

ELECTRONIC RETAIL PAYMENT SYSTEMS IN CONFLICT OF LAWS:

Basic Electronic Payment Systems and Determination of the Applicable Law in North America and Europe**

*Dr. Banu Şit**

ABSTRACT

Emerging technological process has been affecting legal relationships and payment transactions. While contract formation via telephone, fax, telex and telegraph had been argued a few decades ago, today existing communication methods have been developing and affecting a wider part of the legal world on the one hand while on the other hand the internet came on the scene as a new mode of communications.

The law has responded to these technological advances in two ways: either by adapting existing legal framework to cover new technological effects on legal institutions and relationships or by establishing new legal framework in accordance with the demands arising from new technology.

In particular payment methods are developing in parallel with technology and international payment transactions are drawing special attention in terms of determining the law applicable to these transactions. The general view on this issue is characterized on splitting relationships. However the speed and complexity of electronic payment transactions has made those transactions controversial in terms of the applicable law. The main point of this issue is whether a single body of law should govern those transactions as a single transaction or the view of splitting should be considered to be the principal view.

*** This study has been prepared in Dalhousie University Law and Technology Institute, while the author was a visiting scholar provided a post - doctorate grant by Turkish Academy of Sciences.*

** Gazi University, Assistant Professor of Private International Law.*

This article examines electronic payment systems and the law governing international electronic payment transactions with respect to that argument.

ÖZET:

İletişim teknolojisindeki yenilik ve değişiklikler, hukuki ilişkileri ve ödeme sistemlerini etkilemektedir. Sözleşmelerin kurulmasına ilişkin olarak telefon, telgraf, teleks ve faks gibi araçların rolü daha önceleri inceleme konusu edilmiştir. Günümüzde bu iletişim araçları daha geniş bir etki alanına sahiptir ve ayrıca Internet yeni bir iletişim ortamı olarak ortaya çıkmıştır.

Gelişen teknolojik araç ve yöntemlerle ilgili hukuki sorunlara hukukun yaklaşımı ise iki temel üzerinde belirginleşmektedir. Bunlardan ilki, var olan hukuki düzenlemeleri teknolojinin getirdiği yenilik ve değişikliklere uyarlamak; ikincisi de yeni teknolojinin gereklerine uygun olarak yeni hukuki düzenlemeler getirmek şeklinde karşımıza çıkmaktadır.

Ödeme sistemleri de iletişim teknolojisindeki ilerlemelere paralel olarak gelişmekte ve bu sistemler çerçevesinde yapılan milletlerarası nitelikli işlemlere uygulanacak hukukun tespiti konusu dikkat çekmektedir. Bu konuya ilişkin genel görüş, söz konusu işlemlerin parçalanması suretiyle her bir işlem ve/veya ilişkiye uygulanacak hukukun tespiti yönündedir. Ancak, elektronik ödeme işlemlerinin süratli ve karmaşık yapısı, bu işlemleri, uygulanacak hukukun tespiti bakımından tartışmalı hale getirmiştir. Elektronik ödeme işlemlerine uygulanacak hukukun tespitine ilişkin temel sorun, bu işlemlerin tek bir işlem olarak belli bir hukuka mı tâbi olması gerektiği; yoksa parçalama görüşü doğrultusunda ödeme işlemini oluşturan her bir işlem/ilişki için uygulanacak hukukun tespiti yoluna mı gidilmesi gerektiğidir.

Bu makalede, elektronik ödeme sistemleri ve elektronik ödeme işlemlerine uygulanacak hukuk meselesi, söz konusu tartışma çerçevesinde incelenmektedir.

KEY WORDS: *Electronic payment, payment systems, international payment, applicable law.*

ANAHTAR KELİMLER: *Elektronik ödeme, ödeme sistemleri, uluslararası ödeme, uygulanacak hukuk.*

INTRODUCTION

In this study, while examining electronic payment transactions and governing law, it was preferred to handle the issue using international and comparative law sources rather than focusing on a domestic system. From the perspective of comparative law, U.S., Canadian and European Union practices as well as sectoral or legal documents of those systems have been analyzed. This article, composed of Anglo-American and European sources, practices and legal instruments, does not contain specific explanations regarding the Turkish legal system with respect to electronic payment methods and private international law. However, since the problem of applicable law regarding electronic payment transactions is a pending problem in almost all legal systems of today, the explanations made in this article could be deemed substantially relevant to Turkish law as well.

As implied in the title, the topic was considered only within in the framework of conflict of laws. Accordingly, the matter of jurisdiction in international litigation of electronic payment transactions was not included, since jurisdictional issues concerning electronic transactions should be studied separately.

I- ELECTRONIC PAYMENT SYSTEMS

A) OVERVIEW

Technological developments in the field of communications in recent decades have expanded the methods of contract formation as well as payment methods to include new ones such as electronic and internet payment methods.

Since the 1960s the impact of new methods of contracting using telegraph, telephone, telex, fax and lately, electronic mail (e-mail) system, have been discussed by lawyers. Issues such as the place and time of contract or the requirement of writing have been under focus in this transition.¹ These new communication models affect the ways in which parties provide consent to contractual relationships. However, the legal requirement of consent to contractual transactions has not changed with the use of electronic communication media. In many countries, new laws, as well as international regulations like the UNCITRAL Model Laws, have been adopted in response to emerging trends in electronic communications.

¹ G. S. Takach, *Computer Law*, 2nd ed. (Toronto: Irwin Law, 2003) at 517. T. Scassa & M. Deturbide, *Electronic Commerce and Internet Law in Canada* (Toronto: CCH Canadian Limited 2004) at 3-22.

The law of international commercial arbitration can be referenced in this context, since an arbitration agreement is required to be in written form in almost all legal systems and international regulations. Indeed, because of its impact on the jurisdiction of state courts, an arbitration agreement is considered to be an agreement that must be in written form and almost all legal systems have agreed on this requirement, but the necessity of recognizing the effect of communication technology on the field of contract law has resulted in adopting regulations allowing parties to make arbitration agreements by means of this new technology. For example in the UNCITRAL Model Law on International Commercial Arbitration art. 7/2, the rule requiring a written form is laid down in the first sentence, and in the second sentence the ways in which an arbitration agreement is assumed to have been concluded in written form are stated. This statement includes the means of telecommunication. The only restriction on the means of telecommunication is related to the record of the agreement; article 7/2 states that the means of telecommunication by which arbitration agreements are concluded must provide a record of agreement to be regarded as the required written form. Similarly, many legal systems enacting laws on international commercial arbitration have adopted written form requirements in a flexible style in which the parties can make their agreement by new means of telecommunication. An example of this kind of legislation is the law on international commercial arbitration in the 12th Chapter of the Swiss Federal Statute on Private International Law; article 178/1 sets the rule about written form requirement and, in accordance with UNCITRAL Model Law art. 7/2, indicates that the written form requirement can be met by means of telecommunication provided that the agreement is evidenced by a text.

These regulations, and the legal tendency to regard the means of telecommunication as new ways to declare assent, indicate that legal institutions can adapt to new developments without the need to change their main structures. In other words, new developments in the field of communication can be handled within the existing framework of contract law.

