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**The WTO US-PRC UnionPay Dispute:  
Bringing the Back Office Front & Center**

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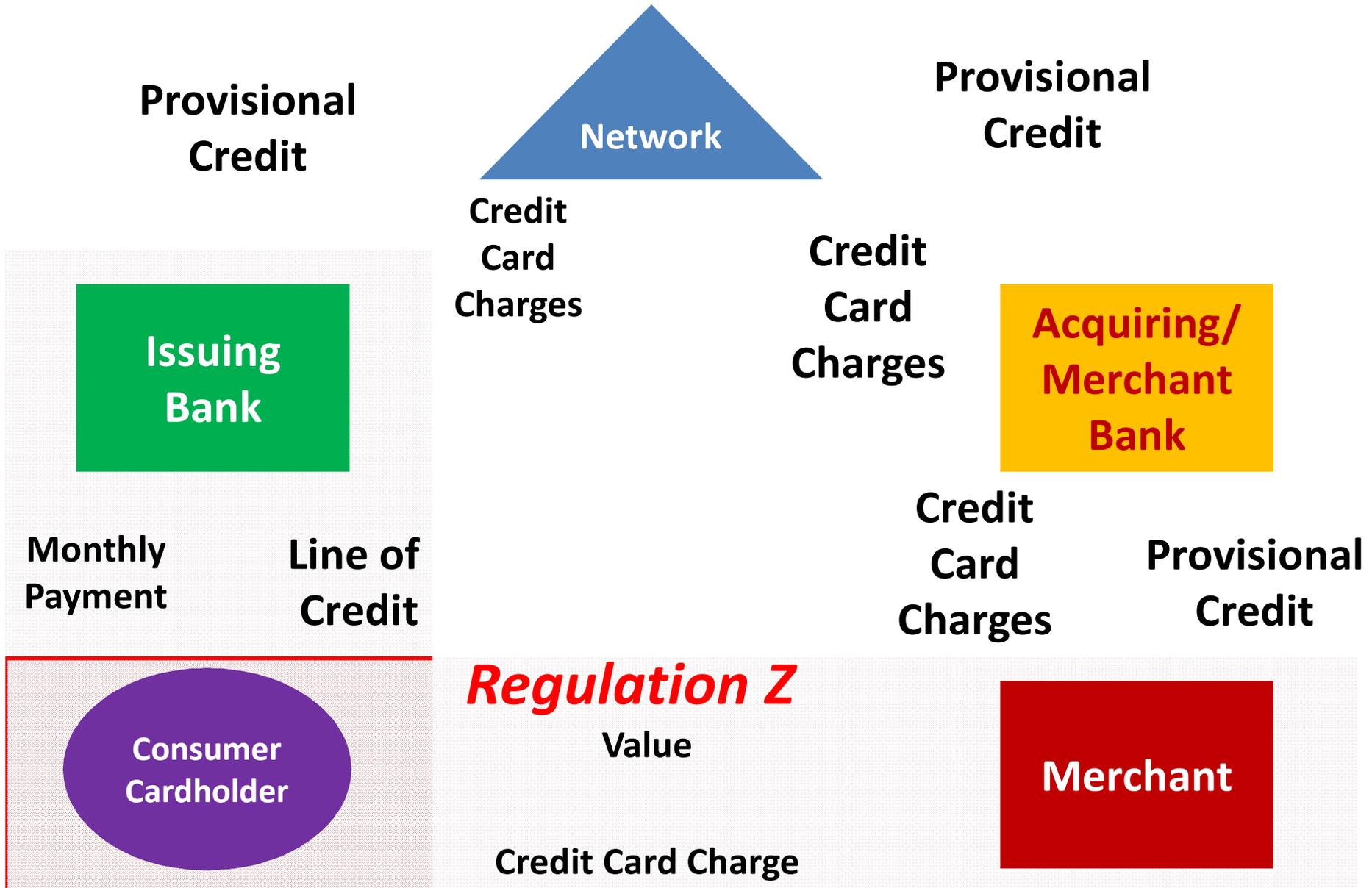
# WTO US-China UnionPay Dispute

- Work-in-progress: preliminary results, lots of questions
- Diagram: Introduction to credit card systems
- Origins of “electronic payment systems” in US
- Globalization of EPS and backlash
  - Network effects, platform markets
- PRC “electronic payment systems” strategy & UnionPay as “national champion”
- GATS Provisions at Issue
- Report of the Panel: explicit and implicit
- Emergence of a New Global *Lex Mercatoria*
- Next steps?

