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

Day 4

January 28, 2016

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(10.30 am)

Opening submissions by MR HOSKINS (continued)

MR JUSTICE BARLING: Good morning, Mr Hoskins.

MR HOSKINS: Good morning, sir. I hope, if nothing else, Messrs Rochet and Wright aided your insomnia last night.

MR JUSTICE BARLING: Yes, I slept very well. No, we've read it carefully.

MR HOSKINS: You've read it, so I will be brief. If we can start, therefore, in bundle E3.6, tab 130A.

If I can pick it up at point 6, you will see that the first paragraph on that page begins:

"Given the obvious importance ..."

It is the second sentence of that paragraph:

"The point of departure from the existing literature is to model credit cards explicitly. An existing literature model's price determination and payment cards networks initiated by Schmalensee, Rochet and Tirole with the earlier date, and Wright. The models in this literature have essentially focused on the choice between payment cards, which could just as well be debit cards, and cash or cheques. We contribute to this literature by extending the models to allow a separate role for the credit functionality of credit cards thereby allowing us to discuss credit card interchange

fees specifically."

This is very important in this case because hopefully you have picked up from our skeleton, because of the Maestro experience, MasterCard has very little presence in the debit card market, which means that credit cards make up over 99% of the value of this claim. So it is the credit card MIF that really matters in this case.

Going on:

"In our model, credit cards can be used for two types of transactions: Ordinary purchases for regular convenience usage for which cash or a debit card are assumed to provide identical benefits, and for credit purchases where credit is necessary for purchases to be realised.

"Credit purchases include a range of different types of purchases, such as unplanned purchases, impulse purchases and large purchases for which the consumer does not have the cash ...(Reading to the words)... of payment facilitates the transaction."

So two types of transaction.

Then, you have read this, so I'm not going to read it all out, but the top of point 7:

"Since consumers do not internalise retailers' cost savings from avoiding direct provision of credit and

since merchants cannot distinguish the type of consumer they face, there is also a case for setting a relatively high interchange fee so that consumers that wish to rely on credit are induced to use credit cards when it is efficient for them to do so. For this reason, to maximise consumer surplus, including the surplus of cash customers, may require setting an interchange fee which induces excessive usage of credit cards for ordinary purchases."

So you set the level to encourage the use for credit purchases accepting that it might lead to a degree of inefficiency for ordinary purchases.

Then the next paragraph -- I pick it up at the second sentence:

"The theory suggests one of two possible caps will maximise consumer surplus. Depending on the relative costs and benefits of the different instruments, the cap should either be based on the issuer's costs to avoid excessive usage of cards for ordinary purchases ..."

That's akin to what the Commission did in the 2002 Visa decision and it is akin to Dr Niels' adjusted cost benefit approach:

"... or on merchant's net avoided costs from not having to provide credit directly, so that consumers use their cards efficiently for credit purchases. Since

evaluating which of the two options gives higher consumer surface is informationally very demanding, a conservative regulatory approach would be to cap interchange fees using the maximum of these two levels, which is likely to be the latter option."

So that is the merchant's avoiding costs for providing their own credit:

"In our model this always raises consumer surplus ...(Reading to the words)... will sometimes result in the best outcome for consumers. In contrast, using issuer costs to regulate interchange fees is realistically only likely to give a lower bound of possible interchange fees that maximise consumer surplus."

They are saying for credit cards, two options. There are informational difficulties and nobody before you is suggesting the avoided cost to merchants of providing their own credit.

What Dr Niels is suggesting is the issuer's cost methodology proposed here. That is one of the methodologies that Rochet and Wright say is appropriate for credit cards. They do not suggest the MIT is appropriate for credit cards, and they say using that issuer's cost approach is likely to give a MIF which is the lower bound of the best interchange fee.

So where does that leave us? The Commission formal decisions they have adopted, exemption decisions, commitments etc, and EU regulation are based on limited data which I think is now generally accepted to be pretty much insufficient for purpose. That is the old national bank studies. In addition, those Commission decisions in the regulations rely on an academic theory, that's Rochet and Tirole, which I showed you yesterday on its face says that it will give too low a figure for MIF if welfare is one of the policy objectives. And I showed you that it is, and which Rochet, one of the authors of Rochet and Tirole, now says isn't suitable for credit cards, which, in our submission, means that what the CAT should do is to assess the evidence which it has before it to produce a more robust proxy. And we say you are in a position to do that. You will have the evidence, you will hear the evidence.

But what this shows is that MIT isn't fit really for this purpose according to its own creator, and certainly even if one were to do a MIT to try to get a grip, to get an idea of how you wield the broad axe, it needs adjustment because the Rochet and Tirole does not take account of the specificities of credit cards.

One little point that crops up, and this is not an ideal place to take it but I will take it now, is

Mr Brealey's free rein point. He says you need to have objective criteria, so he is talking about in the past, and we will see, I will come to it, the way in which MasterCard set its MIF had certain characteristics. I can't remember if they are all confidential or not, but it was based largely on cost surveys and certain other factors with them taken into account. I will come back to that.

He said that's not acceptable because he showed you, I think it was in the Visa decision that the exemption was premised on the basis that there would be objective criteria applied for the future in order to grant an exemption.

But there's really nothing in that point because MasterCard did predominantly seek to base its MIF on costs, and actually what we see from the evidence is it set the actual level of the MIF below the level of the costs that were indicated by the EDC cost studies. So it wasn't taking the costs and then using other factors and pushing the MIF up, it was taking the cost studies, taking other facts into consideration and pushing the MIF down from what would be justified by the costs.

The best place I can show you that is in our skeleton argument. It is paragraphs 86 and 76. So that is bundle A, tab 2 at page 190. The numbers are

confidential so I have to be a bit careful here. But paragraph 86 gives you the results of the cost studies and you will see the percentages there, blue confidential.

If you compare those with the weighted average rates actually charged, which are at paragraph 76, and it is the credit card figures we are interested in, you will see the substantial reduction.

MR JUSTICE BARLING: Yes.

MR HOSKINS: So 86 and 76(a).

PROFESSOR JOHN BEATH: I can't actually see it, it is too --

MR JUSTICE BARLING: It is very ...

MR HOSKINS: What can I do? Can I hand up a tab with the number written on it and you can pass it along? (Pause)

PROFESSOR JOHN BEATH: Okay, that's fine.

MR HOSKINS: Thank you.

MR JUSTICE BARLING: We will adjust our skeletons between us.

MR HOSKINS: The second point is, for the exercise we are currently engaged in, which is looking backwards to determine what the exemptable level of the MIF would have been, it doesn't actually matter how MasterCard set its actual MIF because what, of course, we are engaged in is looking with the benefit actually of material that MasterCard didn't have at the time, because we are going

to go and look, for example, at the Commission's 2015 survey, with the Rochet and Wright article etc.

So what survey was actually doing is, with the benefit of looking backwards and seeing whether the MasterCard level was above or below what is now determined to be the exemptable level of the MIF.

For our purposes it doesn't matter how MasterCard got there. Even if it did that and stuck its finger in the air, as long as the answer comes out in the right place, that's enough.

The reason why objective criteria is important in exemption decisions is of course it is forward looking. What the Commission is saying is "We will give you an exemption, but you have to do the following going forward". But we are engaged in a purely ex-post, looking backwards exercise. It doesn't matter how MasterCard has got there historically as long as it got to the right place. So it is really just a red herring, that free rein point.

I have been through a lot, so let me do an interim conclusion. We still have a little bit to go on exemption and take stock of where we are. First of all, we say the Tribunal is free to make up its own mind about the exemptable level of the UK domestic MIF and it doesn't have to necessarily use a MIT to do so. We saw

that, for example, in recital 50 of the 2014 Visa decision. I took you to that yesterday. But the quote from it, the relevant bit of the quote is:

"National courts are well placed to assess MIFs set by local members domestically."

You will see that again in the 2015 Commission study. It says: we are doing this, but national courts and regulators are well placed to look at domestic MIFs. So you have actually been invited to do so by the Commission.

In the real world, second point, the MIT will tend to underestimate social welfare. We saw that in the 2008 Rochet and Tirole article. And social welfare is one of the objectives of EU competition law, we saw I think it was paragraph 33 of the Commission's 101(3) guidelines.

Third point, in order to take account of credit purchase, in order to take account of the specificities of credit cards, what Rochet now says is that MIFs should be based on issuer costs or merchant's net avoided costs from not having to provide their own credit.

Using issuer costs to regulate interchange fees, according to Rochet and Wright, is realistically only likely to give a lower bound of possible interchange

fees. In any event, whether we are looking at MIT or issuer's costs, the Commission has never sought to calculate a MIT-MIF in its formal decisions on the basis of the 2015 survey data. We will come to the survey. That's next on our list. But the figures that it is arrived at, all the way up to the regulation, are based on the national banks' studies, not on its Deloitte's surveys.

So our submission is the Tribunal is free to, and should, make up its own mind on the exemptable level of the MIF based on the evidence before it.

Can we turn now to the 2015 Commission survey. It is bundle E3.10 at tab 202. You have seen from the previous Commission material we have looked at that the Commission instructed Deloittes to carry out a merchant cost study for it and then it produced this report setting out some updated views on the MIT in light of that survey.

If we can pick it up at page 429.4, "Executive summary and conclusions". Again, if I can do that, asking you to read, because it will save time. If you can read paragraphs 1 to 3 and then I will pick up some points.

Points to note, paragraph 2, the last sentence:

"The study can therefore serve as a basis for debate

and further research."

This is the not the final word, it is an invitation for further consideration and that's what I'm inviting you to do.

Paragraph 3, final sentence:

"Obviously, if and to the extent that parties disagree with this and other methodological choices discussed in the report, or wish to argue that certain elements are not applicable for their specific case, they would have to bring forward arguments and/or further evidence."

That, of course, is what we are doing before you.

Again, the Commission is recognising that that is something that's acceptable, indeed one would say encouraged, because we are trying to push forward what has been a pretty rudimentary treatment of the assessment of the acceptable level of MIFs up to date.

Then paragraphs 4 to 5. Again, if I could ask you to read those. This raises certain reliability issues about the data here.

The points to note there are that because of the difficulties of compiling information, you will see at the bottom of paragraph 4, the second last sentence:

"It was decided to focus the cost measurement only on large merchants in ten countries with the highest

retail turnover in the EU. Eventually this represents a trade-off between precision of data and sample size and representativeness. Furthermore, the data collection did not manage to reach the target number of replies. Several ...(Reading to the words)... to justify their refusal to participate."

This is one of the principal issues between the experts if one is to use a MIT-MIF, because Dr Niels suggests that because the 2015 survey data is limited only to large merchants, it is appropriate to make some adjustments to try to deal with that fact. Mr von Hinten-Reed suggest the adjustments are unnecessary. I will come and I will detail the specific differences between the experts, but as we are going through the survey I think it is useful to flag them up as well.

Then if I could ask you to read paragraphs 6 to 8, which deal with the timescale to be adopted in a calculation and the split between fixed and variable costs. It is the perennial problem of the shorter the timescale, the more costs you exclude, the longer the timescale, the more costs you include in taking it into consideration.

MR JUSTICE BARLING: 6 to 8?

MR HOSKINS: 6 to 8.

Just to note that the appropriate timescale for calculating a MIT-MIF is another principal issue between the economists because Dr Niels believes that a longer timescale is more appropriate than the one that Mr von Hinten-Reed suggests.

Paragraph 13, if I could ask you to read that, please. So what the Commission is concerned with here is that, for the purposes of gathering the data, it was the merchants themselves who allocated cost to fixed variable. And given the Commission itself recognised a problem of self selection bias, you immediately see the problem.

What the Commission did was a third type of analysis, which was to use an econometric technique, and the strength of it, you will see mid-way down, paragraph 13:

"The first econometric techniques are capable of identifying fixed and variable costs without relying on the merchant's views."

That is one advantage of it.

Then at the bottom of the page:

"Second, econometric techniques allow for testing and accounting for different sources of heterogeneity across merchants ..."

So accounting for differences:

"... and therefore allow a richer modelling of the cost functions."

As always in the real world it is not perfect. It is fair for me to point that out:

"It is worth mentioning that the econometric estimations were constrained by the availability of data ...(Reading to the words)... potential imperfect modelling."

So there are problems on both sides.

Ultimately you are going to have to decide which is the most robust if you want to do a MIT-MIF approach, but there are problems on both sides.

Again, this is a principal issue between the experts because Dr Niels believes that the econometric technique is the best way to address various issues, including the subjective nature of allocations fixed and variable costs by experts.

It also allows one to take account of a longer period of time, and Mr von Hinten-Reed disagrees.

Then paragraphs 19 to 22. I don't need you to read the detail of this, but this is where one sees that the Commission presents a number of different MIT-MIF analyses based on different approaches.

Scenario 1 is what is called the short-term approach, and neither of the experts in this case

advocate a short-term approach. A medium-term approach, which it called scenario 2, you will see in paragraph 20, five lines up from the bottom:

"In the medium approach, scenario 2 ..."

That's Mr von Hinten-Reed's preferred approach.

And then thirdly, the econometric approach. That's Dr Niels' preferred approach if one does a MIT-MIF.

We don't need to go into the details just now, it is simply the existence of those three approaches I want to draw to your attention.

Then next I would like to go to paragraph 23:

"The report finally explores the possibility to obtain figures which would describe the whole merchant population, not only large merchants ...(Reading to the words)... Taking this into account and after careful consideration, the Commission therefore considers that without further data from small merchants it is not possible to draw reliable conclusions from the study concerning the level of indifference of all merchants."

That is important because remember from the Rochet and Tirole article, which is the genesis of MIT-MIF, it said one had to look at the average merchant.

So the Commission itself accepts that this exercise, not possible to draw reliable conclusions for level of indifference of all merchants.

Dr Niels suggests a means of taking account of this issue and Mr von Hinten-Reed doesn't agree with it. It is another source of disagreement between the experts.

But the experts do agree that one has to have a one size fits all MIF. So it is not the case, nobody is advocating that MasterCard and/or Visa have to have different MIFs for different merchants. And one can see immediately how that would not be practical because the four-party scheme does not deal directly with merchants.

So they both agree it is a one size fits all, it is an average.

Then paragraphs 24 to 26, the conclusion:

"All results need to be considered taking into account certain caveats. The results therefore are merely a first attempt to consistently apply the MIF."

So if you want to apply a MIT-MIF, the Commission is welcoming, encouraging such an exercise.

25:

"Nonetheless, DG Competition believes these results are based on a precise and complete data set providing valuable cost information."

You can form your own view on that as we go through the case, how reliable and robust this is, having seen what the Commission itself says about the data set:

"There are still areas of improvements. In

particular, two areas can be identified: the evaluation of a representative acquiring margin and ...(Reading to the words)... merchant's costs."

I'll skip a sentence:

"More difficult is the ...(Reading to the words)... proved to be a difficult task, while using information of large merchants to approximate the cost of small merchant is a questionable exercise."