Accordingly, new systems of payment have not changed the legal nature of payment or legal frameworks (such as remittance) for payment methods. Generally speaking, new payment systems can be defined as electronic- or internet-adapted versions of traditional payment systems. For example, an electronic check is treated as the electronic equivalent of a paper-based check.² Likewise, secure payment systems (such as Paypal) developed in order to protect credit card information have not changed the method of payment by credit card or the legal nature of electronic funds transfers via the internet: it is

² J. K. Winn, "Clash of the Titans: Regulating the Competition between Established and Emerging Electronic Payment Systems" 14 Berkeley Tech. L.J. 675 (1999).

still remittance although it shows a complex structure consisting of an electronic transfer system and the internet as a means of operation.³

From a legal point of view, payment systems may be classified into two groups, as either a credit transfer or a debit transfer⁴ regardless of the means of transmission (paper-based, electronic or internet payment) or the number of intermediaries. As such, all payment methods, from payment by credit card via internet or electronic money to internet-initiated international electronic fund transfer or electronic check, can be categorized using this classification. For a legal qualification of payment systems, this classification should be considered to be basic. Since law needs to qualify all legal issues under general categories or institutions to find out which rules are applicable to the matters in question, this basic point serves as a legal framework for payment systems. In other words, a payment transaction generally relies on money transfer from one party to another, and this transfer can be defined as either a credit or a debit transfer, irrespective of transmission method or number of intermediaries.

Despite the fact that advances in technology have not changed the legal structure under payment systems, there are various consequences of those advances that should be considered to be legal issues arising from payment transactions involving new technologies and their use in international payment systems.⁵

B) CLASSIFICATION OF ELECTRONIC PAYMENT SYSTEMS: WITH RESPECT TO INTERNATIONAL TRANSFERS

Before focusing on specific legal issues, it is essential to outline the general structure of payment systems in order to lay out a perspective about payment methods.

First, payment systems can be divided into two general categories: wholesale payment systems and retail payment systems.⁶ The reason for this distinction is to bring light to the issue of retail payment systems by locating

³ Regarding internet-initiated electronic fund transfer in U.S. see M. B. Guard, "NACHA Rules on Internet ACH Debits" (2001), available at: <http://www.bankersonline.com/operations/ach.html>

⁴ L. G. R. D. Brozolo, "International Payments and Conflicts of Laws" 48 Am. J. Comp. L. 307, (2000).

⁵ *Id* at 308, 318. See also S. J. Hughes, "A Call for International Legal Standards for Emerging Retail Electronic Payment Systems" 15 Ann. Rev. Banking L. 197, (1996).

⁶ See U.S. Federal Reserve Bank of Chicago, *Global Electronic Payments*, (Payment Industry Studies - Staff Research Papers) by Carol Clark, Victor Lubasi, Gozde Yazar, Jaclyn Tan, Erin Davis, Carrie Jankowski & Julie Sick (April 2004) online: http://www.chicagofed.org/emerging_payments_and_policy/files/global_electronic_payments.pdf

them under general categories of payment systems. Wholesale payment systems serve to transfer money in large amounts while retail payment systems include transferring smaller amounts such as consumer payments (consumer to business or person to person).⁷

1. Large-Value Payment Systems

Wholesale or large-value payment transactions take place generally as electronic fund transfers.⁸ These payment systems may be subject to different distinctions depending on various factors. Among these factors are: 1) Ownership of the systems by public or private sector;⁹ 2) Settlement time of transfers (they are generally based on real time gross settlement system-RTGS¹⁰ instead of Deferred Net Settlement system-DNS¹¹); 3) Level of operations as national or cross-border/international; and 4) If there is a cross-border or international transfer system, the infrastructure or operational base of the system: these systems are activated pursuant to either a bilateral agreement between banks, i.e. correspondent (or network) banking, or a tiered relationship where there is a supranational agency to facilitate transfers across borders;¹² 5) Messaging systems in transfer systems (almost all transfer systems use the

⁷ *Id.* See also C.R. Cloutier, "Speeding a Bright Future of Electronic Check Processing" 8 NO. 1 Elec. Banking L. & Com. Rep. 13, (2003). Hughes, *supra* note 5.

⁸ *Supra* note 6. See also Winn, *supra* note 2.

⁹ Bank for International Settlements, *New Developments in Large-Value Payment Systems*, (Various Reports by Committee on Payment and Settlement Systems) (May 2005) available at: <http://www.bis.org/publ/cpss67.pdf> [hereinafter *New Developments in Large-Value Payment Systems*] at 21-22.

¹⁰ Bank for International Settlements, *Real-Time Gross Settlement Systems*, (Various Reports by Committee on Payment and Settlement Systems) (March 1997) available at: <http://www.bis.org/publ/cpss22.pdf>. See also Canada Bank of Canada, *The Elements of Global Network for Large-Value Funds Transfers*, (Working Paper 2001-1) by James F. Dingle (February 2001) available at: [http://www.bankofcanada.ca/en/res/wp/wp\(y\)_2001.html](http://www.bankofcanada.ca/en/res/wp/wp(y)_2001.html) [hereinafter *The Elements of Global Network*].

¹¹ About Deferred Net Settlement system see *New Developments in Large-Value Payment Systems*, *supra* note 9 at 1-2.

¹² *Supra* note 6.

SWIFT¹³ platform and message standards; financial institutions that do not have access to SWIFT use Telex-based proprietary systems¹⁴).

Regardless of the level of operation (as national or cross-border), large-value payment systems are generally based on electronic fund transfer systems.¹⁵ Although electronic fund transfer systems have been used since the 1970s, technological improvements in telecommunication in recent years have made these payment systems more accelerated and more widely used. In addition to the technological advances achieved, legal barriers have been lowered and operational progress has been facilitated to some extent.¹⁶ Those improvements have contributed to the development of global financial market integration and have given rise to a transformation of the traditional large-value payment system to a system operated on an international level in multiple currencies.¹⁷

As a result of those improvements, some operators have come to the scene running cross-border or international payment systems, and these payment systems are operated under correspondent (or network) relationships (based on bilateral arrangements) or tiered relationships as mentioned above¹⁸. There are electronic fund transfer systems providing large-value and retail money transfers in almost all domestic economies¹⁹ and they have been involved in a cross-border or international transfer system in terms of either bilateral arrangements or tiered relationships. Those kinds of arrangements, especially tiered relationships, provide more accelerated, more coordinated and lower cost transfers in various aspects such as technical infrastructure or payment currency.²⁰ A correspondent or network relationship is the oldest and most

¹³ Society of Worldwide Interbank Financial Telecommunications. SWIFT, providing electronic transmission of payment messages, accelerates the operation of fund transfers. "Its message types, formats and technical infrastructure provide a common means of processing cross-border payments". See *supra* note 6.

¹⁴ Federal Financial Institutions Examination Council, *Wholesale Payment Systems* (IT Examination Handbook) (July 2004) available at: <http://www.ffiec.gov/ffiecinfobase/booklets/Wholesale/whole.pdf>, at 8-9.

¹⁵ *New Developments in Large-Value Payment Systems*, *supra* note 9 at 5.

