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

Day 2

January 26, 2016

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(10.30 am)

Housekeeping

MR JUSTICE BARLING: Good morning Mr Brealey.

MR BREALEY: Good morning, my Lord.

MR JUSTICE BARLING: Yesterday we were sent by Stewarts Law a letter -- who represent Asda in separate proceedings -- putting down one or two markers about some documents that were disclosed relating to them but in these proceedings. Just to let you know that we have got it. I don't think it requires us to do anything. I hope you also received by email and otherwise the draft confidentiality ring order, which I think Ms Boyle has now condensed to a single order rather than two orders as it was in the High Court.

It would be nice if we could get that sorted out at some point fairly soon.

MR BREALEY: Yes.

MR JUSTICE BARLING: I think we have all read those bits and pieces in the -- General Court.

Opening submissions by MR BREALEY (continued)

MR BREALEY: I will finish the regulatory context, I will go to the section B of our opening submission, which is the infringement, the distortion of competition. I will take that more quickly because obviously I went over

some of the ground yesterday and then after that I will move to exemption. Hopefully I will speed up a bit.

It is paragraph 59 of the written opening. I will try and do this more or less by reference to the written openings rather than going to the authorities because I don't actually believe that the principles of law are really in contention.

Infringement of article 101, clearly we have got to prove some sort of consensus and that consensus has a distortion of competition. As I understand it, the requisite effect on trade is admitted, so we don't have to bother about effect on trade.

So I need to just deal first with the consensus relevant for the application of article 101, because as the Tribunal knows, if it is a purely unilateral act, then it doesn't fit within 101; if there is a degree of consensus, then it does.

As I highlighted yesterday, MasterCard at paragraph 8 of the skeleton say this: although they have amended their defence to plead various matters, they haven't dealt with it so I will try over the next 10 or 15 minutes try and sort out what they are submitting.

Paragraphs 59 to 61, I know the Tribunal knows these principles well but the quote from ANIC is quite illustrative:

"The list in article 101 is intended to apply to all collusion between undertakings, whatever form it takes. There is continuity between the cases listed. The only essential thing is the distinction between independent conduct, which is allowed, and collusion, which is not, regardless of any distinction between the types of collusion."

So the courts have time and time again referred to agreement, concerted practice, decision of association of undertakings. It is all designed to catch a degree of collusion and the only difference is, to a certain extent, the intensity.

So, that is essentially the guiding principle. Over the page at 63 and 64 we set out how the court -- the CJEU approaches the decision of association of undertakings. So the legal principles applicable to the nature of an association of undertakings are set out -- this is in the MasterCard judgments, essentially:

"A question for determination is whether the restrictive conduct, the decision to set the MIF, stems from an institutionalised form of coordination."

So that essentially distinguishes a concerted practice. So you may have a concerted practice in the smoke-filled rooms or just on the question of reciprocity of dealing, but you haven't actually kind of

bought into some sort of institution.

So the question is, is there an institutionalised form of coordination? That is what the European Court is essentially looking for when it is a decision of association of undertakings.

It goes further than that, the concept of concerted practice. I mean, in a nutshell, you don't need the institutionalised bit. You just need a form of coordination between undertakings, which knowingly substitutes practical co-operation between them for the risks of competition.

That's essentially the difference between the two and they can be the same, you can have a concerted practice and a decision, but what you are looking for in a decision of association of undertakings is some form of institutionalised form of coordination, but when it comes to concerted practice are you knowingly substituting practical co-operation for the risks of competition? Those are essentially the two legal principles applicable to the requisite consensus in this case.

If I go to paragraph 73, as I referred to yesterday, but this sets out what MasterCard say now takes them out of an association of undertakings. So I will take this more slowly. So MasterCard now accepts that it formed

part of an association of undertakings at least until June 2006. So at least for two and a half years of the claim period they accept that there was a decision of an association of undertakings.

PROFESSOR JOHN BEATH: Sorry 2006 or 2009?

MR JUSTICE BARLING: 2009.

PROFESSOR JOHN BEATH: 2009, I think.

MR JUSTICE BARLING: You might have said 2006.

MR BREALEY: Sorry, what I meant to say -- so they admit that from 2006, which is the start of our claim period, until June 2009, there was a decision of an association of undertakings.

PROFESSOR JOHN BEATH: That's fine.

MR BREALEY: Sorry. Alternatively they say there was a decision of association of undertakings for a three or four-year period until June 2010, alternatively, until 2014. So we know for starters that there was a decision of an association of undertakings. I referred the Tribunal yesterday to paragraph 373 of the decision. I don't think we have to go back to it, but there the Commission, that's 373, emphasised the continuing effects of the decision of an association of undertakings.

It said the fallback provisions were "rooted in the previous practice". They said the IPO has not really

altered anything. There was a decision prior to the IPO and its continuing effects are rooted. So in other words what I'm trying to submit here is that if you just 73(a): By June 2009, authorities to the board, or June 2010, certain banks had no longer got the class M shares. Does that somehow constitute a guillotine on the continuing effects of what is admitted to be a decision of an association of undertakings for a two-year, three-year, four-year period? I throw that out because it is not really explained why simply because a bank gives up a class M share, the fact that it was a decision of an association of undertakings to begin with, why that doesn't continue in its effects. Why does the mere fact that you are just giving up some shares alter the continuing effects, what the Commission says at 373, "rooted".

So that is one of the first points. But then I will deal with what they call these facts. So June 2009, withdrawn all specific authorities that have previously been granted to the European board. June 2010, certain member banks, class M shares, cease to exist. So a certain class of shares cease to exist. Then UK member banks cease to have any power in relation to MasterCard's UK domestic rules.

So we know in the decision that the banks had no

role in the MIF at all, but they did have some role until 2014 for some ancillary matters. Just before I deal with this, we also know that MasterCard continued to receive statement of objections. One was, we saw that in front of my Lord last year, MasterCard continued to receive statement of objections even in the last couple of years and the Commission is still saying that MasterCard is a decision of an association of undertakings. So the Commission at least in a statement of objections doesn't regard that these three matters have the slightest relevance.

Then Mr Hoskins can explain orally rather than in writing why these three facts alter the analysis and if I can try and do that by reference going to paragraph 90 of the written submissions and just teasing out the sort of considerations that the Commission looked at to determine whether MasterCard and the banks constituted a decision of an association of undertakings, so a form of institutionalised form of coordination.

Paragraph 90 we have set it out in some detail, so I don't have to go to the decision. But first, it says -- again, remember, that what is being submitted that because the banks no longer have any role in the MIF, there's not an association of undertaking:

"First, as before the IPO, each participant in the

organisation remains a credit institution under such undertaking."

So that is the undertaking bit:

"Second, following the IPO, decisions of the organisation's management bodies are still binding upon the organisation's members and no bank can participant in the card's activities of the MasterCard's organisation without complying in all respects with the bylaws, rules and regulations and published policies of the organisation."

So they acquiesce in being bound by these rules:

"Third, the concept of membership equally remained unchanged. Member banks continue to be bound by the very licence agreement that they concluded before the IPO."

And they still have to comply with all the network rules. So we know we have the scheme rules and the banks sign the licence agreement and sign up to the rules and agree to be bound by them.

The fourth point is, I think, Mr Hoskins point which is that the Commission also refers, in the middle of that paragraph, the European board was maintained as a decision-making body, European banks only consented to changes to the governance:

"In approving the IPO, the European member banks

ensured that the European board kept its key decision-making powers."

Again, that wasn't the MIF but the European board did have other powers that Mr Hoskins can explain. So, that, to a certain extent, goes out of the equation in June 2009. Then it goes on:

"Fifth, as before the IPO continue coordinating the market behaviour of the organisation's member banks. MasterCard for an instance continues to publish the results of the multilateral agreements on interchange fees in the payment organisation, so that all banks know and abide by the agreements. As before the IPO, the three legal entities representing the organisation continue to enforce interchange fee agreements between the member banks by supervising the application of the correct interchange clearing message whereby the scheme own the MasterCard processes, the member card's transactions."

So again, there is some sort of institutionalised form of coordination because MasterCard is laying down these binding rules and sorting out the rules which apply to processing the transactions:

"Sixth, in order for a bank to become a member it is not necessary for it to acquire shares. Some banks are shareholders in MasterCard, but there is no such

requirement."

So you can clearly see that had, if you look at paragraph 73, had it been submitted to the Commission: well the banks no longer have the class M shares, it would have got pretty short shrift from the Commission saying: well, that is irrelevant, you can still become a member even though you don't have the shares.

So at paragraph 91 we submit that the Commission's reasons for considering that MasterCard was an association, were not simply to do with matters such as the powers of the European board or with shareholdings or individual banks' powers in relation to domestic rules, ie non-MIF matters. Only minor matters as far as we are aware. There were multiple reasons but at the heart of the Commission's point there was a simple one:

MasterCard's members are all banks. They all agree to be bound by the rules and policies decided on and enforced by MasterCard, both before and after the IPO. These rules, including the setting of the MIFs [and as the Commission went on to say] where undertakings entrust a third party to perform certain tasks that enable or facilitate the restrictive behaviour of the delegated undertakings, that does not exclude the existence of the restriction.

Again, we step back and just see that the MIF restricts, as we have seen and we will see briefly again, restricts -- the banks have agreed, whether expressly -- we would say expressly, but certainly implicitly, to coordinate their behaviour. Why? Because there is a common price chargeable in the UK which merchants indirectly pay.

MR SMITH: Mr Brealey, just so I'm clear, even if, and I have no idea if this is the case or not, even if the decision as to the setting of the MIF is one that is taken entirely internally to MasterCard and effectively is imposed on member banks by virtue of their signing up to the scheme, that is enough, on your case, for this to constitute an association of undertakings? A decision of --

MR BREALEY: The answer to that is yes, sir, but I would go further because that was the very proposition that MasterCard was submitting to the Commission and appealing to the General Court and to the ECJ. They said we don't have -- we, the banks, don't have any powers as regards the MIF. We might have some ancillary loose powers as regards some domestic rules, but we don't have any powers as regards the MIF. That is unilaterally imposed on us and the Commission in the decision upheld by the two courts said, that doesn't

matter. What Mr Hoskins is now saying is: well, I buy into that, but those ancillary powers that the banks retained, you know, he is going to explain, are on a domestic basis, alter the equation and that means that because they have lost those ancillary powers they are no longer an association of undertakings.

Again, I come back to that quote at 357 where banks:

"... entrust a third party to perform certain tasks that enable or facilitate the restrictive behaviour of the banks that does not exclude the existence of the restriction".

We would submit that the European Court has clearly upheld that. There is an institution, it is called MasterCard, and through that institution the banks have coordinated their behaviour and MasterCard to a large extent acts in their collective interests.

The bottom line is that those facts, even if one says it is not an institutionalised form of coordination, so somehow you have got the MasterCard up here and all the network rules and the banks buying into it being bound by these rules, even if you don't say that's an institutionalised form of coordination, we fall back on the concerted practice because it is quite clear that the banks are -- and this is at paragraph 94 -- and the test is at 65, that this MIF is

a form of coordination between banks which knowingly substitute practical co-operation for the risks of competition and we saw that time and time again yesterday, that there is no competition between the banks on the MIF, because MIF sets a multilateral interchange fee. It is inherent in the very word, multilateral interchange fee.

MR SMITH: And it doesn't make any difference to your argument that it is a default multilateral interchange?

MR BREALEY: No.

MR SMITH: Is that a legal point or is that a factual point? I mean, if it were factually the case that yes, there was this default, but actually all the banks who were members were readily agreeing different bilateral rates, would your case still be that this was a decision of association of undertakings.

MR BREALEY: The case would be still be certainly the fact that it was a default didn't bother the Commission. We know as a matter of practice that it is almost exclusively a default and we also know from the scheme, I can take you to it -- we also know that the scheme rules, 3.3, positively encourages the MIF and discourages bilaterals. In practice, there are very, very few bilaterals.

So as a matter of law, the fact that it is a default

doesn't matter, it certainly didn't bother the Commission. As a matter of practice, it is a MIF and it is just a common price that the merchants end up paying, and I'm surprised that MasterCard are still running this point but that's not very relevant.

MR JUSTICE BARLING: Is there anything anywhere in the Commission decision or the General Court or the Court of Justice that touches on the alternative points, agreement of concerted practice that you rely upon?

MR BREALEY: No. As far as I'm aware, the Commission nailed its colours to the decision of an association mast and we see in the reports, again, the stock phrase applies to all forms of collusion, it just depends on the intensity which label you put on it, and the Commission found it was a decision of an association of undertakings. The OFT refers to a decision of an association and a concerted practice.

MR JUSTICE BARLING: Just remind me, in their decision did they find it on that basis or did they find it -- don't worry.

MR BREALEY: I will ask Ms Ford to have a look at that, but certainly I do remember seeing that in certain SOs there is the three. Again, I just come back to the simple point: this is a multilateral interchange fee which is set by MasterCard, which the banks agree to abide by.

MasterCard supervises and enforces it and discourages bilaterals.

That is all I need, I think, say on the decision of association of undertakings. I am not, my Lord, going to go through the relevant market definition, which starts at paragraph 96. The reason for that is we have set it out in writing and MasterCard haven't dealt with it at all in their skeleton, so I will see whether Mr Hoskins makes any oral submissions on it.

We say it is quite clear it has been consistently held that the relevant product market is the acquiring market and that has been upheld by the Commission and the General Court.

We have got to look on the distorted effects on the acquiring market.

MR JUSTICE BARLING: Is your case on that that it is -- do you suggest that that's something on which we are bound or are we, as it were, at liberty to look afresh at the relevant market because we are looking at the UK market now?

MR BREALEY: It is a very interesting point. There are no degrees of being bound, in a sense. I would say that technically this Tribunal is not bound because the Commission found the acquiring market in the context of an EEA MIF. But in circumstances where

the Commission has gone through the analysis -- I mentioned yesterday when -- why is it that the MasterCard has been regulated, because they have not followed the logic of the General Court from the CJEU and the Commission's decisions.

So I say it would be an extreme -- with the greatest respect, I have just said my Lord can do anything -- it would be an extreme departure from what the Commission has held for the last 15 years. I mean, it is a very tricky one. I have said probably you are not bound by the decision but it clearly relates -- the product market, we are not just talking about geographic market, we are talking about the product market and the Commission has gone through the analysis, the General Court has upheld it, it would be an extreme -- and Mr von Hinten-Reed -- and one of the things we have tried not to do, I mean I have gone through the Commission decision because of course the logic is there, but Mr von Hinten-Reed also has gone through a separate analysis.

When one reads Dr Niels' report, it is, with the greatest respect, a little bit wishy-washy. He refers to three markets but says you have got to look at the joint product which has been rejected by the Commission and the General Court. He doesn't

actually -- he strikes but doesn't actually wound. It is not clear from his report -- I shall put it to him, obviously, whether he accepts that there is a distinct market, the acquiring market. He refers to three markets. He then says: well, you have got to look at the issuing market, but that has been rejected by the General Court. The General Court has said you look at the acquiring market.

MR JUSTICE BARLING: They said the Commission looked at the acquiring market and there was no reason to doubt the legitimacy of that approach.

MR BREALEY: Yes, but then in the analysis of 101(3) they certainly proceed on the basis that there are two markets. They certainly proceed on the basis that there is an acquiring market, merchant, and an issuing market, cardholders, and they deal with the interaction between the two. But they certainly hold -- and I referred to some of the passages yesterday, that when you are looking at the restriction of competition in the acquiring market it is impermissible to look at whether cardholders are going to get less free holidays in Berlin or whatever it is.

So that, the General Court has expressly said. So it is a little bit more than just saying the Commission hasn't carried out a manifest error.

MR JUSTICE BARLING: Yes.

MR BREALEY: A lot of the analysis is premised on two separate markets.

MR JUSTICE BARLING: Yes. They doesn't start by saying that, and then go on to look at the circumstances in some detail, don't they?

MR BREALEY: Yes. So we rely on what Mr von Hinten-Reed says and what the Commission says and the General Court. The fact that there is nothing in it, in MasterCard's skeleton at all, we would say, to a certain extent, speaks volumes.

MR SMITH: Mr Brealey, you put it quite neatly to say that there is no degrees of being bound: you are either bound or not bound.

MR BREALEY: Yes.

MR SMITH: Looking at it conversely, if you have a question of fact which is for us to decide, in a sense, would you say that the same feature applies, that we have got to look at the evidence and simply reach a conclusion on the evidence as to what the factual situation is?

MR BREALEY: Yes.

MR SMITH: So would it be fair to say that looking at your case on, let's say, the nature of the product market, we will have the evidence of Mr von Hinten-Reed and that that evidence is given added lustre or weight by fact

that it coincides with the findings of the Commission and the court?

MR BREALEY: Yes.

MR SMITH: Would that be a fair way of putting it?

MR BREALEY: Absolutely. I make my submission on behalf of Sainsbury's, agreeing with all that, but saying it would be an extraordinary proposition to depart from the logic of what the Commission has applied, and has applied since 2002, at least, if not before. So it is the weight -- I mean it is not just supported by the Commission, it is a deep-rooted practice of the Commission. But, my Lord, you are right.