I have already flagged up that issue between the experts. Is it better to do something to try to address that, or to do nothing and just take all the large merchant data as the basis?

So I have already sort of flagged up what the issues are for the Tribunal to decide on the MIT-MIF, but let me just set them out.

If you wish to apply MIT-MIF -- and I'm going to come onto in a minute why we say you shouldn't, and we have already seen quite a lot of why we say it is not appropriate. But if you want to do this exercise, you have to decide whether you are going to apply it as suggested by Dr Niels or by Mr von Hinten-Reed or, indeed, you may decide to take an amalgam of the two. You might like some of the suggestions of Dr Niels, but not others.

But the principal issues for you to decide are

identified and discussed in our skeleton at paragraphs 229 to 278, and I'm not going to go through the skeleton now, but that's where you will find this written out.

First issue, on what basis should the assessment of costs as fixed or variable be carried out? On the basis of the categorisations supplied by the merchants who took part in the survey, ie their own categorisation of costs as fixed or variable. That's Mr von Hinten-Reed's approach. Or on the basis of an econometric technique, which is Dr Niels' approach.

Second issue, should the MIT be applied so as to take account of the fact that the information in the 2005 Deloittes survey only related to large merchants? Third point, should the MIT be applied so as to take account of online transactions? Fourth point, should the MIT be applied so as to take account of the fact that credit cards provide benefits to merchants but cash does not, for example, by allowing sales to be made that would otherwise not happen? And you will have seen that category recognised in the Rochet and Wright article.

And that's what they say characterises credit cards. They don't just deal with ordinary transactions where you have cash or debit cards, there are functions they perform for the consumer which wouldn't otherwise be

available if you only had cash or debit cards.

Let me come to the costs-based approach, which is actually where the economic literature has got to for credit cards. It is Rochet and Wright. Because although Dr Niels has produced a MIT-MIF estimate, Mr Brealey says it is not. It is. It is a MIT taking account of the problems I have identified, that the Commission has identified. But he has serious reservations about using a MIT at all, just like Rochet and Wright do for credit cards.

If you can go to his first report, it is D3, tab 3. At page 311, at 6.9 to 6.18. I was going to ask you to read it now, but if you are happy I can just leave it in your notes. I'm in your hands. If you are finding it helpful to build this up by accretion -- I would rather you read it now, I do not want you to --

MR JUSTICE BARLING: We will read it now.

MR HOSKINS: Hopefully this helps because there's so much paper and this shows you which bits of paper matter.

MR JUSTICE BARLING: Feel free to sit down if you want to.

MR HOSKINS: Thank you. (Pause)

I'm going to come back to this in a minute, so if you can keep it out once you have finished reading it.

For these reasons, Dr Niels' preference is for an adjusted cost benefit balancing approach, which is

essentially the type of issuer's costs approach which we saw in Rochet and Wright.

Dr Niels says: no, can't use this at all. But if one is to apply a cost-based approach, then there is one main issue of principle between the experts and that --

MR JUSTICE BARLING: Do you mean Mr von Hinten-Reed?

MR HOSKINS: I'm sorry, Mr von Hinten-Reed. I'm sorry.

There is one main issue of principle between the experts if one is to adopt this approach, and that is whether the provision of credit is of any benefit to merchants or not.

Mr von Hinten-Reed asserts that the provision of credit is of no benefit to merchants and therefore should be wholly excluded from the calculation. And one sees that, for example, at D2.1, tab 3, page 547, paragraph 615.

If you could read 615, the point is clear in that. He says "exclude costs relating to provision of credit".

Hopefully you will immediately see the problem with that approach when one thinks of the Rochet and Wright article. The whole reason why a cost-based approach is appropriate is because of the specific benefits that credit cards bring, ie they allow transactions in addition to ordinary transactions.

So if one accepts that the cost-based approach is

appropriate because of the features of credit cards, it then makes no sense to exclude any of the costs that relate to those particular features. That's one of the troubles with Mr von Hinten-Reed's approach.

Dr Niels, on the other hand, just to show you very quickly what his approach is, it is back in his first report. So that is D3, tab 3, this time at page 305. I'm sorry, 307. It is paragraph 5.89.

MR JUSTICE BARLING: Same report.

MR HOSKINS: Page 307, paragraph 5.89.

MR JUSTICE BARLING: Thank you.

MR HOSKINS: "Given the important benefits that merchants derive from these costs", that is the costs of providing credit, "in my opinion it would be reasonable but conservative to attribute at least 25% or 50% of these issuer costs to merchants."

He doesn't attribute all the costs, he says:

"... reasonable but conservative to attribute at least 25% or 50% ..."

That's a point, clearly, that's going to have to be explored in cross-examination with both experts, but it won't surprise you to learn that we submit that Dr Niels' approach is clearly preferable.

I'm almost done with exemption, but I want to finish up with just focusing on this point about some aspects

of the nature of credit card use. You have already seen Rochet and Wright's view. Let me just flag up some aspects. Again, these are bound to come up in the cross-examination.

MR JUSTICE BARLING: Can we put D3 away?

MR HOSKINS: We can put that away, sir. We will come back to it at some stage.

First point is we say that credit cards clearly do provide benefits to merchants. As we explained in the factual background section of our skeleton, long before any credit card schemes came into existence, merchants offered customers credit. Think back to all those Western films you used to see where everyone would go to the general store and get things on credit. It has been around a long time. It's been around for centuries.

The reason merchants did that is because they recognised they would benefit from doing so. They also must have recognised that the benefits of doing so outweighed the costs of doing so. What's true then, that is the reason why this started happening, it remains true today.

From the outset as well, when payment systems did come into existence, merchants had been willing to accept credit cards despite these having higher MSCs than debit cards. And the difference, the basic

difference between a credit card and a debit card is the provision of credit to the customer.

If the addition of that credit facility provided no benefit at all to the merchant, the merchants would never have begun to accept credit cards. But they did. We say just as the genesis of the initial decision to give credit and then the acceptance of credit cards despite higher costs, it was all done because it was beneficial to merchants. That remains the same today. Retailers accepted credit cards throughout the period of the claim because they benefit from doing so. The benefits of accepting credit cards outweigh the costs. To be honest, that's not really in dispute.

The case is we don't want to pay so much for accepting credit cards, not that we pay so much that they are loss-making. That is not put. And it wouldn't be correct. We know that the benefits to Sainsbury's and, indeed, many other retailers, substantially exceed the costs involved in accepting MasterCard because Sainsbury's and other retailers are willing to accept American Express, but American Express is significantly more expensive, has been significantly more expensive than MasterCard throughout the relevant period.

You can see the relevant costs of MasterCard and American Express. I'm sorry, I probably was too quick.

It is in Dr Niels' first report, D3, tab 3 at 368. Page 368, figure 7.3.

So figure 7.3:

"Actual blended ...(Reading to the words)... at Sainsbury's."

The red is Amex, the blue is MasterCard.

And you will see the differential in the different respective costs to merchants of Amex and Sainsbury's. We know, it is in the evidence, that Amex is less widely accepted than MasterCard and Visa.

So if a merchant decides to accept Amex, it must be because it believes the benefits outweigh the costs. The costs of Amex are materially higher than the costs of MasterCard, so it must follow that the benefits of accepting MasterCard outweigh the costs of doing so.

Put it another way, Sainsbury's must believe that it will have higher sales through accepting American Express than through not accepting American Express. It must believe it will have more sales through accepting MasterCard than not accepting MasterCard.

I'm going to come back to Dr Niels, so let's put him on one side. Second point is that what Mr von Hinten-Reed says in relation to this is he says, well, that's just transaction stealing. By offering credit, a merchant merely obtains a transaction that

would otherwise have taken place at a competitor who doesn't accept credit cards.

But with respect, that's a bad point, and the reason it is bad is explained by Dr Niels at page 297 of this first report at paragraph 5.49. So we are at D3, 3, page 297, paragraphs 5.49 to 5.53, if I could ask you to read that, please.

You see the point, the decision to accept or not accept a particular type of credit card is just part of the competitive process. Just as much about decisions on opening hours with the costs that entails, about provision of parking, advertising spend; it is just part of the competitive process because if you don't accept credit cards, then you will lose some sales to competitors who do.

MR JUSTICE BARLING: It is an odd thing to call it, I must say, "business stealing" because that's what competition is.

MR HOSKINS: Precisely.

Third point, again, let's stay in Dr Niels and we will go over the page to 299 at paragraph 5.59. If I could ask you to read that, please.

This relates to a category of sales, nothing to do with transaction stealing. This is a category of sales that wouldn't take place at all absent a credit card and

provision of credit, and those are sales where the cardholder ultimately defaults.

Therefore, there's a situation where a customer who ultimately cannot pay for the purchase means that it is a purchase that would not have taken place otherwise, because the purchase could not have taken place without the provision of credit. So it generates additional sales which would not otherwise have happened.

If the merchants provided credit themselves, they would get the benefit of these sales, but they would bear the costs themselves of the default.

By making credit available to customers through the acceptance of credit cards, the merchant gets the benefit of the incremental sale and, under the current MasterCard scheme, gets default protection. But default protection has a cost.

If we go to page 291 of this report, you will see table 5.1:

"Results of EDC pay later credit card cost studies for the UK."

So these are the cost studies that were done for MasterCard that it used to set the MIF. But we are just here looking at the results of those cost studies. This is confidential. So I have got to be a bit careful with it. But you will see the costs involved in

cardholder default are those under the heading "Credit write-offs".

You will see the percentage figure. You will have in your mind the various sorts of percentages that are around for suggested level of MIFs. But the simple point is, we say, there's no justification for saying that merchants should get the benefit of these sorts of additional sales without making any contribution to those costs.

Just staying on this table, on the first day of the trial, this is transcript Day 1, page 167, line 25, Mr Brealey sought to portray the key aspects of the dispute between MasterCard and Sainsbury's about the cost-based approach as being about whether it was appropriate to take account of the interest free period, also referred to as the free funding period. And you will be aware of that, that it's normally 28 days, the 28-day period a cardholder has to pay off the credit card before interest starts to accrue.

But let's look again at the EDC costs study, so table 5.1. The costs of the interest free period are in as the funding costs, and you will see the percentage for that. You will see that that percentage means -- I can't even say it -- it is a certain percentage of the total costs. I can't say it. I will have to ask you to

do the arithmetic.

MR JUSTICE BARLING: Funding costs?

MR HOSKINS: Funding costs. You will see the total ad valorem interchange costs at the bottom, and you will see how much of it is made up of funding costs.

We say really that Mr von Hinten-Reed's approach should fail unless he can persuade you that no account should be taken of these relevant costs, including default costs, whatsoever because he excludes them.

MR SMITH: Mr Hoskins, this debate, in a sense, drags us into why cardholders use cards and which sort of cards they use in preference to other forms of payment. And obviously we are getting a lot of speculation about that.

Isn't there some sort of survey evidence or data done by someone, possibly MasterCard, which gives us insight into what actually cardholders think when they are --

MR HOSKINS: Think about what, sir? Sorry, so I can answer your question.

MR SMITH: For example, we have been talking about why it is that credit may be advantageous to cardholders and whether one might use a credit card rather than a debit card, and it occurred to me that some insight into cardholders' thinking might assist us in working out

whether, as Mr von Hinten-Reed suggests, all the provision of credit does is enable one to buy now but pay later and that in the medium term aggregate demands stay at the same level, or whether there are other forms of thinking on the part of cardholders which might assist us.

MR HOSKINS: There's all sorts of surveys, and we see some of the issues, for example, about whether over a long term credit cards generate more sales than etc, etc. Whether there's that particular type of evidence, I'm not sure. I don't think, if there is, that it is before the Tribunal.

The reason why we get to where we are by looking at it through the rubric we are is because we are in 101(3) territory, we are also in what's the exemptable level of the MIF for overcharge territory. Lots of people have looked at this over the years. It is pretty clear people have decided that the best way to try and look at this is through an appropriate proxy. The proxies on the table, through learning and experience, are MIT-MIF, and I have explained that, issuers' costs, and there was the cost of merchants writing their own credit.

The way it has come before this Tribunal, because of the accretion of learning experience, is it is MIT-MIF, or it is costs, or you could do both and see, take

a view on the broad axe.

But in a sense I'm not trying to completely reinvent the wheel, and I don't think we do have the evidence. It might exist, but it is not before the Tribunal, I'm pretty sure. There is evidence that would go to that sort of issue, but sort of indirectly through costs in relation to credit write-offs are a certain percentage etc, so you know -- whether you call that a cardholder, use that as an advantage, I can make a purchase I can't pay for and never pay for.

So there is an aspect of that in these sort of cost studies etc. But terms of what you are asking me, which is go out and say to cardholders "What are the features of a credit card you value? Is it the 28-day period? Is it the fact you can default?" probably does exist, but I don't think --

MR SMITH: Not before us, anyway.

MR HOSKINS: Mr Cook points out, for example, we have a figure for the credit write-offs and we have some figures for the extent to which customers will roll over, ie not pay off the card within 28 days. There is figures in relation to that, but they tend to be cost figures, how much is it costing, rather than subjective.

But we know that some cardholders do this, so whether one needs to say subjectively is this something

good? We know people use credit cards and roll over and pay the interest. We know that people use credit cards to buy something they don't currently have money for and then they discover, or they know already when they make the purchase, they are not going to have it in 28 days' time, but they want things. We know all these things happen, but we don't have that subjective evidence --

MR SMITH: It just crossed my mind in terms of the transaction stealing point that there might well be a class of transaction where, because of the monetary amount involved, you would want to pay by way of card, but that the nature of the purchase is actually a luxury and not a necessity. So you actually wouldn't buy that particular good but for having a credit or debit card. But if we don't have it --

MR HOSKINS: I had this yesterday, you both put points to me. One of my favourite ones against me. And I sort of discouraged you both from going beyond the evidence, because part of the trouble with this case is you have seen how people have grappled with these problems over the years. I could start speculating with you about things that help me and you could start speculating with me about things that don't help me etc, but I'm trying to make this as objective as I can.

That's why the exercise I'm currently engaged with

is on the evidence we have, what are the particular issues that arise. And I'm encouraging you, can't stop you, to find on the evidence rather than -- and I accept it's part of decision-making, you can go and speculate and say "We think it is fair to assess on the basis -- you may well end up doing that. But I'm really keen to try to say let's stick to the evidence before us and be as objective as possible, and that may work in my favour or against me at the end of the day but I'm trying to keep it manageable for that reason.

MR JUSTICE BARLING: I don't know whether you are leaving table 5.1 now, but I wasn't quite sure, were you intending to make any comment? As well as drawing attention to the funding costs percentage, are you making a relative point as between that and credit write-offs, or were you simply pointing to the fact that funding costs are at that percentage?

MR HOSKINS: No, the point was that Mr Brealey focused on funding costs as being the important cost in relation to credit cards, and I'm saying actually it's not the feature that's the most important.

