

# OPUS 2

## INTERNATIONAL

Sainsbury's Supermarkets Ltd v (1) MasterCard Inc, (2)  
MasterCard International Inc, (3) MasterCard Europe S.P.R.L.

Day 22

March 15, 2016

Opus 2 International - Official Court Reporters

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1 Tuesday, 15th March 2016  
 2 (10.30 am)  
 3 Closing submissions by MR HOSKINS  
 4 MR HOSKINS: Good morning sir.  
 5 MR JUSTICE BARLING: Good morning, Mr Hoskins.  
 6 MR HOSKINS: What I would like to do over the next day or so  
 7 is really is to build on what I did in the opening,  
 8 because first and foremost I want to set down  
 9 a framework for the case.  
 10 We did that in the opening and it is the same  
 11 framework in closing, but hopefully that gives you  
 12 a framework as well to decide what questions you want to  
 13 ask. We might disagree about what the answers are to  
 14 those questions, but that is the second thing,  
 15 obviously, I need to do is to fill in the framework with  
 16 our submissions, with particular reference to the  
 17 evidence.  
 18 It was quite noticeable in Sainsbury's closing  
 19 submissions how light the reference was to the  
 20 cross-examination, particularly of the experts, and  
 21 I intend to actually spend quite a lot of time not  
 22 taking you through it verbatim but pointing out what the  
 23 evidence actually shows in this case.  
 24 I will also attempt to deal with the Tribunal's  
 25 questions, because clearly there are certain issues that

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1 you are interested in and I will try and pre-empt them.  
 2 No doubt you will have further questions for me.  
 3 Given that we have given you a weighty tome,  
 4 literally, and time is relatively short, I intend to  
 5 focus on the question of restriction, that is ancillary  
 6 restraint and restriction within 101(1),  
 7 exemption/exemptible level and pass-through. I think  
 8 probably I won't have time to develop the competitive  
 9 dynamics and volume effects orally, but you have the  
 10 written stuff on that.  
 11 Mr Cook is going to come in at the end and thrill  
 12 you with Sainsbury's Bank interest and ex turpi causa.  
 13 Before I go into the framework can I just point out  
 14 four undisputed facts which are really fundamental in  
 15 this case from a competition perspective, and this is  
 16 a competition case.  
 17 First of all, the MasterCard scheme creates  
 18 substantial benefits for merchants and cardholders.  
 19 I will develop all of these, but it seems to me these  
 20 are themes which really underpin what this case is  
 21 about. The scheme is fantastic, it creates benefits for  
 22 merchants and cardholders.  
 23 Second point, the MIF is the key component of  
 24 competition between payment schemes. Not disputed.  
 25 Third point, the MIF is therefore the key means by

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1 which payment schemes seek to increase their market  
 2 share. That's what competition is.  
 3 The fourth point, the larger a payment scheme, the  
 4 more benefits it produces for cardholders and merchants,  
 5 the more people who are touched by the scheme, the more  
 6 people enjoy the benefits on both sides.  
 7 Just as an introductory remark, we say if you take  
 8 those four points, which really are uncontroversial, in  
 9 light of what we have heard over the last 7 weeks, far  
 10 from being a restriction of competition, the MIF is  
 11 actually a pro-competitive driver of competition. You  
 12 have no doubt read probably you feel enough paper but it  
 13 is quite instructive in our closing, page 7,  
 14 paragraph 4, we have referenced a judgment approving the  
 15 class settlement in the United States and it is quite  
 16 interesting, if you read that document, and you read  
 17 just the extracts that we have given and you read the  
 18 extracts in the court-appointed expert report, you will  
 19 see a very different dynamic to the one you see in front  
 20 of the Commission.  
 21 I'm not saying you have to follow American law or  
 22 whatever, but I think it is useful for the debate to see  
 23 a very different view of what the MIF is.  
 24 Let me move then, if you have our closings, I'm  
 25 going to really make my submissions by reference to it.

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1 I am going to go to restriction of competition -- sorry,  
 2 actually I need to keep going.  
 3 If you go to page 14 of the closings, just to make  
 4 some comments on the status of the EU proceedings: do  
 5 they bind the Tribunal; do they not; what weight do they  
 6 have?  
 7 If I can pick that up at page 16, which is our  
 8 response to the Tribunal's second question about the  
 9 relevance of Crehan, and you have seen that Crehan  
 10 chimes with what we were saying in opening but it is  
 11 a good, pithy way of encapsulating, and two particular  
 12 aspects, Lord Bingham at paragraph 11:  
 13 "Community law does not go to the length of  
 14 requiring national courts to accept the factual basis of  
 15 a decision reached by a Community institution when  
 16 considering an issue arising between different parties  
 17 in respect of a different subject matter."  
 18 Then Lord Hoffmann at paragraph 69:  
 19 "The decision of the Commission is simply evidence  
 20 properly admissible before the English court which,  
 21 given the expertise of the Commission, may well be  
 22 regarded by that court as highly persuasive. As  
 23 a matter of law, however, it is only part of the  
 24 evidence which the court will take into account. If,  
 25 upon an assessment of all the evidence, the judge comes

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1 to the conclusion that the view of the Commission was  
2 wrong, I do not see how, consistently with his judicial  
3 oath, he can say that as a matter of deference he  
4 proposes nevertheless to follow the Commission."

5 You will have your own views. You have heard  
6 a welter of evidence, evidence that the Commission  
7 didn't have the benefit of, evidence which  
8 the Commission didn't have the benefit of  
9 cross-examination on, so you are in a much better  
10 position, to be frank, than anyone who has looked at  
11 this before, because of the nature of the process we  
12 have just finished.

13 What we say is the Tribunal is not bound by  
14 the Commission decision but it is entitled to have  
15 regard to it. The Tribunal is bound by the legal  
16 principles established by the Court of Justice and by  
17 the General Court insofar as it wasn't overturned by the  
18 Court of Justice. Because Mr Brealey repeatedly took  
19 you to the Commission and the General Court, but quite  
20 often didn't follow through the story with the Court of  
21 Justice. As I will show you when we go to that, the  
22 Court of Justice actually didn't follow the Commission  
23 in the General Court in some really important legal  
24 matters which are fundamental in this case.

25 That is on the law. Really you have to look

5

1 absolutely the whole process. What did the Court of  
2 Justice say? Because that's where you find what the law  
3 is. But on the facts as well, when you are potentially  
4 looking at the Commission decision, what one has to has  
5 to remember is that the general courts and the Court of  
6 Justice were reviewing the legality of a particular  
7 competition decision and effectively it was a judicial  
8 review. That's the nature of what the courts were  
9 doing. Therefore, they had to judge the legality of  
10 the Commission decision on the basis of the facts that  
11 were available, because that's the nature of a judicial  
12 review. It wasn't a trial like this was, it was  
13 a judicial review, and that's important for a number of  
14 reasons, but the most important reason, of course, is  
15 that the Commission was dealing with an intra-EEA MIF  
16 and I think it is pretty much common ground that  
17 a threat to the life of a payment scheme is going to be  
18 much greater, whatever the right answer is, but the  
19 threat is much greater when you are looking at the  
20 necessity of a domestic MIF as compared to an intra-EEA  
21 MIF, just because of the proportions in which they make  
22 up the scheme.

23 Again, when you are looking at the Commission,  
24 that's something very important to bear in mind. And  
25 you will understand the submission, this Tribunal has

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1 heard and seen a great deal of evidence that is specific  
2 to the UK, which the Commission didn't have. I know  
3 Mr Brealey kept saying it mentions the UK but that's not  
4 the same as the process that we have had in the last 7  
5 weeks, and we submit that you can and should make up  
6 your own mind on the factual basis of what you have  
7 heard, rather than some sort of an inferential approach  
8 as to what the Commission might or might not have heard  
9 or known about the UK. That's clearly not a very  
10 satisfactory basis.

11 Page 18 of the closings deals with the broad axe and  
12 I do not think there is much dispute about that. I will  
13 come obviously to the issue of exemption against  
14 exemptible level, which you debated with Mr Brealey at  
15 a appropriate time, and how the broad axe fits into  
16 that, but in terms of the principles I understand it is  
17 not pushed back on.

18 Before I begin on restriction of competition, if you  
19 go back to page 8 of the closings, because that  
20 summarises what our main points are on restriction. So  
21 I will just identify what they are and then I will  
22 develop them orally.

23 The first point, paragraph 7; as you know, we say  
24 the realistic counterfactual is that if MasterCard's  
25 domestic MIF were assumed to be zero or very low, ie

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1 0.15, we say Visa and Amex would have maintained their  
2 actual rates or would have maintained their rates at  
3 such a high level that large amounts of switching would  
4 have occurred.

5 On objective necessity, as we will see, we say both  
6 the economic experts accepted that in that  
7 counterfactual MasterCard would have been forced out of  
8 the UK market over time. That's why we say domestic MIF  
9 was objectively necessary.

10 If you reject that -- sorry, before we do that. To  
11 further develop it, what's happened actually during the  
12 hearing is the Tribunal has suggested two further  
13 counterfactuals. One is that acquirers would take steps  
14 to keep MasterCard afloat for the general good of the  
15 market and for acquirers, and I will deal with that, our  
16 submission is not borne out by the evidence but we will  
17 come to the detail of that; and the second  
18 counterfactual that's been floated is that merchants, if  
19 they sold MasterCard at zero or low, would turn towards  
20 Visa and put pressure on Visa to bring its rates down,  
21 and it must be a logic of the suggestion by the Tribunal  
22 that it would come down to such a level that switching  
23 would not occur, therefore not objectively necessary,  
24 and again I will deal with that in detail when we come  
25 to it.

8

1 If you are against me on that, so the objective  
 2 necessity point, then we move to: is there a restriction  
 3 within the meaning of Article 101(1)? And the test  
 4 there is you are looking at what competition was in the  
 5 actual and comparing it to what it would have been in  
 6 the counterfactual. That wasn't really touched on by  
 7 Sainsbury's at all in their oral closing submissions,  
 8 but I obviously intend to deal with that in our  
 9 submissions.

10 Our conclusion is that for either of those reasons  
 11 objective necessity are not a restriction. That  
 12 actually determines the case, because there is no  
 13 restriction, there is no right to damages.

14 That is the broad framework and now I need to go  
 15 into the detail of that. I pick this up, it is page 20  
 16 of our closing submissions.

17 Quite a lot of this early material was covered in  
 18 opening so I can take it quickly.

19 We have the definition of the ancillary restraints  
 20 principle. There is no dispute about that.

21 We have the test for objective necessity. It is  
 22 a high test, I accepted that in opening. Would it be  
 23 impossible for the scheme to operate without a domestic  
 24 MIF? In its opening submissions Sainsbury's suggested  
 25 that this argument, our objective necessity argument, is

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1 a 101(3) argument not 101(1), but that's wrong, with  
 2 respect, because the argument we are putting forward is  
 3 not that our scheme would have been smaller or less  
 4 profitable without the UK MIF, our case is the scheme  
 5 would not have been able to continue without the MIF.  
 6 And that's absolutely consistent with the case law.

7 Now, whether we establish that or not is a matter  
 8 for you, but it is not a 101(3) question, it is clearly  
 9 from the case law a 101(1) question.

10 We now come to page 22, paragraph 64, identifying  
 11 the relevant counterfactual. Again, this hasn't been  
 12 challenged in terms of this level of the legal test.  
 13 The counterfactual must be realistic.

14 As I pointed out in opening, there is a difference  
 15 to what the Court of Justice said is you can have  
 16 different counterfactuals for different purposes and the  
 17 court itself applied different counterfactuals for  
 18 objective necessity and for restriction of competition.  
 19 This is paragraph 64(c) of the closing. Because in  
 20 relation to ancillary restraint, what the court said is  
 21 the test -- the counterfactual is not one that would  
 22 arise in the absence of the MIF, but it can include  
 23 a counterfactual of a realistic situation that might  
 24 arise in the absence of the MIF.

25 What does that mean? Well, one way, we submit, of

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1 understanding what that distinction -- because clearly  
 2 the distinction has been drawn -- what it actually means  
 3 is that the Tribunal, for ancillary restraint, is not  
 4 asking what MasterCard would have done absent the MIF,  
 5 but it is asking what could have been done by the  
 6 operator of a scheme to allow the MasterCard scheme to  
 7 continue to operate. I will come onto that. It is  
 8 another point. It is to allow the MasterCard scheme to  
 9 continue to operate, not a general four-party scheme,  
 10 and that's why it is objective necessity.

11 The question isn't the factual one: what would  
 12 MasterCard have done absent the MIF? The question is:  
 13 what could MasterCard have done absent the MIF to keep  
 14 the scheme afloat? That's why it is objective.

15 In terms of restriction of competition, again I'm  
 16 not really sure there's any dispute between us about  
 17 what the test is. It is just that Sainsbury's didn't  
 18 really engage with this bit of the analysis. It is the  
 19 O2 Germany case, so this is paragraph 65 of the  
 20 closings. The most important point of it, it is  
 21 paragraph 65(d) of the closings, paragraph 73 of O2, we  
 22 have set out the short quote. Again, we saw it in  
 23 opening. What the courts of first instance said in that  
 24 case is:

25 "It is necessary to consider what the competition

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1 situation would have been in the absence of the  
 2 agreement."

3 So again, you are comparing state of competition in  
 4 the actual with state of competition in the  
 5 counterfactual in order to assess whether the MIF is  
 6 a restriction of competition or not.

7 Again, when looking at the relevant counterfactual  
 8 we saw the case law in opening, you have to look in the  
 9 actual context in which the agreement operates or would  
 10 not exist in the counterfactual. You have to look at  
 11 the legal context. You will see it in -- we set it out  
 12 at 66(b):

13 "In that regard it is necessary to take into  
 14 consideration the actual context in which the relevant  
 15 agreement exists, and in particular the economic and  
 16 legal context in which the undertakings concerned  
 17 operated, the nature of the goods or service affected,  
 18 as well as the real conditions of the functioning and  
 19 the structure of the market or markets in question."

20 Again, you are looking at the real context. That is  
 21 perfectly clear from the case law. Then, paragraph 167  
 22 of MasterCard. This is at the top of page 24:

23 "The counterfactual must be based on the assumption  
 24 that the scheme rules which are not challenged, such as  
 25 the honour all cards rule, would remain unchanged."

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1 Again, I don't think there is any dispute between  
 2 the parties that that is the case.  
 3 Then, as I flagged up when I looked at objective  
 4 necessity, the difference when one comes to looking at,  
 5 is there a restriction of competition, is one is looking  
 6 at an appropriate counterfactual for assessing  
 7 restriction of competition, as one that would have been  
 8 likely to arise in the actual market or markets in  
 9 question.  
 10 So it is much more a factual enquiry than a more  
 11 objective enquiry that one has for objective necessity.  
 12 Paragraph 68 of the closing, it is really the point  
 13 I have already made, you have to look at the relevant  
 14 economic and legal contexts when you are taking account  
 15 of the counterfactual. But 68(a) is important.  
 16 This is bullets, it doesn't have quotes round it,  
 17 but it is pretty much a quote from MasterCard, but  
 18 I have taken you to it already:  
 19 "The alleged restriction of competition must be  
 20 considered within its actual context. It is therefore  
 21 necessary to take into account any relevant factor,  
 22 having regard in particular to the nature of the  
 23 services concerned as well as the real conditions of the  
 24 functioning and the structure of the markets in relation  
 25 to the economic or legal context in which the

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1 coordination occurs, regardless of whether or not such  
 2 a factor concerns the relevant market."  
 3 We will come onto that because it is clearly  
 4 an important theme. We say at each turn, even if we are  
 5 looking primarily at a restriction on the acquiring  
 6 market, at each stage of the analysis it is quite clear  
 7 from the case law that you have to take into account  
 8 what's happening in the issuing market as well. This is  
 9 the first place one sees it in terms of identifying the  
 10 counterfactual, the Court of Justice makes it quite  
 11 clear.  
 12 That's a theme I'm going to be coming back to.  
 13 In Sainsbury's closing submissions, it made a number  
 14 of legal points about the assessment of the  
 15 counterfactual. If you can go to their closings, so  
 16 that is bundle B1, it is internal page 73 of their  
 17 closings -- sorry, no, that's the bundle number. Give  
 18 me a second. No, I'm right. Sorry. Internal 73,  
 19 bundle 230.  
 20 You see at the bottom of page 73 there's that  
 21 heading "Objective necessity" not subjective necessity:  
 22 "CJEU emphasised the objective nature of the  
 23 necessity. As the Commission stated in its Costs of  
 24 Cash survey, a restriction of competition may fall  
 25 outside the scope of Article 101 if it can be shown that

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1 it is objectively necessary for the existence of  
 2 an agreement of that type or that nature."  
 3 Then Sainsbury's say:  
 4 "Thus, the focus is not on the need for one person  
 5 of that type to survive vis-a-vis another person of the  
 6 same type, the focus is on the type generally and  
 7 whether the restriction is necessary for that type of  
 8 operation to function."  
 9 This is part of Mr Brealey's submission that you  
 10 don't look at what Visa is doing when you look at the  
 11 counterfactual. He says you take it in a vacuum, what  
 12 would a four-party need to work? That is paraphrasing,  
 13 but that's effectively what he said.  
 14 A number of problems with that. It is just not  
 15 right. These are the reasons why.  
 16 First of all, he seeks to create a legal principle  
 17 which should be of considerable importance from some  
 18 wording taken from the Commission's 2015 cost survey  
 19 that wasn't even directly dealing with that legal  
 20 question. The reference for that -- I don't want to  
 21 take you to it now because you can look it up -- it is  
 22 E3.10, tab 202, page 4307 at paragraph 52. But if you  
 23 go to that quote, it is just taken completely out of the  
 24 context for which it is now being relied on. It is not  
 25 a discussion of this particular legal point. It is not

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1 a discussion of the particular point Mr Brealey seeks to  
 2 obtain from it.  
 3 In his oral submissions Mr Brealey also referred to  
 4 the Court of Justice in MasterCard on this. If we can  
 5 look briefly at that. It is E1. If you can keep the  
 6 Sainsbury's closing submissions handy, I need to come  
 7 back to that in a second. E1, tab 19, at page 428. It  
 8 is paragraphs 163 to 166 of the judgment. 163:  
 9 "As is apparent from paragraph 108 of the present  
 10 judgment, the same counterfactual hypothesis is not  
 11 necessarily appropriate to conceptually distinct issues.  
 12 Where it is a matter of establishing whether the MIF had  
 13 restrictive effects on competition the question of  
 14 whether without those fees that by the effect of  
 15 prohibiting ex-post pricing and open payment systems  
 16 such as the MasterCard system could remain viable is not  
 17 in itself decisive."  
 18 That is what Mr Brealey took you to. But 164:  
 19 "By contrast, the Court should to that end assess  
 20 the impact of the setting of the MIF on the parameters  
 21 of competition ..."  
 22 So you are looking, by definition, at competition at  
 23 the relationship with competitor, not in a vacuum:  
 24 "... such as the price, the quantity and quality of  
 25 the goods and services. Accordingly, it is necessary,

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1 in accordance with the settled case law, to assess the  
2 competition in question [so a relative relationship]  
3 within the actual context in which it would occur in the  
4 absence of those fees."

5 Then 165 is a recitation of the standard case law,  
6 looking at actual context, economic legal effects etc.

7 That judgment doesn't support the proposition  
8 Mr Brealey seeks to get from it, that you look at the  
9 viability of a scheme in a vacuum. Quite the contrary.  
10 It confirms application of the existing case law has to  
11 be realistic, has to take account of actual context, has  
12 to take account of competition. So has to take account  
13 of what Visa is doing.

14 Then, back to the Sainsbury's closings, please.  
15 That's internal 74, paragraph 186. There is  
16 a reference -- a reliance on -- this is looking at their  
17 point which is: if one is looking at the legality of  
18 what MasterCard is doing one, should assume that Visa,  
19 because it is similar, is also acting unlawfully.  
20 Again, probably put a bit crudely but you recognise the  
21 point.

22 Two points are made. First of all they rely on the  
23 OFT decision. Well, the brief point there is that OFT  
24 decision was effectively withdrawn by the OFT because  
25 they couldn't support it, and was put to death by the

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1 CAT, it was quashed. So one doesn't really get much out  
2 of that. Then, in relation to British Airways, it  
3 simply doesn't support the proposition for which it is  
4 put. They have set out the paragraph they rely on at  
5 187 of their closings:

6 "Where, as in this case, the Commission is faced  
7 with the situation where numerous factors give rise to  
8 a suspicion of anti-competitive conduct on the part of  
9 several large undertakings in the same economic sector,  
10 the Commission is even entitled to concentrate its  
11 efforts on one of the undertakings concerned ..."

12 "Concentrate its efforts, ie investigate, one of the  
13 undertakings concerned:

14 "... while inviting the economic operators which  
15 have allegedly suffered damage as a result of the  
16 positively anti-competitive conduct of the other  
17 undertakings to bring the matter before the national  
18 authorities."

19 This has nothing to do with the proposition  
20 Mr Brealey is putting, which is you must assume Visa is  
21 acting unlawfully in order to consider whether  
22 MasterCard was acting unlawfully. What it is actually  
23 dealing with is the Commission's discretion to pursue  
24 investigations against some undertakings but not others  
25 involved in the same conduct.

18

1 It says nothing about the appropriate counterfactual  
2 to be adopted in this case. Mr Brealey sought to seize  
3 on the word "suspected" or "suspicious" in that  
4 paragraph to say there is a legal principle that if  
5 an undertaking is suspected of operating unlawfully,  
6 then one can and should assume it is operating  
7 unlawfully for the purposes of the counterfactual.

8 Nothing to that effect in the paragraph. But,  
9 equally, the presumption of innocence applies just as  
10 much, if not more strongly, in other areas of EU  
11 competition law, and that's simply not an appropriate  
12 basis to act but certainly no support for it in case  
13 law.

14 I'm moving on to page 25 of our closings. We can  
15 put away the Sainsbury's closings for the moment. Let  
16 me start with the parties' proposed counterfactuals.  
17 I will come on to the ones that the Tribunal has floated  
18 after I have dealt with these ones, if that's okay.

19 As you know, Mr von Hinten-Reed's analysis in his  
20 written opinion -- he tried to shift a bit orally, but  
21 in his written opinions -- was based on the assumption  
22 that if the MasterCard MIF had been low or zero, then  
23 the Visa MIF would have been low or zero. But that  
24 wasn't really based on any factual analysis, it was  
25 an assumption on his part. That's the way it was put in

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1 his report.

2 As you know, Dr Niels thinks that if MasterCard's  
3 domestic UK MIF had been low or zero Visa would have  
4 remained high, and indeed he thinks the same of Amex.

5 Let me deal first of all with Mr von Hinten-Reed's  
6 suggested counterfactual and why we say it is simply not  
7 realistic, which is what the case law requires.

8 First of all -- this is at page 26 of our  
9 closings -- as a matter of regulatory control, Visa did  
10 not have any regulatory obligations imposed upon it in  
11 respect of the level of its domestic UK MIF at any stage  
12 during the period of the claim. We have set out what  
13 constraints were imposed on Visa, but none of them  
14 concerned a UK domestic MIF. So no formal regulatory  
15 action taken against them.

16 The second question is regulatory incentive, if one  
17 likes, the threat of regulatory action during the  
18 period. But as a matter of regulatory incentive, at no  
19 stage during the period of the claim did Visa or  
20 MasterCard feel obliged, by virtue of a regulatory  
21 decision taken against the other competitor, to  
22 immediately follow suit. We have given the two examples  
23 at 73(a) and (b). When the Commission adopted its 2002  
24 Visa decision, which exempted Visa's consumer intra-EEA  
25 MIF -- so Visa's EEA MIF was effectively coming down

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1 from what it had been -- MasterCard didn't drop its own  
 2 intra-EEA MIF so as to bring it into line with the new  
 3 Visa MIF, it maintained its position, and that led to  
 4 the Commission decision and all the court proceedings.  
 5 So far from feeling constrained by regulatory  
 6 threat, MasterCard carried on doing what it was doing.  
 7 Equally, in 2009 we had the adoption of  
 8 the Commission's 19th December 2007 decision relating to  
 9 MasterCard's intra-EEA MIF, which brought the level down  
 10 even further. So MasterCard was then below Visa, and  
 11 Visa didn't immediately drop its debit or credit  
 12 intra-EEA MIFs. Indeed, it didn't drop its credit card  
 13 MIF until it gave commitments to the Commission in 2013.  
 14 And the Commission decision originally was 2007.  
 15 So the idea that regulatory threat would have meant  
 16 something happening in the short-term simply isn't borne  
 17 out by the facts of this case.  
 18 MR SMITH: Mr Hoskins, in the UK, the only proceeding was  
 19 the OFT's quashed proceeding against MasterCard, there  
 20 was no parallel proceeding against Visa by the OFT?  
 21 MR HOSKINS: Nothing that led to a formal decision.  
 22 I think -- and people involved can confirm this -- what  
 23 the OFT did generally was to just keep Visa and  
 24 MasterCard sort of on the hook saying, "We have not  
 25 dropped investigations against you", but they did not do

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1 anything pending the outcome of what happened in Europe.  
 2 The third question is: what about commercial choice?  
 3 What would Visa, in this counterfactual -- MasterCard is  
 4 at low or zero -- what would Visa have done as a matter  
 5 of commercial choice? Here Maestro is important.  
 6 Page 28 of the closings. We have got an annex which  
 7 sets out the Maestro story in more detail but just for  
 8 this purpose, what you see is prior to 1st January 2007  
 9 there was a differential between Maestro and Visa Debit,  
 10 6.6 basis points.  
 11 2004/2005, HBOS move from Switch, the predecessor to  
 12 Maestro, to Visa Debit. Around July 2006 Visa announced  
 13 that it was going to put its interchange fee up from  
 14 6.5p per transaction to 8p per transaction. As we know  
 15 from the evidence, Maestro didn't respond because  
 16 MasterCard didn't set the rate and the body that did,  
 17 including issuers and acquirers, couldn't agree to raise  
 18 the Maestro MIF. What that did was it increased the  
 19 differential between Maestro and Visa Debit to 9.2 basis  
 20 points.  
 21 Now, what that shows is that in a situation in which  
 22 MasterCard's interchange fees were materially lower than  
 23 Visa's, far from reducing its fees, Visa put its foot on  
 24 the pedal and raised its interchange fees, because they  
 25 wanted issuers to migrate to Visa.

22

1 Then, of course, we know what happened subsequently  
 2 is HSBC and RBS subsequently decided to switch. At  
 3 page 29 of the closing you will see the way the market  
 4 share went. We have seen that before. But what we know  
 5 is that what Visa actually did was it retained its  
 6 higher MIF whilst Maestro's market share collapsed. It  
 7 didn't drop the rate -- for whatever reason; out of  
 8 commercial choice, out of pressure from acquirers or out  
 9 of pressure from merchants -- it kept its foot on the  
 10 pedal and watched Maestro exit the market, and nobody  
 11 stopped it doing it, not a regulator, not acquirers, not  
 12 merchants.  
 13 That shows that when faced with a competing card  
 14 with materially lower MIFs, Visa did not choose to lower  
 15 its own credit card MIF, it chose to raise it.  
 16 It is important -- I know there is a dispute on  
 17 Maestro about what's the precise reason why HSBC and RBS  
 18 switched, to what extent was it the differential in the  
 19 MIFs, and to what extent was it reduced functionality on  
 20 the part of Maestro; but, important for this part of the  
 21 story, that doesn't matter, the question of why they  
 22 switched. What matters for the purposes of this part of  
 23 the story is that Visa maintained and then raised its  
 24 own MIF at a time when MasterCard was substantially  
 25 lower and at a time that MasterCard was disappearing

23

1 from the market.  
 2 MR JUSTICE BARLING: Was it substantially lower for  
 3 MasterCard's new debit card?  
 4 MR HOSKINS: It wasn't. But, as we saw, MasterCard retained  
 5 3% of the market.  
 6 MR SMITH: MasterCard's rate for its debit MasterCard was  
 7 the same, at 8p.  
 8 MR HOSKINS: Yes, as I just said.  
 9 MR SMITH: I am with you.  
 10 MR HOSKINS: It kept 3% of the market that way.  
 11 MR SMITH: Until the regulation came into effect, did it  
 12 stay at 8p?  
 13 MR HOSKINS: I would need to check that, sir.  
 14 We would need to check that, sir, I don't know the  
 15 answer off the top of my head.  
 16 But in a sense what's most important for this  
 17 present purpose is the period from just before 2004/05  
 18 when HBOS switches, so the early 2000s, we have  
 19 a differential of 6.6 basis points. You can take it up  
 20 until the point when HSBC and RBS switch if you like,  
 21 you have got that period, and what you see is again Visa  
 22 putting its foot to the floor, not the opposite.  
 23 MR JUSTICE BARLING: When did they introduce the new debit  
 24 card, the new MasterCard, roughly? About the same time?  
 25 MR HOSKINS: I would need to pick that up in the appendix.

24

1 (Pause). June 2006.  
 2 MR JUSTICE BARLING: June, thank you.  
 3 MR HOSKINS: Another point that was made by Sainsbury's --  
 4 we don't have to look it up, it is paragraph 176E, for  
 5 echo, of their closing -- they said that:  
 6 "Issuers would not migrate to Visa because they  
 7 would expect legal and commercial pressures to oblige  
 8 Visa to lower its own MIF."  
 9 Mr von Hinten-Reed made that point orally as well.  
 10 But, again, that is disproved by Maestro, because they  
 11 did switch.  
 12 Can I switch to the Amex evidence, if you will  
 13 excuse the pun, because Amex is a bit more specific  
 14 case. This is page 30 of the closing submissions.  
 15 We say that the evidence shows that if MasterCard's  
 16 UK domestic MIF had been zero or low during the claim  
 17 period, Amex would have maintained its merchant discount  
 18 rates at the actual level or, at the very least, would  
 19 have retained a material difference. Either will do.  
 20 Let me break it into periods. First of all, the  
 21 evidence relating to the claim period.  
 22 During the period from 2006 to 2009, Amex's merchant  
 23 discount rate was significantly higher than the MSCs  
 24 charged in respect of MasterCard and Visa. Again,  
 25 common ground, Amex maintained that differential. That

25

1 was despite the fact it had lower acceptance etc. That  
 2 is just Amex's business model. That's what it does.  
 3 You will hopefully remember this because we saw it in  
 4 cross-examination. If we can go to B, tab 11. This is  
 5 some of the information provided in response to the  
 6 Tribunal's questions. That was at page 152 of the  
 7 bundle.  
 8 Hopefully you will recognise that table because  
 9 I took Mr von Hinten-Reed to it in cross-examination.  
 10 What this shows is that whilst during the period 06/09  
 11 Amex had a materially higher merchant discount rate than  
 12 Visa and MasterCard's MIFs, three-party schemes, which  
 13 of course in the UK is primarily Amex, increased its  
 14 market share from 8% to 14%. So they almost doubled  
 15 their market share in that three-year period.  
 16 Again, what does that tell us? Far from seeking to  
 17 lower its merchant discount rates to levels similar to  
 18 the MIFs offered by MasterCard and Visa, Amex chose to  
 19 maintain a high differential in order to grow its market  
 20 share.  
 21 And nobody stopped it. It wasn't subject to  
 22 competition regulation. It didn't deal with acquirers,  
 23 save in relation to 3.5. And merchants weren't saying,  
 24 "Hang on, you have got a large differential so we are  
 25 not going to deal with you or we are going to stop

26

1 accepting you". The facts are what they are; the market  
 2 share went up despite the large differential.  
 3 You will remember from the evidence, this is  
 4 paragraph 94 of our closings, that MasterCard was only  
 5 able to stem the flow of market share to Amex by  
 6 offering higher MIFs on its MasterCard World card, some  
 7 time around 2009 and 2010, and that not only arrested  
 8 the rise in Amex market share at the expense of the  
 9 three-party schemes, it actually clawed some of it back.  
 10 We set out that evidence at paragraph 94.  
 11 What we say is the evidence relating to the claim  
 12 period therefore confirms that Amex was able to, and  
 13 did, maintain a material differential with MasterCard's  
 14 MIF in order to grow its business, same as Visa. It is  
 15 the same business, it is the same commercial imperative.  
 16 And nobody was apparently able to stop it. Whether  
 17 people tried, we don't have the evidence, but what we  
 18 know is it didn't work, because we see the dramatic rise  
 19 in market share.  
 20 Let's move into the evidence relating to the  
 21 regulation. This is paragraph 96 of the closings, and  
 22 what Sainsbury's has brought up in the course of the  
 23 trial is its negotiations with Amex in 2014 and 2015.  
 24 As we know, it related in a certain -- it is  
 25 confidential so I will try and tread carefully --

27

1 merchant discount rate at a certain level, but you will  
 2 note there was still a substantial differential between  
 3 the rate negotiated and the rate of 0.3 allowed for by  
 4 the regulation. It didn't bring it down actually  
 5 anywhere near close to what Visa and MasterCard are now  
 6 constrained to apply.  
 7 Let's look a bit closer at these negotiations.  
 8 First of all, because what we are looking for of course  
 9 is a counterfactual that applied during the claim period  
 10 which is before the regulation, what Sainsbury's say is,  
 11 "Look, we had these negotiations in 2014 and 2015, this  
 12 is evidence of what would have happened in the  
 13 counterfactual in the claim period". One of the points  
 14 we make is no, no, no, no; this is looking at what is  
 15 happening when the regulation is on the stocks and about  
 16 to come into force, therefore it is not relevant when  
 17 you are trying to identify a counterfactual for the  
 18 actual claim period. So it is a bit convoluted but  
 19 that's why we end up in this place.  
 20 But the negotiations with Amex, 2015, take place  
 21 against the backdrop of the impending adoption and  
 22 implementation of the interchange fee regulation. If we  
 23 can look at the regulation, it is at E1, tab 21.  
 24 You have seen this in opening. If you go to  
 25 page 450 you will see Article 1 is "General provisions".

28



1 Then over the page, Article 1(5):  
 2 "When a three-party payment card scheme licences  
 3 other payment service providers for their issuance of  
 4 card-based payment instruments or the acquiring of  
 5 card-based payment transactions or both, or issues  
 6 card-based payment instruments with a co-branding  
 7 partner through an agent, it is considered to be  
 8 a four-party payment card scheme."  
 9 That is Amex's GNS, 3.5. So for the purposes of the  
 10 regulation it is considered to be a four-party payment  
 11 card scheme.  
 12 But Amex get a little time off, potentially:  
 13 "However, until 9 December 2018 in relation to  
 14 domestic payment transactions, such a three-party  
 15 payment card scheme may be exempted from the obligations  
 16 under chapter 2 provided that the card-based payment  
 17 transactions made in a member state under such  
 18 a three-party payment card scheme do not exceed on  
 19 a yearly basis 3% of the value of all card-based payment  
 20 transactions made in that member state."  
 21 Of course, that's a disincentive to grow market  
 22 share for three years. Because if you grow your market  
 23 share too much, you fall into the regulation; and if you  
 24 don't grow it too much, you have a competitive advantage  
 25 for three years, even as a three and a half card scheme

1 competing with a four-party scheme.  
 2 So you look at the negotiation, Amex and  
 3 Sainsbury's, Amex has got this, which it didn't have  
 4 during the period of the claim. During the period of  
 5 the claim, Amex has an incentive to increase its market  
 6 share and it did. At this time, when the negotiations  
 7 are taking place, it actually has a disincentive, a  
 8 regulatory, legislative disincentive, not to increase  
 9 its market share.  
 10 You will see that Dr Niels was asked about this. It  
 11 is at the top of page 33 of our closings. He explained  
 12 the effect of these changes when cross-examined.  
 13 If I could just ask you to read that quote to  
 14 yourselves. Paragraph 100. (Pause).  
 15 You don't need an expert economist to tell you that.  
 16 It is clearly right. That's one reason why looking at  
 17 what happened in 2015 does not tell you what the  
 18 realistic counterfactual would have been in the period  
 19 of the claim when the regulation was just a bright light  
 20 in someone's eye for most of the period. It is just not  
 21 part of the actual counterfactual.  
 22 The second point is, even if one thought it were  
 23 relevant to look at these negotiations for  
 24 a counterfactual in the period of the claim, look at the  
 25 result. MasterCard and Visa now 0.3, and you see what

1 the negotiated rate was.  
 2 I'm now at the bottom of page 33 of our closing  
 3 submissions. It is the evidence relating to Australia,  
 4 because you will remember that in his written reports  
 5 Mr von Hinten-Reed relied heavily, and indeed in his  
 6 cross-examination kept going to Australia. That was his  
 7 lifeboat whenever the going got tough.  
 8 But the truth is Australia died a death during his  
 9 cross-examination. In the first place -- this is  
 10 paragraph 103 of the closings -- it is quite clear from  
 11 the evidence that the reduction in Amex's MSCs in  
 12 Australia was driven by aggressive surcharging by  
 13 Australian merchants. And the evidence we had from  
 14 Sainsbury's own witnesses was that surcharging was  
 15 neither desirable nor feasible for UK retailers. We  
 16 have set out the evidence in detail at paragraph 103.  
 17 I'm not going to read it all out. There you have it.  
 18 Surcharges just isn't on the table in the UK.  
 19 The second point about Australia -- this is page 36,  
 20 paragraph 105 of the closings -- is that under the  
 21 Australian regulation, the caps imposed on MasterCard  
 22 and Visa were weighted average caps. What that meant is  
 23 that MasterCard and Visa were free to set higher  
 24 interchange fees for premium cards to compete directly  
 25 with Amex. And they did so. We have seen that

1 evidence.  
 2 Remember, what we are looking for here, we are  
 3 looking for the counterfactual on Sainsbury's case,  
 4 which is that MasterCard is only entitled to set a MIF  
 5 at up to a maximum of 0.15% for all transactions, and  
 6 that's across the board, whether it be a standard card  
 7 or a premium card.  
 8 So in this UK scenario MasterCard would not be able  
 9 to set competitive premium interchange rates, and that's  
 10 why Australia doesn't help you, because in the UK you  
 11 have MasterCard down here, you have Amex here,  
 12 switching. Mr von Hinten-Reed's world of Australia, you  
 13 have MasterCard and Visa here, Amex here, less  
 14 switching. But it doesn't help you, Australia. I don't  
 15 like taking the point that so-and-so didn't put  
 16 something in cross-examination to someone, and you get  
 17 ridiculous ones where people say, "You didn't put this  
 18 document", or this line, but Australia wasn't put at all  
 19 to Dr Niels as an appropriate counterfactual. It  
 20 literally did die a death during Mr von Hinten-Reed's  
 21 cross-examination.  
 22 Page 37 of the closings. Sainsbury's argued that if  
 23 MasterCard were zero or low, Visa would definitely have  
 24 come down to the same level because of the threat of  
 25 damages, because they know that if they didn't come

1 down, they would have had to have handed over all the  
 2 money in any event in damages. Again, that was killed  
 3 off in cross-examination because it is based on the  
 4 unrealistic assumption that every person who was  
 5 entitled to bring a claim would successfully do so  
 6 against Visa.  
 7 Again, we have set out the cross-examination on that  
 8 at 109. It was accepted by Mr von Hinten-Reed. But,  
 9 equally, again let's stay in the real world. During the  
 10 period of the claim, neither MasterCard nor Visa reduced  
 11 their UK MIF to 0.15 or anything approaching it because  
 12 they were worried about the risk of damages. MasterCard  
 13 fought its corner in Europe. Visa stood its ground as  
 14 well. It was only when the regulation came in that you  
 15 saw those drops in the UK. So that threat of damages is  
 16 simply not part of the realistic counterfactual.  
 17 The final point on this Sainsbury's proposed  
 18 counterfactual is, of course, they have got the point:  
 19 well, unless you assume that Visa are acting unlawfully  
 20 as well, and therefore treat them as coming down to low  
 21 or zero, you can't prove that MasterCard are acting  
 22 unlawfully. The artificiality of that is plain on its  
 23 face, and I think I have dealt with that already;  
 24 Mr Brealey's reliance on the OFT, his reliance on  
 25 British Airways etc. It simply doesn't tally with the

33

1 case law, which is: look at competition, look at the  
 2 actual context, look at something that's realistic. You  
 3 simply cannot adopt the sort of artificial construct  
 4 which requires you to assume that Visa is acting  
 5 unlawfully. It is completely inconsistent with the case  
 6 law.  
 7 That is why we say the realistic counterfactual has  
 8 to be, if MasterCard is low or zero, Visa maintains,  
 9 Amex maintains. It doesn't have to be exactly the same  
 10 level but at or around the same level. That's what we  
 11 say is quite clear from the evidence. So let's take  
 12 that counterfactual. We are low, everyone else high,  
 13 what happens? That's ancillary restraint.  
 14 This is page 40 of the closings. I could take this  
 15 quickly because it is really familiar to you now.  
 16 118, it is common ground between the parties that  
 17 the level of the UK MIF is a very important driver of  
 18 competition. We set out the evidence; it is  
 19 Mr von Hinten-Reed's own first report that that comes  
 20 from.  
 21 Second point, top of page 41, it is also common  
 22 ground between the economic experts that in  
 23 a counterfactual in which MasterCard's domestic UK MIF  
 24 was low but Visa and Amex's remained at their actual  
 25 level for any sustained period, MasterCard would have

34

1 been driven out of the market, the UK market.  
 2 Mr von Hinten-Reed accepted that expressly in  
 3 cross-examination. So you look at 121, we set out what  
 4 the actual differentials were during the period. Then  
 5 you remember, hopefully, I took Mr von Hinten-Reed, you  
 6 remember I took him to part of our skeleton. It is A,  
 7 tab 2, at page 211(e).  
 8 Remember, I wanted to show him what the differential  
 9 would be in the counterfactual of us low, Visa and Amex  
 10 the same. Then I put it to him that if that was the  
 11 position, MasterCard would be driven out of the market,  
 12 and he said he accepted that was yes, as long as that  
 13 applied over the period of the claim.  
 14 We have set out the extract. Bottom of page 41 onto  
 15 page 42. But that's absolutely fundamental. I invite  
 16 you just quickly to read that extract at 42.  
 17 MR JUSTICE BARLING: Which page are we reading? We are  
 18 reading the bit on --  
 19 MR HOSKINS: It is the cross-examination.  
 20 MR JUSTICE BARLING: Right.  
 21 MR HOSKINS: Yes. (Pause).  
 22 Dr Niels agreed. So you have got agreement by the  
 23 experts on what would happen in the counterfactual  
 24 I have identified as the realistic one. There is  
 25 another practical importance, of course, as --

35

1 MR JUSTICE BARLING: Do you think it is realistic that that  
 2 would have stayed the --  
 3 MR HOSKINS: I'm going to come to that. I know it is there  
 4 and I'm going to come to it.  
 5 MR JUSTICE BARLING: Yes.  
 6 MR HOSKINS: No side-stepping.  
 7 MR JUSTICE BARLING: It's all right.  
 8 MR HOSKINS: No side-stepping, I promise.  
 9 MR JUSTICE BARLING: No, okay.  
 10 MR HOSKINS: What I want to do is look at what the evidence  
 11 is before the Tribunal, and I think with this case you  
 12 will probably agree with me that unless one tries to  
 13 keep a framework and keep to it, you get lost very  
 14 quickly, at least I do, so I'm sorry if this is slightly  
 15 pedestrian.  
 16 MR JUSTICE BARLING: No, that's fine.  
 17 MR HOSKINS: I will fall off the log if I go too fast.  
 18 This is quite important because, of course, you have  
 19 the debate about why did people switch from Maestro? To  
 20 what extent was it the difference in the interchange  
 21 fee? To what extent was it reduced functionality? But  
 22 as soon as Mr von Hinten-Reed gave this answer, that  
 23 actually doesn't matter, because he accepts that  
 24 migration would occur at the sort of differentials in  
 25 the counterfactual we are looking at. So you don't have

36

1 to actually resolve that factual aspect of Maestro, once  
 2 both economists agree that we would be wiped out of the  
 3 market at the sort of differentials that they were  
 4 applying it.  
 5 MR JUSTICE BARLING: You think we are bound by what  
 6 economists say about the payment cards as to what would  
 7 happen in a payment card world? They are not really  
 8 experts on that. It is a commercial issue really,  
 9 rather than an economist issue.  
 10 MR HOSKINS: I'm going to deal with that as well. I'm  
 11 coming to that. But the whole point of this was the  
 12 experts. All the counterfactuals are analysed by the  
 13 experts.  
 14 MR JUSTICE BARLING: But experts get used for all sorts of  
 15 things that are not really their expertise, don't they?  
 16 This is one of the problems. Mr von Hinten-Reed's or  
 17 Dr Niels' idea of the commercial realities of the  
 18 intricacies of what happens in a payment card system,  
 19 I mean, would probably be a lot better than mine but  
 20 whether it is a real matter of economic expertise might  
 21 be a bit doubtful, actually.  
 22 MR HOSKINS: I'm going to take you to all the evidence and  
 23 I'm going to come to the factual evidence. I have  
 24 already done it a bit with Maestro.  
 25 MR JUSTICE BARLING: No, it was just the implication that

37

1 because Dr Niels and Mr von Hinten-Reed were agreed on  
 2 something, that was the end of it.  
 3 MR HOSKINS: There is an important point here, sir, and it  
 4 is tempting in this sort of case. We have been here for  
 5 7 weeks and you have heard evidence from economists  
 6 about what would have happened, we have heard some  
 7 relevant evidence from factual witnesses, I will come to  
 8 that, you have seen what happened in Maestro.  
 9 I hope I'm not speaking out of turn, but there is  
 10 a huge temptation to say: actually, stand back from this  
 11 and as a matter of theory we prefer this.  
 12 MR JUSTICE BARLING: But counterfactuals are theory, aren't  
 13 they?  
 14 MR HOSKINS: Based on fact.  
 15 MR JUSTICE BARLING: Based on, you know --  
 16 MR HOSKINS: I will be blunt, sir, if you want to come up  
 17 with a counterfactual --  
 18 MR JUSTICE BARLING: I'm not saying I want to come up with  
 19 anything. I'm just --  
 20 MR HOSKINS: If you want to.  
 21 MR JUSTICE BARLING: I'm just testing whether this is really  
 22 something that is a closed question because two  
 23 economists agree on what would happen in an industry  
 24 with which they are not particularly experts. You know,  
 25 they are not, I mean --

38

1 MR HOSKINS: Sir, as you accepted, but more expert than you.  
 2 We will look at the factual evidence. My point is  
 3 a simple one. I'm sorry if it is going to be too blunt,  
 4 it is probably too blunt already. If you want to say  
 5 there is an alternative counterfactual other than the  
 6 one that has been considered by the parties, it has to  
 7 be based on the evidence, and that's the process I'm  
 8 going through to show you what the evidence is. You are  
 9 not surprised, the punchline is going to be I don't  
 10 think either of your two counterfactuals are actually  
 11 supported by the --  
 12 MR JUSTICE BARLING: You are assuming we have got two  
 13 counterfactuals.  
 14 MR HOSKINS: They are potential ones. I am not going to  
 15 stick my head in the sand. You put a certain form of  
 16 questioning, and you are going to ask me the same  
 17 questions again. You have a completely open mind and  
 18 that's why I'm here to persuade you one way or the  
 19 other, but you have floated two possibilities and I want  
 20 to address them.  
 21 My point is any counterfactual has to be based on  
 22 the evidence, has to be supported by the evidence, and  
 23 I doubt that's going to be controversial between us.  
 24 I'm also reminded, in terms of this particular point  
 25 about what would have happened in the differential of us

39

1 here and everyone else there, of course all our factual  
 2 witnesses say we would have been driven out of the  
 3 market. So it is not just the economists.  
 4 MR JUSTICE BARLING: If it had remained like that?  
 5 MR HOSKINS: If it had remained, correct. That's what the  
 6 experts say but, again, as a sort of adjunct to what you  
 7 have just put to me, it is also confirmed, if you think  
 8 about the sorts of sums that were involved in this  
 9 counterfactual play. It is paragraph 125 of the  
 10 closings. We give you an example.  
 11 Taking 2011 as a mid-point during the claim period,  
 12 total UK purchases on UK MasterCard credit charge cards  
 13 amounted to in excess of £82 billion. Even based on the  
 14 level of exemptible UK MIF proposed by  
 15 Mr von Hinten-Reed, this means UK banks issuing  
 16 MasterCard would have together received over  
 17 £500 million per annum of additional revenue from moving  
 18 their business to Visa and over £800 million per annum  
 19 from moving to Amex.  
 20 If you want some facts -- would they really have  
 21 done it? Yes, they would, because it is worth, to the  
 22 industry, 500 million. Which is pretty compelling. It  
 23 is not peanuts.  
 24 Closings 126. It is the Australia point.  
 25 Mr von Hinten-Reed accepted that Australia doesn't help

40

1 us on this because in Australia Visa and MasterCard were  
 2 subject to regulation at the same time, so you don't  
 3 have the disparity that we are considering.  
 4 Fourth point. In his second report,  
 5 Mr von Hinten-Reed considered what would happen if the  
 6 only way that an acquirer could obtain payment from  
 7 an issuer was by means of a bilateral agreement. This  
 8 was his: no payment moves to the acquirer absent  
 9 a bilateral agreement. And that's the hold-up problem.  
 10 His evidence is the scheme collapses. So that doesn't  
 11 work either.  
 12 So a system, "no payment to acquirer unless  
 13 bilateral" doesn't work because of the hold-up problem,  
 14 it collapses. Because the issuers hold out the charge  
 15 too much.  
 16 PROFESSOR JOHN BEATH: Sorry, could I just ask you to say  
 17 a bit more about that? Because it seems to me that if  
 18 you are thinking about bilateral agreements, it matters  
 19 whether these are agreed ex-ante or ex-post. The  
 20 hold-up problem arises in an ex-post situation but if  
 21 you have a set of bilateral agreements that are  
 22 enshrined in contract, there can't surely be a hold-up  
 23 because there is a right, through contract law, to  
 24 ensure that the amounts that have been agreed ex-ante to  
 25 be handed over are in fact handed over.