That then takes me to distortion of competition. I will take this quickly because we went over some of this ground but I do need to emphasise it because I need to just come back to the counterfactuals.

I start at paragraph 105, the distortion of competition. The law. I have tried to identify four legal principles that guide the Tribunal in determining whether there is a distortion of competition. This is paragraph 105. The first is that the aim of article 101 is to protect the competitive process.

Second, article 101(1) is not concerned with balancing pro-competitive effects with anti-competitive effects. That is the role of article 101(3). So we are

not in a rule of reason, a US-type anti-trust case, where you join it all up together.

Third, a restrictive agreement may fall outside. It is objectively necessary for the viability of a legitimate objective. We will come onto that again but I emphasise the mission impossible, the European Court of Justice have said it is a very high threshold.

Fourth, an examination of whether an agreement distorts competition must be viewed by reference to a counterfactual. That's Mr Hoskins' two principal points he makes in his skeleton.

Again, I will take this as quickly as I can because it is probably familiar territory, but if I can take the first legal proposition, that's protecting the competitive process. Some of these points are made in the guidelines so could I just go to E1. It is tab 2A. These are the Commission's guidelines on article 101(3), the old article 1.3, and 14 to 16 is relevant to the competitive process. I will just highlight the first bit of 14 and 16. So this is on protecting the competitive process:

"The prohibition rule [this is paragraph 14] of article 101(1) applies to restrictive agreements and concerted practices between undertakings and decisions

by association of undertakings ...(Reading to the words)... courts is that each economic operator must determine independently the policy which he intends to adopt on the market."

That is a fundamental principle of article 101, which, if you just, again, sit back and see what MasterCard's scheme rules do, where you have a multilateral interchange fee, it is a multilateral agreement. It is a multilateral consensus. 16:

"Agreements between undertakings are caught by the prohibition when they are likely to have an appreciable adverse effect on the perimeters of competition on the market such as price, output, product quality, product variety, innovation. Agreements can have this effect by reducing rivalry between the parties to the agreement or between them and third parties."

We saw yesterday that a key consideration the Commission and the court had in deciding that this multilateral interchange fee was a distortion of competition is because it did distort the rivalry between MasterCard's member banks; they no longer compete.

We have also referred to T-Mobile but paragraph 14 and 16 emphasises a key aim is to ensure that undertakings compete and they do not act so as to reduce

the rivalry between them. If they do reduce the rivalry between them that is a -- at least a restriction of competition between them. So that is the first point I wanted to -- the protecting the competitive process.

The second legal point is that article 101 is not concerned, this is paragraph 109 of the skeleton, with balancing pro-competitive effects with anti-competitive effects.

Again, we have set out some of the case law on this and it is pretty obvious stuff: European Night Services, the Métropole case. But again, I can take it in the guidelines because these are guidelines relating to 101(3) at paragraphs 10 and 11, which we refer to in our skeleton, particularly 11:

"The assessment under article 101, thus consists of two parts. The first step is to assess whether an agreement between undertakings has an anti-competitive object, actual or potential anti-competitive effects. The second step, which only becomes relevant when an agreement is found to be restrictive of competition, is to determine the pro-competitive benefits produced by the agreement and to assess whether those pro-competitive effects outweigh the anti-competitive effects. The balancing of anti-competitive and pro-competitive effects is

conducted exclusively within the framework laid down by article 101(3)."

I go back to the Visa decision, paragraph 59, where Visa were saying: well, if I don't have a MIF, it makes it more difficult for me to compete with other schemes because it may well be that my cardholders are not as happy, whatever, and the Commission at paragraph 59 of Visa said that is an article 101(3) consideration. The balancing restrictive effects with what you say are the benefits.

MR JUSTICE BARLING: So the rivalry -- coming back to the guidelines -- that would be protected, that needs to be protected but that is impugned by the MIF, is the rivalry that would exist between acquiring banks, is it?

MR BREALEY: Yes. It is as Mr von Hinten-Reed and the Commission has said, that if you don't have this common price, so this common price comes down and it means that the merchants can't go to the acquirer and say that price is a bit iffy. So if the acquirer is looking over their shoulder the whole time not knowing what the other acquirer is going to do, you start to get some competition in the acquiring market and the merchants can start playing off the acquirers.

Now, MasterCard says, well, you know, there are benefits to the MIF but if there are benefits, then

let's have a look at them under article 101(3). But one cannot deny that the MIF dampens the rivalry between the competing banks who are part of the MasterCard scheme.

The third legal principle is objective necessity. Again, I won't go to the cases because of the time but we have set out the relevant paragraph of the CJEU at paragraph 117 of the opening submissions.

This is important to Mr Hoskins' counterfactual. When he is referring to this Visa counterfactual I need this collective price arrangement, I need this, I need my members to coordinate on price. Why? Because I won't be as profitable.

See how the European Court is approaching MasterCard's argument before it. So MasterCard have said for the last 15 years that the MIF is absolutely essential for the scheme and without it we might as well go home. That's essentially what they are saying.

At paragraph 117 of our submission we set out the main court, the CJEU, and I will just read the first paragraph:

"Where it is a matter of determining whether an anti-competitive restriction can escape..."

So escape the prohibition laid down in article 101:

"... because it is ancillary to a main operation that is not anti-competitive in nature, it is necessary

to inquire whether that operation would be impossible to carry out in the absence of the restriction in question."

So we are talking about objective necessity here. To take out the restriction completely from article 101:

"Contrary to the appellant's MasterCard claim, the fact that the operation is simply more difficult to implement or even less profitable without the restriction concerned cannot be deemed to give that restriction the objective necessity required in order for it to be classified as ancillary. Such an interpretation would effectively extend the concept to restrictions which are not strictly indispensable to the implementation of the main operation."

The next sentence is important:

"Such an outcome would undermine the effectiveness of the prohibition laid down in article 101(1)."

MR JUSTICE BARLING: So "impossible" and "strictly indispensable" seem to be the catch phrases there.

MR BREALEY: The catch phrases. Simply because it is less profitable doesn't make it impossible.

MR JUSTICE BARLING: Can I ask you one thing, the answer to which might be obvious, but there is no issue between you that the MasterCard scheme complies with the other requirement, namely, that you don't suggest that absent

the MIF, the main operation is not anti-competitive?

MR BREALEY: No.

MR JUSTICE BARLING: So that is a given.

MR BREALEY: No, I mean, I think everybody says that these credit cards are a jolly good thing.

So as my Lord says, those are the key messages. It is not mission difficult, it is mission impossible.

Counterfactual, this is the fourth legal point and is relevant to Mr Hoskins' two principal points he sets out in the section on 101(1).

I will go to paragraph 121 and then -- and I will just go to the Advocate General which I'm not sure is in the bundle, but I emphasise -- so we are looking at the counterfactual. Again, Mr Hoskins is saying, I'm at 0 MIF, Visa is at 0.91%. In the hypothetical world, I'm going to lose market share.

121 of the opening submissions:

"Any counterfactual must be realistic. The CJEU stated in its judgment [this is in the MasterCard] that in order to contest the ancillary nature of restriction the Commission may rely on the existence of realistic alternatives ...(Reading to the words)... later in the judgment it follows from this that the scenario envisaged on the basis of the hypothesis that the coordination arrangements in question are absent must be

realistic."

So I just emphasise here that Mr Hoskins' counterfactual, when he asked the Tribunal to test the objective necessity, must be realistic. That's the key message.

A counterfactual, by its very nature, is a hypothetical. What would happen if I didn't have the restriction? What would happen? What is the hypothetical world. I don't think, have we got the Advocate General? -- I will just hand that up. (Handed).

Again, what are the considerations that this Tribunal would have to look into when having this realistic counterfactual? This is the Advocate General in the MasterCard case. So MasterCard knows it extremely well.

It is paragraph 53 that I would like to emphasise. This is the sort of considerations that are relevant. Again, this is not new stuff, this is textbook Bellamy and Child, Professor Whish. There's nothing new about this. So paragraph 53 of the Advocate General Mengozzi's opinion, and if I can just read it:

"As the second factor in that comparison is the result of an assessment based on hypothesis, it cannot be required that proof be adduced that the scenario used

in the context of that assessment will inevitably arise in the absence of the ...(Reading to the words)...the position of the parties to the agreement on the relevant market..."

And I emphasise the next bit:

"... the structure of the market and also the economic, legal and technical context governing its functioning, the conditions of competition, both actual and potential, the existence of ...(Reading to the words)... and the existence of intellectual property rights."

So just for example, when he refers to some of the cases in the footnote, for example, footnote 53, which is the economic, legal and technical conduct governing its functioning, footnote 53 refers to the well known O2 case where the General Court emphasised the importance of the examination of competition in the absence of an agreement in the case of markets undergoing liberalisation or emerging markets.

They were looking at -- the counterfactual was: this is a liberalising market, and I will come onto the relevance of that in a moment but it is important when the Tribunal is looking at Mr Hoskins' counterfactual to have regard to all relevant factors, including legal factors. I flag the point, including the fact that Visa

itself has been refused an exemption and has been told that its similar or almost identical four-party system creates an inflated minimum floor as a result of the lack of rivalry between its member banks.

I will just flag that point a bit later on. So that is the law on the counterfactual. One has to look at a realistic counterfactual in the light of all relevant factors and that includes legal factors. If I could then just go very quickly, because I laboured this a little bit yesterday, to the application of the law to the facts.

I won't go through this in any detail because it is in writing, but at paragraph 124, I emphasise what I have called the three vices. At 126 the first vice is the impact on the competitive process and we set out there some of the -- I'm just opening here, I'm not closing, but I'm trying to set out some of the bright line points we say supports the facts -- the facts that support the fact that there is an impact on the competitive process.

So at paragraph 130, the second vice, which is the de facto minimum price. Again, this may appear longer in our closing but we are just setting the scene here. The de facto minimum price we refer to the Visa decision, the MasterCard decision, Mr von Hinten-Reed.

The third vice, at 133, is the upward pressure on MIFs. So it is not just a minimum price, a floor, it also results in an inflated price and I don't think paragraph 134 is confidential.

So the upward pressure of the MIFs -- I mean, MasterCard's own witnesses testify to this, the upward pressure of the MIF is consistent with what Mr Keith Robert Douglas, the executive vice president and general manager says. Mr Roberto Tittarelli, global product and solutions regional lead Europe of MasterCard have to say in their written evidence about the role of higher MIFs and competing to attract issues, and Dr Niels also agrees that:

"Competition between card schemes tend to put upward pressure on the MIF."

So MasterCard's own economist accepts: that throw this money at the issuers does put upward pressure on MIFs. That's their own case.

It is just a question of taking these facts and how you characterise them from a legal perspective. We say it is a distortion of competition that needs to be exempted in some way; they say it falls outside of article 101 completely.

At paragraph 137 I refer to the MasterCard's pro-competitive argument. I will skip over that and if

I could just, in a few minutes, refer to the two counterfactuals. This starts at 144 of the opening submissions. As we know, there are two counterfactuals that are put forward by MasterCard in support of its argument that article 101(1) doesn't apply at all. You never get to the exemption stage.

The first counterfactual is the hold-up argument and we went through that in some detail yesterday. We set it out again in some detail in the written submissions. We say that the problem with the honour all cards rule can be solved as the European Court itself said was likely by this ex-post pricing rule, but, again, we will come onto that in the evidence and in the closing.

On the second counterfactual, the competing schemes counterfactual, so again, this is Mr Hoskins' argument that you have got to assume in the counterfactual world that Visa can, with impunity, carry on charging 0.9% and you have got to assume in the light of what Dr Niels says that the same banks or whatever bank it is, I don't know, I'm making this up, but Lloyds Bank is issuing MasterCards knowing that MasterCard has zero MIF and Visa with 0.9 is going to migrate from MasterCard to Visa.

So he is making two assumptions here: first, that the Visa rate will stay the same and the second is that

the banks will migrate.

And he says therefore this shows that the MIF is objectively necessary within the meaning of the court's case law. So this Visa counterfactual is an object objective necessity point.

MR JUSTICE BARLING: To avoid the Doomsday scenario.

MR BREALEY: The Doomsday scenario, as they submitted before the Commission as regards Amex. We don't know whether this Visa argument was ever made, advanced to the Commission. Certainly as we saw yesterday the Amex counterfactual was. We do know, I will get onto why it is flawed, but we do know that MasterCard and Visa were always saying to the Commission: you have got to treat us the same. I just do not know whether this is a completely new point that has been dreamt up in these proceedings or was advanced at some point before the Commission and then at some point the Commission said you can't be serious and it got dropped, I just don't know.

What I can say is that -- and to a certain extent, MasterCard having said: well, even with Amex there is a death spiral and the Commission is saying no, one would have said that if they really had faith in it they would be making the same point to the Commission in its 2007 decision, notwithstanding this is a UK MIF and that

was a EEA MIF.

Can I just emphasise, as I tried to yesterday, why this Visa counterfactual, we say, is flawed. I will just summarise the three points that I tried to make yesterday. The first point is that it is a 101(3) argument. You have, on the assumption that Visa is acting lawfully and charged the 0.9, we know that you have the MasterCard scheme, where there is a -- however you want to phrase it, there is some sort of coordination on price, and the argument is that this coordination on price is necessary for me to compete with Visa.

We saw in the Visa decision, paragraph 59, the Commission saying that argument is a 101(3) agreement, it is not a 101(1) argument. Again, this is not this case, but one can just test the proposition that Mr Hoskins is putting forward, so it is not this case, but let's assume that you have a hard core price fixing cartel. And that hard core price fixing cartel is saying: I need to have this cartel because otherwise I will be less profitable against this other competitor.

You would only have to just say it to realise that actually there's something wrong with it. So as a matter of law we say it is not a 101(1), it is a 101(3).

MR JUSTICE BARLING: Unless you are looking at it through the eyes of the objective necessity point? I mean, it is the same point, isn't it?

MR BREALEY: Yes.

MR JUSTICE BARLING: I mean they rely upon exactly the same argument in relation to objective necessity.

MR BREALEY: Yes. This Visa counterfactual is an objective necessity point. They say this MIF is objectively necessary --

MR JUSTICE BARLING: Otherwise Doomsday.

MR BREALEY: -- I can't compete with Visa. I will come onto Doomsday, but otherwise Doomsday, yes.

MR JUSTICE BARLING: But that is the argument, I think it is total market collapse.

MR BREALEY: That is the argument.

MR JUSTICE BARLING: Then the point is repeated, but you say -- I'm just trying to understand, what you are dealing with now is not the objective necessity, not in the context of objective necessity. You are saying now, as a reason why there is no distortion of competition, why they say there is no restriction of competition.

MR BREALEY: I see what you --

MR JUSTICE BARLING: Sorry I'm getting muddled here.

MR BREALEY: No, I can see why.

MR JUSTICE BARLING: You say it is not 101, it is 103.

MR BREALEY: What I'm saying is, if someone runs an argument saying that: I need this in order to compete, that, in its character, is a 101(3). We are not in the realms of objective necessity at all.

MR JUSTICE BARLING: Right. I see.

MR BREALEY: Objective necessity is something -- has a character, as the Commission said in paragraph 59 of Visa, is something more technical. If you start to run an argument -- you have your heading "objective necessity", and you say: it is objective necessity because I need to compete better. The answer is that is not an objective necessity argument. The character of it --

MR JUSTICE BARLING: I think what they are saying is, they are saying, first of all, they are saying: we need to compete at all effectively.

MR BREALEY: Yes.

MR JUSTICE BARLING: Aren't they?

MR BREALEY: Yes.

MR JUSTICE BARLING: Because they say the alternative is total market collapse because we can't assume that Visa won't be carrying on with the MIF, at their own desired level.

MR BREALEY: But my first point is that as an argument it is not an objective necessity argument; it is a 101(3)

argument. Why? Because you are saying that I need -- this restriction -- this restrictive agreement produces efficiencies which allows me to compete better.

MR JUSTICE BARLING: They might be saying that as well but are you saying it could never -- my understanding of what they are saying is that: we couldn't compete at all.

MR BREALEY: Let's assume --

MR JUSTICE BARLING: In other words: our scheme will die, collapse or whatever you want to -- whatever phrase you want to use, and Visa -- assuming Visa carries on as before, they will just take all our business. So, in order to compete at all we have to have a MIF that competes. It is not a sort of efficiency argument, it is a --

MR BREALEY: I am submitting it as an efficiency argument, it may be my Lord may disagree.

MR JUSTICE BARLING: It may be an efficiency argument too. They may raise it -- I thought they did raise it a second time in relation to the --

MR BREALEY: It is also slightly crafty that you are talking about losing market share. The way one should be looking at this is that, actually, this is a kind of an article 101 point. You should not have had this MIF at all. So this MIF should have been zero right from

the word go. So you should never have had a MIF. Now you are coming to the court and saying: well, I actually need this. I'm not talking about losing market share, I know that I should never have had that MIF, I want to compete with someone who is acting lawfully and therefore I need this restriction -- depressing the rivalry -- to raise price so I can now compete. So it depends which lens you are looking at. It is very forensically attractive to say: I'm going to lose market share but you can also look at it as you should never have it in the first place and an argument saying: right, I want to start now. A new scheme comes in and the new scheme says, I need a third -- a third scheme comes in and says the -- the Brealey card system, the Brealey card system says: right, I need, in order to compete with Visa and MasterCard, to have this price fixing agreement. MasterCard and Visa, they are acting lawfully, they are not doing it through the coordination, but I need the coordination in order to compete with them.