MR JUSTICE BARLING: These EDC cost studies, I can't remember now because it is some time since I read this, is that in dispute, or are these generally --

MR HOSKINS: I'm not sure, because our evidence -- because

one of our witnesses goes into quite a lot of detail about how these cost studies were produced, and he will be cross-examined --

MR JUSTICE BARLING: It is not obvious yet.

MR HOSKINS: It is not obvious if they are agreed, no.

The fourth point in this, and one gets this from paragraph 5.56 of Dr Niels' first report, so that is page 299, which is an obvious point really, but one sees it in the last sentence there, is that credit cards bring expenditure forward. So it is the net present value of cash points a transaction is made on a credit card, and whilst the cardholder doesn't have to pay within a 28-day period if they want to be interest free or later, indeed, they've got the benefit of credit, you'll have seen that the acquirer and the merchant get the money effectively immediately within 24 hours, or whatever it is, but the receipt of the cash by the merchant is brought forward.

Another way to look at it is whether the merchant itself had offered credit, it wouldn't get paid later, but under this system it would get the money effectively immediately.

These points I have been going through are aspects of the points that Rochet and Wright make about credit cards. They are not exactly the same, but I'm saying

that Rochet and Wright recognise the benefit of credit cards beyond debit cards and cash. And this exercise is about saying yes, and here are some confirmatory examples and some further things for you to think about when you come to consider what's the appropriate way to consider a MIF for credit cards.

Let me conclude on this point, which is what is the acceptable level of the MIF. Main points are these: if necessary, by which I mean if we ever get to the acceptable level of the MIF because we say there is no restriction, the Tribunal should wield the broad axe so as to arrive at the best estimate you can of the exemptable level of the MIF.

As I said earlier, if the actual MasterCard UK domestic MIF during the period of the claim is lower or equal to the Tribunal's estimate, then the MIF will benefit from the exemption or there will be no damages because there is no overcharge. It is the same point. But there's obviously a legal distinction there. Sainsbury's doesn't get any damages.

If the actual MasterCard UK domestic MIF during the period of the claim is higher than the Tribunal's estimate, then the actual MIF will not benefit from the exemption and the difference between the actual MIF and the Tribunal's estimate will represent the overcharge.

If you get to this stage -- we say you don't -- if you get to the stage you of course will have the subtraction sum to do. And at page 274 of Dr Niels' first report, there is table 4.1 which sets out his calculations of the weighted average MasterCard MIF for transactions at Sainsbury's during the period of the claim.

I must confess I'm not sure if this is agreed or not, but it is useful to know that so you know what figures you are working from when you need to calculate an overcharge, what figures you are dealing with.

I'm about to move on if we get to damages calculation, what's involved in that. So that is probably, if it suits you a --

MR JUSTICE BARLING: Yes, we ought to take a break. Are you going to say anything at all about the -- I think it is the Commission's point and others -- about the need to take account of the credit income, you know, the interest? But anyway --

MR HOSKINS: Well, my point on that is Rochet and Wright.

MR JUSTICE BARLING: They just say they haven't taken account of it. Somewhere I read that in their report, they say "Bear in mind our model doesn't include any ... Anyway.

MR HOSKINS: You have put a marker down. I'm not intending

to say anything about it now.

MR JUSTICE BARLING: At this stage, okay.

MR HOSKINS: I will take the point on board.

MR JUSTICE BARLING: We will take a break.

(11.40 am)

(A short break)

(11.50 am)

MR HOSKINS: I'm now moving to a part of the case which we say you should never get to, but I have to deal with it, which is damages calculation.

MR JUSTICE BARLING: Yes.

MR HOSKINS: So if the Tribunal finds that the MasterCard UK domestic MIF applied during the period of the claim was a restriction, and finds that there was an overcharge, then you are into a quantum exercise.

I'm going to deal with exemplary damages separately, for obvious reasons. But in relation to compensatory damages, the Tribunal would have to determine the following issues. First of all, what is the appropriate damages counterfactual? Secondly, to what extent, if any, did Sainsbury's pass on the overcharge in the MIF to its own customers? Thirdly, if Sainsbury's did pass on some or all of the overcharge, did this cause it to lose any sales? It is the so-called volume effect. Fourthly, what account needs to be taken of the change

in corporate tax rates during the period of the claim?

Fifth, what account needs to be taken of the fact that Sainsbury's would have received less benefits from Sainsbury's Bank -- I will explain that when we get to it -- if the MasterCard MIF had been lower during the period of the claim?

Then, sixth, is Sainsbury's entitled to compound interest or simple interest? If it is entitled to compound interest, on what basis should it be calculated?

There are issues tucked in and around those, but those are the main ones.

So dealing with the first issue, the appropriate damages counterfactual, for your notes it is addressed at paragraphs 304 to 314 of our skeleton argument. I don't need you to turn that up now.

As you are well aware, according to the basic principle of tortious damages, the claimant is entitled to be put into the position that he would have been in had the wrong not occurred, and therefore it is necessary to compare what actually occurred with what would have occurred if the wrong had not happened. So we are back into counterfactual issues.

This raises three issues between the parties. The first issue is: what is the appropriate damages

counterfactual? Mr von Hinten-Reed's position is that the appropriate damages counterfactual is to assume that if the wrong had not occurred, both MasterCard and Visa would have applied the same MIF, ie the lower MIF that Mr von Hinten-Reed identifies.

I'm not sure if that figure is confidential, because I think it was referred to in opening. It would make life easier if I could say it.

Can I just consult Mr Brealey. (Pause)

MR BREALEY: Excuse me --

MR HOSKINS: Do you want to take instructions? Sorry about this. It's just I will always have to use quite a longhand every time I refer to it.

MR JUSTICE BARLING: The shorthand is both Visa and MIF would have applied the same MIF?

MR HOSKINS: Exactly, the lower MIF.

MR BREALEY: At the moment I'm told it is, but I shall find out.

MR HOSKINS: That's fine. I wondered if I could short-circuit this.

Dr Niels considers that the appropriate damages counterfactual -- this is all sounding very familiar, I am sure -- is one where MasterCard's MIF -- on this basis we're in damages territory, so it is the one which Mr von Hinten-Reed suggests, but Visa's MIF at the

actual level that's applied. It is a similar debate.

But the reason it is significant in this context is as follows. We have got the Maestro evidence, which tells us if there was that material difference in the MIFs MasterCard would have lost a large part of its business to Visa and Amex. Transactions which actually took place in the real world using MasterCard therefore, in the counterfactual world, would actually take place using Visa or Amex.

In our damages counterfactual, the Visa MIF and Amex merchant costs are higher and therefore there's no loss. Is that sufficiently clear?

I'm sorry, yes, it is not no loss, it is less loss, and I will explain that now. Because what Dr Niels has done is he has modelled the effect on the damages claim by Sainsbury's under his counterfactual, and as a result of the switching effect this analysis is based on the fact that in the counterfactual there would be a switch from MasterCard to Visa and Amex. But that will take a period of time, and during that period of time in the counterfactual world there will still be some transactions that take place on the MasterCard lower MIF, as opposed to the higher Visa and Amex MIFs, and that will have a damages value.

We can see Dr Niels' calculation on this is -- again

back to his first report, so it is D3, tab 3 and he deals with it at paragraph 7.38 to 7.50, which begins at page 364. But you can see the conclusion he reaches on this at page 369. Actually, go to page 368. If I could ask you to read paragraph 7.50.

Then if you go over the page to table 7.3, you see that the effect of this switching exercise is that Sainsbury's total damages, which are in the region of 200 million-odd, that's what they claim, would be reduced to 55 million-odd by this effect. So it is a substantial issue.

So we hear a familiar issue of what's the appropriate counterfactual. As I have already submitted in relation to the previous counterfactuals, we say that the only basis upon which the Tribunal can find a restriction at all, that's what I submitted yesterday, is to adopt a legal fiction which ignores the reality of the market. That's my submission. By definition, if we get to this stage you have rejected that submission.

However, what we see from the Court of Justice judgment in MasterCard is you can have different counterfactuals for different purposes. Horses for courses. Counterfactuals for courses.

Our submission is that if the Tribunal is prepared to find a restriction on the basis of a legal fiction,

it would be doubly harsh, doubly unfair, if it were then also to assess damages on the basis of a legal fiction rather than on the basis of what actually would have occurred.

So don't damn us twice. You can adopt counterfactuals for appropriate purposes. If you decide that Mr Brealey's submission on restriction is an attractive one for legal policy reasons or whatever, it doesn't require you then to simply read across when you come to a damages calculation.

The second point on the counterfactual. Assume you are against me on the counterfactual and you decide to assess damages on the basis of Mr von Hinten-Reed's counterfactual. So that is his counterfactual is MasterCard and Visa at the lower level, but Amex stays at its actual level. It would then be necessary to take account of the loss of business that would have occurred, the switching that would have gone to Amex, to MasterCard. Therefore, transactions in the real world took place on the MasterCard MIF and the counterfactual would take place, some of them, on the Amex merchant fee, which is higher. So, again, that would go to reduce the damages.

We have actually seen it before, but I would like to show it to you again for this purpose, bundle D2, tab 2,

page 211, paragraph 441.

MR JUSTICE BARLING: Yes, I see that.

MR HOSKINS: It is the 5%. I will show it to you again because it comes up again in this context. Dr Niels says actually the switch would have been much higher. That is the dispute between the experts on this point and that's obviously something that will be examined in cross-examination, but I flag that up as the issue.

What would the switch to Amex have been under Mr von Hinten-Reed's damages counterfactual? The third point on the damages counterfactual is this: again, if the Tribunal chooses to assess damages on the basis of Mr von Hinten-Reed's counterfactual, then it will be required to consider what MasterCard would have done if it had been limited to setting the UK MIF at the level suggested by Mr von Hinten-Reed. And Visa is in the same boat.

MR JUSTICE BARLING: Sorry, did you have the reference to Dr Niels' -- you said it would be much higher. Do you want to give it --

MR HOSKINS: I will get it from the skeleton. I will ask Mr Cook to look it up and I will shout it out once he has found it.

If MasterCard had been constrained to adopt the lower level of MIF during the period, what MasterCard's

evidence is is that it would have been compelled to make other changes to the scheme rules. For example, changes to the payment guarantees that were offered in respect of fraud and cardholder default. It would have had to reduce the costs of the system because the MIF was lower. It would have to have introduced different rules about the timing of payment to the merchant. So rather than having immediate payment, there would be potentially some delay.

The argument is that these changes to the system would have had disadvantages to the merchants in the counterfactual, which would have to be taken account of if you are assessing damages, and put in the position you would have been if the wrong had not occurred. You have to look at what the reduced benefits would have been to merchants under the scheme, and the extra costs, therefore, they would have to bear under the Sainsbury's counterfactual.

The evidence about the changes that MasterCard would have had to make to its scheme in light of a low or zero interchange fee, if I just give you the references. First Douglas, paragraphs 60 to 70, bundle C2, tab 2, pages 38 to 41. First Perez, paragraph 17 to 52, bundle C2, tab 5, pages 80 to 90. First Tittarelli, paragraphs 5 to 55, bundle C2, tab 6, page 93. First

Willeart, paragraphs 78 to 87, bundle C2, tab 7.

MR JUSTICE BARLING: C2, tab 7 where?

MR HOSKINS: Page 136.

So in the counterfactual world, a merchant would have to bear increased costs relating to fraud, cardholder default, timing of payment etc, and those would have to be taken into account in the damages calculation.

This is me trying to simplify the flowchart. I'm going to move to pass-through now.

Pass-through. There is no dispute between the parties that pass-through is legally relevant. I don't need to go to it now, but at paragraphs 315 to 324 of our skeleton argument, we explain that English law requires the court to take account of the extent to which any loss has been passed on to customers in the assessment of damages.

That is the British Westinghouse case.

I know there is debate about the precise basis in English law about pass-through, but in our submission, British Westinghouse is a sound legal basis for recognising the principle. But equally, it would just be an aspect of you have put the victim in a position he would have been had the wrong not occurred, and therefore you take account of benefits, but

British Westinghouse is one of the ways in which you can explain why pass-through is available in English law.

Paragraph 287 of the Sainsbury's skeleton argument accepts that it is open to prove Sainsbury's has passed on the overcharge to its own customers, ie they accept that pass-through is relevant to quantification in English and, indeed, EU law. So the debate between the parties is not about whether pass-through is legally relevant, but what is the test for pass-through.

What I would like to do to show you what the test actually is is to, I'm afraid, revisit as quickly as possible the authorities which Mr Brealey showed you to show you what propositions you should take from them.

The first proposition that comes from those authorities is that national rules may ensure the remedy granted to a claimant who has been injured by a breach of EU law is not unjustly enriched. In the absence of EU rules governing such unjust enrichment, national law may be applied provided that it complies with the principles of equivalence and effectiveness.

We don't need to go to them, but I will give you the references for the proposition. Case 68/79, Hans Just, paragraph 26, bundle I.4, tab 2, page 523. Also case C-453/99, Courage v Crehan, paragraphs 29 to 30, bundle I.4, tab 5, page 97.004.

The second proposition one gets from the case law is this. National rules relating to pass-on may not apply legal presumptions or rules of evidence which place the burden on the claimant to prove that pass-on has not occurred.

That's the San Giorgio case, and I do need to go that because there are some aspects of it I would like to show you that you didn't see with Mr Brealey. It is I.4, tab 3.

What I would like to show you is actually what San Giorgio was about because you need to put the judgment in context. First of all, if we could pick it up at paragraph 2 on page 69.

We see that the case was about the fact that San Giorgio, the plaintiff, was required to pay health inspection charges which were levied contrary to community law. And the reason why this case raised an issue that went to the Court of Justice, one sees from paragraphs 4 to 5, is because the claim went through the national courts, and in Italian law there was a provision which is set out at paragraph 4 of the judgment:

"The state finance administration relied on article 10 of the particular law."

It is the second part of the quote citation from the

law.

This is legal provision:

"The charge is presumed to have been passed on, whenever the goods in respect of which the payment was effected have been transferred even after processing transformation …(Reading to the words)… in the absence of documentary proof to the contrary."

So you see it was a very onerous legal presumption of pass-on. Pass-on presumed unless documentary evidence to the contrary and San Giorgio complained that that particular legal provision was contrary to community law.

Then you come to the paragraphs that you saw with Mr Brealey, so I will take them quickly. Paragraph 12 I don't think you saw, but it sets out just the standard community right to restitution, national law, principles of equivalence and effectiveness.

You see at paragraph 14 the court's reasoning for saying that such a presumption is not acceptable:

"Any requirement of proof which has the effect of making it virtually impossible or excessively difficult …"

So it is an aspect of the principle of effectiveness:

"… to secure the repayment of charges levied

contrary to community law would be incompatible with community law. That is so particularly in cases of presumptions and …(Reading to the words)… have not been passed on, or are special limitations concerning the form of the evidence to be adduced, such as the exclusion of any kind of evidence other than documentary evidence. Once it is established the levying of the charge is incompatible with community law, the court must be free to decide whether or not the burden of the charge has been passed on wholly or in part to other persons."