41

1 MR HOSKINS: It depends, because I will come on -- because  
 2 there is a different bilateral, which is one the  
 3 Tribunal floated.  
 4 PROFESSOR JOHN BEATH: Yes, I'm just asking about this one.  
 5 MR HOSKINS: Sure. In this one the presumption is that  
 6 Mr von Hinten-Reed is analysing no payment absent  
 7 bilateral. And his point is that whether it would be  
 8 an ex-post or ex-ante bilateral, the scheme would still  
 9 collapse because the issuers would hold too much power  
 10 because of the honour all cards rule. Because someone  
 11 goes into a shop and makes the purchase --  
 12 PROFESSOR JOHN BEATH: That's to say there would in fact be  
 13 no contract be signed because the issuers would be  
 14 always asking too much of the acquirers.  
 15 MR HOSKINS: I think there would be contracts. That's his  
 16 premise, is that there would be contracts. But the  
 17 issuers would ask for too much, and he says the scheme  
 18 would collapse under that. It is because of the honour  
 19 all cards rule that one gets this problem. That's why  
 20 it is so important that the case law says, the Court of  
 21 Justice said, when you are looking at these sort of  
 22 questions of objective necessity you assume the honour  
 23 all cards rule is valid and is there.  
 24 MR SMITH: I think you will be coming to it, paragraph 128,  
 25 which is assuming the honour all cards rule, is there,

42

1 absent agreement, a right in the issuing bank to make  
 2 such a deduction as it pleases? Which is the genesis of  
 3 the hold-up problem. But I will let you --  
 4 MR HOSKINS: I was about to come to it, absolutely. In that  
 5 situation -- because if you take out the scheme, the  
 6 current scheme is you can have bilaterals, but if no  
 7 bilateral the MIF applies. That's the current  
 8 situation. Absent that, you would have a system that  
 9 didn't actually provide any rules for interchange. We  
 10 talked about the blue pencil. If you just take those  
 11 two out, what are you left with is you are left with  
 12 a system, a very uncertain system of people -- you would  
 13 either have to say there was either some sort of implied  
 14 contract, which might well be difficult because you  
 15 would be asking yourselves exactly the same question  
 16 because to get an implied term in a contract is it  
 17 necessary for the contract to operate? Very similar to  
 18 a ancillary restraint-type issue.  
 19 The only way I can think, but I think it might work  
 20 the other way, is a quantum valebat-type situation,  
 21 where you would be trying to evaluate what value of  
 22 services the issuer provided. But that would be odd,  
 23 because in this case you would presume it would be  
 24 issuer actually holding money back and saying "I'm  
 25 entitled to hold this" or "I'm holding this", whereas

43

1 a quantum valebat, made by the acquirer, the acquirer  
 2 would be saying, "You have charged me too much", and you  
 3 would have to plead some sort of implied term of  
 4 contract in breach of it.  
 5 But the short point is, imagine a scheme which is  
 6 set up without any rules on how much an acquirer is to  
 7 pay an issuer, the point is nobody would join that  
 8 system, because of the legal uncertainty. Because there  
 9 is no clean legal answer in contract or restitution  
 10 absent a scheme rule.  
 11 MR SMITH: I think you may be doing the MasterCard rules  
 12 a little bit of an injustice though, because if one  
 13 looks at, I think it is section 8 of the rules.  
 14 MR HOSKINS: Can you show them to me?  
 15 MR SMITH: E10, isn't it?  
 16 MR BREALEY: E3.10.  
 17 MR JUSTICE BARLING: E3.10, tab 201. I think we looked at  
 18 the other one, which is tab ...  
 19 MR SMITH: Chapter 8 deals with settlement.  
 20 MR HOSKINS: What page are we on?  
 21 MR SMITH: I am looking at page 4155.  
 22 MR HOSKINS: Thank you.  
 23 MR SMITH: 8.3:  
 24 "A transaction settled between customers gives rise  
 25 to the payment of an appropriate interchange fee or

44

1 service fee, as applicable. The corporation has the  
 2 right to establish default interchange fees and default  
 3 service fees ... it being understood that all such fees  
 4 set by the corporation apply only if there's no  
 5 applicable bilateral interchange fee or service fee  
 6 agreement between two customers in place. The  
 7 corporation establishes all fees for interregional  
 8 transactions and intraregional transactions ..."

9 The rest is not relevant. So you will have to apply  
 10 a blue pencil to remove the default fees and only  
 11 contain reference to bilateral fees.

12 What this seems to be saying, but do correct me if  
 13 I'm wrong, is that a transaction settled between  
 14 customers only gives rise to the payment of the  
 15 appropriate fee if (a) it is a default fee or (b) it is  
 16 bilaterally agreed.

17 If you strike a line through the default and say it  
 18 doesn't exist, isn't there simply a right to deduct only  
 19 where there is a bilaterally agreed fee, and otherwise,  
 20 when there is a transaction entered into with  
 21 a merchant, communicated into the system, and the system  
 22 settles, the settlement is at 100% with no discount?

23 MR HOSKINS: The first response to that is that you can't  
 24 blue pencil it in the way you have suggested, sir,  
 25 because the way it is framed is that the corporation has

45

1 the right to establish interchange fees and default  
 2 service fees. It begins that all fees set by the  
 3 corporation apply. So put a line through all of that  
 4 and you are left with only if there is no applicable  
 5 bilateral interchange fee or service fee agreement  
 6 between two customers in place.

7 The blue pencil test is a very mechanical one. That  
 8 is the effect of it, is default applies if absence of  
 9 a bilateral. But there's not actually -- the wording  
 10 isn't there to bear a blue pencil which would leave you  
 11 with bilateral as the rule. That is the first point.

12 Then it doesn't really matter in a sense, that blue  
 13 pencil point, because you can still put the point to me  
 14 in an ancillary restraints/objective necessity scenario,  
 15 one isn't hidebound by having to blue pencil to say is  
 16 it objectively necessary or not? You can still put the  
 17 point to me, which is: what is the position -- I think  
 18 the way you put it during the questioning, so if it has  
 19 moved on apologies if I have got it wrong, but the  
 20 position is: no payment absent bilateral. Which means  
 21 that if the issuer wants money it has to enter into  
 22 a bilateral, and if it doesn't, it won't get any money.  
 23 So it is the flip side of the Mr von Hinten-Reed  
 24 collapsing scenario.

25 MR SMITH: It is the flip side. What we are saying is let's

46

1 suppose there is a transaction where a customer buys  
 2 a book for £25 in the shop and that transaction is  
 3 accepted, so it is communicated into the system, and not  
 4 individually but it will be aggregated, but that £25  
 5 will move from the issuing bank to the acquiring bank to  
 6 the merchant. But at each stage in that process there  
 7 is a deduction, and in the first stage there is  
 8 a deduction in the form of a retention, which is the  
 9 interchange fee, it is not £25 but £25 minus whatever  
 10 percentage it is.

11 MR HOSKINS: Yes.

12 MR SMITH: That net figure moves to the acquiring bank, who  
 13 also retains the difference between the interchange fee  
 14 and the merchant service charge, and the net/net figure  
 15 is passed down to the merchant.

16 MR HOSKINS: Yes.

17 MR SMITH: So he doesn't get 100%, he gets whatever it is,  
 18 97.5 or more. So blue pencil is showing my Common Law  
 19 contractual traditions too much; what we are talking  
 20 about is a form of rules here which somehow, without  
 21 doing too much violence to the provisions of 8.3, is  
 22 removing the default but allowing the bilateral to  
 23 remain, without saying what the bilateral is.

24 MR HOSKINS: Yes.

25 MR SMITH: In that situation, assuming no bilateral, we have

47

1 to ask ourselves what happens at the issuer stage, can  
 2 the issuer take anything?

3 MR HOSKINS: Yes.

4 MR SMITH: It is that issue which I'm puzzled about, because  
 5 whilst I can quite see that there might be an argument  
 6 for a claim against an acquiring bank on a sort of  
 7 quantum valebat, quantum meruit basis. I'm not sure  
 8 I see the basis for self-help here, that the issuing  
 9 bank could say: well, my services are worth 5%.

10 MR HOSKINS: I understand. You have pushed me into  
 11 paragraph 135 of the closings.

12 MR SMITH: I do apologise.

13 MR HOSKINS: That's helpful, because we are in the same  
 14 place. We are assuming that in this situation, absent  
 15 bilateral agreement, issuer gets no payment.

16 MR SMITH: Yes.

17 MR HOSKINS: That's the point. Remember, we are looking at  
 18 an counterfactual that applies in a situation where  
 19 MasterCard would have this rule, Visa and Amex would  
 20 still have a MIF and would still be setting it high;  
 21 subject to the point I'm going to come onto about what  
 22 commercial pressure would do, but let's take this in  
 23 stages.

24 MR SMITH: Indeed, but before we move on to that it would be  
 25 very helpful to know if this construction of 8.3 is

48

1 wrong, why it is wrong.  
 2 MR HOSKINS: That is my submission, which is the blue pencil  
 3 test doesn't allow you to re-write to give effect to the  
 4 rule we are now discussing.  
 5 MR JUSTICE BARLING: Surely we are not doing a blue pencil  
 6 test, are we? We are saying --  
 7 MR HOSKINS: That's my point.  
 8 MR JUSTICE BARLING: It is not a Common Law blue pencilling.  
 9 MR HOSKINS: You can still put the point to me without the  
 10 blue pencil test.  
 11 MR SMITH: There may be a distinction without a difference  
 12 here. What I'm trying to work out is, on our  
 13 counterfactual, where the MIF is excluded, eliminated,  
 14 do we need to go down the route of the hold-up concern  
 15 and the need then to posit in the counterfactual the  
 16 rule against an ex-post facto negotiating or is that in  
 17 fact --  
 18 MR HOSKINS: It is a different analysis.  
 19 MR SMITH: It is a different analysis.  
 20 MR HOSKINS: Yes.  
 21 MR SMITH: What I'm really putting to you is, which is  
 22 right? In other words, is it the case -- and it is  
 23 really just a question of law -- that on the true  
 24 understanding of the rules, if you take away the  
 25 default, there's no entitlement to deduct or,

49

1 conversely, if you take away the default, it is  
 2 a free-for-all?  
 3 MR HOSKINS: Sorry, you are asking me to look at the  
 4 particular rules as they are and imagine that one blue  
 5 pencils the whole of that wording.  
 6 MR SMITH: The Chairman is right that we should lose the  
 7 phrase "blue pencil".  
 8 MR HOSKINS: That's why I said: are we discussing -- sorry  
 9 to ask again, but it will help me answer the question.  
 10 Are we discussing a potential scheme in which the rules  
 11 are the issuer cannot deduct unless there is  
 12 a bilateral? That's what I understood to be the issue.  
 13 That's what I was prepared to address. One gets there  
 14 simply because in the context of objective necessity one  
 15 is asking: is there another way in which the scheme  
 16 could operate, which wouldn't make it impossible for it  
 17 to operate, other than the MIF?  
 18 MR SMITH: When one is discussing the counterfactual, the  
 19 counterfactual is what would happen if this default is  
 20 removed. And one ought -- but again do correct me if  
 21 I'm wrong -- to do the least possible violence to the  
 22 rest of the scheme rules in order to understand how this  
 23 would work in the counterfactual.  
 24 MR HOSKINS: Indeed, they are supposed to remain in place,  
 25 according to the case law, so that's why the honour all

50

1 cards rule is assumed to be valid. Yes, absolutely.  
 2 MR SMITH: Indeed. What I'm asking is, taking away this  
 3 default but keeping everything else, what is the  
 4 position for us to feed into the counterfactual? Is it,  
 5 on the one hand, no deduction? Or is it, on the other  
 6 hand, a free-for-all --  
 7 MR HOSKINS: It's a matter of statutory construction where  
 8 they are in there, it will just be a free-for-all, which  
 9 would clearly have problems because nobody -- that  
 10 scheme would not be viable. Let me take that.  
 11 A free-for-all would not be viable, because nobody would  
 12 sign up to that scheme if you were left with, for  
 13 example, quantum valebat-type issues. That is  
 14 unworkable.  
 15 MR SMITH: Indeed, because one can see that both cardholders  
 16 and merchants, to say nothing of the banks in between,  
 17 but simply the cardholders and merchants would say the  
 18 scheme is not fit for the purpose. The whole point is  
 19 that this is a convenient way of paying the merchant.  
 20 MR HOSKINS: Yes. Then flip side, as a contractual question  
 21 really, is, if those words weren't there, would the  
 22 members be entitled to enter into bilateral agreements?  
 23 Would the scheme allow that? If it didn't expressly  
 24 allow it, if that makes sense.  
 25 I don't know. It is a really difficult question.

51

1 You would have to go through the scheme rules and look  
 2 for objective pointers as a matter of contractual  
 3 construction of whether that was allowed or not. But it  
 4 is a really detailed exercise of contractual  
 5 construction to get to the answer, and I have not done  
 6 it.  
 7 MR SMITH: Okay, well thank you.  
 8 MR HOSKINS: You would probably have to fall  
 9 into, certainly, implied terms. It would be first of  
 10 all a question of whether as a matter of statutory  
 11 construction was this excluded by the rest of the  
 12 contractual rules; and if it weren't expressly excluded,  
 13 you would then be looking to see, is it necessary to put  
 14 something in place to allow the contract to operate?  
 15 Then that probably takes us back into the question of  
 16 competition law, which is: what is it that's necessary?  
 17 Is it sufficient, for example, to have a rule, issuer  
 18 doesn't receive absent bilateral, or do you indeed need  
 19 some sub-default such as a MIF?  
 20 I think, through that contractual analysis, it  
 21 brings us back to that question, just because of the  
 22 similarity between the test of implying a term into  
 23 a contract and indeed the competition law here, which is  
 24 something which is necessary to allow the contract to  
 25 operate, because that's actually, fortuitously, the same

52

1 question, although for a different purpose in each case.  
 2 MR SMITH: You see why we are asking the question? It is  
 3 not in theory what one could have as a scheme, because  
 4 I entirely accept that one could have either a scheme  
 5 that was zero deduction or a scheme that was the issuing  
 6 bank deducts what it thinks its services are worth.  
 7 Either, no doubt, is possible, although one might have  
 8 views as to its viability. But because one needs to  
 9 import into the counterfactual as much of the real world  
 10 as remains when one has taken away the provision that is  
 11 said to be restrictive of competition, it does seem to  
 12 matter what, as a matter of construction, the answer is,  
 13 as opposed to how one might build the scheme apart from  
 14 that.  
 15 MR HOSKINS: The way I have approached it, this may be  
 16 a practical way rather than a sort of perfect way, is  
 17 what one knows is the scheme operates with the MIF  
 18 because that's the way it has operated for years.  
 19 What's then been done is a number of different  
 20 counterfactuals have been proposed: could the scheme  
 21 operate with this or could it operate with this, could  
 22 it operate with this? And the way -- again to put it  
 23 crudely -- we have approached this is to say no, it  
 24 can't operate with that or that or that, and then by  
 25 a process of elimination, so therefore it must need the

1 MIF. Whereas yours is a different approach, and it is  
 2 a more perfectionist approach, which is to say: absent  
 3 this, what would be the proper contractual construction?  
 4 MR SMITH: Then, what would be the consequences given that  
 5 construction? Exactly.  
 6 What I'm in a sense putting to you is, how much of  
 7 the "real world" can we import into our counterfactual  
 8 world to make, as it were, the hypothetical exercise  
 9 that we are undertaking as narrow and as tightly framed  
 10 as possible?  
 11 MR HOSKINS: I think it's difficult, because when one is  
 12 asking what would happen absent the MIF, one has to  
 13 almost -- as everyone has done it -- well, could you put  
 14 this in its place? And a number of different  
 15 possibilities have come up and then one has to look at  
 16 each of them. Because it is quite difficult just  
 17 theoretically, philosophically, to come up with  
 18 an approach which wouldn't require you to say: what  
 19 about this, what about that? Because otherwise you are  
 20 just in a bit of a vacuum.  
 21 MR SMITH: That's what I'm trying to avoid.  
 22 MR HOSKINS: I will be honest, I haven't attempted that sort  
 23 of contractual broad sweep. What I have done -- maybe  
 24 this is my sort of defendant outlook, if you like -- is  
 25 it works with a MIF, these are the other things that

1 have been proposed and I'm going to submit why it  
 2 doesn't work with those.  
 3 But absolutely, I agree that insofar as one is  
 4 asking a question how much of the real world should be  
 5 imported into the counterfactual, the answer is: as much  
 6 as possible. And I accept: as much as practical.  
 7 MR JUSTICE BARLING: You say that, do you, for both the  
 8 objective necessity counterfactual and the restriction  
 9 on competition one?  
 10 MR HOSKINS: Yes. They are actually quite different  
 11 questions -- I'm nodding away, as one does --  
 12 MR JUSTICE BARLING: I know you are.  
 13 MR HOSKINS: Because with objective necessity one is asking:  
 14 is there an alternative that could allow the scheme to  
 15 operate? And, actually, restriction of competition is  
 16 a different exercise, because it is saying: assume the  
 17 actual with the MIF and assume the position without the  
 18 MIF, what's the effect on competition? Now I see there  
 19 is a sort of cross-over but they are not exactly the  
 20 same question.  
 21 MR JUSTICE BARLING: You say we have to take account of the  
 22 competitive realities for both these counterfactuals.  
 23 MR HOSKINS: Yes.  
 24 MR JUSTICE BARLING: Even in the objective necessity one.  
 25 You say it is not just seeing what in theory can work as

1 a four-party system, leaving aside what might happen in  
 2 the market, because of competition --  
 3 MR HOSKINS: I say that's what the case law says, the Court  
 4 of Justice.  
 5 MR JUSTICE BARLING: You say that.  
 6 MR HOSKINS: Yes.  
 7 MR JUSTICE BARLING: The only difference between the two  
 8 counterfactuals, then, is that the "might" versus the  
 9 "would".  
 10 MR HOSKINS: I think that is probably right, to be honest.  
 11 Certainly in the case law.  
 12 MR JUSTICE BARLING: We can be a bit more theoretical or  
 13 a bit more speculative with the ancillary restraint.  
 14 MR HOSKINS: The way I have tried to make sense of it, the  
 15 ancillary restraint is: would there be an alternative  
 16 that would allow the MasterCard payment scheme to  
 17 operate at zero or low MIF if Visa and Amex maintain  
 18 their actual levels? That's what I say the question is.  
 19 MR JUSTICE BARLING: Maintain their actual levels throughout  
 20 the period of the claim.  
 21 MR HOSKINS: Yes.  
 22 MR SMITH: I appreciate there are different tests, but in  
 23 a sense your case is that both at the restriction of  
 24 competition line and on the objective necessity line,  
 25 the outcome is the same answer to both questions,

1 namely --

2 MR HOSKINS: It is premised on us exiting the market.

3 MR SMITH: Yes, exactly. MasterCard is going to exit the

4 market and therefore, on the objective necessity test,

5 it is objectively necessary to have the MIF because

6 MasterCard therefore won't leave; and on the restriction

7 of competition point, again if MasterCard leaves, then

8 the restriction point resolves itself --

9 MR HOSKINS: There may be a difference, because for

10 objective necessity the test is impossibility. So that

11 is MasterCard leaving the market. For restriction of

12 competition, I might need less to establish not

13 a restriction of competition. Because if, for example,

14 in the restriction you reject the argument objective

15 necessity, because you say MasterCard would not have

16 been forced out of the market but it would have

17 remained, albeit at a very low level, say 3%, that could

18 still lead to a conclusion: no restriction of

19 competition. Because instead of having a situation of

20 competition with vibrant MasterCard, vibrant Amex,

21 vibrant Visa, you have MasterCard limping there, you can

22 immediately see where I would go with that submission.

23 So there is that distinction. Objective necessity

24 is more black and white.

25 MR SMITH: More black and white, yes. So there is more

57

1 wiggle room in the restriction of competition line.

2 MR HOSKINS: Yes.

3 MR SMITH: But the broad factual argument you're making is

4 the same --

5 MR HOSKINS: Substantial migration is the basis of both.

6 MR JUSTICE BARLING: I think we'd better give the transcript

7 writers a short break.

8 (12.00 pm)

9 (A short break)

10 (12.15 pm)

11 MR SMITH: Mr Hoskins, before you move on, just as

12 an adjunct to the debate we had before the break, you

13 will recall the discussion that the Tribunal had

14 yesterday with Mr Brealey about the nature of the

15 restriction of competition arising and whether the

16 restriction was because a level was being set; in other

17 words, what was pernicious was not so much how high the

18 MIF was, but the fact that there was a MIF at all at any

19 level.

20 MR HOSKINS: Yes.

21 MR SMITH: One point one might say of the no deduction rule

22 that we were debating before the break, is that if that

23 effectively sets a zero MIF. It would be helpful for

24 you to address us on that point, and if your position is

25 that that is also, therefore, a restriction on

58

1 competition, would the counterfactual rule in fact be

2 something like: you can't participate in the scheme as

3 a licensee of MasterCard or -- licensee of, but you

4 can't actually transact unless you have agreed

5 a bilateral rate?

6 MR HOSKINS: We have made the point at various stages that

7 the zero MIF is as restrictive of competition, and it is

8 my auction point, really. Competition law is not about

9 the level. Mr Brealey actually went -- that's where he

10 got to yesterday in his answers to you; it is whether

11 you join together to agree something, but then it

12 doesn't matter what the level is. A zero MIF would be

13 as much restriction of competition as whatever level.

14 So, yes.

15 So, yes, I agree, that's what Mr Coupe was saying to

16 me in the break actually, because this scenario we are

17 imagining now, which was issuer can't retain anything

18 absent a bilateral, is equivalent to a zero MIF or at

19 par clearing, as it is sometimes called.

20 Then if you discount that as a potential

21 counterfactual because it is itself a restriction,

22 therefore no good, if the rule was you can't join unless

23 you have a bilateral agreement, then -- it has not

24 really been focused so much on this case but certainly

25 it has come up before -- the problem is then, the

59

1 negative effect of competition in that scenario is it is

2 difficult for people to enter the market. New players

3 can't enter the market, because it is not in the

4 interest of people who are in the market as

5 issuers/acquirers to let competition in. So it is

6 a different -- it is not a hold-up problem, it is a keep

7 out problem. People won't do deals.

8 MR SMITH: Let's suppose I'm an issuing bank who signed up

9 with MasterCard, everything is fine, but I have to do

10 a deal with six acquirers, and five say "Fine, this is

11 the bilateral, we are happy with this price", the sixth

12 says, "I'm not agreeing to anything". As you say, there

13 would be an issue there.

14 MR HOSKINS: Yes.

15 MR SMITH: That, I think, was something the OFT discussed in

16 its decision. At paragraphs 528 and following, they

17 suggested exactly what you have said.

18 MR HOSKINS: Certainly in the evidence in the Commission.

19 I was involved to a certain extent in the Commission,

20 and actually in the OFT but my memory is not that good.

21 So I know this is an issue that has come up. It is

22 referred to, I think, in some of our submissions in this

23 case, some of our evidence in this case, but I would

24 need to dig out the references if you want the chapter

25 and verse on it. But that is a problem of deterring new

60



1 entry. If you are allowing purely on bilaterals is  
 2 ground that has been trodden before.  
 3 MR JUSTICE BARLING: It might be argued that although  
 4 I think you are probably right to say that the rule that  
 5 says you can't deduct, you have to pass-on 100% if you  
 6 don't agree, has the same effect as a zero MIF. It  
 7 probably isn't a zero MIF --  
 8 MR HOSKINS: It is sometimes called at par clearing.  
 9 MR JUSTICE BARLING: Yes. It is difficult to see how that's  
 10 a restriction to competition.  
 11 MR HOSKINS: It means the issuers can't charge.  
 12 MR JUSTICE BARLING: Unless they are in agreement.  
 13 MR HOSKINS: They'll all start by charging zero, absent  
 14 bilaterals. That's why it has the same effect as  
 15 a zero --  
 16 MR SMITH: Yes, but the focus is on the payment system.  
 17 What it is saying is that the cardholder's payment of  
 18 £25 will reach, unimpaired, the merchant, he will  
 19 receive £25, unless there is an agreement to which  
 20 everyone in the chain consents, so the deduction can be  
 21 made. Because we have been focusing on the scheme rules  
 22 but, of course, there are also going to be contracts  
 23 between the cardholder and the issuing bank, and the  
 24 merchant and the acquiring bank, and again one would  
 25 register a degree of surprise if there wasn't a rule

61

1 along the lines of the money moves to the payee absent  
 2 an agreed deduction.  
 3 MR HOSKINS: Yes, but I mean the crucial thing is what's the  
 4 contract or what are the rules that apply between the  
 5 issuing and the acquiring banks. Yes, I understand of  
 6 course there would be provisions in that chain, but  
 7 what's in the middle is what we are discussing.  
 8 MR SMITH: Indeed, but the middle will be drafted with  
 9 a view to what the ends expect.  
 10 MR HOSKINS: Yes, but what they expect is it depends --  
 11 I think it is tail wagging dog territory. Because at  
 12 the moment what the cardholder or merchant expects is  
 13 the result of what the issuers and the acquirers are  
 14 doing as between each other.  
 15 MR SMITH: Which is on the basis of an agreement, but it  
 16 happens to be a default.  
 17 MR HOSKINS: Yes. In terms of my approach, if one takes  
 18 this scenario as a possible scenario, which is issuer  
 19 can't deduct any payment absent a bilateral, let's take  
 20 that and see where it leads us, because it also then  
 21 raises the question that Mr Justice Barling put to me,  
 22 which is the caveat in all this is: would Visa and Amex  
 23 have maintained high levels throughout the period?  
 24 Actually, through your questioning there is two elements  
 25 to this and they face different ways.

62

1 The first way that comes out of the questioning is,  
 2 in this situation, if MasterCard had a rule, issuers  
 3 can't deduct absent a bilateral agreement -- and  
 4 remember, this is a counterfactual where Visa and Amex  
 5 have stayed high -- would acquirers agree to pay  
 6 a sufficiently high level to MasterCard because they  
 7 want to keep MasterCard in the market, because it suits  
 8 them to have MasterCard and Visa and Amex rather than  
 9 just Visa and Amex? That's the first way it is put.  
 10 The problem with that one is the evidence doesn't  
 11 support it. This is page 46 of our written closings.  
 12 You have got Mr von Hinten-Reed and he was asked this  
 13 question twice. The first time he said, "I prefer not  
 14 to assist you". That is the extract at 46 onto 47. On  
 15 the second occasion his evidence was that, in his  
 16 opinion, bilateral negotiations could not produce  
 17 an interchange fee in excess of 0.15% and in any event  
 18 he doubted whether the extra cost of negotiating  
 19 bilaterals would make that worthwhile at all. But of  
 20 course, the problem with that in this analysis is we are  
 21 in a world -- so he is assuming that if you had this  
 22 rule and bilaterals came in to fill the gap, they would  
 23 not be higher than 0.15, and in this world Visa and Amex  
 24 are still up here at their actual levels, so that  
 25 migration happens.

63

1 So Mr von Hinten-Reed's take on 'would acquirers  
 2 step in to keep MasterCard afloat?' doesn't work,  
 3 because he puts a ceiling of 0.15 in his approach.  
 4 MR SMITH: Yes, but that's more a point against the 0.15  
 5 level than bilaterals.  
 6 Q. I'm just dealing with his evidence and I will come on to  
 7 deal with --  
 8 MR SMITH: Indeed, but in terms of his evidence, he was  
 9 treating the 0.15, which is his computation of the MIT,  
 10 he was regarding the MIT-MIF as a constraint on  
 11 bilateral negotiations.  
 12 MR HOSKINS: Or was he saying -- I actually understood it  
 13 differently. I understood that he was saying that  
 14 because all the benefit merchants get from credit cards  
 15 is saving the costs that would arise if you were dealing  
 16 with cash instead.  
 17 You may be right. It was not entirely clear. But  
 18 I wasn't sure he was saying this is a sort of legal  
 19 point, but it makes more sense as an analysis if you  
 20 want to try to unpick what he was saying, if he says it  
 21 is 0.15 because that was all acquirers would be willing  
 22 to pay on behalf of merchants, because he thinks that's  
 23 all the benefit merchants get from accepting credit  
 24 cards.  
 25 MR SMITH: Except the MIT analysis is an analysis entirely

64

1 provoked by the Commission's investigation, and one that  
 2 Sainsbury's, for instance, had never done apart from at  
 3 the behest of the Commission.  
 4 MR HOSKINS: I'm not going to go too far into defending  
 5 Mr von Hinten-Reed, for obvious reasons, but that was  
 6 his position on acquirers, and it wouldn't work to keep  
 7 a MasterCard scheme afloat in this counterfactual, is  
 8 the short point.  
 9 MR SMITH: No.  
 10 MR HOSKINS: Everyone gets to --  
 11 MR SMITH: Clearly, if he is right and a bilateral is  
 12 constrained at an upper limit of 0.15, then your point,  
 13 that a Visa MIF of an order of magnitude higher than  
 14 that, well there's no difference between a bilaterally  
 15 agreed 0.15 and a default of zero.  
 16 MR HOSKINS: Yes. Then Dr Niels was asked about this and  
 17 his point really was that he said, as a matter of his  
 18 opinion, that he thinks because acquirers are competing  
 19 with each other, what they would actually do is they  
 20 would take the benefit of no deduction, rather than  
 21 unilaterally reaching a decision that it is better for  
 22 the common good to offer to pay more. We have set out  
 23 his evidence on this, but you get that in particular  
 24 from the extract at page 49 and the long extract at 50  
 25 to 51, where he was asked this question a number of

65

1 times. But you will see for example, on page 50, the  
 2 passages in bold really flag this up.  
 3 Dr Niels:  
 4 "Yes, so I think individually no acquirer would  
 5 really be so enlightened to say, well, we do want the  
 6 scheme to provide, especially if there are competing  
 7 schemes out there, so I'm going to be a bit more  
 8 generous and allow this particular issuer to charge more  
 9 than zero if I can actually get away with zero."  
 10 He basically repeated that point. That was very  
 11 much his position.  
 12 MR SMITH: Indeed, but on this particular question don't we  
 13 really have to go and put ourselves into the shoes of  
 14 Mr Coupe and Mr Rogers.  
 15 MR HOSKINS: That's where I'm coming. I'm just about to go  
 16 into those shoes. Absolutely.  
 17 The question, and I said there's two sides to it,  
 18 the first one is: would the acquirers step in and agree  
 19 bilaterals that would allow MasterCard to bring its MIF  
 20 back up? The other side is: well, if that's not going  
 21 to work, flip the other way, would merchants turn their  
 22 gaze not on MasterCard but to Visa and say, "If  
 23 MasterCard is down at this level, we are going to make  
 24 you come down to this level"? That's a commercial  
 25 pressure point.

66

1 In order to do that, of course, the merchants would  
 2 have to threaten something or do something to get  
 3 negotiating power, and one of the possibilities that was  
 4 put in the questions to Mr Brealey is that in this  
 5 counterfactual Visa might refuse to -- sorry --  
 6 retailers might refuse to accept Visa Credit cards  
 7 whilst continuing to accept Visa Debit cards, and say:  
 8 we are not going to accept Visa Credit cards unless and  
 9 until you bring your MIFs down because MasterCard are  
 10 low.  
 11 Our submission is the evidence does not support that  
 12 counterfactual, for a number of reasons.  
 13 First of all, go back to the Maestro experience,  
 14 because Maestro's MIFs were materially lower than Visa's  
 15 debit over a period of years, and up until 2007 when  
 16 MasterCard brought in its own debit card product, so  
 17 2000 to 2007. Merchants didn't negotiate lower  
 18 Visa Debit MIFs. They didn't turn round to Visa and  
 19 say: you must drop your rates because Maestro is at the  
 20 bottom. It didn't happen. That is just as a question  
 21 of fact. You have seen what happened to the market  
 22 shares, so it didn't happen.  
 23 Second point is, in my submission it is not  
 24 surprising that didn't happen because, to use the  
 25 language of the case law, it is unrealistic to suggest

67

1 that merchants would have ceased to accept Visa Credit  
 2 cards in this scenario or indeed that they could  
 3 credibly have threatened to stop accepting Visa Credit  
 4 cards.  
 5 The reason why that is is because accepting Visa  
 6 cards, Visa Credit cards, is simply far too beneficial  
 7 to merchants. Even at the higher level in this  
 8 scenario, the higher level of Visa MIF, it is still far  
 9 too beneficial to them to either stop accepting them or  
 10 to credibly threaten to stop accepting them.  
 11 Let me give you some figures to put flesh on that.  
 12 Can we go to B1, tab 12. Sainsbury's closing  
 13 submissions. Again, they were asked to provide various  
 14 figures in response to questions by the Tribunal. It is  
 15 appendix 2. B1, I2, appendix 2. It is memorandum from  
 16 CEG setting out Sainsbury's merchant services charges.  
 17 Page 464.  
 18 MR SMITH: Ours don't have bundle numbering. (Pause).  
 19 MR JUSTICE BARLING: First version of appendix 2.  
 20 MR HOSKINS: It is table 5 of that. It is internal page 6,  
 21 sorry.  
 22 MR JUSTICE BARLING: Thank you. Table 5 you want, MSC paid  
 23 on Visa Debits.  
 24 MR HOSKINS: That is the one, and Visa Credit card  
 25 transactions.

68

1 MR JUSTICE BARLING: Internal page 4 in that case.  
 2 MR HOSKINS: I see you have different numbering.  
 3 MR JUSTICE BARLING: There is two versions of this.  
 4 MR HOSKINS: I see. The table I want is "MSC paid on Visa  
 5 Credit card transactions acquired by Barclays GBP".  
 6 PROFESSOR JOHN BEATH: That is page 10, is it?  
 7 MR JUSTICE BARLING: Yes, that is table 11, I think.  
 8 Page 8.  
 9 MR SMITH: We are looking at the older version.  
 10 MR JUSTICE BARLING: Table 5. Tab B.  
 11 MR HOSKINS: It should be Visa Credit card transactions  
 12 acquired by Barclays.  
 13 MR JUSTICE BARLING: Thank you, yes. Sorry about that.  
 14 MR HOSKINS: Remember that what we are positing here is  
 15 a question which is: would a company such as Sainsbury's  
 16 have refused to stop accepting Visa Credit cards? We  
 17 say obviously not. Look at the sales figures. It is  
 18 the second last column. I am not sure if this is  
 19 confidential or not. It is confidential.  
 20 MR JUSTICE BARLING: We can read them anyway.  
 21 MR HOSKINS: Exactly. You get the annual sales and then you  
 22 get the total, over the claim period, at the bottom in  
 23 bold.  
 24 These are just sales on Visa Credit cards. I'm not  
 25 giving away any confidentiality to say they are very,

69

1 very high.  
 2 Remember, when looking at this, trying to put this  
 3 in some sort of context, accepting Visa Credit cards  
 4 gave Sainsbury's higher profits than accepting  
 5 Visa Debit cards. I will show you that again, because  
 6 it is something I have shown you. E9.1, tab 12 at  
 7 page 560. Again, this may well be confidential so  
 8 I won't read it out.  
 9 There is a little table at the bottom. The table  
 10 below details approximate weekly volumes in values by  
 11 the main card types. You will see the ATV, the average  
 12 transaction value, on a Visa Credit card and  
 13 a Visa Debit card and you will see the difference.  
 14 MR JUSTICE BARLING: You are comparing the average  
 15 transaction value on the MasterCard?  
 16 MR HOSKINS: No, I'm comparing Visa Credit with Visa Debit,  
 17 because we are imagining a situation where they say: we  
 18 are not accepting credit any more but we will carry on  
 19 with debit", and hopefully it is obvious, you will see  
 20 one of the reasons why we say that wouldn't be something  
 21 commercially they would do, because if the transactions  
 22 were going to switch to debit rather than credit, you  
 23 will see the impact it is going to have.  
 24 MR SMITH: Debit is far larger than the credit, but the  
 25 credit is still significant.

70

1 MR HOSKINS: It is the average transaction value I'm looking  
 2 at.  
 3 MR JUSTICE BARLING: The credit is --  
 4 MR HOSKINS: You're right, in absolute volumes debit cards  
 5 are used more, but you will see what the average  
 6 transaction value is on credit, people buy more on  
 7 credit cards per each transaction. There are more  
 8 transactions on debit, but each transaction on average  
 9 is worth less. When you are looking at the volume in  
 10 value, these are weekly figures.  
 11 MR SMITH: Maestro too is quite high.  
 12 MR HOSKINS: That is correct. That is the point, I made  
 13 this point in cross-examination. I will come back to  
 14 this, because it is one of the reasons why I say  
 15 merchants benefit from accepting credit cards over debit  
 16 cards. People spend more on credit cards. Sainsbury's  
 17 figures show that.  
 18 Again, this is another reason why we say is it  
 19 realistic that someone like Sainsbury's would say,  
 20 "Actually, we are just going to stop accepting your  
 21 cards"? The answer is no. That is the second reason,  
 22 because they make more on accepting credit cards than  
 23 they do on accepting debit cards.  
 24 MR JUSTICE BARLING: I suppose that might be a dynamic if  
 25 you had a -- you are postulating that over a period of

71

1 about seven or eight years this kind of differential  
 2 would be maintained, and you say, well, the merchants  
 3 couldn't credibly even threaten to do something along  
 4 those lines. But I suppose that this is a differential  
 5 that would apply across the board to all merchants and  
 6 so all merchants would be in the same position of having  
 7 to start different --  
 8 MR HOSKINS: That is my next point.  
 9 MR JUSTICE BARLING: Yes, and --  
 10 MR HOSKINS: That is a point in my favour. Can I explain?  
 11 MR JUSTICE BARLING: It might be. I'm just thinking -- you  
 12 say that wouldn't give them any more clout, though.  
 13 MR HOSKINS: What you have to remember is that when you are  
 14 looking at the commercial decision of a retailer to stop  
 15 accepting Visa Credit cards, somebody has to do it  
 16 first. Imagine you are Sainsbury's and you are saying,  
 17 "Okay, we are making a lot of money, even with a Visa  
 18 MIF at this level. Look at the level of sales, look at  
 19 the average transaction value, higher on the credit  
 20 card. Look at MasterCard. We can get them down a bit,  
 21 we will stop accepting them." What did Tesco and Asda  
 22 do?  
 23 MR JUSTICE BARLING: To do it, yes. Of course you would be  
 24 sticking your neck out, but you were saying they  
 25 couldn't make a credible threat. And what about the

72

1 British Retail Consortium? Are you suggesting that  
 2 there couldn't be any credible rumblings that would  
 3 actually have some impact on Visa?  
 4 MR HOSKINS: It didn't happen in Maestro. It didn't happen.  
 5 It's the UK. It's a large differential. Acquirers,  
 6 merchants, regulators did nothing, put no pressure on  
 7 Visa to drop its MIF, we saw it actually raised its MIF  
 8 during the relevant period, and MasterCard all but  
 9 exited the market, and it just clung on by its nails  
 10 because it introduced a new product in 2007.  
 11 That's why I was so aggressive -- apologies --  
 12 earlier. I was talking about a counterfactual. It has  
 13 to be based on the evidence; and the evidence here is  
 14 Maestro on that. Then it is bolstered by the evidence  
 15 on the amount of money that accepting Visa Credit cards  
 16 is worth to these retailers.  
 17 I think you are ad idem in the sense that nobody  
 18 would take the first step to do it because it would be  
 19 crazy, because Asda and Tesco are probably not going to  
 20 follow, they are just going to say to all the people  
 21 with Visa Credit cards, "Come into our stores". It is  
 22 the same as the expert economic evidence on acquirers,  
 23 would they do something individually but thinking  
 24 collectively? No, they wouldn't. You see how  
 25 cut-throat the supermarket business is. You see how low

73

1 the margins are. If someone jumped first, the rest  
 2 would welcome their customers with open arms, because  
 3 the MIF is actually such a small part of what they do  
 4 that they would much rather have the customers.  
 5 MR SMITH: I don't want to interrupt your flow but have you  
 6 concluded your submissions on what Mr Coupe and  
 7 Mr Rogers would do in this counterfactual world?  
 8 MR HOSKINS: I have one other point to go to, which is  
 9 Mr von Hinten-Reed -- part of the trouble is because --  
 10 it is not a criticism of anyone, because the case has  
 11 moved on while we have been doing it, but this point  
 12 wasn't really part of the original case of any of the  
 13 parties, it was not in the expert reports. So one of  
 14 the things that has happened is Mr Coupe wasn't asked  
 15 about this, because it wasn't something that was being  
 16 raised by Sainsbury's. We don't know. But  
 17 Mr von Hinten-Reed was asked by the Tribunal about this.  
 18 It is quite interesting to see how far he was  
 19 prepared to go. It is transcript Day 12, page 57,  
 20 line 13 to page 58, line -- it goes on to really 24.  
 21 There is a question by Mr Justice Barling:  
 22 "As I understand it you can't imagine Visa staying  
 23 up there --  
 24 "Answer: Exactly. I will explain that and  
 25 hopefully in a cogent and quick way.

74

1 "So we have something which -- a piece of  
 2 information, which I hadn't realised but actually is  
 3 quite crucial, that issuers are forward looking. No  
 4 issuer really wants to change cards unless it can see  
 5 the situation being permanent. And the other thing  
 6 I take from the evidence in court is that things take  
 7 time. It is not instantaneous."  
 8 He responds with a different point, which is his  
 9 point that people wouldn't have switched if they thought  
 10 that Visa was going to come down, which I dealt with as  
 11 a separate point. He goes on to say:  
 12 "So what's the response of a retailer or a group of  
 13 retailers, knowing that, in effect, if you present this  
 14 argument of Visa being high and MasterCard being low, is  
 15 that all the issuers will have an incentive to run to  
 16 Visa.  
 17 "Well, their response is roughly -- and you have  
 18 heard it all before -- that if the MSC is high and all  
 19 you are doing is switching from -- you have been waiting  
 20 for this low MIF for ever more and then you are told  
 21 that basically you have to go to Visa because your  
 22 issuers have moved, you are not going to be very happy  
 23 if you are a retailer.  
 24 "The way in which I would play it would be simple.  
 25 You know it is going it take time to switch, you know

75

1 you have a small amount of time to do it and to  
 2 complain. It doesn't necessarily mean that you  
 3 surcharge, or you don't accept Visa cards, but you can  
 4 certainly put something in the Guardian or The Times or  
 5 The Telegraph to say: if you do not reduce your MIF, we  
 6 will do exactly that."  
 7 I mean, it is pretty unclear what's being driven at,  
 8 but what I take from that is he says people wouldn't  
 9 surcharge, people wouldn't stop accepting cards. He  
 10 seems to be suggesting that somehow you flag your  
 11 intentions to everyone else. But again, if Sainsbury's  
 12 puts an advert in the newspaper, Tesco and Asda think:  
 13 fantastic, the sooner you do it the better.  
 14 If you talk about something being organised through  
 15 the British Retail Consortium or whatever, you have my  
 16 point, it didn't happen in Maestro and that was the same  
 17 scenario.  
 18 I have now finished my submissions on it, subject to  
 19 the question you are about to ask me.  
 20 MR SMITH: I think it is common ground that Mr Perez's  
 21 description of how issuers would evaluate a move to  
 22 a new and different card scheme was quite compelling.  
 23 They would take the longer term view and would balance  
 24 the costs of shifting a scheme against the differential  
 25 in revenues resulting from different MIFs. So shifts

76

1 don't occur instantaneously, unsurprisingly, issuers  
 2 take a considered view.  
 3 MR HOSKINS: Yes.  
 4 MR SMITH: So, any change will be not necessarily gradual,  
 5 but it will be not instantaneous.  
 6 MR HOSKINS: Yes.  
 7 MR SMITH: Let's assume for the sake of argument that you  
 8 are right and in our counterfactual world MasterCard's  
 9 ability to set a default is eliminated but no one else's  
 10 is and they carry on as before, both Amex and Visa. So  
 11 their MIFs or rates are materially higher, I put it no  
 12 more than that, than that of MasterCard.  
 13 Let's put ourselves in the position of Mr Coupe and  
 14 Mr Rogers and try to think how Sainsbury's would analyse  
 15 this. And again, I anticipate that it is common ground  
 16 that, first of all, Sainsbury's is a significant player  
 17 in the merchant markets, someone acquirers will listen  
 18 to, card issuers and indeed schemes will listen to,  
 19 because they are a very, very big operator. That would  
 20 be uncontroversial, I take it?  
 21 MR HOSKINS: I'm only stopping nodding because I want to see  
 22 where this is going before --  
 23 MR SMITH: I thought you might be, Mr Hoskins.  
 24 MR HOSKINS: I will shout if I disagree.  
 25 MR SMITH: Secondly, this was clear from the evidence,

77

1 Mr Coupe and Mr Rogers are both pretty sophisticated  
 2 people, they will take not necessarily an immediate  
 3 short-term view but they will take a medium to long-term  
 4 view, they will take a strategic look as well as  
 5 a short-term look.  
 6 With all those facts in the pot, what are they going  
 7 to do when they see MasterCard at zero and Visa at  
 8 rather more than zero? The short-term view would be to  
 9 say, "I'm going to pressure my acquiring banks to keep  
 10 the merchant service charge as absolutely low as  
 11 possible and eliminate a significant portion of my  
 12 credit card or debit card base. I will still have to  
 13 pay a high level to Visa --  
 14 MR HOSKINS: Sorry, I did not understand that last bit.  
 15 MR SMITH: Sorry. By not agreeing a bilateral, by sticking  
 16 to the default of zero, which is what Dr Niels  
 17 suggested, you achieve a saving on a significant portion  
 18 of your card expenses, the MasterCard side. But the  
 19 Visa side, of course, stays at the level as before.  
 20 That's what we have postulated.  
 21 MR HOSKINS: Yes.  
 22 MR SMITH: So in the short-term you can achieve a saving on  
 23 a significant portion of your credit card transactions  
 24 portfolio. But Mr Coupe and Mr Rogers, would they be  
 25 unaware of the likely move away from MasterCard in the

78

1 medium term?  
 2 MR HOSKINS: Sir, I'm going to interrupt here because you  
 3 are asking me to give evidence, because the closest we  
 4 have got to this in terms of the evidence we have heard  
 5 is the economists giving the evidence on would acquirers  
 6 act in that sort of -- individually act in that sort of  
 7 collective way? We are getting to the same place with  
 8 this chain of thought, which is would retailers, seeing  
 9 the effect of taking the zero MIF for a short period  
 10 would be to drive everyone from MasterCard to Visa,  
 11 would they have individually acted in the collective  
 12 interest? We don't have any evidence that tells us  
 13 that, save for what the economists tell us when you ask  
 14 them a question about acquirers: would they have acted  
 15 in their own interest but collectively? Answer, no.  
 16 And you have Maestro. People didn't do it. That's not  
 17 what people at Sainsbury's did during the Maestro  
 18 period. They stood back and watched Maestro tumble out  
 19 of the market.  
 20 That's why -- you're probably sitting there "Typical  
 21 advocate", but it is evidential and it wouldn't be  
 22 appropriate for me, it is not my role to start saying,  
 23 "Yes, Mr Coupe might have thought this or that". All  
 24 I can do is point you to what the evidence is, and in  
 25 our submission the evidence actually is that it is

79

1 unlikely they would have done that.  
 2 MR SMITH: Right. Let's take a more hypothetical  
 3 counterfactual, then, let's forget Mr Coupe and  
 4 Mr Rogers and let's just take a very large merchant.  
 5 MR HOSKINS: My response is the same.  
 6 MR SMITH: Is it, though? Are we to ignore the effect of  
 7 the point you are making with great force, that  
 8 MasterCard are going to be driven out of the market,  
 9 ignore that fact as having no impact on large merchants,  
 10 even though, if they thought about it, they must know --  
 11 MR HOSKINS: Maestro. They didn't do what you are imagining  
 12 they might do now. They didn't do that. It didn't  
 13 happen. So you have the factual evidence of Maestro and  
 14 you have got the economists saying that people in  
 15 a competitive environment, seeing that they have  
 16 an advantage to take, will actually act in their  
 17 individual interests and will not act individually in  
 18 their collective interests, and that applies the same to  
 19 merchants.  
 20 I will come back to Maestro. It is the same. It  
 21 did not happen. People stood by and watched and allowed  
 22 Maestro to tumble out of the market. Anything else is  
 23 speculation. And that's not the basis -- the  
 24 counterfactual has to be decided realistically, actual  
 25 context, on the basis of the evidence before the

80

1 Tribunal.  
 2 You asked me the question, and my answer is: not  
 3 sustained by the evidence. If I'm being blunt and too  
 4 aggressive again, apologies, but I'm not sure you are  
 5 allowed to or should -- you can do what you want, but  
 6 I'm not sure you should be deciding the case on the  
 7 basis of theoretical --  
 8 MR JUSTICE BARLING: We are. We have to. Because we are  
 9 being asked to speculate not just on one but on three  
 10 different counterfactuals, which does involves  
 11 speculation and can, at times, involve taking judicial  
 12 notice of things. I think what Mr Smith is asking you  
 13 is to take -- maybe whether it is appropriate to take  
 14 judicial -- we obviously have the Maestro evidence but,  
 15 as you know, Sainsbury's case is that that's totally  
 16 different, it is another --  
 17 MR HOSKINS: But not on this point, with respect. That's  
 18 a distinction that doesn't matter in this context.  
 19 MR JUSTICE BARLING: Why shouldn't you give us your best  
 20 shot on whether we should take judicial notice that  
 21 commercial people act rationally, and in a hypothetical  
 22 situation, which didn't happen, so we have no direct  
 23 evidence as to what happened or would happen, we just  
 24 have to speculate --  
 25 MR HOSKINS: But you do have evidence in this case, sir.