So the similar argument would apply to a new entrant, and that's why I say it is an efficiency argument.

MR JUSTICE BARLING: That's why you say it is 101(3)?

MR BREALEY: Yes. That is the first point. The second

point is it is a wholly unrealistic counterfactual, and the reason that I refer to paragraph 53 of the Advocate General is because one has to look at all the relevant factors. Again, standing back from it, having listened to how Visa have been treated in the Visa decision, being told that their MIF has exactly the same three vices, having been told that their exemption would not renewed on the basis that they are putting the free funding of credit onto the merchants and being told that, having given commitments to lower the MIF on the EEA at least, having been told that they are being sued in respect of the high MIF in the Commercial Court, why, in a realistic counterfactual, one should assume that Visa are just acting -- that they can have that MIF, again, you don't have to say that it is unlawful, you just say is this a realistic counterfactual?

Is it realistic that the same banks are going to migrate to Visa when Visa have the same legal problems? They have been investigated by the same competition authority and they have the same legal problems from the same retailers. I come back to this extremely bizarre situation, this argument, that if we had sued MasterCard and Visa together and they were both to my right, and one Visa person on the Monday comes into court and says: I will go bust if I lose out to MasterCard, so he then

goes and then somebody else comes in and says -- from MasterCard; it just -- it doesn't -- it is not a realistic counterfactual.

MR JUSTICE BARLING: Do you say the only realistic counterfactual is one which assumes that Visa are in precisely the same boat and have got to -- we must assume, if we are looking at this counterfactual, that they also are going to have to reduce their MIF to the same level effectively, about the same level?

MR BREALEY: That's essentially what I'm saying. I'm going slightly more. You can't assume it in Mr Hoskins' favour because he is putting forward a positive case which says that MasterCard will lose market share to Visa. So he is asking the Tribunal to assume the existing Visa MIF and the banks will migrate and in my submission there's so much uncertainty about this that it would not be safe to assume it.

That is my second point, that it is not a realistic counterfactual, on the contrary, the Tribunal is divorcing itself from reality if it just says: well, in the counterfactual Visa will charge the same, 0.9, even though I, the Tribunal, know that Visa have been told they have the same three vices and they have been regulated. It is a wholly unrealistic counterfactual.

The third reason which I tried to articulate

yesterday comes to, again, it is a question of fact, which is the Doomsday point. In the skeleton, MasterCard make the point that it is Doomsday, but it is not mission difficult, it is mission impossible, and when one looks at Dr Niels' report, even he -- and this must be the high watermark of their case -- even he says that MasterCard end up with some market share. It might be a low market share, but they end up with some market share.

So the third reason is that although they may make, as the European Court said, less profit, and although as the European Court said it may be more difficult for them, it is not impossible to operate the MasterCard scheme in the absence of a MIF.

For example, if they don't have the MIF, they still have the system of bilaterals, and the bilaterals clearly, even on our case, come up with some interchange fee, it is just a lower one.

I can put a further point into the mix which is that if you are really looking for a realistic counterfactual, what actually happened when one looks at the witness statements, they lowered their MIF to get an exemption. Again, this will have to come out on the evidence, but even on their own case, MasterCard is still there and as -- I refer to the passage, unless you

have the objective necessity criteria interpreted very strictly in this impossible high threshold, you are depriving article 101 of its effectiveness and that's why, as my Lord put to me, you have got these words "less profitable" versus "impossibility".

That is all I have to say on the restriction of competition and I will go onto exemption.

MR JUSTICE BARLING: Shall we have a short break then.

(11.45 am)

(A short break)

(12.00 pm)

MR BREALEY: So, if I could move to section C of the opening submission, which is paragraph 164.

MR JUSTICE BARLING: Yes.

MR BREALEY: Just to flag, I'm not going to go in great detail into MasterCard's two methodologies. I shall flag it, but to a certain extent that --

MR JUSTICE BARLING: All right.

MR BREALEY: I need to set the scene obviously.

Paragraph 164, 165 and 166, just to recap as to where we are:

"Pursuant to the merchant indifference test, the MIF of a payment card cannot exceed the value of the transactional benefits that are generated for retailers by using a card as opposed to cash."

Then we set out:

"The Commission for the last several years has calculated both MasterCard and Visa's intra-EEA MIFs, and some domestics MIFS, by reference to the MIT, having abandoned the methodology based on issuer's costs that had been exempted in the Visa 2 decision. The European Parliament and the Council applied the MIT test to all MIFs in the EU, including domestic MIFs, when the interchange fees regulation was adopted. The application of the MIT has led to a significant reduction in MasterCard and Visa's domestic MIFs which are now subject to a per transaction cap of 0.3 for credit cards. These percentages are a maximum. Member states are entitled to impose lower figures."

So basically, we are just setting the scene here but we do know that after the infringement decision of 2007, the Commission formulated this MIT test, which you will see in a moment formed the basis of the undertakings that MasterCard gave, formed the basis of the commitments that Visa gave and forms the basis of the cap of 0.3% in the interchange fee regulation.

So this is not a test that Mr von Hinten-Reed is coming up with, it is a test that has been applied by DG Comp, the European Commission and the Parliament.

What is the impact? The actual MasterCard UK MIF as

paid by Sainsbury's over the claim period -- I don't think this is in blue -- was on average 0.92 for credit cards. Mr von Hinten-Reed has applied the MIT to calculate MasterCard's UK MIF and reaches the conclusion that the level of the UK MIF should, during the relevant period, have been up to 0.15% for credit cards.

So he concludes therefore that the higher level of the UK MIF was not justified under article 101(3) and we will have a look at some of this in a moment. By way of introduction as well, MasterCard has not calculated the UK MIF by reference to the MIT to the test for the purposes of these proceedings. So it hasn't applied the test. Instead, Dr Niels has adopted two separate methodologies by reference to which he seeks to justify the actual levels of the UK MIF and these are -- I think these are Dr Niels' descriptions -- he applies an adjusted benefit cost balancing approach, which is effectively the discredited issuer's cost methodology. So MasterCard are still pursuing this cost methodology and the free funding point, the cost of credit. And he says he has an adjusted MIT approach, which is not actually a MIT approach at all. We have described it in the opening submissions as a slightly Kafkaesque approach, and the comparator seems to be Amex.

To a certain extent I'm going to leave MasterCard to

develop their methodologies. I shall make some points on it. You have probably seen the diagram, but just to see the diagram of the MIT test, go to bundle D2, tab 2 and it is page 264 of the bundle. So this is the first report of Mr von Hinten-Reed. It gives a neat illustration of the MIT MIF concept. It is page 212 internally and 264 of the bundle at paragraph 708. As you will have seen, the comparator is the cost of cash.

So we see there, on the left-hand side, the cost of cash. On the right-hand side we see the card payment. So the non-MIF cost of cards. Then the shaded bit is essentially the level of the MIF compared to the cost of cash. In other words, it is said that a card payment results in an efficiency gain because it reduces the cost of the payment transaction and merchants can be required to pay for the difference between the card payment and the cost of cash.

So the diagonal bit is essentially the level of the MIF. The top bit that goes on is the current MIF. So in essence, the overcharge is the bit shaded in the lighter grey.

So that is in just a diagram form what the MIT MIF is all about.

MR JUSTICE BARLING: The overcharge is the bit above the thick black horizontal line here?

MR BREALEY: Yes. So you are looking at the cost of cash, you are comparing that to the retailers' costs of card payments. One is seeing that the card payments lead to cost savings, efficiencies, because as I said yesterday you don't have to have the money in the till, the till to go back and the money to go to the bank. There are efficiency gains, that is why you are article 101(3) territory and I will show you a bit later on then why the merchant can be required to pay for that efficiency gain and that level of MIF then goes to the issuers and they can do with it as they want, give it to the cardholders for free holidays in Berlin or whatever it is.

But that is, in very simple terms, the concept of the MIT MIF.

MR JUSTICE BARLING: Sorry, is the efficiency bit the shape of the diagonals?

MR BREALEY: Yes, that is efficiency.

PROFESSOR JOHN BEATH: I think MIT minus MIFs bit is actually in some sense the benefits that go with accepting cards as opposed to cash.

MR BREALEY: Correct.

PROFESSOR JOHN BEATH: The balancing item. Balancing payment on top of the costs.

MR SMITH: And cost of cash is really shorthand for the cost

of processing a cash transaction by the merchant?

MR BREALEY: Correct. That's essentially what -- we will go through it in evidence -- the Commission did in its 2015 cost of cash survey.

I will flag the relevant bit in the opening submission, but the Commission has done a detailed survey. Dr Niels doesn't like all of it, but the Commission has done a detailed survey calculating the cost of cash and the cost of card payments.

Mr von Hinten-Reed, he takes that into consideration when doing his calculations, but it is -- I mean obviously the burden is on MasterCard to prove exemption, but it is noteworthy that they have not done a MIT MIF calculation. I'm going to show the Tribunal in a moment instances where they have, but for the purpose of these proceedings they have not carried out a MIT MIF calculation, as I say. They have done it on the basis -- as I said yesterday, when one looks at the disclosed documents and the witness statements, one doesn't find any calculation that MasterCard made which gives us any idea how the UK MIF was arrived at.

There are certain general policy statements, as we have seen, and I have to be careful because it's blue flashing, but it is clear from the witness statements that they look at a whole host of factors. But how

those factors have fed into any sort of precise calculation is a complete mystery. I went back yesterday to the Visa decision and the MasterCard infringement decision which says that if you give the card scheme a free rein to set a new level, then there's no kind of objective criteria by which you can judge it, that doesn't merit an exemption.

We saw yesterday almost the very first thing that I referred to in the Visa decision was the Commission objecting to what I call the free rein, that the card schemes, Visa and MasterCard, having a free rein to look at all sorts of factors, competing schemes, everything, without any sort of benchmark.

The Commission refused to exempt that and that's why in the Visa decision they had to come up with these three categories of cost which at least could be checked. But the simple point is that the evidence in this Tribunal does not show any precise calculation that MasterCard has undertaken which would, in any shape or form, support the average of 0.92 for credit cards. We know general considerations, but we don't know the detailed calculation and so when Dr Niels comes along and justifies the 0.92, he is justifying it ex post facto. He is saying: well this is a level and actually if you apply my two methodologies they have got it about

right.

That is by way of introduction. I won't kind of rehearse what's in this section, but at 167, the structure of the section, we first of all explain the key legal principles applicable to 101(3) and I will just go to the guidelines in a moment. I think the principles seem to be accepted. MasterCard in their skeleton refers to the guidelines and therefore I shall go to the guidelines.

Then, in the opening we show how the European Union came to adopt the MIT MIF and why it moved away from the issue of cost methodology. We then set out why -- this is paragraph 167 -- the MIT MIF may in principle satisfy the exemption criteria. That's 167(c). We set out at 167(d) how Mr von Hinten-Reed has calculated the UK MIT MIF, and then lastly, we set out some of the key arguments why we say that MasterCard's two methodologies to support its level -- MasterCard is not actually going through the calculation it made, it has the level and then it is seeking to justify it by reference to these two methodologies.

So that is the structure of the exemption section. If I could go to the legal principles relevant to article 101(3), as I say, MasterCard refer to the guidelines. So if I can go to the guidelines, it is

bundle E1, tab 2A again, the ones that we saw for the competitive process. It is the same guidelines. Bundle E1, tab 2A.

As the Tribunal know, there are four conditions that must be satisfied. So if one goes to paragraph 38, there are four conditions that must be satisfied, to pick up a point that Professor Beath made to me yesterday: MasterCard must adduce robust evidence that these conditions are satisfied.

So the guidelines essentially kick off at paragraph 38. The first condition starts at paragraph 48 of the guidelines. We set these out in our skeleton, for example, at paragraph 172:

"According to the first condition, the restrictive agreement must contribute to improving the production or distribution of goods. The provision refers expressly only to goods but applies by analogy to services."

One sees the heading under section 3.2, the first condition of article 101(3), "efficiency gains."

So we see in the section that what we are looking for is efficiency gains. Again, these are pretty, again, textbook points:

"It follows from the case law of the Court of Justice that only objective benefits can be taken into account. This means that efficiencies are not assessed

from the subjective point of view of the parties."

I will leave it to the Tribunal to read but paragraph 50:

"The purpose of the first condition of article 81(3) is to define the types of efficiency gains that can be taken into account and to be subject to the further tests of the second and third conditions of 81(3).

"Given that for article 101(3) to apply the pro-competitive effects flowing from the agreement must outweigh its anti-competitive effects, it is necessary [and we saw this yesterday from the case law] to verify what is the link between the agreement and the claimed efficiencies and what is the value of those efficiencies."

I emphasise that there and again, one sees this from the jurisprudence, one has to verify the link between the MIF and the efficiencies and the value of those efficiencies. That is expanded on in the next paragraph, paragraph 51:

"All efficiency claims must therefore be substantiated so that the following can be verified: the nature of the claimed efficiencies ..."

I will just pause there. When one is looking at Dr Niels' report, which, as one would expect from Dr Niels, it is a good read but one has got to look at

whether he has satisfied these conditions in paragraph 51, because we say he hasn't. One has got to look at the nature of the claimed efficiencies, the link between the agreement and the efficiencies, the likelihood and magnitude of each claimed efficiency and how and when each claimed efficiency would be achieved. These are testing conditions.

MR JUSTICE BARLING: Just remind me, Mr Brealey, is it common ground that when we are talking about the agreement here we are talking only about the restrictive element, the MIF, the allegedly restrictive element?

MR BREALEY: Yes.

MR JUSTICE BARLING: And the link --is it common ground --

MR BREALEY: I think it has to be common ground because the Commission has said it has to be the MIF. The General Court has said it's got to be MIF and the --

MR JUSTICE BARLING: So we can assume --

MR BREALEY: -- that's one of the areas where I would say it is binding on MasterCard. They have to -- it cannot be right that this depends whether it is a UK MIF or a EEA MIF. The European Court has interpreted this insofar as the MasterCard scheme is concerned and in my submission, it is absolutely plain that you have got to look at the MIF and not the scheme.

MR HOSKINS: In terms of it being common ground, I need to

rise, because it is not.

MR JUSTICE BARLING: No, no, it is not.

MR HOSKINS: If one is basing oneself on the guidelines there are certain aspects of the guidelines that specifically distinguish between the restriction which is being considered for exemption and the agreement in which it finds its place. I can't now remember off the top of my head, it is in our skeleton, but I think it comes under proportionality.

MR JUSTICE BARLING: When it is talking here about the link between the agreement and the claimed efficiencies and what is the value, that is in paragraph 50.

MR HOSKINS: Yes.

MR JUSTICE BARLING: Are you reserving your right to argue that it is --

MR HOSKINS: I am, because actually, if it is not clear already, I will spell it out now. What we are going to say is what you see when you track through what the Commission has been doing is that rather than slavishly applying this 101(3) framework to establishing an acceptable level for MIF, what the Commission has done is to apply a proxy and that's what it did in the Visa 2 decision by using a cost-based proxy and that's what it also did when it came to start using the MIF. I will take you to those paragraphs in the opening. But

just so you get the point, is it common ground? We are not necessarily putting our case saying you have to tick all the 101(3)s, we are saying if the proxy is good enough for the Commission, it is good enough for the Tribunal.

I'm sorry that's probably unhelpful but at least it clarifies my position.

MR JUSTICE BARLING: No, it is good to know.

MR BREALEY: To a certain extent, if it is not common ground then it is understandable why they have gone wrong because if one looks at paragraph 232 of the CJEU, if we can go to that --

MR JUSTICE BARLING: Same bundle?

MR BREALEY: It is, I think it is tab 19.

MR JUSTICE BARLING: Yes. Paragraph?

MR BREALEY: 232.

MR JUSTICE BARLING: Yes.

MR BREALEY: Actually 231.

MR JUSTICE BARLING: Yes.

MR BREALEY: I didn't go to the court yesterday, I went to the Commission where it said that you have got to look at the MIF, I went to the General Court which says you have to look at the MIF, I didn't go to the CJEU, but here we get it:

"By contrast, where it is established that such

a decision [this is the MIF] is not objectively necessary to the implementation of a given operation or activity, only the objective advantages resulting specifically from that decision [and the decision is the decision to set the MIF] may be taken into account in the context of article 81(3).

"In the present case, as is apparent from paragraph 78 to 121 of the present judgment, it was open to the General Court to find in paragraph 120 of the judgment under appeal, without erring in law, that the MIF was not objectively necessary for the operation of the MasterCard scheme. In the light of that conclusion, the General Court also concluded that in the analysis of the first condition laid down in article 181(3) called for an examination of the appreciable objective advantages arising specifically from the MIF and not from the MasterCard system as a whole. It follows from this that the argument the General Court wrongly ignored the advantages to cardholders resulting from the MasterCard scheme cannot be accepted."

It could not be clearer, in the Commission's decision, in the General Court and the CJEU -- and Mr Spitz reminds me at paragraph 194 of MasterCard's skeleton:

"First condition, efficiency gains, this calls for

an examination of the appreciable objective advantages arising specifically from the MIF and not from the MasterCard system as a whole."

