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Canada's Prohibition of Automated Bank Machine Withdrawal Charges as a Violation of the WTO's GATS

by David Collins*

I INTRODUCTION

Much has been made recently of Canada's transgression of its international obligations under the Kyoto Protocol and (less spectacularly) the UN Convention on the Control of Narcotic Drugs raising concern that Canada is no longer emblematic of the concerned world citizen. This image may be further tainted by another administrative directive from the Canadian cabinet this year that could violate the nation's key international commitment to liberalize trade. The Canadian Minister of Finance announced in January of 2007 the planned intention to change the Federal Bank Act[1] to require that banks operating in Canada cease imposing service charges for cash withdrawals at automated banking machines. This measure may violate international obligations, depending on what form the regulation ultimately takes if implemented, because while the prohibition appears directed at Canada's largest domestic banks it could also adversely affect foreign banks operating in Canada. This article will illustrate that the enforced elimination of bank service charges, although commendably aimed at protecting consumers from corporate gouging, may represent a violation of the General Agreement on Trade in Services ('GATS') to which Canada is committed as a member of the World Trade Organization ('WTO'). This article will examine in what way this putative regulation, and various potential modifications of it, may breach the GATS should they come into force. This article will not consider any implications that may be engaged under competition law or contract law

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[1] BANK ACT CITATION

Electronic copy available at: http://ssrn.com/abstract=1552942

relating to unfair terms, nor will it evaluate this regulation in light of the North American Agreement on Free Trade or the Organization for Economic Cooperation and Development Code on the Liberalization of Capital Markets. It is helpful to begin with a brief outline of the planned measure and the debate it has stirred.

II AUTOMATED BANK MACHINE SERVICE CHARGES

Canadians paid an estimated $420 million in automated bank machine withdrawal fees in 2006, a year when the earnings of these banks was over $19 billion[2] (source Statistics Canada). In 2005 there were over 15,000 automated banking machines across Canada accounting for over 1 billion transactions.[3] Individual service charges are usually between $1 and $2 per transaction, with higher fees imposed when withdrawing from a machine belonging to a financial institution other than the one in which the customer's account is kept. Federal Bill C-37 tabled to modify the Bank Act which regulates the banking industry in Canada contains only one consumer protection measure and does not address the issue of high service charges imposed on Canadian customers. Such charges are not imposed by banks operating in other developing countries, notably the United Kingdom and the United States. Failing to curtail such charges has been viewed by consumer protection advocates as a "right to gouge"[4]

This article will consider possible permutations of the bank machine withdrawal fee regulation, namely, the selective imposition of the measure against certain types of banking institutions, possibly in relation to the size of their assets or the precise amount of service charge imposed. It must be emphasized from the outset that there is no indication that this is actively in the contemplation of the Ministry of

[2] STATISTICS CANADA
[3] SOURCE: Canadian Bankers Association <https://www.cba.ca.en>
[4] Canadian Commercial Reinvestment Coalition <http://www.cancrc.org/english/relJan2607en.html>

Electronic copy available at: http://ssrn.com/abstract=1552942

Finance, so in that sense the arguments presented herein are purely speculative. Of primary concern is the effect that such potential restrictions may have upon foreign banks authorized by the Federal Bank Act to operate branches in Canada, of which there are currently 22, most of which have their home branches in the United States.[5] Any measure which encroaches on the provision of a service that has an international element accordingly raises issues relating to Canada's commitment under the GATS. It is these commitments to which we will now turn.