81

1 You have the evidence of Maestro --  
 2 MR JUSTICE BARLING: We don't have any -- because we didn't  
 3 have a situation with a zero MasterCard MIF on a credit  
 4 card and a Visa remaining indefinitely at a high level.  
 5 MR HOSKINS: You did, sir. Actually the position in Maestro  
 6 is less extreme than the counterfactual we are  
 7 considering.  
 8 MR JUSTICE BARLING: Because it's--  
 9 MR HOSKINS: Because the differential between the Maestro  
 10 MIF and the Visa Debit MIF was less than we are  
 11 currently considering in the counterfactual, by several  
 12 orders of magnitude. That's the paragraph of our  
 13 skeleton I took you to at E.  
 14 So you did absolutely have that situation of  
 15 a differential in the MIFs. But it is greater in the  
 16 counterfactual we are considering, so any effect would  
 17 be greater. But nobody stepped in, watching what was  
 18 happening to Maestro. You have seen Sainsbury's figures  
 19 and others will have the same. You have seen every week  
 20 how many transactions are being done on Maestro, how  
 21 many are being done on Visa Debit. I think we saw some  
 22 of the figures actually when we were going through it.  
 23 They would see every week Maestro plummeting. But they  
 24 didn't go into a star chamber and say, "Look what's  
 25 happening, this is bad for us in the long term because

82

1 we would actually would prefer to have a vibrant Maestro  
 2 and a vibrant Visa Debit. They just let it happen.  
 3 That's the evidence.  
 4 MR SMITH: Well, up to a point. I mean, in a sense, if we  
 5 have to look at the facts, the fact is that the level of  
 6 Maestro's transactions which Sainsbury engaged in  
 7 carried very high through to 2015. So in a sense the  
 8 perception that Sainsbury's might have had of a Maestro  
 9 collapse would be --  
 10 MR HOSKINS: But we are using Sainsbury's as an example.  
 11 This has to be all retailers, because we are talking  
 12 about a situation -- remember, we are talking about  
 13 a situation in which there is a differential in the  
 14 MIFs, in a scenario where we are low, everyone else  
 15 high, and the evidence is -- and I don't think this is  
 16 contested -- left unchecked, we fall out the market. So  
 17 the question is will someone -- or, sorry, will some  
 18 group step in to avoid that happening? Would acquirers  
 19 step in to stop that happening? Would retailers step  
 20 in? So when we talk about Sainsbury's, we use that  
 21 because we have evidence on them. But the truth is,  
 22 would a sufficient number of retailers put pressure on  
 23 the acquirers to bring it down? We don't know. We  
 24 don't have the evidence save for Maestro, which didn't  
 25 happen.

83

1 MR SMITH: I mean, it is a question really of joining the  
 2 dots, isn't it? You are saying that if the MIF  
 3 differential continues unchecked, this rival scheme to  
 4 Visa, the only rival scheme to Visa, will exit the  
 5 market, with the result that all of the merchants will  
 6 end up paying those MIFs that Visa chooses to set, with  
 7 no competitive check whatsoever. That was the reason we  
 8 put to Dr Niels the question about supply chains and  
 9 what a sophisticated entity in the market would do with  
 10 a view to protecting its supply chains.  
 11 MR HOSKINS: That's why I asked him whether that supply  
 12 chain analysis would apply equally to payment schemes,  
 13 and he said no. Because a supply chain benefits the  
 14 particular retailer who is funding it. His example,  
 15 I think, was a bottling plant or something --  
 16 MR SMITH: It was Tesco's bottling plant.  
 17 MR HOSKINS: But that's someone investing in someone staying  
 18 in the market directly for their own benefit. Whereas  
 19 the example we are considering here, where it goes on  
 20 the evidence, is people not doing something that  
 21 immediately benefits them, but something that benefits  
 22 the greater good. So you can't just leap, in our  
 23 submission, from that bottling plant example, immediate  
 24 benefit to Tesco's, to the scenario we are  
 25 contemplating. Indeed, Dr Niels in re-examination was

84

1 not prepared to make that leap; he thought they were  
2 different.  
3 The Maestro, with respect, it is not right, I don't  
4 think, that Sainsbury's stayed steady. It is table 8.  
5 So it is B1 of appendix 2, table 8, which is internal  
6 page 10 of the original appendix 2. We looked at  
7 original table 5 and this is original table 8:  
8 "MSC paid on Maestro debit card transactions."  
9 The oddity is it starts at 2015/16 and as you go  
10 down a page you go back in time. It is page 468 of the  
11 bundle, internal page 10. (Pause).  
12 MR SMITH: Yes.  
13 MR HOSKINS: From 07/08 there is a spike that is not  
14 consistent with the general shape of the graph, but then  
15 a quick plummeting thereafter.  
16 MR SMITH: No, but you are missing table 11, because  
17 Sainsbury's switched acquiring bank.  
18 MR HOSKINS: Yes, but that's -- I see. I'm sorry.  
19 MR SMITH: You see? Table 8 is Maestro acquisitions through  
20 HSBC and table 11 is Maestro transactions through  
21 WorldPay.  
22 MR HOSKINS: Sorry, the figures, for example, if one takes  
23 2009/2010 and compares the figures on table 11, they are  
24 still substantially less by an order of magnitude, are  
25 they not?

85

1 MR SMITH: Well, it is --  
2 MR HOSKINS: We are looking at billions and millions.  
3 MR SMITH: Yes, well if you -- one would have to check what  
4 was included in the financial year 2015/2016, but  
5 2014/2015 is 111 million, isn't it?  
6 MR HOSKINS: Yes, but on table 8 the figures in 2009/2010  
7 are in the magnitude of billions.  
8 MR SMITH: I see.  
9 MR HOSKINS: So there is a substantial difference, by  
10 a magnitude of times ten. Sorry, that is a point of  
11 detail.  
12 I'm not sure I can take it much further. I can  
13 answer questions.  
14 MR JUSTICE BARLING: Well, you just refused to.  
15 MR HOSKINS: Sorry?  
16 MR JUSTICE BARLING: You just said you won't.  
17 MR HOSKINS: That's a bit harsh.  
18 MR JUSTICE BARLING: No, it's not, it's true.  
19 MR HOSKINS: Ask me any question.  
20 MR JUSTICE BARLING: You carry on.  
21 MR SMITH: Going back to our hypothetical large merchant,  
22 your position is that even though that merchant might be  
23 aware of your point about a MasterCard exit from the  
24 market, such that Visa reigns supreme, that merchant  
25 will not say to its acquiring bank, "We are very

86

1 troubled by this idea of zero because we are getting  
2 value from this transaction, we want to pay a fair price  
3 but no more than a fair price, because we are very  
4 troubled about this idea of issuing banks shifting away  
5 to Visa and we don't want that to happen, we want to  
6 protect our supply chain". And they won't do it, for  
7 the sole reason that it benefits other players in the  
8 market.  
9 MR HOSKINS: No, it is not because they want to harm other  
10 people. The evidence -- as I say, I don't -- the point  
11 you just put to me, I say, is not supported by the  
12 evidence. See Maestro. See the expert economists when  
13 you asked them a similar point about acquirers.  
14 The point is not that a competitor will not do  
15 something that benefits both itself and its competitors.  
16 The point is that in a competitive market, nobody will  
17 actually take the step which will be detrimental to them  
18 in the short to medium term for the greater good.  
19 My main point is the evidence and my main point is  
20 Maestro and my main point is the expert economists. So  
21 it is economics and effects.  
22 MR JUSTICE BARLING: Shall we give you a rest then?  
23 MR HOSKINS: I'm fine, but we should give everyone else  
24 a rest. Thank you.  
25 MR JUSTICE BARLING: We will see you at 2 o'clock.

87

1 (1.01 pm)  
2 (The short adjournment)  
3 (2.00 pm)  
4 MR HOSKINS: Restriction of competition. I can take this  
5 relatively quickly, because a lot of the discussion we  
6 have been having cuts across this as well. It is  
7 page 56 of the closing submissions.  
8 You remember from O2 that what the Tribunal is  
9 required to consider here is what competition was like  
10 in the actual, and compare it with what competition  
11 would be like in the counterfactual.  
12 Again, this is in the context of a counterfactual,  
13 where MasterCard is low and we say Visa and Amex are  
14 high, subject to the discussion we had before lunch, but  
15 I will tie that into the analysis as I go through.  
16 You are aware that our primary case is we would be  
17 driven from the market or there or thereabouts would  
18 still be substantially reduced, and that's the basis on  
19 which we approach it.  
20 We look first of all at the issuing market. In the  
21 counterfactual that Sainsbury's were running, but in  
22 a counterfactual where we are low and everyone else  
23 high, the experts agree that we would be driven out of  
24 the market, so what's the competition in the issuing  
25 market? In the actual there's Visa, Amex, MasterCard.

88

1 In the counterfactual there is Visa and Amex, no  
 2 MasterCard, or a severely wounded MasterCard.  
 3 Therefore, less competition.  
 4 If you take a scenario where you have at par  
 5 clearing, subject to bilaterals, which is issuer  
 6 receives nothing absent bilateral, you have still got,  
 7 we say, a zero MIF, because that is what at par clearing  
 8 is; it is default rule of zero but it's still a common  
 9 floor for merchants, and indeed for issuers as well.  
 10 So we would say on the issuing market, probably  
 11 worse -- at least worse in the counterfactual but  
 12 certainly no better.  
 13 Just to take account of the scenario: what if  
 14 merchants were to put pressure on Visa to bring their  
 15 rates down? Well, what we have got -- you will  
 16 understand my submission, but let's take the Amex  
 17 regulation to see what would happen. We know what  
 18 happened there was Amex was in a very weak position  
 19 because of the regulation I showed you; if its market  
 20 share went up, it was bang into the regulation. In the  
 21 counterfactual we are imagining, there is no regulation,  
 22 so that is a scenario we have got of merchants going to  
 23 Visa, effectively, and saying, "We want to pay less".  
 24 Visa would be in a stronger position than Amex was in  
 25 2015 because there is no regulation.

89

1 In addition, you must remember that Amex is a far  
 2 less attractive proposition to most retailers than Visa.  
 3 It is accepted in less places. It is used for  
 4 groceries, I don't say it is never used for groceries.  
 5 I pay for groceries with Amex. But it's a less  
 6 attractive proposition, partly because the retailer pays  
 7 more to accept Amex.  
 8 But look what happened in that scenario? Did Amex  
 9 come down to 0.3 in the negotiations with Sainsbury's?  
 10 No, it didn't. The actual figure is confidential, but  
 11 it's still a very substantial difference.  
 12 If you are applying your add on to the  
 13 counterfactual, if you like, of merchants putting  
 14 pressure on Visa, you then have to ask the question:  
 15 what effect would that have on Visa? How far would it  
 16 come down? Would it come down to the same level as  
 17 MasterCard? Our submission is probably not, because  
 18 look what happened in the Amex scenario, where Amex was  
 19 in a far weaker position than Visa.  
 20 Would there still be substantial switching? Our  
 21 submission is yes. So you still get, we say, this  
 22 analysis on the issuing market of stronger Visa,  
 23 stronger Amex and sufficiently weaker MasterCard.  
 24 In the acquiring market we say that if you compare  
 25 the actual with the counterfactual, the level of

90

1 competition in the acquiring market is likely to be  
 2 worse, and certainly no better than, under the actual  
 3 scenario.  
 4 One of the points that was floated by Mr Smith in  
 5 questions, it seemed to us, was a point you can take  
 6 here, which is: under the counterfactual we are  
 7 imagining, the number of MasterCard credit cards would  
 8 fall, leading to less interest in acquiring in respect  
 9 of MasterCard credit cards, and thus there would be  
 10 a reduction of competition in the acquiring market.  
 11 There's quite a lot to unpack there. It is  
 12 paragraph 174 of our closing submission.  
 13 So, less MasterCard cards in the market, there's  
 14 less interest in acquiring them, therefore the intensity  
 15 of competition in the acquiring market falls.  
 16 But certainly the other point is that between the  
 17 actual and the counterfactual, competition on the  
 18 acquiring market would certainly have been no better  
 19 because, as both experts stated, the existence in the  
 20 level of the MIF does -- sorry, the level of the MIF  
 21 does not affect competition between acquirers. So  
 22 whether the MIF is here or the MIF is here, acquirers  
 23 compete on the margin.  
 24 That was the evidence of Mr von Hinten-Reed and  
 25 Dr Niels; we have set that out at paragraph 175. So

91

1 wherever one has the defect, whether it be zero or  
 2 whether it be the actual, the level of competition  
 3 between acquirers is the same, as they compete on the  
 4 margin above that.  
 5 In a nutshell, really, that's why we say, if you  
 6 find against us on objective necessity, then it is not  
 7 a restriction of competition within 101(1) when you  
 8 compare the actual with the counterfactual.  
 9 I think I can go to the difficult bit of the case  
 10 now, which is exemption and exemptible level. I say  
 11 difficult; it is more complicated, there is probably  
 12 even more moving parts in this bit.  
 13 Can I start again by just looking at our main points  
 14 on this -- you get that from page 9 of our written  
 15 closings -- just to set out the framework, and I will  
 16 fill in the gaps.  
 17 Can I just ask you to -- I know you have seen it --  
 18 refresh your memories on 9 to 11? Then you will see the  
 19 framework of the submissions I want to make.  
 20 (Pause).  
 21 Can I start with the question that you raised with  
 22 Mr Brealey, or Mr Brealey raised with you when you asked  
 23 him questions about it, which is: how does the Tribunal  
 24 approach the question of whether the actual MIF  
 25 qualified for exemption, and how do you approach the

92



1 question of what the exemptible MIF would have been in  
 2 order to determine what loss, if any, Sainsbury's had  
 3 suffered?  
 4 In deciding whether the actual MIF fulfilled the  
 5 criteria for exemption, the burden of proof is on  
 6 MasterCard, and it is for MasterCard to show that the  
 7 four conditions of Article 101(3) are satisfied.  
 8 If the Tribunal finds that the actual MIF should not  
 9 benefit from an exemption, Sainsbury's doesn't  
 10 immediately have a right to claim damages for any loss  
 11 that it can show it has suffered. There's no  
 12 presumption of loss because a MIF is at a level which is  
 13 above the exemptible level. The claimant still has to  
 14 prove loss. Because the tortious principle, and it is  
 15 perfectly compatible with EU law, is claimant is  
 16 entitled to be put in the position as if the wrong had  
 17 not occurred. So if, for example, there had been 100%  
 18 pass-through, then you don't suddenly say you have got  
 19 a right to claim the whole overcharge, you have actually  
 20 got to go on and see what loss has actually been  
 21 suffered. So there isn't, as Mr Brealey appeared to  
 22 suggest at certain stages, as soon as you show 101(1) is  
 23 satisfied, 101(3) is not, bang, there's your damages.  
 24 That's simply not correct as a matter of domestic or EU  
 25 law.

93

1 There are a number of points about the task of  
 2 damages assessment that the Tribunal would have to  
 3 undertake if we get to this stage.  
 4 First of all, for this purpose, when you are trying  
 5 to identify the exemptible level of the MIF, having  
 6 decided that the actual MIF is not to be exempted, then  
 7 it is quite clear that what you are seeking to identify  
 8 is what the lawful level of MIF would have been.  
 9 That is nothing to do with granting an actual  
 10 exemption, because let's assume you come up with  
 11 a lawful level of MIF at 0.4. You do not then grant  
 12 an exemption at 0.4, because that MIF never existed.  
 13 The reason why I say that -- what you are not doing as  
 14 part of this exercise is you are not saying, "Shall we  
 15 grant an exemption at a certain level?" What you are  
 16 doing is saying, "What's the exemptible level of the  
 17 MIF?" in order to determine whether Sainsbury's have  
 18 suffered a loss, and how much.  
 19 Secondly, the evidence of Mr von Hinten-Reed and  
 20 Dr Niels in this case is that there is an exemptible  
 21 level of a MIF.  
 22 The actual question that's before you is, you have  
 23 got Mr von Hinten-Reed saying here and you have got  
 24 Dr Niels saying here, you may say it is somewhere in the  
 25 middle etc, but both experts say there is an exemptible

94

1 level, so it is difficult to see again how you  
 2 immediately, as soon as -- if we get to that stage, the  
 3 Tribunal finds there is a breach of 101(1), the actual  
 4 level doesn't satisfy 101(3), there is an automatic  
 5 right to damages, because the way the case has been  
 6 brought by the claimant is there is an exemptible level  
 7 of MIF. So you are looking for that counterfactual.  
 8 What would the exemptible level have been?  
 9 We say this is exactly the same sort of exercise  
 10 that you have in cartel damages cases, because if it is  
 11 established that there was a cartel, the question then  
 12 is: well, what would the price have been absent the  
 13 cartel?  
 14 There's no automatic assumption that the whole of  
 15 the price paid during the cartel period is itself  
 16 recoverable. In order to establish loss, the claimant  
 17 has to show what the overcharge is. They can't simply  
 18 say: I have paid a price and the price is unlawful.  
 19 So we say that at this stage, when you are looking  
 20 at what the exemptible level of the MIF would have been,  
 21 that's part and parcel of the task of establishing  
 22 whether there has actually been any overcharge as  
 23 a result of unlawful conduct. It is part and parcel of  
 24 the task of damages assessment. It is nothing to do  
 25 with granting an exemption. That simply doesn't enter

95

1 into the framework at this stage.  
 2 That's why the broad axe approach is applicable.  
 3 Just indeed as it would be in seeking to establish the  
 4 non-cartelised price in a cartel case. Equally, that's  
 5 when Mr Justice Lewison was talking about the broad axe  
 6 in Devenish, it was in a cartel case. It is the same.  
 7 In our submission, loss of a chance case law doesn't  
 8 help us, for this reason. The sort of classic now -- I  
 9 know the beauty parade, but the classic, practical way  
 10 it comes up now is, for example, where a negligent  
 11 solicitor misses a limitation period and the client of  
 12 the solicitor says, "Well, I have lost a chance because  
 13 I could have brought a suit within time", and that's  
 14 where you get into loss of chance, they lost a chance to  
 15 bring a suit that might have been successful.  
 16 But here, in our submission, the MIF didn't cause  
 17 Sainsbury's to lose a chance to enjoy a financial  
 18 benefit. Sainsbury's either did or did not suffer  
 19 a loss of profits due to the existence of a MIF  
 20 overcharge. That's why we say it is a standard damages  
 21 assessment exercise rather than loss of a chance. So  
 22 the question for you is: what would the exemptible level  
 23 of the MIF have been during the claim period?  
 24 MR JUSTICE BARLING: I think that is accepted, isn't it?  
 25 Whether or not there could be other arguments about it,

96

1 I think it is in fact common ground at that stage that  
 2 their measure of loss depends on that exemptible level.  
 3 MR HOSKINS: There was a lot off to-ing and fro-ing with  
 4 Mr Brealey yesterday, so I'm nervous to put words into  
 5 his mouth. He did seem at the end to get to a stage  
 6 where he accepted that as a principle.  
 7 MR SMITH: I think it may be my fault for raising  
 8 Chaplin v Hicks as the example which immediately leads,  
 9 as you say quite rightly, into loss of chance.  
 10 But the distinction I was attempting to draw,  
 11 clearly very badly, was between what had to be proved on  
 12 the balance of probabilities and where one takes a more  
 13 fluid assessment of what would have happened in the  
 14 hypothetical case.  
 15 If you take, to take a case a million miles from  
 16 this, a fatal accident case, where one is trying to  
 17 assess the earning potential of the deceased and you  
 18 will start by looking at the actuarial tables to see how  
 19 long that person would have lived, you will take a view  
 20 on that and you will adjust it by reference to  
 21 particular factors, and it might be a very healthy  
 22 person or a very ill person. Then you have to look at  
 23 what would have happened to that person's career over  
 24 time, if it is a young death, and you will have to look  
 25 at probabilities what would have happened: would they

97

1 have gone to university, what sort of career would they  
 2 have had, and in their career would they have been  
 3 promoted. All these factors have to be assessed and  
 4 weighed. To an extent there may be probabilities  
 5 involved. Would promotion have been received at  
 6 a certain time or not? What would the salary have been?  
 7 These are all the sort of factors one puts into the  
 8 mixing pot in order to reach a conclusion on the matters  
 9 in issue.  
 10 MR HOSKINS: Yes, but we say you don't have to go down that  
 11 route here, because the question was: what was the  
 12 exemptible level of MIF? It's not a question of: what's  
 13 the chance a regulator would have awarded an exemption  
 14 at a particular level? That just adds a degree of  
 15 complexity. Because nowadays you don't have to go and  
 16 get a formal stamp, a decision saying: you have  
 17 an exemption. If you are at the right level, you  
 18 benefit from the exemption without doing anything else.  
 19 That is why, in our submission, the question is  
 20 simply: what is the exemptible level of the MIF? For  
 21 you to decide on the basis of the evidence you have  
 22 before you.  
 23 MR JUSTICE BARLING: You say the significance of that being  
 24 the question we have to answer in relation to damages is  
 25 that the burden of proof is shifted as to what that

98

1 exemptible level is, as I understood it anyway. That  
 2 is, once you failed on, if you fail on, exemption, then  
 3 exemptible level passes over to Mr Brealey.  
 4 MR HOSKINS: They have to establish loss. So just that if  
 5 it is a widget cartel case, a claimant who turned up in  
 6 court without any evidence on what the lawful level  
 7 of -- the level of the MIF -- sorry, the price of the  
 8 widget would have been absent the cartel, they wouldn't  
 9 win, because the court wouldn't say: you are entitled to  
 10 the whole price.  
 11 MR JUSTICE BARLING: That is a bit different, possibly,  
 12 because here you would have an unexempted overcharge.  
 13 Here you have what you say is a restriction of  
 14 competition. You say that there is no -- I think you  
 15 say that in principle there is no distinction, even if  
 16 it is a zero MIF.  
 17 MR HOSKINS: It is not a MIF. What you don't have  
 18 an exemption for is a MIF at a certain level.  
 19 MR JUSTICE BARLING: Yes.  
 20 MR HOSKINS: If we are proceeding on the basis that there is  
 21 an exemptible level of the MIF, which is the evidence  
 22 before this Tribunal.  
 23 MR JUSTICE BARLING: It is not quite like a cartel case.  
 24 MR HOSKINS: I understand. It is a simplified comparison.  
 25 MR JUSTICE BARLING: It seems that, at first sight, it is

99

1 a bit counter-intuitive that, you having failed, on this  
 2 hypothesis, to establish that you have done something  
 3 lawful, therefore the assumption is you have charged  
 4 what is, in effect, an unlawful price, they then have to  
 5 prove what would have been a lawful price in order to  
 6 recover anything.  
 7 MR HOSKINS: I will go back to my widget cartel. We charged  
 8 a price of 10p per widget due to a cartel. That's not  
 9 exemptible, because it was a naked horizontal  
 10 price-fixing cartel. So we charged an unlawful price.  
 11 Can the claimant turn up and simply say: absent the  
 12 cartel, the widget would have cost nothing? Clearly  
 13 not.  
 14 When the sides turn up and the claimant turns up and  
 15 says, "I think the price absent the cartel would have  
 16 been X", the defendant says, "It would have been Y", who  
 17 is the burden of proof on? In that context, actually it  
 18 would be on the claimant because they are proving their  
 19 loss.  
 20 MR SMITH: But in weighing these various factors as to what  
 21 is exemptible, the exemptible level is, whether it can  
 22 be exempted, one of the things we need to take into  
 23 account are the criteria for exemption, and the fact  
 24 that the burden would be on you to establish that, were  
 25 push to come to shove in the counterfactual world.

100

1 MR HOSKINS: But we are removed, in a sense, from this.  
 2 I understand. We are removed from this exercise,  
 3 because you have heard all the evidence and you are  
 4 deciding what the exemptible level is. So you could  
 5 take it one stage of difficulty further and say: well,  
 6 because this is an unclear area, we are going to give  
 7 the benefit of the doubt to the claimant rather than the  
 8 defendant.

9 In my submission that wouldn't be the correct  
 10 approach, because the job for you is to apply the four  
 11 criteria and decide what the exemptible level would be.  
 12 Because you are not granting an actual exemption.

13 MR SMITH: Sure, but suppose --

14 MR HOSKINS: Can I just try -- this might help at least to  
 15 understand what I'm saying. Maybe you won't like it but  
 16 let me hopefully clarify the point.

17 The really interesting point arises, which is what  
 18 if -- we are looking at whether the actual MIF should  
 19 have an exemption, and the answer is no. Then you look  
 20 at the question: what would the exemptible level of MIF  
 21 have been? And using the broad axe you decide that the  
 22 spread of possible exemptible MIFs actually would cover  
 23 up to the level of the actual MIF. That really is where  
 24 it becomes important, if you get to that stage.

25 What my submission would be, so you see where we are

101

1 coming from, is that you could say, in that  
 2 circumstance, MasterCard has failed to prove its  
 3 entitlement to an exemption for the actual MIF, but as  
 4 a matter of quantification Sainsbury's has not  
 5 established any loss. Again, it is a bad one because it  
 6 is not a complete fit, but this is the one that popped  
 7 into my head when I was trying to see, well, why would  
 8 that be right.

9 It is a bit like a crime has been committed and  
 10 there is a criminal prosecution which fails and then  
 11 there is a civil action that succeeds. Now it is not  
 12 perfect, because you have different standards in  
 13 criminal and civil law, but you can see how the same act  
 14 can give rise to one conclusion in one legal context and  
 15 in another.

16 I think I'm a bad lawyer, because I know lawyers are  
 17 supposed to get excited about burden of proof issues.  
 18 My impression is -- I have never sat on that side of the  
 19 bench -- the truth is you have all the evidence before  
 20 you, and if you ask yourselves the question what was the  
 21 exemptible level of the MIF, with all the evidence  
 22 before you, it is not going to turn on the question of  
 23 who bears the burden of proof. Because you have more  
 24 than enough evidence in this case to come to your own  
 25 conclusion on what the exemptible level is.

102

1 MR SMITH: Suppose we take a view that there is  
 2 an exemptible MIF, and we have in mind a range, and at  
 3 the upper end we are confident that it wouldn't be  
 4 exempted, at the lower end we are confident that it  
 5 would be, and we are just not sure in our minds where in  
 6 the range it works. We have established sort of to our  
 7 satisfaction that the probability of exemption increases  
 8 the lower you go.

9 At that point, don't we have to take into account  
 10 the burdens that do lie on your client with regard to  
 11 establishing exemption, and we should say, well, we  
 12 should err towards the lower range of that end rather  
 13 than the --

14 MR HOSKINS: I think it depends how you ask the question.  
 15 Because if, in your example, you have a range and you  
 16 think the upper level wouldn't merit an exemption, then  
 17 it shouldn't be in your range. I think you are looking  
 18 for the range of MIFs that you believe would get  
 19 an exemption. Once you have identified that range, then  
 20 if you are applying the broad axe -- which helps  
 21 Sainsbury's in many ways because they are not required  
 22 to prove loss to the nearest pound and pence, the broad  
 23 axe generally helps the claimant -- but what kicks in  
 24 then is generally that the courts, without a legal  
 25 rule, that the courts have generally said: if we are

103

1 applying the broad axe in order to allow some recovery,  
 2 you err on the side of under-compensation.

3 Our submission would be, first of all, identify the  
 4 range where you think, on the balance of probabilities,  
 5 it would satisfy the exemption criteria. Then, in terms  
 6 of assessing what the overcharge was, you err on the  
 7 side of under-compensation.

8 MR JUSTICE BARLING: You say that in establishing that range  
 9 we have to -- I know you say, and you may well be right  
 10 about this, but most cases don't turn on the burden of  
 11 proof, most issues don't -- but technically, in  
 12 establishing that range, you say the burden is on  
 13 Sainsbury's to establish --

14 MR HOSKINS: No, in terms of establishing -- we have to --  
 15 if one starts from the basis that there is an exemptible  
 16 level of MIF, then yes, the burden is on Sainsbury's.

17 Assume it wasn't common ground, there hadn't been  
 18 evidence, common ground between the parties, that there  
 19 was an exemptible level of MIF, then the burden would be  
 20 on us to show there was an exemptible level, and that  
 21 would probably fold the two questions together. But  
 22 once you have a situation where both parties before you  
 23 are saying there is an exemptible level of MIF, one side  
 24 says X and one side says Y, then I would say the burden  
 25 is on them to show what the exemptible level is.

104

1 PROFESSOR JOHN BEATH: Sorry, in order to show that Y is  
 2 right rather than --  
 3 MR HOSKINS: Yes, to show what the extent of their loss is.  
 4 MR SMITH: You have mentioned, quite rightly, on several  
 5 occasions that both economists agree not as to the level  
 6 of exemptibility but that there ought to be  
 7 an exemptible level.  
 8 You are not going so far as to say that we simply  
 9 take that agreement as read and assume our quest for the  
 10 exemptible level? We presumably have to apply the legal  
 11 test to the facts that the economists have brought  
 12 before us and reach a conclusion as to exemptibility  
 13 first and then go on to --  
 14 MR HOSKINS: I agree with that. Because if you have two  
 15 expert reports that you thought, that's fine, but they  
 16 are completely wrong in law, it wouldn't help you. But  
 17 you will see the submission and you have read the  
 18 clauses, but Mr von Hinten-Reed thinks on his view of  
 19 the law it is satisfied, and we say on our view of the  
 20 law it is satisfied, but I agree you would have to  
 21 satisfy --  
 22 MR SMITH: We have to apply the legal test first and then go  
 23 from there.  
 24 MR HOSKINS: Yes. But that is applying a legal test to  
 25 facts that have been established on the balance of

105

1 probabilities. It is a purely legal exercise, and if a  
 2 burden of proof doesn't come into that then we are  
 3 dancing on the head of a pin.  
 4 MR SMITH: Yes, we are going into an interesting and  
 5 possibly unnecessary debate about what is a question of  
 6 fact and what is a question of law, but yes, we have to  
 7 apply the law to the facts.  
 8 MR HOSKINS: Even a characterisation of facts is generally  
 9 characterised as, for example, as an error of law in  
 10 judicial reviews.  
 11 I was trying to make your job easier, at least at  
 12 some stage.  
 13 Can I move into the four criteria then. I pick it  
 14 up at page 66 of our closing submissions. Both in the  
 15 opening and in the closing we have referred to the  
 16 101(3) guidelines. For example, if you see  
 17 paragraph 202, what the guidelines do say:  
 18 "Each case must be assessed on its own facts and the  
 19 guidelines must be applied reasonably and flexibly."  
 20 Yes, you have to bring robust evidence etc, but it  
 21 is not an impossible burden. It is not intended to be.  
 22 Because that itself would be bad for competition. If  
 23 nobody could ever prove a 101(3) case, then matters that  
 24 should be exempted will not be exempted. So it is odd,  
 25 there is a bit of hard and soft in the regulation.

106

1 Sometimes the language is really hard. Sometimes it is  
 2 actually quite soft, that you have to be flexible and  
 3 reasonable.  
 4 Another aspect of that is you don't always have to  
 5 put a precise number on something in order to come  
 6 within the first condition. So I'm moving into the  
 7 first condition now. Perhaps we can look briefly at the  
 8 guidelines so that is E1 at 2(a).  
 9 As Mr Brealey said, you have to put a value on it.  
 10 Let's see what the guidelines says. It is 38(a).9. It  
 11 is 51, which is the paragraph which Mr Brealey took you  
 12 through a number of occasions:  
 13 "All efficiency claims must therefore be  
 14 substantiated so that the following can be verified and  
 15 see the likelihood and magnitude of each claimed  
 16 efficiency."  
 17 If you then read 56 and 57, whilst you have to  
 18 describe the magnitude that doesn't mean putting  
 19 an actual figure on it in every case.  
 20 You see in 57:  
 21 "In the case of claimed efficiencies in the form of  
 22 new or improved products and other non-cost-based  
 23 efficiencies, the undertakings claiming the benefit of  
 24 Article 81(3) must describe and explain in detail what  
 25 is the nature of the efficiencies, and how and why they

107

1 constitute an objective economic benefit."  
 2 Put it in different language, you can have  
 3 a qualitative assessment. It doesn't always have to be  
 4 quantitative. But it has to be proved by evidence, it  
 5 has to satisfy the burden of proof, etc. But it is not  
 6 always a number.  
 7 MR JUSTICE BARLING: 56 is a bit more --  
 8 PROFESSOR JOHN BEATH: 56 is a --  
 9 MR HOSKINS: Sorry, I would ask you to read both of them  
 10 because where you can put a number on it, you should.  
 11 PROFESSOR JOHN BEATH: The other says there is an efficiency  
 12 that has a qualitative dimension to it.  
 13 MR HOSKINS: Absolutely. I'm not intending to say you can  
 14 never look at numbers. Insofar as you can put numbers,  
 15 you should do numbers. But insofar as you can't do  
 16 numbers, you shouldn't ignore the qualitative.  
 17 If I can go then to page 67 of the closing. We are  
 18 in the first condition now, what efficiency gains, what  
 19 benefits.  
 20 MR JUSTICE BARLING: Yes.  
 21 MR HOSKINS: We have tried to put in very simple terms at  
 22 206 the nub of our case, but this comes into the other  
 23 conditions as well. I will take it in stages, but 206:  
 24 "In the present case, the evidence establishes that  
 25 the MasterCard scheme gives rise to benefits."

108

1 We will come to that:  
 2 "Even if this Tribunal finds that the UK MIF was not  
 3 necessary to allow this scheme to operate, so not  
 4 objective necessity, the scheme will still generate  
 5 relevant benefits within the scope of the first  
 6 condition to the extent that the UK MIF allows the  
 7 MasterCard scheme to be larger and therefore generate  
 8 more benefits than a scheme without a MIF, or indeed  
 9 a scheme with a smaller MIF."  
 10 In other words, benefits which arise from the  
 11 MasterCard scheme that would not arise in the absence of  
 12 a MIF satisfy the first condition. I will develop that,  
 13 but that's the nub of what we say.  
 14 First question, this took up quite a lot of time  
 15 yesterday, benefits on what markets? Because there are  
 16 three markets in play here: there is the intersystems  
 17 market, competition between payment schemes; there is  
 18 the issuers' market; there is the acquiring market.  
 19 In our submission, it is absolutely plain as  
 20 a matter of law that the Tribunal is not limited to  
 21 considering benefits arising solely on the acquiring  
 22 market. You are looking at efficiencies on the other  
 23 markets as well.  
 24 We have referred to *Compagnie Maritime Belge*. That  
 25 is set out almost verbatim, so we have given you the

109

1 reference to the passage, but what that case says is:  
 2 "The CJEU held that regard should be had to the  
 3 advantages arising from the agreement in question, not  
 4 only for the relevant market but also in appropriate  
 5 cases for every other market on which the agreement in  
 6 question might have beneficial effects, and even in  
 7 a more general sense for any service the quality or  
 8 efficiency of which might be improved by the existence  
 9 of that agreement."  
 10 MR JUSTICE BARLING: That is a quote really from the case.  
 11 MR HOSKINS: It is a quote.  
 12 MR JUSTICE BARLING: I can't remember whether you took us to  
 13 that in opening or not.  
 14 MR HOSKINS: I don't think I did.  
 15 MR JUSTICE BARLING: We have the reference and we have  
 16 the quote.  
 17 MR HOSKINS: When we go to MasterCard you get that applied  
 18 specifically in the context of the MasterCard scheme.  
 19 MasterCard isn't an outlier. That is the general  
 20 principle, *Compagnie Maritime Belge*, then you see it  
 21 applied in MasterCard. I think it is worth going  
 22 because this is such an important point. E1, tab 19.  
 23 MR BREALEY: Just so it helps, we do agree that for the  
 24 first condition you look at everything, all the markets.  
 25 I don't want to cut Mr Hoskins short but I thought I had

110

1 agreed that when it comes to the first condition, you  
 2 can look at efficiencies in all markets.  
 3 MR SMITH: Yes, I think the nub of the debate we had  
 4 yesterday was who is a consumer for the purposes of  
 5 101(3), the second condition.  
 6 MR BREALEY: For the second condition, yes.  
 7 MR JUSTICE BARLING: I think that is right.  
 8 MR HOSKINS: Which I will come onto. You weren't taken to  
 9 this in the context of the discussion, and I just want  
 10 to show you that the law is absolutely clear, and  
 11 hopefully that is helpful because you don't then have to  
 12 decide a difficult question of law for yourself because  
 13 it has been decided for you by the Courts of Justice.  
 14 Page 437, paragraphs 236 and 237. If I can just ask  
 15 you to read 236 and 237. I think they speak for  
 16 themselves. (Pause).  
 17 I think it is also helpful to look at 241, where the  
 18 court says:  
 19 "All the advantages on both consumer markets in the  
 20 MasterCard scheme, including therefore on the  
 21 cardholder's market, could, if necessary, have justified  
 22 the MIF."  
 23 Then 242:  
 24 "Thus, where, as in the present case, restrictive  
 25 effects have been found in only one market of

111

1 a two-sided system, the advantages flowing from  
 2 restrictive measure on a separate but connected market  
 3 also associated with that system cannot in themselves be  
 4 of such a character as to compensate for the  
 5 disadvantages resulting from that measure in the absence  
 6 of any proof of the existence of appreciable objective  
 7 advantages attributable to that measure in the relevant  
 8 market."  
 9 I will come on to that, because that is the next  
 10 stage. Because, sir, what you can't do is look at all  
 11 the benefits. Here, if you are looking at a restriction  
 12 on the acquiring market, the fact that there are lots of  
 13 benefits in the issuing market, if there were none on  
 14 the acquiring market, that would not be enough.  
 15 I will come to take that in a bit more nuanced way  
 16 as to what you have to have on the acquiring market. At  
 17 this level, first condition, 'are there efficiencies?',  
 18 you are looking at both markets. That's quite clear  
 19 from the case.  
 20 MR SMITH: In terms of efficiencies, simply as a matter of  
 21 logic, you can't rely upon the benefit that you relied  
 22 upon at the 101(1) stage, namely the collapse of the  
 23 market, because by definition you will have rejected  
 24 that submission if you get to 101(3).  
 25 MR HOSKINS: Exactly. As I put it in paragraph 206, what

112

1 I'm about to do is identify a large number of what we  
 2 say are benefits from the MIF. The argument is going to  
 3 be -- again, I will take you to the evidence, but what  
 4 the MIF allows the scheme to do is compete with other  
 5 schemes and extend its market share; and the more people  
 6 that use credit cards, the more people that benefit from  
 7 the benefits, whether it be cardholders and/or  
 8 merchants. In fact, it is both. This has moved away at  
 9 this stage from --

10 MR SMITH: I thought that was your position. I just wanted  
 11 to be clear.

12 MR HOSKINS: Page 70 of the closings, "Benefits to  
 13 merchants". Now, poor Mr Brealey's fantastic thing  
 14 quote comes back again, but let's look at the benefits  
 15 to the merchants, the evidence that credit cards benefit  
 16 merchants, and also the evidence that the value of those  
 17 benefits exceeds the costs to merchants.

18 At 216 of the closings you have got the point we  
 19 made in our opening oral submissions. When you look at  
 20 how credit cards came into being, long before any credit  
 21 card schemes existed, merchants offered customers  
 22 credit. It has a value to merchants. They did that.  
 23 Why offer credit? Because it was an advantage to do so.  
 24 And they must have decided that, by definition, the  
 25 benefits of accepting credit outweighed the costs to

113

1 them of doing so, otherwise nobody would have done it.

2 It makes me think of those old westerns, where  
 3 people are going into the general store and putting it  
 4 on the slate. It has been around for centuries;  
 5 merchants offer credit because they think it has  
 6 an overall benefit for them.

7 The second point, this is 217, merchants were  
 8 willing to accept credit cards when they were  
 9 introduced, despite the fact they had higher costs to  
 10 them than debit cards. So in that world a few decades  
 11 ago, when there were just debit cards, somebody comes in  
 12 with credit cards, the merchants didn't go: no, no, no.  
 13 You see the success of the schemes. It has been  
 14 incredibly successful.

15 If the addition of the credit facility provided no  
 16 benefit to the merchant at all, merchants would have no  
 17 reason to accept anything other than debit cards.

18 Mr von Hinten-Reed accepted in his  
 19 cross-examination, we have set it out, that each  
 20 merchant which accepts cards must consider the value of  
 21 doing so is greater than the cost to them of doing so.  
 22 He had a different point then, which we will come to.  
 23 But he accepts that for individual merchants you accept  
 24 a credit card because you think the benefits to you  
 25 outweigh the costs.

114

1 Third point, 218, the benefits that merchants  
 2 receive from accepting credit cards is apparent from the  
 3 evidence of expenditure at Sainsbury's. That's the  
 4 table I took you to this morning, you remember the  
 5 average transaction value, where you saw the difference  
 6 for MasterCard credit and Maestro and for Visa Credit  
 7 and for Visa Debit. We have given you the reference  
 8 there, but it is that little table. People spend more  
 9 on credit cards than they do on debit cards.

10 Paragraph 220 -- it is in yellow so I can't read it  
 11 out -- you will see the comparison there is between the  
 12 extra spend on the average transaction value between  
 13 credit and debit and what MIF is being incurred. You  
 14 will see that the benefits quite substantially outweigh  
 15 the detriment to Sainsbury's by accepting credit cards,  
 16 by an order of magnitude.

17 The fourth point, this is at 221, the substantial  
 18 benefit which Sainsbury's, and indeed all other  
 19 retailers, we say, receive from allowing its customers  
 20 to buy on credit is confirmed by the significantly  
 21 higher payments that Sainsbury's agreed to make to  
 22 American Express. Again, a lot of this is in general,  
 23 so I have to be careful. But the point is this: for the  
 24 first eight years of the claim period, Sainsbury's was  
 25 willing to pay American Express an average MSC that was

115

1 much higher or materially higher than the MasterCard and  
 2 Visa fees. Why? Because they thought it had a benefit.

3 I could get into the debate this morning about: did  
 4 they drag Amex down to the level of Visa and MasterCard?  
 5 No, they didn't. We have said enough on that, but in  
 6 passing I will note that.

7 Then in B we have the point that even with this 2015  
 8 negotiation, with the regulation putting the cold hand  
 9 on Amex's shoulder, you will see the level of the  
 10 negotiated fee between Sainsbury's and Amex compared to  
 11 the 0.3 that MasterCard and Sainsbury's have. Why is  
 12 Sainsbury's willing to pay that to Amex? Because it  
 13 thinks there is a benefit in doing so.

14 Fifth point at 222. There is, of course, further  
 15 evidence in relation to the substantial benefits which  
 16 Sainsbury's believe it receives from credit cards in the  
 17 Sainsbury's Bank payment story, because Sainsbury's  
 18 Supermarkets was willing to pay Sainsbury's Bank large  
 19 sums to offer more attractive cards, because it thought  
 20 that would lead to greater sales in its stores.

21 So again, cogent evidence that Sainsbury's believed  
 22 that credit cards have a substantial advantage for it,  
 23 to the tune of the level of the payments that it was  
 24 making.

25 Sixth point at 224. This is actually

116

1 Mr von Hinten-Reed's point, so this point isn't  
 2 controversial. Merchants receive benefits from  
 3 accepting credit cards by avoiding the cost of other  
 4 payment methods. That's Mr von Hinten-Reed's case.  
 5 That's what he says. That's all he says is the benefit.  
 6 That is the starting point.  
 7 Seventh point at 225. Merchants benefit from  
 8 customers being able to purchase goods and pay next  
 9 month at no cost, which the interest-free period  
 10 provides, and that's the net present value point.  
 11 Because someone who -- let's take Mr Brealey's  
 12 restaurant example; you are sitting at home and you have  
 13 got a lonely tin of soup in the cupboard, and you think  
 14 "I don't get paid for a week but I really don't fancy  
 15 that soup for tonight, I will go and have a nice meal on  
 16 my credit card", and the merchant benefits because  
 17 that's a meal that might not otherwise have been taken.  
 18 So there is the net present value point. That is  
 19 a benefit.  
 20 Merchants benefit from the free funding period in  
 21 another way. Let me see if I can break this down.  
 22 In relation to the free funding period, credit card  
 23 issuers, unlike debit card issuers, have no current  
 24 account relationship with the cardholder. So, when the  
 25 cardholder uses the card to make a payment, what happens

117

1 in the current system is that the merchant gets the  
 2 money immediately, but the cardholder has 28 days to  
 3 pay. But in a debit card world, the money is lifted  
 4 immediately from the cardholder's account.  
 5 What a four-party credit card scheme could do is it  
 6 could say, rather than pay the merchant immediately, we  
 7 will pay the merchant in 28 days' time when we actually  
 8 receive the money.  
 9 But that's not what happened. So the free funding  
 10 period has a flip. It gives the customer 28 days to pay  
 11 but, equally, part of the system is the merchant gets  
 12 the money immediately, they are not required to wait 28  
 13 days. So in terms of net present value, it's money in  
 14 the pocket for the merchant.  
 15 MR JUSTICE BARLING: That is an advantage over a store  
 16 charge card, which would presumably -- no, sorry. No.  
 17 They would pay later -- yes, that's just a credit card  
 18 but you have to pay the full amount.  
 19 MR HOSKINS: It is an advantage of a store card. It is the  
 20 advantage of old-fashioned -- if I went back to my  
 21 Wild West store, you could have credit, but that  
 22 merchant wouldn't get the money immediately.  
 23 What actually happens under the four-party scheme --  
 24 MR JUSTICE BARLING: The merchant gets it the next day.  
 25 MR HOSKINS: Exactly.

118

1 I have interleaved that point, but then the ninth  
 2 point in the closings, at 227, is the point that  
 3 Dr Niels explained, that payment cards have contributed  
 4 significantly to the increase in online spending and  
 5 e-commerce. The reason for that is the obvious one,  
 6 cash is not a viable alternative, generally speaking,  
 7 for online transactions.  
 8 Mr von Hinten-Reed agreed in cross-examination, cash  
 9 is not generally suitable for online transactions. So  
 10 he said that is a benefit to merchants. The reason why  
 11 merchants offer online services, again, is because they  
 12 believe that the benefits then will outweigh the costs,  
 13 and you only get the ability to offer these online  
 14 services because of credit cards.  
 15 I'm sorry, Mr Cook has pointed out I missed our  
 16 eighth point, which is at 226, which is an important  
 17 one. Which is that merchants derive significant  
 18 benefits from the payment guarantee and the immediate  
 19 settlement period. The immediate settlement is the  
 20 point I was on.  
 21 MR JUSTICE BARLING: That is the point you made.  
 22 MR HOSKINS: Mr von Hinten-Reed acknowledged that merchants  
 23 do benefit from the fraud guarantee and the cardholder  
 24 default guarantee, because they get the money in any  
 25 event.