So if that is the submission that's being made we can see why they have gone wrong and why I thought it was common ground.

So I was at paragraph 51 of the guidelines:

"All efficiency claims must be therefore substantiated."

I went through the (a),(b),(c) and (d). Again, we have set out in our written submissions how these four conditions, the nature, the link, the likelihood and the how and when, apply to Dr Niels' methodologies. So that is the first condition and obviously, I will come back to this in closing, but this in opening is what we say on the first condition.

On the second condition, which MasterCard refer to in their skeleton, this is at paragraph 85, the second condition of article 81(3) "fair share for consumers", so paragraph 83:

"According to the second condition, consumers must receive a fair share of the efficiencies generated by the restrictive agreement."

Then paragraph or recital 85 is important:

"The concept of fair share implies that the pass-on

of benefits must at least compensate consumers for any actual or likely negative impact caused to them by the restriction of competition found under article 81(1)."

So, again, we don't see the agreement. It is the restriction of competition:

"In line with the overall objective of article 101 to prevent anti-competitive agreements", this is paragraph 85, MasterCard referred to in their skeleton:

"To prevent anti-competitive agreements, the net effect of the agreement must at least be neutral from the point of view of those consumers directly or likely affected by the agreement. If such consumers are worse off following the agreement, the second condition of article 81(3) is not fulfilled."

What is the relevance of that, is that you look at the acquiring market, you look at the acquirers and merchants and having looked at the benefits under the first condition, if it is decided that the merchants are no worse off because of the benefits, then you can have an exemption. If it is concluded that the merchants are worse off, you can't have an exemption.

So this is important, I will just say it again, in line with the overall objective of article 81 to prevent anti-competitive agreements, the net effect of the agreement, that is the anti-competitive agreement, must

at least be neutral from the point of those merchants directly affected by the anti-competitive agreement.

Again, in line with the overall objective of article 101, to prevent an anti-competitive MIF, the net effect of the anti-competitive MIF must at least be neutral from the point of view of those merchants directly affected by the anti-competitive MIF.

That is all I need to say on the relevant legal principles. They are set out in the guidelines, referred to by MasterCard and I move and I will just summarise it from the opening, my Lord.

So if I go to paragraph 177 of the opening.

MR JUSTICE BARLING: Yes.

MR BREALEY: We set out here in summary form, because really there are bundles and bundles and bundles which are relevant to this, how the European Union came to adopt the MIT MIF.

The central efficiency claim, this is 177, advanced by MasterCard during the investigation, prior to the MasterCard infringement decision was that the MIF helped MasterCard to maximise output by balancing cardholders' and merchants' demand. The balance was to skew payments of the issuers' costs of the scheme onto the merchant. This is the same central efficiency claim advanced by Dr Niels in the present proceedings and here we set out

why, just four reasons -- I mean just four reasons -- why the Commission became very concerned by this line of argument.

So why did the Commission become concerned by this balancing argument? First, the basis upon which MasterCard set the EEA MIF was unclear and appeared rather arbitrary. Again, the point I just made about having this free rein. It became apparent during the investigation that the MIF was not actually set to allocate any specific costs.

As they state, the MIF is set for a host of reasons, eg to compete with Visa. Then what is in quotes, MasterCard have blued out as it were, but obviously the Tribunal can read it.

The Commission in the MasterCard infringement decision noticed that MasterCard had disavowed that the MIF was a fee for a service and was clearly concerned at the circularity of requiring merchants to pay a significant proportion of the MasterCard scheme costs.

So the issuers want to give free holidays to cardholders in Berlin, how are we going to do that? Well, let's get the money from the merchants and then it is said: well, we need the money from the merchants in order to get the free holidays for Berlin and the whole thing becomes circular.

So the first reason the Commissioner became very concerned was because of the lack of any seemingly objective criteria to test the exemption. The second reason why the Commission became very concerned was that MasterCard had taken a simplistic view of the imbalance between the issuing and the acquiring side. As we saw yesterday, the Commission noted that MasterCard ignored the fact that in the UK, issuing banks generated 90% of their revenue from a credit card with income from cardholders mainly interest and only 10% from interchange fees and the Commission considered that any analysis of an imbalance had to comprise analysis of revenue as well as costs.

We saw yesterday the General Court agreed, noting at paragraphs 101(6) and 101(8):

"... the substantial revenue issuing banks receive from payment cards and stating that such revenue could not be admitted from MasterCard's analysis."

That's another reason why the Commission became very concerned about the way that MasterCard was calculating its issuers' costs based MIF.

The third reason, the Commission was concerned that MasterCard had not, in its article 101(3) analysis, properly focused on the acquiring market. When one reads the CJEU judgment and the General Court judgment

you see MasterCard and the intervening banks arguing that when one is looking at benefits, merchants and cardholders, although merchants may not receive any benefit, if cardholders get the benefit, that is sufficient. So they were saying: look at it in the round, if cardholders are getting benefits, that is a good thing for the purposes of article 101(3) and the European Court and the General Court and the Commission has said: no, you have got to focus on the acquiring market.

They rejected the submission that cardholder benefits could of themselves be sufficient to compensate the merchants. Lastly, and this is something that will crop up time and time again, I flagged it yesterday, the Commission was not persuaded of the many efficiencies claimed by MasterCard. For example, the Commission did not consider that the free funding period was an efficiency gain within the meaning of 101(3). It referred to footnote 44 of the Visa decision, where it had doubted whether a free funding period was a legitimate consideration in the case of the MIF. We saw that almost within the first hour yesterday. And this issue of free funding has arisen time and time again. It has been rejected time and time again and yet MasterCard are still, with Dr Niels'

methodology, his first methodology, pursuing the same point.

The next heading is "Discussions post-MasterCard infringement". There is quite a lot of blue here but I do want to -- so we have set the scene because -- so we had MasterCard calculated its MIF, it is subject to the infringement decision in 2007, as we know, it then went into a dialogue with the Commission about what to do. We know that in the two-year period from 2007 to 2009 it was in a dialogue and in the end gave undertakings to the Commission to reduce the credit card MIF to 0.3%.

This section is trying to tease out at least some of the documents that have been disclosed to us as to what happened but it is quite important to go to paragraph 189. I can't, as I understand it -- actually, I do not know why this is confidential and at some point we may have to deal with it.

MR JUSTICE BARLING: I'm sorry, I'm still working from the one that we originally had.

MR BREALEY: So paragraph 189 in a skeleton that I got a few days ago is blued out.

MR JUSTICE BARLING: Yes.

MR BREALEY: But I would like to take the Tribunal to it. So this is --

MR JUSTICE BARLING: Is it something that needs to be, or is it something that's just been --

MR HOSKINS: I will have to take instructions on that. If we want to go into that of course we can --

MR JUSTICE BARLING: I don't know to what extent Mr Brealey wants to -- if he feels --

MR HOSKINS: I'm not able to deal with it without taking proper instructions.

MR JUSTICE BARLING: Sure. No, I understand that.

MR BREALEY: Maybe I can take the Tribunal to it and then Mr Hoskins over lunch can take instructions, but I would like at least to show the Tribunal the document.

MR JUSTICE BARLING: Yes. I think if you are going to show us the document to make any points about it, you are probably going to be trespassing on areas that have been blued, aren't you? So we will either need to decide whether to go into camera or --

MR BREALEY: I do apologise. Can we go into camera?

MR JUSTICE BARLING: Well, I mean that's the shorter -- I don't know maybe -- there are so many people here, there are so many people on the list, as it were, I'm just conscious we haven't got an order in place at the moment anyway, have we?

MR BREALEY: No.

MR JUSTICE BARLING: Even for those who are likely to be

listed and give undertakings in the form of the proposed order that we are slightly in a limbo position at the moment unfortunately.

MR BREALEY: We will sort out the undertakings over lunch, hopefully.

MR JUSTICE BARLING: Do you want us to read something over lunch that would make it easier for you to --

MR BREALEY: Personally I would just like to take the Tribunal to it and then you can read it over lunch but just --

MR JUSTICE BARLING: Well, why not do that?

MR BREALEY: Just to flag the -- yes.

So I'm dealing with paragraph 189.

MR JUSTICE BARLING: Yes.

MR BREALEY: I would like to go to the document but I will ask the Tribunal to note the last line of 189.

MR JUSTICE BARLING: Yes.

MR BREALEY: I think it should be fairly obvious -- so if I just go to the -- so the document actually is at E3.5.

MR JUSTICE BARLING: Yes.

MR BREALEY: E3.5 at tab 101. I only wanted --

MR JUSTICE BARLING: Yes?

MR BREALEY: So one sees this paper, one sees the author on the top left.

MR JUSTICE BARLING: Yes.

MR BREALEY: We have seen that before. We see the subject matter. I can make this point, we know that the tourist test is called the MIT.

MR JUSTICE BARLING: Yes, it is another name for the MIT.

MR BREALEY: Paragraph 18, we see the ultimate calculation at the bottom.

MR JUSTICE BARLING: Yes.

MR BREALEY: The credit cards.

MR JUSTICE BARLING: That's the same as referred to in --

MR BREALEY: It is.

MR JUSTICE BARLING: -- your skeleton.

MR BREALEY: I'm told that the document itself is not blued out, but that may be a mistake. If they blued it out in the skeleton, they may actually --

MR JUSTICE BARLING: We better assume at the moment and you can iron it out maybe with Mr Hoskins over lunch.

MR BREALEY: One sees in paragraph 18 the percentage, the last bullet point. We see at paragraph 16 that some -- a study of a member state has been excluded. We see in footnote 225 of our skeleton where Mr von Hinten-Reed recalculates the percentage if you include that state and you see three lines from the bottom of footnote 225, the resulting percentage.

MR JUSTICE BARLING: Yes. You see what difference it makes, yes.

MR BREALEY: This is in the context of me just making a submission that in these proceedings, MasterCard have not come to the Tribunal with a MIT test applied but one can see that when they did it what calculation it was and how that clearly then led to the undertakings.

It is slightly truncated, but it is actually quite an important point which I can't not make just because it has been blued out.

So that is the importance of 189. Just to go back to -- one remembers the table, table 8.2, of Mr von Hinten-Reed's second report. That's at D2.1. Page 551 of the bundle. Internal 128. We saw this yesterday. This is based on MasterCard's own calculations, all that Mr von Hinten-Reed has brought it together. We saw yesterday that -- so we know what the calculation is on Mr von Hinten-Reed applying the MIT MIF, that is 0.15, you can round that up to 0.2.

We know what applying the MIT MIF by MasterCard has been, I won't disclose it until he takes instructions, but it is in paragraph 189 of our written submissions and it is a certain percentage if you exclude that member state and it is another percentage if you include that member state. That is a similar calculation to the one performed by Mr von Hinten-Reed.

We know that if you take Dr Niels' cost methodology,

one hits 0.2% for reduction in transaction costs and a bit of fraud costs. I will ask the Tribunal to draw its own conclusions from all the percentages. It is only when you add this humongous percentage for credit write-offs, collection departments and funding costs you then go off the scale.

That's all I wanted to emphasise on the discussions post-MasterCard infringement. I will speed up a little bit because I have obviously got pass-on to do this afternoon. Hopefully I will finish this before lunch.

Paragraph 194 of the written opening. Again, I don't think there's anything controversial about it. MasterCard may not like the MIT MIF test but clearly there are sufficient documents out there which explain why the MIT MIF may satisfy the exemption conditions of article 101(3) and we set out at 194, 195, 196 even in the interchange fee regulation, so again, the interchange fee regulation, 197, say:

"The caps in this regulation are based on the so-called merchant indifferent test developed in economic literature which identifies the fee level a merchant would be willing to pay if the merchant were to compare the cost of the customers' use of a payment card with those of non-card cash payments. It thereby stimulates the use of efficient payment instruments

through the promotion of those cards that provide higher transaction benefits while at the same time preventing disproportionate merchant fees."

So we have seen the European Commission in its investigations, the undertakings, the commitments applying this merchant indifferent test. We have seen at the highest European level the Council and the Parliament adopting the interchange fee regulation saying that the MIT MIF is the one that creates the efficiencies and prevents "disproportionate merchants' fees".

The next main heading starts at paragraph 200. I am sure that Mr von Hinten-Reed will be cross-examined on this but in section 11 of his first report he sets out how he has calculated the MIT MIF. I don't need to go through that now.

I will finish just by highlighting what MasterCard has done, which starts at 207. We make the point and I have already made it, that there is no expert justification of any calculation actually used. Instead, Dr Niels takes the level that MasterCard fixed and then says: hey, you know what, if I adopt these two methodologies, two different methodologies, they both support the actual level that MasterCard reached.

I have set them out at paragraph 211. The

methodologies are the adjusted benefit cost balancing approach and then the adjusted MIT approach, which as I have already said, is not MIT at all.

We have at 212 onwards set out why we have a difficulty with this adjusted benefit cost balancing approach. In 216 and 217 essentially I'm picking up on -- these figures are, I think, confidential, but I'm picking up on the table 8.1 and 8.2 that we have seen. Then the big point, the big points are not the transactional costs or the fraud costs. The big point is the heading over paragraph 218, where Dr Niels/MasterCard revisit, come back to the notion that merchants should be bearing a huge proportion of the credit costs.

We set out from 218 all the way to 231, again, this will have to be done in cross-examination, but here we are at least giving MasterCard some notice of the criticisms we have of the approach. (a) we say the approach is misconceived to begin with but the actual evidence that is adduced to the Tribunal doesn't begin to satisfy the nature of the claimed efficiencies, the link, the likelihood, how and when which we have seen in the guidelines.

Again, we saw in the Commission decision yesterday that annex 6, right at the end of annex 6,

the Commission saying that that report that had been commissioned failed to show any link between the MIF and the claimed efficiencies. But here we try and set out some of our criticisms on this discredited cost issuers approach and then, lastly, at 233, we try and make some sense -- and I have to confess, it is quite heavy reading in Dr Niels' report -- this adjusted MIT approach, where -- again, you can almost do anything in order to get to the level that you want to. Really in this approach, what is called the adjusted MIT approach, Dr Niels is really making so many adjustments that, in the end, I think, although I can and will ultimately make the forensic point that the adjustments are simply going there to justify this level, he makes a serious -- not a serious -- a mistake -- he makes a major adjustment from the Commission's, Deloitte's report, this is paragraph 236, where he just takes out of the survey a massive section of merchants. So as I flagged, the Commission has looked at the cost of cash, the card, big survey, what does Dr Niels do? He kind of wipes out a lot of the merchants, and lo and behold, if you wipe out these merchants, the MIF goes up. He then, again, comes back to this: well, merchants have got to pay for the cost of credit. This time he is not doing it by reference to the issuers' cost, he is doing it by

reference to the cost of funding and in particular, Amex.

Again, we will have to work out this in cross-examination, but I do make the point in paragraph 250, which is the conclusion on the adjusted MIT MIF. The adjusted MIT MIF is not a MIT at all given the adjustments. In particular, the move away from a card/cash comparison to a comparison that incorporates other card payments, and I stand by this, there is undoubtedly something Kafkaesque about adjusting the MIT MIF to impose on merchants who accept MasterCard a cost based on accepting the more expensive Amex card that has limited acceptability. Article 101(3) is concerned with ensuring that consumers receive a fair share of any efficiency gains, it is not in the business of imposing costs on consumers by reference to the most expensive product in the market.

We say it is not surprising in the least that so far as we know, this adjusted MIT MIF, which takes Amex as a comparator, as far as we know, has never been advanced in any investigation at all and certainly not the one that has been adopted by the EU in the interchange fee regulation.

MR JUSTICE BARLING: Is that a neat moment?

MR BREALEY: It is, my Lord. Yes.

MR JUSTICE BARLING: You are going to have a look at the -- it would be helpful also, as it is related to the confidentiality issue, if we could sort of -- I don't know whether people have had a chance to take a view yet on how we might take the order forward?

MR BREALEY: We will sit down at lunch and at 2 o'clock -- I will have a word with Mr Hoskins as well.

MR JUSTICE BARLING: Because obviously the point that has just arisen on paragraph 189 shows that we need to put something in place, don't we? Good.

(1.00 pm)

(The short adjournment)

(2.00 pm)

MR SMITH: Mr Brealey, before you begin it occurred to us that it might be helpful to have a short reading list dealing with the scheme as it operated insofar as the documents in the E files, things like the scheme rules, the policy documents and the notification of the MIF from time to time by MasterCard to its banks, just so that we could familiarise ourselves with the way it all works.

MR BREALEY: Yes, how the scheme works.

What I was going to do is go to section E. We have done exemption, the overcharge section I think speaks for itself. The figures are in yellow. Before I get to

pass-on, which is section E, as I understand it, my Lord, the parties have agreed the confidentiality order.

MR JUSTICE BARLING: Good.

MR BREALEY: I guess we will be signing those.

MR JUSTICE BARLING: Have you managed to cull off the numbers somewhat?

MR BREALEY: We have culled the numbers, a little bit.

MR JUSTICE BARLING: We will need written undertakings, won't, from them, in that form? I think it is a slightly different form, isn't it, to the form that the undertakings in the High Court?

MR BREALEY: We will certainly sign them, yes.