There is no legal or evidential presumption of the sort that's considered in San Giorgio at play in the present case. We are inviting you to decide on the basis of all the evidence before you whether there is pass-on or not.

The third proposition that comes from the European case law is that the question, and we have just seen it in San Giorgio, whether an overcharge has been passed on in each case is a question of fact to be determined by the national court, which may freely assess the evidence.

So you see that, paragraph 14 of San Giorgio. You also saw it in Comateb at paragraph 25, bundle I.4, tab 4, page 88. Mr Brealey sought to try to put

a restriction on the ability of the Tribunal, of courts generally, to assess the evidence freely, which is clearly the principle, by saying "Ah, this is an exception, it must be interpreted restrictively". He is trying to suggest somehow your ability to freely assess the evidence had to be done through some sort of restrictive framework. But let me show you why that's wrong.

It is the Weber's Wine World case, I4.4, tab 6. It is paragraphs 95 and 96. They are on page 125 of the bundle. You will see that what the court says there is:

"As the exception, ie the pass-on, is a restriction on a subjective right derived from a community legal order, it must be interpreted restrictively. Thus, in the Bianco case the court held in particular that even though indirect taxes ...(Reading to the words)... final consumer and in commerce are normally passed on in whole or in part, it cannot be generally assumed that the charge is passed on in every case", ie the strict interpretation means you can't have general presumptions, general evidential presumptions.

But even within a need to interpret it restrictively it is quite clear, as the court goes on to say:

"Consequently, the question of 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 is free to assess the evidence adduced before it."

There is no restriction on your freedom to assess the evidence. The restriction of interpretation means you can't have general presumptions of evidence or law, but it does not curtail the requirement on the national court or Tribunal to freely assess the evidence before it.

Of course, for example, evidence as to economic theory, which one has from both Dr Niels and Mr von Hinten-Reed, is not a legal or evidential presumption. It is part of the evidence which the court may freely assess. I'm not sure Mr Brealey went quite this far, but there were shades of it. You cannot say: EU law forbids me from looking at economic theory when freely assessing where there is pass-through because the economic theory is just part of the relevant evidence. And of course, Dr Niels makes it quite clear we are not relying on economic theory to say there is a presumption that you must follow. It is simply part of the overall evidence that's before you and he makes that quite clear, and he accepts that.

MR JUSTICE BARLING: I think the point he majored on was this granted directly part.

MR HOSKINS: Which I'm coming to now.

The fourth principle, we say, that comes out of the case law is that acts unrelated to the wrong upon which the claim is based cannot be relied upon so as to establish unjust enrichment. That's my definition, if you like, of what an indirect pass-through would be: acts unrelated to the wrong upon which the claim is based cannot be relied upon so as to establish unjust enrichment.

Let me explain why I put it that way by reference to the Lady v Kid case, I.4, tab 9. Again, you need to see what the case is about because all that Mr Brealey has done is cherrypicked the word "direct" and sought to imbue it with meaning.

If you pick up the judgment at page 199 of the bundle, at paragraph 1:

"The reference for a preliminary ruling relates to the interpretation of community law and recovery of amounts wrongly paid."

Then paragraphs 3 and 4:

"By law number 840, the Kingdom of Denmark introduced a business tax known as the employment market contribution."

Then paragraph 4:

"In return for the introduction of the Ambi,

a number of social charges of employers had been abolished."

So A legislative change where a new law is introduced and certain other laws are abolished at the same time.

The argument that the state ran was because of the different legislative provisions that had been adopted. Even though the new law imposed an unlawful charge, you got a benefit, because we changed other laws at the same time which favoured you, and we can rely on that to say you have not suffered any loss. And that's what the court was dealing with when you see the judgment. Mr Brealey took you to it at page 203, and in particular paragraphs 19 and 20. When the court refused to allow the State to rely on that argument and said in paragraph 20:

"The direct passing on of the tax wrongly ...(Reading to the words)... levied in breach of European Union law," that's what it was talking about.

Denmark could not rely on other law changes which were beneficial to traders to argue that a trader would be unjustly enriched if it were repaid payments made pursuant to a different unlawful law.

You were also taken to Accor, which doesn't really add very much because it simply cited that paragraph

from Lady & Kid. I will confess it is very difficult to get to grips with what was actually happening in Accor. It is all about particular provisions of company tax etc in France, but our submission, to keep it simple, is it doesn't add anything to the definition of "direct".

Our submission is that the domestic law on passing on is entirely consistent with EU law, including the statement in Lady & Kid that only direct passing on can lead to unjust enrichment. And the quickest way I can make good that point is by reference to our skeleton argument. So that is bundle A, tab 2, paragraphs 317 to 320. That's where we refer to the British Westinghouse case.

If I can ask you just to refresh your memory on what the law said in that case. It is paragraph 319. If you could quickly read the quotes there, please. This is the domestic law.

So what one sees in English law, the principle is, one sees it in different language, but for example, it is said that we are an injured party that takes action quite naturally arising out of the circumstances in which it was placed by the breach in the ordinary course of business. That can be taken account of in quantification. That's direct. Would that action form part of the continuous dealing with the situation with

which it found itself and was not an independent or disconnected transaction? The court should take account of it in quantification. That's direct.

"Any benefit arising from the action should take into account assessment of damages in those circumstances."

It is all direct.

That is the whole point. English law is the same as EU law. That's why I put it the way I did. The proposition is to put it from the other perspective that acts unrelated to the wrong upon which the claim is based cannot be relied upon so as to establish unjust enrichment. But related acts can. They are sufficiently direct in domestic law in the UK.

What, really, Sainsbury's is trying to do here is it just picks the word "direct" out of the Lady & Kid judgment and then tries to play a semantic game with it.

But let's look, because what one gets is we get a labelling by Mr von Hinten-Reed of what he considers to be direct and indirect pass-on. And if we can just briefly look at that at D2, tab 2, page 380. Part of this is confidential.

It is paragraph 1169. You see he says:

"I define 'direct pass-on' as any increase in retail prices resulting from an increase in cost."

That is a sort of cost plus type situation.

Then I will leave you to read his indirect pass-on, because part of it is said to be confidential. It is difficult to see how on earth it could be confidential, but I will do what I'm told.

MR JUSTICE BARLING: Yes.

MR HOSKINS: I say that if we make good that form of indirect pass-on, then clearly as a matter of domestic law it must be taken into account, see British Westinghouse. And clearly as a matter of community law, your taking into account is not precluded because it is sufficiently direct.

MR JUSTICE BARLING: You say what he describes as indirect is good enough for you?

MR HOSKINS: Exactly. Don't play with the language, that's why they have set up a semantic game. Take direct from Lady & Kid, then the expert says: this is what I call direct, this is what I call indirect. So what? The legal principle is quite clear that this is legally relevant if we make good the point on the facts.

I make the point about the broad axe. You already have my submission that the broad axe should be applied to the quantification of damages. It allows you a broad discretion in the assessment of damages. I took you to the cases where both Mr Justice Rimer and the

Court of Appeal both felt it was appropriate when wielding the broad axe to err on the side of under-compensation. And when you come to look at pass-through, it is simply part of the quantum calculation so it must also be subject to the broad axe and it must also be subject to the need to err on the side of under-compensation.

Sainsbury's skeleton suggests otherwise. Paragraph 295 suggests that if the court is unable to determine the actual rate of any pass-on, then the pass-on defence must fail.

Well, that's patently nonsense, I'm sorry. It is flatly inconsistent with the broad axe, and if you applied that logic to pass-on, we can only benefit from pass-on if we prove the actual rate, then you would have to apply the same exacting standard to Sainsbury's when trying to prove the overcharge. And good luck with that, given the economic evidence before the court. So that is hopeless.

Sainsbury's skeleton, paragraph 288(c), suggests that:

"Any uncertainty as to whether the overcharge has been passed on benefits Sainsbury's."

No authority is cited in support of that proposition. And you have my submissions on the need to

err on the side of under-compensation if you are wielding the broad axe.

US law. Mr Brealey tries to pray in aid the policy decision that has been taken in US law to exclude pass-through and to limit claims in federal anti-trust law to direct purchasers. I was passed a note to point out, while Mr Brealey was making these submissions, that Sainsbury's itself was an indirect purchaser because the acquirer is in the middle and the MIF is only passed on to the MSC, which made me smile. But there is a better argument which is that US policy is irrelevant in English law and is said to be so by the Chancellor, Sir Andrew Morritt.

I will show you Emerald Supplies v British Airways. It is I2.2, tab 13, at page 1762. This arises out of the air cargo litigation. Page 1762, it is paragraph 37. You see that Hanover Shoe was raised in the context of this particular issue. It was about the ability to bring collective action, and the issue was whether you could have a collective action where your direct and indirect purchasers, who clearly had a tension between who would actually get any pot at the end of the day. And Hanover Shoe was brought before the court and swiftly dismissed by the Chancellor at paragraph 37:

"The judgment of the US Supreme Court in United ...(Reading to the words)... was a policy decision not open to the courts in England.

"For that reason alone, it demonstrates that the problems the claimants ...(Reading to the words)... anticipate are better dealt with by Parliament than by stretching the use of a particular CPR rule to accommodate cases such as this."

So you shouldn't allow US policy decisions to infect your application of the pure domestic law which we have in British Westinghouse. Put it out of your mind.

What evidence do we have in this case? Well, we have set out a summary of the evidence upon which we rely. Our skeleton argument, paragraphs 325 to 346. It won't surprise you to know I don't intend to add anything to that at this stage, but one point I do want to just quickly knock on the head is this.

For obvious reasons, and I would have done the same, Mr Brealey took great delight in saying "Look at what MasterCard submitted on pass-through in the past". Two points in relation to that. First of all, retailers are in a far better position to judge whether they have passed-through MSCs and retail costs or not.

You will see in the evidence that they did say generally they did pass through MSCs. So retailers are

far better placed than MasterCard to know whether they have passed through or not.

The second point is what MasterCard did was it was making submissions and producing reports it had commissioned in order to put to regulators who were going to make decisions. And having heard the evidence from MasterCard, or submissions from MasterCard, and the evidence saying "We believe there is pass-through", and having heard the submissions of MasterCard saying "No pass-through", the retailers say "We do pass through", the regulators have invariably agreed with the retailers that they do pass through.

So when one is looking at, well, MasterCard made submissions, they were not accepted by regulators, and I will give you one example of that.

EU Commission. Can we go to our skeleton again, bundle A, tab 2, page 263. So you will see there that MasterCard hasn't actually got far with these submissions because they weren't accepted. The Cruickshank Report passed through. The OFT passed through. The Commission passed through.

If you look in particular, this is leading to the regulation, 340(d):

"The EU's proposal for the regulation. Such interchange fees paid by acquiring payment service

...(Reading to the words)... MSCs, which merchants in turn pass onto consumers. Thus, high interchange fees paid by merchants result in higher final prices for goods and services which are paid by all consumers."

(e):

"The Commission's impact assessment leading to the regulation", the same.

These costs are passed on by merchants to consumers. And the preamble to the regulation itself, so the final reasons for its adoption, the justification for its adoption, recital 10:

"Interchange fees remain part of the fees charged to merchants by acquiring ...(Reading to the words)... incorporate those card costs, like all their other costs, in the general prices of goods and services."

So the EU has decided it is appropriate to regulate the level of MIFs because they are passed through by retailers leading to higher retail prices.

So with respect --

MR JUSTICE BARLING: That would mean you could never really get any damages in this situation.

MR HOSKINS: This is just one of the aspects of evidence. Again, I'm going nowhere near --

MR JUSTICE BARLING: "Incorporating them generally in costs, like all other costs", is that really what is being

spoken of?
MR HOSKINS: Sir, we will come to that. My point here is Mr Brealey has had his fun with MasterCard's submissions.
MR JUSTICE BARLING: Yes. You are having your fun now.
MR HOSKINS: What we will do, we have a number of heads of evidence, this is one of them and you will decide at the end of the day, looking at all the evidence in the round, whether we have established the indirect/direct pass-through in Mr von Hinten-Reed's category. That's it.
The next heading in the flowchart, for your decision-making, is "Volume effects". Now, remember that this only arises if you have found there has been some pass-through, because then the issue is to what extent has this resulted in lost sales for Sainsbury's?
MR JUSTICE BARLING: Yes.
MR HOSKINS: Given this is a bit of a cul de sac, I will deal with it very quickly. It is dealt with in our skeleton argument at paragraphs 349 to 356.
There is a large measure of agreement between the experts as to how any volume effect should be assessed. There are three points of dispute. First of all, the experts disagree about the counterfactual to be applied, and it is our old friend. Secondly, the experts

disagree about the level of switching that would have taken place to Amex under Mr von Hinten-Reed's counterfactual. Another old friend. Thirdly, they disagree about the extent to which it is possible that consumers might switch to a lower priced product, but it might have a higher margin.
I won't dwell on the detail of that, I just flag it up as the third issue between you. The point to retain in your mind is that you can have lower price products with higher margins. And our submission is that Sainsbury's does and is able to flex the way it prices to control its margins, so it can make better margins on lower priced products. And I will explain in closing why that can have an effect on the volume effect.
The next heading is "Tax". Since the decision of the House of Lords in -- amazingly, I don't think it is in the bundle among all the authorities -- British Transport Commission v Gourley, it is 1956, Appeal Court 185:
"... it has been necessary to take account of the impact of taxation when assessing damages."
I know why it is not in the bundle, it is because it is not an issue between the parties.
Both experts say you should take account of tax, and nobody denies that. The reason why it is important here

is the level of corporation tax has changed over the period. The experts agree that the impact of taxation reduces the size of Sainsbury's claim in the present case.
This is confidential, but I will show you Mr von Hinten-Reed's position. So that is the most conservative position for our purposes. It is the addendum to his second report, so it is D2.1, tab 6 at page 763. This is all confidential, so I will tread carefully.
If you look on page 764 at table 4.5, you can see that his calculation of the effect of taxation, you will see the figure at the bottom of that table:
"Total pre-tax damages, including tax effect," which actually means not taking account of the tax change. And you will see the figure there and then the figure above is total post-tax damages, and you will see the figure there.
So you will see that it makes a sizeable difference to the claim, and obviously that has to be taken into account.
MR JUSTICE BARLING: Sorry, where was the second one?
MR HOSKINS: Sorry, table 4.5.
MR JUSTICE BARLING: I have got that.
MR HOSKINS: The last two figures, there is a difference,

what he calls total pre-tax damages.
MR JUSTICE BARLING: Yes.
MR HOSKINS: And total post-tax damages.
MR JUSTICE BARLING: Yes.
MR HOSKINS: The difference between them --
MR JUSTICE BARLING: The language is slightly counter intuitive because --
MR HOSKINS: It is.
MR JUSTICE BARLING: -- the one that is said to include the tax effect doesn't.
MR HOSKINS: It is because of what he is calling -- the easiest way to understand it is score out the words, or ignore the words "including tax effect". You will see "total pre-tax damages", "total post-tax damages", and you get a lesser sum once you take account of the tax changes.
MR JUSTICE BARLING: That level, in principle it is agreed that it reduces.
MR HOSKINS: You will see it has a material impact on the level of damages.
MR JUSTICE BARLING: Yes.
MR HOSKINS: The maths can hopefully be worked out this side of the room.
MR JUSTICE BARLING: Yes. Are your rival figures to be found somewhere?

