KEY POINTS

- Direct debit schemes in Europe, including the schemes promoted by the European Payments Council for the Single European Payment Area, differ in some respects from the English direct debit scheme.
- The decision of the Netherland Supreme Court relating to a Dutch national direct debit scheme has identified circumstances in which the right of return can be exercised by banks for their benefit when an account holder becomes insolvent.
- Similar rights appear to exist under the European direct debit schemes with which banks in the UK are likely to become increasingly familiar, although the exact scope of the rights is not certain.

Feature

Author Elizabeth Ovey

The right of return: a new sort of money back guarantee for banks?

A recent decision of the Netherlands Supreme Court offers some interesting pointers to the possible effect of the Single European Payments Area (SEPA) business to consumer direct debit scheme (the Core Direct Debit scheme) and the SEPA business to business direct debit scheme (the B2B Direct Debit scheme).

INTRODUCTION

On 16 September 2011 the Netherlands Supreme Court gave judgment in the *SNS Bank v Pasman* case (LJN BQ 8732 SNS Bank/Pasman). The case concerned the right of a paying bank under the Dutch direct debit scheme to reverse a previously executed direct debit transaction without having to give one of a number of specified reasons for doing so.

At first sight, the case seems to have little relevance for English lawyers, since the Dutch direct debit scheme is different from the English one. The English scheme confers no such right on a paying bank. But there are several reasons why an English lawyer might find the case of some interest:

- although a right of this nature is not required by the Payment Services Directive (Dir 2007/64/EC), a similar right is currently included in the Single European Payments Area (SEPA) Core Direct Debit scheme, which is operated by a number of banks conducting banking business in the UK that engage in cross-border transactions denominated in euro. Indeed, a bank which is a member of the European Payments Council is obliged to offer such a service. The current version of the SEPA rule book took effect on 19 November 2011 (after both the Payment Services Directive and *Pasman*). Such a right also appears in the SEPA B2B Direct Debit scheme, which is optional;
- the European Commission wishes to ensure broad public support for the SEPA project and is currently conducting a review of the Payment Services Directive. Further, in February 2012 the European Parliament decided that direct debit transactions in euro and conducted in the euro zone would have to be in accordance with the SEPA requirements by 1 February 2014. Transactions in euro but outside the euro zone will have to comply with SEPA requirements by 1 October 2016;
- as *Pasman* shows, such a right may benefit the paying bank.

THE FACTS

The payer in the *Pasman* case was a company called Vetrans which had an overdraft with SNS Bank. It had given a direct debit mandate pursuant to which payments were made out of Vetrans' account with SNS Bank. The payments increased the amount of the overdraft but did not cause the overdraft limit to be exceeded. A few days later Vetrans was declared bankrupt. SNS Bank then exercised its right to reverse the payments, thus reducing the amount of Vetrans' overdraft again.

Vetrans' bankruptcy trustee claimed the amount of the direct debit payments from SNS Bank on two grounds:

- that, in effect, by reversing the payments the bank had created post-bankruptcy debts owed by it to Vetrans which could not be set off against Vetrans' indebtedness to the bank; and
- the bank had committed a tortious act in reversing the payments and was liable to Vetrans in damages.

The terms of the relevant Dutch direct debit scheme provided that when a direct debit payment was collected the account of the payee was credited and the account of the payer was debited with the amount of the direct debit subject to a condition subsequent with retroactive effect permitting the payer's bank, either on its own initiative or at the request of the payer, to require the reversal of the transaction. The payee's bank was obliged to accept such a reversal, irrespective of the reason given, if initiated within a specified time limit.

THE DECISION

It appears that the Netherlands Supreme Court had already held, in *Mendel v ABN Amro* (NJ 2005, 200) decided on 3 December 2004, that the reversal of a direct debit did not constitute a payment followed by a repayment but an administrative act of bookkeeping. This conclusion was based on conditions which made the crediting of the payee's account subject to a condition precedent, but did not contain a similar provision in relation to the debiting of the payer's account. The Supreme Court, however, found no difficulty in holding that the debiting of the payer's account was equally subject to a condition subsequent. The result was that when the condition was fulfilled the legal consequence was that the payment was effectively treated as never having been made, so that questions of set-off did not arise. The level of

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Vetrans' indebtedness was as it had been before the payments were purportedly made.