MR JUSTICE BARLING: Right.

MR BREALEY: There is an issue, I have just spoken to Mr Hoskins, about that document that I was referring to. I haven't kind of worked it through yet, he has explained it to me. Although it is not marked blue in the file and we may want to look at other documents in that file which are not marked blue, the reason that MasterCard want to keep it confidential --

MR HOSKINS: Can I explain this?

MR BREALEY: Is because it is part of negotiations with the Commission, and although those negotiations have finished, they don't want to set a precedent. I'm not

actually objecting at the moment, but Mr Hoskins can articulate it, but that's what he told me, that it is part of a process of negotiations. Although those negotiations have finished, because obviously they entered into the 2009 undertakings, it is a point of principle and I haven't actually had time just to think whether that's a valid reason or not.

MR JUSTICE BARLING: You have got out of it what you sought?

MR BREALEY: Yes. I did it in a way which didn't disclose anything but you have got the --

MR JUSTICE BARLING: So we should mark that as still potentially confidential, the document?

MR HOSKINS: Please, we claim confidentiality in relation to it and obviously if Mr Brealey wants to object then we will have to deal with it. But please, at the moment, yes.

MR JUSTICE BARLING: You think there may be other documents in that same category --

MR BREALEY: Well I was just speaking to Ms Houghton, that whole file basically is negotiations and doesn't appear to be blue.

MR JUSTICE BARLING: Right, so we will treat that one with caution.

MR HOSKINS: We have been consistent because negotiations with the Commission, for example, in the witness

statements, confidentiality has been claimed, so if it has not been done it is an oversight rather than us suddenly going: ah. There is an inconsistency on our part, so I'm grateful to Mr Brealey for raising it.

MR BREALEY: The fascinating principle of pass-on, which is at section E.

Really a lot of this is confidential but confidential to Sainsbury's. So when you look at section E in the colour-coded version, a lot of it is in yellow because it relates to how Sainsbury's does business. So I'm not proposing to go through that orally today. It is only an opening, clearly we will have to do something in closing and there will have to be cross-examination probably in camera.

What I would like to do though, because I think it is fundamentally important as to how the Tribunal deals with pass-on is there are very important legal considerations which govern the pass-on defence. So it is not just a question of Dr Niels or indeed for that matter Mr von Hinten-Reed just coming to court and saying, as an economist, in my view, it is passed on. Obviously they can say that and the Tribunal will take it as evidence.

But my purpose to put forward Sainsbury's case is to ensure that the expert evidence is still confined to the

legal principles because the legal principles on pass-on are quite important, and if one compares our written opening with that of MasterCard's written opening, you will see immediately that we are relying on EU law because we say that EU law dictates the conditions for the pass-on defence. So there are EU law considerations to how the Tribunal interprets the pass-on defence.

In other words, the economists -- maybe Dr Niels has tried to confine his evidence within these legal principles, I will have to find that out, but as I say, it is very important to realise that this pass-on defence is just not a free for all. There are legal considerations.

MR JUSTICE BARLING: A lot of the cases deal with sort of reimbursement of charges unlawfully levied, don't they, contrary to community rules.

MR BREALEY: And that's what I'm going to go through. I need to take it in stages and what I would like to do, in section E, paragraphs 268, 269, 270, 271, we set out the introduction to pass-on. 270 is coloured yellow. I won't read that out. That is what we say happens in the real world.

I kick off at 272 with the law on pass-on. In my submission, this is extremely important because, as I say, it governs how the Tribunal should accept the

economic evidence.

The first case and we need to go to tab 14 of authorities. The authorities tab 14 which is the case of Courage v Crehan. It is the I -- I just have authorities --

MR HOSKINS: I4?

MR BREALEY: It is I4, is it?

MR HOSKINS: Yes.

MR BREALEY: Sorry. I read it as 14, so it is I4, tab 5. I can't believe it was 1999 when the Court of Appeal made the reference, and it is my birthday today.

MR JUSTICE BARLING: 29 again.

MR BREALEY: 16th July 1999, made the reference. I will go through some of the passages in Courage v Crehan, my Lord knows it extremely well. It was Mr Crehan suing Courage for the operation of the beer tie and one of the questions was whether -- it goes to the ex turpi causa point as well, but whether Mr Crehan could claim damages.

What I want to get out of this -- we will go through the paragraphs -- there are two things I get out of this. The first is that the right to claim damages is a right afforded under EU law.

That achieves a policy objective of the treaty, which is to enforce the competition rules. So the

European Court says the right to claim damages achieves this policy objective of private enforcement.

So that is the first thing. The second thing is that it is not often recognised, but clearly the Court of Justice, as it was, recognised that, as a matter of national law, there could be a pass-on defence.

It is not often recognised, and I will show you the passage, but I think it is clear that when the European Court refers to the Hans Just case, it was recognising the pass-on defence.

So we can pick it up and, again, I apologise if, my Lord, we are going through old ground, but paragraph 25:

"As regards the possibility of seeking compensation for loss caused by a contract or conduct liable to restrict or distort competition, it should be remembered from the outset that, in accordance with settled case law, the national courts whose task it is to apply the provisions of community law in areas within their jurisdiction must ensure that those rules take full effect and must protect the rights which they confer on individuals."

So it is the subjective rights of individuals, the direct effect. We see this in the tax cases a bit later on. 26:

"The full effectiveness of article 85, now 101, and in particular, the practical effect of the prohibition laid down in 101 would be put at risk if it were not open to any individual to claim damages for loss caused to him by a contract or conduct liable to restrict or distort competition."

This is the policy bit:

"Indeed, the existence of such a right strengthens the working of the community competition rules and discourages agreements or practices which are frequently covert, which are liable to restrict or distort competition. From that point of view, actions for damages for the national courts can make a significant contribution to the maintenance of effective competition in the community."

Then they go on in 28 to deal with the issue in hand, which was the application of the Tinsley v Milligan, the absolute bar, the ex turpi causa, there can't be any absolute bar to the claim for damages.

But those paragraphs are informing the Tribunal that the right to claim damages is a right afforded under community law. The right to claim damages is a correlative right of the principle of direct effect, and this right to claim damages strengthens the private enforcement of the competition rules. So there is

a policy reason behind this right to claim damages.

We then go to 29, to the standard condition. So it is in the absence of community rules, it is for national rules to satisfy or to govern how the right to claim damages is made and we see there that the standard conditions, the principle of equivalence and the principle of effectiveness, which we see time and time again.

Then, the second point that I want to get out of Courage v Crehan is paragraph 30. So having said there is a right to claim damages which strengthens the private enforcement of the competition rules, the court says:

"In that regard, the court has held that community law does not prevent national courts [in other words, does not prevent national law] from taking steps to ensure that the protection of the rights guaranteed by community law does not entail the unjust enrichment of those who enjoy it."

See those cases. One of which, which is the famous Hans Just case which essentially kicked off the unjust enrichment, the passing-on defence we will see in a moment in the tax area.

So the reason I draw the Tribunal's attention to this, first, we see that the right to claim damages is

a policy right; it strengthens the enforcement of competition law, but similarly, it doesn't prevent national law from laying down a passing-on defence. So community law is not providing for a passing-on defence, it is just saying that in the absence of harmonisation, if national law does provide for a passing-on defence, we will allow it and then I shall come on in a moment, we will allow it, subject to certain conditions.

So that is the nature of Sainsbury's claim to claim damages. It is very, very important right as a matter of community law, but if MasterCard want to rely on a national domestic English UK law, Scottish law, which allows for pass-on, then community law, EU law will allow it.

That's what I get from paragraph 30. So if we then go to the Hans Just case, which is referred to in paragraph 30, which is at tab 2. So what is the Court of Justice -- what does it mean when it is referring to the principle of unjust enrichment and the reference to Hans Just?

Well, if we go to tab 2, paragraph 26. I don't think the facts matter, it is just the principles that are important. So my Lord is right, this is obviously a tax case. It is the trader seeking restitution of an unlawful tax and then the government saying: well,

you haven't suffered any loss, you will be unjustly enriched if you double recovered. Paragraph 26:

"It should be specified in this connection that the protection of rights guaranteed in the matter by community law does not require an order for the recovery of charges improperly made to be granted in conditions which would involve the unjust enrichment of those entitled. There is nothing, therefore, from the point of view of community law to prevent national courts, national law, from taking account in accordance with their national law of the fact that it has been possible for charges unduly levied to be incorporated in the prices of the undertaking liable for the charge and to be passed on to the purchasers."

Again, just to nail the point, in Courage v Crehan, having said you have this right to claim damages, when paragraph 30 refers to the unjust enrichment and paragraph 26, so it refers to paragraph 26 of Hans Just, you could almost read that paragraph as a further paragraph in Courage v Crehan. In other words, you have a right to claim damages under community law, but is subject to any national pass-on defence. So that is Hans Just.

I will just go through the cases in the opening submissions. The next one is San Giorgio. Again,

my Lord and the Tribunal will know it is a famous case, San Giorgio. I will just go to the relevant paragraphs. Paragraphs 13 -- San Giorgio is tab 3, paragraphs 13 to 15. Page 72 of this bundle. At the bottom. So again, another tax case but the court says:

"However, as the court has also recognised in previous decisions and in particular, in Hans Just, community law does not prevent a national legal system [so a national legal system] from disallowing the repayment of charges which have been unduly levied where to do so would entail unjust enrichment of the recipient. There is nothing in community law therefore to prevent courts from taking account under their national law of the fact that the unduly levied charge has been incorporated in the price of the goods and thus passed onto the purchasers. Thus national legislative provisions which prevent the reimbursement of taxes, charges and duties levied in breach of community law cannot be regarded as contrary to community law where it is established that the person required to pay such charges has actually passed them on to the persons.

"On the other hand, any requirement of proof which has the effect of making it virtually impossible or excessively difficult to secure the repayment of charges levied contrary to community law would be incompatible

with community law. That is so particularly in the case of presumptions or rules of evidence intended to place upon the taxpayer the burden of establishing that the charges unduly paid have not been passed on to other persons or special limitations concerning the form of evidence to be adduced.

"Once it is established that the levying of the charge is incompatible with community law, the court [the Tribunal] must be free to decide whether or not the burden of the charge has been passed on wholly or in part to other persons."

So important points of principle here. I emphasise paragraph 15:

"In a market economy based on freedom of competition, the question whether, and if so, to what extent, a fiscal charge [here we would say the MIF, the overcharge] on an importer [here we would say Sainsbury's] actually passed on in subsequent transactions involves a degree of uncertainty for which the person obliged to pay a charge, contrary to community law [ie Sainsbury's] cannot be held systematically held responsible."

So it is recognising to a certain extent that it is difficult to prove pass-on and that shouldn't operate to the disadvantage of the person who has paid it and we

will see this theme is developed by the court subsequently.

That is San Giorgio. Comateb, tab 4. If we can pick this up, so at page 87 of the bundle. Actually sorry, page 88 of the bundle, paragraph 17:

"The French government and the Commission contend that the legal obligation to incorporate the charge in the cost price does not mean that traders are required to pass it on to purchasers."

So there was a French law which required the charge (inaudible) to be incorporated in the cost price:

"Traders can always take the commercial decision to absorb the charge in whole or in part and thus eliminate its effect on the sale price. In view of the French government and the Commission, a legal obligation to incorporate the charge in the cost price is irrelevant as regards the case law of the court concerning recovery of sums not due. Consequently it is necessary to determine in each case whether or not the disputed charge is actually being passed on".

I emphasise this, just pausing here: The Court of Justice, the CJEU, emphasises time and time again that it is in each case, specific to each case.

Paragraph 22:

"In such circumstances, the burden of the charge

levied but not due has been borne not by the trader but by the purchaser to whom the cost has been passed on. Therefore, to repay the trader the amount of the charge already received from the purchaser would be tantamount to paying him twice over, which may be described as unjust enrichment, whilst in no way remedying the consequence for the purchaser of the illegality of the charge."

23, important:

"It is accordingly for the national court to determine in the light of the facts in each case, whether the burden of the charge has been transferred in whole or in part by the trader. In this respect it should be made clear first, that if the final consumer is able to ...(Reading to the words)... that trader must in turn be able to obtain reimbursement from the national authorities."

For the transcript, I know I'm wobbling on a bit, it is paragraph 24.

25, three lines down:

"It cannot generally be assumed that the charge is actually passed on in every case.

"The actual passing on of such taxes, either in whole or in part, depends on the various factors in each commercial transaction which distinguish it from other

transactions in other contexts. Consequently, the question whether an indirect tax has or has not been passed on in each case is a question of fact to be determined by the national court which may freely assess the evidence.

"However, in the case of indirect taxes, it may not be assumed that there is a presumption that they have been passed on and that it is for the taxpayer to prove the contrary."

It is very important when one sees the reports of Mr Greg Harman and Dr Niels on pass-on, they refer to all sorts of presumptions. It is very important to put them in their context and they don't take such evidential weight that somehow it is for Sainsbury's to dispute pass-on.

I will continue. I have three more cases on this. We have to be very, very careful about presumption, even in the case of indirect taxes.

Weber's Wine is at tab 6. This was essentially a duty on beverages. This is concerning a duty on beverages. If we can pick it up at paragraph 51. I appreciate it is a bit small but it is at page 119. Paragraph 51, we are talking about a duty on alcoholic beverages:

"In the present case, the claimants in the main

proceedings contend that they themselves bore the duty on the alcoholic beverages. In that regard, although it is true in principle that the duty on alcoholic beverages must be borne by the final consumer because the law provides that it is only to be passed on, in practice, however, for reasons relating to competition, it is only in rare cases that Austrian undertakings are able to pass the duty on to the consumer. In most cases the duty reduces the profit margin of the undertaking liable for the duty and is therefore de facto borne by the undertaking. Statistical studies show that in Europe, the Republic of Austria is the state in which beverages bear the highest duty."

54, last sentence:

"The great majority of undertakings including the claimants in the main proceedings do not pass the duty on to the final customers."

55:

"In 1994, virtually all Austrian catering undertakings made a loss. Their situation has continued to deteriorate. Since then those undertakings have been constantly overburdened with debt, owing to competitive pressures and the need to respond to the demands of the market. The claimants in the main proceedings also state [so this is what they are saying] in November 2000

the Austrian Institute for Economic Research carried out a micro economic study into the question of passing on the costs of the duty. The study did not make it possible to provide general answers to the question of the passing on of the duty. It contains no specific answers to the question."

This is everything that they are submitting. But one sees here that they are looking at the conditions of competition, even though this is a tax on alcoholic beverages. This is not what the court is saying, this is what they are submitting. 57:

"Accordingly, according to the claimants, the question of unjust enrichment can only be answered on a case by case basis following a specific investigation."

So that's what they say, and that is essentially endorsed by the court, so we can pick this up at paragraph 93. Remembering the right to claim damages is a right afforded under community law, EU law, the right to restitution is a right afforded under EU law. This is on the passing-on defence:

"The relationship between the passing-on of the duty on alcoholic beverages and unjust enrichment."

Paragraph 93:

"The court has consistently held that individuals

are entitled to obtain repayment of charges levied in a member state in breach of community provisions. That right is the consequence ...(Reading to the words)... to repay charges levied in breach of community law."

Just pausing there. The same applies to the present case. You have a right to claim damages under 101 and there has to be some sort of repayment:

"According to the case law, there is only one exception to that obligation to make repayment: A member state may resist repayment to the trader of the charge levied, though not due, only where it is established by the national authorities that the charge has been borne in its entirety by someone other than the taxable person and that reimbursement of the charge would constitute unjust enrichment. It follows that if the burden of the charge has been passed on only in part, the national authorities are required to pay the amount not passed on."

Important, 95:

"As that exception is a restriction on a subjective right derived from the community legal order, it must be interpreted restrictively, taking into account particular of the fact that the passing on of the charge does not necessarily neutralise the economic effects of the tax on the taxable persons. Thus at paragraph 17

...(Reading to the words)... it cannot be generally assumed that a charge is actually passed on in every case. The actual passing on of such charges, either in whole or in part, depends on various factors in each commercial transaction which distinguish it from other transactions in other contexts. Consequently the question whether an indirect tax has or has not been passed on is a question of fact to be determined by the national court which is free to assess the evidence adduced before it.

"The court stated in Bianco that it is quite probable, depending on the nature of the market, that the charge has been passed on. However, the numerous factors which determine commercial strategy vary from one case to another, so it is virtually impossible to determine how they each affect the passing on of the charge."

Again, it is very fact specific, no general presumptions. I emphasise, we will come onto it in a moment, the court is saying that the defence of pass-on must be restrictively interpreted and applied. That is paragraph 95.

Then we get to Lady & Kid.

MR JUSTICE BARLING: Then he goes on in that case to go on about the volume effect, don't they?

MR BREALEY: The volume effect.

MR JUSTICE BARLING: I don't know whether you want us to note that in passing.

MR BREALEY: I know my Lord has it in mind, but clearly if you raise prices, yes.

MR JUSTICE BARLING: It crops up after that passage that you read.

MR BREALEY: Yes. It is recognised as a matter of EU law that if you have raised the price, you may have suffered an effect on volume and the economists have tried to agree the principles in this case apply that.