119

1 That is merchants. I am not pretending that is  
 2 an exhaustive list, but there is a serious -- I put it  
 3 there is overwhelming evidence of material benefits to  
 4 merchants. I leave the hyperbole at that.  
 5 Then one looks at cardholders as well, because we  
 6 are to look at both sides. This is paragraph 229 of the  
 7 closing.  
 8 Mr von Hinten-Reed accepted again, in  
 9 cross-examination -- we give there the references --  
 10 cardholders benefit from short-term flexibility of the  
 11 credit provided by credit cards, they benefit from the  
 12 interest-free period, they benefit from the ability to  
 13 make online purchases and they benefit from the  
 14 availability of rewards.  
 15 For Mr Brealey rewards are a vicious circle, but in  
 16 our submission they are a virtuous circle, because  
 17 rewards encourage cardholders to use their cards. How  
 18 do they use their cards? By spending money with  
 19 merchants. It is a virtuous cycle, not a vicious cycle.  
 20 In terms of the first condition, what are the  
 21 benefits of credit cards, those are the benefits.  
 22 I will come on -- I know the legal test is benefits  
 23 flowing from the MIF, and I have given you a flavour of  
 24 that, it is because the MIF increases the use of credit  
 25 cards, but I will come to that, and I am going to do

120

1 that under one of the other conditions. I haven't  
 2 forgotten that.  
 3 Let's go to the second condition, which is a fair  
 4 share for consumers.  
 5 First of all, we have set out the exemption  
 6 guidelines at paragraph 85. This is this notion of: is  
 7 social welfare relevant or not? In our submission it  
 8 clearly is. One sees that most clearly really in 85 of  
 9 the exemption guidelines:  
 10 "The concept of fair share implies that the pass-on  
 11 of benefits must at least compensate consumers for any  
 12 actual or likely negative impact caused to them by the  
 13 restriction of competition. It allows the overall  
 14 objective of Article 81 to prevent anti-competitive  
 15 agreements. The net effect of the agreement must at  
 16 least be neutral from the point of view of those  
 17 consumers directly or likely affected by the agreement.  
 18 If such consumers are worse off following the agreement,  
 19 the second agreement is not fulfilled. The positive  
 20 effects of the agreement must be balanced ...(Reading to  
 21 the words)... valuable products, and thus to more  
 22 efficient allocation of resources."  
 23 That is a clear, we say, description of social  
 24 welfare. As I will show you, to unlock social welfare  
 25 certain legal criteria have to be fulfilled and that's

1 21

1 the next heading, "Which consumers?"  
 2 In our submission, it is quite clear again from the  
 3 law that when you are looking at which consumers  
 4 benefit, you are looking at merchants who accept payment  
 5 cards, you are not looking at merchants who do not  
 6 accept payment cards.  
 7 This is one of the real flaws in  
 8 Mr von Hinten-Reed's analysis, where he looks at all  
 9 merchants. That is quite clear again, we say, from the  
 10 exemption guidelines. We have set it out at 234,  
 11 paragraph 84:  
 12 "The concept of consumers encompasses all direct or  
 13 indirect users of the products covered by the  
 14 agreement ..."  
 15 Here it is users of MasterCard. It is merchants who  
 16 accept MasterCards and cardholders who accept  
 17 MasterCards. It does not include merchants who do not  
 18 accept MasterCards. Not surprisingly, if you think  
 19 through the logic.  
 20 Then you follow that quote through:  
 21 "... including producers that use the products as  
 22 an input, wholesalers, retailers and final consumers, ie  
 23 natural persons who are acting for purposes which can be  
 24 regarded as outside their trade or profession. In other  
 25 words, consumers within the meaning of Article 101(3)

1 22

1 are the customers of the parties to the agreement and  
 2 the subsequent purchasers."  
 3 The parties to the agreement here are the issuing  
 4 and acquiring banks and MasterCard itself, and the  
 5 subsequent purchasers are the cardholders on one side  
 6 and the merchants on the other.  
 7 Those are the consumers who have to have a fair  
 8 share; cardholders who have MasterCard, merchants who  
 9 accept MasterCards.  
 10 That's also, we say, clear from the Court of  
 11 Justice in MasterCard. If we go back that, that's  
 12 E1.19. It is page 437, paragraphs 235 to 237. You have  
 13 read these before but it is in particular from the  
 14 language of 237:  
 15 "It follows from this that in the case of a two  
 16 sided system such as the MasterCard scheme ..."  
 17 Sorry, I should pick it up -- if you see in 236 the  
 18 final sentence says:  
 19 "Furthermore, under Article 81.3 EC it is the  
 20 beneficial nature of the effect on all consumers in the  
 21 relevant markets."  
 22 It is not all consumers; it is all consumers in the  
 23 relevant markets. So in the relevant issuing markets  
 24 and the relevant acquiring markets, they must be taken  
 25 into consideration.

1 23

1 That follows through in 237:  
 2 "It follows from this that in a case of a two-sided  
 3 system such as the MasterCard scheme, in order to assess  
 4 whether a measure which in principle infringes Article  
 5 101(1) can fulfil the first condition it is necessary to  
 6 take account of the system of which that ...(Reading to  
 7 the words)... advantages flowing from that measure, not  
 8 only on the market in respect to which the restriction  
 9 has been established but also in a market which includes  
 10 the other group of consumers associated with that  
 11 system."  
 12 I understand that this is talking about the first  
 13 condition, but the language is clearly of the consumers  
 14 associated with the MasterCard system on the issuing  
 15 side and the acquiring side, which is what the  
 16 guidelines tells us we should do.  
 17 Mr von Hinten-Reed's analysis is based on the  
 18 assumption that as a matter of law, under  
 19 Article 101(3), all merchants must be shown to benefit  
 20 from the MIF. That is why he kept going on about, for  
 21 example, business stealing and he excludes it. But he  
 22 was absolutely wrong to do so as a matter of law. I'm  
 23 afraid he has just got the law wrong. That's important  
 24 because, of course, as soon as you realise what the law  
 25 actually is, then business dealing becomes highly

1 24



1 relevant; because insofar as a merchant who accepts  
2 a MasterCard credit card steals, obtains a purchase from  
3 someone else who does not, that is a relevant  
4 efficiency. And it is also part of the fair share for  
5 that merchant under the second condition.

6 The final question on this second condition is 'how  
7 much benefit?', which is an important point. This is  
8 paragraph 239 of the closings. I have just put that  
9 judgment away and I'm going to have to go back to it.  
10 Sorry. E1.19. What the legal position is -- before  
11 I take you there, it is paragraph 248, I think that is  
12 at page 438.

13 If you could read 248, that's the quickest way to  
14 take it. (Pause).

15 Again, what we say, the case law is quite clear.  
16 For the second condition, fair share, it is not  
17 necessary to find that each group of consumers,  
18 merchants and cardholders, should benefit equally from  
19 the benefits, provided that merchants do enjoy  
20 appreciable objective advantages. Merchants have to  
21 enjoy the MIF as well as cardholders, but not to the  
22 same extent as them.

23 Equally, within that group of merchants -- if you  
24 could take up 13 at tab 8, it is a case that you have  
25 been referred to but I don't think you have seen

125

1 Shaw and Falla, which is one of the beer cases.

2 It is paragraph 163 at page 315. You should read  
3 the paragraph, but it is the final sentence that is  
4 really the important one:

5 "From the point of view of the grant of  
6 an individual exemption, it is not material that the  
7 benefits produced by the notified agreements do not  
8 entirely compensate the price differential suffered by  
9 a particular tied lessee. If the average lessee does  
10 enjoy that compensation, it is therefore such as to  
11 produce an effect on the market generally."

12 What this is saying is we know that merchants must  
13 enjoy the benefits as well as cardholders, but not to  
14 the same extent as them, and equally you don't have to  
15 show that each individual merchant benefits from the  
16 same level of efficiencies as all other merchants. You  
17 are looking at the merchants who accept MasterCard in  
18 aggregate or the average of them.

19 Then we come to the third condition, which is  
20 indispensability. I pick this up at page 80 of the  
21 closing submissions. The point is not: does the  
22 MasterCard system generate benefits? The question is:  
23 does MIF generate benefits? That's the test. Again,  
24 that comes from the Court of Justice in MasterCard as  
25 well.

126

1 In looking at this, paragraph 245, we have set out  
2 again an extract from the exemption guidelines,  
3 paragraph 75. When looking at indispensability what the  
4 guidelines say, it's halfway down paragraph 245:

5 "Undertakings invoking the benefit of Article 101(3)  
6 are not required to consider hypothetical or theoretical  
7 alternatives. The business judgment of the party should  
8 not be second-guessed. The authority or court should  
9 only intervene where it is reasonably clear that there  
10 are realistic and attainable alternatives. The parties  
11 need only explain and demonstrate why such seemingly  
12 realistic and significantly less restrictive  
13 alternatives to the agreement would be significantly  
14 less efficient."

15 Again, as I said, sometimes the language in the  
16 guidelines is very hard but sometimes it is more  
17 practical, and this is one of those areas.

18 Again, if you go then to 247, which is taken from  
19 the guidelines, and our restriction, in our context, is  
20 the MIF. What the guidelines say is the MIF is  
21 indispensable if its absence would eliminate or  
22 significantly reduce the efficiencies that follow from  
23 the agreement or make it significantly less likely that  
24 they will materialise. The assessment of alternative  
25 solutions must take into account the actual or potential

127

1 improvement in the field of competition by the  
2 elimination of a particular restriction or  
3 an application of a less restrictive alternative.

4 In short, third condition, the MIF will satisfy the  
5 third condition if more efficiencies are produced with  
6 the MIF than would be the case without the MIF.

7 It's not all or nothing. It's does the MIF  
8 contribute to the benefits of the scheme, does it  
9 increase them? If it does, it's relevant.

10 What's the evidence of indispensability in this  
11 case? This is paragraph 250 of the closing submissions.  
12 The evidence in this case establishes that -- this is  
13 the point I started with -- the MIF is:

14 (1) A critical aspect of competition between payment  
15 schemes.

16 (2) It encourages increased use of payment cards;  
17 (b) cardholders receive higher benefits from card use in  
18 a system with a MIF than they would if there were no  
19 MIF.

20 (3) Merchants benefit from the MIF because the MIF  
21 allows a payment scheme to attract more cardholders, who  
22 in turn use their cards to make purchases from the  
23 merchants who accept them, and increased card use is a  
24 benefit to merchants.

25 Then we set out the evidence, but I'm not going to

128

1 go through it in detail because we just don't have time,  
 2 but I take each of those points and we have given you  
 3 the evidence that supports them.  
 4 251. The MIF increases competition between schemes  
 5 and increases use of payment cards.  
 6 We have given you the evidence, and  
 7 Mr von Hinten-Reed accepted those principles in  
 8 cross-examination. We have set out the quotes.  
 9 254 onwards deals with the increasing number of  
 10 cards. 254, in cross-examination, Mr von Hinten-Reed  
 11 agreed that MasterCard set the MIF at a level designed  
 12 to maximise the number of MasterCard cards. Again, we  
 13 have set out all the evidence there.  
 14 255, the MIF allows cardholders to receive higher  
 15 benefits.  
 16 Again we have set out the relevant evidence, from  
 17 Mr von Hinten-Reed's own report and cross-examination.  
 18 You see at 256 he accepted cardholders would like to  
 19 get rewards and he accepts that rewards are financed by  
 20 the MIF.  
 21 257. In cross-examination Mr von Hinten-Reed  
 22 accepted that low cost balance transfers, low  
 23 interest-free periods, credit card access to less  
 24 affluent customers, higher rewards on cards had all  
 25 developed as a result of competition between card

129

1 issuers and the intersystem market.  
 2 We say, therefore, all that evidence, I will leave  
 3 you to look at the detail, but what it confirms is if  
 4 there were no MIF, such benefits to cardholders would be  
 5 reduced. It is obvious from the evidence.  
 6 If one is looking at the fact that MIF increases  
 7 benefits to merchants, I have just dealt with  
 8 cardholders -- at 259 there is a typo I should correct,  
 9 it says the MIF increases benefits to merchants.  
 10 First, the MIF increases card use, thus producing  
 11 a corresponding increase in the benefits which, it  
 12 should say "merchants" obtain from the use of cards.  
 13 Again, you have got the evidence of  
 14 Mr von Hinten-Reed accepting those points. Then at 260:  
 15 "Reduced use of payment cards would lead to  
 16 increased use of alternative payment means, such as cash  
 17 or cheques, which would be more expensive for  
 18 merchants."  
 19 That is Mr von Hinten-Reed's case. That's all he  
 20 was prepared to admit.  
 21 Then, third at 261 you have got the evidence about  
 22 Project Forward, Project Porsche etc, where the  
 23 MasterCard was -- I have to be careful because a lot of  
 24 that was confidential, but you will see the final  
 25 sentence at 261/262. It is not marked but I just want

130

1 to be a bit sensitive about it.  
 2 MR SMITH: Mr Hoskins, just going back to your  
 3 paragraph 258, where you begin to enumerate the benefits  
 4 if there were no MIF, the counterfactual you are  
 5 assuming there is that there will be a MIF of zero; is  
 6 that right? What I'm trying to work out is what you are  
 7 gauging the benefits against.  
 8 MR HOSKINS: It is that, but it is also the higher the MIF,  
 9 the more the benefits are.  
 10 MR SMITH: Right.  
 11 MR HOSKINS: There is clearly a breaking point, but the  
 12 difficulty is we don't know what it is. But in terms  
 13 of -- I mean, for example -- this is not a complete  
 14 answer. I was trying to put it in context. You heard  
 15 the evidence, on the EDC study, the 2008 one, if one  
 16 took the level of all the costs, and I will come to this  
 17 when I do the adjusted cost/benefit analysis, the MIF  
 18 was actually set substantially below the total costs  
 19 that were assessed there.  
 20 Yes, the argument is not just some MIF is better  
 21 than no MIF, generally speaking there is an increasing  
 22 level of benefits, but I accept at some stage there must  
 23 be a break point and that's when merchants would  
 24 actually turn round and say, "I'm sorry, we are not  
 25 accepting credit cards anymore because we are not

131

1 anymore receiving more benefits than it is costing us".  
 2 MR SMITH: So something of a sliding scale.  
 3 MR HOSKINS: Yes.  
 4 MR SMITH: Or an upward demand curve.  
 5 MR HOSKINS: Yes.  
 6 MR SMITH: Subject to your limit, the greater the MIF, the  
 7 greater the benefits to all concerned.  
 8 MR HOSKINS: Yes. To all concerned, absolutely.  
 9 MR JUSTICE BARLING: I think all we are looking at now is  
 10 under the heading of indispensability, but in terms --  
 11 I was going to ask, but I think you have partially  
 12 answered it, maybe fully answered it: in terms of where  
 13 you fit -- how you fit the level of a MIF as opposed to  
 14 the existence of a MIF into those four criteria --  
 15 MR HOSKINS: I'm going to come to that, because you are  
 16 absolutely right that that is then the next question, if  
 17 you like. It is what I have just been discussing with  
 18 Mr Smith. Because it is all very well to say a MIF  
 19 creates these extra benefits. The trouble is you have  
 20 got to decide what level of MIF. I'm going to come to  
 21 that as a separate question, because obviously that is  
 22 a big issue. I just want to finish the four conditions.  
 23 MR JUSTICE BARLING: What I'm asking is: should we look at  
 24 fair share or is it under 7?  
 25 MR HOSKINS: I put it under indispensability. I appreciate

132

1 there is not a neat compartment. I have tried to  
 2 identify the issues and I've put them under the  
 3 conditions, but I fully accept you can look at them as  
 4 having interactions. I hope I'm covering all the  
 5 points, but I accept you may say they may have some  
 6 relevance to other headings.  
 7 If I can finish on this bit. Page 88. Again, the  
 8 case isn't a very difficult one to follow. We have got  
 9 the evidence. It is not just me telling a story, we  
 10 have set out in detail the evidence.  
 11 262, on page 88. It is clear from the evidence that  
 12 more efficiencies are produced with the MIF, and that's  
 13 on both sides, issuing and acquiring, than would be the  
 14 case in the absence of the MIF.  
 15 The existence of a MIF brings significant benefits  
 16 to intersystem competition, merchants and cardholders.  
 17 Then, as you see at 264, the crucial question is  
 18 then what level of MIF satisfies indispensability?  
 19 Which in a sense is the \$6 million question, but I will  
 20 come to that after the short break.  
 21 Let me finish the fourth condition, because I can do  
 22 that quickly. No elimination of competition. You see  
 23 that at 266. We see that condition is clearly  
 24 satisfied, because the existence of the MIF hasn't led  
 25 to the elimination of competition in the payment systems

133

1 market. On the contrary, as we have seen from the  
 2 evidence, it is the critical driver of competition  
 3 between the payment system schemes.  
 4 If you are happy, that is a good -- sorry, I think  
 5 Mr Smith may have something.  
 6 MR SMITH: If it is a short answer then we can do it now.  
 7 Obviously we know your case on bilaterals, that they  
 8 wouldn't be agreed. But assuming that bilaterals could  
 9 be agreed, to what extent does the fact that they could  
 10 be agreed affect the four criteria for exemption,  
 11 insofar as they apply to a MIF?  
 12 MR HOSKINS: I think you can still -- the 101(3) case  
 13 remains as it is, insofar as you are satisfied that  
 14 a MIF creates more efficiencies. In the context we are  
 15 imagining, because we are back -- the counterfactual is  
 16 MasterCard here, Visa/Amex here, but because of pressure  
 17 on Visa and Amex they come down a bit. You have still  
 18 got MasterCard there, and we say when you are looking at  
 19 efficiencies, MasterCard with a MIF here can still  
 20 satisfy the four conditions. Because that scheme, we  
 21 say, creates more benefits than the bilateral scheme.  
 22 Because the bilateral scheme you are looking at to say:  
 23 can the MasterCard system function at all without a MIF?  
 24 And the answer may be: yes, but with bilaterals.  
 25 That doesn't exclude the fact that even if it could

134

1 function with bilaterals, if it is functioning with  
 2 a MIF, it will create more efficiencies than it would if  
 3 it were functioning with bilaterals.  
 4 MR SMITH: Would those efficiencies be confined to the  
 5 transaction costs of negotiated bilaterals or would they  
 6 be more? In a sense it depends on the level of the  
 7 bilateral interchange fee agreed, doesn't it?  
 8 MR HOSKINS: That is right. On your analysis, what we  
 9 discussed this morning was MasterCard there, and Visa  
 10 and Amex coming down. So by definition, given that Visa  
 11 is at the actual level of the MIF, in the counterfactual  
 12 we were discussing this morning it is coming down below.  
 13 But if you accept the submissions I have just made,  
 14 which is the higher MIF, the more the advantages, then  
 15 this is a true 101(3).  
 16 What I have been looking at in -- it comes back to  
 17 your point about --  
 18 MR JUSTICE BARLING: In a bilateral wouldn't the zero be  
 19 coming up?  
 20 MR HOSKINS: It is possible. That is part of the point  
 21 I put to you. It is difficult to know whether that  
 22 happens or --  
 23 MR JUSTICE BARLING: Or A bit of both.  
 24 MR HOSKINS: On the point you were putting to me it is more  
 25 Visa coming down. MasterCard might come back up, but

135

1 what's not going to happen I think in your  
 2 counterfactual -- I would be delighted if it were and  
 3 I will explain why -- if the counterfactual is Visa are  
 4 there and MasterCard comes back up, there is no loss  
 5 suffered. You don't get into exemption.  
 6 MR JUSTICE BARLING: That's your fallback. I think it  
 7 appears somewhere in your submissions.  
 8 MR HOSKINS: It does. Beyond exemption, if the  
 9 counterfactual the Tribunal adopts is that MasterCard is  
 10 saved, because, for example, acquirers pay enough money  
 11 to keep it alive, then in that counterfactual  
 12 Sainsbury's suffers no or very little loss.  
 13 MR SMITH: Yes. It would depend on quite how much of the  
 14 bilateral was negotiated in which direction.  
 15 MR HOSKINS: Absolutely.  
 16 MR SMITH: In a sense, though, I think you are accepting  
 17 then that the factors that go to the exemptibility of  
 18 the MIF might turn -- and I appreciate I'm asking you to  
 19 assume that bilaterals would be agreed -- but might turn  
 20 on the level of the bilateral agreement.  
 21 MR HOSKINS: The oddity with 101(3) is, and I think the way  
 22 the guidelines are framed, it is not the same sort of  
 23 counterfactual exercise we did for ancillary  
 24 restriction. They tend to talk about benefits with or  
 25 without the restriction.

136

1 I need to go back and refresh my memory, but from  
 2 memory you don't get that sort of debate within, for  
 3 example, the exemption guidelines about needing to  
 4 identify a counterfactual in the same way you do. It  
 5 does seem to be more a sort of crude approach in some  
 6 respects, which is look at the system with or without  
 7 the measure that has been found to be a restriction,  
 8 rather than look at it with or without restriction, and  
 9 look at what the actual counterfactual would have been.  
 10 I could be wrong about that, but that's my  
 11 recollection.  
 12 MR SMITH: I suppose what I was getting at was looking at  
 13 a number of the benefits that you have articulated going  
 14 to merchants as a result of a credit card scheme, they  
 15 need to be funded, but in a sense those benefits accrue  
 16 whether they are funded by a multilaterally imposed  
 17 interchange fee or a bilaterally agreed interchange fee,  
 18 assuming those two to be the same.  
 19 MR HOSKINS: My point is they are always going to get more  
 20 benefits with the higher MIF, because you will have more  
 21 cardholders. Because the higher the MIF, the more the  
 22 rewards. That is what we are told. The more rewards,  
 23 the more cardholders. The more cardholders, the more  
 24 purchasers and the retailers using credit cards. We  
 25 know, for example, average spend on a credit card is

137

1 higher than a debit card, etc. The more cardholders,  
 2 the more transactions in which the merchant gets the  
 3 money earlier. The more cardholders, the more  
 4 transactions in which the merchant gets money he  
 5 wouldn't have got at all because the cardholder turned  
 6 out not to have the money to pay for it, etc.  
 7 It is not binary in that sense. It is the whole  
 8 thing creates more cardholders, which is good for  
 9 merchants. Because the more people come into their  
 10 shops and buy things, the better for merchants.  
 11 MR SMITH: Right. I appreciate you would say there's no  
 12 loss in this case, but I think what you are saying is  
 13 that even if the bilaterally agreed interchange fee was  
 14 at the level of the MIF imposed during the claim period,  
 15 a higher MIF could still be exempted.  
 16 MR HOSKINS: If the bilateral was at the actual -- yes,  
 17 that's possible.  
 18 MR JUSTICE BARLING: I'm afraid I don't quite follow you,  
 19 because all the benefits you just referred to could be  
 20 available if bilaterals are in place --  
 21 MR HOSKINS: It depends on the level --  
 22 PROFESSOR JOHN BEATH: Generally, they are called the  
 23 interchange fee. We don't use this word "MIF", it is  
 24 just whatever the price is agreed --  
 25 MR HOSKINS: Yes. The higher the interchange fee, the more

138

1 the benefits.  
 2 PROFESSOR JOHN BEATH: Yes.  
 3 MR JUSTICE BARLING: So subject to your damages point --  
 4 I mean there are no efficiencies, are there, or no  
 5 significant ones that you have outlined --  
 6 MR HOSKINS: Because of it being a default.  
 7 MR JUSTICE BARLING: A MIF rather than an interchange fee.  
 8 PROFESSOR JOHN BEATH: A MIF rather than a BIF.  
 9 MR HOSKINS: No, there would be some transaction costs. But  
 10 my point, as I fought tooth and nail this morning, is  
 11 a bilateral interchange fee wouldn't be at the level of  
 12 the MIF. If it were at the level of the MIF, you don't  
 13 get into 101(3), because Sainsbury's won't have suffered  
 14 any loss.  
 15 MR SMITH: I quite see that. What I was trying to unpack  
 16 was the point you were making about the benefits  
 17 increasing as the interchange fee increases, and  
 18 I wanted to test that by asking you to suppose  
 19 a bilateral at the level of the MIF --  
 20 MR HOSKINS: It is Professor Beath's point. It is the  
 21 higher the interchange fee, the more you get these  
 22 benefits.  
 23 MR SMITH: Subject to your point about an absolute limit,  
 24 which is when the merchants say, "This is just too much,  
 25 we are not going to pay".

139

1 MR HOSKINS: We are going to come onto the tests which have  
 2 been applied to try to identify, rather than actually  
 3 just in practice squeezing merchants until they break,  
 4 you have the adjusted cost benefit analysis, you have  
 5 the MIT-MIF. That is an attempt. That's what has been  
 6 done by the Commission, by the EU legislature and the  
 7 regulation etc. That is their attempt to come up with  
 8 an answer to the indispensability question of how much  
 9 MIF or how much -- in the EU analysis we had how much  
 10 interchange fee, but for 101(3) the question is how much  
 11 MIF?  
 12 MR JUSTICE BARLING: We will have a short break.  
 13 (3.20 pm)  
 14 (A short break)  
 15 (3.30 pm)  
 16 MR HOSKINS: I will pick it up at page 88 of the closings.  
 17 MR JUSTICE BARLING: Yes.  
 18 MR HOSKINS: I describe at 264 the crucial question is then  
 19 what level of MIF satisfies the indispensability  
 20 criterion? That is what we pick up at 267 onwards.  
 21 There are, of course, two relevant methodologies,  
 22 basic methodologies, before you. There are variations  
 23 within them. As we say at 267, both the expert  
 24 economists agree, and this is a quote from the joint  
 25 experts' statement:

140

1 "A UK MIF based on the merchant indifference test  
 2 (MIT), if applied properly, [there is the heavy words]  
 3 satisfies the exemption conditions."  
 4 That is one approach. Certainly what we would be  
 5 encouraging you to do is to follow through the MIT  
 6 methodology -- obviously we would say we are the proper  
 7 one -- and take a view on where that comes out. But  
 8 then equally you have the adjusted cost benefit, the  
 9 adjusted cost methodology which Dr Niels prefers and  
 10 which Mr von Hinten-Reed has accepted is a useful  
 11 cross-check. He plainly says do that because then --  
 12 there is no right answer here. People have been, you  
 13 know, suffering for years trying to come up with the  
 14 exemptible level, and what people have come up with,  
 15 through experience, is, well, there's this way, there is  
 16 the MIT way, there is a cost base way, but there's no  
 17 reason why you can't do both, take a view on both, and  
 18 then take your broad axe and give them a good whack to  
 19 come up with a good figure. I'm sorry it is not very  
 20 scientific but that may well be where we are.  
 21 Let me go through the two of them and say how we  
 22 think they should be applied. This is paragraph 270  
 23 onwards. I'm dealing with the MIT-MIF.  
 24 As we know, the Commission has on a number of  
 25 occasions applied a MIT methodology but never to

141

1 establish a UK domestic MIF.  
 2 We have set out at 271 when they have done it. Part  
 3 of the problem is most of the time the Commission has  
 4 done it, it has been on the basis of the Central Bank  
 5 studies, which I think nobody wants to go near anymore  
 6 because I think everyone accepts they are not fit for  
 7 purpose. Equally, the Commission, it seems fairly  
 8 clear, has been applying the 2008 Rochet and Tirole  
 9 tourist test which, as we know, Rochet has now said  
 10 isn't suitable for credit cards.  
 11 We say, clearly, that's there's problems with what  
 12 the Commission has been doing.  
 13 Even the regulation -- this is at 272 -- the  
 14 regulation is at actually based on Central Bank studies,  
 15 not Deloitte's. So one can't just go and say 0.3,  
 16 because really -- it is legislation, so they can do  
 17 that, but in terms of this court, looking back and  
 18 saying what was the exemptible level during the claim  
 19 period, that's really not acceptable because it is  
 20 Central Bank territory.  
 21 The Commission, to be fair, has made it clear that  
 22 national authorities aren't bound to follow its previous  
 23 attempts. We have set this out at 273. There is  
 24 actually a flaw in the quote at 273(a), it has been  
 25 truncated and the important bit has been left off.

142

1 I will dictate it and you can look it up afterwards.  
 2 Recital 50 of the 2014 Visa decision says:  
 3 "Domestic MIF rates set by local Visa Europe members  
 4 are not covered by the scope of these proceedings.  
 5 Therefore, the Commission is not in a position to demand  
 6 commitments on those rates."  
 7 If you put dot, dot, dot:  
 8 "In addition, national competition authorities or  
 9 national courts are well-placed to assess MIFs set by  
 10 local members domestically."  
 11 In addition, national competition authorities or  
 12 national courts are well-placed to assess MIFs set by  
 13 local members domestically.  
 14 MR JUSTICE BARLING: Thank you.  
 15 MR HOSKINS: Equally, over the page, in the 2015 survey, I  
 16 showed you passages in opening, it says it is intended  
 17 to serve as a basis for debate and further research, and  
 18 the survey is merely an attempt to consistently apply  
 19 the MIT.  
 20 Again, a green light to you or anyone else in your  
 21 position to actually take the matter forward, to take  
 22 the learning forward.  
 23 So when one looks at what the Commission has done,  
 24 flashing light, it is 2008 Rochet and Tirole, which  
 25 Rochet says is not suitable for credit cards, and

143

1 Central Bank studies generally, except for 2015.  
 2 275, the Rochet and Tirole article. You have the  
 3 problem, the article makes it clear on its face that the  
 4 test discussed therein does not provide a comprehensive  
 5 test for the calculation of acceptable MIFs, and it  
 6 would suggest suboptimal results from the point of view  
 7 of social welfare.  
 8 The way I say that the law on the second condition  
 9 interacts with this is if you show that merchants are no  
 10 worse off, so that is the second condition test, so the  
 11 benefits they receive means they are no worse off in  
 12 a position with the MIF than absent the MIF, then you  
 13 are into 101(3). As long as the benefits that merchants  
 14 get is enough to make them neutral -- I actually say it  
 15 takes them way beyond that, there are actually far more  
 16 benefits, and cardholders are also taken into account --  
 17 when you are actually coming to assess what the  
 18 exemptible level of the MIF would be, you can and should  
 19 take account of social welfare as well. Because that is  
 20 what the guidelines tell us, that competition law is  
 21 concerned not just with the benefit to merchants and the  
 22 benefit to cardholders, but also with social welfare.  
 23 But in order to get into 101(3) you have to show  
 24 that merchants benefit enough.  
 25 MR JUSTICE BARLING: You accept that, do you? Sorry, this

144

1 might be just reiterating something you already made  
 2 plain, but you do accept that when applying the "no  
 3 worse off" part of the second criterion, we need only  
 4 look at merchants? We are not looking, at that stage --  
 5 you accept that the cardholders are not the people, we  
 6 don't include them in the people who must be --  
 7 MR HOSKINS: No, I think it is a necessary condition that  
 8 merchants have to be no worse off.  
 9 MR JUSTICE BARLING: Yes.  
 10 MR HOSKINS: When you are looking at fair share, you are  
 11 looking at --  
 12 MR JUSTICE BARLING: Both.  
 13 MR HOSKINS: -- both sides.  
 14 MR JUSTICE BARLING: You say both for fair share.  
 15 MR HOSKINS: I'm not sure that the case law is absolutely  
 16 clear as to whether -- I don't think it deals with the  
 17 position if merchants are below or slightly worse off,  
 18 but cardholders above. I'm not sure the case law  
 19 actually nails that.  
 20 MR JUSTICE BARLING: Because Mr Brealey said that "no worse  
 21 off" only applied to the merchants' side, I think.  
 22 MR HOSKINS: It is a sort of necessary trigger.  
 23 MR JUSTICE BARLING: We needn't worry about anything else.  
 24 But -- and you agree with that, I think.  
 25 MR HOSKINS: For the second condition?

145

1 MR JUSTICE BARLING: Yes.  
 2 MR HOSKINS: Fair share. Yes. But then you are taking  
 3 account of all the benefits when you are looking at the  
 4 first condition.  
 5 MR JUSTICE BARLING: Yes, for merchants.  
 6 MR SMITH: As you said, it might be difficult if on one side  
 7 there was a disbenefit and on the other side there was  
 8 a benefit, and the law may be unclear here, but here you  
 9 are saying that cardholders benefit and merchants  
 10 benefit.  
 11 MR HOSKINS: That's my case, yes.  
 12 MR SMITH: And in a sense the cardholder case isn't really  
 13 being heard here, because no one is saying they don't  
 14 benefit.  
 15 MR HOSKINS: Yes.  
 16 MR SMITH: It is really a question of the merchant benefit  
 17 and whether it is a fair share and so on.  
 18 MR HOSKINS: Yes.  
 19 MR SMITH: In a sense, although they are part of the  
 20 equation, they are a rather silent part for the purposes  
 21 of today.  
 22 MR HOSKINS: Particularly when you come to set what the  
 23 exemptible level of MIF is, you have to take account of  
 24 the benefits to cardholders and merchants. They are  
 25 both relevant.

146

1 MR JUSTICE BARLING: It is a strange paraphrase --  
 2 MR HOSKINS: That's why you talk about it as a trigger. If  
 3 merchants are no worse off, that doesn't mean that is  
 4 the end of the equation, when you are looking at the MIF  
 5 you are just looking at benefits to merchants. You are  
 6 looking, I say -- as long as that trigger is satisfied,  
 7 you are trying to get a MIF that gives the benefits to  
 8 merchants and the benefits to cardholders, and indeed  
 9 which promotes social welfare. Once you are through  
 10 that gateway.  
 11 MR SMITH: It is a peculiarity not so much of two-sided  
 12 markets but of the fact that the MIF or the interchange  
 13 fee is the pivot or the price in two markets.  
 14 MR HOSKINS: It is, yes.  
 15 MR SMITH: For that reason, you draw in not a single market,  
 16 you don't study a single market, you look at both sides  
 17 of the pivot.  
 18 MR HOSKINS: That's what the Court of Justice Tells us, yes.  
 19 MR JUSTICE BARLING: Thank you.  
 20 MR HOSKINS: Do you want me to go back to the case law on  
 21 that?  
 22 MR SMITH: No.  
 23 MR HOSKINS: So that is Rochet and Tirole which on its own  
 24 face says doesn't take account, will be suboptimal for  
 25 social welfare and you have the submission this is 278

147

1 I took you to the exemption guidelines which clearly  
 2 refer to social welfare as being one of the objectives  
 3 of competition law. I was trying to think of another  
 4 example which makes it here that competition law is  
 5 concerned with social welfare and not just the position  
 6 of individual parties.  
 7 It is the GlaxoSmithKline I think is quite a good  
 8 example. This is done on the hoof, so I don't have the  
 9 reference for it. It is a well-known case.  
 10 GlaxoSmithKline established or stated the principle,  
 11 which has been stated a number of times, that EU  
 12 competition law protects the process of competition, not  
 13 individual competitors.  
 14 MR JUSTICE BARLING: Yes.  
 15 MR HOSKINS: That seems to me quite a good example to show  
 16 that you are not just looking at, for example,  
 17 merchants, it is a much broader scope. But, yes, for  
 18 fair share merchants have to get enough of the benefit  
 19 for 101(3) to be opened up, but once the gateway is  
 20 opened up, you are looking at the benefits that a MIF  
 21 creates for merchants and cardholders and social  
 22 welfare.  
 23 We then move on to 280, because the Rochet and  
 24 Wright article, it was published twice, so it is 2009  
 25 and 2010, but it is the same article. You have the

148

1 point, I took you to it in opening, that  
2 Professor Rochet has said that his tourist test in 2008,  
3 yes for debit cards, but no for credit cards. Precisely  
4 because of the sorts of benefits that we have been  
5 discussing, and we set out the quotes from 281. I have  
6 taken you to them and we have set them out again. But  
7 credit has a benefit for merchants and therefore that  
8 should be taken into account.

9 Interestingly, this is at page 94 at (c), this is  
10 a summary of what's concluded but what the Rochet and  
11 Wright article concludes is that:

12 "As a result, a conservative regulatory approach  
13 would be to cap interchange fees for credit cards based  
14 on retailers' net avoided costs from not having to  
15 provide credit themselves, and that using issuer costs  
16 to regulate interchange fees is only likely to give  
17 a lower bound of possible interchange fees."

18 We say that's very important because, of course, we  
19 come on to do our costs analysis. But what Rochet and  
20 Wright tells us is that that's actually the lower bound  
21 for credit cards.

22 Then we come onto the MIT-MIF and, as you know,  
23 there are various differences between the experts about  
24 how it should be applied. This is 282 of the closing.

25 The first point is that Dr Niels says that the costs

149

1 data used to calculate the MIT-MIF should be based on  
2 the Commission's econometric models, long run  
3 econometric models, not its medium term calculation,  
4 which is what Mr von Hinten-Reed prefers, and Dr Niels  
5 says that is for two reasons. First, because it takes  
6 proper account of all costs which may vary over time,  
7 and equally, it avoids the need to rely on the  
8 merchant's own subjective costs allocations.

9 I will develop these. Those are the two reasons he  
10 said he prefers econometric to the medium term data.

11 The second point of difference between the experts  
12 is this question: the Commission survey only had data  
13 for category 6 to 8, the large merchants, what should  
14 you do about that to get to the average merchant?

15 The third point really has two in it, which is that  
16 cash, according to Dr Niels, isn't an appropriate  
17 comparator both for face-to-face transactions that will  
18 only take place if credit is available, and also for  
19 online purchases. He says, well, it is not fair to look  
20 at cash because that's not a real comparator, and that  
21 is the dispute.

22 So, first of all, the econometric model against the  
23 medium term model. I say that gives rise to two issues;  
24 taking account of all costs that vary over time, and the  
25 relying on the merchants' own subjective data.

150

1 First of all, costs that vary over the longer term.  
2 Obvious stuff. Whether a cost is fixed or variable  
3 depends on the timeframe considered in the analysis.  
4 Paragraph 286. At 289, some costs may vary over  
5 a longer period, because merchants can alter the scale  
6 of their payment processing operations if they are  
7 concluding more card and less cash transactions.

8 We gave some examples, and Mr von Hinten-Reed  
9 accepted that these were examples of costs that could  
10 vary over a longer than his medium term period.

11 Rysman and Wright at 291, they raised this point and  
12 they say in reality there are some lumpy costs -- very  
13 technical language, I can understand that sort of  
14 thing -- so things that might shift over a longer  
15 period. Again, Mr von Hinten-Reed accepted that such  
16 lumpy costs exist and are not taken into account by his  
17 medium-term approach.

18 I'm worried you are going to pick me up on the  
19 terminology.

20 PROFESSOR JOHN BEATH: It is just that if you do look at  
21 econometric analysis of total costs against the scale of  
22 an operation, what it does allow you to do is to test  
23 for economies of scale, which a kind of survey data  
24 can't possibly explore. So it adds a dimension which  
25 may be quite important, especially when you are thinking

151

1 about the average transaction or the average merchant,  
2 trying to identify what is the proportion of fixed and  
3 variable costs for that average merchant.

4 MR HOSKINS: Yes, Dr Niels has put forward various reasons.

5 I am sure he would agree with that one as well.

6 PROFESSOR JOHN BEATH: Lumpiness gives rise to economies of  
7 scale.

8 MR HOSKINS: I knew I would get into trouble --

9 PROFESSOR JOHN BEATH: No, no --

10 MR HOSKINS: I'm happy to adopt that.

11 293, again Mr von Hinten-Reed accepted if costs are  
12 classified as fixed rather than variable, that leads to  
13 a lower MIF. So you see the way this problem is  
14 arising. We say, therefore, it is obvious from what  
15 Mr von Hinten-Reed has said that a MIT-MIF calculated on  
16 the basis of the medium-term approach will produce  
17 a result which is too low. That is at 294.

18 That is the first reason for preferring the  
19 long-term approach.

20 The second one is it avoids relying on the  
21 merchant's own categorisation. 295, the point was made  
22 that the task of characterising costs as fixed or  
23 variable isn't straightforward. I think it is common  
24 ground that if you leave it to the finance departments  
25 of retailers, they are probably going to struggle,

152

1 because it is not the sort of thing they normally do.  
 2 Yes, they are absolutely dealing with costs all day, but  
 3 not analysing whether they are fixed or variable.  
 4 You see that, what the Commission said itself, 295,  
 5 it is the quote from paragraph 13 of its own survey.  
 6 Econometric techniques are capable of identifying fixed  
 7 and variable costs without relying on a merchant's view.  
 8 That is why we go there.  
 9 But is this really a problem? Let's look at the  
 10 extent to which relying on merchants' views would  
 11 actually be something to be concerned about.  
 12 296, the survey. One cannot entirely rely on  
 13 potential self-selection bias.  
 14 At 297, as we see, the split is crucial for the  
 15 determination of an application of the MIT.  
 16 298, if it is fixed rather than variable you get  
 17 a lower MIF.  
 18 At 299 it is the point again, it is challenging for  
 19 retailers or merchants' finance departments, it is not  
 20 what they normally do.  
 21 We have the answers from Mr von Hinten-Reed at 300.  
 22 This was really quite striking, because he had, of  
 23 course, been shown, as we discovered during the course  
 24 of cross-examination, Sainsbury's own response or  
 25 proposed response to the Deloitte's survey. What he

153

1 said at 300(c), in Mr von Hinten-Reed's view:  
 2 "Sainsbury's response to the survey was horribly  
 3 wrong. Horribly."  
 4 Then (d):  
 5 "I should state categorically I was asked whether  
 6 they should send this submission in and I said no,  
 7 because I was not happy about some of the supporting  
 8 evidence."  
 9 (e) Sainsbury's had submitted its response to the  
 10 Deloitte's survey even after Mr von Hinten-Reed had told  
 11 them it was not fit for purpose.  
 12 You will see the exchange, sir, with yourself. The  
 13 point is simply this one: if even a large and  
 14 well-resourced company like Sainsbury's submitted  
 15 an assessment of its fixed and variable costs that was  
 16 horribly wrong and not fit for purpose, it is highly  
 17 likely that many other merchants would have done the  
 18 same.  
 19 It is not a great advert for relying on the  
 20 merchants' own data. Because Mr von Hinten-Reed looked  
 21 at the Sainsbury's submissions and said: it is rubbish,  
 22 you shouldn't send it in.  
 23 Paragraph 302, there's also the clear problem,  
 24 a risk of bias, that the merchants that participated in  
 25 the Deloitte's survey were told of the purpose of the

154

1 survey, and Mr von Hinten-Reed very fairly accepted,  
 2 well, that gives rise to a risk of bias. It clearly  
 3 does.  
 4 There is no need for us to allege that Sainsbury's  
 5 was biased. I'm not going to put anyone in that  
 6 difficult position. We don't have to. I didn't  
 7 question on that basis. All I need to do is make the  
 8 point that clearly there was a risk of bias.  
 9 Sainsbury's, we make no allegation about that, but it is  
 10 obvious that there is a real risk, in the way the survey  
 11 was set up, of bias of other people.  
 12 303, sixth point, you remember what  
 13 Mr von Hinten-Reed said he did, because he thought the  
 14 Sainsbury's assessment was rubbish, so he did his own.  
 15 He went to the costs and did his own categorisation of  
 16 the costs as fixed or variable. The problem with that  
 17 is twofold; you are then relying on a data sample of  
 18 one, rather than a hundred-odd, and Sainsbury's is one  
 19 of the largest merchants in the UK and it is not going  
 20 to be representative of the average merchant. I will  
 21 come onto that in more detail. But really, to say  
 22 "Sainsbury's was rubbish, so I have looked at it and I'm  
 23 going to rely on this as a sample of one" is clearly  
 24 unsatisfactory.  
 25 304, Mr von Hinten-Reed made the point, he said,

155

1 "Econometric estimation requires assumptions to be made  
 2 based on subjective judgment".  
 3 Of course, remember what we are talking about is  
 4 the Commission carrying out an econometric analysis, and  
 5 it is very unlikely that the Commission will have been  
 6 biased to try to produce or even subconsciously trying  
 7 to produce a higher MIF, given the way it has been  
 8 behaving over the last decade. So of course econometric  
 9 analysis requires judgment, but the Commission, you can  
 10 assume, will have been doing at the very least a neutral  
 11 job to produce a MIF that was accurate.  
 12 What Mr Brealey says is there are all these problems  
 13 with Dr Niels. We are not saying Dr Niels is perfect.  
 14 Dr Niels doesn't say Dr Niels is perfect. But we are in  
 15 imperfect world and you have a choice between these two  
 16 things. You have an econometric model, which does take  
 17 account of costs which vary over the longer term. You  
 18 have an econometric model which avoids the obvious  
 19 problems of relying on merchants' own categorisation of  
 20 costs as fixed or variable.  
 21 Our submission is it is pretty obvious, in that  
 22 scenario, which the preferable route is, because what  
 23 Mr von Hinten-Reed offers you is his sample of one,  
 24 "I have gone off and looked at the Sainsbury's data".  
 25 You are looking at -- whether you call it the average

156



1 transaction or average merchant, to base it on a sample  
 2 of one is absolutely hopeless.  
 3 The second point is what do you do about the fact  
 4 that the 2015 Commission survey only included large  
 5 merchants, categories 6 to 8? Mr Brealey took you --  
 6 this is 307 of our closings -- to the eight classes. We  
 7 have got data for 6 to 8 but nothing more.  
 8 What we know from the Commission's survey, we set it  
 9 out at 308, the Commission's survey recognises, this is  
 10 the last couple of lines of paragraph 4:  
 11 "... it is a trade off between precision of data and  
 12 sample size and representativeness."  
 13 Paragraph 23:  
 14 "The Commission therefore considers [this is at the  
 15 bottom of 23] that without further data from small  
 16 merchants it is not possible to draw reliable  
 17 conclusions from the study concerning the level of  
 18 indifference of all merchants."  
 19 That is the Commission saying that. 26:  
 20 "Collecting data from small merchants proved to be  
 21 a difficult task, while using data from large merchants  
 22 to approximate the cost of small merchants is  
 23 a questionable exercise."  
 24 That is the Commission's view. Again,  
 25 Mr von Hinten-Reed accepted that in cross-examination.

157

1 We have set it out at 309. Again, does it matter if we  
 2 just take 6 to 8? Does it really matter? It does  
 3 matter. Because it is quite clear from the evidence  
 4 that if you base your analysis on the data for classes 6  
 5 to 8, you will get a result, a MIT-MIF, which is too  
 6 low. I say that for the following reasons.  
 7 First of all, 311, the relative costs of payment  
 8 methods will vary depending on the size of the merchant.  
 9 The Commission itself again recognised merchant  
 10 heterogeneity. At 311(b) the wrong quote is set out, so  
 11 if you can strike that through. I will show you what he  
 12 actually said. It is at transcript Day 13, page 126.  
 13 The actual reference should be to T13, page 126.  
 14 PROFESSOR JOHN BEATH: At lines 4 to 10?  
 15 MR HOSKINS: 4 to 24:  
 16 "Question: Do you agree that one of the factors  
 17 that may have an impact on costs is the size of the  
 18 merchant?  
 19 "Answer: Yes.  
 20 Then dropping down to 21:  
 21 "Question: Do you agree that large retail firms  
 22 will tend to have lower costs in accepting cash due to  
 23 economies of scale?  
 24 "Answer: Yes."  
 25 MR JUSTICE BARLING: That is what should have been in

158

1 paragraph (b)?  
 2 MR HOSKINS: That is correct. T13, page 126. If one goes  
 3 to paragraph 312 of the closing, larger merchants are  
 4 likely to have lower costs in accepting cash due to  
 5 economies of scale. We have just seen  
 6 Mr von Hinten-Reed accept that. It is also in Rysman  
 7 and Wright, and then we give the proper reference to  
 8 lines 21 to 24.  
 9 If you pick it up at 313 of the closing, we say  
 10 relying solely on data in relation to large merchants is  
 11 therefore likely to lead to a MIT-MIF which is too low.  
 12 One gets that from Rochet and Tirole. Merchants are  
 13 heterogeneous, and IF that properly guides cardholders'  
 14 decisions must reflect the average, not the marginal  
 15 merchant benefit. This implies that the merchants who  
 16 benefit least from the card, say the large retailers,  
 17 are likely to fail the tourist test at the social  
 18 optimum, ie you get a MIT-MIF that is just too low if  
 19 you base it solely upon large retailers. Again,  
 20 Mr von Hinten-Reed agreed with that statement from  
 21 Rochet and Tirole in cross-examination.  
 22 MR JUSTICE BARLING: I hadn't spotted that. Why do they  
 23 benefit of use from the card? It probably doesn't  
 24 matter.  
 25 MR HOSKINS: It does matter. I'm going fast because it's

159

1 late in the day but I'm probably going too fast, as it  
 2 is late in the day. If you back to 312, larger  
 3 merchants are likely to have lower costs in accepting  
 4 cash due to economies of scale.  
 5 MR JUSTICE BARLING: I see. They benefit least from the  
 6 card because of the comparison --  
 7 MR HOSKINS: Exactly.  
 8 MR JUSTICE BARLING: But then someone else says they're both  
 9 likely to --  
 10 MR HOSKINS: No, what the Commission says is it is not clear  
 11 that will be the case, because they --  
 12 MR JUSTICE BARLING: They are both likely --  
 13 MR HOSKINS: I'm about to take you to the evidence that will  
 14 demonstrate that in fact it is clear that there is  
 15 a major difference, on the basis of the evidence,  
 16 between the levels of MIFs or MSCs you get to if you  
 17 rely on the large merchant information and what you  
 18 would get to if you looked at the average merchant.  
 19 If I'm going too fast, obviously you will slow me  
 20 down.  
 21 I'm at page 105, paragraph 314. This is where we  
 22 get to the facts. 314, the fact that the MIT-MIF will  
 23 differ depending on the size of the merchant and will be  
 24 lower for larger merchants is confirmed by the  
 25 calculation set out in the Commission's survey.