MR HOSKINS: Well, we have put our figures, in -- particularly it is in our flowcharts, and I will come to that.
MR JUSTICE BARLING: In your flowcharts.
MR HOSKINS: I think there may be a problem with one of them, which we are currently investigating.
MR JUSTICE BARLING: Right.
MR HOSKINS: That's why I said the flowcharts are illustrative.
MR JUSTICE BARLING: Yes.
MR HOSKINS: I'm hoping we will be able to, this side of the bench, spare you from having to do the maths. As you have seen, it is what I'm trying to do. I am trying to put you in a position where, if you are having to try to calculate damages, have a decent stab at it.
We are going to keep the addendum we have just looked at out. The next heading is:
"The effect a lower MIF would have on the benefits to Sainsbury's from Sainsbury's Bank."
Again, this is an agreed deduction:
"Sainsbury's Supermarkets benefited from the fact that Sainsbury's banks offered Nectar points to its MasterCard holders which could be used to make purchases in Sainsbury's."
If the MasterCard MIF had been lower, the Nectar

points offered by Sainsbury's Bank to its cardholders would also have been lower, and therefore there would have been less purchases in Sainsbury's as a result. There would have been less Nectar points to use for purchases in Sainsbury's Supermarkets.
So the experts agree there is a need for a deduction for that reason, but they disagree as to the amount of the reduction.
Again, just to show you the level of figures. It is in the addendum to Mr von Hinten-Reed's second report, so it is the one we have just looked at. This time it is at table 4.7, 4-7 on page 765.
MR JUSTICE BARLING: Same page, yes.
MR HOSKINS: You will see again the figures are confidential, but the table --:
"Total damages before including the impact of Nectar awards."
Then:
"The impact of Nectar awards."
Then:
"Total damages excluding the Nectar awards."
MR JUSTICE BARLING: It should be --
MR HOSKINS: Again, it is slightly difficult language. Again, you will see the value of the Nectar awards on the reduction that has to be made according to

Mr von Hinten-Reed.
MR JUSTICE BARLING: Including the impact of --
MR HOSKINS: If you take the middle figure, you will see the value of the deduction.
MR JUSTICE BARLING: Yes.
MR HOSKINS: As I say, there is a dispute as to the amount. You get the counter position from fourth Harman, D3.1, tab 7. You can get his figure from paragraph 2.25 on page 650. This is where he sets out in a table his calculation of the benefits that would be lost to Sainsbury's Supermarket of the lower MIF. So D3.1, tab 7, page 650.
MR JUSTICE BARLING: Yes.
MR HOSKINS: He sets out in the rows his calculation of the benefits that would be lost, and the figures for comparison to compare with Mr von Hinten-Reed is in the total row. It is the final one under the column "Difference GB pounds million". You will see the figure.
MR JUSTICE BARLING: Yes.
MR HOSKINS: Which I'm not allowed to say.
MR JUSTICE BARLING: Yes.
MR HOSKINS: But that's the dispute. There is to be a deduction --
MR JUSTICE BARLING: But it is a higher --

MR HOSKINS: Exactly. It is just the exact amount.
Sir, I'm conscious that if we get to this stage, you wielding your broad axe have to come up with a figure in pounds and pence. One could have a situation where, for example, you delivered a judgment, we all went away to consider it and came back and argued about the pound and pence, but it is probably not an attractive prospect to anyone. So what we have tried to do is see if there is a way in which we can help you come up with the pounds, hence our flowcharts that we appended. They are illustrative; they don't include everything.
For example, they don't include the Nectar card benefits, if I can use that shorthand, we just looked at. They are not in the flowcharts. They also don't include the extra costs that merchants would have had to bear because MasterCard would have changed its scheme if the MIF had been lower. So it would have changed the fraud protection rules, the default payment guarantee etc.
It doesn't take account of that, so the illustrative figures still have a couple of chunks taken out of them. But we put them forward at this early stage to see if there's a way in which we could help you, and say, look, if you find this helpful we are happy to refine them.
The other side said can we have the calculation and

we said of course, because it seems to us if we can come up with some sort of collaborative charts that's even better if that assists you. I must admit the Sainsbury's flowchart wasn't very helpful because there's so much missing from it. It gave you a sort of here is the highest figure, here is the lowest figure. It is not even actually the lowest figure, because the lowest figure is zero. Even if we are doing quantum there is a restriction. But if you find it useful, happy to take it further. Happy to take it further with Sainsbury's, and if you have got any indications that you want to give us at any stage as to what you would find useful in relation to the charts, obviously we will do what we can.

That is why we put them forward. This isn't really an advocacy exercise at all, those charts. It is just supposed to be seeing if we can help.

MR JUSTICE BARLING: Well, we are duly grateful, thank you.

MR HOSKINS: Compound interest, Mr Cook is going to deal with. So I will just put a marker down for that. You can slot it in.

The last point I need to deal with with you is exemplary damages. Sainsbury's claim for exemplary damages is explained very half heartedly in its skeleton, paragraphs 429 to 438. It was not dealt with

at all in opening, so I will make the usual forensic point, which is that I'm not sure whether this is being pursued and whether or not their heart is in it. What I would like to do is kill it at best, then we won't have to waste any more time on it.

The law on exemplary damages, and in particular its application in the context of competition law, has of course been considered by the Tribunal in two recent cases, Cardiff Bus and Albion Water.

Cardiff Bus is at I.6, tab 11, at page 352. If I can ask you to pick it up, paragraph 448. It sets out some of the general principles established by the law in relation to exemplary damages. For example, we see the object of exemplary damages is to punish and deter. At the bottom of that page, exemplary damages are a remedy of last resort which are not to be encouraged. And at the court's inherence, discretion towards exemplary damages must be cautiously exercised.

You see at paragraph 451, they are well known, there are three categories of cases where exemplary damages can be potentially granted, and we are in the second category, or rather we are dealing with the second category. We say we are not in it.

Sainsbury's says:

"Conduct calculated to make a profit which may well

exceed the compensation payable to the claimant."

That second category, the contents of it, is defined at paragraph 461 of the Tribunal judgment. You will see the reference to Rookes v Barnard. It actually has two limbs, so the claimant has to show two things. It has to show, first of all, a cynical disregard for a plaintiff's rights, and secondly, it has to show a calculation that the money to be made out of the wrongdoing would probably exceed the damages at risk.

Then paragraphs 480 to 490 analyse what is meant by the first limb of the test, "cynical disregard of the claimant's rights". I would like to draw your attention in particular to paragraph 484:

"On the face of it, Lord Devlin's second category is specifically aimed at the punishment and deterrence of such calculated risks. Yet we consider that, unless we are compelled to by higher authority, to impose an undertaking is an exposure to exemplary damages in all cases where a company proceeds with conduct despite there being a known risk of an infringement of the chapter 2 prohibition would be wrong."

490:

"We consider that it will only be in those cases where an undertaking is aware that its proposed conduct is either probably unlawful or clearly unlawful that

a risk can be classed as unacceptable. Whether the risk is in fact unacceptable will, in addition, depend on all the facts of the case, including for example any expected pro-competitive effects of the conduct that ...(Reading to the words)... by following a different course of action with less serious anti-competitive effects."

I'm probably not doing justice to the detail of the judgment, but at least one of you is very familiar with it.

Albion Water, same bundle, behind tab 11A. If we can pick it up at paragraph 231. And 233, you will see that, not surprisingly, what the Tribunal did in Albion Water was to adopt the approach of the Tribunal in Cardiff Bus when dealing with the first limb, cynical disregard. That's Albion Water, 231 to 233. But then considered the second limb, calculated to make a profit, that is at #356 to 365.

If I can draw your attention to 362:

"Dwr Cymru had well in mind the economic advantages that could be gained and it recognised that if it could justify such an approach, that was likely to protect its existing revenue."

363:

"However, the case law cited above shows that it is

necessary for there to be some additional evidence not only that the defendant was motivated by the desire to make a profit or avoid a loss of revenue, but that there had been some weighing up or balancing of the likely gain against the likely loss in terms of having to pay compensation to the claimant."

364:

"In the present case, there is no evidence before us that Dwr Cymru or anyone else in Dwr Cymru weighed the risks of going ahead with the first access price against the likely downsides."

365:

"We recognise the point made that if it had turned its mind to the question of whether any benefit would outweigh compensation, it would have realised that the maximum compensation payable to Albion would be a subset of the money they made in the interim," ie it would have made more money. "We do not regard that as an ...(Reading to the words)... thought about it."

Then the conclusion at 366:

"We have concluded that Albion's claim for exemplary damages must fail on two grounds."

If I can just ask you to read (a) and (b), please.

We deal with the application of the evidence, the facts of this case, in our skeleton argument, paragraphs 390

to 410. But let me just encapsulate the main points.

We say the application for exemplary damages is hopeless. We rely on the points in the skeleton, but let me just take it shortly. In relation to the first limb, cynical disregard, there is no basis in the evidence to support a finding that MasterCard acted with cynical disregard of Sainsbury's rights. This is not a case where MasterCard sought to conceal its conduct. It notified the domestic UK MIF to the OFT in 2000. And the OFT's infringement decision was unsustainable and was overturned by the Tribunal.

The Commission has never considered the legality of the UK domestic MIF. On the contrary, as I have shown you, the Commission has indicated that national courts and competition authorities are best placed to consider the legality of the domestic MIF.

Of course what we have in the UK is the Maestro experience. It is a particular characteristic of the UK market. It has not previously been considered by any court or regulator. Whether you agree with my submissions or not, I hope you will at least see, I hope you will agree with me, but I hope you will agree that the point, the argument we are making is a strong one, whether you like it or not.

But this is not a case where MasterCard is simply

putting up a hopeless or artificial legal argument to justify conduct over a period of years. This is a genuine and strong legal argument. We go back to the counterfactuals: what would MasterCard have done? Because it has been said it should pay exemplary damages for cynical disregard. If MasterCard had lowered its credit card MIF during the period of the claim, it would have lost the market share. Forget the context of that about objective necessity, restriction etc. Just on exemplary damages, has MasterCard acted with cynical disregard due to the need to compete with Visa by having the level of MIF it had? This is clearly not a case that satisfies the first limb.

On the second limb, equally, there is no evidence to show that MasterCard ever addressed its mind to whether the likely profit it would make from setting the UK MIF at the level it did would exceed any potential damages.

You have seen from Albion that that's necessary. An actual addressing the mind to that issue. So we will see, but in our submission, really we hope not to hear from exemplary damages again because there's nothing in it.

You have Mr Cook to entertain you after lunch.

MR JUSTICE BARLING: We look forward to that.

MR HOSKINS: Unless you have any further questions?

MR JUSTICE BARLING: No, we will see you at 2 o'clock.

MR HOSKINS: Thank you very much.

(1.00 pm)

(The short adjournment)

(2.00 pm)

MR HOSKINS: Don't worry, I just have one reference to give you.

MR JUSTICE BARLING: Oh yes.

MR HOSKINS: It is the evidence from Dr Niels to show that the switching from MasterCard to Amex would be more than 5%.

MR JUSTICE BARLING: We left a space for that somewhere, right.

MR HOSKINS: It comes up, for example, in the damages counterfactual and I took you to Mr von Hinten-Reed. It is at paragraph 144/141.

MR JUSTICE BARLING: Yes.

MR HOSKINS: Anyway, the counter figure for switching to Amex is first Niels, paragraph 7.27 and then there is a diagram called 7.2 and it is bundle D3, tab 3 at 362. It is not a figure as such, it is a graph that plots the switch.

MR JUSTICE BARLING: Thank you very much.

MR HOSKINS: Mr Brealey has a housekeeping point.

MR JUSTICE BARLING: Right.

Housekeeping

MR BREALEY: It was just the witnesses we were debating, and I just need to get that sorted if I could to let people know.

So next week we have Monday as a non-sitting day.

MR JUSTICE BARLING: Hang on, let's just ...

MR BREALEY: No witnesses. It is not a non-sitting day, but no one is coming to give evidence.

MR JUSTICE BARLING: So --

MR BREALEY: So it is a holiday or a non-sitting day.

MR JUSTICE BARLING: We can just chat among ourselves?

MR BREALEY: Read?

MR JUSTICE BARLING: So not sitting because no witnesses.

MR BREALEY: And the same applies to Tuesday morning. That's the 2nd. Then in the afternoon, I will be calling Mr Brooks. On Wednesday morning I will be calling Hannah Bernard. In the afternoon will be Mr Rogers. Thursday is, of course, free for the palace. Then Friday morning is Mr Coupe, and then that's the end of my evidence. Then Mr Scott Abrahams will be Friday pm. That is the start of the defendant's witnesses.

Mr Hoskins has been very helpful but he was going to let me know at some point tomorrow or the day after the order of his witnesses.

MR JUSTICE BARLING: In the following week after that.

MR BREALEY: The following week.

MR JUSTICE BARLING: Right. Good. Thank you for that.

MR HOSKINS: Can I just make three very brief observations on that.

We have lost a day because we had three days scheduled for cross-examination; we have now got two. I think that should be sufficient. I just want to make the point so that if we are squeezed for time --

MR JUSTICE BARLING: You have some credit in the bank, you mean?

MR HOSKINS: That's it. What a good boy I have been ... In relation to Mr Brooks, I may well not be the whole afternoon with him, so I don't want you to be disappointed if we all pitch up on Tuesday afternoon and we are not here for the whole afternoon. It may well go shorter than the half day.

MR JUSTICE BARLING: So be it.

MR HOSKINS: In relation to Mr Rogers, it is the opposite problem. If I'm not finished with him on Wednesday afternoon, and I think this is right, he would need to be able to come back for a bit of Friday potentially, or we would need to sit a bit late. But I don't want to lose that time with Rogers if --

MR JUSTICE BARLING: You do not think it is appropriate to

have Ms Bernard standing by in case you are short with Mr Brooks? You don't think there's any point in that?

MR HOSKINS: It is not my --

MR JUSTICE BARLING: I was just throwing that out.

MR HOSKINS: To be fair, we have discussed ... (Pause)

MR BREALEY: I will certainly do my utmost to find out whether she is available.

MR JUSTICE BARLING: It is just it sounds as though Mr Hoskins has reason to believe he doesn't need two hours, or two hours and a quarter with Mr Brooks. If it is significantly shorter than that in all probability, like if it is only an hour, I don't know, it might be worth thinking about if it is --

MR BREALEY: She is no longer employed at --

MR JUSTICE BARLING: I see. So is she is not here anyway.