Lady & Kid and Accor are important -- Lady & Kid is at tab 9 -- because it gives context to this concept of restrictive interpretation.

I can pick this up at paragraph 16. Maybe if I can just ask the Tribunal to read 16 to 19 and then I will pick it up at 20.

16 to 19 is essentially -- sorry this is tab 9.

MR JUSTICE BARLING: Yes, I have it.

MR BREALEY: Lady & Kid. Tab 16.

MR JUSTICE BARLING: I'm just checking, I'm not reading the Advocate General's --I don't know whether it is included in the...

MR BREALEY: It is right at the back.

MR JUSTICE BARLING: It is. I am reading the Advocate

General --

MR HOSKINS: It is page 203 of the bundle.

MR JUSTICE BARLING: Yes. Page 203.

MR BREALEY: For the transcript, it is 16 and 17.

MR JUSTICE BARLING: Yes.

MR BREALEY: So paragraph 20 is a very important paragraph.

MR JUSTICE BARLING: Paragraph 20?

MR BREALEY: Yes:

"Nonetheless, since such a refusal of reimbursement of a tax levied on the sale of goods is a limitation of a subjective right derived from the legal order of the European Union, it must be interpreted narrowly. Accordingly, the direct passing on to the purchaser of the tax wrongly levied constitutes the sole exception to the right to reimbursement of tax levied in breach of European Union law."

What I'm starting to get from this and then we will see it from the next case, is that the pass-on defence is an exception to the right to claim damages. As such, it is interpreted narrowly, restrictively and the European Court has said that there has to be direct pass-on:

"The direct passing on to the purchaser constitutes the sole exception to the right to reimbursement."

It is emphasising you have to show direct pass-on.

If we go to the last case, Accor, at tab 10. Again, it's got the Advocate General at the beginning. So this is this 245 of the bundle, Accor.

Again, we get the same -- as the court always does -- rehearses the principles, paragraphs 70, 71, 72 and then 73, again, I emphasise:

"It is settled law that the disallowing of a repayment in such circumstances entails placing a limitation on a subjective right derived from the EU legal order. That restriction must be narrowly construed."

So, again, I come back to the right to claim damages is a right which is derived from the EU legal order. The pass-on defence must be narrowly construed, thus, it is apparent from paragraphs 20 and 25 of Lady & Kid that the only exception to the right to repayment of taxes, so the only exception to the right to claim damages, is in a case in which a charge that was not due has been directly passed on by the taxable person to the purchaser.

So when one is looking to see whether Sainsbury's has passed on the overcharge to its retail customers, that pass-on defence which MasterCard rely on must be interpreted narrowly, strictly and MasterCard must prove that there has been direct pass-on.

MR JUSTICE BARLING: Does that mean you have got to be able to show that it is reflected in the prices?

MR BREALEY: Directly in the prices. We will see this in the Hanover Shoe, the American case, where you have a cost plus. So if you have a cost plus model, whether you are an agent, whatever costs you have and you have a fixed margin, that you may see that you can see that there is direct pass-on because you have got your costs and you have your fixed margin and there is direct pass-on.

MR JUSTICE BARLING: So you are allowed to look at the aggregate margin -- I mean, Sainsbury's must have many tens or hundreds of thousands of lines, must they not, of product but you can -- you don't have to show -- you can look at it in a global sense, can you, or you can't look at it per transaction, obviously?

MR BREALEY: Certainly the first thing you have got to do is look to see how Sainsbury's would calculate its selling price and ascertain whether the interchange fee ever formed part of any consideration in setting a retail price.

So if -- again, I'm in slight difficulty --

MR JUSTICE BARLING: Blue area?

MR BREALEY: I'm in a yellow area actually, and it may well be that at some point we will have to clear the court so

we can have a proper discussion.

But if you could see that a buyer was to take the cost of goods, have the interchange fee and then add a fixed margin, I'm not saying it is inevitable but it looks more likely that if the cost of goods goes up or the interchange fee goes up and you have a fixed margin, there is direct pass-on. But in circumstances where the buyers who are responsible for pricing, are pricing, for example, by reference to the market, and do not have any interchange fee in mind at all, they are looking at cost of goods, they are looking at pricing in the market generally, it is impossible to say that a higher or lower interchange fee is being reflected into the retail prices because it is just not part of the equation.

I think that I would prefer to -- at some point I would like to have a fuller and franker discussion by reference to the facts, but again, I don't think it is giving anything away that in many, many businesses if there is an increase in cost -- so let's assume -- we have already said there's no direct correlation -- let's assume that there is an increase in the cost of something, is that going to be directly passed on into retail prices? The answer is well, it may depend on many, many factors.

MR JUSTICE BARLING: You might just advertise less or ...

MR BREALEY: You might absorb the cost, you might spend less on advertising, you might spend less on store labour. It can go, just as a general concept, an increase in cost can be absorbed in many ways: you reduce your advertising, you reduce your discretionary spend, you may make less profit.

If you take a really complex business and say a small amount of cost goes up, particularly when you are pricing by reference to the market, what's going to happen? And therefore -- I'm not saying this is Sainsbury's, for the record, we will have to have this debate --

MR HOSKINS: You have got a friend.

MR BREALEY: But it is -- in a complex -- where there are billions of costs involved, thousands upon thousands of product lines, labour costs, IT costs, logistical costs, where you add a tiny proportion of that cost, where is it going to directly feed into a higher retail price?

MR SMITH: I'm trying to get to what "directly" adds to the concept of passed on. I understand that you can't run the pass-on defence if you retain the cost yourself. Obviously you have retained the, in this case, tax, yourself. If you pass it on, does "direct" mean identifiably passed on or does it have a temporal element, meaning you passed it on quickly. What does

"directly" actually add to the passing on?
MR BREALEY: It is in contradistinction to -- I would say that if there is -- well, first of all, it means, I think, identifiable. So you have got to show an identifiable increase in a retail price as a result of an increase in an import price. It's got to be identifiable. Clearly identifiable, as in I just said, you know, a cost plus model.
Similarly in a cartel case you may -- the economist may come to court and say: well, on the Sunday there was a cartel, a spike in the wholesale price, and lo and behold, on a Monday there was an identical spike in the retail price. There's just a complete correlation between the two. And you would be able to say: well, I can see that has been directly passed on.
If, on the other hand, you can't identify in a cost plus or a spike and you are just saying: well, it goes into the mix and it may or may not have fed into prices, it could have gone in anywhere, in my submission, you don't satisfy this concept of direct pass-on.
MR SMITH: So, in essence, the more complicated the business, the greater the number of product lines you run, the harder it is to establish a pass-on defence?
MR BREALEY: Absolutely. Absolutely. If I have got one product and one raw material, and the price of that raw

material goes up, it may well be a lot easier to see, if there's that spike, the direct correlation between that cartel price and the higher input price.
But in circumstances where -- for example, let's assume in Sainsbury's there is a coffee cartel, and the coffee cartel increases the price of coffee by 5%, but you can't actually see that Sainsbury's has increased the price of coffee, so you say, well, where has that increase price gone? Sainsbury's have paid that little bit more to the cartelist in coffee, but where has it gone? We can't see it has gone in -- we don't see any direct correlation between the price of coffee going up, so where has it gone? If you say: well, I don't really know, it could go into all sorts of areas, you don't satisfy this strict condition of direct pass-on that's required by the court.
MR SMITH: Unless, presumably, looking globally at the figures you could show that Sainsbury's prices had increased across the board in a manner that matched exactly the price of this hypothetical coffee cartel that Sainsbury's had had to pay?
MR BREALEY: Maybe.
MR SMITH: Maybe?
MR BREALEY: Maybe. If you could show that prices had exactly matched the price of the increased wholesale

price, then, again, I say maybe because it is fact-specific. To a certain extent you are asking me to give generalisations. You have got to remember that if -- and I won't take -- but let's take any supermarket with all these product lines and you have got this relatively small, but we are here because it is important -- but a relatively small in the scheme of things where these retailers have billions of costs, billions of costs, and you are going to ask yourself the question, how has this manifested itself in retail prices? Because if you were to spread it across the board you are looking at fractions of a penny. Fractions of a penny. If you are a manufacturer of one product and you buy one raw material, it may well be that you can see that there has been direct pass-on, it is clear, but how is one going to determine there has been pass-on in fractions of a penny?
So you are absolutely right, and this is -- we will come onto it in a moment -- why the European -- sorry, the Supreme Court has held that it is so difficult to identify pass-on. That's why at the federal level it has prevented it, which I will come on to show.
If you come and you say, well, like in this case: I think they must have passed it on somehow but I'm not sure how, and I do accept it could have gone into the --

they may just have spent less on advertising or it could have gone into a little bit of lower/higher profit, you can't prove that direct pass-on.
We saw yesterday that passage that MasterCard relied on, which I -- where MasterCard referring to the Australian experience, submitted to the Commission:
"It shows clearly that there is no correlation between cost reductions, reduced merchant fees and retail prices. Indeed, retailers often take cost changes to their margin as there are many factors other than cost that influence their prices." So that is what they were saying about retailing business.
Then they relied on the OEC document:
"It is not possible to measure these price changes and their timing, particularly given other more significant changes in firms' costs and prices that are going on all the time."
That was MasterCard's view of the world back in whenever it was, 2006. So it is right, if the Tribunal accepts, which in my submission it should, that the defence of pass-on, because it is an exception to the right to claim damages which, as I say, is a policy objective and must be interpreted strictly, you are limited to showing direct pass-on, the more complicated the business, the more areas where that higher import

cost can go, being absorbed or in slightly lower profits, as I say, in less discretionary spend or whatever, a myriad of ways, then MasterCard can't prove direct pass-on.

MR SMITH: I know it is not this case, but I suppose what you are saying is that, in any case where there's a tax or it is a cartellised increase goes to the common costs of an undertaking, it is going to be very hard to establish pass-on, whether it be a cartel for the properties of supermarkets or an increase in corporation tax?

MR BREALEY: Yes. And I would say there is a really important policy behind that. Again, I come back to the right to claim damages is part of the private enforcement of competition law. So let's just take a step back and let's assume -- this is not -- I'm only assuming for the sake of the argument that MasterCard somehow show that Sainsbury's have passed on, or it is assumed -- let's assume that the Tribunal says I will have a general presumption, supermarkets, they are all very competitive, I'm going to look at the textbooks, when you get a competitive market there can be pass-on. So I'm going to apply this presumption. I am not actually going to look at the specifics, but I'm going to -- some sort of presumption.

So Sainsbury's doesn't, as the direct purchaser, have any cause of action because it has passed it on. Who is then going to sue MasterCard for damages. Remembering that any pass-on has resulted, at best, if you look across the board at retail prices, that all of us at some point may have been in Sainsbury's, in fractions of a penny. You are never, ever going to get an indirect purchaser claim, not even in a class action, because I am not going to go to court and claim 0.11p because I bought a Mars bar in Sainsbury's, let alone ten Mars bars or whatever.

MR JUSTICE BARLING: I suppose if your weekend shopping is £150 you might and you do it -- you might -- I might just get a class action up and running, I suppose.

MR BREALEY: You may do, but are you ever going to get the whole overcharge in fractions of a penny? Even if you were to accept that some people who had done a weekly shop could and they would have had to have kept all the invoices, all the receipts --

MR JUSTICE BARLING: It is a long shot.

MR BREALEY: It is a long shot. This is what the policy -- you know, there is an important policy point here and it is why the Supreme Court on the federal level banned -- and we have set it out in the skeleton -- why the federal court -- the Supreme Court on the federal level

said no pass-on defence (a) because of the complexity of it, and it is just going to increase the cost and (b) because the people who have got -- the indirect purchasers have got "a tiny stake" and are very unlikely to bring action.

I know there are some indirect purchasers, the Supreme Court in Canada allows indirect purchase claims but there is still a policy element that if you make the direct pass-on defence too lax, too liberal, so too easy for the cartelists to win on, then you are undermining the private enforcement of competition law.

MR SMITH: But subject to the point about it not being worth powder and shot for the indirect claim to be brought, if you have the potential for an indirect claim then the cartelist runs the risk of being forced to pay twice?

MR BREALEY: Well that's yet to be determined.

MR SMITH: That was really my question.

MR BREALEY: As you know, the Commission is quite vexed on this, wants cases to be brought together, if possible. Allowing indirect claims does cause procedural nightmares for defendants. I'm not saying -- I mean as you see from this skeleton, we have accepted that as a matter of national law, domestic law, it is open to MasterCard to run the pass-on defence which would mean that theoretically, long-stop, Sainsbury's customers

could bring some sort of action against MasterCard.

But all I'm saying is that the European Court has given a clear steer or a clear condition of strict interpretation and direct pass-on.

MR JUSTICE BARLING: I think all we are trying to do is get a handle on what is direct and what isn't direct within the case law. The case law is pretty clear. It is saying it has got to be directly passed on and that is easy in a sense, you can take an example, where there is your example of a cartel and let's raise prices by 10% and lo and behold the commodity goes up and you have got the spike and you can more or less equate the two.

Here, as far as I know, we are in a situation where there has always been a -- throughout the period of the claim, there has always been a MIF at about the level that you complain of and so we are not going to see any spikes.

PROFESSOR JOHN BEATH: We are in an equilibrium.

MR JUSTICE BARLING: We are in an equilibrium, yes. Exactly. So there might be evidence about -- I don't know what happened and I don't know whether there were any spikes and troughs in the UK MIF, I am afraid, or anything that could be pointed to, but absent that kind of thing, it is very difficult. Then you have got to compare it with the prices, the overall price --

Sainsbury's overall prices, presumably.
MR BREALEY: Certainly Mr Hoskins can cross-examine Mr Coupe and Mr Rogers about the lowering of interchange fees this year, that's a counterfactual. We say -- well again, I can't -- I'm yellowed.
MR JUSTICE BARLING: Yes.
MR BREALEY: But in answer to the direct point. Mr von Hinten-Reed goes through the pass-on and he refers to direct and indirect. Again, maybe it is for another day, but for a starter, that's where I would invite the Tribunal to go.
MR JUSTICE BARLING: To start. Yes.
MR BREALEY: To see what he as an economist regards as a direct pass-on.
MR JUSTICE BARLING: Because I mean all costs, if you have a business that's breaking even, all costs are obviously passed on, aren't they? So the interchange fee. Assuming Sainsbury's is a profit centre and all its costs, including the MIF, are going to be passed on.
MR BREALEY: All the costs are recovered but not necessarily all the overcharge will be passed on. That's what is clear from all the cases I have just cited. So one mustn't confuse recovering the costs, because otherwise you would only limit it to loss-making companies. So there is a fundamental difference between recovering

costs and passing on a spike. Why? Because, as I say, you can lose that increase in price in a multitude of ways.
So I might have -- just take Brealey Enterprises, I have a yearly annual lunch budget of £100 and the rent goes up by 50% and that's going to eat into my lunch budget. So I have reduced my cost. I have actually absorbed that increase in rent and spent less.
MR JUSTICE BARLING: Yes, but you are still --
MR BREALEY: Well, no, it is a bad analogy.
MR JUSTICE BARLING: I'm getting confused now with your lunches. Having an annual lunch budget of £100 --
MR BREALEY: Let's take a retail --
MR JUSTICE BARLING: Let's take a sweet shop that has got costs of £1,000.
MR BREALEY: And the sweet shop obviously buys its sweets, it re-sells them, but it has other costs and let's assume it has an advertising budget and it has an advertising budget of £100 per year. All of a sudden it finds that its rent has gone up by £10. You subsequently find out that that £10 was because of a cartel. So it has now paid £10 more.
MR JUSTICE BARLING: For its rent.
MR BREALEY: Yes. The cartelist landlord can't show that the prices of the sweets in the shop went up at all.

There is no spike, there's no nothing, they don't operate on a cost plus, but you find that actually rather than spending £100 in advertising, it spent £90. So it absorbs -- although it is still covering costs because it is still making -- let's assume it is making a profit, it has used -- it has reduced its discretionary spend --
MR JUSTICE BARLING: It is not a direct pass-on.
MR BREALEY: It is not a direct pass-on.
MR JUSTICE BARLING: You don't like the word pass-on, but it has recovered the £10 extra rent as part of its costs from its customers but it has not passed it on directly is what you are --
MR BREALEY: Correct. Or, I would say, at all. Put another way, let's assume the sweet shop --
MR JUSTICE BARLING: It has passed it on in a way, hasn't it, from its customers, including the £10.
MR BREALEY: Let's assume it has made -- rather than mess around with the advertising budget, let's assume that it just made £10 less profit, so rather than making £50, it has only made £40, and that £10 increase in rent, which is the cartellised overcharge has gone into lower profit. Now, again, the sweet shop is recovering all its costs. It's not making a loss, but --
MR JUSTICE BARLING: But if the sweet shop sets its profit

targets without reference to any of that, so it always makes the same profit, then you could say it will have passed it on?
PROFESSOR JOHN BEATH: Let's move into the next planning period, that the sweet shop discovers that its profits were less than it had expected to be. It might continue to simply carry on with a lower advertising budget but it may feel that there is a danger in that, in having reduced its -- longer term, having reduced its advertising budget, and so the way in which it can recover its existing -- get back on to its existing strategy, the only way it can do that by, in the next period, having a higher price for its sweets. So, in a sense, the pass-on can actually happen with a long delay.
MR BREALEY: And I would say --
PROFESSOR JOHN BEATH: But in fact if you really knew how the business process worked, you could in fact in a year's time or whenever the relevant planning arises, indeed discover that there was a relationship between the change in cost in the previous period and a price that was charged in the subsequent period.
MR BREALEY: And I that understand, but again, when it comes to direct, normally when you talk about direct it is something predominant. It's got to be the main cause.