¹⁶ *Id.* at 24.

¹⁷ *Id.*

¹⁸ See *supra* note 6. See also *ibid.*

¹⁹ See generally Bank for International Settlements, *CPSS/BIS Publications on Payment Systems for Particular Countries* available at: <http://www.bis.org/cpss/paysysinfo.htm>.

²⁰ *Supra* note 6 at 12-16. See also *New Developments in Large-Value Payment Systems*, *supra* note 9 at 24-25.

common way of establishing international transfer system.²¹ Under this kind of relationship, financial institutions (or their branches in network banking) in different countries are connected to each other's RTGS systems.²² The other case, where there is a multinational agency at the apex of the payment structure,²³ is a phenomenon seen since the advancement in recent years in global market integration²⁴ by means of telecommunication technology, legal and operational convenience.²⁵ Banks and financial institutions performing electronic fund transfers generally constitute the parties or participants of a correspondent and/or tiered relationship. Correspondent (or network) arrangements can show different levels of cooperation between banks or financial institutions. Common types of correspondent arrangements are run between national RTGS systems of each country.²⁶ Although technological advances have affected electronic fund transfer systems in several aspects, correspondent or network arrangements are still considered slow and expensive.²⁷ However, with the effect of globalization in financial markets, tiered relationships are much more advanced in this context, since they are being developed to meet the needs of speed, multiple currencies, lower cost, and similar factors.²⁸ Primary examples of such structures are CLS (Continuous Linked Settlement) Bank and TARGET (Trans-European Automated Real-time Gross Settlement Express Transfer System). Although CLS is not used for cross-border transfers, it is the one large-value transfer system providing multicurrency settlement,²⁹ and TARGET is a decentralized RTGS system which connects 15 RTGS system in the European Economic Area to serve for large-value euro payment.³⁰ One of the important characteristics of TARGET is

²¹ See *The Elements of Global Network*, *supra* note 10 at 4-5.

²² Y. Kuzu, *Türkiye Cumhuriyet Merkez Bankası'nda Uluslararası Elektronik Finansal İletişim ve Yurt Dışı Odeme Sistemleri ile İlişkiler* (Expertise Proficiency Thesis, Central Bank of the Republic of Turkey 2003) available at: <http://www.tcmb.gov.tr/kutuphane/TURKCE/tezler/YaseminKuzu.PDF>, at 86.

²³ *Supra* note 6 at 12.

²⁴ *New Developments in Large-Value Payment Systems*, *supra* note 9 at 24-25.

²⁵ *Id.* at 24.

²⁶ *Supra* note 22 at 23-24. See also *supra* note 6 at 19.

²⁷ *Supra* note 6 at 19.

²⁸ *New Developments in Large-Value Payment Systems*, *supra* note 9 at 24. See also Bank for International Settlements, *The Role of Central Bank Money in Payment Systems*, (Various Reports by Committee on Payment and Settlement Systems) (August 2003) available at: <http://www.bis.org/publ/cpss55.pdf>, at 17 [hereinafter *The Role of Central Bank*].

²⁹ *Supra* note 22 at 23. See *The Role of Central Bank*, *id.* at 17. See also *supra* note 6 at 29.

³⁰ *Supra* note 6 at 28.

its functionality as an international transfer system. Indeed, TARGET also provides payment services for indirect participants (represented by direct participants).³¹ For example, a national central bank outside the European Union can use TARGET through the European Central Bank as a client of the European Payment Mechanism.³² As such, TARGET is the only international large-value payment system connecting different RTGS systems in different countries. The transactions processed through TARGET are subject to the Guideline of the European Central Bank of 30 December 2005 on a Trans-European Automated Real-time Gross Settlement Express Transfer System (ECB 2005/16) (2006/21/EC)³³ as well as RTGS rules of national RTGS systems participating in or connected to TARGET.³⁴ According to article 10a of the Guideline, disputes between national central banks or between any national central bank and European Central Bank related to TARGET shall be subject to i) rules and procedures laid down in this Guideline and, ii) in disputes arising from cross-border payments as a supplementary source to the law of the member state where the receiving bank is located.

This provision is of significance as an example of provisions determining applicable law. It gives a hint of the way to provide a single applicable law for cross-border money transfers, although it is related to large-value payments and disputes arising between banks. The factors underlying this provision and especially the effects of particularities coming from tiered relationship and the role of national central banks as parties to disputes can be evaluated to help clarify the issue of determining a proper law for electronic transfers of money in general.

2. Retail Payment Systems

There are cross-border or international payment structures in retail payment systems such as bilateral cross-border ACH³⁵ (Automated Clearing

³¹ European Central Bank, *Information Guide for Credit Institutions Using TARGET*, (Information Guide) (June 2005) available at: <http://www.ecb.int/pub/pdf/other/targetguide2005en.pdf>, at 11 [hereinafter *Information Guide*]. See also European Central Bank, *TARGET Annual Report 2004*, (Publications on Payment and Securities- Annual Report) (May 2005) available at: <http://www.ecb.int/pub/pdf/other/targetar2004en.pdf>, at 6.

³² *Supra* note 22 at 48-49.

³³ EC, *Guideline of the European Central Bank 2005/16 (2006/21/EC) of 30 December 2005 on a Trans-European Automated Real-time Gross Settlement Express Transfer System*, [2005] O.J.L. 18/1.

³⁴ *Information Guide*, *supra* note 31 at 7.

³⁵ ACH network is a type of electronic fund transfer system used especially in the United States for low value payments. ACH transactions are operated by National Automated Clearing House

House) arrangements,³⁶ but a system of tiered relationships where there is a supranational agency like TARGET is not found in the field of retail payment. The similarity between large-value payment systems and retail payment systems can be found in bilateral arrangements since there is not any system like TARGET for retail payment systems. As mentioned above, cross-border ACH arrangements or gate arrangements can be considered to be advanced types of correspondent relationships. In terms of electronic transfers of money, there are some common points between large-value and retail payment systems, but retail payment systems are not limited to electronic fund transfer systems. There are some other types of systems for retail payments, including consumer payments. Accordingly, in terms of infrastructure, retail payment systems can be categorized as electronic fund transfer systems and other systems providing payments by credit card, debit card, electronic money (e-money) or electronic check (e-check).

With respect to domestic transactions, the value and the number of payment types used commonly can change depending on various factors such as population density, economic concentration, technical infrastructure or legal framework in the concerned domestic market. In this context, the preferred payment methods in retail payment systems show diversity in different countries.³⁷ For example, in the United States and Canada, a check is the most effective means of payment, although an increasing number of payments are made through electronic media,³⁸ while in European countries card-based

Association in this country as a nation-wide payment system. See Federal Financial Institutions Examination Council, *Retail Payment Systems* (IT Examination Handbook) (March 2004) available at: <http://www.ffiec.gov/ffiecinfo/base/booklets/Retail/retail.pdf>, at 19.

