

## **CROSS-BORDER SERVICE PAYMENTS UNDER EU FAIR COMPETITION AND SEPA RULES**

ANCA D CHIRIȚĂ\*

### **A. THE SEPA REGULATION ON CROSS-BORDER ELECTRONIC PAYMENTS: AN INTRODUCTION**

On 14 December 2011, the Vice President of the European Commission, Joaquin Almunia, explained why “a fair and open system for payments” is needed in Europe:<sup>1</sup>

*“It will not be a surprise to you that the Commission considers the development of fair, comprehensive and efficient payment systems for the whole of the EU as a precondition for the integration of commerce and the development of a true digital economy”.<sup>2</sup>*

Technical barriers and the lack of security standards<sup>3</sup> impede the integration of payment systems. These barriers need to be removed and thereby more transparency, competition and innovation be brought to the European payment market. The Competition Commissioner seems rightfully concerned about how best to achieve interoperability and foster competition by making the European payment market more open and accessible.

This article explains why the above worries are legitimate, but also underlines from the outset one of the criticisms of this direction.<sup>4</sup> The new mission of competition is said to overlap with industrial policy and the decision-making within the DG Internal Market and Services, which is enhancing competitiveness, stimulating innovation and promoting financial stability. One commentator supporting the banking industry emphasised the need

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Dr. iur. (Europa-Institut der Universität des Saarlandes), lecturer in law, Durham Law School, UK, DAAD visiting fellow at Europa-Kolleg and Max-Planck-Institut für ausländisches und internationales Privatrecht, Hamburg. An earlier draft was presented at the Durham Law School Seminar on 19 October 2011.

<sup>1</sup> J Almunia, “A Fair and Open System for Payments in the Single Market”, Speech 11/889, European Payments Council Plenary Meeting, Brussels, 14 December 2011.

<sup>2</sup> The Digital Agenda is one of the initiatives of the Europe 2020 strategy aimed at developing better electronic forms of payment.

<sup>3</sup> J Almunia, “Building Europe’s Future Payments Market”, speech, Next Generation Cards and Payments Conference, Brussels, 12 October 2011; see also Green Paper, “Towards an Integrated European Market for Card, Internet and Mobile Payments”, MEMO/12/6 (Brussels, 11 January 2012).

<sup>4</sup> See, eg J Santamaria, “Reflections on Recent Contributions from the European Commission Directorate General Competition to the Innovation in Payments Debate: Seeking Common Ground between Policy Makers and Technical Experts” (2012) 13 *European Payments Council Newsletter* 3.

for “legally binding” guidelines. *Ex ante* regulation would make clear those requirements which banks need to fulfil in order to promote market integration and innovation.<sup>5</sup>

So far, it seems that everything coming from Brussels needs to be supported by some sort of soft law. Regulation 924/2009 on cross-border payments, therefore, is an unfamiliar experience for the EU competition lawyer.<sup>6</sup> The regulation provides a transitional regime for the Single Euro Payment Area (SEPA direct debit) until 1 November 2012 and awaits a further amendment to establish in particular technical standards for credit transfers and direct debits.<sup>7</sup>

The Commission supports SEPA to promote competition among banks by removing national borders in the banking industry.<sup>8</sup> According to Article 114 TFEU, the Council of the EU shall adopt “measures for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market,”<sup>9</sup> ie the free movement of services of general economic interest. This is one of the grounds for enactment of the regulation. Its first recital mentions the principle of equality of charges for cross-border payments in euros. Charges should be the same as for corresponding payments in another Member State. However, this leaves cross-border payments in currencies other than the euro outside its scope of application.

The regulation retains a cross-border threshold, previously established by Regulation 2560/2001, for payments in euros and in Swedish kronor up to €50,000 or equivalent. Consequently, the principle of equality of charges does not apply when making payments in another EU currency. In the third recital, the regulation identifies some of the past enforcement difficulties. First, its enforcement lacks “identified national competent authorities”, and, secondly, it does not apply to direct debits, but to credit transfers and cross-border electronic transactions.<sup>10</sup> Its failure is not to indicate any relevant national authorities to supervise electronic payments as banking services. Thus national guidelines are demanded imperatively and Member States remain responsible for procedural aspects and complaints.

What the regulation does not acknowledge is that the principle of equality of charges cannot be applied proportionately so as to create an internal market for banking services of

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<sup>5</sup> Santamaria, *ibid.*

<sup>6</sup> EC Regulation 924/2009 of the European Parliament and the Council on cross-border payments in the Community, repealing EC Regulation 2560/2001 [2009] OJ L226/11; for an overview of the regulation see M Van Empel, “Retail Payments and the Arduous Road to SEPA” (2009) 46 *Common Market Law Review* 921.

<sup>7</sup> See [http://ec.europa.eu/competition/sectors/financial\\_services/sepa\\_en.html](http://ec.europa.eu/competition/sectors/financial_services/sepa_en.html) (last accessed on 9 March 2012).

<sup>8</sup> *Ibid.*

<sup>9</sup> This article should be read in the light of Art 26 TFEU.

<sup>10</sup> See recital 5 of the above regulation.

economic interest to EU consumers insofar as it applies only to electronic transactions in the euro. This runs counter to its ambitious goal of creating the same conditions for cross-border payments EU-wide, since it opts out of this principle in regard to the transparency of charges for currency conversion.<sup>11</sup>

In substance, it is easier to process cross-border electronic transactions if the order of payment complies with the banks' requirements of standardised payments, which both IBAN and BIC must be provided.<sup>12</sup> This marks no major progress from the previous requirements of the 2001 Regulation, particularly since banks rely on the same business model in the setting of charges. Progressive steps in the regulation would have obliged banks to justify a transparent setting of the exchange rate for conversion. The outcome in practice is that the EU consumer is left without protection at both the EU and the national level, because there is no "identified" authority dealing with consumer claims when prejudiced through the imposition of unfair service charges. Their imposition in an unfair manner could also distort the cross-border market of electronic banking. The cause of hindrance lies in charging "inter-banking" fees for standardised payments, which should enable a faster payment.

Recital 11 requires the Commission to issue urgently guidance on "*the objectives and measurable criteria for the compatibility of such multilateral inter-banking remuneration, which could include multilateral interchange fees (MIF), with EC competition law and the Community regulatory framework*".<sup>13</sup>

A prohibition of MIF per transaction will enter into force on 1 November 2012 for cross-border direct debits.<sup>14</sup> An important remaining issue, therefore, is to ensure the compliance of bank charges with EU competition rules. In September 2011, the Commission opened another antitrust investigation into the standardisation process of electronic payments undertaken by the European Payments Council (EPC),<sup>15</sup> to prove whether the standardisation process limits market entry or innovation through the exclusion of new entrants and payment providers who are not controlled by a bank. As rightfully pointed out in the Green Paper,<sup>16</sup> the only two international card schemes (Visa and MasterCard) reflect a situation of duopoly on the card market. Furthermore, the true cost of payment services is

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<sup>11</sup> See recital 6. According to Art 3(4), currency conversion charges are exempted.

<sup>12</sup> International Bank Account Number and Bank Identifier Code respectively.

<sup>13</sup> See the Commission Decision COMP 34579/2007—*Europay (Eurocard-Mastercard)*, where the Commission found that MasterCard multilateral interchange fee was a restriction by object under ex Art 81 EC (now Art 101 TFEU).

<sup>14</sup> *Supra* n 7. MIFs are fees charged by the issuing bank of the cardholder to a merchant's bank for each sales transaction with a payment card. Payment schemes, such as Visa and Mastercard, operate a MIF that is a decision of an association of undertakings which may have the object or effect of restricting competition between acquiring banks.

<sup>15</sup> See EU Commission, Press Release IP/11/1076, Brussels, 26 September 2011.

<sup>16</sup> *Supra* n 3, 2.

unknown to EU consumers and not transparent for merchants. This means that there is no competition pressure on the price of the payment instruments.