160

1 We need to go to E3.10, tab 202, 4358. You see  
 2 there is a number of -- you see what it's doing at  
 3 paragraph 212:  
 4 "The tables below show the median in different  
 5 thresholds for the merchants service charge in both the  
 6 card-based and retail-based approach."  
 7 What's important is they calculate different MIT  
 8 MSCs on different bases for categories 6 to 7 and  
 9 category 8. You will see the sort of differential that  
 10 one comes up with, in particular it is 12(b) for us,  
 11 credit cards.  
 12 It doesn't really matter the detail of how they got  
 13 there. The point is they do an exercise which is  
 14 separate, MSC for categories 6 to 7 and get 0.4.2, and  
 15 they do the calculation for size A, the largest gets  
 16 0.14. That is a dramatic indication of how, if you are  
 17 relying on just larger merchants, you will get a MIT MSC  
 18 that is dramatically different and lower. We say  
 19 clearly too low for the average merchant.  
 20 So what do you do? The problem matters. So what do  
 21 you do to try and palliate the problem?  
 22 As you know, what Dr Niels has done is to say: well,  
 23 we have got categories 6, 7 and 8, the problem is we  
 24 don't have 1 to 5. Again, it is not perfect but I'm  
 25 more likely to get something approximating the right

161

1 answer by taking categories 6 and 7 and excluding 8.  
 2 It is a simple point. He says: if you have not got  
 3 the bottom half, I chop a bit off the top and I'm more  
 4 likely to get something that arrives at the average.  
 5 Mr von Hinten-Reed says: no, I'm going to take 6, 7  
 6 and 8. Which, as I hope I have demonstrated already,  
 7 will take you to a MIF that is going to be too low.  
 8 What Mr von Hinten-Reed did to try and justify his  
 9 approach, remember he said: I did this, I took 6, 7 and  
 10 8, but then I did the sensitivity analysis to show that  
 11 it is all right -- sorry, just using Sainsbury's data,  
 12 and then performed a sensitivity analysis. But  
 13 Sainsbury's is category 8, so it is even worse than  
 14 I described.  
 15 A number of problems with that. This is at 317 of  
 16 the closing. First of all, of course, again, you have  
 17 got Mr von Hinten-Reed relying on a sample of one, very  
 18 large, whilst Dr Niels has got a sample of 126  
 19 merchants.  
 20 You had Mr Brealey poking sticks into Dr Niels  
 21 saying, "This takes out a number of merchants in the  
 22 UK". Again, we are not saying it is perfect, but the  
 23 exercise here is not: how imperfect is Dr Niels? The  
 24 exercise for you is: which is the preferable approach,  
 25 Dr Niels or Mr von Hinten-Reed, in the world of

162

1 imperfection? So Dr Niels sample of 26 merchants in  
 2 categories 6 and 7. Mr von Hinten-Reed, sample of one  
 3 in category 8.  
 4 He then tries to justify it with his sensitivity  
 5 analysis. You remember that, in his report, he had  
 6 an assumption that smaller merchants would have  
 7 a MIT-MIF which was twice or three times higher than  
 8 large merchants, and in cross-examination he admitted he  
 9 had no evidential basis for taking two and three.  
 10 Q. What the data in the Commission survey shows is that  
 11 that sort of assumed differential, times two or times  
 12 three, was clearly unrealistic. I took him to the  
 13 survey. If we pick it up again, E3.10, tab 202, this  
 14 time at page 4351. You remember I took him to this in  
 15 cross-examination. This was a distribution of the  
 16 estimated MIF MSCs by the number of merchants.  
 17 This, by definition, is just within categories 6, 7  
 18 and 8, because that's all the Commission had. What  
 19 I did was I looked at the median of the most common MIT  
 20 MSC, which was 0 to 0.5, and I compared it with the  
 21 median of the other results in this category. I did it  
 22 in cross-examination but we set out the results in the  
 23 closing at page 107, because it gives you a sense of  
 24 what the differentials of MIT MSC are, even within the  
 25 category of large retailers.

163

1 You will see (ii):  
 2 "Around 15% of large merchants had a MIT MSC around  
 3 three times higher than the majority of large  
 4 merchants."  
 5 (iii):  
 6 "Around 6 to 7% of large merchants had a MIT MSC  
 7 around six times higher than the majority of large  
 8 merchants.  
 9 (iv):  
 10 "Around 5% of large merchants had a MIT MSC around  
 11 14 times higher than the majority of large merchants".  
 12 Then (v):  
 13 "Around 2% of large merchants had a MIT MSC at least  
 14 20 times higher."  
 15 That is the sort of spread one is getting just  
 16 within categories 6 to 8. You remember I took  
 17 Mr von Hinten-Reed through that, and he confirmed that  
 18 he would expect the disparity to be greater if one were  
 19 comparing the large retailers with the retailers in  
 20 categories 1 to 5. So he would expect a larger spread.  
 21 That is the top of page 108 at (c).  
 22 In our submission, it is quite possible, indeed  
 23 probable, that you are talking about differentials that  
 24 might be in the order of 20-odd, not certainly of 2  
 25 and 3.

164

1 So what Mr von Hinten-Reed was then -- go and do  
 2 another exercise and show us what would happen if you  
 3 take higher differentials. Oxera did the same exercise  
 4 and they have put their conclusions in appendix C  
 5 because again I think, from memory, Mr von Hinten-Reed's  
 6 goes no higher than times 7 in the one that he redid,  
 7 which is still nowhere near the ballpark spread we are  
 8 seeing from the Commission's own data. Oxera have done  
 9 it with higher factors including a factor of 10 and 20.

10 It is in appendix C to our closings but we  
 11 summarised the results at 321 and what it shows, I will  
 12 pick it up in the third line, this shows that with the  
 13 differential of times 20, which as I have shown is  
 14 perfectly possible and indeed probable, the MIT-MIF  
 15 would be 0.75 using the Commission's scenario 2, at  
 16 least 1.67 based on the Commission's scenario 3 and 0.86  
 17 even on Mr von Hinten-Reed's Sainsbury's based  
 18 calculation. The factor of 10, you get the equivalent  
 19 figure, 0.42, 0.94 and 0.49.

20 With respect to Mr von Hinten-Reed, his sensitivity  
 21 analysis just isn't worth the paper it is written on  
 22 because it is based on unrealistic assumptions and  
 23 that's also the case indeed for his updated one, which  
 24 only goes to times seven.

25 This is paragraph 322. Mr von Hinten-Reed sought to

165

1 defend his reliance on Sainsbury's, on using Sainsbury's  
 2 data only, ie a sample of one, by saying: well, typical  
 3 payment takes place at a large retailer, therefore it is  
 4 reasonable to assume that the MIT-MIF obtained by such a  
 5 large retailer would represent the large majority of UK  
 6 sales.

7 As we set out at 323 it is quite clear from the  
 8 Rochet and Tirole 2008 article, which Mr von Hinten-Reed  
 9 himself relies on, is what you are looking for is the  
 10 average merchant. So even within his own world that's  
 11 not really justification for a sample of one.

12 Therefore we say Mr von Hinten-Reed's suggested  
 13 approach is clearly unreliable, relying on Sainsbury's  
 14 sensitivity analysis, clearly unrealistic, and it will  
 15 lead to a MIT-MIF which is too low.

16 In Sainsbury's closing, at paragraph 319, they make  
 17 the point it would be unfair to impose a MIF that is too  
 18 high on the very large merchants. But that's dealt with  
 19 by the Shaw case that I showed you. You are not looking  
 20 at the effect on each individual merchant, you are  
 21 looking at the effect on the average merchant. For your  
 22 note the point made in Sainsbury's closing,  
 23 paragraph 319, is dealt with in our closing at  
 24 paragraph 240.

25 Again Dr Niels isn't saying that his approach is

166

1 perfect. But we say it is better, clearly better than  
 2 Mr von Hinten-Reed's and should be preferred. Then, the  
 3 final point of difference, which is: is it correct to  
 4 always use cash as the relevant comparator for this  
 5 calculation? First of all, online transactions. As  
 6 I already said, it is common ground that cash is  
 7 generally not a substitute for online transactions. So  
 8 if you are not using a four-party payment scheme credit  
 9 card, what are you using? What's available? It is Amex  
 10 and it is PayPal.

11 Again, it is not that we say it is perfect but the  
 12 problem you have got is that Mr von Hinten-Reed doesn't  
 13 take any account of online transactions, but yet it is  
 14 clear that the MIT-MIF is intended to apply to online  
 15 transactions and for all its advantages and  
 16 disadvantages. At least Dr Niels has taken account of  
 17 the fact that the MIT-MIF has to apply to online  
 18 transactions and that in online transactions cash is not  
 19 an appropriate comparator.

20 Again, you get this very sort of stark approach from  
 21 Mr von Hinten-Reed: I'm not doing anything, I'm not  
 22 taking any account of this fact. It is interesting that  
 23 what Mr von Hinten-Reed sort of criticises: well, why  
 24 does Dr Niels go to Amex and PayPal? The reason is  
 25 because those are the realistic alternatives for online

167

1 transactions. He doesn't suggest any other alternative  
 2 himself, he just ignores online transactions.

3 Again, we say neither is perfect, but Dr Niels is  
 4 clearly preferable. Then the final point between them  
 5 relates to this idea of increased sales resulting from  
 6 the availability of credit.

7 What we have seen is that there are certain face to  
 8 face credit card purchases that wouldn't take place  
 9 absent credit. So, for example, the worker who is  
 10 getting paid at the end of the week but wants to go for  
 11 a nice meal couldn't afford it unless he used credit.  
 12 Transactions where something is bought on credit and  
 13 then there is subsequently a default.

14 So there are, we submit, quite clearly categories  
 15 where transactions take place that wouldn't otherwise  
 16 take place if credit weren't available. Dr Niels takes  
 17 some account of them; Mr von Hinten-Reed takes no  
 18 account of them. We say Dr Niels is therefore clearly  
 19 preferable.

20 I think it is important to note, this is  
 21 paragraph 338, he applies a weighted approach to this.  
 22 So it is a nuanced approach. It may not be perfect but  
 23 there is some attempt at nuance. Whereas  
 24 Mr von Hinten-Reed is simply: no account.

25 For that basis we say, if you are going to -- and

168

1	you should -- I think it is worth looking at a MIF	1
2	approach -- but it should be with the proper approach,	2
3	the best approach is the one put forward by Dr Niels	3
4	rather than Mr von Hinten-Reed.	4
5	You will see the range that Dr Niels gets to,	5
6	paragraph 347. Subject to the sorts of debates we have	6
7	been having about whether you go to the lower or the	7
8	higher end of the range, for most of that range there is	8
9	then no overcharge because the comparison is between the	9
10	figures in 346A for credit cards and the range in 347.	10
11	MR JUSTICE BARLING: You won't have time to do the adjusted	11
12	cost benefit, if you are --	12
13	MR HOSKINS: I won't have time to finish it today.	13
14	MR JUSTICE BARLING: No. You have probably got another	14
15	5 minutes if you want?	15
16	MR HOSKINS: To be safe, I imagine we want to finish	16
17	tomorrow, and that includes Mr Brealey's reply. So what	17
18	I'm trying to do is get to a situation where I sit down	18
19	at lunchtime. I have got to finish this and I have got	19
20	to do pass-through and then we have got Mr Cook, who	20
21	will have slightly over ... I think we agreed	21
22	Mr Brealey would have an hour in reply --	22
23	MR JUSTICE BARLING: Would it be sensible if we sit earlier?	23
24	MR HOSKINS: I think if we could start at 10.00 we would be	24
25	safe. 9.30 is an awfully long day.	25

	INDEX	
		PAGE
	Closing submissions by MR HOSKINS .....	1

169

171

1 MR JUSTICE BARLING: I agree. We will sit at 10.00.  
2 MR HOSKINS: Then I will stop now and take this when we're  
3 fresh in the morning. Thank you.  
4 MR JUSTICE BARLING: Thank you.  
5 (4.25 pm)  
6 (The court adjourned until 10.00 am on  
7 Wednesday, 16th March 2016)

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19  
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21  
22  
23  
24  
25

170



146:1,5 147:1,19 148:14 158:25 159:22 160:5,8,12 169:11,14,23 170:1 170:4 <b>base (5)</b> 78:12 141:16 157:1 158:4 159:19 <b>based (19)</b> 12:23 19:21,24 33:3 38:14,15 39:7,21 40:13 73:13 124:17 141:1 142:14 149:13 150:1 156:2 165:16,17,22 <b>bases (1)</b> 161:8 <b>basic (1)</b> 140:22 <b>basically (2)</b> 66:10 75:21 <b>basis (27)</b> 4:14 6:10 7:6,10 19:12 22:20 22:19 24:19 29:19 48:7,8 58:5 62:15 80:23,25 81:7 88:18 98:21 99:20 104:15 142:4 143:17 152:16 155:7 160:15 163:9 168:25 <b>bear (2)</b> 6:24 46:10 <b>bears (1)</b> 102:23 <b>BEATH (14)</b> 41:16 42:4 42:12 69:6 105:1 108:8,11 138:22 139:2,8 151:20 152:6,9 158:14 <b>Beath's (1)</b> 139:20 <b>beauty (1)</b> 96:9 <b>beer (1)</b> 126:1 <b>begins (1)</b> 46:2 <b>behalf (1)</b> 64:22 <b>behaving (1)</b> 156:8 <b>behest (1)</b> 65:3 <b>Belge (2)</b> 109:24 110:20 <b>believe (3)</b> 103:18 116:16 119:12 <b>believed (1)</b> 116:21 <b>bench (1)</b> 102:19 <b>beneficial (4)</b> 68:6,9 110:6 123:20 <b>benefit (55)</b> 5:7,8 64:14,23 65:20 71:15 84:18,24 93:9 96:18 98:18 101:7 107:23 108:1 112:21 113:6,15 114:6,16 115:18 116:2,13 117:5,7 117:19,20 119:10 119:23 120:10,11 120:12,13 122:4 124:19 125:18 127:5 128:20,24 140:4 141:8 144:21 144:22,24 146:8,9 146:10,14,16 148:18 149:7 159:15,16,23 160:5 169:12 <b>benefit? (1)</b> 125:7 <b>benefits (77)</b> 2:18,21 3:4,6 84:13,21,21 87:7,15 108:19,25 109:5,8,10,15,21 112:11,13 113:2,7 113:12,14,17,25 114:24 115:1,14 116:15 117:2,16 119:12,18 120:3,21	120:21,22 121:11 125:19 126:7,13,15 126:22,23 128:8,17 129:15 130:4,7,9 130:11 131:3,7,9 131:22 132:1,7,19 133:15 134:21 136:24 137:13,15 137:20 138:19 139:1,16,22 144:11 144:13,16 146:3,24 147:5,7,8 148:20 149:4 <b>best (2)</b> 81:19 169:3 <b>better (12)</b> 5:9 37:19 58:6 65:21 76:13 89:12 91:2,18 131:20 138:10 167:1,1 <b>beyond (2)</b> 136:8 144:15 <b>bias (5)</b> 153:13 154:24 155:2,8,11 <b>biased (2)</b> 155:5 156:6 <b>BIF (1)</b> 139:8 <b>big (2)</b> 77:19 132:22 <b>bilateral (43)</b> 41:7,9 41:13,18,21 42:2,7 42:8 43:7 45:5,11 46:5,9,11,20,22 47:22,23,25 48:15 50:12 51:22 52:18 59:5,18,23 60:11 62:19 63:3,16 64:11 65:11 78:15 89:6 134:21,22 135:7,18 136:14,20 138:16 139:11,19 <b>bilaterally (5)</b> 45:16 45:19 65:14 137:17 138:13 <b>bilaterals (16)</b> 43:6 61:1,14 63:19,22 64:5 66:19 89:5 134:7,8,24 135:1,3 135:5 136:19 138:20 <b>billion (1)</b> 40:13 <b>billions (2)</b> 86:2,7 <b>binary (1)</b> 138:7 <b>bind (1)</b> 4:5 <b>Bingham (1)</b> 4:12 <b>bit (32)</b> 11:18 17:20 19:20 25:13 28:7 28:18 35:18 37:21 37:24 41:17 44:12 54:20 56:12,13 66:7 72:20 78:14 86:17 92:9,12 99:11 100:1 102:9 106:25 108:7 112:15 131:1 133:7 134:17 135:23 142:25 162:3 <b>black (2)</b> 57:24,25 <b>blue (14)</b> 43:10 45:10 45:24 46:7,10,12 46:15 47:18 49:2,5 49:8,10 50:4,7 <b>blunt (4)</b> 38:16 39:3,4 81:3 <b>board (2)</b> 32:6 72:5 <b>body (1)</b> 22:16 <b>bold (2)</b> 66:2 69:23 <b>bolstered (1)</b> 73:14 <b>book (1)</b> 47:2 <b>borne (2)</b> 8:16 21:16 <b>bottling (3)</b> 84:15,16 84:23	<b>bottom (8)</b> 14:20 31:2 35:14 67:20 69:22 70:9 157:15 162:3 <b>bought (1)</b> 168:12 <b>bound (6)</b> 5:13,15 37:5 142:22 149:17 149:20 <b>breach (2)</b> 44:4 95:3 <b>break (12)</b> 25:20 58:7 58:9,12,22 59:16 117:21 131:23 133:20 140:3,12,14 <b>breaking (1)</b> 131:11 <b>Brealey (28)</b> 5:18 7:3 7:14 16:1,3,18 17:8 18:20 19:2 44:16 58:14 59:9 67:4 92:22,22 93:21 97:4 99:3 107:9,11 110:23 111:6 120:15 145:20 156:12 157:5 162:20 169:22 <b>Brealey's (5)</b> 15:9 33:24 113:13 117:11 169:17 <b>brief (1)</b> 17:23 <b>briefly (2)</b> 16:5 107:7 <b>bright (1)</b> 30:19 <b>bring (11)</b> 8:20 18:17 21:2 28:4 33:5 66:19 67:9 83:23 89:14 96:15 106:20 <b>brings (2)</b> 52:21 133:15 <b>British (4)</b> 18:2 33:25 73:1 76:15 <b>broad (12)</b> 7:11,15 9:14 54:23 58:3 96:2,5 101:21 103:20,22 104:1 141:18 <b>broader (1)</b> 148:17 <b>brought (6)</b> 21:9 27:22 67:16 95:6 96:13 105:11 <b>build (2)</b> 1:7 53:13 <b>bullets (1)</b> 13:16 <b>bundle (6)</b> 14:16,17 14:19 26:7 68:18 85:11 <b>burden (14)</b> 93:5 98:25 100:17,24 102:17,23 104:10 104:12,16,19,24 106:2,21 108:5 <b>burdens (1)</b> 103:10 <b>business (8)</b> 26:2 27:14,15 40:18 73:25 124:21,25 127:7 <b>buy (3)</b> 71:6 115:20 138:10 <b>buys (1)</b> 47:1	<b>capable (1)</b> 153:6 <b>caps (2)</b> 31:21,22 <b>card (58)</b> 21:12 23:13 23:15 24:3,24 27:6 29:2,8,11,15,18,25 32:6,7 37:7,18 67:16 68:24 69:5 69:11 70:11,12,13 72:20 76:22 77:18 78:12,12,18,23 82:4 85:8 113:21 114:24 117:16,22 117:23,25 118:3,5 118:16,17,19 125:2 128:17,23 129:23 129:25 130:10 137:14,25 138:1 151:7 159:16,23 160:6 167:9 168:8 <b>card-based (6)</b> 29:4,5 29:6,16,19 161:6 <b>cardholder (8)</b> 61:23 62:12 117:24,25 118:2 119:23 138:5 146:12 <b>cardholder's (3)</b> 61:17 111:21 118:4 <b>cardholders (36)</b> 2:18 2:22 3:4 51:15,17 113:7 120:5,10,17 122:16 123:5,8 125:18,21 126:13 128:17,21 129:14 129:18 130:4,8 133:16 137:21,23 137:23 138:1,3,8 144:16,22 145:5,18 146:9,24 147:8 148:21 <b>cardholders' (1)</b> 159:13 <b>cards (83)</b> 12:25 31:24 37:6 40:12 42:10 42:19,23,25 51:1 64:14,24 67:6,7,8 68:2,4,6,6 69:16,24 70:3,5 71:4,7,15,16 71:16,21,22,23 72:15 73:15,21 75:4 76:3,9 91:7,9 91:13 113:6,15,20 114:8,10,11,12,17 114:20 115:2,9,9 115:15 116:16,19 116:22 117:3 119:3 119:14 120:11,17 120:18,21,25 122:5 122:6 128:16,22 129:5,10,12,24 130:12,15 131:25 137:24 142:10 143:25 149:3,3,13 149:21 161:11 169:10 <b>career (3)</b> 97:23 98:1 98:2 <b>careful (2)</b> 115:23 130:23 <b>carefully (1)</b> 27:25 <b>carried (2)</b> 21:6 83:7 <b>carry (3)</b> 70:18 77:10 86:20 <b>carrying (1)</b> 156:4 <b>cartel (14)</b> 95:10,11 95:13,15 96:4,6 99:5,8,23 100:7,8 100:10,12,15 <b>case (94)</b> 1:9,23 2:15 2:16,20 5:24 9:12	10:4,6,9 11:19,24 12:8,21 13:2 14:7 17:1,5,10 18:6 19:2 19:12 20:7 21:17 25:14 32:3 34:1,5 36:11 38:4 42:20 43:23 49:22 50:25 53:1 56:3,11,23 59:24 60:23,23 67:25 69:1 74:10 74:12 81:6,15,25 88:16 92:9 94:20 95:5 96:4,6,7 97:14 97:15,16 99:5,23 102:24 106:18,23 107:19,21 108:22 108:24 110:1,10 111:24 112:19 117:4 123:15 124:2 125:15,24 128:6,11 128:12 130:19 133:8,14 134:7,12 138:12 145:15,18 146:11,12 147:20 148:9 160:11 165:23 166:19 <b>cases (4)</b> 95:10 104:10 110:5 126:1 <b>cash (14)</b> 14:24 64:16 119:6,8 130:16 150:16,20 151:7 158:22 159:4 160:4 167:4,6,18 <b>CAT (1)</b> 18:1 <b>categorically (1)</b> 154:5 <b>categories (10)</b> 157:5 161:8,14,23 162:1 163:2,17 164:16,20 168:14 <b>categorisation (3)</b> 152:21 155:15 156:19 <b>category (6)</b> 150:13 161:9 162:13 163:3 163:21,25 <b>causa (1)</b> 2:12 <b>cause (1)</b> 96:16 <b>caused (1)</b> 121:12 <b>caveat (1)</b> 62:22 <b>ceased (1)</b> 68:1 <b>CEG (1)</b> 68:16 <b>ceiling (1)</b> 64:3 <b>Central (4)</b> 142:4,14 142:20 144:1 <b>centuries (1)</b> 114:4 <b>certain (11)</b> 1:25 27:24 28:1 39:15 60:19 93:22 94:15 98:6 99:18 121:25 168:7 <b>certainly (12)</b> 19:12 52:9 56:11 59:24 60:18 76:4 89:12 91:2,16,18 141:4 164:24 <b>chain (6)</b> 61:20 62:6 79:8 84:12,13 87:6 <b>chains (2)</b> 84:8,10 <b>Chairman (1)</b> 50:6 <b>challenged (2)</b> 10:12 12:24 <b>challenging (1)</b> 153:18 <b>chamber (1)</b> 82:24 <b>chance (8)</b> 96:7,12,14 96:14,17,21 97:9 98:13 <b>change (2)</b> 75:4 77:4 <b>changes (1)</b> 30:12 <b>Chaplin (1)</b> 97:8	<b>chapter (3)</b> 29:16 44:19 60:24 <b>character (1)</b> 112:4 <b>characterisation (1)</b> 106:8 <b>characterised (1)</b> 106:9 <b>characterising (1)</b> 152:22 <b>charge (8)</b> 40:12 41:14 47:14 61:11 66:8 78:10 118:16 161:5 <b>charged (5)</b> 25:24 44:2 100:3,7,10 <b>charges (1)</b> 68:16 <b>charging (1)</b> 61:13 <b>check (4)</b> 24:13,14 84:7 86:3 <b>cheques (1)</b> 130:17 <b>chimes (1)</b> 4:10 <b>choice (4)</b> 22:2,5 23:8 156:15 <b>choose (1)</b> 23:14 <b>chooses (1)</b> 84:6 <b>chop (1)</b> 162:3 <b>chose (2)</b> 23:15 26:18 <b>circle (2)</b> 120:15,16 <b>circumstance (1)</b> 102:2 <b>civil (2)</b> 102:11,13 <b>CJEU (2)</b> 14:22 110:2 <b>claim (25)</b> 20:12,19 25:16,21 27:11 28:9,13,18 30:4,5 30:19,24 33:5,10 35:13 40:11 48:6 56:20 69:22 93:10 93:19 96:23 115:24 138:14 142:18 <b>claimant (10)</b> 93:13 93:15 95:6,16 99:5 100:11,14,18 101:7 103:23 <b>claimed (2)</b> 107:15,21 <b>claiming (1)</b> 107:23 <b>claims (1)</b> 107:13 <b>clarify (1)</b> 101:16 <b>class (1)</b> 3:15 <b>classes (2)</b> 157:6 158:4 <b>classic (2)</b> 96:8,9 <b>classified (1)</b> 152:12 <b>clauses (1)</b> 105:18 <b>clawed (1)</b> 27:9 <b>clean (1)</b> 44:9 <b>clear (28)</b> 12:21 14:6 14:11 31:10 34:11 64:17 77:25 94:7 111:10 112:18 113:11 121:23 122:2,9 123:10 125:15 127:9 133:11 142:8,21 144:3 145:16 154:23 158:3 160:10,14 166:7 167:14 <b>clearing (4)</b> 59:19 61:8 89:5,7 <b>clearly (28)</b> 1:25 7:9 10:8 11:1 14:3 30:16 51:9 65:11 97:11 100:12 121:8 121:8 124:13 131:11 133:23 142:11 148:1 155:2 155:8,23 161:19 163:12 166:13,14	167:1 168:4,14,18 <b>client (2)</b> 96:11 103:10 <b>close (1)</b> 28:5 <b>closed (1)</b> 38:22 <b>closer (1)</b> 28:7 <b>closest (1)</b> 79:3 <b>closing (32)</b> 1:3,11,18 3:13 9:7,16 10:19 13:12 14:13 16:6 23:3 25:5,14 31:2 68:12 88:7 91:12 106:14,15 108:17 120:7 126:21 128:11 149:24 159:3,9 162:16 163:23 166:16,22 166:23 171:3 <b>closings (33)</b> 3:24 4:3 7:11,19 11:20,21 14:15,17 17:14 18:5 19:14,15 20:9 22:6 27:4,21 30:11 31:10,20 32:22 34:14 40:10,24 48:11 63:11 92:15 113:12,18 119:2 125:8 140:16 157:6 165:10 <b>clout (1)</b> 72:12 <b>clung (1)</b> 73:9 <b>co-branding (1)</b> 29:6 <b>co-agent (2)</b> 74:25 116:21 <b>cold (1)</b> 116:8 <b>collapse (4)</b> 42:9,18 83:9 112:22 <b>collapsed (1)</b> 23:6 <b>collapses (2)</b> 41:10,14 <b>collapsing (1)</b> 46:24 <b>Collecting (1)</b> 157:20 <b>collective (3)</b> 79:7,11 80:18 <b>collectively (2)</b> 73:24 79:15 <b>column (1)</b> 69:18 <b>come (64)</b> 2:11 7:13 8:17,22,24 10:10 11:7 14:3 16:6 19:17 28:16 32:24 32:25 36:3,4 37:23 38:7,16,18 42:1 43:4 48:21 54:15 54:17 59:25 60:21 64:6 66:24 71:13 73:21 75:10 80:20 90:9,16,16 94:10 100:25 102:24 106:2 107:5 109:1 111:8 112:9,15 114:22 120:22,25 126:19 131:16 132:15,20 133:20 134:17 135:25 138:9 140:1,7 141:13,14,19 146:22 149:19,22 155:21 <b>comes (14)</b> 4:25 13:4 34:19 63:1 96:10 108:22 111:1 113:14 114:11 126:24 135:16 136:4 141:7 161:10 <b>coming (12)</b> 14:12 20:25 33:20 37:11 42:24 66:15 102:1 135:10,12,19,25 144:17
---	--	---	--	--	--	---

<p><b>comments (1)</b> 4:4 <b>commercial (11)</b> 22:2 22:5 23:8 25:7 27:15 37:8,17 48:22 66:24 72:14 81:21 <b>commercially (1)</b> 70:21 <b>Commission (46)</b> 3:20 4:19,21 5:1,4,6,8 5:14,19,22 6:4,10 6:15,23 7:2,8 14:23 18:6,10 20:23 21:4 21:13,14 60:18,19 65:3 140:6 141:24 142:3,7,12,21 143:5,23 150:12 153:4 156:4,5,9 157:4,14,19 158:9 160:10 163:10,18 <b>Commission's (12)</b> 15:18 18:23 21:8 65:1 150:2 157:8,9 157:24 160:25 165:8,15,16 <b>commitments (2)</b> 21:13 143:6 <b>committed (1)</b> 102:9 <b>common (16)</b> 6:16 25:25 34:16,21 47:18 49:8 65:22 76:20 77:15 89:8 97:1 104:17,18 152:23 163:19 167:6 <b>communicated (2)</b> 45:21 47:3 <b>Community (2)</b> 4:13 4:15 <b>Compagnie (2)</b> 109:24 110:20 <b>company (2)</b> 69:15 154:14 <b>comparator (4)</b> 150:17,20 167:4,19 <b>compare (3)</b> 88:10 90:24 92:8 <b>compared (3)</b> 6:20 116:10 163:20 <b>compares (1)</b> 85:23 <b>comparing (5)</b> 9:5 12:3 70:14,16 164:19 <b>comparison (4)</b> 99:24 115:11 160:6 169:9 <b>compartment (1)</b> 133:1 <b>compatible (1)</b> 93:15 <b>compelling (2)</b> 40:22 76:22 <b>compensate (3)</b> 112:4 121:11 126:8 <b>compensation (1)</b> 126:10 <b>compete (4)</b> 31:24 91:23 92:3 113:4 <b>competing (4)</b> 23:13 30:1 65:18 66:6 <b>competition (82)</b> 2:15 2:16,24 3:2,10,11 4:1 6:7 7:18 9:4 10:18 11:15,25 12:3,4,6 13:5,7,19 14:24 16:13,21,22 17:2,12 19:11 26:22 34:1,18 52:16,23 53:11 55:9,15,18 56:2,24 57:7,12,13,19,20</p>	<p>58:1,15 59:1,7,8,13 60:1,5 61:10 88:4,9 88:10,24 89:3 91:1 91:10,15,17,21 92:2,7 99:14 106:22 109:17 121:13 128:1,14 129:4,25 133:16,22 133:25 134:2 143:8 143:11 144:20 148:3,4,12,12 <b>competitive (7)</b> 2:8 29:24 32:9 55:22 80:15 84:7 87:16 <b>competitor (3)</b> 16:23 20:21 87:14 <b>competitors (2)</b> 87:15 148:13 <b>complain (1)</b> 76:2 <b>complete (2)</b> 102:6 131:13 <b>completely (4)</b> 15:23 34:5 39:17 105:16 <b>complexity (1)</b> 98:15 <b>complicated (1)</b> 92:11 <b>component (1)</b> 2:23 <b>comprehensive (1)</b> 144:4 <b>computation (1)</b> 64:9 <b>concentrate (2)</b> 18:10 18:12 <b>concept (2)</b> 121:10 122:12 <b>conceptually (1)</b> 16:11 <b>concern (1)</b> 49:14 <b>concerned (10)</b> 12:16 13:23 18:11,13 20:14 132:7,8 144:21 148:5 153:11 <b>concerning (1)</b> 157:17 <b>concerns (1)</b> 14:2 <b>concluded (2)</b> 74:6 149:10 <b>concludes (1)</b> 149:11 <b>concluding (1)</b> 151:7 <b>conclusion (7)</b> 5:1 9:10 57:18 98:8 102:14,25 105:12 <b>conclusions (2)</b> 157:17 165:4 <b>condition (27)</b> 107:6,7 108:18 109:6,12 110:24 111:1,5,6 112:17 120:20 121:3 124:5,13 125:5,6,16 126:19 128:4,5 133:21,23 144:8,10 145:7,25 146:4 <b>conditions (9)</b> 12:18 13:23 93:7 108:23 121:1 132:22 133:3 134:20 141:3 <b>conduct (4)</b> 18:8,16 18:25 95:23 <b>confident (2)</b> 103:3,4 <b>confidential (6)</b> 27:25 69:19,19 70:7 90:10 130:24 <b>confidentiality (1)</b> 69:25 <b>confined (1)</b> 135:4 <b>confirm (1)</b> 21:22 <b>confirmed (4)</b> 40:7 115:20 160:24 164:17 <b>confirms (3)</b> 17:10 27:12 130:3</p>	<p><b>connected (1)</b> 112:2 <b>consents (1)</b> 61:20 <b>consequences (1)</b> 54:4 <b>conservative (1)</b> 149:12 <b>consider (5)</b> 11:25 18:21 88:9 114:20 127:6 <b>considerable (1)</b> 15:17 <b>consideration (2)</b> 12:14 123:25 <b>considered (7)</b> 13:20 29:7,10 39:6 41:5 77:2 151:3 <b>considering (7)</b> 4:16 41:3 82:7,11,16 84:19 109:21 <b>considers (1)</b> 157:14 <b>consistent (2)</b> 10:6 85:14 <b>consistently (2)</b> 5:2 143:18 <b>Consortium (2)</b> 73:1 76:15 <b>constitute (1)</b> 108:1 <b>constrained (3)</b> 21:5 28:6 65:12 <b>constraint (1)</b> 64:10 <b>constraints (1)</b> 20:13 <b>construct (1)</b> 34:3 <b>construction (8)</b> 48:25 51:7 52:3,5,11 53:12 54:3,5 <b>consumer (3)</b> 20:24 111:4,19 <b>consumers (16)</b> 121:4 121:11,17,18 122:1 122:3,12,22,25 123:7,20,22,22 124:10,13 125:17 <b>contain (1)</b> 45:11 <b>contemplating (1)</b> 84:25 <b>contested (1)</b> 83:16 <b>context (24)</b> 12:9,11 12:14,16,20 13:20 13:25 15:24 17:3,6 17:11 34:2 50:14 70:3 80:25 81:18 88:12 100:17 102:14 110:18 111:9 127:19 131:14 134:14 <b>contexts (1)</b> 13:14 <b>continue (3)</b> 10:5 11:7 11:9 <b>continues (1)</b> 84:3 <b>continuing (1)</b> 67:7 <b>contract (12)</b> 41:22,23 42:13 43:14,16,17 44:4,9 52:14,23,24 62:4 <b>contracts (3)</b> 42:15,16 61:22 <b>contractual (8)</b> 47:19 51:20 52:2,4,12,20 54:3,23 <b>contrary (2)</b> 17:9 134:1 <b>contrast (1)</b> 16:19 <b>contribute (1)</b> 128:8 <b>contributed (1)</b> 119:3 <b>control (1)</b> 20:9 <b>controversial (2)</b> 39:23 117:2 <b>convenient (1)</b> 51:19 <b>conversely (1)</b> 50:1</p>	<p><b>convoluted (1)</b> 28:18 <b>Cook (3)</b> 2:11 119:15 169:20 <b>coordination (1)</b> 14:1 <b>corner (1)</b> 33:13 <b>corporation (5)</b> 45:1,4 45:7,25 46:3 <b>correct (9)</b> 40:5 45:12 50:20 71:12 93:24 101:9 130:8 159:2 167:3 <b>corresponding (1)</b> 130:11 <b>cost (14)</b> 15:18 63:18 100:12 114:21 117:3,9 129:22 140:4 141:8,9,16 151:2 157:22 169:12 <b>cost/benefit (1)</b> 131:17 <b>costing (1)</b> 132:1 <b>costs (40)</b> 14:23 64:15 76:24 113:17,25 114:9,25 119:12 131:16,18 135:5 139:9 149:14,15,19 149:25 150:6,8,24 151:1,4,9,12,16,21 152:3,11,22 153:2 153:7 154:15 155:15,16 156:17 156:20 158:7,17,22 159:4 160:3 <b>counter-intuitive (1)</b> 100:1 7:24 8:7,18 9:6 10:11,13,21,23 12:5,7,10,23 13:6 13:15 14:10,15 15:11 16:10 19:1,7 20:6 22:3 28:9,13 28:17 30:18,21,24 32:3,19 33:16,18 34:7,12,23 35:9,23 36:25 38:17 39:5 39:21 40:9 48:18 49:13,15 50:18,19 50:23 51:4 53:9 54:7 55:5,8 59:1,21 63:4 65:7 67:5,12 73:12 74:7 77:8 80:3,24 82:6,11,16 88:11,12,21,22 89:1,11,21 90:13 90:25 91:6,17 92:8 95:7 100:25 131:4 134:15 135:11 136:2,3,9,11,23 137:4,9 <b>counterfactuals (12)</b> 8:13 10:16,17 19:16 37:12 38:12 39:10,13 53:20 55:22 56:8 81:10 <b>Coupe (9)</b> 59:15 66:14 74:6,14 77:13 78:1 78:24 79:23 80:3 <b>couple (1)</b> 157:10 <b>course (25)</b> 6:14 23:1 26:13 27:22 28:8 29:21 33:18 35:25 36:18 40:1 61:22 62:6 63:20 67:1 72:23 78:19 116:14 124:24 140:21 149:18 153:23,23 156:3,8 162:16</p>	<p><b>court (31)</b> 4:20,22,24 5:16,17,18,19,20 5:22,23 6:1,5 10:15 10:17,20 14:10 16:4,19 21:4 42:20 56:3 75:6 99:6,9 111:18 123:10 126:24 127:8 142:17 147:18 170:6 <b>court-appointed (1)</b> 3:18 <b>courts (9)</b> 4:14 6:5,8 11:23 103:24,25 111:13 143:9,12 <b>cover (1)</b> 101:22 <b>covered (3)</b> 9:17 122:13 143:4 <b>covering (1)</b> 133:4 <b>crazy (1)</b> 73:19 <b>create (2)</b> 15:16 135:2 <b>creates (7)</b> 2:17,21 132:19 134:14,21 138:8 148:21 <b>credible (2)</b> 72:25 73:2 <b>credibly (3)</b> 68:3,10 72:3 <b>credit (93)</b> 21:11,12 23:15 40:12 64:14 64:23 67:6,8 68:1,3 68:6,24 69:5,11,16 69:24 70:3,12,16 70:18,22,24,25 71:3,6,7,15,16,22 72:15,19 73:15,21 78:12,23 82:3 91:7 91:9 113:6,15,20 113:20,22,23,25 114:5,8,12,15,24 115:2,6,9,13,15 115:20 116:16,22 117:3,16,22 118:5 118:17,21 119:14 120:11,11,21,24 125:2 129:23 131:25 137:14,24 137:25 142:10 143:25 149:3,7,13 149:15,21 150:18 161:11 167:8 168:6 168:8,9,11,12,16 169:10 <b>Crehan (2)</b> 4:9,9 <b>crime (1)</b> 102:9 <b>criminal (2)</b> 102:10,13 <b>criteria (8)</b> 93:5 100:23 101:11 104:5 106:13 121:25 132:14 134:10 <b>criterion (2)</b> 140:20 145:3 <b>critical (2)</b> 128:14 134:2 <b>criticises (1)</b> 167:23 <b>criticism (1)</b> 74:10 <b>cross-check (1)</b> 141:11 <b>cross-examination (...)</b> 1:20 5:9 26:4,9 31:6,9 32:16,21 33:3,7 35:3,19 71:13 114:19 119:8 120:9 129:8,10,17 129:21 153:24 157:25 159:21 163:8,15,22 <b>cross-examined (1)</b> 30:12</p>	<p><b>cross-over (1)</b> 55:19 <b>crucial (5)</b> 62:3 75:3 133:17 140:18 153:14 <b>crude (1)</b> 137:5 <b>crudely (2)</b> 17:20 53:23 <b>cupboard (1)</b> 117:13 <b>current (4)</b> 43:6,7 117:23 118:1 <b>currently (1)</b> 82:11 <b>curve (1)</b> 132:4 <b>customer (2)</b> 47:1 118:10 <b>customers (11)</b> 44:24 45:6,14 46:6 74:2,4 113:21 115:19 117:8 123:1 129:24 <b>cut (1)</b> 110:25 <b>cut-throat (1)</b> 73:25 <b>cuts (1)</b> 88:6 <b>cycle (2)</b> 120:19,19</p>	<p><b>December (2)</b> 21:8 29:13 <b>decide (6)</b> 1:12 98:21 101:11,21 111:12 132:20 <b>decided (5)</b> 23:2 80:24 94:6 111:13 113:24 <b>deciding (3)</b> 81:6 93:4 101:4 <b>decision (19)</b> 4:15,19 5:14 6:4,7,10 17:23 17:24 20:21,24 21:4,8,14,21 60:16 65:21 72:14 98:16 143:2 <b>decisions (1)</b> 159:14 <b>decisive (1)</b> 16:17 <b>deduct (6)</b> 45:18 49:25 50:11 61:5 62:19 63:3 <b>deduction (9)</b> 43:2 47:7,8 51:5 53:5 58:21 61:20 62:2 65:20 <b>deducts (1)</b> 53:6 <b>default (20)</b> 45:2,2,10 45:15,17 46:1,8 47:22 49:25 50:1 50:19 51:3 62:16 65:15 77:9 78:16 89:8 119:24 139:6 168:13 <b>defect (1)</b> 92:1 <b>defend (1)</b> 166:1 <b>defendant (3)</b> 54:24 100:16 101:8 <b>defending (1)</b> 65:4 <b>defence (1)</b> 5:3 <b>definitely (1)</b> 32:23 <b>definition (6)</b> 9:19 16:22 112:23 113:24 135:10 163:17 <b>degree (2)</b> 61:25 98:14 <b>delighted (1)</b> 136:2 <b>Deloitte's (2)</b> 142:15 153:25 <b>Deloitte's (2)</b> 154:10 154:25 <b>demand (2)</b> 132:4 143:5 <b>demonstrate (2)</b> 127:11 160:14 <b>demonstrated (1)</b> 162:6 <b>departments (2)</b> 152:24 153:19 <b>depend (1)</b> 136:13 <b>depending (2)</b> 158:8 160:23 <b>depends (7)</b> 42:1 62:10 97:2 103:14 135:6 138:21 151:3 <b>derive (1)</b> 119:17 <b>describe (3)</b> 107:18,24 140:18 <b>described (1)</b> 162:14 <b>description (2)</b> 76:21 121:23 <b>designed (1)</b> 129:11 <b>desirable (1)</b> 31:15 <b>despite (3)</b> 26:1 27:2 114:9 <b>detail (12)</b> 8:17,24 9:15 22:7 31:16 86:11 107:24 129:1 130:3 133:10</p>
---	--	---	---	--	---	--

**D**

<p><b>d (1)</b> 154:4 <b>damage (1)</b> 18:15 <b>damages (14)</b> 9:13 32:25 33:2,12,15 93:10,23 94:2 95:5 95:10,24 96:20 98:24 139:3 <b>dancing (1)</b> 106:3 <b>data (19)</b> 150:1,10,12 150:25 151:23 154:20 155:17 156:24 157:7,11,15 157:20,21 158:4 159:10 162:11 163:10 165:8 166:2 <b>day (8)</b> 1:6 74:19 118:24 153:2 158:12 160:1,2 169:25 <b>days (3)</b> 118:2,10,13 <b>days' (1)</b> 118:7 <b>deal (11)</b> 1:24 7:1 8:15,24 9:8 20:5 16:22,25 37:10 60:10 64:7 <b>dealing (8)</b> 6:15 15:19 18:23 64:6,15 124:25 141:23 153:2 <b>deals (5)</b> 7:11 44:19 60:7 129:9 145:16 <b>dealt (6)</b> 19:18 33:23 75:10 130:7 166:18 166:23 <b>death (4)</b> 17:25 31:8 32:20 97:24 <b>debate (8)</b> 3:22 36:19 58:12 106:5 111:3 116:3 137:2 143:17 <b>debated (1)</b> 7:14 <b>debates (1)</b> 169:6 <b>debating (1)</b> 58:22 <b>debit (36)</b> 21:11 22:9 22:12,19 24:3,6,23 67:7,15,16,18 70:5 70:13,16,19,22,24 71:4,8,15,23 78:12 82:10,21 83:2 85:8 114:10,11,17 115:7 115:9,13 117:23 118:3 138:1 149:3 <b>Debits (1)</b> 68:23 <b>decade (1)</b> 156:8 <b>decades (1)</b> 114:10 <b>deceased (1)</b> 97:17</p>
---

