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Financial references, negligent misstatement and duty of care:
Playboy Club London Ltd v Banca Nationale del Lavoro SpA [2016] 2 B.C.L.C. 442

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Introduction

Playboy raised novel issues of whether a bank owed a duty of care to a casino for which the former had supplied a reference in relation to a customer who gambled at the latter, whether the scope of the duty related to counterfeit cheques presented by that customer, whether the casino's loss in being unable to cash the customer's cheques was caused by the bank's breach of duty and whether any claim should be reduced on account of contributory negligence by the casino in accepting patently bad cheques. The peculiarity of the case was the bank's use of an intermediary to obtain the reference.

Facts and first instance decision

B was a member of the claimant casino ("the club"). In 2010 B asked the club for a cheque cashing facility (CCF); a CCF allowed a customer to present a cheque and, before the cheque was cashed, obtain high-value gaming chips to an equivalent amount. The club in turn required a positive reference from B's bank, the defendant. The club's request for a reference was made by a separate company ("Burlington") since that was the club's standard practice to preserve confidentiality for customers preferring to keep their gaming activities private; Burlington had no employees or business of its own and was used only for administrative purposes. The bank gave a financial reference to Burlington:

> ("We confirm and certify that [B] maintains an account [number] with us to our satisfaction and he is financially healthy and capable to meet his business commitments and all his obligations … and is trustworthy up to £1.6m in any one week.")

and the club approved the CCF, allowing B to present cheques in return for gaming chips. In fact, while B had applied for an account with the bank at the date of the reference, the bank had never received any funds from B. When the club sought to cash two cheques in the sum of £1.25m that B had presented they were returned unpaid on the ground that they were counterfeit; in other words, not genuine cheques drawn on B's account but photocopies signed by B and stamped with his bank account number. The club was unable to trace B and as a result it was out of pocket in the amount of just over £800,000.

The club raised proceedings against the bank to recover its losses. At the trial the bank did not call the employee who had signed the reference but it emerged that she had been dismissed for misconduct. The judge at first instance ([2014] EWHC 2613 (QB) at [1]) described the action as the

> "conventional case where two innocent parties disagree about which of them should be responsible for the consequences of a disreputable third party, except that it seems that [B] was assisted by an employee of the [Bank]".

He found that the bank was responsible for the reference (whether by the doctrine of apparent authority or vicarious liability) since it had been issued through a conventional channel in circumstances that would not have put a third party on inquiry. He then held that the bank owed a duty of care not just to the separate company that had asked for the reference but also to the club because there had been no attempt to limit liability to the inquirer and because there had been no evidence that if the reference had been sought by the club the bank would have behaved differently. On that basis he found that the bank had breached its duty of care and, but for the reference, the club would not have accepted the cheques. He found that the fact that the cheques were counterfeit did not break the chain of causation but also found the club contributorily negligent to the extent of 15 per cent because the cheques looked odd on their face. He awarded the club the sum claimed less the 15 per cent deduction.

The bank appealed. Although it had appealed originally from the findings on apparent authority and vicarious liability, that was not pursued in light of the Supreme Court's reaffirmation of the "close connection" test in *Mohamud v Wm Morrison Supermarkets Plc* [2016] A.C. 677 in respect of wrongdoing by an employee in the course of his employment (this is perhaps surprising since the employee's conduct was an extreme example of deliberate wrongdoing in relation to the bank as well as the club). The basis of the bank's appeal was that its duty of care did not extend beyond Burlington to the club, that the scope of its duty extended only to the giving of the reference and not to the giving of obviously bad cheques by its customer; the club's own negligence in relation to the cheques broke the chain of causation or the degree of contributory negligence was far greater than 15 per cent. The club argued that the duty of care in giving a reference extended to any person for whom Burlington was acting even if the bank did not know that person's identity; the judge had correctly applied the "but for" test of causation so that the scope of the duty (i.e. the fact that the means of the fraud was counterfeited cheques) was irrelevant; there was no novus actus on the part of the club breaking the chain of causation and the finding on contributory negligence was reasonable.