³⁶ The main examples of cross-border or international ACH arrangements are in force between the US ACH system and analogous systems in other countries' such as Canada, Mexico and five European countries (Austria, Germany, Netherlands, Switzerland and United Kingdom). See NACHA, Electronic Payment Association, *International Payment Resources* (Resources) available at: <http://www.nacha.org/OtherResources/Buyers2005/bg-international/bg-international.htm>. See also *supra* note 6 at 26.

³⁷ *Supra* note 22 at 39-40. See generally Bank for International Settlements, *Survey of Developments in Electronic Money and Internet and Mobile Payments*, (Various Reports by Committee on Payment and Settlement Systems) (March 2004) available at: <http://www.bis.org/publ/cpss62.pdf> [hereinafter *Survey of Developments*].

³⁸ Federal Reserve System, *The 2004 Federal Reserve Payments Study*, (Research Paper) (2004) available at: <http://www.frb-services.org/Retail/pdf/2004PaymentResearchReport.pdf> [hereinafter *Federal Reserve Payments*]. See also Bank for International Settlements, *Payment Systems in Canada*, (CPSS/BIS publications on payment systems for particular countries) (2003) available at: <http://www.bis.org/cpss/paysysinfo.htm#pgtop>, at 49-53 [hereinafter *Payment Systems in Canada*].

systems (credit/debit cards) and credit transfers are in the foreground.³⁹ However, in the process of technological evolution, these trends have been changing in favor of either electronic or advanced variations of existing payment systems or new systems such as electronic money.⁴⁰ It can be observed at the domestic and international level that electronic payment methods have been increasing with the value and number of transactions compared to traditional means of payment. For example in the United States as of 2003, electronic payments in total (credit card, online debit, ACH, offline debit, electronic benefits transfer) increased, while the number of check payments decreased.⁴¹ A similar trend has been found in Canada.⁴² With cross-border or international payment transactions, although payment volume is smaller than domestic transactions, it is estimated that the volume of retail, cross-border payments will increase at a rate of 10.2 percent annually on a global level.⁴³

As mentioned above, electronic retail payment systems can be divided into two categories with respect to their infrastructure: electronic fund transfer systems and other systems providing payment by credit card, debit card, e-check and electronic money. This distinction is effective also for cross-border or international retail payments.⁴⁴

First of all, electronic fund transfers in retail payment systems are not as widely used as in large-value payment systems. There are two operational structures in the form of correspondent (or network) and tiered relationships for large value fund transfers, but only correspondent (or network) relationships are active for electronic fund transfers in retail payment systems. As such, electronic fund transfers in retail payment systems should be handled within the

³⁹ European Central Bank, *E-Payments Without Frontiers*, (Issues Paper for the ECB Conference on 10 November 2004) available at: <http://www.ecb.int/events/pdf/conferences/epayments2004/epaymentsconference-issues2004en.pdf>, at 14 [hereinafter *E-Payments*].

⁴⁰ *Id.*, at 11-12.

⁴¹ *Federal Reserve Payments*, *supra* note 38 at 3-4. See also S. A. Anenberg, "Selected Regulatory Developments" 9 NO. 7 Elec. Banking L. & Com. Rep. 17, (2004).

⁴² See *Payment Systems in Canada*, *supra* note 38 at 49-50.

⁴³ See *supra* note 6 at 11. See also Bank for International Settlements, *Policy Issues for Central Banks in Retail Payments*, (CPSS/BIS publications on retail payments) available at: <http://www.bis.org/publ/cpss52.pdf>, at 22-24 [hereinafter *Policy Issues*]

⁴⁴ See *Policy Issues*, *id.* at 22-24. Means of international electronic payment other than electronic fund transfer systems consist of several instruments but electronic money should not be considered to be in this category, since electronic money products have uses dominantly in domestic markets. See *Survey of Developments*, *supra* note 37 at 7. See also D. Tunkel & S. York, eds., *E- Commerce: A Guide to the Law of Electronic Business*, 2nd ed. (London: Butterworths 2000) at 379.

framework of correspondent relationships between banks or their branches. Especially concerning cross-border or international correspondent relations, some forms of consolidation have been developed by financial institutions, banks or postal institutions.⁴⁵ The FedACH cross-border payment arrangement between the US and Canada and the Eurogiro network founded by 16 financial and postal institutions and participated in by 45 countries, including European Union countries or STEP1 and STEP2 in Europe, can be considered to be examples. Those intensive relationships are given more importance because they rely on operational rules which can be considered as applicable rules, such as the *Cross Border Payment Operating Rules* included in the *Cross Border Payments User Guide* by NACHA⁴⁶ for cross-border payments between the US and Canada. However, cross-border or international electronic fund transfers do not have to be based on such relationships. If there is no such consolidated relationship or arrangement, a transfer can be subjected to the laws of the concerned country or countries, but in this case electronic fund transfers cost more and take more time.

Electronic retail payment systems, especially international payment systems other than electronic fund transfers are generally based on card-based systems. Card-based electronic payment systems can be described as the most effective payment method used for retail payments. Especially consumers in international transactions prefer to use credit cards and increasingly debit cards for POS (point of sale) and remote (mail, phone or internet) transactions.⁴⁷ Although credit cards can be used directly in transactions by mail, phone or internet, there are some other ways for credit cards to be used via the internet. These ways or so-called secure credit card payment services (other than payment by credit card in a system secured by Secure Electronic Transactions - SET or Secure Sockets Layer - SSL⁴⁸) were developed by some companies doing business on the internet. Past or present examples of these services are First Virtual, PayPal⁴⁹ or InstaBuy.⁵⁰ These payment services perform the function of an online intermediary between merchant and consumer using bank account or credit card information that the consumer provides. With these

⁴⁵ See *Policy Issues*, *supra* note 43 at 22.

⁴⁶ National Automated Clearing House Association, *Cross Border Payments User Guide* (Guide) available at: http://gpf.nacha.org/docs/Cross_Border_Payments_User_Guide.doc.

⁴⁷ *Supra* note 6 at 20-21. See also M. Rustad & C. Daftary, *E-Business Legal Handbook*, 2002 Ed. (New York: Aspen Law & Business, 2002) at § 6.08[a].

⁴⁸ See *supra* note 2. See also J. D. Muller, "Selected Developments in the Law of Cyberspace Payments" 54 *Bus. Law.* 403, (1998).

⁴⁹ A. G. González, "E-Commerce – Payment Systems: PayPal: the Legal Status of C2C Payment Systems" *Computer Law and Security Report* Vol. 20 No. 4, (2004).

⁵⁰ See *supra* note 2.

services, a buyer does not have to disclose account information to the seller.⁵¹ Although there have been some discussions about the legal status of these payment services with respect to the legal status of those companies (as a bank, saving institution or electronic money institution) and the liability of service providers,⁵² given the infrastructure of payment operations these payment services can be considered to be in the same category as credit card payments. Card-based systems, as can be seen below, regardless of the number of intermediaries, are operated under contracts (like other payment systems), and the international level laws applicable to these contracts and/or banking regulations of the concerned countries governing the payment transactions. This evaluation covers both credit/ debit card payments and secure credit card payment services.