III GATS GENERAL OBLIGATIONS- MOST FAVOURED NATION

The GATS is perhaps the most complex potentially wide ranging of the WTO Agreements. As part of the WTO collection of agreements the GATS aims to achieve free trade in services by reducing the regulatory barriers on services that cross borders. Penetrating deeply in domestic regulation, GATS affords wide protection to multi-national businesses, such as banks, which trade services, as defined in Article I (2) by one of the four modes of supply. The third mode of supply, Commercial Presence, is relevant for the purposes of this article: GATS obligations apply to services by a service supplier of one WTO Member through commercial presence in the territory of any other Member. The GATS itself does not define Financial Services, but Annex on Financial Services to the agreement defines Financial Services to include, *inter alia*, banking services.[6] GATS will thus apply to the regulation of a foreign bank which operates a branch in Canada. Article II of the Annex on Financial Services permits Members to establish prudential regulatory measures to protect investors in order to ensure the integrity of the financial system – an authorization that

[5] SOURCE: Canadian Bankers Association: <http://www.cba.ca/en/>
[6] Article V.

contemplates the basic functioning of the system and consequently has limited scope.[7] While the concept of a prudential measure should evolve over time, it is suffused with an obligation of good faith to prevent abuse.[8] The prudential measure exception would not encompass price restrictions on particular banking services.

The possibility that the bank service charge elimination will apply to some banks and not other (e.g. should the regulation only apply to the largest banks) or potentially the location of the automated machine (e.g. should the regulation only apply to automated machines in affluent areas) could violate the Most Favoured Nation obligation under GATS Article II if banks which have their home branch in different Member states are treated differently. This article prohibits discrimination between like service and service suppliers from different countries and General Agreement on Tariffs and Trade ('GATT') jurisprudence suggests that the "effect" of a measure will include incidental effects – harm to a member that may not have been intended.[9] "Likeness" is not defined in GATS but principles drawn from GATT may be helpful. Consequently likeness should include the general features of the service, how it is classified by the United Nations, as well as potentially consumer habits and preferences. As automated bank machines share the same primary feature, that they dispense cash, it is not difficult to conclude that they are substantially "like", irrespective of the bank with which they are affiliated.

The Panel in EC Bananas established also that entities providing "like" services should be considered "like" suppliers[10], which has been criticized as an overly broad concept of likeness in that it is focused entirely on the characteristic of

[7] C. Thomas, "Globalization in Financial Services: What Role for GATS" 21 Annual Review of Banking Law 323 at 331
[8] Leroux at 431.
[9] Both *de jure* and *de facto* discrimination are prohibited. AB in EC Bananas at paras 233-234.
[10] CITATION para 7.322

the service itself while ignoring completely the characteristics of the supplier.[11] In a strict sense, small banks and large banks are not truly "like" service suppliers. The value of a deposit held in a bank is linked to that bank's performance over time: more successful banks are able to provide higher rates of interest.[12] Well-established providers are not like new market entrants of foreign origin[13] because well-established providers may depend less on service charges than new market entrants therefore might be deserving of different treatment. The confusion over likeness in relation to services is multiplied when one considers that the underlying transaction through an automated bank machine is for the provision of goods (namely cash) and the service aspect is merely an accessory, a situation that is outside the GATS concept of trade in services.[14] The GATS' inadequate classification scheme has been criticized for exacerbating problems with core and incidental services.[15] However, measures can be simultaneously challenged under both GATS and GATT as they are both part of the WTO Agreement, although the Appellate Body in *Canada – Periodicals* avoided deciding how to deal with products that are simultaneously goods and services[16]. Admittedly it would be difficult to envisage bank machine withdrawals as goods transactions, as cash is only a means of facilitating further transactions rather than something which can itself be consumed and also because the cash in question already belongs to the consumer. As such bank withdrawals would not be within the scope of GATT.

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[11] Zdouc at 333
[12] Trachtman at 67
[13] Zdouc at 333.
[14] The failure of GATS to encompass trade in services in association with trade in goods is examined in greater detail by A Abu-Akeel, "Definitions of Trade in Services Under the GATS: Legal Implications" 32 George Washington Journal of Law and Economy 189 at 192-196. See also C Thomas ABOVE NOTE X at 327 and TREBILCOCK AND HOWSE AT 349.
[15] A Matoo and S Wunsch-Vincent, "Pre-Empting Protectionism in Services: The GATS and Outsourcing" 7 J International Economic L 765 at 774-778.
[16] WT/DS31/AB/R par 19 (magazines as goods and advertisement as a service).