MR BREALEY: I would have to go back and just check, that's the only thing.

MR JUSTICE BARLING: The danger would be if Mr Hoskins takes longer than he thinks, she will have to come back. I will leave it with you.

MR HOSKINS: I do flag that Mr Rogers may have to come back on Friday on that basis. I will try and avoid it.

MR JUSTICE BARLING: If you get squeezed with Mr Rogers, yes.

MR HOSKINS: In relation to order of our witnesses, we are

having to just make sure, because the days have slipped a little bit when they can all fit in, but we will obviously let you know as soon as possible.

MR JUSTICE BARLING: Thank you very much. That would be helpful.

Mr Cook, you are taking over.

Opening submissions by MR COOK

MR COOK: I am, sir.

Sir, I have been left to deal with three issues: the issue of compound interest or interest, ex turpi and association of undertakings.

And I will try not to use the afternoon as a target. Once I have done those issues, I hope I will sit down, but hopefully that will be some time before the end, but I will see how matters progress.

MR JUSTICE BARLING: Sure.

MR COOK: Dealing firstly with the issue of interest. Now, Mr Brealey skipped over the issue of interest on Tuesday saying -- and it is the transcript from Day 2, page 119 to page 120 -- that the economists were agreed that interest should be compounded, it was just a question of rates.

Now, we obviously hope we won't get to the issue of interest, but if we do Sainsbury's case faces rather more fundamental difficulties than Mr Brealey would

suggest.

The starting point for interest is the statutory power to award interest, which is section 35A of the Senior Courts Act 1981. And under this provision a claimant can only claim simple interest, and the conventional practices of the courts has been to award interest, at least in pounds, by reference to the Bank of England base rate plus 1% or sometimes 2%.

And whatever the commercial criticisms that may be levelled about awarding simple rather than compound interest, that is the only approach permitted by statute.

Now, Sainsbury's rather optimistically suggest in its opening, paragraph 389, that if the Tribunal awards simple interest pursuant to the Senior Courts Act, it should do so at a rate of 5% above the Bank of England base rate. That doesn't reflect the conventional approach adopted by the courts which, as Sainsbury's itself describes in paragraph 62 of its particulars of claim, is to reflect the cost of the borrowing of claimants in general by using a rate of 2% above the Bank of England base rate. So the 5% simply at the moment, it is a swing, it is not going anywhere.

Now, MasterCard accepts that the statutory power to award interest is not the end of the story in than

following the decision of the House of Lords in Sempra Metals, it is open for a claimant to recover compound interest where it can claim and prove that it suffered actual loss on this basis.

However, this is a claim for damages and it must be pleaded and proved as an actual loss. Now, I was going to deal with the extracts from the cases from our skeleton argument which sets out the relevant passages, rather than taking you through to a number of authorities.

So if I could ask you to turn to that written openings, paragraph 359.

MR JUSTICE BARLING: Yes.

MR HOSKINS: We set out at 359 quotes from three of their Lordships in Sempra Metals, firstly, and just for the Tribunal's reference Sempra Metals is in the bundles at bundle I5, tab 1A.

MR JUSTICE BARLING: Yes.

MR COOK: As I said, I am going to deal with it from the extracts that we have quoted for the moment.

The first quote is from Lord Hope. He says:

"I also agree with Lord Nicholls that the loss on a late payment of a debt ...(Reading to the words)... compound interest [I emphasise the next words] the claimant must claim and prove his actual interest losses

if he wishes to recover compound interest as is the case where the claimants for a sum that includes interest charges."

So he must claim and prove his actual interest losses.

Then we have extracts from Lord Nicholls paragraphs 94 and 96 of the judgment, who concludes:

"The house should hold in principle that it is always open to a claimant to plead and prove his ...(Reading to the words)... payment of a debt."

We accept that is a principle that applies in relation to tortious damages as well, as we see from the next extract from Lord Scott.

He then goes on to say:

"But an unparticularised and unproved claim simply for damages will not suffice. General damages are not recoverable. The Common Law does not assume that delay in payment of debt will of itself cause damage. Loss must be proved."

Finally, Lord Scott at paragraph 132 of the judgment:

"Interest losses caused by a breach of contract or by a tortious wrong ..."

Obviously we are in that territory at least in terms of the cause of action being advanced:

"... should be held in principle to be recoverable, but subject to proof of loss."

Which is the key point I emphasise.

He goes on to address a number of other ones. These are all making clear it needs to be our particularised and proven case for an interest claim on a compound basis.

And going on in our written opening at paragraph 360, we can see from the judgment of Mr Justice Teare in JSC BTA v Ablyazov, 2013, the Tribunal's reference, that is in bundle I5, tab 2, we can see how these requirements have been followed in practice by the courts. Again, we have the relevant extract at paragraph 360 of our opening.

Now, Mr Justice Teare accepted at paragraph 4 that following Sempra Metals, the claim could be brought for compound interest, but he noted that the house emphasised the need for such damages to be pleaded and proved.

Rather than reading out those two lengthy paragraphs, if I could ask the Tribunal just to read the two of them to themselves. Then I will emphasise the final sentence of paragraph 18 to the second extract.

MR JUSTICE BARLING: Right.

MR COOK: So it's the final sentence which said:

"In the absence of a specific plea of actual interest losses, the remedy ...(Reading to the words)... This is clear guidance for trial judges which I must follow."

We say again the Tribunal should follow it. It is therefore simply wrong for Sainsbury's to suggest, as it does at paragraph 389 of its written opening, that it is open to the Tribunal to award Sainsbury's compound interest at an conventional, commercial rate.

That's simply not correct. There is no basis for the award of compound interest at some general commercial rate. In order to take itself outside the statutory provision, section 35A, Sainsbury's must plead and prove its actual interest losses.

Now, in terms of Sainsbury's pleaded case, we see this at paragraph 61 and 62 of the particulars of claim, which is bundle B, tab 2, and it is at page 31. There are two paragraphs in which Sainsbury's sets out its case.

In paragraph 61, Sainsbury's starts by asserting that it is entitled to complete compensation, whether for lost return on investments, additional finance costs or for interest losses incurred. Now, that's correct in principle. We don't disagree with it, but only if it can plead and prove those losses. And of course, there

they are raising three possible grounds of loss.

At paragraph 62 we then have the actual pleading on the basis on which Sainsbury's says it would have suffered loss, and it says:

"Over the period of its claim, Sainsbury's undertook substantial capital expenditure, including investments in new ...(Reading to the words)... In the absence of the allegedly unlawful UK MIFs, Sainsbury's would have reinvested a substantial portion of the sums claimed above in its business thereby generating further profits."

That is an assertion they would have made more profits:

"Secondly, and/or Sainsbury's would have needed to borrow less."

So that is reduction in borrowing:

"And/or raise less equity capital than it did to finance its capital expenditure and operations."

That is an argument that it would have issued less shares to its shareholders and therefore received less equity capital.

So, at that stage, it raises three possible grounds of loss: reduction in profits, reduction in borrowings and reduction in equity capital. So money advanced by shareholders. It doesn't tell us which of these are

meant to have happened or the extent of the loss said to have been suffered as a result.

We say Sainsbury's factual evidence is similarly lacking in any detail at all. We have set out at paragraph 362 of our written opening two extracts from the evidence which we say are the critical extracts, from the evidence of first Mr Coupe, and secondly Mr Rogers.

If I could ask the Tribunal to read those because they are confidential and so I can't read them out loud.

Without trespassing on issues of confidentiality, we say that this evidence, and in particular the evidence of Mr Coupe, suggests that Sainsbury's may well not have suffered any interest rate loss at all. He raises the possibility the money may have been spent in a way which would not have resulted in an interest cost arising.

What is, however, quite clear, we say, is this evidence falls in far short of identifying any specific loss by Sainsbury's based on which Sainsbury's can say it suffered a compound interest loss. And we say that's simply the end of the story in relation to anything other than statutory damages. It has not identified a specific loss and it's not pleaded and proved that loss.

Now, Sainsbury's tries to fall back on its expert

evidence, and in particular on the evidence of Mr Reynolds, in order to fill that hole. However, all Mr Reynolds does is look at the weighted average cost of capital and not even at the claimant, but at Sainsburys plc, the parent.

With respect, that does not work. Mr Reynolds cannot identify the loss which Sainsbury's Stores Limited actually suffered without evidence, which I have said is simply not there, but as a result of the UK MIF Sainsbury's Store Limited in fact increased its funding by the amount of the overcharge, and that this additional funding was obtained at J Sainsbury plc's weighted average cost of capital, if anything it would have been Sainsbury's itself borrowing at whatever its actual costs were, not some weighted average across everything it did in the business. And without any evidence, how the money was actually borrowed and without the evidence of the increases in the rates of that specific borrowing, Mr Reynolds is not looking at actual losses, he is looking at some hypothetical broad measure. And that's simply, as the case law shows, not adequate for a claim of compound damages under Sempra Metals.

We say that is simply the end of the matter and it shouldn't be necessary ultimately for the Tribunal to

get into what are undoubtedly complicated issues of disagreement between the experts about weighted average cost of capital versus average debt costs, incremental debt costs and matters of the kind, and within each calculation the appropriate way to calculate each of them.

If and when it becomes appropriate to get into those matters, they are confidential matters which will need to be dealt with in camera, so I'm not going to develop them any more today. We obviously rely upon the evidence of Mr Harman in relation to those and if it becomes necessary we will invite the Tribunal to accept his evidence. But we say fundamentally, and the reason why we have opened this today, is to make clear that there is a fundamental and very high threshold that Sainsbury's has to satisfy to persuade the Tribunal that it's appropriate to award Sempra Metals compound interest. And we say they come nowhere near to discharging that particular measure, and coming back to statutory measure that's the measure applied for all damages claims up until Sempra Metals, and it continues to be what courts throughout the land do on a day-to-day basis.

That is the issue of interest. Turning to the issue of ex turpi causa. Of course if the Tribunal concludes

there is a breach of article 101, then MasterCard relies upon that principle to say the claim is simply cut off at its knees.

Now, Mr Smith, as you rightly observed on Tuesday, what we are doing is combining both English law and European law principles there. We rely upon the English doctrine of ex turpi causa subject to the restriction on that doctrine imposed by the European Court in Courage v Crehan, namely the requirement for significant responsibility. Although I would say it is extremely open to doubt, particularly in the light of the approach taken by the Supreme Court in Apotex, whether that requirement actually adds anything to English law or whether it is simply a different formulation of exactly the same principles.

I am not sure in the end it is necessary for the Tribunal to worry about that too much. My submission would be that the English law principles on significant responsibility are broadly the same test.

We then rely upon what was originally a European law concept, but under the Competition Act 1998 is an English law concept, the concept of an undertaking in order to show the claimant in this case was party to the infringement and therefore falls within the ex turpi causa doctrine.

Now, Mr Smith, you raised the issue of attribution under English law principles. There obviously are circumstances under English law in which the actions of one party, often an employee or an agent, can be attributed to another party. We say we are simply not in that territory at all. Under competition law, it is an undertaking which commits an infringement. Therefore, we say the relevant question is whether Sainsbury's stores was part of an infringing undertaking.

Now, before I get into the detail of these issues, I would just like to put the point we are addressing in context. Since December 2012, Sainsbury's stores has been bringing the present claim against MasterCard contending that the UK default MIF is set at an excessive and consequently unlawful level. And Sainsbury's internal documents show, as you might expect, that that claim was in contemplation for some time before it was launched.

However, throughout the claim period, including from September 2012 when it was commenced, onwards and right up until today's date, Sainsbury's Bank, which was at least 50% owned by the Sainsbury's group throughout the claim period and has been 100% owned for the past two years, has issued MasterCard credit cards to all of its

credit card customers and continues to do all of its MasterCard credit card business on the basis of the default UK MIF, demanding that acquirers pay it the very charge which Sainsbury's stores is, in front of you today, saying is excessive and unlawful.

It is also clear on the evidence that no attempt has ever been made by Sainsbury's Bank to change that. There is no suggestion that Sainsbury's Bank has ever tried to agree bilateral agreements which would have reduced interchange fees to what Sainsbury's stores contends is the lawful level.

Bear in mind it is important to emphasise it is a default interchange fee, it is not compulsory, people are free to contract out of it. There is no indication that they have they have made any attempt to do so.

To put the scale of that in context, I would ask the Tribunal to turn to Mr Abrahams' witness statement. Mr Abrahams is the current employee of MasterCard formerly employed by Sainsbury's stores. And that's in bundle C2, tab 4.

It is paragraphs 22 and 24, or more accurately the tables beneath each of them, which are confidential that I wanted to take the Tribunal to. We see at paragraph 22 and the table below it the annual interchange fee revenue that Sainsbury's Bank has

received on MasterCard credit cards year on year.

The details of the specific numbers are obviously confidential, but the Tribunal can see the substantial scale of the sums that we are talking about.

If the Tribunal compares those numbers in that table to the first row, or the first significant row in the table below paragraph 24, that row records the total interchange fee is paid by Sainsbury's stores. So one can see comparing the money in to Sainsbury's Bank versus the money paid out by Sainsbury's stores, what a substantial percentage of the interchange bill at Sainsbury's stores is offset within the group by money coming in from interchange fees revenues.

What we would also emphasise is what's dealt with in the rest of table 24, which is a very substantial part of the sums being claimed. And we see that in the second substantial row in financial terms, and the third row deals with, as a percentage, what is a substantial part of the sums being claimed in these proceedings are in fact money that simply went out of Sainsbury's stores and next door into Sainsbury's Bank, its half sister and now full sister.

So that is the situation. And we now are in a position where the Sainsbury's group is challenging the legality of the UK MIF with one hand while, at the

same time, enthusiastically participating and profiting from the UK MIF with the other hand.

Moreover, a large part of that claim for damages includes money which, as far as the group is concerned, it simply paid itself. Now, there's obviously a forensic point I can make here about whether the Sainsbury's group really believed the UK MIF is unlawful, because if it really believed that, would it honestly still be continuing to charge that default interest rate fee?

However, we say the problem is more profound than simply a forensic point. It means that Sainsbury's claim is barred by the principle ex turpi causa. Now, I will develop why we say that's the case. While I go on to explain why we disagree with a number of the points made by Mr Brealey, I would certainly echo his comments that both illegality as a general matter of English law and its relationship with a competition law concept of undertakings are undoubtedly complicated issues.

In particular, many of the points the Tribunal will ultimately have to decide are ones on which there are no decided cases. The European cases are largely concerned with moving fines up the chain to find the person with the ability to pay them, the person with deep pockets.

Whereas the English cases to date have predominantly been in relation to jurisdiction, and therefore concerned whether or not a claim against an anchor defendant, usually a small part of a wider group, but an English company, which will therefore allow a justification for suing in England with the perceived advantage of English litigation, so people have just joined a lesser connected part of the group as an anchor defendant to allow them to bring lots of different foreign defendants here. Because those have been dealt with at a preliminary stage, as your Lordship is of course very familiar with, having dealt with it in the Dixons' matter.