The concept that the reversal might have been tortious is not easy for an English lawyer to follow, given that the relevant clause in the scheme did not appear to impose any limitations on SNS Bank's right to reverse the transaction. If the intention had been to limit the right to cases where there were insufficient funds in the relevant account to meet the payment or where an overdraft limit would be exceeded, it would have been easy for the clause so to provide.

The approach of the Netherlands Supreme Court, however, was a little more nuanced than such an analysis would suggest. The court recognised that the right was expressed in general terms and was not limited in any such way, and said that in principle a bank was entitled to exercise the right to protect its own interests. Nevertheless, the court added that "in exceptional circumstances" the exercise of the right could constitute an abuse, in which event the reversal could be successfully challenged.

It is unclear what might constitute exceptional circumstances for this purpose, although it must follow from the decision in the case itself that the simple fact that the payer has been declared bankrupt or that the payment did not cause an overdraft limit to be exceeded is not sufficient to constitute an exceptional circumstance giving rise to an abuse. One possibility is that the court had in mind the case where the bank concerned has sufficient security elsewhere to recover the debt it is owed. In such circumstances, the exercise of the right would not ultimately benefit the bank but would have the effect of turning a creditor who had apparently been properly paid into an unpaid creditor.

COMPARISON WITH SEPA DIRECT DEBIT SCHEMES

The terms and conditions of the SEPA Core Direct Debit scheme, although different from the Dutch national scheme in some details, appear similar in principle. Thus, in general the payment will be credited and debited and settlement between the banks concerned will be made on the due date for payment and that will be that. There are, however, various circumstances in which the process is not followed or, having been followed, is reversed. These are called "R-transactions". R-transactions include "Refunds", when the payer, after settlement, asks his bank to undo the transaction, and "Returns", when the payer's bank itself seeks to undo the transaction.

The terms and conditions give the payer an unrestricted right for eight weeks to request a refund even where the debit has been made strictly in accordance with the authority given by the mandate. This appears to be a form of consumer protection and is one of the matters which the European Commission is considering with a view to possible adoption in a revised Payment Services Directive. The protection is typically given under schemes which impose limited checking obligations on the payer's bank.

More relevantly for present purposes, the terms and conditions also give the payer's bank a right to make a return within five business days of settlement. A reason code must be specified, but the codes include "reason not specified". In practice, therefore, it seems that the SEPA Core Direct Debit scheme offers banks a right similar to that under the Dutch scheme.

The SEPA B2B Direct Debit scheme does not give the payer a right to a refund of a payment made in accordance with the authority given by the mandate. It does, however, contain a right of return for the payer's bank, albeit within the shorter time limit of two business days. Again, then, the SEPA B2B Direct Debit scheme offers banks a right similar to that under the Dutch scheme.

> "The banks' right of return does not appear to form the basis for an express condition subsequent in the same way as in the *Pasman* case."

APPLICATION OF *PASMAN* CASE TO SEPA DIRECT DEBIT SCHEMES

The question which then arises is how far the approach of the Netherlands Supreme Court will be applied by courts dealing with transactions under the SEPA Direct Debit schemes. If and when amendments are made to the Payment Services Directive, some answers may emerge. As matters stand, however, the position is not entirely clear.

First, the banks' right of return does not appear to form the basis for an express condition subsequent in the same way as in the *Pasman* case. Nevertheless, many of the other reasons for a return (eg technical or regulatory bars, closure of the account, insufficient funds) tend to suggest that the payment may have been made when it ought not to have been made and point to the administrative bookkeeping explanation of a return. It would be surprising if a return made on one of those grounds was treated as administrative bookkeeping while a return on another ground was treated as something different. It therefore seems likely that the *Pasman* approach would be adopted.

Rather more uncertain, however, is the scope of a possible abuse argument based on "exceptional circumstances", as envisaged by the Netherlands Supreme Court. As already noted, the exercise of the right of return protects the bank's position to the detriment of another creditor, whose payment would *prima facie* have been unchallengeable if it had been made by a different method. This potentially raises policy issues about the impact of a right of return in such circumstances on the general principles of insolvency law. It will be interesting to see whether the SEPA Direct Debit schemes continue to offer a generally expressed right of return for no specified reason and if so whether any limits come to be applied to the circumstances in which that right may be exercised. ■