we are able to do this because it is easier to prove negligence in the law of tort than it is to prove negligence in the law of estoppel.

Given the tenor of the banks' submission, it should excite no surprise to find the Privy Council stating the issue as follows:<sup>69</sup>

. . . The question of general principle is as to the nature and extent of the *duty of care* owed by a customer to his bank in the operation of a current account.

Notwithstanding the previous authorities in this area, their Lordships did not think that the relevant general principle for this case was estoppel.

The Privy Council, speaking through Lord Scarman, proceeded to determine what had been decided by the House of Lords in *Macmillan*. Lord Scarman said that in *Macmillan* 'the House approved'<sup>70</sup> the judgment of Bray J in *Kepitigalla*. With respect, this is not accurate. Of the four members of the House who decided *Macmillan*, only Lord Findlay LC and Viscount Haldane approved *Kepitigalla*. The other members, Lord Shaw of Dunfermline and Lord Parmoor, made no reference to that case. Consequently, 'the House of Lords'<sup>71</sup> in *Macmillan* did not, as a House, approve *Kepitigalla*.

Lord Scarman also took occasion to propound the view that the customer's liability in *Macmillan* was based on his breach of an implied contractual term, saying:<sup>72</sup>

. . . Indeed, their Lordships read the speeches in *Macmillan's* case as proceeding upon the basis, which their Lordships have no doubt is correct, that the relationship between banker and customer is contractual and that its incidents, in the absence of express agreement, are such as must be implied into the contract because they can be seen to be obviously necessary.

It is one thing to say, incontrovertibly, that the relationship between banker and customer is contractual. But it is a totally different thing to declare, as Lord Scarman did,<sup>73</sup> that the House in *Macmillan* found the customer's duty not to mislead his bank within the four corners of his contract with his bank, and not in the law of estoppel which, although not itself contractual, was raised in the context created by the contract. Thus Lord Scarman should have recognized that the customer's liability in *Macmillan* was not found in the content, but in the context, of his contract with the bank. The test for the implication of a contractual term was nowhere alluded to in *Macmillan*, presumably because it was not relevant to their Lordships' reasoning in that case.

Having determined that all duties owed by the customer to his bank were contractual, Lord Scarman then entered upon the question of whether there was an implied term in the banker/customer contract which

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69 [1986] 1 AC 80, at 97. Emphasis added.

70 [1986] 1 AC 80, at 103. emphasis added.

71 Ibid.

72 [1986] 1 AC 80, at 104.

73 [1986] 1 AC 80, at 107.

imposed on the customer either the wider or narrower duty of care for the existence of which the banks had argued. His Lordship said: . . . 'the test of implication is necessity . . . '74

No doubt. But why was it necessary to find an implied contractual term to support the duty not to mislead? Of course, if estoppel were discarded in favour of implied contract, as was done, then it could very easily be said, as was said, that it was not necessary for the business efficacy of the banker/customer contract to imply a term therein to require the customer to take reasonable care not to mislead his bank on his mandates, because the absence of such a term would not render that contract 'inefficacious, futile and absurd'.75 Once the Privy Council had resolved to discover the customer's duties to his bank solely within their contract the failure of the banks in *Tai Hing* became inevitable.

Not content merely to remove *Macmillan* from the field of estoppel, their Lordships in *Tai Hing* ventured to say that not only *Macmillan*, but *Greenwood* as well, was a case on implied contract76 only, referring to the supposed respective contractual 'limits'77 set in *Macmillan* and *Greenwood*, and counselling banks, if they felt themselves in need of 'protection',78 to provide expressly for such protection. It is sufficient to point out that there was no hint of implied contract in *Greenwood*.

In respect of the submission by the banks that the wider duty, even if it could not be discovered in implied contract, could nonetheless be found in the law of tort, Lord Scarman said:79

Their Lordships do not believe that there is anything to the advantage of the law's development in searching for a liability in tort where the parties are in a contractual relationship. This is particularly so in a commercial relationship.

. . .

Their Lordships do not, therefore, embark on an investigation as to whether in the relationship of banker and customer it is possible to identify tort as well as contract as a source of the obligations owed by the one to the other. Their Lordships do not, however, accept that the parties' mutual obligations in tort can be any greater than those to be found expressly or by necessary implication in their contract. . . .

Be that as it may, why was it necessary in the first place to search for an implied contractual term to support the customer's duty not to mislead his bank, a 'duty' that is as old as the decision in *Young*?

Finally, Lord Scarman's treatment of the issue of estoppel in the case was by no means elaborate, his Lordship saying:80

Their Lordships having held that the company was not in breach of any duty owed by it to the banks, *it is not possible* to establish in this case an estoppel arising from mere silence, omission, or failure to act.

If the Privy Council in *Tai Hing* is correct on this last point, then, as between contracting parties, estoppel will be no more and no less than a contractually conferred right. There is neither principle nor authority

74 [1986] 1 AC 80, at 104.

75 *Liverpool City Council v Irwin and Another* [1977] AC 239, at 262, per Lord Salmon.

76 [1986] 1 AC 80, at 106 and 107.

77 *Ibid* at 106.

78 *Ibid*.

79 [1986] 1 AC 80, at 107.

80 [1986] 1 AC 80, at 110. Emphasis added.



(apart from *Tai Hing* itself) to support so conceptually disruptive a proposition. It is submitted that such a proposition is fundamentally wrong and should not be followed in Australia.

It is submitted that *Tai Hing* should have been decided in favour of the banks. It was not disputed that if the customer had been found to owe the banks the 'two duties'<sup>81</sup> asserted by the banks to exist, then those duties would have been breached. If the law of estoppel had been given its proper scope in *Tai Hing*, there would have been no reason why, undistracted by exegesis on implied contract and its interaction with tort, the gross and prolonged failure of the customer to supervise its accounts clerk would not have been seen to require it to be estopped from pleading the forged cheques which it had negligently caused the banks to believe to be its genuine orders.<sup>82</sup>

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81 [1986] 1 AC 80, at 103, per Lord Scarman.

82 *Grundt and Others v The Great Boulder Proprietary Gold Mines Limited* (1937) 59 CLR 641. See also n 58.