As a preliminary conclusion, Regulation 924/2009 makes practically no significant effort to challenge current bank charges for electronic transactions or online banking services that EU customers have at their disposal when making payments from or to another Member State. This does not suggest that its applicability to currencies other than the euro is excluded should a Member State so wish, but it places no compulsory requirement within the meaning of this regulation.<sup>17</sup> Only a declaratory recognition exists for the scope of application to currencies other than the euro, which “would have clear benefits”.<sup>18</sup>

Therefore, whilst the regulation remains limited in scope, its area of application could be potentially extended. Currently, it refers to individual consumers and micro-enterprises.<sup>19</sup>

## **B. HOW SEPA RULES FUNCTION IN ANOTHER CURRENCY THAN THE EURO**

Outside the euro zone, UK banks already run a SEPA direct debit scheme intended to service consumers, including individuals, small businesses and business customers (B2B). The scheme is aimed at processing cross-border payments of utilities bills and other regular payments. As previously noted, from the outset, the SEPA regulation encouraged limited applicability for EU currencies other than the euro. For example, “for payments effected within the European Economic Area in the currency of a member state, the beneficiary will be liable for their bank’s charges”.<sup>20</sup> This suggests that even standardised payments, for which a customer already provides both IBAN and SWIFT<sup>21</sup> or BIC, would be subject to higher inter-banking fees, which another bank would not otherwise charge in euros.

The use of the standard is actually intended to ease and minimise the final transaction’s costs. Thus, it is less effective outside the euro zone as UK banks consider it a mandatory requirement on the part of the foreign or overseas (EU) bank. Therefore, they enjoy discretion in setting their own service charges.

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<sup>17</sup> See Art 14.

<sup>18</sup> Recital 18.

<sup>19</sup> See Art 2(11) and (12). See the Commission Recommendation 2003/361/EC [2003] OJ L124/36, which defined a medium-sized or micro-enterprise as any enterprise with fewer than 250 employees and an annual turnover of less than €50 million.

<sup>20</sup> See HSBC on priority payments charges at <http://www.business.hsbc.co.uk/1/2/internationalbusiness/international-payment-processing/international-payments> (last accessed January 2012).

<sup>21</sup> SWIFT is the Society for Worldwide Interbank Financial Telecommunication which enables financial institutions to send and receive information about financial transactions in a secure and standardised environment.

If one compares bank charges in euros to those in the UK, the perception is that the free movement of services benefiting EU consumers via online banking is somewhat affected by higher charges, which are not justified as value for the same service elsewhere in the EU.<sup>22</sup> Should, then, the principle of proportionality be followed by all EU Member States? For online SEPA payments in euros there are no inter-banking fees for standardised payments, so why should there be any fees for like services in another Member State, having a different currency? Apart from the charge for conversion, which depends on the exchange rate, there might be, for example, a £17 service fee per transaction via internet banking. This could rise to £20 for non-electronic payments, ie payments made in a branch of the bank.<sup>23</sup> And the bank would then add a €8 flat fee for urgent online transactions in euros. Leaving aside the pricing factor of the inter-banking service charges, a business strategy currently used is delaying electronic, or instant, payments by unfair business terms. Accordingly, another surcharge operates as a flat fee for faster delivery beside the three days regular service. This prompts the question: what is actually electronically fast? Are these banks suggesting that their communication is somewhat moderated elsewhere to set additional charges? For customers, the additional charge is truly disguised. They may not immediately see how an electronic order cannot be processed immediately unless a flat service fee is paid. The same customers may recognise a slower service via the bank's branch. Thus, priority payments are actually those payments made via internet banking being filled in by consumers directly to the beneficiary bank. These payments do not even need any further assistance on the part of the bank's employee. Another service provider<sup>24</sup> charges, for example, a £9 fee per SEPA transaction, irrespective of whether it is made via telephone, internet banking or post. This is a slightly lower charge. For euro payments that need local conversion, the above supplier also offers, in a more transparent manner, an advance notice with a cut-off time.

However, the way SEPA rules function in practice is simply not workable for smaller payments. Only EU standardised payments up to €50,000 are received free of charge. The same treatment also applies for the use of a SEPA direct debit when one receives such payments.<sup>25</sup> Thus, any non-priority payments are charged a £19 fee for sending. The

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<sup>22</sup> SEPA electronic payments are free of charges in most EU Member States: see <http://www.deutsche-bank.de/pbc/gk-auslands-geschaft-sepa.html?link=search>; [https://www.commerzbank.com/en/hauptnavigation/institutions/products\\_services/cash\\_services/sepa/SEPA.html](https://www.commerzbank.com/en/hauptnavigation/institutions/products_services/cash_services/sepa/SEPA.html); [https://www.ing.be/en/retail/day-to-day-banking/other-payments/Pages/international-payments.aspx?WT.xmenusource=LEFTNAVIGATION\\_International+payments](https://www.ing.be/en/retail/day-to-day-banking/other-payments/Pages/international-payments.aspx?WT.xmenusource=LEFTNAVIGATION_International+payments). Note that, for example, UK City Bank receives SEPA orders free of charge: <http://www.citibank.co.uk/personal/banking/info/tariffandinterest/index.htm?merchant=citi>.

<sup>23</sup> See the HSBC charges on [hsbc.co.uk/business](http://hsbc.co.uk/business) (last accessed January 2012). These examples are purely illustrative.

<sup>24</sup> See Lloyds TBS's terms and conditions for SEPA payments.

<sup>25</sup> See Lloyds TBS's terms and conditions for SEPA payments.

person to whom the payment is actually made does not incur any shared expenses. In return, the person who sends the money has to pay a higher service fee. The same bank reserves the right to charge £7 extra for non-standardised payments. This is odd, because this service shows no benefits passed on to consumers, who are not better off when making a standardised payment when they are charged £19. The charge applies irrespective of any economic loss consumers may reasonably expect because the bank enjoys discretion over the exchange rate. It is normal business to commercially exploit the customer who depends economically on the payment service since payment services are of general economic interest.

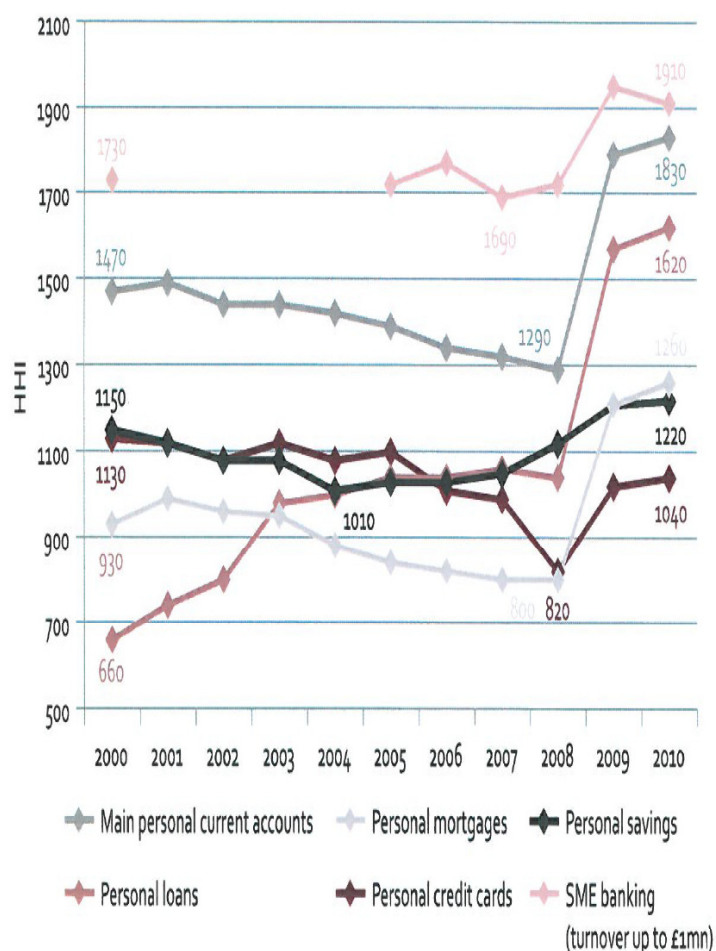
Finally, do individual customers have reasonable alternatives for smaller payments or are banks (un)avoidable business partners? Do consumers, including intermediaries, accept any notice of terms and conditions in order to proceed with the electronic payment? It would be fair if the answer is in the affirmative.