As an emerging electronic payment system, electronic check (e-check) system was developed in the United States to meet the need of an electronic version of paper-based checks.⁵³ In fact, payment by check is a payment method used especially in the United States; while the rate of credit card usage or holding a credit card is very low in that country, check payments are second only to cash payments.⁵⁴ As such, one would anticipate that electronic checks would be popular in the United States, especially because of their secure structure. Indeed, payment by electronic check can be described as the most secure way of electronic payment, since cryptographic signatures are used to secure the check. The general outline of this system's operational infrastructure

⁵¹ C. Kaminski, "Online Peer to Peer Payments: PayPal Primes the Pump, Will Banks Follow?" 7 N.C. Banking Inst. 375, (2003).

⁵² See *supra* note 49 at 296. See also Federal Reserve Bank of Chicago, *The Growth of Person-to-Person Electronic Payments*, (Essays on Issues) by Tim McHugh (2002) Chicago Fed Letter August 2002, Number 180, available at: http://www.chicagofed.org/publications/fedletter/2002/cflaug2002_180.pdf.

⁵³ Electronic check and electronic conversion of checks are different subjects. Although they seem similar and the same concept at first glance, an electronic check is a payment method used instead of a paper check over internet and signed with an electronic signature (generally digital signature); electronic conversion of checks means transforming clearing and settlement process of checks into an electronic procedure from a physical one. While an electronic check is used as an electronic payment method, electronic conversion can cover all types of checks, especially when they are used in a store or sent by mail. Because electronic conversion system has been developed to hasten the clearing and settlement process of checks and it is regulated by the Check Clearing for the 21st Century Act. See D. Hayes, "Implementation of the Check Clearing for the 21st Century Act" 10 NO. 1 Elec. Banking L. & Com. Rep. 11 (2005). See also ECheck Org, *Architectural Overview of the FSTC eCheck System – The Electronic Check Architecture*, (White Papers) by Milton Anderson (1998), available at: <http://www.echeck.org/library/wp/ArchitectualOverview.pdf> [hereinafter *The Electronic Check*].

⁵⁴ *Federal Reserve Payments*, *supra* note 38 at 3-4.

may be examined under two main processes: drawing and sending an electronic check to the payee and clearing and settlement of an electronic check.

Electronic checks are drawn in an electronic environment, signed with an electronic signature and sent by either interactive web messages or electronic mail. At this point, entering into an international or cross-border transaction, drawing an e-check in one country and sending it to a payee in another country is possible. However at this stage, the e-check process works as the payment part of a transaction between parties. Since the banks involved in this payment transaction (the payer's bank and the payee's bank) are in the United States, we cannot say that there is an international electronic payment. The electronic check is not a payment method widely used in other countries and banking sectors. To draw an electronic check, one must have an e-checking account and banks must be in the same organization providing clearing and settlement rules, or if they are in different countries, they can agree to clear and settle e-checks bilaterally.⁵⁵ As such, if banks in different countries have bilateral clearing and settlement arrangements (generally these arrangements are operated over electronic fund transfer systems), e-checks can be drawn internationally, by a drawer whose bank is in one country to a payee whose bank is in another country. However, this theoretical presumption does not mean that the e-check, by itself, is an international payment means (the reason for this fact is related to the national nature of check payments⁵⁶); the international aspect depends on the electronic transfer of money to be ordered with an e-check. Because the international flow of the money occurs through means of electronic fund transfer between banks, and in this case if it is accepted that there is an international payment, then the e-check can be categorized as an electronic transfer of money.

⁵⁵ *The Electronic Check*, *supra* note 53 at 4.

⁵⁶ As a payment means, a check has not universal implementation like credit cards. Indeed, payment with credit cards are managed by some international institutions such as Visa International but in this sense, a check is a payment means which has a national usage and which is regulated on the national level. For the reason that e-check is just an electronic version of paper-based check and its operation is very similar to paper-based check other than its formation in electronic environment, one cannot say that e-check is an international payment method in terms of its formation and transmission to the payee, even it is issued by a drawer in one country and sent to a payee in another one as far as the banks involved are in the same organization.

II. INTERNATIONAL ELECTRONIC RETAIL PAYMENT SYSTEMS IN CONFLICT OF LAWS

A) ELECTRONIC RETAIL PAYMENT SYSTEMS IN INTERNATIONAL TRANSACTIONS

Electronic retail payment systems mainly consist of electronic fund transfers and card-based systems. Electronic money products are essentially used in domestic markets.⁵⁷ As mentioned above, electronic checks can qualify as international if there is a clearing and settlement process between foreign banks. In this case this payment can be categorized as an electronic fund transfers.

The rapid growth of electronic commerce is becoming a major factor of demand for international payments, especially payments initiated over the internet.⁵⁸ However, the use of borderless communication, particularly the use of internet technology, for electronic payments in international transactions can leave an impression that all electronic payment transactions initiated over the internet have an international nature. This impression is not always in accordance with the reality, because the distinctive factor for international payments is the money transfer from one country to another.⁵⁹ As such, electronic payment systems providing international money transfer can be classified as international payment systems.

In the case of international electronic fund transfers, the international character of an electronic payment, by means of banks in different countries, is clear. However, for example, if one party located in country A, buys a product from a website of a company located in country B and pays with her/his credit card and uses the PayPal system, it is easy to conclude that there is an international contract of sale. However it is not so easy to reach the same conclusion for an international payment; i.e. it is not clear absolutely if there is an international payment transaction or not because the payment transaction is operated via international credit card institutions (such as Visa International) and PayPal under a number of contracts. Although in a general sense there is an international money transfer via credit card, this transaction is governed by contracts in effect between parties such as credit card holder (payer) and her/his

⁵⁷ See *supra* note 44. About electronic money legislation and cross-border electronic payment prospect within European Union see *E-Payments*, *supra* note 39.

⁵⁸ See United States General Accounting Office, *International Electronic Commerce – Definitions and Policy Implications*, (Report to the Ranking Senate Minority Member of the Joint Economic Committee) (March 2002) available at: <http://www.gao.gov/new.items/d02404.pdf>, at 46-48. See also *Policy Issues*, *supra* note 43 at 22.

⁵⁹ *Supra* note 4 at 308-309.

bank, payer and PayPal, payee and her / his bank, banks and international credit card institutions.⁶⁰ These contracts govern the payment transaction and laws applicable to these contracts will be applied to disputes arising from the payment transaction. However, one can not say absolutely that there is an international payment in the sense of direct money transfer from one country to another, so it is necessary to determine the law applicable to this particular payment transfer separately from the underlying contracts.

Although payment via card-based systems is the most common way for payment transactions in international electronic commerce,⁶¹ since the possible disputes will be subject to the laws governing the contractual relationships, there is no controversy in terms of conflict of laws regarding international electronic payment transactions by cards.

However, an electronic fund transfer system is also in use in international electronic commerce⁶² and needs to be qualified with respect to issues arising in the framework of private international law. Nevertheless, prior to dealing with those issues, it is essential to remember the operation of electronic transfer of funds in international electronic commerce and consolidated structures providing service for enhanced electronic fund transfer in this sphere.