And that's another point that when you are talking about in causation terms a direct cause is something which is a really important -- has an important causal link. So I do take the point but the longer the time period goes on, the more likely it is that other causes have also come into the equation.

PROFESSOR JOHN BEATH: It becomes just a big mess of trying to disentangle all these things that might have changed in that period of time.

MR BREALEY: Correct. And once you get into that situation, in my submission, you have failed this pass-on test.

MR SMITH: Just looking at an enterprise that is faced with an unavoidable increase in cost, one it has to pay, as I see it, it can do one of four things: It can make less profit or incur greater loss, or it can cut back on its discretionary spending, the yearly lunch fund gets reduced from £100 to £70, or it can reduce its costs by negotiating with its own suppliers and saying: look, I paid you £100 last year, I'm sorry it is going to be £70 this year or it can increase its own prices.

You are saying that heads 1, 2 and 3 cannot constitute pass-on.

MR BREALEY: Correct.

MR SMITH: Head 4 can, provided you meet the requisite standard of proof.

MR BREALEY: Correct, absolutely, and that is a brilliant way of putting it, in my respectful submission, and in the supermarket world and I don't think this is giving too much away, the number 3 is quite important.

You only have to take, well, I think it is Tescos, they were not dealing with their suppliers that well, cutting costs with their suppliers. But number 3 you can go back and say, you know: I want 5% off here. So you go back and you say: I want a reduction of 5% in what you are offering me. I would also say again it comes to this multitude thing. So you could have less profit, I might add a further one, which is quality. Quality may fall within your third head.

For a company like Sainsbury's where quality is extremely important, you are not passing it on.

I'm told that I'm getting into the yellow area and I --

MR JUSTICE BARLING: Look, we have -- this has been a very helpful discussion but we have delayed you a bit. Are there any more cases in bundle I4 that you want to take us to?

MR BREALEY: No, is the answer, my Lord. The pass-on in the United States I won't go through but I will hand up better copies because the top of the pages are missing. But the Hanover Shoe is worth it. Again, if one looks

at paragraph 283 and the very last paragraph of the quote, there is this reference to substantially reducing effectiveness. So one of the reasons that the Supreme Court at federal level denied pass-on is because it would reduce the effectiveness of private enforcement. The European Court has not gone down that road, it has not banned the pass-on defence but it has said it's got to be interpreted strictly and you have got to prove direct pass-on. Then, I will not deal anymore with the facts because one will see, if you have got the colour coding, the reference to how Sainsbury's prices, and it is all in yellow, and I have done my best to answer the questions but I know I'm going to get into slight trouble.

I do emphasise and I will just come onto a few points here -- so paragraph 325, I have made the point in opening yesterday, but one cannot in all consciousness ignore as irrelevant what MasterCard -- I'm at 325 here -- have been submitting for over a decade and if one remembers, we did not get disclosure of this until we found -- because MasterCard had amended its defence to plead this decision of association undertakings point, before Professor Beath and Mr Smith came on board, they amended their defence to plead the consensus point, that meant they had to give disclosure

and when we found out -- when we saw the extra disclosure on the IPO point, the consensus point, we saw reference to MasterCard denying the pass-on defence and that led us to an application for specific disclosure in front of my Lord. A lot of these documents then came out of the woodwork.

I make the point because some of the documents are MasterCard talking to journalists, submitting to the Commission x, y and z as to why there is zero pass on. I will quickly go through some of these. But some of the documents are from fairly eminent firms of economists: NERA, Europe Economics, all looking at the Australian experience, the Spanish experience and the American experience and saying: well, the studies so far suggest that this small import price, we can't see any way that it feeds into higher retail prices.

It is not just a forensic point. It is MasterCard have for the last -- over ten years been relying on reports by firms of economists to argue that there is zero pass-on. Therefore, when they come to the Tribunal in the next couple of weeks with further economists to say there is a 100 per cent pass-on, one has to take it with a degree of scepticism.

So on 325 we set out the documents that we have found on the disclosure, where MasterCard have said zero

pass-on. Paragraph 333 refers to the NERA study, which refers to the Australian experience. The only document, because, again, I have already submitted you have got to look at it on a case by case basis, but it is important to see what MasterCard have been arguing. 335, I don't think that's -- that's fine is it? 335 is at E5.4.

MR JUSTICE BARLING: That's the Europe Economics.

MR BREALEY: Just to see the extent to which they have been going.

MR JUSTICE BARLING: E5.4?

MR BREALEY: Tab 54.

MR JUSTICE BARLING: When we have had a look at this, perhaps we should give the transcript writers a break.

MR BREALEY: I'm sorry, a break. Then I will try and finish, after the break, ex turpi causa and then I will probably call it a day.

MR JUSTICE BARLING: Okay.

MR BREALEY: What we refer to in paragraph 335 of the opening submissions, it is E5.4. Europe Economics. Now, until we referred to this or we got disclosure of this -- and this is something I will have to ask -- I can say it now -- the two economists from MasterCard's side had not in any meaningful way, if at all, referred to the Australian evidence, the Spanish evidence and any of these documents.

So we find this document:

"The economic impact of interchange fee regulations, UK."

We see from the disclosure that this was prepared on behalf of MasterCard who then had -- at 359 we see that this was a covering email, the report was distributed within MasterCard and that an executive to the report went out to 17 national journalists, who they had been briefing. So this was part of a wide campaign.

We see at 134.1:

"Executive summary. Headline findings and impacts for the UK if interchange fee regulation is introduced."

So this is what MasterCard, relying on studies:

"In Spain and Australia, the regulation of interchange fees, [IF], resulted in a transfer of costs from retailers and consumers. Retailers' costs fell as they paid lower merchant service charge, but this cost reduction was not passed on to consumers in the form of lower retail prices."

So they are referring to experiences in Spain and Australia where they could not identify that the retail prices had changed.

If we could just pick this up in Spain --

MR HOSKINS: Before we leave that, could you just look at the second and third bullets, where they deal with the

UK, and you will see from the third bullet it says "if it is passed on in the UK".

MR BREALEY: Yes. What that means, they don't actually say that it will be passed on, when one actually goes to the document. They are not saying it will be passed on, they are actually saying, it will not be passed on but what they go on to do, if it is passed on, what is the impact on retail prices and then when you do the calculations you see that it results in fractions of a penny.

MR JUSTICE BARLING: The third bullet point says:

"... a reduction in retailers' costs up to 2.2 billion. This saving would not be passed on to consumer."

MR BREALEY: Then it says:

"Even if retailers passed on these savings, prices would fall by only [those figures]."

When you translate that into a price of a product, and clearly the economists are going to deal with this, when you translate that into the price of a particular product, again, it comes out at fractions of a penny.

So Spain we see at 1360. That's where it starts. So this is MasterCard representing to the world what is going to be the impact in the UK. So exception 3.1.4:

"Impact on consumers."

Bundle page 1360:

"No impact on final prices [MasterCard says]. The intended effect of imposing a cap on interchange fees that they would translate into lower prices of goods and services is summarised below."

Then we get sort of diagrams:

"Consumers were intended to be the main benefits."

We go on, and then:

"As reported in Iranzo et al ,this chain of effects did not take place in Spain. Although the reduction in IF did translate into lower ...(Reading to the words)... having been passed through to decreased prices was found by the study. The explanation given was that the reduction in the price per transaction would have been insufficient to justify a move in price points. Also the authors found no evidence of an improvement in the quality of products offered."

Again, the quality is maybe part of the third point that Mr Smith (inaudible) or it could be the fourth point.

So that was Spain. Then we have Australia and all I need to do at the moment -- if I go to 1373. Right at the bottom of 1373:

"It is noted in the previous section, the Spanish case, there was zero passed through by merchants to

consumers."

Then 1374, across the page, almost right at the bottom:

"Although no pass-through to consumers by means of lower retail prices was identified in Spain, Australia and more recently in the US, we have estimated the forward and retail prices that would be equivalent to a 50% reduction."

It is not the case that they are saying there would be pass-on. They are estimating what the impact on retail prices would be assuming that 50% was passed on. Then you do the maths, which I can't do without the help of the economists.

PROFESSOR JOHN BEATH: Could I just ask a question while we are on this. I want to get clear in my own mind. The studies we have been looking at here have to do with reductions in the interchange fee. The discussions that we were having about prices -- the setting of prices in industry seem to be implying that the thing we were talking about was an increase in a fee. Now, you could understand, or one might understand, here is an open question, why, where a cost goes up, a price would adjust to reflect that, but where a cost goes down it is taken as a bonus and not passed on because it is a bonus. So there's probably a difference in the way in

which pricing behaviour works whether we are talking about cost increases or cost reductions.

MR BREALEY: I take that point. What is being said here and again, I don't want to get into too much yellow territory --

PROFESSOR JOHN BEATH: No, I understand.

MR BREALEY: You have made the point, sir, which is that no one can refer to a price hike in this case. What MasterCard are doing are basically saying: if we gave you X million pounds by way of a bonus, you would have had lower prices. You would have directly -- well they don't say directly, I'm not sure they apply that test but they say that because of that reduction in interchange fee, you will have directly fed that into lower prices. It is not necessarily the same as if the higher -- it may be a bonus and you may do it with all sorts of ways. You may take that bonus and put it into quality.

PROFESSOR JOHN BEATH: Or maybe as you said we are talking about things that mathematicians would call the second order of smalls. They are just noise in the system and nobody notices it.

MR JUSTICE BARLING: Shall we take a short break.

(3.25 pm)

(The short adjournment)

(3.35 pm)

MR SMITH: Mr Brealey, I see further to my request after the short adjournment we have identified the MasterCard rules in bundle E3.10, beautifully shaded blue, unsurprisingly, but they are dated 15th May 2014, which struck us as being a little late for the purposes of these proceedings and we wondered if it would be possible to have earlier versions such as they were during the course of the claim going back to 2006.

MR HOSKINS: The ones that were in place --

MR SMITH: That were in place from 2006 onwards.

MR HOSKINS: I understand, of course.

MR BREALEY: Again, it is late in the day, we have got quite a lot of yellow and so I'm going to finish on pass-on, if that's --

MR JUSTICE BARLING: Can we put Europe Economics away?

MR BREALEY: We can put Europe Economics away, yes, my Lord.

I'm going to go on to the ex turpi causa and try and finish that today, just for obviously, completeness, after pass-on we have section F at paragraph 360 which is where, assuming that there is some pass-on, then the economists look at the volume effects.

Then, section G, interest, I hadn't quite appreciated the subtle nuances as to what and what was not being argued in the sense of it being confidential,

so I'm just going to ask the Tribunal to read the interest and if we then -- obviously we will have to cross-examine in camera and then we will have to do it, I would imagine, maybe, depending on the evidence that comes out, argue it in camera in closing.

But we have tried to set it out pretty fully here.

MR JUSTICE BARLING: Yes.

MR BREALEY: It is no secret that the economists do agree that it should be compounded, it is just a question of the rates. I will pass over section I, exemplary damages, that is fact-specific, and just for half an hour or so, finish on ex turpi causa and then you can, in a sense, get rid of me.

So this is section J, 439.

MR JUSTICE BARLING: Yes.

MR BREALEY: I have three cases to go to, but the background facts are pretty uncontested. I don't think this is -- none of this is yellow.

We know that Sainsbury's, that's Sainsbury's Supermarket, is a wholly owned subsidiary of J Sainsbury's, and we know from February 1997 until February 2007 that the parent, J Sainsbury's, held 55% of the shares in Sainsbury's Bank and Bank of Scotland. Then at paragraph 441, J Sainsbury's sold 5% of its shareholding in Sainsbury's Bank to Bank of Scotland so

they both held 50% each.

Then, on 31st January 2014, J Sainsbury's acquired the Bank of Scotland's 50% shareholdings and became the sole owner.

443 Sainsbury's Supermarkets and Sainsbury's Bank were -- we have called half sisters, not full sisters because of the Bank of Scotland shareholding, but half sisters between the period 1997 and 2014 and then were sister companies thereafter, sharing the same parent, so this it is all common ground.

It is also common ground that until the beginning of 2014 Sainsbury's Bank was an affiliate rather than a principal member and that Sainsbury's Bank operated under the umbrella of the Bank of Scotland, which was the principal member and certain of the MasterCard witnesses will explain what affiliate means, but it is one below.

As the Tribunal have picked up, the Sainsbury's evidence comes in the form of two witness statements, one is Hannah Bernard and the second in part is Mr Rogers, the CFO.

I would like really just to flag some of the points that we rely on as to why Sainsbury's Supermarkets is not precluded by the principle of the ex turpi causa from bringing this claim.

If I could go to -- so as I said in opening, there are two key issues to decide. One is whether Sainsbury's Supermarkets forms part of the same economic unit as Sainsbury's Bank. So they are clearly two legal entities, but does Supermarkets form one economic with the Bank and the second main issue is, if so, does that economic unit of the Bank/Supermarkets have significant responsibility for the breach of competition law?

There are little things in between, but those are the two principal issues. The economic unit point and the significant responsibility point.

Can I kick off with the single economic entity point and that starts at 459. The concept of an undertaking within the meaning of article 101 is aimed at economic entities which consist of a unitary organisation of personal, tangible and intangible elements which pursues a specific economic aim on a long-term basis and can contribute to the commission of an infringement of the kind referred to in that provision, and we set out the cases. I emphasise the very old case of Hydrotherm v Andreoli which is at paragraph 460 and we have set out the quote there. I emphasise the bits underlined:

"In competition law, the term undertaking must be understood as designating an economic unit for the purpose of the subject matter of the agreement in

question, even if in law the economic unit consists of several persons. The requirement of 101 is therefore fulfilled if one of the parties to the agreement is made up of undertakings having identical interests controlled by the same natural person who also participates in the agreement, for in those circumstances competition between the persons participating together as a single party is impossible."

I just emphasise the subject matter of the agreement. This will be, to a certain extent, the subject of evidence, but it comes to what's often called the shoe polish example in jurisdictional -- in the Brussels Convention. You may have a subsidiary that is governed by the parent, but if the subsidiary is acting in a completely ancillary field and it cannot be said to be party to the agreement, then the subsidiary, although it is a subsidiary controlled by the parent, is not part of the same economic unit for the purposes of the infringement. So, again, if you have a vitamins cartel and it is in Switzerland and you have a subsidiary in the UK, but that UK subsidiary is not selling vitamins but is selling shoe polish, you would not say that that shoe polish subsidiary is part of the same economic unit.

MR JUSTICE BARLING: Regardless of decisive influence.

MR BREALEY: Regardless of decisive influence. That, again if we need to, we will go the Cooper Tire-type jurisprudence where Mr Justice Teare -- where the shoe polish example has been debated, but you get this from Hydrotherm v Andreoli.

So just because you are connected doesn't mean to say that you are an economic unit for the purposes of infringement.

I want to just concentrate, paragraph 464, on the two cases relating to sister companies and that is the Aristrain case which I think is at -- I always thought it was tab 17 but it is not, it is I7, tab 6.(Pause).

What I really want to get out of these two cases is in order for Supermarkets and the Bank to be one economic unit, so that -- so if the bank has been guilty of an infringement, is somehow Supermarkets to be fingered also for that infringement? That's what it is all about. So before we get to significant responsibility, the Bank has been party to the unlawful agreement but does that preclude Supermarkets from bringing the claim?

The case law clearly states that there has got to be some influence that Supermarkets has over the Bank. In order for you to say that the Bank has committed that infringement, Supermarkets is going to also be liable

for that infringement, why should Supermarkets be somehow liable also for that infringement? It's because Supermarkets are essentially party to that, they are one economic unit. Why? Because there is a degree of control or influence that is being exerted by Supermarkets over the Bank. Because if it is completely separate and the Bank is acting independently, then it is the Bank's fault.

So that is why in Hannah Bernard's witness statement she emphasises for regulatory reasons the Bank had to act independently.

So there is going to be a key factual issue in the case as to the degree of independence that the bank had. This is why these two cases are quite --

MR JUSTICE BARLING: Independent from Supermarkets or independent -- sorry, I missed it when you said who had to have the influence. Obviously J Sainsbury's Plc is the holding company, isn't it, or the parent.

MR BREALEY: We submit that -- we take it two ways. The first is that independence from the parent, J Sainsbury's, but even if we are wrong on that, in order for the Supermarkets to be banned/barred, there has to be some influence or a degree of control, the Supermarkets over the Bank, and that's not even alleged. So we say that J Sainsbury's did not have sufficient

control over the Bank. The Bank has to operate independently, but we go further than that and say even if the Bank did, why is that Supermarkets fault as well, simply because they are 100 per cent owned by J Sainsbury's?