In theory, the banks in question might not have a significant market share in relation to their competitors. Since the practice lies in the commercial exploitation of customers, there could be less exclusionary focus upon the market entry of competitors. Exploitation occurs irrespective of the market shares of a bank's competitors. How, then, should the financial power of banks be interpreted? Reasonably, the bank in question should not have been recently established, but it needs to enjoy a significant or considerable economic power, ie control over capital and assets. In practice, a recent report of the Independent Commission on Banking shows that the total market share of the four biggest UK banks (Barclays, HSBC, Lloyds TSB and the Royal Bank of Scotland) fell from 74% in 2000 to 64% in 2008, but rose again to 77% in 2010, following the Lloyds TSB/HBOS merger.<sup>26</sup> It is also revealed that, for all of the investigated markets, namely main personal current accounts, personal loans, personal mortgages, personal savings, personal credit cards, and small and medium enterprise (SME) banking, the Herfindahl–Hirschman indices are above 1,000, which indicates a concentrated market. Eventually, economists may not interpret these concentration levels as being sufficiently serious over the whole period of time, as shown in Fig 1. The figure is reproduced from the Independent Commission on Banking and reveals the concentration levels in retail banking measured using the Herfindahl–Hirschman Index.

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<sup>26</sup> See Final Report of the Independent Commission on Banking, 12 September 2011, 7.7, 166, available at <http://bankingcommission.independent.gov.uk/> (last accessed on 15 April 2012).

Fig 1 Concentration levels in retail banking measured using the Herfindahl–Hirschman Index



Source: Commission analysis of SME banking data from the Competition Commission (2000), TNS (2005-2009) and Charterhouse (2010), and personal banking data from GfK FRS.<sup>27</sup>

[Fig 7.1 First Report of the Independent Commission on Banking, 167]

The above report also identified potential problems of new entrants into SME banking in attracting customers who are basically locked into the available option due to a “strong brand loyalty”.<sup>27</sup> Another potential barrier to entry is the regulatory requirement—some disproportionately high capital requirements relative to incumbents—which makes the entry of newcomers difficult.<sup>28</sup>

<sup>27</sup> *Ibid.*, 7.19, 171.

<sup>28</sup> *Ibid.*, Table 7.1.

Since consumers are unwilling to switch to other competing banks, there are no incentives from banks to provide better deals.<sup>29</sup> Even though reluctance to change banks seems to be a cultural characteristic in the UK, I am reluctant to believe that consumers have any bargaining power to negotiate their own favourable business terms and conditions. If consumers have the alternative of switching to another bank, those terms should vary significantly and not be identical. The individual preference of bank customers seems obviously tied to the banks' pricing model of "free-if-in-credit", whereby there are no charges as long as the account balance remains positive.<sup>30</sup> Banks are said to derive revenues from net interest margins, monthly and transaction fees, charges for overdraft facilities, insurance services, etc. Thus, due to their nature, electronic payments do not have the option of flexible service switching. Because the exchange rates are variable and depend upon market fluctuations, it can be said that inter-banking fees are alike because they are meeting the same technical standard. It is therefore unfair when interbanking fees for online SEPA payments are nil in euros whereas the same payment in another currency incurs a cost. This charge is made in addition to those already to be deducted in a less transparent manner for the loss in the exchange rate. It therefore seems that most banks operate very similar, albeit not identical, terms and conditions for their service to the detriment of consumers.<sup>31</sup>

All the above bank charges form part of a payment order which must be agreed in order to proceed with the payment. Therefore, it is essential to understand whether competition is fair to consumers in the banking sector, or if there is a problem caused by the electronic payments regulation. Is this regulation perhaps too permissive for banks outside the Eurozone? According to its own designation, SEPA should be a European Union, and not just a Single Euro, Payment Area. It strives not only for a single currency, but in particular for proportionality or equality of charges and transparency. Therefore, if the driver is not politically motivated but economically oriented, the rule of economic efficiency would require that EU-wide banks should apply standard charges.

### **C. THE IMPACT OF BANKING TERMS AND CONDITIONS ON THE ECONOMICS OF CONTRACTS**

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<sup>29</sup> *Ibid.* 7.33, 179.

<sup>30</sup> *Ibid.* 7.46, 188.

<sup>31</sup> For an interesting economic evaluation of the Competition Commission's investigation on bank service charges see, eg D Ridyard, "The Competition Commission's Northern Ireland Banking Market Investigation—Some Unanswered Questions on the Role of Market" (2008) 3 *European Competition Law Review* 29, 173.



Substantive issues are better traced back to the notion of “unfairness” in both terms and conditions, particularly since, based on the economics of contracts,<sup>32</sup> their assessment often fails to identify an economic incentive over a particular term or condition included in the binding contract. It is customary business practice to mention terms and conditions formally as “terms and conditions apply”, without giving the exact details of economic expectations. In practice, contracts do not always specify the economic value for delivery or the transportation costs of the good or service with the main pricing. Usually, such expenses are stipulated together with the main obligation, which is why the final value of the service contract might rise above the initial expectations. Because of the individual freedom of contract, it is also not easy to identify economic incentives for those terms or conditions which differ significantly when they are not customary practice or cannot be known in advance.

The failure of economics of contracts lies particularly in the practical difficulty of distinguishing between terms and conditions which do not lead directly, or at least not immediately, to financial incentives, because of an asymmetric information exchange or unequal bargaining power.<sup>33</sup> Put simply, consumers identify bank charges with a basic service fee as a reasonable pricing that is expected. Thus banks usually have economic incentives for processing an order of payment with sub-divisions of less than three days or even within a few hours. This could then be justified to consumers as a faster service to meet a certain deadline. It is, however, unclear why there should be a faster subservice for electronic orders at all, and whether the service is then reasonable and fair. It appears that banks have a strong incentive to create multiple options which could increase the final service fee.

## **1. The EU Competition Law on Terms & Conditions**

The background to the EU law of unfair competition in Article 102 TFEU on the imposition of “other unfair trading conditions” by dominant undertakings could be further complemented by the Council Directive on Unfair Terms in Consumer Contracts

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<sup>32</sup> On the economics of contract law see A Kronman and R Posner, *The Economics of Contract Law* (Little Brown, 1979); EA Posner, “Economic Analysis of Contract Law after Three Decades: Success or Failure?”, John M Olin Law & Economics Working Paper no 146/2002 (Chicago, 2002).

<sup>33</sup> One advocate of this idea is Eric Posner, *ibid.* See H Beale, “Inequality of Bargaining Power” (1986) 6 *Oxford Journal of Legal Studies* 131; see F Kessler, “Contracts of Adhesion—Some Thoughts About Freedom of Contract” (1943) 43 *Colombia Law Review* 624, 631; on the understanding of unfairness as related to “strong bargaining position” and the early private litigation cases of the English law of contract see SN Thal, “The Inequality of Bargaining Power Doctrine: The Problem of Defining Contractual Unfairness” (1988) 8 *Oxford Journal of Legal Studies* 29.

13/1993/EC.<sup>34</sup> Otherwise, the lack of a unified understanding leaves an important practical issue of fair terms and conditions outside the scope of competition law. The Treaty proviso also has a lot to gain for its interpretation and future application in the light of the directive. In particular, the sixth recital made it clear that disparities concerning contract terms between the seller or supplier of services and the consumer may lead to distortions of competition in cross-border sale or supply. The elimination of unfair terms from consumer contracts is therefore essential for the establishment of the internal market with free movement of services.<sup>35</sup> Thus, the most important recital, no 13, explains the key issue of fair competition, which justifies the intervention of competition in the absence of market dominance. It refers to the “protection of the economic interest of consumers” and the sale of goods and services where consumers should be protected against the abuse of power by the seller or supplier, in particular against one-sided standard contracts. This recital creates a lower threshold of intervention based on the abuse of power, together with a stronger and imperative protection of consumers against any acts of unfair competition, irrespective of the dominance threshold of a monopolist. It thus prohibits any abuse of power by non-dominant sellers or suppliers in unilaterally imposing unfair terms. The recital highlights one major objective of fair competition.<sup>36</sup>

The understanding of terms is revealed in another recital, where the assessment of unfairness in this directive is not intended to cover the main subject matter of the contract or the quality/price ratio. Put simply, the sale contract entails one major obligation—to pay the price—together with secondary obligations, such as conditions of carriage, transportation or any other terms of delivery. These additional obligations must be understood as terms and conditions other than the main pricing factor. The secondary legislation is intended to act as a control mechanism where parties agree on the price and later discover that the final obligation is more onerous due to particular terms and conditions which did not play any role during the negotiations. Thus recital 13 does not exclude assessing “the fairness of other terms”, such as price or value for money. The directive further clarifies that fair terms mean acting in good faith where the seller or supplier deals “fairly and equitably”. What is meant by good faith is to establish a relative position of economic power which lies in the “strength of the bargaining position of the parties”, whereas the consumer is induced to agree on unfair terms. This is a clearly lower

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<sup>34</sup> UTCC or Council Directive 93/13/EEC, 5 April 1993 on unfair terms in consumer contracts [1994] OJ L95/29, as amended by Directive 2011/83/EU of the European Parliament and of the Council on consumer rights, 25 October 2011, [2011] OJ L304/64, 22 November 2011.