As mentioned above, international or cross-border electronic transfer of funds is subject to correspondent banking relations. However, general correspondent or network banking relations provide electronic transfer of money internationally based on the SWIFT messaging system; today many banks and financial institutions are involved in consolidated arrangements such as FedACH between the US and Canada or Eurogiro, STEP1 and STEP2 in Europe. The STEPS in Europe have been designed especially to realize Single European Payment Area (SEPA) and they mainly serve in cross-border euro payments within the European Union, although today these systems have participants from other countries for instance, STEP1 has participants from the United States, Japan, United Arab Emirates, Philippines and Australia; while STEP2 as a pan-European ACH system has an ACH gateway arrangement with FedACH of the US.⁶³

These consolidated arrangements are run under operational rules as well as the laws of the countries concerned. As a sample of these operational rules,

⁶⁰ See H. L. Judy & S. P. Rodeman, "The ABA's Project on Jurisdiction and the Internet: Banking and Payment Systems" 5 NO. 7 Elec. Banking L. & Com. Rep. 1, (2001).

⁶¹ See *Policy Issues*, *supra* note 43 at 22-23. See also *supra* note 6 at 20-21.

⁶² See *Policy Issues*, *supra* note 43 at 22.

⁶³ For information about these systems see *supra* note 6 at 23-26.

Cross Border Payment Operating Rules included in the *Cross Border Payments User Guide* by NACHA⁶⁴ for payments between the US and Canada can be singled out. This *Guide* states in article V that gateway operators transferring payments will be bound by these *Operating Rules* and unless otherwise agreed by the parties, the relationship between them shall be governed by the law of the State (country) of the receiving gateway operator. This rule, even though it concerns only the relationship between gateway operators, can show clarify the way to determine the proper law for the payment transaction. Besides operational rules of different payment systems, in the European Union there have been initiatives to regulate cross-border payment transactions within Europe, particularly with respect to facilitating cross-border euro transfers between member states. The first initiative to regulate cross-border euro payments between member states was the Directive of the European Parliament and of the Council of 27 January 1997 on cross-border credit transfers.⁶⁵ This Directive aims to establish minimum information and performance requirements for cross-border credit transfers so as to ensure that funds can be transferred from one part of the Community to another rapidly, reliably and inexpensively.⁶⁶

In the same context, Regulation (EC) No 2560/2001 of the European Parliament and of the Council of December 2001⁶⁷ on cross-border payments in euros came into effect to regulate cross-border payments, mainly with respect to equality of charges in cross-border payments made within a member state and across a border⁶⁸.

Although these two legal instruments regulate some aspects of cross-border credit transfers and payments in general within the European Union borders, on

⁶⁴ See *supra* note 46.

⁶⁵ EC, Council Directive 97/5 of 27 January 1997 on cross-border credit transfers, [1997] O. J. L. 043, P. 0025 – 0030. Before this Directive, there has been a Recommendation (97/489/EC) providing for the protection of consumers using electronic payment verification instruments. See EC, Commission Recommendation 97/489 of 30 July 1997 Concerning Transactions by Electronic Payment Instruments and in particular the Relationship between Issuer and Holder, [1997] O. J. L. 208, P. 0052 – 0058.

⁶⁶ See Objectives given in the text of the Directive.

⁶⁷ EC, *Council Regulation* 2560/2001 of 28 December 2001 on Cross-border Payments in Euro, [2001] O.J.L. 344, P. 0013-0016.

⁶⁸ About this Regulation see European Commission Internal Market and Services DG, *Working Document of the Commission Services – Consultative Document to contribute to the Preparation of a Report on the Application of Regulation (EC) No 2560/2001 on Cross-Border Payments in Euro*, (Working Document) (19 October 2005) available at: http://europa.eu.int/comm/internal_market/payments/docs/reg-2001-2560/report_final2005_10_19.pdf

1 December 2005 the Commission of the European Communities presented a new proposal for a Directive⁶⁹ from the European Parliament and from the Council on payment services in the internal market. The aim of the Proposal is to make payments across borders as easy, cheap and speedy as those made in one country. This Proposal has a wide range of provisions and it considers those payments as if they are made in one internal market. However, whereas it is the first initiative to regulate electronic transfer of money systems that have a cross-border nature, some provisions of the Proposal can be used to find a way to solve conflict of laws problems in international electronic transfer systems. Examples are: article 26 (d) laying down the requirement of choosing an applicable law and competent court for single payment transactions; article 31 (c) specifying the same requirement for framework contracts between payment service provider and payment service user; and article 68 entitled *Transfers to third countries*, limiting the liability of the payment service provider of the payer until the funds reach the payee's payment service provider in cases where the payment service provider of the payee is not located in a Member State. All of these reflect an approach to the problem of applicable law and shows that the Proposal designates its scope in conformity with the fact that payment transactions are fragmented on a country basis. According to this Proposal, EU will be considered to be one country with respect to cross-border payment transactions. In this context, international payment transactions, with respect to the European Union, to or from third countries will still need to be examined in the framework of private international law.

As mentioned above, the current international payment system is nationally-based and fragmented; this fact leads to a number of results including the problem of applicable law for international payment transactions as well as international unification efforts such as UNCITRAL Model Law on International Credit Transfers.⁷⁰ However, the electronic environment in which payments initiated and performed should be given due consideration, because it speeds up payment transactions and helps integrate transactions.

⁶⁹ Commission of the European Communities, *Proposal for a Directive of the European Parliament and of the Council on Payment Services in the Internal Market*, 1.12.2005, 2005/0245 (COD) available at: http://europa.eu.int/comm/internal_market/payments/docs/framework/com_2005_603_en.pdf.

⁷⁰ UNCITRAL Model Law on International Credit Transfers adopted by UNCITRAL on its 25th Session (15.05.1992) available at: <http://www.uncitral.org/pdf/english/texts/payments/transfers/ml-credittrans.pdf>. [hereinafter Model Law].

B) APPLICABLE LAW OF ELECTRONIC RETAIL PAYMENT TRANSACTIONS

The main issue arising from international electronic payment systems appears to be the problem of applicable law.⁷¹ Indeed, not specifically electronic international payment transactions but generally international payment transactions need to be categorized according to connecting factors. However, although there has been some work done and evaluations⁷² made to determine law governing these transactions, so far there is not a clear settlement of this problem. Among those, the UNCITRAL Model Law on International Credit Transfers and Proposed Directive⁷³ by the Commission of European Communities as well as Rome Convention of 19 June 1980 on the Law Applicable to Contractual Obligations⁷⁴ should be handled under concerning provisions. Besides these legal instruments as mentioned above operational rules for some international payment systems will be helpful to clarify the issue, especially in respect to the electronic environment.

Our analysis of international payment transactions shall be restricted to the international electronic transfer of money within the scope of this study. First, the general structure of determination of the law governing international credit transfers will be dealt with, and second, the electronic environment and its particularities for money transfer systems will be examined in this part.

While trying to handle the issue of the law governing international payment transactions in terms of credit transfers, a good starting point would be the UNCITRAL Model Law on International Credit Transfers since it is the first specific work in this field.