The fundamental issue to be kept in mind is that according to GATS case law which, as noted above, focuses on the nature of the service rather than the nature of the supplier, banks of all sizes and all sizes and types of assets which offer automated cash withdrawal are comparable for the purposes of GATS. Thus there is significant potential to engage the aforementioned Most Favoured Nation obligation, as well as the Specific Obligations of National Treatment and Market Access, which we will now examine.

IV GATS SPECIFIC OBLIGATIONS – NATIONAL TREATMENT AND MARKET ACCESS

The GATS contains specific obligations meaning that they are only engaged if a Member has made specific commitments in that sector. These highly qualified rules embrace National Treatment, which has been described as the "core" of GATS[17], and Market Access. Canada's Schedule of Commitments lists Financial Services and does not contain any restrictions such as those regarding service charges and consequently the GATS specific obligations apply and must be considered when any measure is taken that may affect the international provision of these services. Canada's current exemptions under its Scheduled Commitments involve primarily constraints on foreign ownership of banking institutions.

Again it should be emphasized that the withdrawal fee measure as planned should not contravene the National Treatment obligation of Article XVII (prohibiting discrimination between the treatment of foreign and domestic suppliers in such a way that foreign suppliers face competitive disadvantages) as there is no indication that the measure will be applied to foreign banks and not to domestic ones. It appears as

[17] M Matsushita, T Schoenbaum, P Mavroidis, *The World Trade Organization* (PUB INFO) AT 230.

though the measure is primarily intended to regulate fees charged by Canada's six largest domestic banks. However, should select domestic banks be exempt, perhaps because of their smaller capital holdings, the government must ensure that foreign banks of similar size (and thus "likeness") enjoy the same exemptions from the regulation. Indeed, "better than National Treatment" may be necessary to allow free trade in services where the application of the domestic regulation would inappropriately deter or foreign entry or undermine competitive opportunities.[18] This preference for substantive rather than formal National Treatment could entitle a foreign bank to an exemption from the withdrawal fee prohibition on its bank machines to allow it to gain a foothold in the Canadian banking market dominated by domestic institutions. Trachtman has summarized this cogently:

> ..regulation that has non-trade purposes may affect foreign service providers differently than domestic providers that have grown accustomed to local regulation, have structured their affairs optimally in light of local regulation …the cumulative application of host …state regulation may dampen the competitiveness of foreign service providers.[19]

In contrast to this view, footnote 10 to Article XVII on National Treatment states that a Member's National Treatment commitment does not require it to "compensate for any inherent competitive disadvantages which result from the foreign character of the relevant service or service suppliers." However a restrictive interpretation of this footnote was taken by the Panel in *Canada – Autos* which held that the footnote "does not provide cover for actions which might modify the conditions of competition against services or service suppliers which are already disadvantaged due to their

[18] Joel P Trachtman, "Trade in Financial Services Under GATS, NAFTA, and the EC: A Regulatory Jurisdictional Analysis" 34 Columbia Journal of Transnational Law 37 at 65-66 and TREBILCOCK AND HOWSE AT 366.
[19] Trachtman ABOVE NOTE X at 46.

foreign character."[20] Such a disadvantage could be consumer's unfamiliarity with a foreign bank's name or brand. Consequently there may be room to suggest that any measures which harm foreign banks to a greater degree than domestic banks could contravene Canada's National Treatment obligation.