<p>155:21 161:12  <b>detailed (1)</b> 52:4  <b>details (1)</b> 70:10  <b>determination (1)</b>            153:15  <b>determine (2)</b> 93:2            94:17  <b>determines (1)</b> 9:12  <b>deterring (1)</b> 60:25  <b>detriment (1)</b> 115:15  <b>detrimental (1)</b> 87:17  <b>develop (6)</b> 2:8,19            7:22 8:11 109:12            150:9  <b>developed (1)</b> 129:25  <b>Devenish (1)</b> 96:6  <b>dictate (1)</b> 143:1  <b>die (1)</b> 32:20  <b>died (1)</b> 31:8  <b>differ (1)</b> 160:23  <b>difference (16)</b> 10:14            13:4 25:19 36:20            47:13 49:11 56:7            57:9 65:14 70:13            86:9 90:11 115:5            150:11 160:15            167:3  <b>differences (1)</b> 149:23  <b>different (35)</b> 3:19,23            4:16,17 10:16,16            10:17 42:2 49:18            49:19 53:1,19 54:1            54:14 55:10,16            56:22 60:6 62:25            69:2 72:7 75:8            76:22,25 81:10,16            85:2 99:11 102:12            108:2 114:22 161:4            161:7,8,18  <b>differential (24)</b> 22:9            22:19 23:18 24:19            25:25 26:19,24            27:2,13 28:2 35:8            39:25 72:1,4 73:5            76:24 82:9,15            83:13 84:3 126:8            161:9 163:11            165:13  <b>differentials (6)</b> 35:4            36:24 37:3 163:24            164:23 165:3  <b>differently (1)</b> 64:13  <b>difficult (15)</b> 43:14            51:25 54:11,16            60:2 61:9 92:9,11            95:1 111:12 133:8            135:21 146:6 155:6            157:21  <b>difficulty (2)</b> 101:5            131:12  <b>dig (1)</b> 60:24  <b>dimension (2)</b> 108:12            151:24  <b>direct (2)</b> 81:22            122:12  <b>direction (1)</b> 136:14  <b>directly (4)</b> 15:19            31:24 84:18 121:17  <b>disadvantages (2)</b>            112:5 167:16  <b>disagree (2)</b> 1:13            77:24  <b>disappearing (1)</b>            23:25  <b>disbenefit (1)</b> 146:7  <b>discount (7)</b> 25:17,23            26:11,17 28:1            45:22 59:20  <b>discovered (1)</b> 153:23</p>	<p><b>discretion (1)</b> 18:23  <b>discussed (3)</b> 60:15            135:9 144:4  <b>discussing (8)</b> 49:4            50:8,10,18 62:7            132:17 135:12            149:5  <b>discussion (6)</b> 15:25            16:1 58:13 88:5,14            111:9  <b>disincentive (3)</b> 29:21            30:7,8  <b>disparity (2)</b> 41:3            164:18  <b>disproved (1)</b> 25:10  <b>dispute (6)</b> 7:12 9:20            11:16 13:1 23:16            150:21  <b>disputed (1)</b> 2:24  <b>distinct (1)</b> 16:11  <b>distinction (7)</b> 11:1,2            49:11 57:23 81:18            97:10 99:15  <b>distribution (1)</b>            163:15  <b>document (2)</b> 3:16            32:18  <b>dog (1)</b> 62:11  <b>doing (25)</b> 6:9 15:10            17:13,18 21:6,6            23:11 44:11 47:21            49:5 62:14 74:11            75:19 84:20 94:13            94:16 98:18 114:1            114:21,21 116:13            142:12 156:10            161:2 167:21  <b>domestic (13)</b> 6:20            7:25 8:8 9:23 20:3            20:11,14 25:16            29:14 34:23 93:24            142:1 143:3  <b>domestically (2)</b>            143:10,13  <b>dot (3)</b> 143:7,7,7  <b>dots (1)</b> 84:2  <b>doubled (1)</b> 26:14  <b>doubt (5)</b> 2:2 3:12            39:23 53:7 101:7  <b>doubted (1)</b> 63:18  <b>doubtful (1)</b> 37:21  <b>Dr (38)</b> 20:2 30:10            32:19 35:22 37:17            38:1 65:16 66:3            78:16 84:8,25            91:25 94:20,24            119:3 141:9 149:25            150:4,16 152:4            156:13,13,14,14            161:22 162:18,20            162:23,25 163:1            166:25 167:16,24            168:3,16,18 169:3            169:5  <b>drafted (1)</b> 62:8  <b>drag (1)</b> 116:4  <b>dramatic (2)</b> 27:18            161:16  <b>dramatically (1)</b>            161:18  <b>draw (3)</b> 97:10 147:15            157:16  <b>drawn (1)</b> 11:2  <b>drive (1)</b> 79:10  <b>driven (8)</b> 31:12 35:1            35:11 40:2 76:7            80:8 88:17,23  <b>driver (3)</b> 3:11 34:17            134:2</p>	<p><b>drop (6)</b> 21:1,11,12            23:7 67:19 73:7  <b>dropped (1)</b> 21:25  <b>dropping (1)</b> 158:20  <b>drops (1)</b> 33:15  <b>due (5)</b> 96:19 100:8            158:22 159:4 160:4  <b>dynamic (2)</b> 3:19            71:24  <b>dynamics (1)</b> 2:9</p> <hr/> <p style="text-align: center;"><b>E</b></p> <p><b>e (2)</b> 82:13 154:9  <b>e-commerce (1)</b> 119:5  <b>E1 (5)</b> 16:5,7 28:23            107:8 110:22  <b>E1.19 (2)</b> 123:12            125:10  <b>E10 (1)</b> 44:15  <b>E3.10 (5)</b> 15:22 44:16            44:17 161:1 163:13  <b>E9.1 (1)</b> 70:6  <b>earlier (3)</b> 73:12 138:3            169:23  <b>early (2)</b> 9:17 24:18  <b>earning (1)</b> 97:17  <b>easier (1)</b> 106:11  <b>EC (1)</b> 123:19  <b>echo (1)</b> 25:5  <b>econometric (11)</b>            150:2,3,10,22            151:21 153:6 156:1            156:4,8,16,18  <b>economic (11)</b> 8:6            12:15 13:14,25            17:6 18:9,14 34:22            37:20 73:22 108:1  <b>economics (1)</b> 87:21  <b>economies (5)</b> 151:23            152:6 158:23 159:5            160:4  <b>economist (2)</b> 30:15            37:9  <b>economists (13)</b> 37:2            37:6 38:5,23 40:3            79:5,13 80:14            87:12,20 105:5,11            140:24  <b>EDC (1)</b> 131:15  <b>EEA (1)</b> 20:25  <b>effect (21)</b> 16:14 19:8            24:11 30:12 46:8            49:3 55:18 60:1            61:6,14 75:13 79:9            80:6 82:16 90:15            100:4 121:15            123:20 126:11            166:20,21  <b>effectively (6)</b> 6:7            15:13 17:24 20:25            58:23 89:23  <b>effects (7)</b> 2:9 16:13            17:6 87:21 110:6            111:25 121:20  <b>efficiencies (15)</b>            107:21,23,25            109:22 111:2            112:20 126:16            127:22 128:5            133:12 134:14,19            135:2,4 139:4  <b>efficiencies? (1)</b>            112:17  <b>efficiency (6)</b> 107:13            107:16 108:11,18            110:8 125:4  <b>efficient (2)</b> 121:22            127:14  <b>efforts (2)</b> 18:11,12</p>	<p><b>eight (3)</b> 72:1 115:24            157:6  <b>eighth (1)</b> 119:16  <b>either (10)</b> 9:10 25:19            39:10 41:11 43:13            43:13 53:4,7 68:9            96:18  <b>elements (1)</b> 62:24  <b>eliminate (2)</b> 78:11            127:21  <b>eliminated (2)</b> 49:13            77:9  <b>elimination (4)</b> 53:25            128:2 133:22,25  <b>else's (1)</b> 77:9  <b>emphasised (1)</b> 14:22  <b>encapsulating (1)</b> 4:11  <b>encompasses (1)</b>            122:12  <b>encourage (1)</b> 120:17  <b>encourages (1)</b> 128:16  <b>encouraging (1)</b> 141:5  <b>ends (1)</b> 62:9  <b>engage (1)</b> 11:18  <b>engaged (1)</b> 83:6  <b>English (1)</b> 4:20  <b>enjoy (6)</b> 3:6 96:17            125:19,21 126:10            126:13  <b>enlightened (1)</b> 66:5  <b>enquiry (2)</b> 13:10,11  <b>enshrined (1)</b> 41:22  <b>ensure (1)</b> 41:24  <b>enter (5)</b> 46:21 51:22            60:2,3 95:25  <b>entered (1)</b> 45:20  <b>entirely (5)</b> 53:4 64:17            64:25 126:8 153:12  <b>entitled (8)</b> 5:14            18:10 32:4 33:5            43:25 51:22 93:16            99:9  <b>entitlement (2)</b> 49:25            102:3  <b>entity (1)</b> 84:9  <b>entry (1)</b> 61:1  <b>enumerate (1)</b> 131:3  <b>environment (1)</b>            80:15  <b>equally (13)</b> 19:9 21:7            33:9 84:12 96:4            118:11 125:18,23            126:14 141:8 142:7            143:15 150:7  <b>equation (2)</b> 146:20            147:4  <b>equivalent (2)</b> 59:18            165:18  <b>err (3)</b> 103:12 104:2,6  <b>error (1)</b> 106:9  <b>especially (2)</b> 66:6            151:25  <b>establish (11)</b> 10:7            45:2 46:1 57:12            95:16 96:3 99:4            100:2,24 104:13            142:1  <b>established (7)</b> 5:16            95:11 102:5 103:6            105:25 124:9            148:10  <b>establishes (3)</b> 45:7            108:24 128:12  <b>establishing (6)</b> 16:12            95:21 103:11 104:8            104:12,14  <b>estimated (1)</b> 163:16  <b>estimation (1)</b> 156:1  <b>EU (7)</b> 4:4 19:10 93:15</p>	<p>93:24 140:6,9            148:11  <b>Europe (3)</b> 22:1 33:13            143:3  <b>evaluate (2)</b> 43:21            76:21  <b>event (3)</b> 33:2 63:17            119:25  <b>evidence (113)</b> 1:17            1:23 4:19,24,25 5:6            5:6,7 7:1 8:16            22:15 25:12,15,21            27:3,10,11,17,20            28:12 31:3,11,13            31:16 32:1 34:11            34:18 36:10 37:22            37:23 38:5,7 39:2,7            39:8,22,22 41:10            60:18,23 63:10,15            64:6,8 65:23 67:11            73:13,13,14,22            75:6 77:25 79:3,4,5            79:12,24,25 80:13            80:25 81:3,14,23            81:25 82:1 83:3,15            83:21,24 84:20            87:10,12,19 91:24            94:19 98:21 99:6            99:21 101:3 102:19            102:21,24 104:18            106:20 108:4,24            113:3,15,16 115:3            116:15,21 120:3            128:10,12,25 129:3            129:6,13,16 130:2            130:5,13,21 131:15            133:9,10,11 134:2            154:8 158:3 160:13            160:15  <b>evidential (2)</b> 79:21            163:9  <b>ex (1)</b> 2:12  <b>ex-ante (3)</b> 41:19,24            42:8  <b>ex-post (5)</b> 16:15            41:19,20 42:8            49:16  <b>exactly (13)</b> 34:9            43:15 54:5 55:19            57:3 60:17 69:21            74:24 76:6 95:9            112:25 118:25            160:7  <b>example (27)</b> 40:10            51:13 52:17 57:13            66:1 83:10 84:14            84:19,23 85:22            93:17 96:10 97:8            103:15 106:9,16            117:12 124:21            131:13 136:10            137:3,25 148:4,8            148:15,16 168:9  <b>examples (3)</b> 20:22            151:8,9  <b>exceed (1)</b> 29:18  <b>exceeds (1)</b> 113:17  <b>excess (2)</b> 40:13 63:17  <b>exchange (1)</b> 154:12  <b>excited (1)</b> 102:17  <b>exclude (1)</b> 134:25  <b>excluded (3)</b> 49:13            52:11,12  <b>excludes (1)</b> 124:21  <b>excluding (1)</b> 164:1  <b>excuse (1)</b> 25:13  <b>exempted (8)</b> 20:24            29:15 94:6 100:22            103:4 106:24,24</p>	<p>138:15  <b>exemptibility (3)</b>            105:6,12 136:17  <b>exemptible (40)</b> 7:14            40:14 92:10 93:1            93:13 94:5,16,20            94:25 95:6,8,20            96:22 97:2 98:12            98:20 99:1,3,21            100:9,21,21 101:4            101:11,20,22            102:21,25 103:2            104:15,19,20,23,25            105:7,10 141:14            142:18 144:18            146:23  <b>exemption (34)</b> 7:13            92:10,25 93:5,9            94:10,12,15 95:25            98:13,17,18 99:2            99:18 100:23            101:12,19 102:3            103:7,11,16,19            104:5 121:5,9            122:10 126:6 127:2            134:10 136:5,8            137:3 141:3 148:1  <b>exemption/exempti...</b>            2:7  <b>exercise (15)</b> 52:4            54:8 55:16 94:14            95:9 96:21 101:2            106:1 136:23            157:23 161:13            162:23,24 165:2,3  <b>exhaustive (1)</b> 120:2  <b>exist (3)</b> 12:10 45:18            151:16  <b>existed (2)</b> 94:12            113:21  <b>existence (8)</b> 15:1            91:19 96:19 110:8            112:6 132:14            133:15,24  <b>existing (1)</b> 17:10  <b>exists (1)</b> 12:15  <b>exit (4)</b> 23:10 57:3            84:4 86:23  <b>exited (1)</b> 73:9  <b>exiting (1)</b> 57:2  <b>expect (5)</b> 25:7 62:9            62:10 164:18,20  <b>expects (1)</b> 62:12  <b>expenditure (1)</b> 115:3  <b>expense (1)</b> 27:8  <b>expenses (1)</b> 78:18  <b>expensive (1)</b> 130:17  <b>experience (2)</b> 67:13            141:15  <b>expert (9)</b> 3:18 30:15            39:1 73:22 74:13            87:12,20 105:15            140:23  <b>expertise (3)</b> 4:21            37:15,20  <b>experts (15)</b> 1:20 8:6            34:22 35:23 37:8            37:12,13,14 38:24            40:6 88:23 91:19            94:25 149:23            150:11  <b>experts' (1)</b> 140:25  <b>explain (5)</b> 72:10            74:24 107:24            127:11 136:3  <b>explained (2)</b> 30:11            119:3  <b>explore (1)</b> 151:24  <b>Express (2)</b> 115:22,25</p>	<p><b>expressly (3)</b> 35:2            51:23 52:12  <b>extend (1)</b> 113:5  <b>extent (12)</b> 23:18,19            36:20,21 60:19            98:4 105:3 109:6            125:22 126:14            134:9 153:10  <b>extra (3)</b> 63:18 115:12            132:19  <b>extract (6)</b> 35:14,16            63:14 65:24,24            127:2  <b>extracts (2)</b> 3:17,18  <b>extreme (1)</b> 82:6  <b>eye (1)</b> 30:20</p> <hr/> <p style="text-align: center;"><b>F</b></p> <p><b>face (6)</b> 33:23 62:25            144:3 147:24 168:7            168:8  <b>face-to-face (1)</b>            150:17  <b>faced (2)</b> 18:6 23:13  <b>facility (1)</b> 114:15  <b>fact (25)</b> 26:1 38:14            41:25 42:12 49:17            58:18 59:1 67:21            80:9 83:5 97:1            100:23 106:6            112:12 113:8 114:9            130:6 134:9,25            147:12 157:3            160:14,22 167:17            167:22  <b>facto (1)</b> 49:16  <b>factor (4)</b> 13:21 14:2            165:9,18  <b>factors (8)</b> 18:7 97:21            98:3,7 100:20            136:17 158:16            165:9  <b>facts (14)</b> 2:14 6:3,10            21:17 27:1 40:20            78:6 83:5 105:11            105:25 106:7,8,18            160:22  <b>factual (12)</b> 4:14 7:6            11:11 13:10 19:24            37:1,23 38:7 39:2            40:1 58:3 80:13  <b>fail (2)</b> 99:2 159:17  <b>failed (3)</b> 99:2 100:1            102:2  <b>fails (1)</b> 102:10  <b>fair (15)</b> 87:2,3 121:3            121:10 123:7 125:4            125:16 132:24            142:21 145:10,14            146:2,17 148:18            150:19  <b>fairly (2)</b> 142:7 155:1  <b>fall (6)</b> 14:24 29:23            36:17 52:8 83:16            91:8  <b>Falla (1)</b> 126:1  <b>fallback (1)</b> 136:6  <b>falls (1)</b> 91:15  <b>familiar (1)</b> 34:15  <b>fancy (1)</b> 117:14  <b>fantastic (3)</b> 2:21            76:13 113:13  <b>far (14)</b> 3:9 21:5 22:23            26:16 65:4 68:6,8            70:24 74:18 90:1            90:15,19 105:8            144:15  <b>fast (4)</b> 36:17 159:25            160:1,19</p>
---	---	---	---	---	---	---



<b>fatal (1)</b> 97:16	153:16 154:15	<b>fro-ing (1)</b> 97:3	68:12 74:8,19	121:6,9 122:10	70:4 72:19 77:11	58:2,5,11,20 59:6
<b>fault (1)</b> 97:7	155:16 156:20	<b>front (1)</b> 3:19	75:21 82:24 85:9	124:16 127:2,4,16	114:9 115:21 116:1	60:14,18 61:8,11
<b>favour (1)</b> 72:10	<b>flag (2)</b> 66:2 76:10	<b>fulfil (1)</b> 124:5	85:10 88:15 92:9	127:19,20 136:22	116:1 128:17	61:13 62:3,10,17
<b>feasible (1)</b> 31:15	<b>flagged (1)</b> 13:3	<b>fulfilled (3)</b> 93:4	93:20 98:10,15	137:3 144:20 148:1	129:14,24 131:8	64:12 65:4,10,16
<b>fee (28)</b> 22:13 28:22	<b>flashing (1)</b> 143:24	121:19,25	100:7 103:8 105:13	<b>guides (1)</b> 159:13	135:14 137:20,21	66:15 68:20,24
36:21 44:25 45:1,5	<b>flavour (1)</b> 120:23	<b>full (1)</b> 118:18	105:22 108:17		138:1,15,25 139:21	69:2,4,11,14,21
45:5,15,15,19 46:5	<b>flaw (1)</b> 142:24	<b>fully (2)</b> 132:12 133:3	110:17 114:12	<b>H</b>	156:7 163:7 164:3	70:16 71:1,4,12
46:5 47:9,13 63:17	<b>flaws (1)</b> 122:7	<b>function (3)</b> 15:8	117:15 121:3	<b>half (2)</b> 29:25 162:3	164:7,11,14 165:3	72:8,10,13 73:4
116:10 135:7	<b>flesh (1)</b> 68:11	134:23 135:1	123:11 125:9	<b>halfway (1)</b> 127:4	165:6,9 169:8	74:8 77:3,6,21,23
137:17,17 138:13	<b>flexibility (1)</b> 102:10	<b>functionality (2)</b> 23:19	127:18 129:1	<b>hand (3)</b> 51:5,6 116:8	<b>highly (3)</b> 4:22 124:25	77:24 78:14,21
138:23,25 139:7,11	<b>flexible (1)</b> 107:2	36:21	136:17 137:1	<b>handed (3)</b> 33:1 41:25	154:16	79:2 80:5,11 81:17
139:17,21 140:10	<b>flexibly (1)</b> 106:19	<b>functioning (4)</b> 12:18	141:21 142:5,15	41:25	<b>Hinten-Reed (61)</b> 25:9	81:25 82:5,9 83:10
147:13	<b>flip (5)</b> 46:23,25 51:20	13:24 135:1,3	147:20 153:8 161:1	<b>handy (1)</b> 16:6	26:9 31:5 33:8 35:2	84:11,17 85:13,18
<b>feed (1)</b> 51:4	66:21 118:10	<b>fundamental (3)</b> 2:14	165:1 167:24	<b>Hang (1)</b> 26:24	35:5 36:22 38:1	85:22 86:2,6,9,15
<b>feel (2)</b> 3:12 20:20	<b>floated (5)</b> 8:18 19:17	5:24 35:15	168:10 169:7	<b>happen (23)</b> 35:23	40:15,25 41:5 42:6	86:17,19 87:9,23
<b>feeling (1)</b> 21:5	39:19 42:3 91:4	<b>funded (2)</b> 137:15,16	<b>goes (7)</b> 42:11 74:20	37:7 38:23 41:5	46:23 63:12 65:5	88:4 97:3 98:10
<b>fees (19)</b> 16:14 17:4	<b>floor (2)</b> 24:22 89:9	<b>funding (4)</b> 84:14	75:11 84:19 159:2	50:19 54:12 56:1	74:9,17 91:24	99:4,17,20,24
22:22,23,24 31:24	<b>flow (2)</b> 27:5 74:5	117:20,22 118:9	165:6,24	67:20,22,24 73:4,4	94:19,23 105:18	100:7 101:1,14
45:2,3,3,7,10,11	<b>flowing (3)</b> 112:1	<b>further (9)</b> 2:2 8:11,12	<b>going (79)</b> 2:11 3:25	76:16 80:13,21	114:18 119:8,22	103:14 104:14
46:1,2,2 116:2	120:23 124:7	21:10 86:12 101:5	4:1,2 6:17 14:12	81:22,23 83:2,25	120:8 129:7,10,21	105:3,14,24 106:8
149:13,16,17	<b>fluid (1)</b> 97:13	116:14 143:17	22:13 26:25,25	87:5 89:17 136:1	130:14 141:10	108:9,13,21 110:11
<b>field (1)</b> 128:1	<b>focus (4)</b> 2:5 15:4,6	157:15	31:6,7,17 36:3,4	165:2	150:4 151:8,15	110:14,17,25 111:8
<b>Fifth (1)</b> 116:14	61:16	<b>Furthermore (1)</b>	37:10,22,23 39:3,8	<b>happened (18)</b> 8:11	152:11,15 153:21	112:25 113:12
<b>figure (6)</b> 47:12,14	<b>focused (1)</b> 59:24	123:19	39:9,14,16,23	22:1 23:1 28:12	154:10,20 155:1,13	118:19,25 119:22
90:10 107:19	<b>focusing (1)</b> 61:21		48:21 55:1 57:3	30:17 38:6,8 39:25	155:25 156:23	131:2,8,11 132:3,5
141:19 165:19	<b>fold (1)</b> 104:21	<b>G</b>	61:22 65:4 66:7,20	67:21 74:14 81:23	157:25 159:6,20	132:8,15,25 134:12
<b>figures (11)</b> 68:11,14	<b>follow (12)</b> 3:21 5:4	<b>gains (1)</b> 108:18	66:23 67:8 70:22	89:18 90:8,18	162:5,8,17,25	135:8,20,24 136:8
69:17 71:10,17	5:20,22 20:22	<b>gap (1)</b> 63:22	70:23 71:20 73:19	97:13,23,25 118:9	163:2 164:17 165:1	136:15,21 137:19
82:18,22 85:22,23	73:20 122:20	<b>gaps (1)</b> 92:16	73:20 75:10,22,25	<b>happening (7)</b> 14:8	165:20,25 166:8	138:16,21,25 139:6
86:6 169:10	127:22 133:8	<b>gateway (2)</b> 147:10	77:22 78:6,9 79:2	82:25 83:18,19	167:12,21,23	139:9,20 140:1,16
<b>fill (3)</b> 1:15 63:22	138:18 141:5	148:19	80:8 82:22 86:21	<b>happens (8)</b> 34:13	168:17,24 169:4	140:18 143:15
92:16	142:22	<b>gauging (1)</b> 131:7	89:22 101:6 102:22	37:18 48:1 62:16	<b>Hinten-Reed's (18)</b>	145:7,10,13,15,22
<b>final (8)</b> 33:17 122:22	<b>following (4)</b> 60:16	<b>gaze (1)</b> 66:22	105:8 106:4 110:21	63:25 117:25	19:19 20:5 32:12	145:25 146:2,11,15
123:18 125:6 126:3	107:14 121:18	<b>GBP (1)</b> 69:5	113:2 114:3 120:25	118:23 135:22	32:20 34:19 37:16	146:18,22 147:2,14
130:24 167:3 168:4	158:6	<b>general (12)</b> 5:17,19	124:20 125:9	<b>happy (5)</b> 60:11 75:22	64:1 117:1,4 122:8	147:18,20,23
<b>finance (2)</b> 152:24	<b>follows (3)</b> 123:15	5:23 6:5 8:14 11:9	128:25 131:2	134:4 152:10 154:7	124:17 129:17	148:15 152:4,8,10
153:19	124:1,2	28:25 85:14 110:7	132:11,15,20 136:1	<b>hard (3)</b> 106:25 107:1	130:19 154:1 165:5	158:15 159:2,25
<b>financed (1)</b> 129:19	<b>foot (3)</b> 22:23 23:9	110:19 114:3	137:13,19 139:25	127:16	165:17 166:12	160:7,10,13 169:13
<b>financial (2)</b> 86:4	24:22	115:22	140:1 151:18	<b>harm (1)</b> 87:9	167:2	169:16,24 170:2
96:17	<b>force (2)</b> 28:16 80:7	<b>generally (13)</b> 15:6	152:25 155:5,19,23	<b>harsh (1)</b> 86:17	<b>Hoffmann (1)</b> 4:18	171:3
<b>find (3)</b> 6:2 92:6	<b>forced (2)</b> 8:7 57:16	21:23 103:23,24,25	159:25 160:1,19	<b>HBOS (2)</b> 22:11 24:18	<b>hold (3)</b> 41:14 42:9	<b>hour (1)</b> 169:22
125:17	<b>foremost (1)</b> 1:8	106:8 119:6,9	162:5,7 168:25	<b>head (4)</b> 24:15 39:15	43:25	<b>HSBC (4)</b> 23:2,17
<b>finds (3)</b> 93:8 95:3	<b>forget (1)</b> 80:3	126:11 131:21	<b>good (15)</b> 1:4,5 4:11	102:7 106:3	<b>hold-up (7)</b> 41:9,13,20	24:20 85:20
109:2	<b>forgotten (1)</b> 121:2	138:22 144:1 167:7	8:14 59:22 60:20	<b>heading (3)</b> 14:21	41:22 43:3 49:14	<b>huge (1)</b> 38:10
<b>fine (5)</b> 36:16 60:9,10	<b>form (4)</b> 39:15 47:8	<b>generate (4)</b> 109:4,7	65:22 84:22 87:18	122:1 132:10	60:6	<b>hundred-odd (1)</b>
87:23 105:15	47:20 107:21	126:22,23	134:4 138:8 141:18	<b>headings (1)</b> 133:6	<b>holding (2)</b> 43:24,25	155:18
<b>finish (6)</b> 132:22	<b>formal (3)</b> 20:14 21:21	<b>generous (1)</b> 66:8	141:19 148:7,15	<b>healthy (1)</b> 97:21	<b>home (1)</b> 117:12	<b>hyperbole (1)</b> 120:4
133:7,21 169:13,16	98:16	<b>genesis (1)</b> 43:2	<b>goods (3)</b> 12:17 16:25	<b>heard (12)</b> 3:9 5:5 7:1	<b>honest (2)</b> 54:22	<b>hypothesis (2)</b> 16:10
169:19	<b>fortuitously (1)</b> 52:25	<b>Germany (1)</b> 11:19	117:8	7:7,8 38:5,6 75:18	56:10	100:2
<b>finished (2)</b> 5:12	<b>forward (7)</b> 10:2 75:3	<b>getting (5)</b> 79:7 87:1	<b>gradual (1)</b> 77:4	79:4 101:3 131:14	<b>honour (6)</b> 12:25	<b>hypothetical (6)</b> 54:8
76:18	130:22 143:21,22	137:12 164:15	<b>grant (3)</b> 94:11,15	146:13	42:10,18,22,25	80:2 81:21 86:21
<b>firms (1)</b> 158:21	152:4 169:3	168:10	126:5	<b>hearing (1)</b> 8:12	50:25	97:14 127:6
<b>first (57)</b> 1:8 2:17 7:23	<b>fought (2)</b> 33:13	<b>give (17)</b> 14:17 18:7	<b>granting (3)</b> 94:9	<b>heavily (1)</b> 31:5	<b>hoof (1)</b> 148:8	
11:23 14:9 15:16	139:10	40:10 49:3 58:6	95:25 101:12	<b>heavy (1)</b> 141:2	<b>hook (1)</b> 21:24	<b>I</b>
17:22 20:5,8 25:20	<b>found (2)</b> 111:25	68:11 72:12 79:3	<b>graph (1)</b> 85:14	<b>held (1)</b> 110:2	<b>hope (3)</b> 38:9 133:4	<b>I2 (1)</b> 68:15
28:8 31:9 34:19	137:7	81:19 87:22,23	<b>great (3)</b> 7:1 80:7	<b>help (7)</b> 32:10,14	162:6	<b>I3 (1)</b> 125:24
45:23 46:11 47:7	<b>four (9)</b> 2:14 3:8 93:7	101:6 102:14 120:9	154:19	40:25 50:9 96:8	<b>hopefully (8)</b> 1:11	<b>idea (5)</b> 21:15 37:17
52:9 63:1,9,13	101:10 106:13	141:18 149:16	82:15,17 84:22	101:14 105:16	26:3,8 35:5 70:19	87:1,4 168:5
66:18 67:13 68:19	132:14,22 134:10	159:7	87:18 114:21	<b>helpful (5)</b> 48:13,25	74:25 101:16	<b>idem (1)</b> 73:17
72:16 73:18 74:1	134:20	<b>given (13)</b> 2:3,3 3:17	116:20 132:6,7	58:23 111:11,17	111:11	<b>identified (2)</b> 35:24
77:16 88:20 94:4	<b>four-party (9)</b> 11:9	4:21 20:22 54:4	164:18	<b>helps (3)</b> 103:20,23	<b>hopeless (1)</b> 157:2	103:19
99:25 104:3 105:13	15:12 29:8,10 30:1	109:25 115:7	<b>green (1)</b> 143:20	110:23	<b>horizontal (1)</b> 100:9	<b>identify (10)</b> 7:21
105:22 107:6,7	56:1 118:5,23	120:23 129:2,6	<b>groceries (3)</b> 90:4,4,5	<b>heterogeneity (1)</b>	<b>horribly (3)</b> 154:2,3,16	28:17 94:5,7 104:3
108:18 109:5,12,14	167:8	135:10 156:7	<b>ground (13)</b> 6:16	158:10	<b>Hoskins (215)</b> 1:3,4,5	113:1 133:2 137:4
110:24 111:1	<b>fourth (4)</b> 3:3 41:4	<b>gives (10)</b> 1:11 44:24	25:25 33:13 34:16	<b>heterogeneous (1)</b>	1:6 21:18,21 24:4,8	140:2 152:2
112:17 115:24	115:17 133:21	45:14 108:25	34:22 61:2 76:20	159:13	24:10,13,25 25:3	<b>identifying (3)</b> 10:10
120:20 121:5 124:5	<b>framed (3)</b> 45:25 54:9	118:10 147:7	77:15 97:1 104:17	<b>Hicks (1)</b> 97:8	35:19,21 36:3,6,8	14:9 153:6
124:12 130:10	136:22	150:23 152:6 155:2	104:18 152:24	<b>hidebound (1)</b> 46:15	36:10,17 37:10,22	<b>ignore (3)</b> 80:6,9
146:4 149:25 150:5	<b>framework (10)</b> 1:9	163:23	167:6	<b>high (21)</b> 8:3 9:22	38:3,14,16,20 39:1	108:16
150:22 151:1	1:11,12,15 2:13	<b>giving (2)</b> 69:25 79:5	<b>group (5)</b> 75:12 83:18	20:4 26:19 34:12	39:14 40:5 42:1,5	<b>ignores (1)</b> 168:2
152:18 158:7	9:14 36:13 92:15	<b>GlaxoSmithKline (2)</b>	124:10 125:17,23	48:20 58:17 62:23	42:15 43:4 44:14	<b>ii (1)</b> 164:1
162:16 167:5	92:19 96:1	<b>GNS (1)</b> 29:9	29:21,22,24	63:5,6 70:1 71:11	44:20,22 45:23	<b>iii (1)</b> 164:5
<b>fit (7)</b> 51:18 102:6	<b>frank (1)</b> 5:10	<b>go (56)</b> 2:13 4:1,3,13	<b>guarantee (3)</b> 119:18	75:14,18 78:13	47:11,16,24 48:3	<b>ill (1)</b> 97:22
132:13,13 142:6	<b>fraud (1)</b> 119:23	5:21 7:19 9:14	119:23,24	82:4 83:7,15 88:14	48:10,13,17 49:2,7	<b>imagine (5)</b> 44:5 50:4
154:11,16	<b>free (4)</b> 31:23 117:20	14:15 15:23 26:4	<b>Guardian (1)</b> 76:4	88:23 166:18	49:9,18,20 50:3,8	72:16 74:22 169:16
<b>fits (1)</b> 7:15	117:22 118:9	28:24 36:17 49:14	<b>guidelines (18)</b> 106:16	<b>higher (37)</b> 23:6 25:23	50:24 51:7,20 52:8	70:17 80:11 89:21
<b>five (1)</b> 60:10	<b>free-for-all (4)</b> 50:2	52:1 57:22 65:4	106:17,19 107:8,10	26:11 27:6 31:23	53:15 54:11,22	91:7 134:15
<b>fixed (10)</b> 151:2 152:2	51:6,8,11	66:13,15 67:13		63:23 65:13 68:7,8	55:10,13,23 56:3,6	<b>immediate (4)</b> 78:2
152:12,22 153:3,6	<b>fresh (1)</b> 170:3				56:10,14,21 57:2,9	

84:23 119:18,19  
**immediately (12)**  
 20:22 21:11 57:22  
 84:21 93:10 95:2  
 97:8 118:2,4,6,12  
 118:22  
**impact (6)** 16:20  
 70:23 73:3 80:9  
 121:12 158:17  
**impending (1)** 28:21  
**imperative (1)** 27:15  
**imperfect (2)** 156:15  
 162:23  
**imperfection (1)**  
 163:1  
**implementation (1)**  
 28:22  
**implication (1)** 37:25  
**implied (4)** 43:13,16  
 44:3 52:9  
**implies (2)** 121:10  
 159:15  
**implying (1)** 52:22  
**import (2)** 53:9 54:7  
**importance (2)** 15:17  
 35:25  
**important (26)** 5:23  
 6:13,14,24 11:20  
 13:15 14:4 22:5  
 23:16,20 24:16  
 34:17 36:18 38:3  
 42:20 101:24  
 110:22 119:16  
 124:23 125:7 126:4  
 142:25 149:18  
 151:25 161:7  
 168:20  
**imported (1)** 55:5  
**impose (1)** 166:17  
**imposed (5)** 20:10,13  
 31:21 137:16  
 138:14  
**impossibility (1)** 57:10  
**impossible (3)** 9:23  
 50:16 106:21  
**impression (1)** 102:18  
**improved (2)** 107:22  
 110:8  
**improvement (1)**  
 128:1  
**incentive (4)** 20:16,18  
 30:5 75:15  
**include (3)** 10:22  
 122:17 145:6  
**included (2)** 86:4  
 157:4  
**includes (2)** 124:9  
 169:17  
**including (4)** 22:17  
 111:20 122:21  
 165:9  
**inconsistent (1)** 34:5  
**increase (6)** 3:1 30:5,8  
 119:4 128:9 130:11  
**increased (6)** 22:18  
 26:13 128:16,23  
 130:16 168:5  
**increases (8)** 103:7  
 120:24 129:4,5  
 130:6,9,10 139:17  
**increasing (3)** 129:9  
 131:21 139:17  
**incredibly (1)** 114:14  
**incurred (1)** 115:13  
**indefinitely (1)** 82:4  
**INDEX (1)** 171:1  
**indication (1)** 161:16  
**indifference (2)** 141:1  
 157:18

**indirect (1)** 122:13  
**indispensability (8)**  
 126:20 127:3  
 128:10 132:10,25  
 133:18 140:8,19  
**indispensable (1)**  
 127:21  
**individual (7)** 80:17  
 114:23 126:6,15  
 148:6,13 166:20  
**individually (6)** 47:4  
 66:4 73:23 79:6,11  
 80:17  
**industry (2)** 38:23  
 40:22  
**inferential (1)** 7:7  
**information (3)** 26:5  
 75:2 160:17  
**infringes (1)** 124:4  
**injustice (1)** 44:12  
**innocence (1)** 19:9  
**input (1)** 122:22  
**insofar (7)** 5:17 55:3  
 108:14,15 125:1  
 134:11,13  
**instance (2)** 11:23  
 65:2  
**instantaneous (2)**  
 75:7 77:5  
**instantaneously (1)**  
 77:1  
**institution (1)** 4:15  
**instructive (1)** 3:13  
**instruments (2)** 29:4,6  
**intend (3)** 1:21 2:4 9:8  
**intended (3)** 106:21  
 143:16 167:14  
**intending (1)** 108:13  
**intensity (1)** 91:14  
**intentions (1)** 76:11  
**interactions (1)** 133:4  
**interacts (1)** 144:9  
**interchange (31)**  
 22:13,22,24 28:22  
 31:24 32:9 36:20  
 43:9 44:25 45:2,5  
 46:1,5 47:9,13  
 63:17 135:7 137:17  
 137:17 138:13,23  
 138:25 139:7,11,17  
 139:21 140:10  
 147:12 149:13,16  
 149:17  
**interest (6)** 2:12 60:4  
 79:12,15 91:8,14  
**interest-free (3)** 117:9  
 120:12 129:23  
**interested (1)** 2:1  
**interesting (5)** 3:16  
 74:18 101:17 106:4  
 167:22  
**Interestingly (1)** 149:9  
**interests (2)** 80:17,18  
**interleaved (1)** 119:1  
**internal (7)** 14:16,18  
 17:15 68:20 69:1  
 85:5,11  
**interregional (1)** 45:7  
**interrupt (2)** 74:5 79:2  
**intersystem (2)** 130:1  
 133:16  
**intersystems (1)**  
 109:16  
**intervene (1)** 127:9  
**intra-EEA (6)** 6:15,20  
 20:24 21:2,9,12  
**intraregional (1)** 45:8  
**intricacies (1)** 37:18  
**introduce (1)** 24:23

**introduced (2)** 73:10  
 114:9  
**introductory (1)** 3:7  
**investigate (1)** 18:12  
**investigation (1)** 65:1  
**investigations (2)**  
 18:24 21:25  
**investing (1)** 84:17  
**invite (1)** 35:15  
**inviting (1)** 18:14  
**invoking (1)** 127:5  
**involve (1)** 81:11  
**involved (5)** 18:25  
 21:22 40:8 60:19  
 98:5  
**involves (1)** 81:10  
**issuance (1)** 29:3  
**issue (11)** 4:16 7:13  
 37:8,9 43:18 48:4  
 50:12 60:13,21  
 98:9 132:22  
**issuer (16)** 41:7 43:22  
 43:24 44:7 46:21  
 48:1,2,15 50:11  
 52:17 59:17 62:18  
 66:8 75:4 89:5  
 149:15  
**issuers (20)** 22:17,25  
 25:6 41:14 42:9,13  
 42:17 61:11 62:13  
 63:2 75:3,15,22  
 76:21 77:1,18 89:9  
 117:23,23 130:1  
**issuers' (1)** 109:18  
**issuers/acquirers (1)**  
 60:5  
**issues (8)** 1:25 16:11  
 29:5 51:13 102:17  
 104:11 133:2  
 150:23  
**issuing (19)** 14:8  
 40:15 43:1 47:5  
 48:8 53:5 60:8  
 61:23 62:5 87:4  
 88:20,24 89:10  
 90:22 112:13 123:3  
 123:23 124:14  
 133:13  
**it's-- (1)** 82:8  
**iv (1)** 164:9

**J**

**January (1)** 22:8  
**job (3)** 101:10 106:11  
 156:11  
**JOHN (14)** 41:16 42:4  
 42:12 69:6 105:1  
 108:8,11 138:22  
 139:2,8 151:20  
 152:6,9 158:14  
**join (3)** 44:7 59:11,22  
**joining (1)** 84:1  
**joint (1)** 140:24  
**judge (2)** 4:25 6:9  
**judgment (8)** 3:14  
 16:8,10 17:7 125:9  
 127:7 156:2,9  
**judicial (8)** 5:2 6:7,11  
 6:13 81:11,14,20  
 106:10  
**July (1)** 22:12  
**jumped (1)** 74:1  
**June (2)** 25:1,2  
**Justice (125)** 1:5 5:16  
 5:18,21,22 6:2,6  
 10:15 14:10 16:4  
 24:2,23 25:2 35:17  
 35:20 36:1,5,7,9,16  
 37:5,14,25 38:12

38:15,18,21 39:12  
 40:4 42:21 44:17  
 49:5,8 55:7,12,21  
 55:24 56:4,5,7,12  
 56:19 58:6 61:3,9  
 61:12 62:21 68:19  
 68:22 69:1,3,7,10  
 69:13,20 70:14  
 71:3,24 72:9,11,23  
 74:21 81:8,19 82:2  
 82:8 86:14,16,18  
 86:20 87:22,25  
 96:5,24 98:23  
 99:11,19,23,25  
 104:8 108:7,20  
 110:10,12,15 111:7  
 111:13 118:15,24  
 119:21 123:11  
 126:24 132:9,23  
 135:18,23 136:6  
 138:18 139:3,7  
 140:12,17 143:14  
 144:25 145:9,12,14  
 145:20,23 146:1,5  
 147:1,18,19 148:14  
 158:25 159:22  
 160:5,8,12 169:11  
 169:14,23 170:1,4

**K**

**keep (13)** 4:2 8:14  
 11:13 16:5 21:23  
 36:13,13 60:6 63:7  
 64:2 65:6 78:9  
 136:11  
**keeping (1)** 51:3  
**kept (5)** 7:3 23:9  
 24:10 31:6 124:20  
**key (2)** 2:23,25  
**kicks (1)** 103:23  
**killed (1)** 33:2  
**kind (2)** 72:1 151:23  
**know (1)** 152:8  
**know (42)** 7:2,23  
 19:19 20:2 22:14  
 23:1,4,16 24:14  
 27:18,24 32:25  
 36:3 38:15,24  
 48:25 51:25 55:12  
 60:21 74:16 75:25  
 75:25 80:10 81:15  
 83:23 89:17 92:17  
 96:9 102:16 104:9  
 120:22 126:12  
 131:12 134:7  
 135:21 137:25  
 141:13,24 142:9  
 149:22 157:8  
 161:22  
**knowing (1)** 75:13  
**known (1)** 7:9  
**knows (1)** 53:17

**L**

**language (7)** 67:25  
 107:1 108:2 123:14  
 124:13 127:15  
 151:13  
**large (34)** 8:3 18:9  
 26:24 27:2 73:5  
 80:4,9 86:21 113:1  
 116:18 150:13  
 154:13 157:4,21  
 158:21 159:10,16  
 159:19 160:17

162:18 163:8,25  
 164:2,3,6,7,10,11  
 164:13,19 166:3,5  
 166:5,18  
**larger (8)** 3:3 70:24  
 109:7 159:3 160:2  
 160:24 161:17  
 164:20  
**largest (2)** 155:19  
 161:15  
**late (2)** 160:1,2  
**law (58)** 3:21 4:13,23  
 5:25 6:2 10:6,9  
 12:8,21 14:7 17:1,5  
 17:10 19:11,13  
 20:7 34:1,6 41:23  
 42:20 47:18 49:8  
 49:23 50:25 52:16  
 52:23 56:3,11 59:8  
 67:25 93:15,25  
 96:7 102:13 105:16  
 105:19,20 106:6,7  
 106:9 109:20  
 111:10,12 122:3  
 124:18,22,23,24  
 125:15 144:8,20  
 145:15,18 146:8  
 147:20 148:3,4,12  
**lawful (5)** 94:8,11  
 99:6 100:3,5  
**lawyer (1)** 102:16  
**lawyers (1)** 102:16  
**lead (5)** 57:18 116:20  
 130:15 159:11  
 166:15  
**leading (1)** 91:8  
**leads (3)** 62:20 97:8  
 152:12  
**leap (2)** 84:22 85:1  
**learning (1)** 143:22  
**leave (5)** 46:10 57:6  
 120:4 130:2 152:24  
**leaves (1)** 57:7  
**leaving (2)** 56:1 57:11  
**led (3)** 21:3,21 133:24  
**left (6)** 43:11,11 46:4  
 51:12 83:16 142:25  
**legal (26)** 5:15,23  
 10:12 12:11,16  
 13:14,25 14:14  
 15:16,19,25 17:6  
 19:4 25:7 44:8,9  
 64:18 102:14  
 103:24 105:10,22  
 105:24 106:1  
 120:22 121:25  
 125:10  
**legality (3)** 6:6,9 17:17  
**legislation (1)** 142:16  
**legislative (1)** 30:8  
**legislature (1)** 140:6  
**length (1)** 4:13  
**lessee (2)** 126:9,9  
**let's (20)** 27:20 28:7  
 33:9 34:11 46:25  
 48:22 60:8 62:19  
 77:7,13 80:2,3,4  
 89:16 94:10 107:10  
 113:14 117:11  
 121:3 153:9  
**level (105)** 2:7 7:14  
 8:3,22 10:12 20:11  
 21:9 25:18 28:1  
 32:24 34:10,10,17  
 34:25 40:14 57:17  
 58:16,19 59:9,12  
 59:13 63:6 64:5  
 66:23,24 68:7,8  
 72:18,18 78:13,19

82:4 83:5 90:16,25  
 91:20,20 92:2,10  
 93:12,13 94:5,8,11  
 94:15,16,21 95:1,4  
 95:6,8,20 96:22  
 97:2 98:12,14,17  
 98:20 99:1,3,6,7,18  
 99:21 100:21 101:4  
 101:11,20,23  
 102:21,25 103:16  
 104:16,19,20,23,25  
 105:5,7,10 112:17  
 116:4,9,23 126:16  
 129:11 131:16,22  
 132:13,20 133:18  
 135:6,11 136:20  
 138:14,21 139:11  
 139:12,19 140:19  
 141:14 142:18  
 144:18 146:23  
 157:17  
**levels (6)** 26:17 56:18  
 56:19 62:23 63:24  
 160:16  
**Lewisohn (1)** 96:5  
**licences (1)** 29:2  
**licensee (2)** 59:3,3  
**lie (1)** 103:10  
**life (1)** 6:17  
**lifeboat (1)** 31:7  
**lifted (1)** 118:3  
**light (5)** 1:19 3:9  
 30:19 143:20,24  
**likelihood (1)** 107:15  
**likes (1)** 20:17  
**limit (3)** 65:12 132:6  
 139:23  
**limitation (1)** 96:11  
**limited (1)** 109:20  
**limping (1)** 57:21  
**line (10)** 21:2 32:18  
 45:17 46:3 56:24  
 56:24 58:1 74:20  
 74:20 165:12  
**lines (5)** 62:1 72:4  
 157:10 158:14  
 159:8  
**list (1)** 120:2  
**listen (2)** 77:17,18  
**literally (2)** 2:4 32:20  
**little (5)** 29:12 44:12  
 70:9 115:8 136:12  
**lived (1)** 97:19  
**local (3)** 143:3,10,13  
**log (1)** 36:17  
**logic (3)** 8:21 112:21  
 122:19  
**lonely (1)** 117:13  
**long (9)** 35:12 65:24  
 82:25 97:19 113:20  
 144:13 147:6 150:2  
 169:25  
**long-term (2)** 78:3  
 152:19  
**longer (6)** 76:23 151:1  
 151:5,10,14 156:17  
**look (60)** 5:25 12:8,10  
 13:13 15:10,10,21  
 16:5 17:8 25:4 28:7  
 28:11,23 30:2,23  
 30:24 34:1,1,2 35:3  
 36:10 39:2 50:3  
 52:1 54:15 69:17  
 72:18,18,20 78:4,5  
 82:24 83:5 88:20  
 90:8,18 97:22,24  
 101:19 107:7  
 108:14 110:24  
 111:2,17 112:10

113:14,19 120:6  
 130:3 132:23 133:3  
 137:6,8,9 143:1  
 145:4 147:16  
 150:19 151:20  
 153:9  
**looked (9)** 5:10 13:3  
 44:17 85:6 154:20  
 155:22 156:24  
 160:18 163:19  
**looking (66)** 6:4,19,23  
 9:4 12:7,20 13:4,5  
 14:5 16:22 17:6,16  
 17:17 28:8,14  
 30:16 32:2,3 36:25  
 42:21 44:21 48:17  
 52:13 69:9 70:2  
 71:1,9 72:14 75:3  
 86:2 92:13 95:7,19  
 97:18 101:18  
 103:17 109:22  
 112:11,18 122:3,4  
 122:5 126:17 127:1  
 127:3 130:6 132:9  
 134:18,22 135:16  
 137:12 142:17  
 145:4,10,11 146:3  
 147:4,5,6 148:16  
 148:20 156:25  
 166:9,19,21 169:1  
**looks (4)** 44:13 120:5  
 122:8 143:23  
**Lord (2)** 4:12,18  
**lose (2)** 50:6 96:17  
**loss (22)** 93:2,10,12  
 93:14,20 94:18  
 95:16 96:7,14,19  
 96:21 97:2,9 99:4  
 100:19 102:5  
 103:22 105:3 136:4  
 136:12 138:12  
 139:14  
**lost (3)** 36:13 96:12  
 96:14  
**lot (10)** 1:21 9:17  
 37:19 72:17 88:5  
 91:11 97:3 109:14  
 115:22 130:23  
**lots (1)** 112:12  
**low (32)** 7:25 8:19  
 19:22,23 20:3 22:4  
 25:16 32:23 33:20  
 34:8,12,24 35:9  
 56:17 57:17 67:10  
 73:25 75:14,20  
 78:10 83:14 88:13  
 88:22 129:22,22  
 152:17 158:6  
 159:11,18 161:19  
 162:7 166:15  
**lower (23)** 22:22  
 23:14,14,25 24:2  
 25:8 26:1,17 67:14  
 67:17 103:4,8,12  
 149:17,20 152:13  
 153:17 158:22  
 159:4 160:3,24  
 161:18 169:7  
**Lumpiness (1)** 152:6  
**lumpy (2)** 151:12,16  
**lunch (1)** 88:14  
**lunchtime (1)** 169:19