<sup>35</sup> Recital 10 UTCC.

<sup>36</sup> On lack of a European unfair competition law see T Möllers and A Heinemann (eds), *The Enforcement of Competition Law in Europe* (Cambridge University Press, 2010).

threshold of intervention than dominance in the relative economic power. So where should EU competition law draw the dividing line?

As will be explained below, the English courts interpreted Article 4(2) of the EC Directive on How to Assess Unfairness by looking only at the requirement that terms are written in plain and intelligible language. This refers to the procedural assessment of standard terms as a whole. However, the text of the directive builds on its explanatory recitals, which detail the policy objectives to be pursued. The directive should not be read “article by article” without the recitals; otherwise, one’s understanding of it is substantially flawed, particularly because the ambitious goal of the directive is the imperative of protection of the weaker consumer against any abuse of power by non-dominant market participants, such as sellers or suppliers. This is based on the premise that their position in bargaining creates an imbalance in contractual rights and obligations, such as unfair terms and conditions. Contracts cannot be negotiated individually if they are drafted in advance. The practice offers many such examples which economists identify with tools of behavioural economics as marketing strategies of businesses to influence consumers.<sup>37</sup>

## **2. Interpretation of Terms & Conditions**

Under English contract law, both the Unfair Contract Terms Act 1977 and the Unfair Terms in Consumer Contracts Regulations 1999 reflect a part of economic contracts with a clear consumer protection function. Their existence makes the valid point that there is an English law of unfair competition. Thus the separation of administrative powers over pricing and the judge-made law on unfair or unreasonable terms is somewhat misleading. Sometimes, it also results in less protection afforded to consumers and a loss in economic welfare. There is, however, considerable controversy over the text of Article 4(2) in the EC directive, which required the assessment of unfairness not to be based on the definition of the “main subject matter” of the contract, ie the price, or on the price/remuneration which could reflect the quality of the service, but on whether those contract terms are written in “plain intelligible language”.

In practice, the Supreme Court of England and Wales had practically tied the hands of the Office of Fair Trading (OFT) based on its understanding of the directive. The court held that the directive did not confer on the national competition authority more enforcement

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<sup>37</sup> See, eg C Jolls, CR Sunstein and R Thaler, “A Behavioural Approach to Law and Economics” (1998) 50 *Stanford Law Review* 1471; on imperfect market information available to consumers see, eg M Armstrong, “Interactions between Competition and Consumer Policy” (2008) 4 *Competition Policy International* 1, 98.

powers to attack bank charges under the unfair terms regulations, with the exception of evaluating “the adequacy of the price or remuneration” as against the service supplied in exchange.<sup>38</sup> It is unclear how the Supreme Court<sup>39</sup> ruled out the competition law concerns, since the character of unfairness is already listed as exploitative abuse under the competition rules on pricing and other trading conditions. Furthermore, the OFT safeguards the fairness of contract terms and acts as a filter mechanism against unfair competition in that it is responsible for applying to the court for injunctions. How, then, can the same competition authority not be held responsible for evaluating the fairness of contract terms in their substance? This would obviously include pricing as a main obligation, but also the relationship between pricing and the service delivery, which reflects the quality or value for money. Otherwise, it has no logic. The court could have analysed the entire economic context of unfair terms under the English and EU law of unfair competition. The court also declined to make a reference to the Court of Justice for a preliminary ruling on the concept of unfairness.<sup>40</sup>

Under the common competition rules of the Treaty on the Functioning of the EU (TFEU), other unfair trading conditions may include unfair terms. Thus, sometimes a term is taken for a condition and vice versa.

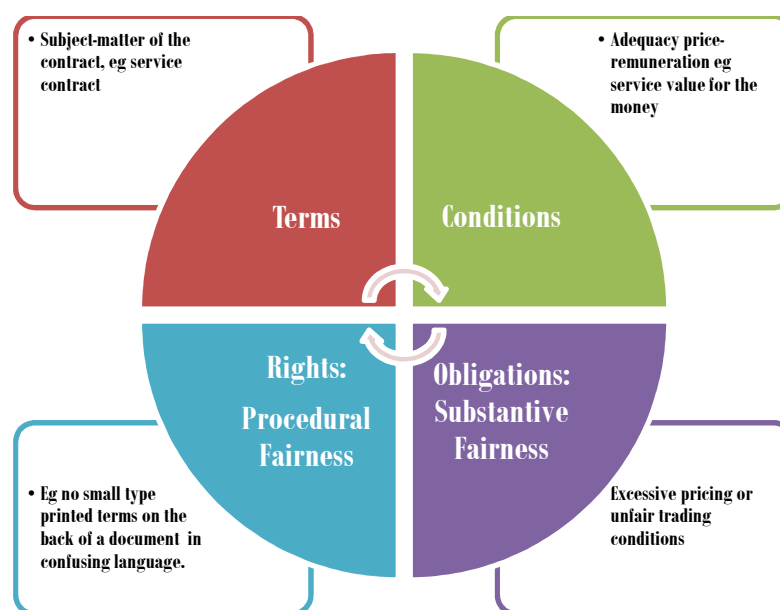
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<sup>38</sup> Recently see, eg S Whittaker, “Unfair Contract Terms, Unfair Prices and Bank Charges” (2011) 74 *Modern Law Review* 1, 109; M Armstrong and J Vickers, “Consumer Protection and Contingent Charges”, MPRA Paper no 37239 (Munich, March 2012).

<sup>39</sup> *Office of Fair Trading v Abbey National plc* [2008] EWHC 875 (Comm), [2009] EWCA Civ 116, [2009] 2WLR 1286, [2009] UKSC 6, [2009] 3 WLR 1215; *Director General of Fair Trading v First National Bank plc* [2001] UKHL 52, [2001] 1 AC 481; H Beale (ed), *Chitty on Contracts* (Sweet & Maxwell, 30th edn, 2008), ch 15.

<sup>40</sup> See N Andrews, *Contract Law* (Cambridge University Press, 2011), 439–40; R Stone, J Devenney and R Cunningham, *Text, Cases and Materials on Contract Law* (Routledge, 2011), 301–15; J Beatson, A Borrows and J Cartwright, *Anson’s Law of Contract* (Oxford University Press, 2010), 211–16.

In practice, the headline “terms and conditions apply” is the usual disclaimer, as shown in Fig 2.



In the absence of EU common rules or principles of contract law, attempts to harmonise contract terms Union-wide regard only one side of the coin: the directive ignores the impractical separation of terms from conditions. In fact, those terms referred to in the directive’s annex are merely described as “terms which have an object or effect”, but also include conditions. This is the same language of restraints of competition by object or by effect, whereas the object is the subject matter of the contract, eg a service contract, and the effect is the intention of the parties to the agreement or the effect of the agreement in relation to third parties. For example, point 1(c) refers to “making an agreement binding on the consumer whereas provision of services by the seller or supplier is subject to a condition whose realization depends on his own will alone”.

Under Article 102 (a), therefore, there should be no problem in including unfair terms in “other unfair trading conditions”. The drafting of the EU Treaty could not foresee that their interpretation would make no sense because of the separation of terms from conditions. The Treaty detailed this in EC Directive 13/93 and then developed an intricate evaluation of unfair terms which was needed primarily to understand the lapse proviso of Article 102(a). Otherwise, why should a rule of law be interpreted in isolation from its economic context?