All that is required to show is that there is an arguable claim against those defendants, and so a lot of the cases that have addressed this have ultimately dealt with whether the point are arguable or not, rather than actually deciding them.

The only other case in relation to this issue is that of Mrs Justice Asplin in Tesco v MasterCard, which did deal with the exactly the same issues which were in front of the Tribunal, but because it was a summary judgment application and we didn't succeed, ultimately didn't decide any of the point, she just concluded a number of matters were more than barely arguable,

which is the -- or merely arguable -- the words used -- which is the basic non-summary judgment threshold.

So that is the territory the Tribunal is in.

Sir, I'm obviously conscious that I appeared in front of you in the Dixons matter dealing with the jurisdiction point, and it is right to say from a jurisdiction perspective MasterCard would prefer a narrower approach to liability within corporate groups than it does for the present purposes.

Ultimately, the current law is not clear in relation to where the lines are drawn, and MasterCard in both the Tesco and Dixons cases has been trying to get some clarity. And ultimately, and unfortunately, it may fall to this Tribunal to provide that clarity at the moment is lacking in the case law, which I appreciate is not a helpful thing to be told, but that is, I'm afraid, the situation in which the Tribunal is in.

We set out in paragraph 412 of our written opening the four propositions that MasterCard aims to establish in this case in order to establish ex turpi causa. The Tribunal will see the four of them there.

I will deal firstly with what I suggest, the second one of those, is a relatively simple point -- they get more difficult after that -- which is whether or not Sainsbury's Bank was involved in any infringement.

Now, the basis of Sainsbury's claim against MasterCard is that the UK MIF was either the product of an agreement or concerted practice between MasterCard and its licensees, or a decision of association of undertakings, ie an association of MasterCard's licensees.

Now, throughout the period of the claim Sainsbury's Banks have been licensed to issue credit cards. It is therefore one of the licensees which Sainsbury's stores contends was either party to an agreement or concerted practices with MasterCard, or on whose behalf MasterCard was making decisions about the MIF as opposed to the MIT. On either basis, we say it is more than sufficient to show that if the Tribunal concludes there is an infringement, that Sainsbury's Bank was party to any infringement.

However, ultimately it is not necessary to show that Sainsbury's Bank was party to the agreement or was one of the associations of undertakings since it is well established law, and I'll hand up a copy of Provimi which refers to the European court cases showing it -- Provimi at paragraph 26 -- that implemented an anti-competitive agreement itself involved a breach of article 101.

So you don't have to be involved in the agreement.

If you implement the anti-competitive agreement by somebody else, that itself is sufficient. And there can be no doubt that Sainsbury's Bank has implemented the UK MIF.

We say that's more than sufficient to show that, on any view, if there is an infringement, Sainsbury's Bank is a participant in it. Then we say that, as a matter of law, I agree this is going to be a complicated matter we are going to have to go through some of the cases in due course on, in competition law, infringements are not committed by companies, they are committed by undertakings. And we say Sainsbury's stores and Sainsbury's Bank are all part of the same undertaking, and therefore Sainsbury's stores is liable for that infringement by that undertaking.

That brings me to the question which is sort of number 1 on our list, which is we say Sainsbury's stores and Sainsbury's Bank are part of the same single economic unit or undertaking. We set out the relevant case law in relation to this, what we say are the relevant points, we've set out the points, relevant paragraphs 413 to 418 of our written opening.

The starting point, and this appears to be very much common ground between the parties, we then move away from our areas of agreement, is that the test for

identifying a single economic unit, an undertaking, requires unity of conduct on the market.

This unity of conduct is said to arise in a unitary organisation of personal, tangible and intangible elements which pursue a specific economic aim on a long-term basis. For me at least, that is not a definition that is terribly helpful. What I would submit may be a more helpful definition, a more helpful way of looking at the concept, is to understand that what the Tribunal is seeking to do is determine whether companies are acting independently of each other or whether they act jointly. And that's not simply something that I'm making up.

If I could ask you to turn to Sainsbury's skeleton because it sets out again, briefly, a couple of paragraphs that they agree are significant, and we do as well, although we use them for slightly different purposes, at paragraphs 461 and 462.

461 deals with the Preinsulated Pipe case, and 462 is the DaimlerChrysler v Commission case. Both of these cases deal with the rationale for the focus of undertakings in competition law, and the Preinsulated Pipe case, as Sainsbury's says:

"The court emphasised the need to ensure that the formal separation between those companies resulting from

their separate legal personality could not pretend to find that they had acted jointly on the market for the purposes of applying the rules of competition."

What it is really saying is sometimes companies that are connected within groups will act jointly, and therefore they are seen as undertakings. And we will come back in the extract above from Hydrotherm, which explains the logical point of why competition law doesn't worry about what separate legal entities acting jointly in certain circumstances, ie when they are within a group. But therefore, the emphasis is on them acting jointly on the market.

Then at paragraph 462, the quote from DaimlerChrysler said:

"The test of whether entities were part of a single undertaking is concerned with whether those entities were adopting the same course of conduct on the market."

Then Uralita:

"The court said the essential element is whether there is unity in their conduct on the market."

This is essentially the description of the unitary organisation of personal, tangible and intangible elements. It is ultimately seeking to determine whether the companies act independently of each other, or whether they act jointly, and the rationale for that

distinction and the reason why competition law uses the concept of undertakings, rather than just simply, as we do in every other field, just saying companies are separate, is that you would normally expect companies in a group to work together and not fight each other because, frankly, the point of view of a group, that's simply wasted money taking business from each other.

What it means is you cannot have a cartel between two members of the same group because they are controlled by the same group, and therefore you would normally expect the competition between them won't happen. So you can't have an agreement between them if it's just between members of the group, which affects competition, because there shouldn't be, it is understood that there shouldn't be, any in the first place.

That is a proposition that we take -- the obvious explanation of why you use undertakings in competition law. And one can see that in the extract from Hydrotherm at paragraph 460 of the claimant's skeleton argument, matters that are familiar to the Tribunal in any way.

The final sentence:

"The requirement of article 101 is therefore fulfilled if one of the parties to the agreement is made

up of ...(Reading to the words)... is impossible."

So group companies don't normally compete and that's why they are treated as being one for the purpose of competition law. You can't have a cartel between themselves.

We say what that principle also shows is that whether Sainsbury's stores is part of a single economic undertaking with Sainsbury's Bank does not depend upon whether Sainsbury's stores exercised decisive influence over Sainsbury's Bank.

Now, certainly if one company exercised its decisive influence over another they would be part of the same single economic undertaking, and that's the very common way, particularly when you go up the chain of the fines, that the matters have been dealt with. Yes, the decisive influence will often be the useful way to determine, seek an economic undertaking.

We say that's not the only test. What that shows is when you have a triangular arrangement, two sister companies controlled by a parent, they are all part of the same undertaking and they work together because they are controlled by the same person, and so they are not going to fight each other.

But we obviously accept that common ownership is not enough. We don't start and finish and say that's the

end of the story. You need to look at how their relationships work with each other. But nonetheless the fact they are jointly owned is, we say, an important factor to be considered.

So what fundamentally the Tribunal has to look at when we get to the evidence is whether Sainsbury's stores and Sainsbury's Bank are companies that work together or work independently.

Now, we acknowledge the shoe polish example made by Mr Justice Teare in Cooper Tire, namely that there won't be a single economic entity between two companies in a group which are involved in completely different businesses and nothing to do with each other. And the example given in that case, which related to the Butadiene Rubber cartel -- and there are no doubt people in the room who know better than I do what Butadiene Rubber is, but that was the relevant cartel. The example given was if there was a subsidiary in the group that sold shoe polish. No involvement in Butadiene Rubber at all, would that be sufficient?

We accept that might well be, even if it is wholly owned and controlled outside the single economic entity, because it's simply not having anything to do with the companies that are involved in the infringement. But it is important to understand the limitations of that

principle. It is because it is involved in something completely different.

If you, on the other hand, had a shoe cartel and there was then a shoe polish subsidiary which operated in conjunction with the shoe company, so you actually got products that are closely related and they worked together, so you had people going out selling shoe polish and also extolling the benefits of the cartelised shoes, then in our submission, it would be that you can actually get a situation in which they are working together, they are acting in conjunction with each other, and so that may be insufficient.

So we say it is not simply a question of saying do they deal in the specific products. It is about whether or not they are working together and if they are all actively part of the same relevant business for these purposes.

When we come to the evidence, what we are going to submit is this is a situation where they are not looking at the shoe polish subsidiary, wholly unconnected. What we submit you will see is Sainsbury's stores actively helping Sainsbury's Bank sell financial products, including in particular sell credit cards to its Sainsbury's stores retail customers, with a structure of that credit card offering being designed to feed back

into increased sales at Sainsbury's stores.

We say decisions are being taken, as you would expect within a group, based on how they benefit the group as a whole, not based on whether they benefit Sainsbury's stores or whether they benefit Sainsbury's Bank.

So we say evidentially what you are going to see is two group companies working hand in glove for their mutual benefit, including very much in the area of credit cards, which is the essential part of the benefits that both get from it. And you heard from Mr Hoskins this morning the point about Nectar points, the benefits that arise from Sainsbury's stores. And it is common ground that without the Nectar points their sales would have been materially lower. I can't put a number on it because you will have seen those two numbers are confidential, but you were shown the two conflicting disagreement numbers this morning.

But those are sort the feedback loops that exist between the two, and we are going to say, when you have seen all the evidence in relation to this -- a lot of it is confidential, so I'm not going to develop it any further now and obviously these are matters that we are going to need to develop with the witnesses, but we say there is a list of key indicators at paragraphs 419

to 426 of our written opening and we will need to develop these points whilst the witnesses give evidence.

What we say is what the Tribunal will see is two companies working hand in glove in relation to the credit card arena for their mutual benefit, and that, we say, is more than sufficient to show they are a single legal entity and consequently they are legally responsible for the infringement which, if Sainsbury's stores is right, Sainsbury's Bank has clearly committed.

That brings me to the issue of significant responsibility, the requirement laid down by the European Court in Courage v Crehan. I would briefly like to take the Tribunal that decision which we will find in bundle I4, tab 5.

Just to remind the Tribunal, and I am sure you do remember, of the facts of Courage v Crehan, this was one where Mr Crehan was the owner of a pub and Courage was the enormous brewery chain which, among other things, owned pubs and was requiring anyone who rented a pub from it to buy beer only from Courage. And that was the beer tie problem.

So that is what the court was focused on in dealing with this. It is paragraphs 30 to 34, the paragraphs I particularly wanted to take the Tribunal to to look at the considerations that the European Court identified in

relation to the significant responsibility doctrine. If I could ask the Tribunal to read 31 to 34 and I will go back to emphasise the passages which I submit are significant.

Sir, I would emphasise in paragraph 32 the requirements to take into account are the economic and legal context in which the parties find themselves, and based on the UK Government's submissions, the respective bargaining power and conduct of the two parties to the contract.

In paragraph 33, I would emphasise that:

"Whether the party making the claim found himself in a markedly weaker position than the other party such as to seriously compromise or even eliminate his freedom to negotiate the terms of the contract, his capacity to avoid the loss or reduce the extent, in particular by availing himself in good time of all of the legal remedies available to him."

It is the availing oneself in good time of all the legal remedies we say is of particular importance in this case.

Then in the paragraph below obviously Sainsbury's would like to focus upon:

"If the sole reason is the agreement was part of a network of similar contracts which have a cumulative

effect on competition."

Then it goes on to say:

"The person controlling ...(Reading to the words)... particularly where in practice the terms of the contract were imposed on him by the party controlling the network."

We say that's not the position here. But we say when the Tribunal comes to -- at this stage, obviously introducing the arguments we are making, but we will say in due course that it is quite clear that the Sainsbury's undertaking does bear significant responsibility for any distortion of competition. And we say the relevant test -- and I will come to explain why -- is whether the Sainsbury's undertaking bears significant responsibility.

So that is a point that will be established here. We say perhaps the most significant point to bear in mind and what makes the present situation very different from Courage v Crehan is that the relevant agreement was not compulsory. Courage v Crehan, poor Mr Crehan was in a situation where he had no ability to negotiate and was compelled to accept those terms. Here we have a situation where it is not a compulsory agreement. The UK interchange fee is a default. It only applies up until the point at which somebody decides to contract

out of it and they are free to do so.

So MasterCard was not requiring Sainsbury's Bank to do its business pursuant to the UK MIF. It was always open to Sainsbury's Bank, and remains open to this very day, for Sainsbury's Bank to enter into a bilateral agreement with the acquirers on different terms.

Now, at this point I should deal with footnote 360 which loomed large in Mr Brealey's submissions on day one and which Mr Brealey completely misunderstands. If I could invite the Tribunal to make sure they have reminded themselves of what footnote 360 says.

I am just reminding myself, footnote 360 isn't confidential.

MR JUSTICE BARLING: No, it is not.

MR COOK: I'm just checking I can discuss its terms.

To be clear, footnote 360 is not dealing with any counterfactual situation. It is not addressing how the world would operate if MasterCard just operated on the basis of bilateral agreements, either on its own or with a zero default MIF, or with a low default MIF or some ex post facto restriction on pricing.

Footnote 360 concerns the actual situation in which there was a UK default MIF at the real level that was in place throughout the period. And the point we make is a simple one, which is if an issuer like Sainsbury's

Bank approached an acquirer saying "I want you to pay me less money, I want to have a lower interchange fee and we can agree on that bilaterally" then an acquirer, particularly if encouraged to do so by one of the largest retailers in the UK, Sainsbury's stores, would have of course agreed to that lower bilateral interchange fee. There would simply have been no reason for them not to do so.

Now, it is encouraging that point doesn't appear to be contested. But to be clear, the fact that you can agree a bilateral when the issuer proposes actively a lower interchange fee to the benefit of the acquirer and the merchant and, obviously, the acquirer and the merchant see the benefit of a lower fee, that tells you absolutely nothing about the operation of any of the counterfactuals in circumstances when issuers were positively trying to get higher fees, and acquirers would obviously try and get lower fees.

So the attempt to say that MasterCard is making any kind of acknowledgement of acceptance of how the counterfactual would operate based on footnote 360 is misconceived. It is dealing with the real life situation, but showing the point we say it demonstrates with a commonsense proposition, that if Sainsbury's Bank had said "Give me less money", the acquirers would have

agreed to it, particularly in circumstances where, as we know, Sainsbury's stores was on -- I'm checking whether that's confidential or not -- the terms of the relationship was such that it was a pass-through of the interchange fee so that this interchange fee was automatically passed through directly to Sainsbury's stores.

Sainsbury's answer to the bilaterals points is to put up a witness that we will hear from next week, Ms Bernard, who says she didn't know until it was raised by MasterCard in this claim that it was open to Sainsbury's Bank to negotiate bilateral agreements.