# Preliminary Results, Lots of Questions

- US may be only country in the world with standard “Payments Law” course covering negotiable instruments, electronic funds transfers, payment cards, etc
- Ongoing study of payment regulations in US, EU and China
  - Ongoing study of e-commerce law and globalization
    - Rise of self-regulation in global arenas, ICT may intensify impact under certain circumstances
- My first in-depth study of WTO dispute
  - Why is the panel report so unhelpful?
- My first in-depth study of electronic payment systems in China

# Introduction to Credit Card System



# Origins of US Electronic Payment Systems

- Automated Clearing House/ATM branch
  - 19<sup>th</sup> century bank clearing houses for checks
  - 1970s converted to automated clearinghouses, electronic fund transfer systems established
  - 1980s Domestic alliances, international networks growing
  - 1990s global interoperability of ATM networks
  - 2000s check image exchanges replace paper
- Credit card branch
  - 1950s travel cards (Amex, Carte Bleue)
  - 1960s BankAmericard + national franchise
  - 1970s MasterCard & Visa (formerly BACard) begin to migrate to electronic clearing and settlement
  - 1980s International networks growing
  - 1990s V & MC launch “signature debit” to compete with ACH/ATM branch

# Globalization of EPS & Backlash

- 1970s: SWIFT emerges as global network for cross-border funds transfers
  - No significant controversy ever, why not?
- 1990s: Visa & MasterCard achieve global dominance of retail card market
  - 1996 In US, Walmart sues, “honor all card” is antitrust tying violation, settlement in 2003
  - EU Competition Authority actions against Visa & MasterCard 2001, 2007, 2010
  - 2002 Reserve Bank of Australia limits interchange on debit cards, permits merchant credit card surcharges
  - 2005 In US, retail merchants sue again, 2012 settlement reduces interchange fees
  - Durbin Amendment to 2010 Dodd-Frank Act requires Fed to impose price controls on debit card interchange

# Network Effects

- What is an externality?
  - Cost or benefit not reflected in market price
- Physical versus ICT versus Virtual Networks
  - Physical network = trains, roads
  - ICT networks = telephones, Internet, bank ATM machines
  - Virtual networks = Microsoft Windows, iPhone applications; lawyers' boilerplate contract terms
- What is a network externality?
  - Cost or benefit of participating in ICT network not reflected in market price
  - More serious interoperability problems leads to more intense externalities: in/out without grey areas
  - “Lock-in” problems once everyone is using same ICT, hard to change
- What impact on ICT markets?
  - “first mover advantage” if network effects favor proprietary technology
  - But “open” standards allow interoperability without lock-in to proprietary solution

# Multi-Sided Platform Markets

- Rochet & Tirole: platforms in multi-sided markets set prices without relation to standard cost allocations in order to exploit network externalities
- Who are the sides?
  - Regulated financial institutions, mobile network operators, retailers, end users
- Who/What will be the global mobile money platform?
- Who should subsidize whom?
  - Party with more commitment to platform success should pay subsidy, party with less commitment should receive
- Should the poor pay high fees to attract service providers to the platform?
  - Is the platform private property or a public good?

# PRC Electronic Payments Strategy

- “National Champions” in national industrial policy  
[http://en.wikipedia.org/wiki/National\\_champions](http://en.wikipedia.org/wiki/National_champions)
  - Boeing, EADS/Airbus
- 1993 PRC Golden Card strategy 金卡工程
  - Golden Shield 金盾 Golden Bridge 金桥 Golden Finance (clearinghouse) 金融 Golden Tax 金税 Golden Customs 金关
- 2001 PRC WTO accession, GATS commitment finalized
- 2002 UnionPay strategy launched
  - Develops global network, now third in the world after Visa and MasterCard
- Mid-2000s US begins complaining, 2010 files WTO dispute
  - 2012 US wins on market access, PRC wins on “monopoly”

# GATS Provisions at Issue

- China committed in its schedules to open:
  - All payment and money transmission services, including credit, charge and debit cards, travellers cheques and bankers draft (including import and export settlement)
- Annex Paragraph 5(a) Banking and other financial services (excluding insurance) excludes:
  - Settlement and clearing services for financial assets, including securities, derivative products, and other negotiable instruments

# Report of the Panel

- Explicit
  - “Ordinary Meaning” of China’s commitment and exclusion for settlement & clearing covers UnionPay activities
- Implicit
  - UnionPay is run as a for-profit business, settlement & clearing are excluded from GATS because they are basic financial market infrastructure normally operated as public services by government, regulator or industry self-regulatory organization

# Emergence of New Global Lex Mercatoria?

- Old Lex Mercatoria: European feudalism
- Modern Lex Mercatoria: Lord Mansfield and negotiable instruments law
- New Lex Mercatoria: Berthold Goldman & International Commercial Arbitration
- New Global Lex Mercatoria
  - Technical standards and business process “schemes” operated by self-regulatory organizations
    - One example of rise of private regulation in global markets
- Visa, MasterCard, UnionPay \*ARE\* fifth parties in 5 party model as private global regulators
  - But under GATS, they must compete as private parties

# Next steps?

- History and current operation of Hong Kong interbank clearinghouse?
- Other?