A logical argument requires that economic contracts by undertakings are based on the freedom of contract as a principle, but there are also special competition rules. Article 102(a) refers to the concept of unfairness in any of those terms and conditions. One should not fall

into the trap of history: EU competition rules were already enacted before the directive detailed the purpose of fair competition when it referred to consumers and other market participants such as suppliers or sellers. The directive must therefore be read into the general context of unfair terms for competition rules. It is unacceptable to ignore what is fair competition's most obvious concern by saying in a crisp style that: "any assessment based on matters not relating to the appropriateness in amount of the price or remuneration is not excluded by regulation 6(2)(b)". The national court found that excess overdraft charges were transparent pricing because an average customer must know that being overdrawn bears a further risk of being charged excessively. One could consider whether it is a good option to allow national courts to ensure fair competition with regard to unfair terms. The risk is that national courts may not be able to offer a more economic interpretation in the light of the crossroads between the economics of contracts and competition. This means that contract terms, for which there is no economic incentive and which do not challenge the price/remuneration, fall outside the scope of the national regulation. However, this interpretation overlooks the danger of cross-subsidisation. If a bank sets a high charge for unauthorised overdrafts, this will generate profit from those consumers who naively get overdrawn.<sup>41</sup> In a hypothetical competitive market, this profit will subsidise the bank account of those customers who avoid getting overdrawn. One of the solutions advanced by Armstrong and Vickers is "to require, where technically feasible, banks to warn consumers in advance when they request a transaction which will incur a contingent charge".<sup>42</sup> National competition rules are *lex specialis* (special laws). Even if, under the common law, there is a statute of unfair terms, the general law of contracts should be interpreted in the light of the economic context of competition rules. Courts therefore must analyse the legal and economic context of economic contracts under the special competition rules. Competition authorities need to observe the general context of contracts where a lower threshold of intervention applies and differentiate from the requirement of dominance narrow oligopolies.

A look back at the 1960s reveals that the application of competition rules to oligopolies created legal uncertainty and it was difficult to distinguish good from bad oligopolistic behaviour, including ancillary and non-ancillary agreements, and agreements on price.<sup>43</sup> As

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<sup>41</sup> Armstrong, *supra* n 37, 122; Armstrong and Vickers, *supra* n 38, with a timely and excellent research piece on the economic dichotomy of sophisticated and naïve consumers and contingent charges.

<sup>42</sup> Armstrong and Vickers, *ibid.* Other solutions are: to allow consumers to opt out or to eventually place a cap on contingent charges. The latter is currently used when setting smart phones charges.

<sup>43</sup> See, eg J Weissman, "Is Oligopoly Illegal? A Jurisprudential Approach" (1960) 74(3) *The Quarterly Journal of Economics* 437.

a result, this led to the articulation of “modern” competition standards that stressed more formal analysis.<sup>44</sup>

Form took precedence over economics, as described by Weissman’s evolutionary perspective in the *Quarterly Journal of Economics*: “the revolt against formalism: oligopoly recognized”.<sup>45</sup> “And to the extent that oligopoly emerged as an important factor in the new portrait, doubts about the validity and usefulness of the antitrust norms inevitably appeared.” This shift occurred when statutory provisions replaced the law of contract in many facets of economic life, including the regulation of utilities and banks with a public interest.<sup>46</sup> The standardisation of many commercial agreements did not offer too much free choice to the “sovereign consumer”. These parallels with the law of contract highlight the role of individual intent and the reluctance to apply competition rules to oligopoly cases. The essence of an oligopolistic market is “the mutual awareness of the few who are on one side of a market that their actions affect each other, and this awareness need not have resulted in any way from intent of the parties”.<sup>47</sup> Therefore, the recognition of the oligopoly phenomenon has been largely a contribution of economists.<sup>48</sup>

The concept of fairness in economic contracts has been broken down into price or main remuneration and non-pricing terms and conditions. Thus Article 102 adopted a general approach not restricted to unfair pricing; it is not addressed to traders but to dominant undertakings, which makes its application in the context of dominance impossible.

The confusion in the UK ruling seems to have its origin in the less structured approach of the common law compared to continental law. In particular, contract terms are not the same as trade conditions. Furthermore, there is a different perception of terms and conditions as a secondary obligation that is additional to the main subject matter of the contract. Thus contract obligations cannot be technically divided in practice. It is the courts’ formalism that perceives them as such. This is also proven by the Union only enacting its general legislation on consumer contracts in late 1993—bearing in mind that Article 86 of the Treaty of Rome included unfairness in 1957, followed by the Directive on Unfair Terms. Meanwhile, after years of controversies over how to assess unfairness under the competition rules, the internal market set out its target of reaching consensus over a significant market segment affecting consumer contracts, but left this task (ie the harmonisation of the general

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<sup>44</sup> *Ibid.*, 438, 450.

<sup>45</sup> *Ibid.*, 453.

<sup>46</sup> *Ibid.*, 454.

<sup>47</sup> *Ibid.*, 455.

<sup>48</sup> *Ibid.*, 456; EH Chamberlin, *The Theory of Monopolistic Competition* (Harvard University Press, 1948); more recently see, eg I Kokkoris, *A Gap in the Enforcement of Article 82* (British Institute of International and Comparative Law, 2009); I Kokkoris, *The Gap in the ECMR and National Merger Legislations* (Routledge, 2010).

rules of contracts) to the Member States. It is well known that continental law relies on codes, whilst common law contains few principles of contract law. It has thus been an immense burden imposed on Member States to identify those concepts set out in the directive which are similar under the national law of contract. It is therefore not surprising that this has given rise to unclear interpretations. They are the consequence of a vacuum in the legal foundation of the EU, where there are no common principles of economic contracts, but strong competition enforcement. Usually, terms refer to the moment when a payment ceases to exist by meeting a delivery deadline; the method of payment may be imposed as a contractual condition. This suggests that an electronic order of payment as a service would not need a separate condition on how fast the respective order will be processed; such a condition could be temporal and used as a term in trade. Competition, however, identifies whether there are other free of charge service alternatives. Thus, it could also question whether, balancing the imposed terms and conditions other than the basic price, the respective banking service package challenges a normal competitive level with its final price, because those terms and conditions involve additional expenses.

### **3. Unfair Pricing under Terms and Conditions**

Recently, EU consumers have been requested to pay using the utility provider's preferred method (eg paying by debit card or over the phone) and persuaded that this is the cheapest option, as there will be a yearly discount. This raises a future concern of fairness in marketing the respective banking service tied to the main utilities contract. Customers are locked in as they need the service facility, so will accept such imposed terms that providers demand they agree in advance.

Another case of misleading and unfair pricing is where low-cost airline companies advertise a basic service price and then add a variety of terms and conditions of carriage. One must agree to proceed with a payment which usually ends with a further surcharge<sup>49</sup> for the use of one's own debit card, rather than the airline's fidelity or club debit card. This is a technique based on an economic calculus on how to boost sales. There is, however, increasing innovation displayed by many EU airline companies in how to charge unfairly. What is the point in advertising low-cost travel if one then has to pay for one's preferred seat and so on? Consumers are informed how much the airport taxes that must be paid are, but are subject to predatory pricing for purchases on board, which is an extra service, not a normal commodity. Upon acceptance of the terms and conditions, when the consumer ticks

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<sup>49</sup> See OFT notice of investigation into airline payment card surcharges, June 2011, CREE/27017.



in the respective box, there is thus exposure to a *risk* of being overcharged significantly. It is the freedom of contract which justifies the gains in trade. What then should competition law do, if not limit this freedom? After all, it is true that enjoying a dominant position is not prohibited if there is no abuse or misuse, and that the position may only temporarily be limited. The same limitations on the freedom of contract apply when the customer must accept “agreed terms and conditions” as a usual notice to them. Terms are being imposed on customers so there is actually nothing a consumer cannot agree to, unless one carries no bag, takes whatever seat, and so on. Otherwise, unfair terms and conditions of this kind should be punished as unfair competition.