**M**

**Maestro (45)** 22:5,7,9  
 22:12,15,18,19  
 23:10,17,20 25:10  
 36:19 37:1,24 38:8  
 67:13,19 71:11

73:4,14 76:16 79:16,17,18 80:11 80:13,20,22 81:14 82:1,5,9,18,20,23 83:1,8,24 85:3,8,19 85:20 87:12,20 115:6 <b>Maestro's (3)</b> 23:6 67:14 83:6 <b>magnitude (8)</b> 65:13 82:12 85:24 86:7 86:10 107:15,18 115:16 <b>main (6)</b> 7:20 70:11 87:19,19,20 92:13 <b>maintain (4)</b> 26:19 27:13 56:17,19 <b>maintained (8)</b> 8:1,2 21:3 23:23 25:17 25:25 62:23 72:2 <b>maintains (2)</b> 34:8,9 <b>major (1)</b> 160:15 <b>majority (4)</b> 164:3,7 164:11 166:5 <b>making (5)</b> 58:3 72:17 80:7 116:24 139:16 <b>March (2)</b> 1:1 170:7 <b>margin (2)</b> 91:23 92:4 <b>marginal (1)</b> 159:14 <b>margins (1)</b> 74:1 <b>Maritime (2)</b> 109:24 110:20 <b>marked (1)</b> 130:25 <b>market (87)</b> 3:1 8:8,15 12:19 13:8 14:2,6,8 23:3,6,10 24:1,5,10 26:14,15,19 27:1,5 27:8,19 29:21,22 30:5,9 35:1,1,11 37:3 40:3 56:2 57:2 57:4,11,16 60:2,3,4 63:7 67:21 73:9 79:19 80:8,22 83:16 84:5,9,18 86:24 87:8,16 88:17,20,24,25 89:10,19 90:22,24 91:1,10,13,15,18 109:17,18,18,22 110:4,5 111:21,25 112:2,8,12,13,14 112:16,23 113:5 124:8,9 126:11 130:1 134:1 147:15 147:16 <b>markets (17)</b> 12:19 13:8,24 77:17 109:15,16,23 110:24 111:2,19 112:18 123:21,23 123:23,24 147:12 147:13 <b>MasterCard (132)</b> 2:17 8:7,14,19 11:4 11:6,8,12,13 12:22 13:17 16:4,16 17:18 18:22 19:22 20:20 21:1,6,10,19 21:24 22:3,16 23:24,25 24:4,6,24 25:24 26:18 27:4,6 28:5 30:25 31:21 31:23 32:4,8,11,13 32:23 33:10,12,21 34:8,25 35:11 40:12,16 41:1 44:11 48:19 56:16 57:3,6,7,11,15,20 57:21 59:3 60:9	63:2,6,7,8 64:2 65:7 66:19,22,23 67:9,16 70:15 72:20 73:8 75:14 77:12 78:7,18,25 79:10 80:8 82:3 86:23 88:13,25 89:2,2 90:17,23 91:7,9,13 93:6,6 102:2 108:25 109:7 109:11 110:17,18 110:19,21 111:20 115:6 116:1,4,11 122:15 123:4,8,11 123:16 124:3,14 125:2 126:17,22,24 129:11,12 130:23 134:16,18,19,23 135:9,25 136:4,9 <b>MasterCard's (11)</b> 7:24 20:2 21:9 22:22 24:3,6 25:15 26:12 27:13 34:23 77:8 <b>MasterCards (4)</b> 122:16,17,18 123:9 <b>material (5)</b> 9:17 25:19 27:13 120:3 126:6 <b>materialise (1)</b> 127:24 <b>materially (6)</b> 22:22 23:14 26:11 67:14 77:11 116:1 <b>matter (35)</b> 4:17,23 5:3 10:7 16:12 18:17 20:9,18 22:4 23:21 36:23 37:20 38:11 46:12 51:7 52:2,10 53:12,12 59:12 65:17 81:18 93:24 102:4 109:20 112:20 124:18,22 143:21 158:1,2,3 159:24,25 161:12 <b>matters (6)</b> 5:24 23:22 41:18 98:8 106:23 161:20 <b>maximise (1)</b> 129:12 <b>maximum (1)</b> 32:5 <b>meal (3)</b> 117:15,17 168:11 <b>mean (12)</b> 10:25 37:19 38:25 62:3 76:2,7 83:4 84:1 107:18 131:13 139:4 147:3 <b>meaning (2)</b> 9:3 122:25 <b>means (8)</b> 2:25 11:2 40:15 41:7 46:20 61:11 130:16 144:11 <b>meant (2)</b> 21:15 31:22 <b>measure (7)</b> 97:2 112:2,5,7 124:4,7 137:7 <b>mechanical (1)</b> 46:7 <b>median (3)</b> 161:4 163:19,21 <b>medium (7)</b> 78:3 79:1 87:18 150:3,10,23 151:10 <b>medium-term (2)</b> 151:17 152:16 <b>member (2)</b> 29:17,20 <b>members (4)</b> 51:22 143:3,10,13 <b>memorandum (1)</b> 68:15	<b>memories (1)</b> 92:18 <b>memory (4)</b> 60:20 137:1,2 165:5 <b>mentioned (1)</b> 105:4 <b>mentions (1)</b> 7:3 <b>merchant (53)</b> 25:17 25:22 26:11,17 28:1 45:21 47:6,14 47:15 51:19 61:18 61:24 62:12 68:16 77:17 78:10 80:4 86:21,22,24 114:16 114:20 117:16 118:1,6,7,11,14,22 118:24 125:1,5 126:15 138:2,4 141:1 146:16 150:14 152:1,3 155:20 157:1 158:8 158:9,18 159:15 160:17,18,23 161:19 166:10,20 166:21 <b>merchant's (3)</b> 150:8 152:21 153:7 <b>merchants (132)</b> 2:18 2:22 3:4 8:18 23:9 23:12 26:23 31:13 51:16,17 64:14,22 64:23 66:21 67:1 67:17 68:1,7 71:15 72:2,5,6 73:6 80:9 80:19 84:5 89:9,14 89:22 90:13 113:8 113:13,15,16,17,21 113:22 114:5,7,12 114:16,23 115:1 117:2,7,20 119:10 119:11,17,22 120:1 120:4,19 122:4,5,9 122:15,17 123:6,8 124:19 125:18,19 125:20,23 126:1,2 126:16,17 128:20 128:23,24 130:7,9 130:12,18 131:23 133:16 137:14 138:9,10 139:24 140:3 144:9,13,21 144:24 145:4,8,17 146:5,9,24 147:3,5 147:8 148:17,18,21 149:7 150:13 151:5 154:17,24 155:19 157:5,16,18,20,21 157:22 159:3,10,12 159:15 160:3,24 161:5,17 162:19,21 163:1,6,8,16 164:2 164:4,6,8,10,11,13 166:18 <b>merchants' (6)</b> 145:21 150:25 153:10,19 154:20 156:19 <b>merely (1)</b> 143:18 <b>merit (1)</b> 103:16 <b>meruit (1)</b> 48:7 <b>methodologies (2)</b> 140:21,22 <b>methodology (3)</b> 141:6,9,25 <b>methods (2)</b> 117:4 158:8 <b>mid-point (1)</b> 40:11 <b>middle (3)</b> 62:7,8 94:25 <b>MIF (205)</b> 2:23,25 3:10,23 6:15,20,21 7:25 8:8 9:24 10:4	10:5,22,24 11:4,12 11:13 12:5 16:12 16:20 19:22,23 20:3,11,14,25,25 21:2,3,9,13 22:18 23:6,15,24 25:8,16 27:14 32:4 33:11 34:17,23 40:14 43:7 48:20 49:13 50:17 52:19 53:17 54:1,12,25 55:17 55:18 56:17 57:5 58:18,18,23 59:7 59:12,18 61:6,7 65:13 66:19 68:8 72:18 73:7,7 74:3 75:20 76:5 79:9 82:3,10,10 84:2 89:7 91:20,20,22 91:22 92:24 93:1,4 93:8,12 94:5,6,8,11 94:12,17,21 95:7 95:20 96:16,19,23 98:12,20 99:7,16 99:17,18,21 101:18 101:20,23 102:3,21 103:2 104:16,19,23 109:2,6,8,9,12 111:22 113:2,4 115:13 120:23,24 124:20 125:21 126:23 127:20,20 128:4,6,6,7,13,18 128:19,20,20 129:4 129:11,14,20 130:4 130:6,9,10 131:4,5 131:8,17,20,21 132:6,13,14,18,20 133:12,14,15,18,24 134:11,14,19,23 135:2,11,14 136:18 137:20,21 138:14 138:15,23 139:7,8 139:12,12,19 140:9 140:11,19 141:1 142:1 143:3 144:12 144:12,18 146:23 147:4,7,12 148:20 152:13 153:17 156:7,11 162:7 163:16 166:17 169:1 <b>MIFs (20)</b> 21:12 23:14 23:19 26:12,18 27:6 67:9,14,18 76:25 77:11 82:15 83:14 84:6 101:22 103:18 143:9,12 144:5 160:16 <b>migrate (2)</b> 22:25 25:6 <b>migration (3)</b> 36:24 58:5 63:25 <b>miles (1)</b> 97:15 <b>million (6)</b> 40:17,18 40:22 86:5 97:15 133:19 <b>millions (1)</b> 86:2 <b>mind (4)</b> 6:24 7:6 39:17 103:2 <b>minds (1)</b> 103:5 <b>mine (1)</b> 37:19 <b>minus (1)</b> 47:9 <b>minutes (1)</b> 169:15 <b>missed (1)</b> 119:15 <b>misses (1)</b> 96:11 <b>missing (1)</b> 85:16 <b>MIT (16)</b> 64:9,25 141:2,5,16,25 143:19 153:15	161:7,17 163:19,24 164:2,6,10,13 <b>MIT-MIF (16)</b> 64:10 140:5 141:23 149:22 150:1 152:15 158:5 159:11,18 160:22 163:7 165:14 166:4 166:15 167:14,17 <b>mixing (1)</b> 98:8 <b>model (5)</b> 26:2 150:22 150:23 156:16,18 <b>models (2)</b> 150:2,3 <b>moment (2)</b> 19:15 62:12 <b>money (19)</b> 33:2 43:24 46:21,22 62:1 72:17 73:15 118:2,3,8,12,13,22 119:24 120:18 136:10 138:3,4,6 <b>month (1)</b> 117:9 <b>morning (8)</b> 1:4,5 115:4 116:3 135:9 135:12 139:10 170:3 <b>mouth (1)</b> 97:5 <b>move (11)</b> 3:24 9:2 22:11 27:20 47:5 48:24 58:11 76:21 78:25 106:13 148:23 <b>moved (4)</b> 46:19 74:11 75:22 113:8 <b>moves (3)</b> 41:8 47:12 62:1 <b>moving (5)</b> 19:14 40:17,19 92:12 107:6 <b>MSC (13)</b> 68:22 69:4 75:18 85:8 115:25 161:14,17 163:20 163:24 164:2,6,10 164:13 <b>MSCs (5)</b> 25:23 31:11 160:16 161:8 163:16 <b>multilaterally (1)</b> 137:16	13:11 14:21,21,23 42:22 46:14 50:14 55:8,13,24 56:24 57:4,10,15,23 92:6 109:4 <b>neck (1)</b> 72:24 <b>need (25)</b> 1:15 4:2 9:14 15:4,12 16:6 24:13,14,25 30:15 49:14,15 52:18 53:25 57:12 60:24 100:22 127:11 137:1,15 145:3 150:7 155:4,7 161:1 <b>needing (1)</b> 137:3 <b>needn't (1)</b> 145:23 <b>needs (1)</b> 53:8 <b>negative (2)</b> 60:1 121:12 <b>negligent (1)</b> 96:10 <b>negotiate (1)</b> 67:17 <b>negotiated (5)</b> 28:3 31:1 116:10 135:5 136:14 <b>negotiating (3)</b> 49:16 63:18 67:3 <b>negotiation (2)</b> 30:2 116:8 <b>negotiations (9)</b> 27:23 28:7,11,20 30:6,23 63:16 64:11 90:9 <b>neither (3)</b> 31:15 33:10 168:3 <b>nervous (1)</b> 97:4 <b>net (6)</b> 47:12 117:10 117:18 118:13 121:15 149:14 <b>net/net (1)</b> 47:14 <b>neutral (3)</b> 121:16 144:14 156:10 <b>never (6)</b> 65:2 90:4 94:12 102:18 108:14 141:25 <b>nevertheless (1)</b> 5:4 <b>new (9)</b> 21:2 24:3,23 24:24 60:2,25 73:10 76:22 107:22 <b>newspaper (1)</b> 76:12 <b>nice (2)</b> 117:15 168:11 <b>Niels (37)</b> 20:2 30:10 32:19 35:22 38:1 65:16 66:3 78:16 84:8,25 91:25 94:20,24 119:3 141:9 149:25 150:4 150:16 152:4 156:13,13,14,14 161:22 162:18,20 162:23,25 163:1 166:25 167:16,24 168:3,16,18 169:3 169:5 <b>Niels' (1)</b> 37:17 <b>ninth (1)</b> 119:1 <b>nodding (2)</b> 55:11 77:21 <b>non-caterisled (1)</b> 96:4 <b>non-cost-based (1)</b> 107:22 <b>normally (2)</b> 153:1,20 <b>note (4)</b> 28:2 116:6 166:22 168:20 <b>notice (2)</b> 81:12,20 <b>noticeable (1)</b> 1:18 <b>notified (1)</b> 126:7 <b>notion (1)</b> 121:6 <b>nowadays (1)</b> 98:15	<b>nuance (1)</b> 168:23 <b>nuanced (2)</b> 112:15 168:22 <b>nub (3)</b> 108:22 109:13 111:3 <b>number (25)</b> 6:13 14:13,17 15:14 53:19 54:14 65:25 67:12 83:22 91:7 94:1 107:5,12 108:6,10 113:1 129:9,12 137:13 141:24 148:11 161:2 162:15,21 163:16 <b>numbering (2)</b> 68:18 69:2 <b>numbers (4)</b> 108:14 108:14,15,16 <b>numerous (1)</b> 18:7 <b>nutshell (1)</b> 92:5
<b>O</b>						
<b>o'clock (1)</b> 87:25 <b>O2 (3)</b> 11:19,21 88:8 <b>oath (1)</b> 5:3 <b>objective (30)</b> 8:5 9:1 9:11,21,25 10:18 13:11 14:21,22 42:22 50:14 52:2 55:8,13,24 56:24 57:4,10,14,23 92:6 108:1 109:4 112:6 121:14 125:20 <b>objectively (5)</b> 8:9,23 15:1 46:16 57:5 <b>objectives (1)</b> 148:2 <b>obligations (2)</b> 20:10 29:15 <b>oblige (1)</b> 25:7 <b>obliged (1)</b> 20:20 <b>obtain (3)</b> 16:2 41:6 130:12 <b>obtained (1)</b> 166:4 <b>obtains (1)</b> 125:2 <b>obvious (9)</b> 65:5 70:19 119:5 130:5 151:2 152:14 155:10 156:18,21 <b>obviously (1)</b> 1:15 7:13 9:8 69:17 81:14 132:21 134:7 141:6 160:19 <b>occasion (1)</b> 63:15 <b>occasions (3)</b> 105:5 107:12 141:25 <b>occur (4)</b> 8:23 17:3 36:24 77:1 <b>occurred (2)</b> 8:4 93:17 <b>occurs (1)</b> 14:1 <b>odd (2)</b> 43:22 106:24 <b>oddy (2)</b> 85:9 136:21 <b>offer (6)</b> 65:22 113:23 114:5 116:19 119:11,13 <b>offered (2)</b> 26:18 113:21 <b>offering (1)</b> 27:6 <b>offers (1)</b> 156:23 <b>OFF (8)</b> 17:23,23,24 21:20,23 33:24 60:15,20 <b>OFF's (1)</b> 21:19 <b>okay (4)</b> 19:18 36:9 52:7 72:17 <b>old (1)</b> 114:2 <b>old-fashioned (1)</b> 118:20						

<p><b>older (1)</b> 69:9 <b>once (6)</b> 37:1 99:2 103:19 104:22 147:9 148:19 <b>ones (5)</b> 19:17,18 32:17 39:14 139:5 <b>online (15)</b> 119:4,7,9 119:11,13 120:13 150:19 167:5,7,13 167:14,17,18,25 168:2 <b>onwards (3)</b> 129:9 140:20 141:23 <b>open (3)</b> 16:15 39:17 74:2 <b>opened (2)</b> 148:19,20 <b>opening (15)</b> 1:7,10 4:10 9:18,22,24 10:14 11:23 12:8 28:24 106:15 110:13 113:19 143:16 149:1 <b>operate (15)</b> 9:23 11:7,9 43:17 50:16 50:17 52:14,25 53:21,21,22,24 55:15 56:17 109:3 <b>operated (2)</b> 12:17 53:18 <b>operates (2)</b> 12:9 53:17 <b>operating (2)</b> 19:5,6 <b>operation (2)</b> 15:8 151:22 <b>operations (1)</b> 151:6 <b>operator (2)</b> 11:6 77:19 <b>operators (1)</b> 18:14 <b>opinion (3)</b> 19:20 63:16 65:18 <b>opinions (1)</b> 19:21 <b>opposed (2)</b> 53:13 132:13 <b>opposite (1)</b> 24:22 <b>optimum (1)</b> 159:18 <b>optimal (3)</b> 9:7 16:3 113:19 <b>orally (4)</b> 2:9 7:22 19:20 25:9 <b>order (20)</b> 12:5 18:21 26:19 27:14 50:22 65:13 67:1 85:24 93:2 94:17 95:16 98:8 100:5 104:1 105:1 107:5 115:16 124:3 144:23 164:24 <b>orders (1)</b> 82:12 <b>organised (1)</b> 76:14 <b>original (4)</b> 74:12 85:6 85:7,7 <b>originally (1)</b> 21:14 <b>ought (2)</b> 50:20 105:6 <b>outcome (2)</b> 22:1 56:25 <b>outlier (1)</b> 110:19 <b>outlined (1)</b> 139:5 <b>outlook (1)</b> 54:24 <b>outside (2)</b> 14:25 122:24 <b>outweigh (3)</b> 114:25 115:14 119:12 <b>outweighed (1)</b> 113:25 <b>overall (2)</b> 114:6 121:13 <b>overcharge (7)</b> 93:19 95:17,22 96:20 99:12 104:6 169:9</p>	<p><b>overturned (1)</b> 5:17 <b>overwhelming (1)</b> 120:3 <b>Oxera (2)</b> 165:3,8</p> <hr/> <p><b>P</b></p> <p><b>page (70)</b> 3:13 4:3,7 7:11,19 9:15 10:10 12:22 14:16,20 15:22 16:7 19:14 20:8 22:6 23:3 25:14 26:6 28:25 29:1 30:11 31:2,19 32:22 34:14,21 35:7,14,15,17 44:20,21 63:11 65:24 66:1 68:17 68:20 69:1,6,8 70:7 74:19,20 85:6,10 85:10,11 88:7 92:14 106:14 108:17 111:14 113:12 123:12 125:12 126:2,20 133:7,11 140:16 143:15 149:9 158:12,13 159:2 160:21 163:14,23 164:21 171:2 <b>paid (7)</b> 68:22 69:4 85:8 95:15,18 117:14 168:10 <b>palliate (1)</b> 161:21 <b>paper (2)</b> 3:12 165:21 <b>par (4)</b> 59:19 61:8 89:4,7 <b>parade (1)</b> 96:9 <b>paragraph (63)</b> 3:14 4:12,18 7:23 10:10 10:19 11:19,21,21 12:21 13:12 15:22 16:9 17:15 18:4 19:4,8 25:4 27:4,10 27:21 30:14 31:10 31:16,20 40:9 42:24 48:11 82:12 91:12,25 106:17 107:11 112:25 115:10 120:6 121:6 122:11 125:8,11 126:2,3 127:1,3,4 128:11 131:3 141:22 151:4 153:5 154:23 157:10,13 159:1,3 160:21 161:3 165:25 166:16,23,24 168:21 169:6 <b>paragraphs (4)</b> 16:8 60:16 111:14 123:12 <b>parallel (1)</b> 21:20 <b>parameters (1)</b> 16:20 <b>paraphrase (1)</b> 147:1 <b>paraphrasing (1)</b> 15:12 <b>parcel (2)</b> 95:21,23 <b>part (23)</b> 4:23 15:9 18:8 19:25 23:20 23:20,22 30:21 33:16 35:6 74:3,9 74:12 94:14 95:21 95:23 118:11 125:4 135:20 142:2 145:3 146:19,20 <b>partially (1)</b> 132:11 <b>participate (1)</b> 59:2 <b>participated (1)</b> 154:24</p>	<p><b>particular (19)</b> 1:16 4:11 6:6 12:15 13:22 15:25 16:1 39:24 50:4 65:23 66:8,12 84:14 97:21 98:14 123:13 126:9 128:2 161:10 <b>particularly (3)</b> 1:20 38:24 146:22 <b>parties (11)</b> 4:16 13:2 34:16 39:6 74:13 104:18,22 123:1,3 127:10 148:6 <b>parties' (1)</b> 19:16 <b>partly (1)</b> 90:6 <b>partner (1)</b> 29:7 <b>parts (1)</b> 92:12 <b>party (1)</b> 127:7 <b>pass-on (2)</b> 61:5 121:10 <b>pass-through (3)</b> 2:7 93:18 169:20 <b>passage (1)</b> 110:1 <b>passages (2)</b> 66:2 143:16 <b>passed (1)</b> 47:15 <b>passes (1)</b> 99:3 <b>passing (1)</b> 116:6 <b>Pause (8)</b> 25:1 30:14 35:21 68:18 85:11 92:20 111:16 125:14 <b>pay (21)</b> 44:7 63:5 64:22 65:22 78:13 87:2 89:23 90:5 115:25 116:12,18 117:8 118:3,6,7,10 118:17,18 136:10 138:6 139:25 <b>payee (1)</b> 62:1 <b>paying (2)</b> 51:19 84:6 <b>payment (53)</b> 2:24 3:1 3:3 6:17 16:15 29:2 29:3,4,5,6,8,10,14 29:15,16,18,19 37:6,7,18 41:6,8,12 42:6 44:25 45:14 46:20 48:15 56:16 61:16,17 62:19 84:12 109:17 116:17 117:4,25 119:3,18 122:4,6 128:14,16,21 129:5 130:15,16 133:25 134:3 151:6 158:7 166:3 167:8 <b>payments (2)</b> 115:21 116:23 <b>PayPal (2)</b> 167:10,24 <b>pays (1)</b> 90:6 <b>peanuts (1)</b> 40:23 <b>peculiarity (1)</b> 147:11 <b>pedal (2)</b> 22:24 23:10 <b>pedestrian (1)</b> 36:15 <b>pence (1)</b> 103:22 <b>pencil (12)</b> 43:10 45:10,24 46:7,10 46:13,15 47:18 49:2,5,10 50:7 <b>pencilling (1)</b> 49:8 <b>pencils (1)</b> 50:5 <b>pending (1)</b> 22:1 <b>people (34)</b> 3:5,6 21:22 27:17 32:17 36:19 43:12 60:2,4 60:7 71:6,16 73:20 75:9 76:8,9 78:2 79:16,17 80:14,21 81:21 84:20 87:10</p>	<p>113:5,6 114:3 115:8 138:9 141:12 141:14 145:5,6 155:11 <b>percentage (1)</b> 47:10 <b>perception (1)</b> 83:8 <b>Perez's (1)</b> 76:20 <b>perfect (10)</b> 53:16 102:12 156:13,14 161:24 162:22 167:1,11 168:3,22 <b>perfectionist (1)</b> 54:2 <b>perfectly (3)</b> 12:21 93:15 165:14 <b>performed (1)</b> 162:12 <b>period (47)</b> 20:12,18 20:19 24:17,21 25:17,21,22 26:10 26:15 27:12 28:9 28:13,18 30:4,4,18 30:20,24 33:10 34:25 35:4,13 40:11 56:20 62:23 67:15 69:22 71:25 73:8 79:9,18 95:15 96:11,23 115:24 117:9,20,22 118:10 119:19 120:12 138:14 142:19 151:5,10,15 <b>periods (2)</b> 25:20 129:23 <b>permanent (1)</b> 75:5 <b>pernicious (1)</b> 58:17 <b>person (6)</b> 15:4,5 33:4 97:19,22,22 <b>person's (1)</b> 97:23 <b>persons (1)</b> 122:23 <b>perspective (1)</b> 2:15 <b>persuade (1)</b> 39:18 <b>persuasive (1)</b> 4:22 <b>philosophically (1)</b> 54:17 <b>phrase (1)</b> 50:7 <b>pick (12)</b> 4:7 9:15 24:25 106:13 123:17 126:20 140:16,20 151:18 159:9 163:13 165:12 <b>piece (1)</b> 75:1 <b>pin (1)</b> 106:3 <b>pithy (1)</b> 4:11 <b>pivot (2)</b> 147:13,17 <b>place (18)</b> 14:9 28:19 28:20 30:7 31:9 45:6 46:6 48:14 50:24 52:14 54:14 79:7 138:20 150:18 166:3 168:8,15,16 <b>places (1)</b> 90:3 <b>plain (3)</b> 33:22 109:19 145:2 <b>plainly (1)</b> 141:11 <b>plant (3)</b> 84:15,16,23 <b>play (3)</b> 40:9 75:24 109:16 <b>player (1)</b> 77:16 <b>players (2)</b> 60:2 87:7 <b>plead (1)</b> 44:3 <b>please (1)</b> 17:14 <b>pleases (1)</b> 43:2 <b>plummeting (2)</b> 82:23 85:15 <b>pm (7)</b> 58:8,10 88:1,3 140:13,15 170:5 <b>pocket (1)</b> 118:14 <b>point (141)</b> 2:13,23,25 3:3 7:23 9:2 11:8</p>	<p>11:20 13:12 15:25 16:1 17:17,21,23 24:20 25:3,9 30:22 31:19 32:15 33:17 33:18 34:21 37:11 38:3 39:2,21,24 40:24 41:4 42:7 44:5,7 46:11,13,13 46:17 48:17,21 49:7,9 51:18 57:7,8 58:21,24 59:6,8 64:4,19 65:8,12,17 66:10,25 67:23 71:12,13 72:8,10 74:8,11 75:8,9,11 76:16 79:24 80:7 81:17 83:4 86:10 86:23 87:10,13,14 87:16,19,19,20 91:5,16 101:16,17 103:9 110:22 113:18 114:7,22 115:1,17,23 116:7 116:14,25 117:1,1 117:6,7,10,18 119:1,2,2,16,20,21 121:16 125:7 126:5 126:21 128:13 131:11,23 135:17 135:20,24 137:19 139:3,10,16,20,23 144:6 149:1,25 150:11,15 151:11 152:21 153:18 154:13 155:8,12,25 157:3 161:13 162:2 166:17,22 167:3 168:4 <b>pointed (2)</b> 10:14 119:15 <b>pointers (1)</b> 52:2 <b>pointing (1)</b> 1:22 <b>points (14)</b> 3:8 7:20 14:14 17:22 22:10 22:20 24:19 28:13 91:4 92:13 94:1 129:2 130:14 133:5 <b>poking (1)</b> 162:20 <b>poor (1)</b> 113:13 <b>popped (1)</b> 102:6 <b>Porsche (1)</b> 130:22 <b>portfolio (1)</b> 78:24 <b>portion (3)</b> 78:11,17 78:23 <b>posit (1)</b> 49:15 <b>positing (1)</b> 69:14 <b>position (26)</b> 5:10 21:3 35:11 46:17 46:20 51:4 55:17 58:24 65:6 66:11 72:6 77:13 82:5 86:22 89:18,24 90:19 93:16 113:10 125:10 143:5,21 144:12 145:17 148:5 155:6 <b>positive (1)</b> 121:19 <b>positively (1)</b> 18:16 <b>possibilities (3)</b> 39:19 54:15 67:3 <b>possible (13)</b> 50:21 53:7 54:10 55:6 62:18 78:11 101:22 135:20 138:17 149:17 157:16 164:22 165:14 <b>possibly (3)</b> 99:11 106:5 151:24 <b>postulated (1)</b> 78:20</p>	<p><b>postulating (1)</b> 71:25 <b>pot (2)</b> 78:6 98:8 <b>potential (6)</b> 39:14 50:10 59:20 97:17 127:25 153:13 <b>potentially (2)</b> 6:3 29:12 <b>pound (1)</b> 103:22 <b>power (2)</b> 42:9 67:3 <b>practical (5)</b> 35:25 53:16 55:6 96:9 127:17 <b>practice (1)</b> 140:3 <b>pre-empt (1)</b> 2:1 <b>precise (2)</b> 23:17 107:5 <b>Precisely (1)</b> 149:3 <b>precision (1)</b> 157:11 <b>predecessor (1)</b> 22:11 <b>prefer (3)</b> 38:11 63:13 83:1 <b>preferable (4)</b> 156:22 162:24 168:4,19 <b>preferred (1)</b> 167:2 <b>preferring (1)</b> 152:18 <b>prefers (3)</b> 141:9 150:4,10 <b>premise (1)</b> 42:16 <b>premised (1)</b> 57:2 <b>premium (3)</b> 31:24 32:7,9 <b>prepared (4)</b> 50:13 74:19 85:1 130:20 <b>present (8)</b> 16:9 24:17 75:13 108:24 111:24 117:10,18 118:13 <b>pressure (11)</b> 8:20 23:8,9 48:22 66:25 73:6 78:9 83:22 89:14 90:14 134:16 <b>pressures (1)</b> 25:7 <b>presumably (2)</b> 105:10 118:16 <b>presume (1)</b> 43:23 <b>presumption (3)</b> 19:9 42:5 93:12 <b>pretending (1)</b> 120:1 <b>pretty (6)</b> 6:16 13:17 40:22 76:7 78:1 156:21 <b>prevent (1)</b> 121:14 <b>previous (1)</b> 142:22 <b>price (19)</b> 16:24 60:11 87:2,3 95:12,15,18 95:18 96:4 99:7,10 100:4,5,8,10,15 126:8 138:24 147:13 <b>price-fixing (1)</b> 100:10 <b>pricing (1)</b> 16:15 <b>primarily (2)</b> 14:5 26:13 <b>primary (1)</b> 88:16 <b>principle (9)</b> 9:20 15:16 19:4 93:14 97:6 99:15 110:20 124:4 148:10 <b>principles (3)</b> 5:16 7:16 129:7 <b>prior (1)</b> 22:8 <b>prior-competitive (1)</b> 3:11 <b>probabilities (5)</b> 97:12 97:25 98:4 104:4 106:1 <b>probability (1)</b> 103:7 <b>probable (2)</b> 164:23 165:14</p>	<p><b>probably (21)</b> 2:8 3:12 17:20 36:12 37:19 39:4 52:8,15 56:10 61:4,7 73:19 79:20 89:10 90:17 92:11 104:21 152:25 159:23 160:1 169:14 <b>problem (21)</b> 41:9,13 41:20 42:19 43:3 59:25 60:6,7,25 63:10,20 142:3 144:3 152:13 153:9 154:23 155:16 161:20,21,23 167:12 <b>problems (7)</b> 15:14 37:16 51:9 142:11 156:12,19 162:15 <b>proceeding (4)</b> 21:18 21:19,20 99:20 <b>proceedings (3)</b> 4:4 21:4 143:4 <b>process (7)</b> 5:11 6:1 7:4 39:7 47:6 53:25 148:12 <b>processing (1)</b> 151:6 <b>produce (6)</b> 63:16 126:11 152:16 156:6,7,11 <b>produced (3)</b> 126:7 128:5 133:12 <b>producers (1)</b> 122:21 <b>produces (1)</b> 3:4 <b>producing (1)</b> 130:10 <b>product (2)</b> 67:16 73:10 <b>products (4)</b> 107:22 121:21 122:13,21 <b>profession (1)</b> 122:24 <b>Professor (16)</b> 41:16 42:4,12 69:6 105:1 108:8,11 138:22 139:2,8,20 149:2 151:20 152:6,9 158:14 <b>profitable (1)</b> 10:4 <b>profits (2)</b> 70:4 96:19 <b>prohibiting (1)</b> 16:15 <b>Project (2)</b> 130:22,22 <b>promise (1)</b> 36:8 <b>promoted (1)</b> 98:3 <b>promotes (1)</b> 147:9 <b>promotion (1)</b> 98:5 <b>proof (9)</b> 93:5 98:25 100:17 102:17,23 104:11 106:2 108:5 112:6 <b>proper (5)</b> 54:3 141:6 150:6 159:7 169:2 <b>properly (3)</b> 4:20 141:2 159:13 <b>proportion (1)</b> 152:2 <b>proportions (1)</b> 6:21 <b>proposed (6)</b> 19:16 33:17 40:14 53:20 55:1 153:25 <b>proposes (1)</b> 5:4 <b>proposition (5)</b> 17:7 18:3,19 90:2,6 <b>prosecution (1)</b> 102:10 <b>protect (1)</b> 87:6 <b>protecting (1)</b> 84:10 <b>protects (1)</b> 148:12 <b>prove (6)</b> 33:21 93:14 100:5 102:2 103:22 106:23 <b>proved (3)</b> 97:11</p>
---	--	---	--	---	--	---

108:4 157:20 <b>provide (5)</b> 43:9 66:6 68:13 144:4 149:15 <b>provided (6)</b> 26:5 29:16 43:22 114:15 120:11 125:19 <b>providers (1)</b> 29:3 <b>provides (1)</b> 117:10 <b>proving (1)</b> 100:18 <b>provision (1)</b> 53:10 <b>provisions (3)</b> 28:25 47:21 62:6 <b>provoked (1)</b> 65:1 <b>published (1)</b> 148:24 <b>pun (1)</b> 25:13 <b>punchline (1)</b> 39:9 <b>purchase (3)</b> 42:11 117:8 125:2 <b>purchasers (3)</b> 123:2,5 137:24 <b>purchases (5)</b> 40:12 120:13 128:22 150:19 168:8 <b>purely (2)</b> 61:1 106:1 <b>purpose (9)</b> 22:8 24:17 51:18 53:1 94:4 142:7 154:11 154:16,25 <b>purposes (7)</b> 10:16 19:7 23:22 29:9 111:4 122:23 146:20 <b>pursue (1)</b> 18:23 <b>push (1)</b> 100:25 <b>pushed (2)</b> 7:17 48:10 <b>put (56)</b> 8:20 17:20,25 18:4 19:15,25 22:13,23 32:15,17 32:18 35:10 39:15 40:7 46:3,13,16,18 49:9 52:13 53:22 54:13 62:21 63:9 66:13 67:4 68:11 70:2 73:6 76:4 77:11,13 83:22 84:8 87:11 89:14 93:16 97:4 107:5,9 108:2,10,14,21 112:25 120:2 125:8 131:14 132:25 133:2 135:21 143:7 152:4 155:5 165:4 169:3 <b>puts (3)</b> 64:3 76:12 98:7 <b>putting (10)</b> 10:2 18:20 24:22 49:21 54:6 90:13 107:18 114:3 116:8 135:24 <b>puzzled (1)</b> 48:4	16:13 17:2 20:16 22:2 23:21 38:22 43:15 49:23 50:9 51:20,25 52:10,15 52:21 53:1,2 55:4 55:20 56:18 62:21 63:13 65:25 66:12 66:17 67:20 69:15 74:21 76:19 79:14 81:2 83:17 84:1,8 86:19 90:14 92:21 92:24 93:1 94:22 95:11 96:22 98:11 98:12,19,24 101:20 102:20,22 103:14 106:5,6 109:14 110:3,6 111:12 125:6 126:22 132:16,21 133:17 133:19 140:8,10,18 146:16 150:12 155:7 158:16,21 <b>questionable (1)</b> 157:23 <b>questioning (4)</b> 39:16 46:18 62:24 63:1 <b>questions (15)</b> 1:12 1:14,25 2:2 26:6 39:17 42:22 55:11 56:25 67:4 68:14 86:13 91:5 92:23 104:21 <b>quick (2)</b> 74:25 85:15 <b>quickest (1)</b> 125:13 <b>quickly (6)</b> 9:18 34:15 35:16 36:14 88:5 133:22 <b>quite (42)</b> 1:18,21 3:13,15 5:19 9:17 14:6,10 17:9 31:10 34:11 36:18 48:5 54:16 55:10 71:11 74:18 75:3 76:22 91:11 94:7 97:9 99:23 105:4 107:2 109:14 112:18 115:14 122:2,9 125:15 136:13 138:18 139:15 148:7,15 151:25 153:22 158:3 164:22 166:7 168:14 <b>quote (13)</b> 11:22 13:17 15:23 30:13 110:10,11,16 113:14 122:20 140:24 142:24 153:5 158:10 <b>quotes (3)</b> 13:16 129:8 149:5	143:3,6 <b>rationality (1)</b> 81:21 <b>RBS (3)</b> 23:2,17 24:20 <b>re-examination (1)</b> 84:25 <b>re-write (1)</b> 49:3 <b>reach (3)</b> 61:18 98:8 105:12 <b>reached (1)</b> 4:15 <b>reaching (1)</b> 65:21 <b>read (18)</b> 3:12,16,16 3:17 30:13 31:17 35:16 69:20 70:8 105:9,17 107:17 108:9 111:15 115:10 123:13 125:13 126:2 <b>reading (4)</b> 35:17,18 121:20 124:6 <b>real (11)</b> 12:18,20 13:23 33:9 37:20 53:9 54:7 55:4 122:7 150:20 155:10 <b>realise (1)</b> 124:24 <b>realised (1)</b> 75:2 <b>realistic (15)</b> 7:24 10:13,23 17:11 20:7 30:18 33:16 34:2,7 35:24 36:1 71:19 127:10,12 167:25 <b>realistically (1)</b> 80:24 <b>realities (2)</b> 37:17 55:22 <b>reality (1)</b> 151:12 <b>really (54)</b> 1:7 2:14,20 3:8,25 5:23,25 9:6 11:16,18 13:12 18:1 19:24 34:15 37:7,8,15 38:21 40:20 46:12 49:21 49:23 51:21,25 52:4 59:8,24 65:17 66:2,5,13 74:12,20 75:4 84:1 92:5 101:17,23 107:1 110:10 117:14 121:8 126:4 142:16 142:19 146:12,16 150:15 153:9,22 155:21 158:2 161:12 166:11 <b>reason (18)</b> 6:14 23:7 23:17 30:16 68:5 71:18,21 84:7 87:7 94:13 96:8 114:17 119:5,10 141:17 147:15 152:18 167:24 <b>reasonable (2)</b> 107:3 166:4 <b>reasonably (2)</b> 106:19 127:9 <b>reasons (11)</b> 6:14 9:10 15:15 65:5 67:12 70:20 71:14 150:5 150:9 152:4 158:6 <b>recall (1)</b> 58:13 <b>receive (9)</b> 52:18 61:19 115:2,19 117:2 118:8 128:17 129:14 144:11 <b>received (2)</b> 40:16 98:5 <b>receives (2)</b> 89:6 116:16 <b>receiving (1)</b> 132:1 <b>Recital (1)</b> 143:2	<b>recitation (1)</b> 17:5 <b>recognise (2)</b> 17:20 26:8 <b>recognised (1)</b> 158:9 <b>recognises (1)</b> 157:9 <b>recollection (1)</b> 137:11 <b>recover (1)</b> 100:6 <b>recoverable (1)</b> 95:16 <b>recovery (1)</b> 104:1 <b>reddid (1)</b> 165:6 <b>reduce (2)</b> 76:5 127:22 <b>reduced (6)</b> 23:19 33:10 36:21 88:18 130:5,15 <b>reducing (1)</b> 22:23 <b>reduction (2)</b> 31:11 91:10 <b>refer (1)</b> 148:2 <b>reference (13)</b> 1:16,19 3:25 15:20 17:16 45:11 97:20 110:1 110:15 115:7 148:9 158:13 159:7 <b>referenced (1)</b> 3:14 <b>references (2)</b> 60:24 120:9 <b>referred (6)</b> 16:3 60:22 106:15 109:24 125:25 138:19 <b>reflect (1)</b> 159:14 <b>refresh (2)</b> 92:18 137:1 <b>refuse (2)</b> 67:5,6 <b>refused (2)</b> 69:16 86:14 <b>regard (5)</b> 5:15 12:13 13:22 103:10 110:2 <b>regarded (2)</b> 4:22 122:24 <b>regarding (1)</b> 64:10 <b>regardless (1)</b> 14:1 <b>register (1)</b> 61:25 <b>regulate (1)</b> 149:16 <b>regulation (24)</b> 24:11 26:22 27:21 28:4 28:10,15,22,23 29:10,23 30:19 31:21 33:14 41:2 89:17,19,20,21,25 106:25 116:8 140:7 142:13,14 <b>regulator (2)</b> 23:11 98:13 <b>regulators (1)</b> 73:6 <b>regulatory (11)</b> 20:9 20:10,14,16,17,18 20:20 21:5,15 30:8 149:12 <b>reigns (1)</b> 86:24 <b>reiterating (1)</b> 145:1 <b>reject (2)</b> 8:10 57:14 <b>rejected (1)</b> 112:23 <b>related (1)</b> 27:24 <b>relates (1)</b> 168:5 <b>relating (5)</b> 21:8 25:21 27:11,20 31:3 <b>relation (9)</b> 10:20 13:24 18:2 26:23 29:13 98:24 116:15 117:22 159:10 <b>relationship (3)</b> 16:23 17:2 117:24 <b>relative (2)</b> 17:2 158:7 <b>relatively (2)</b> 2:4 88:5 <b>relevance (2)</b> 4:9 133:6	<b>relevant (26)</b> 10:11 12:7,14 13:13,21 14:2 28:16 30:23 38:7 45:9 73:8 109:5 110:4 112:7 121:7 123:21,23,23 123:24 125:1,3 128:9 129:16 140:21 146:25 167:4 <b>reliable (1)</b> 157:16 <b>reliance (4)</b> 17:16 33:24,24 166:1 <b>relied (3)</b> 15:24 31:5 112:21 <b>relies (1)</b> 166:9 <b>rely (7)</b> 17:22 18:4 112:21 150:7 153:12 155:23 160:17 <b>relying (11)</b> 150:25 152:20 153:7,10 154:19 155:17 156:19 159:10 161:17 162:17 166:13 <b>remain (4)</b> 12:25 16:16 47:23 50:24 <b>remained (5)</b> 20:4 34:24 40:4,5 57:17 <b>remaining (1)</b> 82:4 <b>remains (2)</b> 53:10 134:13 <b>remark (1)</b> 3:7 <b>remember (24)</b> 6:5 26:3 27:3 31:4 32:2 35:5,6,8 48:17 63:4 69:14 70:2 72:13 83:12 88:8 90:1 110:12 115:4 155:12 156:3 162:9 163:5,14 164:16 <b>reminded (1)</b> 39:24 <b>remove (1)</b> 45:10 <b>removed (3)</b> 50:20 101:1,2 <b>removing (1)</b> 47:22 <b>repeated (1)</b> 66:10 <b>repeatedly (1)</b> 5:18 <b>reply (2)</b> 169:17,22 <b>report (6)</b> 3:18 20:1 34:19 41:4 129:17 163:5 <b>reports (3)</b> 31:4 74:13 105:15 <b>represent (1)</b> 166:5 <b>representative (1)</b> 155:20 <b>representativeness ...</b> 157:12 <b>require (1)</b> 54:18 <b>required (4)</b> 88:9 103:21 118:12 127:6 <b>requires (4)</b> 20:7 34:4 156:1,9 <b>requiring (1)</b> 4:14 <b>research (1)</b> 143:17 <b>resolve (1)</b> 37:1 <b>resolves (1)</b> 57:8 <b>resources (1)</b> 121:22 <b>respect (9)</b> 4:17 10:2 20:11 25:24 81:17 85:3 91:8 124:8 165:20 <b>respects (1)</b> 137:6 <b>respond (1)</b> 22:15 <b>responds (1)</b> 75:8 <b>response (11)</b> 4:8	26:5 45:23 68:14 75:12,17 80:5 153:24,25 154:2,9 <b>rest (6)</b> 45:9 50:22 52:11 74:1 87:22 87:24 <b>restaurant (1)</b> 117:12 <b>restitution (1)</b> 44:9 <b>restraint (6)</b> 2:6 10:20 11:3 34:13 56:13 56:15 <b>restraint-type (1)</b> 43:18 <b>restraints (1)</b> 9:19 <b>restraints/objective ...</b> 46:14 <b>restriction (46)</b> 2:5,6 3:10 4:1 7:18,20 9:2,11,13 10:18 11:15 12:6 13:5,7 13:19 14:5,24 15:7 55:8,15 56:23 57:6 57:8,11,13,14,18 58:1,15,16,25 59:13,21 61:10 88:4 92:7 99:13 112:11 121:13 124:8 127:19 128:2 136:24,25 137:7,8 <b>restrictive (7)</b> 16:13 53:11 59:7 111:24 112:2 127:12 128:3 <b>result (10)</b> 18:15 30:25 62:13 84:5 95:23 129:25 137:14 149:12 152:17 158:5 <b>resulting (3)</b> 76:25 112:5 168:5 <b>results (4)</b> 144:6 163:21,22 165:11 <b>retail (3)</b> 73:1 76:15 158:21 <b>retail-based (1)</b> 161:6 <b>retailer (7)</b> 72:14 75:12,23 84:14 90:6 166:3,5 <b>retailers (19)</b> 31:15 67:6 73:16 75:13 79:8 83:11,19,22 90:2 115:19 122:22 137:24 152:25 153:19 159:16,19 163:25 164:19,19 <b>retailers' (1)</b> 149:14 <b>retain (1)</b> 59:17 <b>retained (3)</b> 23:5 24:4 25:19 <b>retains (1)</b> 47:13 <b>retention (1)</b> 47:8 <b>revenue (1)</b> 40:17 <b>revenues (1)</b> 76:25 <b>review (3)</b> 6:8,12,13 <b>reviewing (1)</b> 6:6 <b>reviews (1)</b> 106:10 <b>rewards (8)</b> 120:14,15 120:17 129:19,19 129:24 137:22,22 <b>ridiculous (1)</b> 32:17 <b>right (38)</b> 6:18 9:13 14:18 15:15 30:16 35:20 36:7 41:23 43:1 45:2,18 46:1 49:22 50:6 56:10 61:4 64:17 65:11 71:4 77:8 80:2 85:3 93:10,19 95:5 98:17 102:8 104:9 105:2 111:7 131:6	131:10 132:16 135:8 138:11 141:12 161:25 162:11 <b>rightly (2)</b> 97:9 105:4 <b>rise (10)</b> 18:7 27:8,18 44:24 45:14 102:14 108:25 150:23 152:6 155:2 <b>risk (5)</b> 33:12 154:24 155:2,8,10 <b>rival (2)</b> 84:3,4 <b>robust (1)</b> 106:20 <b>Rochet (13)</b> 142:8,9 143:24,25 144:2 147:23 148:23 149:2,10,19 159:12 159:21 166:8 <b>Rogers (6)</b> 66:14 74:7 77:14 78:1,24 80:4 <b>role (1)</b> 79:22 <b>room (1)</b> 58:1 <b>roughly (2)</b> 24:24 75:17 <b>round (3)</b> 13:16 67:18 131:24 <b>route (3)</b> 49:14 98:11 156:22 <b>rubbish (3)</b> 154:21 155:14,22 <b>rule (20)</b> 12:25 42:10 42:19,23,25 44:10 46:11 48:19 49:4 49:16 51:1 52:17 58:21 59:1,22 61:4 61:25 63:2,22 89:8 <b>rule,that (1)</b> 103:25 <b>rules (14)</b> 12:24 43:9 44:6,11,13 47:20 49:24 50:4,10,22 52:1,12 61:21 62:4 <b>rumbblings (1)</b> 73:2 <b>run (2)</b> 75:15 150:2 <b>running (1)</b> 88:21 <b>Rysman (2)</b> 151:11 159:6
<b>Q</b>	<b>R</b>					<b>S</b>
<b>qualified (1)</b> 92:25 <b>qualitative (3)</b> 108:3 108:12,16 <b>quality (2)</b> 16:24 110:7 <b>quantification (1)</b> 102:4 <b>quantitative (1)</b> 108:4 <b>quantity (1)</b> 16:24 <b>quantum (5)</b> 43:20 44:1 48:7,7 51:13 <b>quashed (2)</b> 18:1 21:19 <b>quest (1)</b> 105:9 <b>question (78)</b> 2:5 4:8 10:8,9 11:11,12 12:19 13:9 15:20	<b>raise (2)</b> 22:17 23:15 <b>raised (7)</b> 22:24 23:23 73:7 74:16 92:21 92:22 151:11 <b>raises (1)</b> 62:21 <b>raising (1)</b> 97:7 <b>range (14)</b> 103:2,6,12 103:15,17,18,19 104:4,8,12 169:5,8 169:8,10 <b>rate (10)</b> 22:16 23:7 24:6 25:23 26:11 28:1,3,3 31:1 59:5 <b>rates (11)</b> 8:2,2,20 25:18 26:17 32:9 67:19 77:11 89:15					<b>safe (2)</b> 169:16,25 <b>Sainsbury (1)</b> 83:6 <b>Sainsbury's (8)</b> 1:18 2:12 9:7,24 11:17 14:13 15:3 16:6 17:14 19:15 25:3 27:22 28:10 30:3 31:14 32:3,22 33:17 65:2 68:12 68:16 69:15 70:4 71:16,19 72:16 74:16 76:11 77:14 77:16 79:17 81:15 82:18 83:8,10,20 85:4,17 88:21 90:9 93:2,9 94:17 96:17 96:18 102:4 103:21 104:13,16 115:3,15 115:18,21,24 116:10,11,12,16,17 116:17,18,21 136:12 139:13 153:24 154:2,9,14 154:21 155:4,9,14 155:18,22 156:24 162:11,13 165:17 166:1,11,13,16,22 <b>sake (1)</b> 77:7 <b>salary (1)</b> 98:6 <b>sales (7)</b> 69:17,21,24 72:18 116:20 166:6