As stated above, international payment means a money transfer from one country to another. This “transfer criterion” requires two different payment service providers subject to two different legal systems. Even those payment services are branches of the same payment institution, they can be branches of an international financial institution, since they perform their activities subject to different legal systems. They must therefore be considered to be autonomous

⁷¹ A. Fitzgerald et al., eds., *Going Digital 2000 – Legal Issues for E-Commerce, Software and the Internet*, 2nd ed. (Australia: Printing Headquarters, 2000) at 163-164. See also *supra* note 60.

⁷² See *supra* note 4.

⁷³ See *supra* note 69.

⁷⁴ EC, Convention on the Law Applicable to Contractual Obligations opened for signature in Rome on 19 June 1980 (80/934/EEC), O. J. L 266, 09/10/1980 P. 0001 – 0019.

bodies in terms of transferring money from one country to another.⁷⁵ The Model Law signifies this criterion as the fact that the banks involved are in different countries.⁷⁶

Before dealing with conflict of laws rules included in the above-mentioned instruments, it is necessary to mention the actual argument about the law governing international payment transactions. This argument consists of two views: one view defends the requirement of splitting international payment transactions into the relationships between parties such as payer and payer's payment service provider, payment service provider and (if there is one) clearing house, payee and his/her payment service provider, etc. and law governing any payment transaction should be determined according to those relationships.⁷⁷ Every relationship is a separate transaction and the applicable law is determined for every relationship separately.⁷⁸ The other view states that payment transactions, especially electronic transfers, should be regarded as single transactions for the reason that it is not possible to detach a single a payment transaction from the chain of operations so the same approach must be used for the entire chain.⁷⁹

However, although the Model Law adopts the view of splitting transactions and the entire wording of the text reflects this approach, UNCITRAL excluded the conflict of laws provision from the main text at the 1992 session although it was included in a footnote (as Article Y) to Chapter I of the Model Law for States that might wish to adopt it.⁸⁰ According to the Explanatory Note, although designating a single legal regime for entire transaction would be desirable in the abstract, it is not feasible, either technically or politically; that's why UNCITRAL accepted (with less consensus and in a footnote article⁸¹) that

⁷⁵ See Model Law art. 1 (3). It is clearly stated in this provision that "...branches or separate offices of a bank in different States are separate banks".

⁷⁶ See Model Law art. 1 (1).

⁷⁷ For the basis of this approach with respect to contracts law see J. H. Sommer, "A Law of Financial Accounts: Modern Payment and Securities Transfer Law" 53 Bus. Law. 1181, (1998).

⁷⁸ See *supra* note 4 at 317-318. See also *supra* note 70 at Explanatory Note by the UNCITRAL Secretariat on the Model Law on International Credit Transfers, section 16.

⁷⁹ See *supra* note 4 at 319-322.

⁸⁰ See *supra* note 70 at Explanatory Note by the UNCITRAL Secretariat on the Model Law on International Credit Transfers, section 16-18.

⁸¹ See *supra* note 4 at 317.

each of the operations carried out in the transaction would be subject to the law applicable to that operation.⁸²

Article Y (1) of the Model Law states that “the rights and obligations arising out of a payment order shall be governed by the law chosen by the parties. In the absence of an agreement, the law of the state of the receiving bank shall apply.” Considering the general approach of the Model Law, which regards payment transactions as separate operations, the article Y (1) is required to be applied separately to each part of the payment.⁸³ This approach leads to the application of different legal regimes to separate relationships constituting of one payment transaction.

Although the Rome Convention on the Law Applicable to Contractual Obligations does not have a specific provision related to payment transactions, article 3 and 4 of it regulating general conflict rules for contracts should be taken into consideration in this respect. Article 3, similar to UNCITRAL article Y, gives priority to the choice of parties for determination of the applicable law, while article 4 states that – if there is no choice of law – the closest connection to the transaction determines the applicable law and this closest connection can be determined by a rebuttable presumption considering the place of “characteristic performance.” According to this presumption, the place of business of the party who provides the characteristic performance has the closest connection with the transaction.

Regarding article 4 of the Convention, there have been some argument as to whether it shows consistency with UNCITRAL article Y and leads to the fragmentation of payment transactions or it should be interpreted in the way that allows the designation of a single governing law.⁸⁴ Although the trend prevailing in the UNCITRAL rule is clear, especially in the general approach of the Model Law, and gives priority to the certainty rather than permitting interpretations in favor of “single law” view, the Rome Convention has a more flexible approach in its article 4. This provision can be interpreted in both ways: accepting the payment transaction as an integrated transaction of separate relationships, or as a single transaction which requires determining single governing law. Its wording at first glance can be interpreted in a way that accepts the view splitting the transactions into its components and requires all relationships consisting of one payment transaction to be handled separately and, if there is no choice of law clause for the concerned specific contractual

⁸² See *supra* note 70 at Explanatory Note by the UNCITRAL Secretariat on the Model Law on International Credit Transfers, section 16.

⁸³ See *supra* note 4 at 318.

⁸⁴ See *supra* note 4 at 319-321.

relationship, to be governed by the law of the place of business of the party fulfilling the characteristic performance. Where the party providing the characteristic performance is the bank or financial institution providing service in consideration of the payment by its customer, the place of business of the bank or financial institution receiving instructions is the determining factor of applicable law.⁸⁵ This interpretation leads to the same result achieved by the application of UNCITRAL article Y, as it selects the law of the receiving bank in all of the contractual relationships.⁸⁶ As can be seen, this approach, especially as it is expressed in the Explanatory Note, gives priority to the legal certainty rather than considering particular conditions of payment transactions.⁸⁷

However, it is possible to interpret this provision as allowing a single law to be applied. If there is a law which has the closest connection to all relationships involved in the payment transactions but is not the law of the characteristic performance of any party, i.e. if the presumption does not work in a way that the closest connection shows the law of the place of business of the receiving bank, then, at least in theory, it can be argued that article 4 can allow, by the way of closest connection to all components of the transaction, the application of a single law.⁸⁸ Although this is a theoretical assumption, it must be accepted that article 4 does not prevent the determination of a single law for international payment transactions.

Consequently, both of these main instruments, as well as doctrine, strongly support the trend of splitting the transaction into its components for conflict of laws analysis.⁸⁹ While it is consistent with the structure of the payment transaction since the transaction consists of separate bilateral relationships, this view shows a deficiency in that it leads to the application of several legal regimes to an integrated transaction. Although this fact is not a favorable situation in the framework of conflict of laws, the very nature of payment transactions involves the necessity of compartmentalization.⁹⁰ This necessity gives rise to the application of separate legal regimes to different parts of a payment transaction.

⁸⁵ See *supra* note 4 at 320.

⁸⁶ See *supra* note 4 at 320.

⁸⁷ See *supra* note 70 at Explanatory Note by the UNCITRAL Secretariat on the Model Law on International Credit Transfers, section 16.

⁸⁸ For this explanation see *supra* note 4 at 321.

⁸⁹ See *supra* note 4. See also *supra* note 77.

⁹⁰ See *supra* note 77.