The essence of the ordoliberal current lies not only in free and open markets to guarantee the freedom to compete of businesses, but also in the freedom of contract and the freedom of choice. Competition therefore must intervene to control and temporarily limit natural freedoms in order to achieve better market outcomes and to prevent the anarchy of markets. It should not intervene to safeguard absolute freedoms for businesses or consumers, but to create a balance of social justice and fair business ethics even where this temporarily limits the freedom of action or choice. If the party, who would otherwise enjoy the free choice, is being locked into a service offer, the terms and conditions of which have proven misleading because they cannot be substantially changed, a temporary limitation should be imposed by competition intervention in such unfairness. As has been argued elsewhere,<sup>50</sup> the prohibition of abuse of a dominant position is based on the exploitation of market participants, such as consumers or businesses, through the imposition, directly by the monopolist or indirectly via a distribution supply chain or intermediaries, of higher prices, which cannot be justified economically, or other conditions which are customary practice in trade. In conclusion, using the alternative “other”, where terms and conditions are actually inseparable, a structured economic law of contracts by undertakings is put in place.

#### **D. HOW DOES EU COMPETITION LAW APPLY SECONDARY LEGISLATION OF UNFAIR COMPETITION?**

The terms and conditions implied by banks and imposed on consumers highlight the main objective or primary obligation of the contract to pay for the service. This gives rise to various other obligations on the part of the service provider—known as terms or conditions—with regard to the method of payment itself, the speed of delivery and other

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<sup>50</sup> See AD Chiriță, “The EU Control of Unfair Competition Practices: The Interpretation of Unfair Pricing” in *The German and Romanian Abuse of Market Dominance in the Light of Article 102 TFEU* (Nomos, 2011), 346.

delivery details. There is not much choice over the method of payment. The special regulation only makes sure that electronic payments observe the principle of equality of charges; it says nothing about the terms of payment. Thus, if those terms were to imply higher charges over the statutory level in another EU Member State, then they would simply be unfair. The problem underpinning EU competition law is that there is still no recognition on the part of the EU Commission of secondary legislation on unfair terms as an unfair competition practice.<sup>51</sup> However, there are many such examples in behavioural economics.

As the unfairness of terms needs to be assessed by the courts, not by administrative competition authorities, the latter are considered to be less equipped to conduct the legal analysis of economic contracts. However, are the courts really equipped to deal with economic analysis? Or, to put it another way, what exactly is of the greatest or utmost importance in economic contracts by undertakings: a fair price remuneration in return for quality of service or those secondary terms that only make the primary obligation more onerous? The law, as it stands, has provided two areas in which consumers need protection and welfare. Both of them are complementary in ensuring an overall appraisal of the final service charge. The split of unfair terms and conditions may lead to absurd outcomes. In particular, no judge can conduct a proper economic analysis, whilst competition authorities may not analyse unfair terms, which remains the responsibility of courts. A pragmatic approach to fair EU competition would be to follow the economics of fairness in the character of pricing from cost analysis and supplement it with legal analysis of contracts to favour both consumer welfare and protection. Both terms and conditions reflect a single service package any customer will receive in return for the service charge agreed. It is therefore artificial to discuss them separately when only an overall evaluation of all the facts of the economic service can reasonably determine whether there is fairness or not.

It is beyond doubt that little could be achieved by the study of economics, independently of those financial incentives, to help classify types of terms and conditions based on the individual freedom of contract. This freedom should not be seen as an obstacle for economics, but, rather, as a clarification of who is the weaker party in the course of negotiation. Fair competition has a lot more to say on whether individual customers continue to pay bank charges because they have no alternative or cannot directly negotiate terms implied in trade. The fact that one has agreed to pay the service charge, because one has to, does not make one's bargain fair. A more stringent consequence is that, under Article

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<sup>51</sup> Favours consideration of unfair terms as unfair commercial practice, see S Orlando, "The Use of Unfair Contractual Terms as an Unfair Commercial Practice" (2011) *European Review of Contract Law* 1.

102 TFEU, the character of unfairness is basically restricted to the economic scrutiny of dominant undertakings only and not to any traders as under the law of unfair competition.<sup>52</sup> This is a trap set by the EU Treaty itself and supplemented by secondary legislation which receives no recognition.

Therefore, a narrow interpretation focused on competition rules addressed to dominant undertakings as defined by EU competition law creates a true paradise for those not yet too big to be dominant in the relevant service market, but who could impose unfair terms and conditions in trade and harm consumers directly. On the other hand, the legal interpretation of unfair terms can safely predict as a rule that only those contract terms that are individually negotiated may be found to be fair.<sup>53</sup> However, consumers hardly have any say when proceeding with their electronic payment. There is also no transparency of exchanging information on the conversion rate with the commercial trading bank. How much market share a trading bank has plays almost no role for the inquiry in question. What matters is the market conduct of the bank, which could unfairly charge customers who are placed in a disproportionate bargaining position.

Article 3(1) of the Unfair Terms Directive used a general principle when it defined as unfair those contract terms that, contrary to the above principle, “cause a significant imbalance in the parties’ rights and obligations arising under the contract, to the detriment of the consumer”. This can be translated in the economics of competition to include those situations where there is no consumer negotiating power and more onerous charges for the service. The principle of good faith is intended to cover those honest practices in the market which observe business ethics over market participants. However, even banks cannot risk losing customers in order to gain higher profits in the long run, since fair deals with clients create trustworthy business relationships.

In contrast, an attempt by economics to translate the concept of unequal bargaining power of the seller and buyer which is defined by courts as “unconscionable” has been identified with the economic concept of market or monopoly power.<sup>54</sup> This is in principle correct as regards the economic power of one party which must be significant, but it fails to recognise what courts have intended to interpret, namely, whether any mutual consent is given, and whether during the negotiation process those terms and conditions have been individually agreed or merely imposed by the most powerful party. Thus, the 1992 draft of Directive 93/13 identified the “different bargaining power between the consumer and the

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<sup>52</sup> See the Unfair Commercial Practices Directive 29/2005/EC on business-to-consumers practices, amending the Council Directive 84/450/EEC, Directives 97/7/EC, 98/27/EC and 2002/65/EC [2005] OJ L149; Council Directive 93/13/EEC on unfair terms in consumer contracts [1993] OJ L95.

<sup>53</sup> Whittaker, *supra* n 38, 30.

<sup>54</sup> Posner, *supra* n 32, 13.

supplier as a major distinction between standard terms and individually negotiated terms”.<sup>55</sup> This implied a greater bargaining power of the supplier when the term was negotiated individually.

In conclusion, fair competition based on the freedom of contract recognises the concept of *relative* market power which is a lower measurement or threshold for which both the boundaries and the substance of the market do not matter as much as the conduct on that market does. This is an implied recognition that not only efficient monopolists may treat consumers unfairly, but also less efficient competing market players. Thus, it is not only the pricing itself that is exploitative of consumers,<sup>56</sup> as there may be other *disguised* terms and conditions which altogether make the main pricing obligation more onerous.

The concept of fairness looks like a difficult conundrum for economists for which they must rely on legal interpretation. At this point, it is a fact that competition enforcement is better to pursue because economists speak the same language of economics and often agree with each other more than continental and common law lawyers do on the legal interpretation of contract law. Finally, terms negotiated collectively are typically found in sample or non-binding models of commercial contracts.<sup>57</sup>

## **E. SHOULD COMPETITION ASSESS THE FAIRNESS AND TRANSPARENCY OF BANK SERVICE TERMS?**

One of the most obscure practical outcomes is to ignore the unfairness of both terms and charges because banks are not dominant (scenario I) and, when a trading bank is market dominant, not to assess the fairness of its terms because of their apparent exclusion and analysis in the secondary legislation (scenario II). It is clear that the drafters of the Treaty of Rome could not predict how their proviso would be enforced within a Union of 27 Member States that all have thoughts about what, how and when it is to be achieved. Legal interpretation is intended to correct undesired or absurd enforcement outcomes of rules whose application, based on a mechanical and unfortunate division of competence, results in less welfare for EU consumers. It can also be said that the choice of consumers is significantly impaired as banks are an unavoidable trading partner for efficient, faster payment services. Aside from electronic payments, there is no transparency of information with regard to charges by the foreign bank and shared charges. When an account

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<sup>55</sup> See H-W Micklitz, “Reforming European Unfair Terms Legislation in Consumer Contracts” (2010) 6(4) *European Review of Contract Law* 347, 360.