168:5	118:23 123:16	136:16 137:15	<b>short-term (6)</b> 21:16	169:18	<b>sort (35)</b> 7:7 21:24	87:17
<b>sample (11)</b> 155:17,23	124:3 128:8,21	138:7 146:12,19	78:3,5,8,22 120:10	<b>six (2)</b> 60:10 164:7	34:3 36:24 37:3	<b>stepped (1)</b> 82:17
156:23 157:1,12	134:20,21,22	163:23	<b>shot (1)</b> 81:20	<b>sixth (3)</b> 60:11 116:25	38:4 40:6 42:21	<b>steps (1)</b> 8:13
162:17,18 163:1,2	137:14 167:8	<b>sensible (1)</b> 169:23	<b>shoulder (1)</b> 116:9	155:12	43:13 44:3 48:6	<b>stick (1)</b> 39:15
166:2,11	<b>schemes (14)</b> 2:24 3:1	<b>sensitive (1)</b> 131:1	<b>shout (1)</b> 77:24	<b>size (5)</b> 157:12 158:8	53:16 54:22,24	<b>sticking (2)</b> 72:24
<b>sand (1)</b> 39:15	26:12 27:9 66:7	<b>sensitivity (5)</b> 162:10	<b>shove (1)</b> 100:25	158:17 160:23	55:19 64:18 70:3	78:15
<b>sat (1)</b> 102:18	77:18 84:12 109:17	162:12 163:4	<b>show (24)</b> 5:21 35:8	161:15	79:6,6 95:9 96:8	<b>sticks (1)</b> 162:20
<b>satisfaction (1)</b> 103:7	113:5,21 114:13	165:20 166:14	39:8 44:14 70:5	<b>skeleton (2)</b> 35:6	98:1,7 103:6	<b>stocks (1)</b> 28:15
<b>satisfactory (1)</b> 7:10	128:15 129:4 134:3	<b>sentence (3)</b> 123:18	71:17 93:6,11,22	82:13	136:22 137:2,5	<b>stood (3)</b> 33:13 79:18
<b>satisfied (7)</b> 93:7,23	<b>scientific (1)</b> 141:20	126:3 130:25	95:17 104:20,25	<b>slate (1)</b> 114:4	145:22 151:13	80:21
105:19,20 133:24	<b>scope (4)</b> 14:25 109:5	<b>separate (4)</b> 75:11	105:1,3 111:10	<b>sliding (1)</b> 132:2	153:1 161:9 163:11	<b>stop (12)</b> 26:25 27:16
134:13 147:6	143:4 148:17	112:2 132:21	121:24 126:15	<b>slightly (3)</b> 36:14	164:15 167:20,23	68:3,9,10 69:16
<b>satisfies (3)</b> 133:18	<b>second (30)</b> 1:14 2:23	161:14	144:9,23 148:15	145:17 169:21	<b>sorts (4)</b> 37:14 40:8	71:20 72:14,21
140:19 141:3	4:8 8:17 14:18 16:7	<b>serious (1)</b> 120:2	158:11 161:4	<b>slow (1)</b> 160:19	149:4 169:6	76:9 83:19 170:2
<b>satisfy (7)</b> 95:4 104:5	20:16 30:22 31:19	<b>serve (1)</b> 143:17	162:10 165:2	<b>small (5)</b> 74:3 76:1	<b>sought (2)</b> 19:2	<b>stopped (2)</b> 23:11
105:21 108:5	34:21 41:4 63:15	<b>service (11)</b> 12:17	<b>showed (3)</b> 89:19	157:15,20,22	165:25	26:21
109:12 128:4	67:23 69:18 71:21	29:3 45:1,3,5 46:2	143:16 166:19	<b>smaller (3)</b> 10:3 109:9	<b>soup (2)</b> 117:13,15	<b>stopping (1)</b> 77:21
134:20	111:5,6 114:7	46:5 47:14 78:10	<b>showing (1)</b> 47:18	163:6	<b>speak (1)</b> 111:15	<b>store (4)</b> 114:3 118:15
<b>save (3)</b> 26:23 79:13	121:3,19 125:5,6	110:7 161:5	<b>shown (5)</b> 14:25 70:6	<b>Smith (104)</b> 21:18	<b>speaking (3)</b> 38:9	118:19,21
83:24	125:16 144:8,10	<b>services (8)</b> 13:23	124:19 153:23	24:6,9,11 42:24	119:6 131:21	<b>stores (2)</b> 73:21
<b>saved (1)</b> 136:10	145:3,25 150:11	16:25 43:22 48:9	165:13	44:11,15,19,21,23	<b>specific (2)</b> 7:1 25:13	116:20
<b>saving (3)</b> 64:15 78:17	152:20 157:3	53:6 68:16 119:11	<b>shows (8)</b> 1:23 22:21	46:25 47:12,17,25	<b>specifically (1)</b> 110:18	<b>story (6)</b> 5:20 22:7
78:22	<b>second-guessed (1)</b>	119:14	23:13 25:15 26:10	48:4,12,16,24	<b>speculate (2)</b> 81:9,24	23:21,23 116:17
<b>saw (8)</b> 11:22 12:8	127:8	<b>set (52)</b> 1:8 11:22	163:10 165:11,12	49:11,19,21 50:6	<b>speculation (2)</b> 80:23	133:9
24:4 26:3 33:15	<b>Secondly (2)</b> 77:25	12:11 18:4 20:12	<b>side (17)</b> 46:23,25	50:18 51:2,15 52:7	81:11	<b>straightforward (1)</b>
73:7 82:21 115:5	94:19	22:16 27:10 31:16	51:20 66:20 78:18	53:2 54:4,21 56:22	<b>speculative (1)</b> 56:13	152:23
<b>saying (43)</b> 3:21 4:10	<b>section (1)</b> 44:13	31:23 32:4,9 33:7	78:19 102:18 104:2	57:3,25 58:3,11,21	<b>spend (5)</b> 1:21 71:16	<b>strange (1)</b> 147:1
7:3 21:24 26:23	<b>sector (1)</b> 18:9	34:18 35:3,14	104:7,23,24 123:5	60:8,15 61:16 62:8	115:8,12 137:25	<b>strategic (1)</b> 78:4
38:18 43:24 44:2	<b>see (80)</b> 3:19,19,22	41:21 44:6 45:4	124:15,15 145:21	62:15 64:4,8,25	<b>spending (2)</b> 119:4	<b>strike (2)</b> 45:17
45:12 46:25 47:23	5:2 8:5 12:11 14:20	46:2 58:16 65:22	146:6,7	65:9,11 66:12	120:18	158:11
49:6 55:16 59:15	22:8 23:3 24:21	77:9 84:6 91:25	<b>side-stepping (2)</b> 36:6	68:18 69:9 70:24	<b>spike (1)</b> 85:13	<b>striking (1)</b> 153:22
61:17 64:12,13,18	30:25 48:5,8 51:15	92:15 109:25	36:8	71:11 74:5 76:20	<b>split (1)</b> 153:14	<b>stronger (3)</b> 89:24
64:20 72:16,24	52:13 53:2 55:18	114:19 121:5	<b>sided (1)</b> 123:16	77:4,7,23,25 78:15	<b>spotted (1)</b> 159:22	90:22,23
79:22 80:14 84:2	57:22 61:9 62:20	122:10 127:1	<b>sides (7)</b> 3:6 66:17	78:22 80:2,6 81:12	<b>spread (4)</b> 101:22	<b>strongly (1)</b> 19:10
89:23 94:14,16,23	66:1 69:2,4 70:11	128:25 129:8,11,13	100:14 120:6	83:4 84:1,16 85:12	164:15,20 165:7	<b>structure (2)</b> 12:19
94:24 98:16 101:15	70:13,19,23 71:5	129:16 131:18	133:13 145:13	85:16,19 86:1,3,8	<b>squeezing (1)</b> 140:3	13:24
104:23 126:12	73:24,25 74:18	133:10 142:2,23	147:16	86:21 91:4 97:7	<b>stage (20)</b> 14:6 20:11	<b>struggle (1)</b> 152:25
138:12 142:18	75:4 77:21 78:7	143:3,9,12 146:22	<b>sight (1)</b> 99:25	100:20 101:13	20:19 47:6,7 48:1	<b>studies (3)</b> 142:5,14
146:9,13 156:13	82:23 85:18,19	149:5,6 155:11	<b>sign (1)</b> 51:12	103:1 105:4,22	94:3 95:2,19 96:1	144:1
157:19 162:21,22	86:8 87:12,12,25	157:8 158:1,10	<b>signed (2)</b> 42:13 60:8	106:4 111:3 112:20	97:1,5 101:5,24	<b>study (3)</b> 131:15
166:2,25	89:17 92:18 93:20	160:25 163:22	<b>significance (1)</b> 98:23	113:10 131:2,10	106:12 112:10,22	147:16 157:17
<b>says (35)</b> 15:11 19:1	95:1 97:18 101:25	166:7	<b>significant (8)</b> 70:25	132:2,4,6,18 134:5	113:9 131:22 145:4	<b>stuff (2)</b> 2:10 151:2
42:17,20 56:3	102:7,13 105:17	<b>sets (2)</b> 22:7 58:23	77:16 78:11,17,23	134:6 135:4 136:13	<b>stages (4)</b> 48:23 59:6	<b>sub-default (1)</b> 52:19
60:12 61:5 64:20	106:16 107:10,15	<b>setting (3)</b> 16:20	119:17 133:15	136:16 137:12	93:22 108:23	<b>subconsciously (1)</b>
76:8 96:12 100:15	107:20 110:20	48:20 68:16	139:5	138:11 139:15,23	<b>stamp (1)</b> 98:16	156:6
100:16 104:24,24	114:13 115:11,14	<b>settled (3)</b> 17:1 44:24	<b>significantly (7)</b> 25:23	146:6,12,16,19	<b>stand (1)</b> 38:10	<b>subject (11)</b> 4:17
107:10 108:11	116:9 117:21	45:13	115:20 119:4	147:11,15,22	<b>standards (1)</b> 17:5 32:6	26:21 41:2 48:21
110:1 111:18 117:5	123:17 129:18	<b>settlement (5)</b> 3:15	127:12,13,22,23	<b>so-and-so (1)</b> 32:15	96:20	76:18 88:14 89:5
117:5 123:18 130:9	130:24 133:17,22	44:19 45:22 119:19	<b>silent (1)</b> 146:20	<b>social (12)</b> 121:7,23	<b>standards (1)</b> 102:12	132:6 139:3,23
141:11 143:2,16,25	133:23 139:15	119:19	<b>similar (4)</b> 17:19	121:24 144:7,19,22	<b>star (1)</b> 82:24	169:6
147:24 149:25	152:13 153:4,14	<b>settles (1)</b> 45:22	26:17 43:17 87:13	147:9,25 148:2,5	<b>stark (1)</b> 167:20	<b>subjective (4)</b> 14:21
150:5,19 156:12	154:12 160:5 161:1	<b>seven (2)</b> 72:1 165:24	<b>similarity (1)</b> 52:22	148:21 159:17	<b>start (8)</b> 19:16 61:13	150:8,25 156:2
160:8,10 162:2,5	161:2,9 164:1	<b>Seventh (1)</b> 117:7	<b>simple (4)</b> 39:3 75:24	<b>soft (2)</b> 106:25 107:2	72:7 79:22 92:13	<b>submission (29)</b> 6:25
<b>scale (8)</b> 132:2 151:5	169:5	<b>severely (1)</b> 89:2	108:21 162:2	<b>sold (1)</b> 8:19	92:21 97:18 169:24	8:16 15:9 49:2
151:21,23 152:7	<b>seeing (4)</b> 55:25 79:8	<b>shape (1)</b> 85:14	<b>simplified (1)</b> 99:24	<b>sole (1)</b> 87:7	<b>started (1)</b> 128:13	57:22 67:11,23
158:23 159:5 160:4	80:15 165:8	<b>share (27)</b> 3:2 23:4,6	<b>simply (21)</b> 4:19 18:3	<b>solely (3)</b> 109:21	<b>starting (1)</b> 117:6	79:25 84:23 89:16
<b>scenario (21)</b> 32:8	<b>seek (1)</b> 3:1	26:14,15,20 27:2,5	19:11 20:6 21:16	159:10,19	<b>starts (2)</b> 85:9 104:15	90:17,21 91:12
46:14,24 59:16	<b>seeking (3)</b> 26:16 94:7	27:8,19 29:22,23	33:16,25 34:3	<b>solicitor (2)</b> 96:11,12	<b>state (5)</b> 12:3,4 29:17	96:7,16 98:19
60:1 62:18,18 68:2	96:3	30:6,9 89:20 113:5	45:18 50:14 51:17	<b>solutions (1)</b> 127:25	29:20 154:5	101:9,25 104:3
68:8 76:17 83:14	<b>seeks (3)</b> 15:16 16:1	121:4,10 123:8	68:6 93:24 95:17	<b>somebody (2)</b> 72:15	<b>stated (4)</b> 14:23 91:19	105:17 109:19
84:24 89:4,13,22	17:8	125:4,16 132:24	95:25 98:20 100:11	114:11	148:10,11	112:24 120:16
90:8,18 91:3	<b>seemingly (1)</b> 127:11	145:10,14 146:2,17	105:8 112:20	<b>someone's (1)</b> 30:20	<b>statement (2)</b> 140:25	121:7 122:2 147:25
156:22 165:15,16	<b>seen (14)</b> 4:9 7:1 23:4	148:18	154:13 168:24	<b>soon (4)</b> 36:22 93:22	159:20	154:6 156:21
<b>scheme (75)</b> 2:17,21	28:24 31:25 38:8	<b>shares (1)</b> 67:22	<b>single (2)</b> 147:15,16	95:2 124:24	<b>States (1)</b> 3:15	164:22
3:3,5 6:17,22 9:23	67:21 82:18,19	<b>Shaw (2)</b> 126:1	<b>sir (12)</b> 1:4 24:13,14	<b>sooner (1)</b> 76:13	<b>status (1)</b> 4:4	<b>submissions (27)</b> 1:3
10:3,4 11:6,6,8,9	92:17 125:25 134:1	166:19	38:3,16 39:1 45:24	<b>sophisticated (2)</b> 78:1	<b>statutory (2)</b> 51:7	1:16,19 3:25 9:7,9
11:14 12:24 17:9	159:5 168:7	<b>shift (2)</b> 19:20 151:14	79:2 81:25 82:5	84:9	52:10	8:16,24 14:13 16:3
29:2,8,11,15,18,25	<b>sees (2)</b> 14:9 121:8	<b>shifted (1)</b> 98:25	112:10 154:12	<b>sorry (32)</b> 4:1 8:10	<b>stay (2)</b> 24:12 33:9	16:6 25:14 31:3
30:1 41:10 42:8,17	<b>seize (1)</b> 19:2	<b>shifting (2)</b> 76:24 87:4	<b>sit (3)</b> 169:18,23	14:17,18 36:14	<b>stayed (3)</b> 36:2 63:5	60:22 68:13 74:6
43:5,6 44:5,10	<b>self-help (1)</b> 48:8	<b>shifts (1)</b> 76:25	170:1	39:3 41:16 50:3,8	85:4	76:18 88:7 92:19
50:10,15,22 51:10	<b>self-selection (1)</b>	<b>shoes (2)</b> 66:13,16	<b>sitting (2)</b> 79:20	67:5 68:21 69:13	<b>staying (2)</b> 74:22	106:14 113:19
51:12,18,23 52:1	153:13	<b>shop (2)</b> 42:11 47:2	117:12	78:14,15 83:17	84:17	126:21 128:11
53:3,4,5,13,17,20	<b>send (2)</b> 154:6,22	<b>shops (1)</b> 138:10	<b>situation (22)</b> 10:23	85:18,22 86:10,15	<b>stays (1)</b> 78:19	135:13 136:7
55:14 56:16 59:2	46:12 51:24 54:6	<b>short (15)</b> 2:4 11:22	12:1 18:7 22:21	91:20 99:7 105:1	<b>steady (1)</b> 85:4	154:21 171:3
61:21 65:7 66:6	56:14,23 64:19	44:5 58:7,9 65:8	41:20 43:5,8,20	108:9 118:16	<b>stealing (1)</b> 124:21	<b>submit (4)</b> 7:5 10:25
76:22,24 84:3,4	73:17 83:4,7 101:1	79:9 87:18 88:2	47:25 48:14,18	119:15 123:17	<b>steals (1)</b> 125:2	55:1 168:14
108:25 109:3,4,7,8	110:7 133:19 135:6	110:25 128:4	57:19 63:2 70:17	125:10 131:24	<b>stem (1)</b> 27:5	<b>submitted (2)</b> 154:9
109:9,11 110:18		133:20 134:6	75:5 81:22 82:3,14	134:4 141:19	<b>step (7)</b> 64:2 66:18	154:14
111:20 113:4 118:5		140:12,14	83:12,13 104:22	144:25 162:11	73:18 83:18,19,19	<b>suboptimal (2)</b> 144:6

147:24 <b>subsequent (2)</b> 123:2 123:5 <b>subsequently (3)</b> 23:1 23:2 168:13 <b>substantial (9)</b> 2:18 28:2 58:5 86:9 90:11,20 115:17 116:15,22 <b>substantially (6)</b> 23:24 24:2 85:24 88:18 115:14 131:18 <b>substantiated (1)</b> 107:14 <b>substitute (1)</b> 167:7 <b>succeeds (1)</b> 102:11 <b>success (1)</b> 114:13 <b>successful (2)</b> 96:15 114:14 <b>successfully (1)</b> 33:5 <b>suddenly (1)</b> 93:18 <b>suffer (1)</b> 96:18 <b>suffered (8)</b> 18:15 93:3,11,21 94:18 126:8 136:5 139:13 <b>suffering (1)</b> 141:13 <b>suffers (1)</b> 136:12 <b>sufficient (2)</b> 52:17 83:22 <b>sufficiently (2)</b> 63:6 90:23 <b>suggest (4)</b> 67:25 93:22 144:6 168:1 <b>suggested (7)</b> 8:12 9:24 20:6 45:24 60:17 78:17 166:12 <b>suggesting (2)</b> 73:1 76:10 <b>suggestion (1)</b> 8:21 <b>suit (3)</b> 20:22 96:13 96:15 <b>suitable (3)</b> 119:9 142:10 143:25 <b>suits (1)</b> 63:7 <b>summarised (1)</b> 165:11 <b>summarises (1)</b> 7:20 <b>summary (1)</b> 149:10 <b>sums (2)</b> 40:8 116:19 <b>supermarket (1)</b> 73:25 <b>Supermarkets (1)</b> 116:18 <b>supply (5)</b> 84:8,10,11 84:13 87:6 <b>support (6)</b> 17:7,25 18:3 19:12 63:11 67:11 <b>supported (3)</b> 39:11 39:22 87:11 <b>supporting (1)</b> 154:7 <b>supports (1)</b> 129:3 <b>suppose (8)</b> 47:1 60:8 71:24 72:4 101:13 103:1 137:12 139:18 <b>supposed (2)</b> 50:24 102:17 <b>supreme (1)</b> 86:24 <b>surcharge (2)</b> 76:3,9 <b>Surcharges (1)</b> 31:18 <b>surcharging (2)</b> 31:12 31:14 <b>sure (13)</b> 11:16 42:5 48:7 64:18 69:18 81:4,6 86:12 101:13 103:5 145:15,18 152:5 <b>surely (2)</b> 41:22 49:5	<b>surprise (1)</b> 61:25 <b>surprised (1)</b> 39:9 <b>surprising (1)</b> 67:24 <b>surprisingly (1)</b> 122:18 <b>survey (20)</b> 14:24 15:18 143:15,18 150:12 151:23 153:5,12,25 154:2 154:10,25 155:1,10 157:4,8,9 160:25 163:10,13 <b>survive (1)</b> 15:5 <b>suspected (2)</b> 19:3,5 <b>suspicion (1)</b> 18:8 <b>suspicious (1)</b> 19:3 <b>sustained (2)</b> 34:25 81:3 <b>sweep (1)</b> 54:23 <b>switch (8)</b> 22:11 23:2 24:20 25:11,12 36:19 70:22 75:25 <b>switched (4)</b> 23:18,22 75:9 85:17 <b>switches (1)</b> 24:18 <b>switching (6)</b> 8:3,22 32:12,14 75:19 90:20 <b>system (26)</b> 16:16 37:18 41:12 43:8 43:12,12 44:8 45:21,21 47:3 56:1 61:16 112:1,3 118:1,11 123:16 124:3,6,11,14 126:22 128:18 134:3,23 137:6 <b>systems (2)</b> 16:15 133:25	146:23 147:24 150:18 156:16 158:2 160:13 162:5 162:7 165:3 167:13 168:8,15,16 170:2 <b>taken (15)</b> 13:18 15:18,23 20:15,21 53:10 111:8 117:17 123:24 127:18 144:16 149:6,8 151:16 167:16 <b>takes (10)</b> 52:15 62:17 85:22 97:12 144:15 150:5 162:21 166:3 168:16,17 <b>talk (4)</b> 76:14 83:20 136:24 147:2 <b>talked (1)</b> 43:10 <b>talking (8)</b> 47:19 73:12 83:11,12 96:5 124:12 156:3 164:23 <b>tally (1)</b> 33:25 <b>task (5)</b> 94:1 95:21,24 152:22 157:21 <b>technical (1)</b> 151:13 <b>technically (1)</b> 104:11 <b>techniques (1)</b> 153:6 <b>Telegraph (1)</b> 76:5 <b>tell (5)</b> 26:16 30:15,17 79:13 144:20 <b>telling (1)</b> 133:9 <b>tells (4)</b> 79:12 124:16 147:18 149:20 <b>temptation (1)</b> 38:10 <b>tempting (1)</b> 38:4 <b>ten (1)</b> 86:10 <b>tend (2)</b> 136:24 158:22 <b>term (13)</b> 43:16 44:3 52:22 76:23 79:1 82:25 87:18 150:3 150:10,23 151:1,10 156:17 <b>terminology (1)</b> 151:19 <b>terms (19)</b> 7:16 10:12 11:15 14:9 39:24 52:9 62:17 64:8 79:4 104:5,14 108:21 112:20 118:13 120:20 131:12 132:10,12 142:17 <b>territory (2)</b> 62:11 142:20 <b>Tesco (3)</b> 72:21 73:19 76:12 <b>Tesco's (2)</b> 84:16,24 <b>test (27)</b> 9:3,21,22 10:12,21 11:17 46:7 49:3,6,10 52:22 57:4,10 105:11,22,24 120:22 126:23 139:18 141:1 142:9 144:4,5,10 149:2 151:22 159:17 <b>testing (1)</b> 38:21 <b>tests (2)</b> 56:22 140:1 <b>thank (10)</b> 25:2 44:22 52:7 68:22 69:13 87:24 143:14 147:19 170:3,4 <b>theme (2)</b> 14:4,12 <b>themes (1)</b> 2:20 <b>theoretical (3)</b> 56:12 81:7 127:6 <b>theoretically (1)</b> 54:17	<b>theory (4)</b> 38:11,12 53:3 55:25 <b>thereabouts (1)</b> 88:17 <b>thing (7)</b> 1:14 62:3 75:5 113:13 138:8 151:14 153:1 <b>things (9)</b> 37:15 54:25 74:14 75:6 81:12 100:22 138:10 151:14 156:16 <b>think (87)</b> 2:7 3:22 6:16 7:12 13:1 21:22 33:23 36:1 36:11 37:5 39:10 40:7 42:15,24 43:19,19 44:11,13 44:17 46:17 52:20 54:11 56:10 58:6 60:15 22 61:4 62:11 66:4 69:7 73:17 76:12,20 77:14 81:12 82:21 83:15 84:15 85:4 92:9 96:24 97:1,7 99:14 100:15 102:16 103:14,16 103:17 104:4 110:14,21 111:3,7 111:15,17 114:2,5 114:24 117:13 122:18 125:11,25 132:9,11 134:4,12 136:1,6,16,21 138:12 141:22 142:5,6 145:7,16 145:21,24 148:3,7 152:23 165:5 168:20 169:1,21,24 <b>thinking (4)</b> 41:18 72:11 73:23 151:25 <b>thinks (7)</b> 20:2,4 53:6 64:22 65:18 105:18 116:13 <b>third (9)</b> 2:25 22:2 115:1 126:19 128:4 128:5 130:21 150:15 165:12 <b>thought (13)</b> 30:22 75:9 77:23 79:8,23 80:10 85:1 105:15 110:25 113:10 116:2,19 155:13 <b>threat (8)</b> 6:17,19 20:17 21:6,15 32:24 33:15 72:25 <b>threaten (3)</b> 67:2 68:10 72:3 <b>threatened (1)</b> 68:3 <b>three (9)</b> 29:22,25,25 81:9 109:16 163:7 163:9,12 164:3 <b>three-party (5)</b> 26:12 27:9 29:2,14,18 <b>three-year (1)</b> 26:15 <b>thresholds (1)</b> 161:5 <b>thrill (1)</b> 2:11 <b>tie (1)</b> 88:15 <b>tied (1)</b> 126:9 <b>tightly (1)</b> 54:9 <b>time (29)</b> 1:21 2:4,8 7:15 8:8 23:24,25 24:24 27:7 29:12 30:6 41:2 63:13 75:7,25 76:1 85:10 96:13 97:24 98:6 109:14 118:7 129:1 142:3 150:6,24 163:14 169:11,13 <b>timeframe (1)</b> 151:3	<b>times (15)</b> 66:1 76:4 81:11 86:10 148:11 163:7,11,11 164:3 164:7,11,14 165:6 165:13,24 <b>tin (1)</b> 117:13 <b>Tirole (7)</b> 142:8 143:24 144:2 147:23 159:12,21 166:8 <b>to-ing (1)</b> 97:3 <b>today (2)</b> 146:21 169:13 <b>told (4)</b> 75:20 137:22 154:10,25 <b>tome (1)</b> 2:3 <b>tomorrow (1)</b> 169:17 <b>tonight (1)</b> 117:15 <b>tooth (1)</b> 139:10 <b>top (6)</b> 12:22 24:15 30:11 34:21 162:3 164:21 <b>tortious (1)</b> 93:14 <b>total (4)</b> 40:12 69:22 131:18 151:21 <b>totally (1)</b> 81:15 <b>touched (2)</b> 3:5 9:6 <b>tough (1)</b> 31:7 <b>tourist (3)</b> 142:9 149:2 159:17 <b>trade (2)</b> 122:24 157:11 <b>traditions (1)</b> 47:19 <b>transact (1)</b> 59:4 <b>transaction (21)</b> 22:14 22:14 44:24 45:13 45:20 47:1,2 70:12 70:15 71:1,6,7,8 72:19 87:2 115:5 115:12 135:5 139:9 152:1 157:1 <b>transactions (33)</b> 29:5 29:14,17,20 32:5 45:8,8 68:25 69:5 69:11 70:21 71:8 78:23 82:20 83:6 85:8,20 119:7,9 138:2,4 150:17 151:7 167:5,7,13 167:15,18,18 168:1 168:2,12,15 <b>transcript (3)</b> 58:6 74:19 158:12 <b>transfers (1)</b> 129:22 <b>tread (1)</b> 27:25 <b>treat (1)</b> 33:20 <b>treating (1)</b> 64:9 <b>trial (2)</b> 6:12 27:23 <b>Tribunal (23)</b> 4:5 5:13 5:15 6:25 8:12,21 11:3 19:17 36:11 42:3 58:13 68:14 74:17 81:1 88:8 92:23 93:8 94:2 95:3 99:22 109:2 109:20 136:9 <b>Tribunal's (3)</b> 1:24 4:8 26:6 <b>tried (5)</b> 19:20 27:17 56:14 108:21 133:1 <b>tries (2)</b> 36:12 163:4 <b>trigger (3)</b> 145:22 147:2,6 <b>trodden (1)</b> 61:2 <b>trouble (3)</b> 74:9 132:19 152:8 <b>troubled (2)</b> 87:1,4 <b>true (3)</b> 49:23 86:18 135:15	<b>truncated (1)</b> 142:25 <b>truth (3)</b> 31:8 83:21 102:19 <b>try (9)</b> 2:1 27:25 64:20 77:14 101:14 140:2 156:6 161:21 162:8 <b>trying (18)</b> 28:17 43:21 49:12 54:21 70:2 94:4 97:16 102:7 106:11 131:6 131:14 139:15 141:13 147:7 148:3 152:2 156:6 169:18 <b>Tuesday (1)</b> 1:1 <b>tumble (2)</b> 79:18 80:22 <b>tune (1)</b> 116:23 <b>turn (13)</b> 8:19 14:4 38:9 66:21 67:18 100:11,14 102:22 104:10 128:22 131:24 136:18,19 <b>turned (2)</b> 99:5 138:5 <b>turns (1)</b> 100:14 <b>turpi (1)</b> 2:12 <b>twice (3)</b> 63:13 148:24 163:7 <b>two (29)</b> 4:11 8:12 17:22 20:22 38:22 39:10,12,19 43:11 45:6 46:6 56:7 62:24 66:17 69:3 104:21 105:14 123:15 137:18 140:21 141:21 147:13 150:5,9,15 150:23 156:15 163:9,11 <b>two-sided (3)</b> 112:1 124:2 147:11 <b>twofold (1)</b> 155:17 <b>type (5)</b> 15:2,5,6,6,7 <b>types (1)</b> 70:11 <b>typical (2)</b> 79:20 166:2 <b>typo (1)</b> 130:8	<b>U</b> <b>UK (32)</b> 7:2,3,9 8:8 10:4 20:3,11,14 21:18 25:16 26:13 31:15,18 32:8,10 33:11,15 34:17,23 35:1 40:12,12,14 40:15 73:5 109:2,6 141:1 142:1 155:19 162:22 166:5 <b>unaware (1)</b> 78:25 <b>uncertain (1)</b> 43:12 <b>uncertainty (1)</b> 44:8 <b>unchanged (1)</b> 12:25 <b>unchecked (2)</b> 83:16 84:3 <b>unclear (3)</b> 76:7 101:6 146:8 <b>uncontroversial (2)</b> 3:8 77:20 <b>under-compensatio...</b> 104:2,7 <b>underpin (1)</b> 2:20 <b>understand (13)</b> 6:25 7:16 48:10 50:22 62:5 74:22 78:14 89:16 99:24 101:2 101:15 124:12 151:13 <b>understanding (2)</b> 11:1 49:24 <b>understood (5)</b> 45:3 50:12 64:12,13	99:1 <b>undertake (1)</b> 94:3 <b>undertaking (2)</b> 19:5 54:9 <b>undertakings (8)</b> 12:16 18:9,11,13 18:17,24 107:23 127:5 <b>undisputed (1)</b> 2:14 <b>unexempted (1)</b> 99:12 <b>unfair (1)</b> 166:17 <b>unilaterally (1)</b> 65:21 <b>unimpaired (1)</b> 61:18 <b>United (1)</b> 3:15 <b>university (1)</b> 98:1 <b>unlawful (4)</b> 95:18,23 100:4,10 <b>unlawfully (8)</b> 17:19 18:21,22 19:5,7 33:19,22 34:5 <b>unlock (1)</b> 121:24 <b>unnecessary (1)</b> 106:5 <b>unpack (2)</b> 91:11 139:15 <b>unpick (1)</b> 64:20 <b>unrealistic (5)</b> 33:4 67:25 163:12 165:22 166:14 <b>unreliable (1)</b> 166:13 <b>unsatisfactory (1)</b> 155:24 <b>unsurprisingly (1)</b> 77:1 <b>unworkable (1)</b> 51:14 <b>updated (1)</b> 165:23 <b>upper (3)</b> 65:12 103:3 103:16 <b>upward (1)</b> 132:4 <b>use (19)</b> 67:24 83:20 113:6 120:17,18,24 122:21 128:16,17 128:22,23 129:5 130:10,12,15,16 138:23 159:23 167:4 <b>useful (2)</b> 3:22 141:10 <b>users (2)</b> 122:13,15 <b>uses (1)</b> 117:25	<b>V</b> <b>v (2)</b> 97:8 164:12 <b>vacuum (4)</b> 15:11 16:23 17:9 54:20 <b>valebait (1)</b> 44:1 48:7 <b>valebait-type (2)</b> 43:20 51:13 <b>valid (2)</b> 42:23 51:1 <b>valuable (1)</b> 121:21 <b>value (18)</b> 29:19 43:21 70:12,15 71:1,6,10 72:19 87:2 107:9 113:16 113:22 114:20 115:5,12 117:10,18 118:13 <b>values (1)</b> 70:10 <b>variable (10)</b> 151:2 152:3,12,23 153:3 153:7,16 154:15 155:16 156:20 <b>variations (1)</b> 140:22 <b>various (5)</b> 59:6 68:13 100:20 149:23 152:4 <b>vary (7)</b> 150:6,24 151:1,4,10 156:17 158:8 <b>verbatim (2)</b> 1:22
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109:25 <b>verified (1)</b> 107:14 <b>verse (1)</b> 60:25 <b>version (2)</b> 68:19 69:9 <b>versions (1)</b> 69:3 <b>versus (1)</b> 56:8 <b>viability (2)</b> 17:9 53:8 <b>viable (4)</b> 16:16 51:10 51:11 119:6 <b>vibrant (5)</b> 57:20,20 57:21 83:1,2 <b>vicious (2)</b> 120:15,19 <b>view (21)</b> 3:23 5:1 62:9 76:23 77:2 78:3,4,8 84:10 97:19 103:1 105:18 105:19 121:16 126:5 141:7,17 144:6 153:7 154:1 157:24 <b>views (3)</b> 5:5 53:8 153:10 <b>violence (2)</b> 47:21 50:21 <b>virtue (1)</b> 20:20 <b>virtuous (2)</b> 120:16,19 <b>vis-a-vis (1)</b> 15:5 <b>Visa (133)</b> 8:1,20,20 15:10 17:13,18 18:20 19:23 20:3,9 20:13,19,24 21:3 21:10,11,20,23 22:3,4,9,12,12,19 22:23,25 23:5,14 23:23 24:21 25:6,8 25:24 26:12,18 27:14 28:5 30:25 31:22,23 32:13,23 33:6,10,13,19 34:4 34:8,24 35:9 40:18 41:1 48:19 56:17 57:21 62:22 63:4,8 63:9,23 65:13 66:22 67:5,6,7,8,18 67:18 68:1,3,5,6,8 68:23,24 69:4,11 69:16,24 70:3,5,12 70:13,16,16 72:15 72:17 73:3,7,15,21 74:22 75:10,14,16 75:21 76:3 77:10 78:7,13,19 79:10 82:4,10,21 83:2 84:4,4,6 86:24 87:5 88:13,25 89:1,14 89:23,24 90:2,14 90:15,19,22 115:6 115:7 116:2,4 134:17 135:9,10,25 136:3 143:2,3 <b>Visa's (4)</b> 20:24,25 22:23 67:14 <b>Visa/Amex (1)</b> 134:16 <b>volume (2)</b> 2:9 71:9 <b>volumes (2)</b> 70:10 71:4 <b>von (79)</b> 19:19 20:5 25:9 26:9 31:5 32:12,20 33:8 34:19 35:2,5 36:22 37:16 38:1 40:15 40:25 41:5 42:6 46:23 63:12 64:1 65:5 74:9,17 91:24 94:19,23 105:18 114:18 117:1,4 119:8,22 120:8 122:8 124:17 129:7 129:10,17,21	130:14,19 141:10 150:4 151:8,15 152:11,15 153:21 154:1,10,20 155:1 155:13,25 156:23 157:25 159:6,20 162:5,8,17,25 163:2 164:17 165:1 165:5,17,20,25 166:8,12 167:2,12 167:21,23 168:17 168:24 169:4 <hr/> <b>W</b> <b>wagging (1)</b> 62:11 <b>wait (1)</b> 118:12 <b>waiting (1)</b> 75:19 <b>want (32)</b> 1:8,12 15:20 36:10 38:16 38:18,20 39:4,19 40:20 60:24 63:7 64:20 66:5 68:22 69:4 74:5 77:21 81:5 87:2,5,5,9 89:23 92:19 110:25 111:9 130:25 132:22 147:20 169:15,16 <b>wanted (4)</b> 22:25 35:8 113:10 139:18 <b>wants (4)</b> 46:21 75:4 142:5 168:10 <b>wasn't (14)</b> 5:17 6:12 9:6 15:19 19:24 24:4 26:21 32:18 61:25 64:18 74:12 74:14,15 104:17 <b>watched (3)</b> 23:10 79:18 80:21 <b>watching (1)</b> 82:17 <b>way (41)</b> 4:11 10:25 19:25 23:3 24:10 39:18 41:6 43:19 43:20 45:24,25 46:18 50:15 51:19 53:15,16,16,18,22 56:14 63:1,9 66:21 74:25 75:24 79:7 95:5 96:9 112:15 117:21 125:13 136:21 137:4 141:15,16,16 144:8 144:15 152:13 155:10 156:7 <b>ways (2)</b> 62:25 103:21 <b>we're (1)</b> 170:2 <b>weak (1)</b> 89:18 <b>weaker (2)</b> 90:19,23 <b>Wednesday (1)</b> 170:7 <b>week (4)</b> 82:19,23 117:14 168:10 <b>weekly (2)</b> 70:10 71:10 <b>weeks (3)</b> 3:9 7:5 38:5 <b>weighed (1)</b> 98:4 <b>weighing (1)</b> 100:20 <b>weight (1)</b> 4:5 <b>weighted (2)</b> 31:22 168:21 <b>weighty (1)</b> 2:3 <b>welcome (1)</b> 74:2 <b>welfare (1)</b> 121:7,24 121:24 144:7,19,22 147:9,25 148:2,5 148:22 <b>well-knowing (1)</b> 148:9 <b>well-placed (2)</b> 143:9 143:12 <b>well-resourced (1)</b>	154:14 <b>welter (1)</b> 5:6 <b>went (6)</b> 23:4 27:2 59:9 89:20 118:20 155:15 <b>weren't (5)</b> 26:23 51:21 52:12 111:8 168:16 <b>West (1)</b> 118:21 <b>westerns (1)</b> 114:2 <b>whack (1)</b> 141:18 <b>whatsoever (1)</b> 84:7 <b>whilst (6)</b> 23:6 26:10 48:5 67:7 107:17 162:18 <b>white (2)</b> 57:24,25 <b>wholesalers (1)</b> 122:22 <b>widget (5)</b> 99:5,8 100:7,8,12 <b>wiggle (1)</b> 58:1 <b>Wild (1)</b> 118:21 <b>willing (5)</b> 64:21 114:8 115:25 116:12,18 <b>win (1)</b> 99:9 <b>wiped (1)</b> 37:2 <b>withdrawn (1)</b> 17:24 <b>witnesses (3)</b> 31:14 38:7 40:2 <b>word (2)</b> 19:3 138:23 <b>wording (3)</b> 15:18 46:9 50:5 <b>words (9)</b> 49:22 51:21 58:17 97:4 109:10 121:21 122:25 124:7 141:2 <b>work (13)</b> 15:12 27:18 41:11,13 43:19 49:12 50:23 55:2 55:25 64:2 65:6 66:21 131:6 <b>worker (1)</b> 168:9 <b>works (2)</b> 54:25 103:6 <b>world (18)</b> 27:6 32:12 33:9 37:7 53:9 54:7 54:8 55:4 63:21,23 74:7 77:8 100:25 114:10 118:3 156:15 162:25 166:10 <b>WorldPay (1)</b> 85:21 <b>worried (2)</b> 33:12 151:18 <b>worry (1)</b> 145:23 <b>worse (12)</b> 89:11,11 91:2 121:18 144:10 144:11 145:3,8,17 145:20 147:3 162:13 <b>worth (8)</b> 40:21 48:9 53:6 71:9 73:16 110:21 165:21 169:1 <b>worthwhile (1)</b> 63:19 <b>wouldn't (23)</b> 50:16 54:18 65:6 70:20 72:12 73:24 75:9 76:8,9 79:21 99:8,9 101:9 103:3,16 105:16 118:22 134:8 135:18 138:5 139:11 168:8,15 <b>wounded (1)</b> 89:2 <b>Wright (5)</b> 148:24 149:11,20 151:11 159:7 <b>writers (1)</b> 58:7 <b>written (7)</b> 2:10 19:20 19:21 31:4 63:11	92:14 165:21 <b>wrong (15)</b> 5:2 10:1 45:13 46:19 49:1,1 50:21 93:16 105:16 124:22,23 137:10 154:3,16 158:10 <hr/> <b>X</b> <b>X (2)</b> 100:16 104:24 <hr/> <b>Y</b> <b>Y (3)</b> 100:16 104:24 105:1 <b>year (1)</b> 86:4 <b>yearly (1)</b> 29:19 <b>years (7)</b> 29:22,25 53:18 67:15 72:1 115:24 141:13 <b>yellow (1)</b> 115:10 <b>yesterday (5)</b> 58:14 59:10 97:4 109:15 111:4 <b>young (1)</b> 97:24 <hr/> <b>Z</b> <b>zero (35)</b> 7:25 8:19 19:22,23 20:3 22:4 25:16 32:23 33:21 34:8 53:5 56:17 58:23 59:7,12,18 61:6,7,13,15 65:15 66:9,9 78:7,8,16 79:9 82:3 87:1 89:7 89:8 92:1 99:16 131:5 135:18 <hr/> <b>0</b> <b>0 (1)</b> 163:20 <b>0.14 (1)</b> 161:16 <b>0.15 (11)</b> 8:1 32:5 33:11 63:17,23 64:3,4,9,21 65:12 65:15 <b>0.3 (5)</b> 28:3 30:25 90:9 116:11 142:15 <b>0.4 (2)</b> 94:11,12 <b>0.4.2 (1)</b> 161:14 <b>0.42 (1)</b> 165:19 <b>0.49 (1)</b> 165:19 <b>0.5 (1)</b> 163:20 <b>0.75 (1)</b> 165:15 <b>0.86 (1)</b> 165:16 <b>0.94 (1)</b> 165:19 <b>06/09 (1)</b> 26:10 <b>07/08 (1)</b> 85:13 <hr/> <b>1</b> <b>1 (5)</b> 28:25 128:14 161:24 164:20 171:3 <b>1(5) (1)</b> 29:1 <b>1.01 (1)</b> 88:1 <b>1.67 (1)</b> 165:16 <b>10 (6)</b> 69:6 85:6,11 158:14 165:9,18 <b>10.00 (3)</b> 169:24 170:1,6 <b>10.30 (1)</b> 1:2 <b>100 (1)</b> 30:14 <b>100% (4)</b> 45:22 47:17 61:5 93:17 <b>101 (1)</b> 14:25 <b>101(1) (9)</b> 2:6 9:3 10:1 10:9 92:7 93:22 95:3 112:22 124:5 <b>101(3) (20)</b> 10:1,8 93:7,23 95:4 106:16,23 111:5	112:24 122:25 124:19 127:5 134:12 135:15 136:21 139:13 140:10 144:13,23 148:19 <b>103 (2)</b> 31:10,16 <b>105 (2)</b> 31:20 160:21 <b>107 (1)</b> 163:23 <b>108 (2)</b> 16:9 164:21 <b>109 (1)</b> 33:8 <b>10p (1)</b> 100:8 <b>11 (7)</b> 4:12 26:4 69:7 85:16,20,23 92:18 <b>111 (1)</b> 86:5 <b>118 (1)</b> 34:16 <b>12 (3)</b> 68:12 70:6 74:19 <b>12(b) (1)</b> 161:10 <b>12.00 (1)</b> 58:8 <b>12.15 (1)</b> 58:10 <b>121 (1)</b> 35:3 <b>125 (1)</b> 40:9 <b>126 (5)</b> 40:24 158:12 158:13 159:2 162:18 <b>128 (1)</b> 42:24 <b>13 (3)</b> 74:20 153:5 158:12 <b>135 (1)</b> 48:11 <b>14 (2)</b> 4:3 164:11 <b>14% (1)</b> 26:14 <b>15% (1)</b> 164:2 <b>152 (1)</b> 26:6 <b>15th (1)</b> 1:1 <b>16 (1)</b> 4:7 <b>163 (3)</b> 16:8,8 126:2 <b>164 (1)</b> 16:18 <b>165 (1)</b> 17:5 <b>166 (1)</b> 16:8 <b>167 (1)</b> 12:21 <b>16th (1)</b> 170:7 <b>174 (1)</b> 91:12 <b>175 (1)</b> 91:25 <b>176E (1)</b> 25:4 <b>18 (1)</b> 7:11 <b>186 (1)</b> 17:15 <b>187 (1)</b> 18:5 <b>19 (2)</b> 16:7 110:22 <b>19th (1)</b> 21:8 <b>1st (1)</b> 22:8 <hr/> <b>2</b> <b>2 (11)</b> 29:16 35:7 68:15,15,19 85:5,6 87:25 128:16 164:24 165:15 <b>2% (1)</b> 164:13 <b>2(a) (1)</b> 107:8 <b>2.00 (1)</b> 88:3 <b>20 (4)</b> 9:15 164:14 165:9,13 <b>20-odd (1)</b> 164:24 <b>2000 (1)</b> 67:17 <b>2000s (1)</b> 24:18 <b>2002 (1)</b> 20:23 <b>2004/05 (1)</b> 24:17 <b>2004/2005 (1)</b> 22:11 25:22 <b>2006 (3)</b> 22:12 25:1 25:22 <b>2007 (6)</b> 21:8,14 22:8 67:15,17 73:10 <b>2008 (5)</b> 131:15 142:8 143:24 149:2 166:8 <b>2009 (4)</b> 21:7 25:22 27:7 148:24 <b>2009/2010 (2)</b> 85:23 86:6 <b>201 (1)</b> 44:17	<b>2010 (2)</b> 27:7 148:25 <b>2011 (1)</b> 40:11 <b>2013 (1)</b> 21:13 <b>2014 (3)</b> 27:23 28:11 143:2 <b>2014/2015 (1)</b> 86:5 <b>2015 (11)</b> 15:18 27:23 28:11,20 30:17 83:7 89:25 116:7 143:15 144:1 157:4 <b>2015/16 (1)</b> 85:9 <b>2015/2016 (1)</b> 86:4 <b>2016 (2)</b> 1:1 170:7 <b>2018 (1)</b> 29:13 <b>202 (4)</b> 15:22 106:17 161:1 163:13 <b>206 (3)</b> 108:22,23 112:25 <b>21 (3)</b> 28:23 158:20 159:8 <b>211(e) (1)</b> 35:7 <b>212 (1)</b> 161:3 <b>216 (1)</b> 113:18 <b>217 (1)</b> 114:7 <b>218 (1)</b> 115:1 <b>22 (1)</b> 10:10 <b>220 (1)</b> 115:10 <b>221 (1)</b> 115:17 <b>222 (1)</b> 116:14 <b>224 (1)</b> 116:25 <b>225 (1)</b> 117:7 <b>226 (1)</b> 119:16 <b>227 (1)</b> 119:2 <b>229 (1)</b> 120:6 <b>23 (2)</b> 157:13,15 <b>230 (1)</b> 14:19 <b>234 (1)</b> 122:10 <b>235 (1)</b> 123:12 <b>236 (3)</b> 111:14,15 123:17 <b>237 (5)</b> 111:14,15 123:12,14 124:1 <b>239 (1)</b> 125:8 <b>24 (4)</b> 12:22 74:20 158:15 159:8 <b>240 (1)</b> 166:24 <b>241 (1)</b> 171:17 <b>242 (1)</b> 111:23 <b>245 (2)</b> 127:1,4 <b>247 (1)</b> 127:18 <b>248 (2)</b> 125:11,13 <b>25 (7)</b> 19:14 47:2,4,9 47:9 61:18,19 <b>250 (1)</b> 128:11 <b>251 (1)</b> 129:4 <b>254 (2)</b> 129:9,10 <b>255 (1)</b> 129:14 <b>256 (1)</b> 129:18 <b>257 (1)</b> 129:21 <b>258 (1)</b> 131:3 <b>259 (1)</b> 130:8 <b>26 (3)</b> 20:8 157:19 163:1 <b>260 (1)</b> 130:14 <b>261 (1)</b> 130:21 <b>261/262 (1)</b> 130:25 <b>262 (1)</b> 133:11 <b>264 (2)</b> 133:17 140:18 <b>266 (1)</b> 133:23 <b>267 (2)</b> 140:20,23 <b>270 (1)</b> 141:22 <b>271 (1)</b> 142:2 <b>272 (1)</b> 142:13 <b>273 (1)</b> 142:23 <b>273(a) (1)</b> 142:24 <b>275 (1)</b> 144:2 <b>278 (1)</b> 147:25 <b>28 (5)</b> 22:6 118:2,7,10 118:12	<b>280 (1)</b> 148:23 <b>281 (1)</b> 149:5 <b>282 (1)</b> 149:24 <b>286 (1)</b> 151:4 <b>289 (1)</b> 151:4 <b>29 (1)</b> 23:3 <b>291 (1)</b> 151:11 <b>293 (1)</b> 152:11 <b>294 (1)</b> 152:17 <b>295 (2)</b> 152:21 153:4 <b>296 (1)</b> 153:12 <b>297 (1)</b> 153:14 <b>298 (1)</b> 153:16 <b>299 (1)</b> 153:18 <hr/> <b>3</b> <b>3 (3)</b> 128:20 164:25 165:16 <b>3(4) (2)</b> 4:5,10 29:19 57:17 <b>3.20 (1)</b> 140:13 <b>3.30 (1)</b> 140:15 <b>3.5 (2)</b> 26:23 29:9 <b>30 (1)</b> 25:14 <b>300 (1)</b> 153:21 <b>300(c) (1)</b> 154:1 <b>302 (1)</b> 154:23 <b>303 (1)</b> 155:12 <b>304 (1)</b> 155:25 <b>307 (1)</b> 157:6 <b>308 (1)</b> 157:9 <b>309 (1)</b> 158:1 <b>311 (1)</b> 158:7 <b>311(b) (1)</b> 158:10 <b>312 (2)</b> 159:3 160:2 <b>313 (1)</b> 159:9 <b>314 (2)</b> 160:21,22 <b>315 (1)</b> 126:2 <b>317 (1)</b> 162:15 <b>319 (2)</b> 166:16,23 <b>321 (1)</b> 165:11 <b>322 (1)</b> 165:25 <b>323 (1)</b> 166:7 <b>33 (2)</b> 30:11 31:2 <b>338 (1)</b> 168:21 <b>346A (1)</b> 169:10 <b>347 (2)</b> 169:6,10 <b>36 (1)</b> 31:19 <b>37 (1)</b> 32:22 <b>38(a).9 (1)</b> 107:10 <hr/> <b>4</b> <b>4 (5)</b> 3:14 69:1 157:10 158:14,15 <b>4.25 (1)</b> 170:5 <b>40 (1)</b> 34:14 <b>41 (2)</b> 34:21 35:14 <b>4155 (1)</b> 44:21 <b>42 (2)</b> 35:15,16 <b>428 (1)</b> 16:7 <b>4307 (1)</b> 15:22 <b>4351 (1)</b> 163:14 <b>4358 (1)</b> 161:1 <b>437 (2)</b> 111:14 123:12 <b>438 (1)</b> 125:12 <b>450 (1)</b> 28:25 <b>46 (2)</b> 63:11,14 <b>464 (1)</b> 68:17 <b>468 (1)</b> 85:10 <b>47 (1)</b> 63:14 <b>49 (1)</b> 65:24 <hr/> <b>5</b> <b>5 (7)</b> 68:20,22 69:10 85:7 161:24 164:20 169:15 <b>5% (2)</b> 48:9 164:10 <b>50 (3)</b> 65:24 66:1 143:2
---	---	---	--	--	--	---



500 (2) 40:17,22  
 51 (2) 65:25 107:11  
 52 (1) 15:22  
 528 (1) 60:16  
 56 (4) 88:7 107:17  
 108:7,8  
 560 (1) 70:7  
 57 (3) 74:19 107:17  
 107:20  
 58 (1) 74:20

**6**

6 (17) 68:20 133:19  
 150:13 157:5,7  
 158:2,4 161:8,14  
 161:23 162:1,5,9  
 163:2,17 164:6,16  
 6.5p (1) 22:14  
 6.6 (2) 22:10 24:19  
 64 (1) 10:10  
 64(c) (1) 10:19  
 65 (1) 11:19  
 65(d) (1) 11:21  
 66 (1) 106:14  
 66(b) (1) 12:12  
 67 (1) 108:17  
 68 (1) 13:12  
 68(a) (1) 13:15  
 69 (1) 4:18

**7**

7 (15) 3:9,13 7:4,23  
 38:5 132:24 161:8  
 161:14,23 162:1,5  
 162:9 163:2,17  
 165:6  
 7% (1) 164:6  
 70 (1) 113:12  
 73 (4) 11:21 14:16,18  
 14:20  
 73(a) (1) 20:23  
 74 (1) 17:15  
 75 (1) 127:3

**8**

8 (24) 7:19 44:13,19  
 69:8 85:4,5,7,19  
 86:6 125:24 150:13  
 157:5,7 158:2,5  
 161:9,23 162:1,6  
 162:10,13 163:3,18  
 164:16  
 8% (1) 26:14  
 8.3 (3) 44:23 47:21  
 48:25  
 80 (1) 126:20  
 800 (1) 40:18  
 81 (1) 121:14  
 81(3) (1) 107:24  
 81.3 (1) 123:19  
 82 (1) 40:13  
 84 (1) 122:11  
 85 (2) 121:6,8  
 88 (3) 133:7,11  
 140:16  
 8p (3) 22:14 24:7,12

**9**

9 (3) 29:13 92:14,18  
 9.2 (1) 22:19  
 9.30 (1) 169:25  
 94 (3) 27:4,10 149:9  
 96 (1) 27:21  
 97.5 (1) 47:18