So, when we get to the Aristrain case, I can pick this up. It is concerned with fines. I can pick this up at paragraph 96. I don't know whether I asked the Tribunal to go to paragraph 96, page 219 of the bundle. This is a case of two sister companies and the Commission taking essentially the turnover of one sister company and pooling it with the other:

"It is settled case law that the anti-competitive conduct of an undertaking can be attributed to another undertaking where it has not decided independently its own conduct on the market but carried out in all material respects the instructions given to it by that other undertaking having regard in particular to the economic and legal links between them."

I just state that again:

"It is settled case law that the anti-competitive conduct", so the MIF of the Bank "can be attributed to" Supermarkets where the Bank has not decided independently upon its own conduct on the market but carried out in all material respects instructions given

to it by that other undertaking, Supermarkets.

"In the present case, however, the contested decision does not establish that the appellant had the power to direct the conduct [so the appellant, one subsidiary] of the other subsidiary to the point of depriving it of any real independence in determining its own course of action on the market.

"The court at first instance was wrong to rule that it is impossible to impute..."

And this is all about imputation:

"... it is impossible to impute to a company all of the acts of a group even though that company has not been identified as the legal person at the head of that group with responsibility for coordinating the group's activities.

"The simple fact that the share capital of two separate commercial companies [ie sisters] is held by the same person or the same family is insufficient in itself to establish that those two companies [those two sister companies] are an economic unit with the result that under community competition law the actions of one [say the bank] can be attributed to the other, and the other can be held liable to pay a fine for the other..."

Or in this case to be barred from bringing their claim:

"The contested decision states no reason in that regard and even contains an internal contradiction since it suggests the responsibility for the infringements found to have been committed must be attributed to both companies in equal measure, while at the same time, ordering only one of them to pay a global fine."

Again, MasterCard, I think, take a slightly different view of this but we say that this shows that simply because you are part of the same group, if the Bank has independently committed an infringement, if one subsidiary has committed an infringement, how are you going to attribute liability for that infringement to Supermarkets in circumstances where Supermarkets -- and this will be a question of fact and cross-examination -- doesn't exercise any influence over the Bank.

Again, it comes back to the key question, does the Bank act independently on the market? You see that's a case -- the principle in our favour, we say, and the conclusion in our favour, we could then go to the Jungbunzlauer case -- I think that is at tab 9 -- where again the same principle applies of attribution of liability, but here it was found on the facts that there was. Again, I just take the Tribunal to the relevant passages. It is 320 of the bundle. Paragraph 122. Again, here, on the facts what happened was there were

two sister companies but as a matter of fact, one sister company had been appointed essentially to control various parts of the group. So on the facts the sister company was acting as some sort of parent.

Again, paragraph 122:

"It is clear from the case law that in prohibiting undertakings inter alia for entering into agreements or participating in concerted practice ... effect trade ... object to effect the prevention, restriction, distortion of competition is aimed at economic units made up of a combination of personal and physical elements which can contribute to the commission of an infringement of the kind referred to in that provision."

So one is starting to look for some personal physical elements which are contributing to the bank committing the infringement.

"In the present case the applicant does not deny the existence of the infringement. It does argue that the Commission could not attribute responsibility for that infringement to it."

So one sister had committed the offence and could that infringement be laid at the door of the other?

"On that point it must be observed that until 1993 the group was managed by the GmbH which also produced citric acid, but after that restructuring,

Jungbunzlauer, as a management company, managed all the business of the Group including that on the citric acid market, and the Group was headed by a holding company. With regard to the Group's subsequent restructuring, the court notes that the applicant, a wholly owned subsidiary, was a sister company and not its parent. In that context the applicant rightly submits that the present case differed from those that gave rise to the case law of ...(Reading to the words)...which states in essence that the Commission is correct to presume that a wholly owned subsidiary carries on in all material respects the instructions of its parent company without having to ascertain whether the parent actually exercised that power."

In other words, the sister company was saying: you can't presume control or decisive influence because I'm a sister, I'm not a parent.

"However, the court says it is clear from the recitals in the decision and contrary to the applicant's submissions that the Commission did not rely on such a presumption but instead examined on the basis of the replies given by Jungbunzlauer and GmbH during the administrative procedure, the question whether, notwithstanding the structure as described above, the infringement should be attributed to the sister

company."

So, again, we are looking for facts which would show that the infringement should be attributed to them.

"In that regard the court notes ... describing the structure, stating in particular the management of the group was handled by AG, which is a management company who managed the companies owned by holding."

Then over the page, a few lines down:

"Jungbunzlauer added that it was GmbH which was operational on the citric acid market, save with regard to the distribution of that product which was handled by another subsidiary. All management was handled as existed as a management company. [So the conclusion is that] On the basis of the joint statements the Commission was justified in finding that after the restructuring of the Jungbunzlauer Group in 1993, the activities of GmbH were limited to mere production whilst the management of the group business, including that involved in citric acids, was in the hands of the sister company, so that the infringer did not decide independently its own conduct on the market..."

I emphasise that. So a sister company was essentially managing the business and the infringer, "did not decide independently its own conduct on that market, but carried out in all material respects the

instructions given by the sister company".

"The Commission was justified in finding that the parent company in common had decided to entrust the sister company with the task of conducting the entire business of the group, including consequently that associated with the group's conducted in the market covered by the cartel, namely, the citric acid market."

In a nutshell, what had happened was that the sister company, who was complaining that, "I am not responsible for the infringement, I'm a sister company", actually was controlling and the infringer was not deciding independently its own conduct on the market.

Again, that is what we say is the law, in order to attribute the alleged infringement of the Bank onto the Supermarket, there has got to be some fact which shows that that infringement can be attributed to the Supermarkets. If the bank is operating independently on the market, then one is not going to be able to show that fundamental condition.

That's really what I want to say on economic unit and I will leave it to see how Mr Hoskins deals with this point. Clearly, it is a matter of fact but ultimately, ultimately, the key criterion is, if the Bank was operating independently on the market, then, Supermarkets' retail cannot be liable for that

infringement as an economic unit.
MR SMITH: Mr Brealey, how far has there been cross-fertilisation, if I can call it that, between European principles and English law principles in relation to the ex turpi causa defence? Let me unpack that a little bit. Ex turpi causa, as I understand it, is a general defence in actions of tort, whether it is a competition claim or not.
When in a non-competition tortious claim, the defence is raised, as I understand it, there are two essential elements. One is that the illegality in some way be related to the claim that is being advanced, it can't be completely detached. Then, secondly, the illegality, assuming it is not completely detached, must in some way be attributable to the claimant.
Absent a competition element, one wouldn't get into the question of economic units or undertakings at all, you would simply look at the identity of the claimant and work out whether certain conduct was attributable to the claimant using principles like those that the House of Lords articulated in Meridian and cases like that.
I suppose my question is this, it seems to be implicit in your submissions that there is a European element to the ex turpi causa defence in a competition

context because of all this discussion about undertakings or are you citing these cases on undertakings because they go to the question of attribution?
MR BREALEY: I think we are doing both. If we go to 482, we do rely on certain of the English law principles. In answer to your question, which is that the English law of: it's got to be related, is very similar to the Hydrotherm v Andreoli, which is the shoe polish. I think that's why the two dovetail there.
So that is the economic unit. But when it comes to the turpitude, which is essentially the ex turpi causa bit, the ex turpi causa has essentially two elements to it. One is an English law principle of the requisite turpitude and if you do have the requisite turpitude, does a necessary EU law trump that because of the significant responsibility because the significant responsibility is not a criterion of domestic law, it is a criterion of EU law? So just as in Courage v Crehan, Tinsley v Milligan applied to bar his claim, but EU law intervened.
We would say that's why at paragraph 482 onwards we refer to the English law principles and we say, for example, 485, where Mrs Justice Asplin has looked at this in the context of the Tesco v MasterCard, so

MasterCard was making the same point in Tesco's Bank:
"It is more than merely arguable that in order to fall within the category of quasi criminal civil sanctions it is necessary to establish intentional or negligent conduct and that it is necessary to establish whether the claimants have, each of them, the requisite state of knowledge."
That is essentially where we are coming from on your second point. That it's got to be attributable and that if you don't have the requisite knowledge or intent, it can't be attributed to you.
MR JUSTICE BARLING: I thought you were showing us these cases because MasterCard, to get off first base on this point, they have to show that you are part of the same economic unit?
MR BREALEY: Yes.
MR JUSTICE BARLING: I mean if you were applying purely English law, you know the separation of persons and corporate personalities would be such that this would be a very uphill task.
MR BREALEY: Correct.
MR JUSTICE BARLING: But it is because community law has this concept of an undertaking, which overlaps legal personalities, that it is open to them to raise the point.

MR BREALEY: Yes.
MR JUSTICE BARLING: Then your second limb is the pure illegality limb, pure ex turpi causa.
MR BREALEY: Yes.
MR JUSTICE BARLING: The first point is your answer to them, isn't it, on corporate personality?
MR BREALEY: On corporate personality. So if it was just a matter of domestic law, not competition law, we would say we are two separate entities, why are we here? But because there's no -- you know, you are not party to the illegality at all, you don't get past first base.
As my Lord correctly says, we are dealing with economic unit because they say you are fingered together, you are one economic unit, and then if we say we are not -- and I can see where you are coming from, the tests might be kind of similar, but if we are not part of the same economic unit, then we have to work out whether there is sufficient turpitude on Supermarkets and if there is sufficient turpitude on Supermarkets, nevertheless whether they are significant and responsible for the breach.
MR JUSTICE BARLING: But if you are not part of the same economic unit, isn't that the end of their case on this?
MR BREALEY: Yes, absolutely.
MR JUSTICE BARLING: Don't they have to succeed on both?

MR BREALEY: Absolutely, yes.
MR JUSTICE BARLING: I think they would accept that.
MR BREALEY: I think they must do. I don't know what they accept but --
MR JUSTICE BARLING: I don't know, but I just assume that they have to succeed on both.
MR BREALEY: I'm almost certain that -- it is the way they put it in their skeleton, they have to establish at first base that we are part of the same economic unit. Having said that, we can tease out whether Supermarkets has the necessary turpitude as a matter of domestic law and that's Tesco's and MasterCard, and if they do, whether there is significant responsibility for the breach.

I think that's the way it is put against us and we might find out from Mr Hoskins tomorrow --
MR SMITH: I suppose I was wondering how far the first stage was actually necessary in the sense that one can have, again, taking a non-competition context, a claimant who acts through a third party and who by virtue of agency or some other form of attribution, has that agent's acts attributed to the claimants so that they become the claimants.

It seemed to me that the European cases and the English cases might actually be the same or the same

point there. So I was wondering how far this actually was a question of undertakings and how far in fact it was a question of attribution.
MR BREALEY: Well certainly I would need to -- I don't think we have forensically analysed it like that. I have come from it, I think everyone has come from it on the basis that you prove economic unit, then whether there is sufficient turpitude, and then significant responsibility for the breach.

But I do take the point, and I'm trying to work it through, whether the English law principles on attribution are essentially the same as the economic unit point.
MR SMITH: Let me put it the other way round: suppose you can show the turpitude and you can show the significant responsibility for the turpitude, albeit in another entity, would you say that the illegality defence would fail because they are not part of the same economic undertaking?
MR BREALEY: Well, certainly. If they showed that Bank had sufficient turpitude, knowingly breached it, whatever, was significantly responsible because it participated big time in setting the MIFs, does that still bar the claim by the separate legal entity, Supermarkets? Answer: no, we say, because there is not sufficient

attribution. Now I hadn't really focused on whether that sufficient attribution is a matter of domestic law or EU law and undertakings. I have always looked at it from the perspective of European law and unless you can show sufficient attribution as a matter of European law, then you are out. The ex turpi causa defence doesn't apply.
MR SMITH: Right.
MR BREALEY: Does that makes sense?
MR SMITH: That does make sense, it is simply that there are many, many English legal cases on attribution which probably when all is said and done, amounts to the same as the European cases --
MR BREALEY: I think we will probably have to check those cases and see the extent to which they differ, if at all, from the European cases.
MR JUSTICE BARLING: I'm a bit confused now, I have to say, because we now have three areas, and I'm not sure whether the turpitude bit comes into the first or second, because I had rather assumed that in order to show you are part of the same economic unit you have got to show this element of control.
MR BREALEY: Yes.
MR JUSTICE BARLING: Which is very akin to -- do you need turpitude apart from control? I thought control --

I appreciate control and decisive influence, whichever way you want to put it, is the test of making you a single economic unit, but also doesn't it also get you somewhere down the road of turpitude, because you are in control of something that is an infringer. You know, ex hypothesi is infringed, but you have got to find something in it above and beyond that, have you?
MR BREALEY: Yes, if I go to paragraph 484 of the opening submission, let's for the moment forget economic unit and/or attribution. Let's just concentrate on the Bank. Let's assume the Supermarkets are out of it and the Bank is claiming or whatever. So 484, Lord Sumption pointed out:

"There is a recognised exception to the category of turpitudinous acts, the cases of strict liability generally arising under statute where the claimant was not privy to the facts making ...(Reading to the words)... a reason for holding that it is not turpitude at all."

That applies we would say equally to Supermarkets and the Bank, but let's just keep it simple:

"In Tesco v MasterCard it is ...(Reading to the words)... that in order to fall with the category of ... it is necessary to establish intentional or negligent conduct and that it is necessary to establish whether

the claimants and each of them have the requisite state of knowledge."

So there is an element here of you just don't take the strict liability angle. You don't just say: you are guilty of an infringement in order to bar the claim has there got to be something extra, which is a state of knowledge. That's where you are getting turpitude from. If you conspire together to defraud the National Health or whatever, or you conspire together to raise prices, that would have the requisite turpitude.

But if you are one of the undertakings of a decision of an association and you are the 1,000th one and the big players are guilty of the infringement, or they are directing the infringement, what this is going to is whether that thousandth person has a sufficient turpitude, sufficient as a matter of public policy, to bar the claim. If it is found that you did have -- you did know about it, for example, but there is nothing that you could have done, because you had to sign on standard terms and conditions, you had an equal -- so you did know about it -- so arguably you had that element of turpitude, but you didn't have significant responsibility for it --

MR JUSTICE BARLING: So this really goes back to Mr Smith's point, that there may not be much difference between the

turpitude and requirement of national domestic law and the significant responsibility point in Courage v Crehan.

MR BREALEY: That's what I hadn't really, to be quite frank, focused on.

MR SMITH: It is three points. You start with the turpitude: Is it naughty? And the question then is: is it naughty enough? And we have had a lot of learning from the Supreme Court in Apotex about what can and can't be sufficiently naughty to trigger a public policy defence.

Then even if there is naughtiness, illegality, it has to be related to the claim, so something which is completely unrelated to the claim, even if it is particularly heinous, won't matter.

MR BREALEY: Correct.

MR SMITH: That's sort of Jungbunzlauer, they have a discussion about that there. Then, assuming you pass those two, there is the question of whether the naughtiness can be tied to the claimant, and that is a question of was it the claimant's own act or if it wasn't the claimant's own act, can that act, through one of the various legal tests that exist, be attributed to the claimant?

MR BREALEY: Correct.

MR SMITH: As I say, there is a lot of law on what that is.

MR BREALEY: Yes.

MR SMITH: I suppose what started this discussion in my mind was how far the concept of an undertaking was relevant to this question of attribution. It seems relevant on the peripheries, but actually, it is quite a loose form of association, the undertaking test. It seemed to me what you were looking at in terms of the European cases where you are saying significant responsibility for another entity within the same economic unit was coming quite close to the English law test of attribution of acts of another to a claimant and my question was how far is it a question of English law and how far is it a question of European law?

MR BREALEY: The simple answer to that, it is primarily a question of English law. So EU law is not laying down a rule of turpitude. So it is for France, Spain, Germany, Scotland, whatever, to lay down its own public policy rule, which relates to barring claims where you are party to the same breach.

So the simple answer to that is it is a matter of English law. The only caveat to that which is the Courage v Crehan, which is where Lord Sumption deals with this and we set this out at paragraph 493, in the Jetivia case where Lord Sumption refers to the case of

Courage v Crehan and says: well,EU law may interfere in the application of national law if the claimant has not been significantly responsible for the breach. I'm not sure and I would have to go back and check the cases, whether that is consistent with the English law of attribution. I think certainly as far as he is concerned I'm not sure it does, but I read him saying there that -- he says courts normally examine the policy rationale and he is looking at the competing public policies and he is saying that when it comes to breach of EU law, Courage v Crehan, you can look at essentially significant responsibility and I have read that so far as being a brake on the application of domestic law, whatever it be.

But I certainly take the point that you start off with English law and maybe we are doing it in the wrong way, starting off with economic unit.

MR SMITH: Thank you, that was very clear.

MR BREALEY: Sir, I'm not going to finish by the looks of it tonight.

MR JUSTICE BARLING: Shall we all contemplate that and those interesting points overnight then.

What have you got to deal with now?

MR BREALEY: That's it.

MR JUSTICE BARLING: Just a few bits and pieces then? A bit

more of ex turpi causa.
MR BREALEY: I will have a look at the cases and that's really it. This is the last chapter.
MR JUSTICE BARLING: Yes. Right. Thank you very much. We will have Mr Hoskins on his feet tomorrow.
(4.30 pm)
(The court adjourned until 10.30 am on Wednesday, 27th January 2016)

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