<sup>56</sup> *Ibid.*

<sup>57</sup> See COM(2010) 348/3, 1 July 2010.

denominated in another currency than the euro is credited there is no explanation of the structure of service costs,<sup>58</sup> shared costs or what is basically known as *hidden charges* because it is not in the interest of banks to inform the customer how much is actually paid for the service. In support of an argument for transparency stands the DG SANCO Study on Bank Charges in Europe (2009)<sup>59</sup> which, following an analysis of electronic payment tools found that even experts had difficulties understanding the price structure.<sup>60</sup>

As has already been explained, the EU attempt to create a SEPA free service market Union-wide does not accommodate electronic transactions from a different currency than the euro. It seems that the past enforcement focus of EU competition law has placed too great an emphasis on the notion of market power and dominance to create the free movement of goods, and perhaps too little on the internal market for services. We can, finally, understand why the Guidance Paper on Article 102 is a reform document of the EU Commission,<sup>61</sup> which was written to meet post-Lisbon challenges.<sup>62</sup> In particular, Article 5 made it clear that consumers benefit from a wider choice of “new” or “improved” services, while Article 11 refers to the “quality” of services as a parameter of competition which may be “influenced to the detriment of the consumer” and several other articles refer to services. It is obvious that a bank, irrespective of its market dominating position, is in a position to influence its customers based on a segmented offering of standard and faster electronic payments.

As has been argued elsewhere by Kaplow<sup>63</sup> product markets definition is mostly defective. One can only strongly emphasise that trying to define the service market for electronic payments is rendered obsolete by narrow market definitions. It can only result in the end in consumers enjoying less welfare because there is no *anti-trust* intervention. It is certainly defective to analyse the market shares of banks when dealing with imposed terms and conditions which are unfair. Why then did the Treaty on the Functioning of the Union introduce a general-abstract proviso in the competition law context? Certainly, it must have had in mind to produce an enforcement outcome (*effet utile*) and generate more protection for individuals over the unfairness spread by big economic players. When the law of

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<sup>58</sup> See in contrast Ridyard, *supra* n 31, 178 on the UK Competition Commission’s criticism of the complexity of personal current account charges and of unauthorised overdraft charges.

<sup>59</sup> See [ec.europa.eu/consumers/.../prices\\_current\\_accounts\\_report\\_en.pdf](http://ec.europa.eu/consumers/.../prices_current_accounts_report_en.pdf) (last accessed on 15 April 2012).

<sup>60</sup> The same result is reached in the Final Report of the Independent Commission on Banking, 7.33, 179.

<sup>61</sup> On the legal impact of soft laws see W Weiß, “After Lisbon, Can the European Commission Continue to Rely on ‘Soft Legislation’ in its Enforcement Practice?” (2011) 2(5) *Journal of European Competition Law & Practice* 441; P Marsden and L Lovdahl Gormsen, “Guidance on Abuse in Europe: The Continued Concern for Rivalry and a Competitive Structure” (2010)

55(4) *Antitrust Bulletin* 707.

<sup>62</sup> Communication from the Commission—Guidance on the Commission’s enforcement priorities in applying Article 82 of the EC Treaty to exclusionary conduct by dominant undertakings [2009] OJ C45/02, 24 February 2009.

<sup>63</sup> L Kaplow, “Why (Ever) Define Markets?” (2010) 124 *Harvard Law Review* 438.

contract referred to terms and conditions which are negotiated individually, it obviously set another task to competition law enforcement for those economic contracts whose terms are only externally influenced and imposed by undertakings on consumers. Naturally, if one reads Article 102 TFEU narrowly, it will then define a relevant service market, analyse market shares, and allow the too big to escape because those banks may never be found to be dominant.

In order to clarify how the imposition of unfair pricing and other trading conditions should be interpreted a closer look is necessary into the EU Draft Common Framework of Reference on contracts.<sup>64</sup> Article 7/13 reads that terms supplied by one party and not individually negotiated may be invoked only (i) if the other party was aware of them or (ii) at least took reasonable steps to draw attention to them. This circumstance is different in contracts concluded by electronic means without “individualised” communication because there is no notice system for these specific transactions. This requires banks that supply terms to invoke them against the consumer only if they were made available in textual form, before or at the time of the conclusion of the order. We have also seen in the Bank Charges case that the economists’ solution lies in overdraft warnings *ex ante*.<sup>65</sup>

As can be understood from the example given below, if a foreign bank imposes no charges in euro for SEPA payments, any consumer relying on that information would not check it twice if the receiver does, as he should not be bound by a service contract with a third party whose terms and conditions are unknown. The original bank should inform the consumer whether the payment is free of charge until it reaches the border of the foreign bank and how much it will be charged thereafter. Otherwise, the imposition indirectly by the receiver of inter-banking fees is not justified because there is no effort on the part of this bank to improve the quality of its service in ensuring better transparency. That no automatic information exchange service exists to advise the client how much the service will cost is an unacceptable technical default due to a lack of innovation.<sup>66</sup> The consumer has only one alternative: to wait until the payment, or better said, what is left of the payment after deducting higher service charges, reaches the destination on the account credited in a local currency.

In contrast, the Court of Justice made it clear that the legal protection conferred on consumers by the Unfair Terms Directive is extended to those economic contracts with

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<sup>64</sup> 64 Prepared by the Study Group on a European Civil Code and the Research Group on EC Private Law (Aquis Group), see [ec.europa.eu/justice/contract/files/european-private-law\\_en.pdf](http://ec.europa.eu/justice/contract/files/european-private-law_en.pdf) (last accessed on 15 April 2012).

<sup>65</sup> Armstrong and Vickers, *supra* n 38, 15.

<sup>66</sup> See, eg Ridyard on static markets for banking services, *supra* n 31, 173; see also Almunia, *supra* n 3, who noted the perverse effect of the interchange fee, where banks compete by offering higher fees and consumers are happy because they do not know the true costs of such payments.

sellers or suppliers where the consumer is unable to litigate over the unfairness character, either because “he is unaware of his rights or because he is deterred from enforcing them on account of the costs which judicial proceedings would involve”.<sup>67</sup> There is no better example of lack of information than bank clients using online banking services, especially when those services cross the border of one Member State to another. For example, an EU national resident in a country of the Eurozone wishing to transfer money using a SEPA online order form is charged unfairly by a UK bank. When a complaint is raised, the euro bank justifies itself by saying that the foreign bank charged extra fees that it did not communicate to the customer. In dealing with this claim, a consumer would, in practice, need to introduce the complaint to a foreign bank, in another state of his domicile, and fight and win against a powerful commercial bank. This is an impossible mission, particularly when the conflict of rules dictates that an EU national has to introduce lawsuits on unfair competition to the competent court. This is based on the understanding of the Rome I Regulation on the Law Applicable to Contractual Obligations.<sup>68</sup> In particular, the general choice of contract law can vary because, “as regards contracts concluded with parties regarded as being weaker, those parties should be protected by conflict-of-law rules that are more favourable to their interests than the general rules”.<sup>69</sup>

The Rome I Regulation has recently been mentioned in one of the recitals of the EU Parliament’s Draft Report on the Adoption of an EU Contract Law.<sup>70</sup> The report expressed concern that “the application of foreign (consumer) law to cross-border transactions under the Rome-I Regulation has been seen to entail considerable transaction costs for businesses, in particular for SMEs, which have been estimated at €15,000 per business and per Member State”.

Therefore, EU laws do not protect even businesses in cross-border transactions because their substance is not in line with the current economic context and the digital revolution. Paragraph 14 of the report suggests linking the optional instrument of EU contract law with the EU Order of Payment and Small Claims Procedures. Thus, the Union’s legitimate legislative body also lacks a great deal of pragmatism. An Electronic Payments Supervision of financial services would not make economic analysis work as efficiently as DG Competition in competition matters.

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<sup>67</sup> See C-473/00 *Cofidis SA v Jean-Louis Fredout* [2002] ECR-I-10875, para 34; C-243/08 *Pannon GSM*

<sup>68</sup> EC Regulation 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations [2008] OJ L177/6.

<sup>69</sup> See recital 23.

<sup>70</sup> See European Parliament, Committee on Legal Affairs, Draft Report on policy options for progress towards a European Contract Law for consumers and businesses, 2011/2013 (INI), 25 January 2011, recital E.