Of greater concern is Canada's specific Market Access obligation for Financial Services as outlined in Article XVI of GATS. This is an obligation for each Member to proactively open up its markets to permit entry of foreign suppliers. Accordingly Article XVI(2)(b) prohibits: limitations on the total value of service transactions or assets in the form of numerical quotas or the requirement of an economic needs test. A prohibition on withdrawal charges is a limit on the total value of service transactions (the value limit on withdrawal transactions is zero). Should the withdrawal fees be permitted in higher income areas (or only prohibited in low income areas) this would amount to an economic needs test. It is important to recognize that for such a measure to transgress the Market Access commitment it need not be discriminatory (inconsistenly applied to foreign and domestic suppliers) – non-discriminatory barriers of this kind are also impermissible.[21] The potential for non-discriminatory measures to transgress commitments is seen in the text of the the Understanding on Commitments in Financial services, which formed part of the Uruguay Round negotiations and outlined a framework to the liberalization of trade in financial services as alternative to Part III of the GATS. The Understanding is not binding on every WTO Member, only those who voluntarily adhered to it, including Canada and most members of the OECD. Article 10 of the Understanding requires a commitment from a Member to "endeavour to remove or limit any significant adverse effects on financial service suppliers of any other Member" and specifically lists

[20] CANADA AUTOS CITE PARA 10.300
[21] Van den Bossche at 483.

"non-discriminatory measures that prevent financial service providers from offering in the Member's territory, in the form determined by the Member, all the financial services permitted by the Member."[22] A withdrawal fee prohibition against both domestic and foreign banks may be a *prima facie* neutral barrier but they have a discriminatory effect because new entrants will suffer more than established businesses and new entrants are likely to be foreign providers.[23] Thus it could be argued that well-established foreign banks may not actually be harmed any more than domestic ones. Newer foreign entrants, for example banks from Eastern European states, could still suffer from this regulation, particularly when one considers that such banks might be more reliant on their service charges from Canadian clients than a large Canadian bank would be. It has been suggested that negotiations leading up to the Agreement on Financial Services, which focused on crystallizing pre-existing liberalization, were lacking with respect to the introduction of competition through new entrants[24] and perhaps this mentality has persisted in the mindset of domestic financial regulators. Of course, any negative effects on new entrants would have to be demonstrated through a full review of the market situation, as indicated by the Appellate Body in *Canada- Automotive Industry*.[25] Evidentiary problems associated with evaluating the particular situation of each private operator have been noted by Zdouc, who has also suggested that representative samples might be acceptable.[26] Still, it is at least probable that as Canada has undertaken Market Access commitments with respect to Financial Services, then it cannot maintain a restriction that limits the value that a bank may charge for a particular service.

[22] Understanding on Commitments in Financial Services Article 10 b.
[23] Trachtman at 78.
[24] MATSUSHITA at 252.
[25] CITE CASE para 164-165.
[26] Zdouc at 339-340.

Van den Bossche has suggested, without explanation, that price controls which impose minimum or maximum prices on services would not constitute a market access barrier.[27] It is far from clear that this is an accurate viewpoint. We can take from this theory that whether a measure will be regulated by XVII:2 may depend on the precise way in which it is phrased. If the regulation establishes that no withdrawal charges are permissible then it might survive a strict analysis, however if the measure limits a bank's total revenue from automated service charges then it would transgress GATS. Thus it is conceivable that Canada could achieve its consumer protection objective in a non trade-violative way. Delimatsis urges that the restrictions in subparagraph XVI:2 will be applicable as long as the measure is in some way quantitative, irrespective of whether a number is actually used.[28] The measure need not be explicitly cardinal, as long as it is descriptively so. Thus measures which incorporate words like "none" or "all" or even "some" would fall within the purview of that section.

V EXCEPTIONS

General exceptions to GATS obligations are included under Article XIV for measures that protect public morals; public order; health of humans, animals or plants; the prevention of fraud and protection of privacy; the collection of taxes and national security. The only plausible exception for bank machine withdrawal fee prohibition is public order. Banking services have been viewed by some as "essential services" similar to heat, electricity and phones[29] and consequently any barrier to them is an affront to the proper functioning of society. This is particularly so as more than a

[27] Van den Bossche at 497
[28] P Delimatsis, "Don't Gamble With GATS: The Interaction Between Articles VI, XVI, XVII and XVIII GATS in Light of the *US Gambling* Case" 40 J of World Trade 1059 at 1068.
[29] Canadian Commercial Reinvestment Coalition <http://www.cancrc.org/english/relJan2607en.html>

third of Canadians have reported that automated banking machines are their principle means of conducting financial transactions.[30] Accordingly sectors of society such as those with low incomes, students and the disabled might be seen as especially vulnerable to high banking fees. In a similar ideological vein, domestic control of the banking system, and with it the economy, is a vital component of a nation's sovereignty.[31] Consequently the ability to regulate bank's operating within one's territory should fall within the sphere of public order.