The law

The starting point for liability for negligent misstatement is *Hedley Byrne Ltd v Heller & Partners Ltd* [1964] A.C. 465. Also a banker's reference case, the bank, Heller & Partners, gave a reference for their customer at the request of a bank acting for advertising agents, Hedley Byrne, who were personally liable for the price of advertising space they were purchasing on behalf of the bank's customer. The reference stated that the bank considered its customer "good for its ordinary business engagements". The customer went into liquidation and the advertising agents were liable for the costs of the advertising. The bank's argument before the House of Lords was that, in addition to English law not recognising liability for economic loss for negligent misstatement, it only owed a duty to the other bank, not its unidentified customer. Lord Reid said that, as the bank knew that the inquiry was in relation to an advertising contract, he would treat the case as though the misrepresentation had been made directly to the advertising agents and he did not attempt to decide "what kind of degree of proximity is necessary before" a duty can be owed (482). Lord Morris noted that this issue was not important because it was

> "inherently unlikely that the bank would have entertained a direct application from Hedleys asking for a report or would have answered an inquiry made by Hedleys themselves" (493).

The basis for liability was a special relationship between the advisor and advisee. Following *Caparo Industries Plc v Dickman* [1990] 2 A.C. 605, it has become customary when determining whether a duty of care exists to ask: (1) whether the defendant assumed responsibility to the claimant; (2) whether loss was a foreseeable consequence/sufficiently proximate relationship/fair just and reasonable to impose the duty of care; and (3) whether the addition to existing categories of duty is incremental rather than indefinable. It is also customary to use the three tests as cross-checks on each other.

The Court of Appeal (Laws, Longmore and David Richards LJJ):
The appeal was allowed. Longmore LJ noted that the factual difference between *Playboy* and *Hedley Byrne* was that the bank knew the identity of the customer but nothing of the purpose for which the reference was required, whereas in *Hedley Byrne* the bank did not know the identity of the customer seeking the reference but did know the purpose, and he asked whether it was a relevant legal distinction [15]. In deciding that it did, he noted Lord Hoffmann in *Customs and Excise Commissioners v Barclays Bank Plc* [2007] 1 A.C. 181 at [35] that in cases in which loss had been caused by the claimant's reliance on information provided by the defendant,

> "it is critical to decide whether the defendant assumed responsibility for the accuracy of the information to the claimant or for its use by the claimant for the one purpose".

Longmore LJ said that in the circumstances where the true purpose of the reference was not revealed there could not have been an assumption of responsibility to the club (rather than Burlington) for the use of the reference in trusting B in his gambling activities. Further, the special relationship did not extend past Burlington to the club. And finally, he found that where the club had kept its identity secret by using Burlington it was not fair, just and reasonable to impose liability, nor was there a proximate relationship for the same reason [24].

The bank also argued that any duty of care only extended to the giving of a reference as to B's creditworthiness and not as to whether he was the sort of person who would not present counterfeit cheques. The judge had accepted that the reference did not refer to B's general trustworthiness so the bank argued that, where the loss had arisen from the counterfeit cheques rather than the absence of funds in the account, the scope of the bank's duty was not to protect the club from accepting counterfeit cheques (by reference to *South Australia Asset Management Corporation v York Montague Ltd* [1997] A.C. 191, Lord Hoffman at 213:

> "Normally the law limits liability to those consequences which are attributable to that which made the act wrongful. In case of liability in negligence for providing inaccurate

information, this would mean liability for the consequences of the information being wrong").

However, the judge had said that but for the reference the club would not have accepted the cheque; Longmore LJ agreed at [28], saying that the consequence of the inaccurate information was that the club extended credit to an impecunious gambler and the problem of the bounced cheques only became problematic because the club had relied on the reference. Had he found that a duty of care existed he would have found causation established [28].

Conclusion

The peculiarity of this case was the club's use of an intermediary to obtain the reference. The judge at first instance and the Court of Appeal fundamentally disagreed about how established principles applied to the case, with the former seeing it as of no significance whereas the latter considered it to be the critical factor against the imposition of the duty of care. It is not clear whether the case will establish a precedent that liability is restricted to the known recipient of the reference, particularly where Lord Reid in Hedley Byrne had declined to proscribe what kind of degree of proximity was necessary before a duty could be owed.