Based on the empirical data available,<sup>71</sup> another conclusion overlaps both EU contract and competition soft laws. The Commission raised concern over business-to-consumers e-commerce because “consumers are disadvantaged by limited product choice, higher prices and lower quality due to weak cross-border competition; consumers even may be refused access to cross-border offers altogether”.<sup>72</sup> The Guidance on Article 82 EC says that “consumers benefit from competition through lower prices, better quality and a wider choice of new or improved services”.<sup>73</sup> Therefore, the Commission will pursue enforcement against “conduct which is directly exploitative of consumers, for example charging excessively high prices”, in accordance with Article 102(a). The Guidance is also mindful that “certain behaviour . . . undermines the efforts to achieve an integrated internal market”, which is the internal market for services of economic interest. This is particularly relevant because the lack of intervention in the banking sector contributed to the current financial unrest. It is indisputable that there is a competition consumer-protection function of intervention, elsewhere argued as unfair competition,<sup>74</sup> “in particular where the protection of consumers and the proper functioning of the internal market cannot otherwise be adequately ensured”.<sup>75</sup> If cross-border payments involving unfair bank charges are not sufficient ground for competition intervention, how is this goal to be achieved in practice? One may argue, with reason, that the Commission should not intervene, but it would be deplorable to have an enforcement mechanism with no economic expertise on competition matters and to split the service market and consumer claims elsewhere. Thus, the Commission has the pragmatic solution of having DG Competition, trained in economics, to build on its existing strengths in competition law.

Finally, another argument is to build on the positive assessment of what is fair. How can one know that pricing is fair? The obvious concern is that consumers are happy with reasonably low pricing. But is this the only value to define fairness? Another powerful argument considers fairness with regard to the transparency of the terms and conditions. Since 1998, the Unit Price Directive<sup>76</sup> has set out the common pricing rules for retail sales according to which products should be offered at a final selling price, including VAT and taxes. Not observing these sales requirements is clearly considered an unfair competition

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<sup>71</sup> See the EU Commission, Communication of 22 October 2009 on Cross-Border Business-to-Consumer e-Commerce in the EU, COM(2009) 0557.

<sup>72</sup> *Ibid.*, 9.

<sup>73</sup> Guidance Paper on Art 82 EC, para 5.

<sup>74</sup> AD Chiriță, “Undistorted, (Un)fair Competition, Consumer Welfare and the Interpretation of Article 102 TFEU” (2010) 33(3) *World Competition Law and Economics Review* 417. In favour of Article 12 TFEU supporting a “common approach to how consumer protection measures should be interpreted” see, eg Whittaker, *supra* n 38, 115.

<sup>75</sup> Guidance Paper on Article 82 EC, para 7.

<sup>76</sup> Directive 98/6/EC of the European Parliament and the Council of 16 February 1998 on consumer protection in the indication of the prices of products offered to consumers OJ L080/27 [1998].



practice.<sup>77</sup> It also remains questionable whether transparency in service pricing should also stress more competition actions against price partitioning, which intentionally fragments the basic price only to add other “indispensable” items to be selected to top up the final price. Should the average well-informed consumer be an expert in behavioural economics in order to detect the exact point at which he was locked in, induced, forced, misled and so forth? If such price partitioning occurs, should it not be for the EU Commission to intervene directly and correct unfair market behaviour? Or should one have to go before the national court to be told that a contract concluded without noticing the terms and conditions, written in clear language, is still a valid contract? What happens when an otherwise diligent consumer fails to untick an additional service and ends up paying a higher insurance cover which was never needed? It is absurd to expect only the courts’ intervention and to rely on their economic analysis when those courts often fail to interpret coherently their own contract rules and to provide a cogent legal analysis.

For FA von Hayek, the primary objective of competition was to “discover the still unknown possibilities in a society where competition was previously limited”.<sup>78</sup> This means that competition enforcement should be open to new dimensions of unfairness, irrespective of whether they are regulated in advance or not. Since “competition represents a kind of personal coercion that will cause many individuals to change their behaviour in a way that could not be brought about by any kind of instructions or command”, in our context, having grey unfair terms exemptions, of which businesses are aware in advance, will act as a knowledge safeguard not to pursue certain unfair practices. This by no way means that businesses will not seek new ways to potentially harm consumers.<sup>79</sup>

## F. CONCLUSIONS

Recently, the EU Commission opened a SEPA investigation into an alleged refusal to set up a business standardised method of payment, whereby a specific logo could be used to indicate that an electronic payment is secure, in order to reassure consumers of the safety of their online transaction.<sup>80</sup> The investigation follows a competitor’s complaint and could be extended to include collusion by banks over credit default swaps under Article 101 TFEU.

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<sup>77</sup> For behavioural economics of price partitioning see, eg WH van Boom, “Price Intransparency, Consumer Decision Making and European Consumer Law” (2011) 34 *Journal of Consumer Policy* 359.

<sup>78</sup> FA Hayek, “Der Wettbewerb as Entdeckungsverfahren” (2002) 5 *Kieler Vorträge* 56 (Institut für Weltwirtschaft 1968) 2; (2002) 5 *Quarterly Journal of Austrian Economics* 3, 9–23 (translated by MS Snow).

<sup>79</sup> On services of general economic interest harmful to consumers see P Rott, “Consumers and Services of General Economic Interest: Is EC Consumer Law the Future?” (2007) 30 *Journal of Consumer Policy* 49.

<sup>80</sup> EU Commission, Press Release IP/11/1076, 26 September 2011.

The current financial crisis is also caused by the weak competition intervention in the banking sector. For financial transactions, the banking sector already makes use of sophisticated service techniques involving risks such as “predatory borrowing”,<sup>81</sup> and there is no transparency of information. Non-intervention is accepting that the consumer must know everything when he buys any financial package.

There is a massive proliferation of cases, both insignificant and major, where EU consumers, including intermediaries, have limited resources to ever challenge their own business failures against commercial banks. This has in turn led to the assumption that the consumer will always cover the risk of failure. Banks are too big to fail, especially when—at the expense of those misled into buying risky service packages, with intricate terms and conditions— they also receive financial aid incentives. In practice, the EU consumer has often to pay the costs of intelligent techniques and business strategies.

In conclusion, the SEPA economic regulation has attempted to solve a number of problems but has not solved any of them—perhaps because SEPA is descriptive of what should happen, not of how it should happen. There is, however, hope that the EU competition enforcement will extend its business-to-business market investigations of serious competition concerns to consumer welfare. There is no better enforcement mechanism than competition for the application of secondary legislation in the economic context of EU competition rules. The Court of Justice has already highlighted that one should not wait for the less-informed consumer to complain over unfair terms because he/she might not have the economic resources to do so. Instead, this should be a matter for public enforcement. The critical paradox is to intervene in favour of a bank’s market competitor but to remain passive to the needs of the thousands of EU consumers affected. Why did the Council enact a regulation without prescribing enforcement powers at the national level? Both the form and content of the regulation could have been achieved by means of a weaker legal act, such as a harmonising directive. How should one attempt to simplify the saga of how customers are economically dependent on powerful businesses that impose on them packages of financial services, whether minor or of significant value, which induce the most rational consumer to agree to services which prove to be unfair? Turning back to the EU law issue of cross-border payment services, they do not yet provide the simple service that EU citizens should enjoy: the free movement of one’s own gains in capital and a market for services that is not only free from barriers, ie there are no inter-banking fees and the exchange rates are transparent, but also a timely, efficient service. The

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<sup>81</sup> On the sophistication of securitisation transactions see, eg O Akseli, “Was Securitisation the Culprit? Explanation of Legal Processes behind Creation of Mortgage-backed Sub-prime Securities” in J Gray and O Akseli (eds), *Financial Regulation in Crisis? The Role of Law and the Failure of Northern Rock* (Edward Elgar, 2011), 7–9.

SEPA has already enacted two regulations to eliminate cross-border barriers to the electronic trade. The

unfortunate conclusions are that there are fewer SEPA benefits EU-wide and that banks are in a powerful position to dictate their own terms and conditions, based on the narrow area of application of the regulation. The overall impression is that the EU fails to reach its own ambitious goals because of a lack of coherence with other fields of law, and efficiently coordinated enforcement mechanisms; it either enacts too many economic regulations or directives, or enacts them too late, and what used to be a structured understanding is lost in the processing of a vast amount of Union rules by national courts that may have different legal traditions of doing things. The 2009 Regulation is a missed opportunity, and the challenge of EU competition enforcement remains.