However the footnote to Article XIV explains that the public order exception may be invoked only where a genuine and sufficiently serious threat is posed to one of the fundamental interests of society. This appears to be a very high threshold and consequently it is unlikely that a minor financial burden to most elements of society would engage the public order exception. The public order exception was successfully invoked in the *US – Measures Affecting Gambling*[32] decision – the control of gambling was seen as a key aspect of public morals and public order by the WTO Panel and the Appellate Body. However the Appellate Body refused to permit the exception to operate as it was applied in a discriminatory fashion. GATT caselaw on these exceptions (which are substantially similar to those under GATS) may be also be illustrative and suggests that "necessary" means that the measure must be an "indispensable" means of achieving the objective, although this will be decided on a case by case basis.[33]

There are several important reasons why automated bank withdrawal machines are not an essential service and they can all be generally categorized under the heading of consumer choice. If there is a viable alternative to using the service,

[30] SOURCE: Canadian Banker's Association <http://www.cba.ca/en/>
[31] Trachtman ABOVE NOTE X at 48
[32] Panel Report WT/DS285/R, AB Report WT/DS28/AB/R
[33] Panel Report, EC-Sardines WT/DS231/R; AB Report, Japan – Agricultural Products WT/DS76/AB/R

then the service cannot be classified as essential such that the public order exemption can be invoked. First, clients of banks are free to withdraw cash from bank branches in person, which although perhaps not as convenient as automated machines that can be found throughout the city and are open constantly, do offer the same service. Thus the issue is really one of convenience, and it is difficult to argue that convenience, meaning here same service with less effort, could possibly withstand judicial scrutiny as an "indispensable" exemption from an international treaty obligation. The Canadian Banker's Association notes that 75% of cash machine withdrawals do not result in service charges because they are by customers using their own banks. Using these higher-fee machines most often represent convenience in the form of mere metres of walking distance to a bank machine of the consumer's own bank. Avoiding inconvenience of this nature is not essential. While cash itself is debatably essential (credit and debit cards have rendered it largely redundant) easy storage and retrieval of it is not. The popularity of banks that impose no service charges and maintain no automated withdrawal machines, such as ING Direct, is testimony to this.

The "essential" nature of the automated withdrawal service is further fallacious because there are other ways in which machine withdrawal charges can be avoided (other than using one's own bank). The most obvious of these is to make fewer withdrawals of larger quantities – indeed most banks have a small number of free withdrawals per month that might be termed "essential" withdrawals. Withdrawals beyond those exempted transactions could well be viewed as superficial or luxury withdrawals. Consumers can also obtain cash back on debit card purchases in stores. Again, convenient access to cash is itself a service distinct from the value obtained from a simple bank account in isolation (such as security and interest payments). The Canadian Banker's Association has observed that cash withdrawal

machines not operated by the banks themselves (so-called White Label machines) that are found frequently in stores and which charge even higher service charges have become incredibly popular – demonstrating that Canadians are willing to pay for the convenience of easy access to cash.[34] This convenience is provided at cost to the banks, who have commented that there is a significant expense in maintaining a network of machines. The banking industry has reportedly spent more than $30 million investing in technology to deliver automated services to customers.[35]

Finally, while it was not intended that this article examine bank withdrawal fees from a contract law perspective, it should be noted that there are no provisions regarding maximum prices for goods or services in any provincial consumer protection legislation.[36] Moreover, there is international precedent, for example under the European Community Directive on Unfair Terms in Consumer Contracts, establishing that the evaluation of the price of a good or service is outside the scope of a court's discretion when assessing the fairness of contractual terms.[37] The common law has also shown that the availability of an alternative for the consumer – many examples of which have been suggested above – is strongly indicative of equal bargaining power and therein legal validity of contractual terms.[38] Of course, one of the primary concerns with bank service charges is that consumers are not aware of them suggesting that greater transparency requirements be imposed upon banks, a consideration which is also outside the scope of this article.