Nevertheless, this necessity is a fact with its disadvantages; with respect to electronic environment, in which payment transactions operated very fast, it was stated that there is a need for due consideration in the framework of conflict of laws.⁹¹ Indeed, the Permanent Bureau of the Hague Conference on Private International Law stated in its comment for UNCITRAL Model Law that:

...in the case of paper-based transfers the segmentation of a global international credit transfer into a series of distinct bilateral operations, to each of which a different law would apply, may be conceivable (although it does not seem desirable), but it would seem quite impracticable in the case of an electronic credit transfer. The extreme speed of such transfers makes it in practice impossible to split them into different bilateral operations within the overall transfer, and for this new method of transfer a system should be devised in which a single law regulates the transfer as a whole.

While developing its view, the Permanent Bureau relied on some provisions found in U.S. legislation⁹² and in Rules and Administrative Procedures of CHIPS,⁹³ which is the international large-value wire transfer system of the U.S., are examples of conflict rules designating a single law for electronic payment transactions. According to rule 3 of CHIPS Rules and Administrative Procedures, the rights and obligations of Participants and all other parties to a fund transfer of which a CHIPS payment message is a part shall be governed by the law of the State of New York. Besides determining applicable law, this article also describes a fund transfer as designating the process of fund transfer and states that

“... A fund transfer means the series of transactions, beginning with the originator’s payment order, made for the purpose of making payment to the beneficiary of the order and includes any payment order issued by the originator’s bank or an intermediary bank intended to carry out the originator’s payment order.”

⁹¹ See the Report of the Permanent Bureau of the Hague Conference on Private International Law, Model Law on International Credit Transfers: Compilations of Comments by Governments and International Organizations (A/CN.9/347 and Add. 1), Yearbook of the United Nations Commission on International Trade Law, 1991, Vol. XXII, P. 133-134.

⁹² The provision in U.S. legislation is incorporated in Regulation J which regulates interstate electronic fund system operated by Fedwire and it is the legal instrument for all parties involved in the fund transfer system. Regulation J available at: http://www.ffiec.gov/ffiecinfobase/resources/fedline/frb-reg_j_12%20cfr210_sub_b.pdf. Since this regulation covers interstate transfers, it will not be dealt with in the scope of this study.

⁹³ CHIPS (Clearing House Interbank Payment System), *Rules and Administrative Procedures*, October 2005, available at: http://www.chips.org/reference/docs_rules/000720.pdf, rule 3 titled “Conflict of Laws”.

This rule regards the “fund transfer” as a series of transactions, with more than one participant and party, consisting of an overall payment, and designates one single governing law for the entire transaction. This means any international fund transfer operated with a CHIPS payment message will be subject to the law of the State of New York regardless of which legal regime other connecting factors are related to. Although it seems that this approach ignores other connecting factors of the transaction to some extent, having considered the nature of payment in terms of volume (large-value payments operated with CHIPS) and its speed, it can be compatible with the interests of the parties who are generally business companies, banks and financial institutions.⁹⁴

As a large-value payment system, CHIPS’ designation of a single law for an entire transaction should be given due consideration; this approach is of significance in terms of taking into account a series of operations as an overall transaction. Since all parties to, and participants of, the transaction are in business life, there can be a presumption about their consent to this rule 3.

However, with regards to retail payments it is not so easy to come to a conclusion only by way of considering the speed and complicated environment of the electronic transaction. As mentioned above, like CHIPS Rules, in large-value payments there are also some operational rules sets for retail payment systems. One of them is the *Cross Border Payment Operating Rules* included in the *Cross Border Payments User Guide* by NACHA⁹⁵ for payments between the U.S. and Canada. Article V states that gateway operators transferring payments will be bound by these *Operating Rules* and unless otherwise agreed by the parties, the relationship between them shall be governed by the law of the State (country) of the receiving gateway operator. Although this rule seems to have a limited scope as designating the law applicable to relationships between gateway operators, it is of significance since this relationship is the one operating cross-border payment transactions. The determinative elements can be extracted from this rule as: 1) it gives priority to the choice of parties for the governing law; 2) it considers the operational stage of the electronic transaction between gateway operators as a separate relationship; 3) it designates the law of receiving gateway operator as the governing law in the absence of choice of law.

This rule as an example of rules designating governing law, although it relates to only gateway relationships, shows the necessity of party autonomy, fragmentation of payment transaction in terms of different contractual relationships between participants and parties of one payment transaction and, most importantly the connecting factor of the characteristic performance and the

⁹⁴ See *New Developments in Large-Value Payment Systems*, *supra* note 9.

⁹⁵ See *supra* note 46.

presumption that the place of business of the party providing characteristic performance will govern.

At this point, the newest and specific resource of the electronic payment transactions, the Proposed Directive by the Commission of European Communities should be discussed. As mentioned above, this Proposed Directive in its articles 26 (d), 31 (c) and 68, reveals the approach of splitting in general. Indeed, articles 26 (d) and 31(c) designate a choice of law requirement for the payment service provider and payment service user in single payment contracts and framework contracts. In accordance with these articles, the provision in article 68 articulates a liability limitation for the payment service provider in transfers to third countries and determines that the payment service provider of the payer shall be liable until the funds reach the payee's payment service provider. This means that the payment operation is divided into two parts in terms of liability and the payment transaction on the side of the payer's service provider shall be subject to the law chosen in the contract between payer and payer's service provider and on the side of the payee's service provider the same situation will occur.

Although segmentation of electronic payment transactions seem undesirable, because it leads to the application of different legal regimes to separate parts of one transaction, those provisions favor this approach. Indeed, regarding electronic retail payment transactions, if even though the operational basis of transactions is similar to those in large-value payment transactions, the different sides of these transactions are parties and their positions. In large-value payment transactions, the operations can be seen as overall transactions, since they serve all parties' interests in terms of legal certainty and unity. However, retail payments show some diversity at this point with respect to the parties and their relationships with banks and financial institutions. Accordingly, payment service users may be customers in retail payment transactions, and not only customer protection policies but also contract formation requires segmentation of payment transactions. This requirement is reflected in the above mentioned provisions of the Proposed Directive by giving priority to party autonomy in contract formation. Under these provisions, to perform a cross-border payment it will be necessary to choose an applicable law for the contractual relationships.

Having considered those provisions found in various legal instruments and operational rules of payment systems, the segmentation approach with respect to retail payment transactions appears to predominate. In this case, although the application of different legal regimes to the separate parts of one transaction is not desirable in theory, the necessity to recognize the interests of all parties involved in the transaction legitimizes this result.

CONCLUSION

The speedy and complex structure of electronic payment mechanisms make electronic payment transactions appear to be integrated transactions overall. However, rules developed lately in this field show the demand for segmentation to meet the needs of different contractual parties. This necessity also requires priority to be given to the rules arising from sui generis structure of the electronic environment.

Indeed, initiatives for legislative work both at the international and national or regional level show some ways to find determinative points for conflict of laws in international electronic payment transactions, but the very nature of international electronic payment transactions as having been initiated and/or operated in electronic environment can lead to diverse results in the framework of electronic commerce and private international law. So far, the segmentation view seems to be the dominant approach for determining applicable law; however, advances in this field require that we pay attention to the rules developed by payment systems especially. These kinds of rules will determine how conflict rules will evolve in the developing process of electronic payment systems.