Even if the elimination of service charges were to fit under an extremely generous interpretation of public order, the exception would still need to satisfy the chapeau of Article XIV which requires that the measure not constitute a disguised

[34] NATIONAL POST ARTICLE SAVED ON FAVOURITES
[35] P Viera, "Flaherty Demands Direct Answers on ATMs" The Financial Post, 15 February 2007.
[36] EG ONTARIO ACT
[37] CITATION REG
[38] Eg *Smith v Eric Bush* [1990] 1 AC 831 (HL).

restriction on trade in services. This contemplates not the specific content of the measure, but the manner in which it is applied – it cannot be applied in a way that abuses the enumerated exceptions.[39] There is no GATS caselaw on the application of this requirement, but a similarly worded provision can be found in GATT where case law has suggested that this requirement is meant to prevent an abuse of the Article XIV exceptions, ensuring that a balance be struck between the regulatory rights of the Member and its international duties.[40] The purpose of the bank service charge clearly does not aim to interfere with the international trade of financial services and in that sense an attempt to invoke the public order exception should not rightly be seen as an abuse of the exception, however this caution underlines that the exceptions will be scrutinized vigorously. Additionally, the text of the chapeau and the *US-Gambling* decision urge that for an exception to be valid, all WTO consistent alternatives must be explored first in order to achieve the least trade-restrictive measure that fulfils the policy exception and this may include negotiations with Members[41]. Eliminating other bank service charges, such as those associated with banking in person in a branch have been debated, however these other service fee eliminations have been contemplated *in conjunction* with withdrawal fee removal, not in place of them and (FOOTNOTE NEWS ARTICLE), there is no indication that this was conducted via international negotiation with a view to limiting trade restrictions on foreign banks.

Additionally, it is difficult to argue that the goal of regulating the banking industry, and accordingly ensuring the integrity of the domestic economy, is an aspect of public order as withdrawal fees represent a miniscule portion of bank's revenues, generally estimated at approximately 5% of their total revenues. Certainly there would be more

[39] E Leroux, "Trade in Financial Services Under the World Trade Organization" 36 J of World Trade 413 at 425.
[40] Van den Bossche at 627-628. See also M Park, "Market Access Exceptions under the GATS and On-line Gambling Services" 12 Southwestern Journal of Law and Trade in the Americas 511.
[41] Park at 520-521.

effective alternatives. With all these considerations in mind the regulatory elimination of bank service charges would probably not be saved by one of the GATS exceptions.

VI CONCLUSION

GATS is a very broad and complex agreement that provides enormous protection to multinational corporations and the Canadian federal government must be mindful of its international obligations under this agreement when implementing any restrictions on bank's ability to impose service charges to automated bank machine withdrawals. Depending on what form these restrictions ultimately take, if any, Canada may transgress one or more of the Most Favoured Nation, National Treatment and Market Access provisions of GATS, particularly if the restriction is not imposed universally. Even with the goal of consumer protection in mind, it is unlikely that any discriminatory effects suffered by ubiquitous foreign banks would survive through GATS exceptions, most notably because of the large degree of consumer choice that remains available to those who use bank machines. One of the underlying purposes of the GATS' Commercial Presence category is to liberalize foreign direct investment and any hindrance of that aim must be approached with extreme caution. At a foundational level while denying domestic consumers benefit of a costless service, this measure represents a potential assault on international free enterprise and accordingly a violation of GATS. It is an aphorism that GATS is less concerned with consumers than it is with producers, and perhaps this is a flaw of the WTO regime itself, but until that is corrected, Canada's obligations under it must continue to colour our domestic policies.