With respect, that doesn't help Sainsbury's. First, Ms Bernard does not explain why, on her evidence, she didn't know about the possibility of bilaterals until it was raised in this claim. It was raised three years ago, so there have been three years of opportunities for Sainsbury's Bank to attempt to negotiate bilaterals and bring the interchange fee down to the level which is said to be lawful.

It is quite clear on the evidence there's no suggestion that any attempt to that effect has ever been made. To this day, Sainsbury's Bank is charging the fee that is said to be unlawful. We say it is quite clear, therefore, that even on the best case on the evidence,

that there is a significant responsibility for actively pursuing the infringement that is said to have taken place.

Secondly, even if it is the case that Ms Bernard didn't know the details of the MasterCard scheme, frankly, there were people at Sainsbury's Bank who dealt with the credit card on a day-to-day basis who would have done. But even if the ignorance was more general, it would mean that the claimants, Sainsbury's, the undertaking made no attempt to consider the legal options available to it.

But Crehan makes very clear you must avail yourself in good time of the legal options available to you. A policy of Nelsonian blindness just is not good enough.

In terms of the legal options, it is also important to emphasise, as we make clear because we identify a number of factors at paragraph 433 to 438 in our submissions, that of course this claim is only commenced in December 2012 and they are trying to sue going back to December 2006. So, again, legal remedies were not pursued in good time. They were pursued six years after the start of the claim period.

So if they wanted to alter the position, they could have done so six years earlier. And there is no suggestion that any of the matters on which their claim

is based emerged at some later stage. And there were obviously, in other MasterCard claims, attempts to say people didn't know matters and those failed in front of the Court of Appeal.

Sainsbury's has never taken that line of saying it didn't know all of the important matters on which it bases its case, and therefore it could and should, in the context of the Crehan doctrine, have pursued those legal remedies if it was concerned about the matters it now raises. That indicates, therefore, it has significant responsibility under the terms of that test.

Sainsbury's also make a single-line assertion at paragraph 512 of their written opening submissions. They say Sainsbury's Bank could not have entered into bilateral agreements with acquirers when it was an affiliate licensee. Again, that doesn't get it off the hook for the last couple of years because it has been a primary licensee. But again, no explanation is given for that proposition and it simply is not correct.

Sainsbury's also argue that the MasterCard scheme rules discourage bilaterals. To be clear, we don't agree with that contention. The provision they quote is about forcing parties into bilateral agreements. MasterCard say you should not force people into bilateral agreements. That doesn't alter the fact that

it was always open to Sainsbury's Bank to propose and try and negotiate a bilateral agreement down to what it contends would have been a lawful level of interchange fee. It didn't even make the attempt.

So we say it is quite clear that the Sainsbury's undertaking has happily implemented what it contends is the unlawful MIF when it always had the option not to do so. And we identify a number of other points that, again, we are going to be developing with the witnesses. Paragraphs 433 to 438 of our written opening.

That brings me to the English law principles, and in particular I was going to go to the Supreme Court decision of Servier v Apotex and the three questions identified by Lord Sumption. And that's bundle I7.1 at tab 25.

It is paragraph 22. The Tribunal has of course already been taken to this by Mr Brealey, which sets out the three questions identified by Lord Sumption. He gave the leading judgment, which were the application of the ex turpi causa principle commonly raises three questions. What acts constitute turpitude for the purpose of this defence? 2, what relationship must the turpitude have to the claim? 3, on what principles should the turpitude of an agent be attributed to his principal, especially when the principal is

a corporation?

So turning to those three questions. In relation to the first one, it is clear from paragraph 25 of Lord Sumption's judgment and previously from the decision of the court at first instance and in the Court of Appeal in Safeway v Twigger, that a breach of competition law is serious enough to engage the ex turpi causa principle.

That doesn't seem to be in dispute. Now, at paragraph 29 of the judgment, Lord Sumption goes on to refer -- and, again, Mr Brealey took you to this in his opening -- to the principle that where there is a strict liability infringement, where there may be a recognised exception where the claimant was not privy to the facts making his act unlawful. You see that four or five lines down in that paragraph.

It is about ten lines down, I apologise:

"In such cases, the fact the liability is strict and that the claimant is not aware of the facts making his conduct unlawful may prove a reason for holding that it was not turpitude at all."

Then Lord Sumption goes on at the bottom of paragraph 29, which is a very long paragraph, to explain what the test is in relation to the application of the exception for cases of strict liability.

He says:

"It may require a court to determine whether the claimant was in fact privy to the illegality. To that extent, an inquiry into the claimant's moral culpability ...(Reading to the words)... as turpitude. This may be a difficult question, but it is not a question of degree.

"The conclusion will be a finding that the claimant was aware of the illegality or that he was not. It is a long way from the kind of value judgment implicit in the search for a proportionate relationship between the illegality and its legal consequences of the claim."

So ultimately, the Tribunal at this stage will be making a binary decision. Either there was sufficient knowledge of the facts, or there wasn't. It is not a value judgment about whether the punishment fits the crime. Illegality to some extent as always had perhaps a clear bright line approach to matters, and the Tribunal is not concerned with does it fit the crime, the question is whether there's sufficient knowledge under the strict liability principle.

We say there's simply no possible escape, and my learned friend took you to this principle and suggested he might rely upon it. We say there's simply no possible escape by reference to this principle. As

a starting point, we would say that the proposition described as arguable by Mr Justice Aikens at paragraph 31 is correct, namely that legal entities that are part of one undertaking have no independence of mind or actions of will, they are to be regarded as one.

It was described as arguable at that point. We say it is the correct principle. But even if that's not the case, there's no scope if the claimant was here to argue that either Sainsbury's stores or Sainsbury's Bank were unaware of the relevant facts. Everyone knew, it was very, very overt what MasterCard were doing. There was an Office of Fair Trading investigation into it, the Competition Appeal Tribunal proceedings in relation to it all before the start of the claim period.

So Sainsbury's stores knew that of course the Sainsbury's Bank was issuing MasterCard's credit cards. It was doing it pursuant to the UK MIF. This is not a situation where one party can say "I have simply no idea my sister company was doing this, I didn't know about it at all". All of the key facts were well known, so we're not in the kind of territory where they can escape in relation -- on that basis.

The second question or principle identified by Lord Sumption was the question of the relationship of the turpitude to the claim. This issue is one which we

say is not going to be of practical relevance in this claim. We say what it does is it relates to the question of whether the wrongdoing is connected to the basis of the claim.

To give the Tribunal an example, if I'm a burglar and I go and buy a glass cutting tool for the sake of breaking into people's houses, and in breaking into someone's house, I injure myself, in those circumstances my illegality, the fact that I'm a burglar, is closely connected to the fact I want to sue for cutting myself with my glass cutting tool. My illegality is connected to my cause of action.

If, on the other hand, I'm a burglar and I buy a sandwich for lunch because I'm hungry, the fact that I happen to be a burglar in the rest of my time doesn't mean that my illegality is connected to the fact that I would quite like some lunch. That's simply all it is doing: is there a connection between the two? And we say that's the proposition that it is dealing with.

Here we say it is quite clear that the turpitude directly connects you to the claim. The turpitude is participating in the UK MIF, charging acquirers the UK MIF, and that's directly connected to the subject matter of the claim, which is the UK MIF.

So the second principle we say is clearly going to

be met here. It is not particularly an application in these circumstances.

The third principle is one of attribution. We say that's not relevant again in these circumstances. As the Court of Appeal held in Safeway v Twigger, the basis of liability under competition law is not vicarious liability, it is the undertaking itself which commits the infringement.

So we don't have to attribute the acts to a third party. It is if you are part of the undertaking, you commit the infringement, then we say that's the end of the story. There's no need for attribution, you yourself are responsible for the actions of the undertaking of which you are a part.

Those, sir, are the reasons why we are going to say the ex turpi causa principle applies if the Tribunal concludes that there was wrongdoing on the part of MasterCard. And obviously a number of those factual points which we will be developing with the witnesses and then we will develop in closing.

Unless I can assist you, that was ex turpi causa.

MR JUSTICE BARLING: Yes.

Shall we have a break now? You have something else to do?

MR COOK: I have association of undertakings to do. It

might be a sensible moment to have a break.

MR JUSTICE BARLING: Let's give the shorthand writers a break. That is all you have, then.

MR HOSKINS: Yes, association of undertakings.

(3.00 pm)

(A short break)

(3.10 pm)

MR COOK: Sir, since this wasn't a point that, as Mr Brealey has pointed out, we have developed in our written submissions, I do have a hand-up in relation to it on the association of undertakings.

MR JUSTICE BARLING: Right.

MR SMITH: Thank you.

Mr Cook, before you move on to that we had one question on the role of an undertaking in the ex turpi causa defence.

As I understand it, what you are saying looking at the description of that defence in paragraph 22 of Lord Sumption's opinion in Apotex, you say:

"We don't need to trouble ourselves with III on what principles should the ...(Reading to the words)... the attributed."

Because that effectively is taken over by the European law on undertakings, which you have expounded for us.

I just want to be clear as to the basis on which you say that. Do you say that because the anti-competitive claim that is being advanced by the claimant is effectively based upon European law and therefore you read across the undertaking (inaudible) any defences that are run by the defendant, or do you have any more specific authority to refer us to? I notice you mentioned Safeway v Twigger.

MR COOK: Yes, in relation to that -- I will look at the question again. No, it is not because it is a claim based on the European law that we say that. I mean, obviously the claim is partly based on European law, it is partly based on the Competition Act, which is a matter of English law insofar as it is meaningful to distinguish English and European law in any event.

No, we say that applies on the basis that the question is: is there wrongdoing committed by the claimant company? And the concept of an undertaking in competition law is undertakings commit infringements and therefore the question is: is there an infringement committed by an undertaking involving the claimant?

So we simply say what we are doing is saying if they are right in their allegations against us, then we will respond by saying the Sainsbury's undertaking has committed exactly the same infringement along with us,

and so it is not so much their claim is based on anything in particular, it is that we can retaliate with exactly the same accusation against them. And having engaged illegality, we say the ex turpi causa defence simply is triggered by turpitude illegality. So provided we can point to connected illegality by the claimant company, then we are within ex turpi causa.

To some extent if their claim had been -- and it is not this case at all, but if their claim had been in a different context, most of the claims aren't as connected, in a sense people aren't retaliating with exactly the same plea back to the claimant company.

In a lot of the cases what you are doing is saying it is a claim for breach of contract, breach of tort on a very basic level, and you retaliate with yes, but you were acting illegally.

So you don't need to have, you know, an exact mirror image answer. You just need to be able to say your claim contract in tort is barred by your own wrongdoing. In our case, it so happens we are in a position to advance a mirror defence, but it wouldn't need to be.

MR SMITH: You may say it is not an oddity, but the oddity it appears to give rise to is that one then has a scope of defence, ex turpi causa defence, that is different depending on whether the turpitude is a competition law

turpitude as opposed to any other turpitude.

In other words, if it is a competition law turpitude you can say, well, the fact that the wrong wasn't that of the claimant but of the company in the same economic entity or group, that's fine. But if it were any other area of law, you would be forced down the rather different route of the English law on attribution, as Lord Sumption puts it in III.

MR COOK: To some extent we would suggest it is not so much an oddity, other than it might be said the competition law, it is unusual by using the concept of an undertaking.

So to some extent we are looking at how illegality arises, and if illegality arises however it does, it engages the ex turpi causa principle. And the competition law principle of undertakings is often helpful to groups of companies in the sense that it allows them to do things with each other that if one adopted simply a separate legal entity doctrine would make agreements between group companies unlawful. But the flip side of that is equally it means that when you structure your arrangements so that you have separate legal personality, but in reality you are a single economic business, then both or multiple parts of that entity are responsible for the actions of that group.

So we say if there is an oddity, it only is the oddity arising from the fact that competition law ignores corporate personality in a way that most but not all other areas of law don't.

MR SMITH: Is this one of your open questions that should we get to ex turpi causa we will be forced to decide? In other words, is there any authority you can point us to to say that in a competition case, in lieu of Lord Sumption's III, we apply the undertaking analysis, or is it an open question as to whether we do that or do what Lord Sumption describes in III, even in this case?

MR COOK: I believe it is an open question, yes. The cases which have applied ex turpi, and the leading one is Safeway v Twigger, and that has dealt with a situation where what happened in that case was the company was liable for Safeway stores, was liable for a competition law infringement, and what it wanted to do was sue its directors and then be able to claim on their directors' insurance policies for the amount of a fine.

That was the case that dealt with the fact that the infringement was committed by the company, and it wasn't something for which -- they are not vicariously liable for the actions of the employees. That was a case which focused on the facts that undertakings commit infringements and that the ex turpi causa principle

therefore applied, but not in a circumstance in which it was being widened out beyond the single group company. It was not relevant in that circumstance.

So it is right to say that Tesco was a case where we advanced a number of these arguments, and they weren't decided or said to be arguable --

MR SMITH: Not helpfully decided for our purposes because it was summary judgment application.

MR COOK: Yes, they weren't decided any more than some of them were said to be arguable or not.

MR SMITH: Yes.

MR COOK: Ultimately, it is a point where you will have to decide exactly this principle. And we can point to cases and say it points in a particular direction or not. But so far as I'm aware, nobody has applied ex turpi causa in this particular context previously.

MR SMITH: If memory serves, and do feel free to take us through it if it helps, Safeway v Twigger was both Mr Justice Flaux and the Court of Appeal applied the English law rules of attribution but, as you say, in a different context to this. It was as between the company or the undertaking and its employees, rather than anything else. So we don't get much help than that.

MR COOK: Oddly enough, sir, the Safeway v Twigger in the

Court of Appeal is not actually in the bundles. Safeway v Twigger at first instance seemed to me, but I looked earlier Safeway v Twigger in the Court of Appeal wasn't. I have copies of it with me, which I haven't used today, but it will be sensible because we probably will have to look at it in due course if we make sure they go into the Tribunal's bundles.

In the context of Safeway v Twigger and what was decided, and this was a case in which a different decision was taken at first instance and then by the Court of Appeal, what was done in the Court of Appeal to the best of my recollection was not to make a decision based on attribution, other than in the simple sense that obviously a company can only act through -- the company has no real personality, it only has legal personality, so it needs to physically act through somebody.

In that case, the Office of Fair Trading have decided, if I recall, that there had been an infringement by the undertaking, by the company, and the Court of Appeal concluded that the only person who can commit an infringement of competition law is a company. Well, an undertaking, so not a company.

So it wasn't a situation where you normally get with

vicarious liability, where you say: my lorry driver who I employ was irresponsible, he crashed while driving, and that is a wrong committed by him as an individual which somebody can sue him for, and then they come after me as an employer saying he was driving, he was doing what he was meant to do, he was negligent, you are vicariously liable for his wrong. And that's an attribution argument.

What they actually said was there isn't an attribution point here because there was no infringement by the individuals. An individual can't commit an infringement competition law like that.

MR JUSTICE BARLING: They were sued by breach of directors' duties, or something like that?

MR COOK: That was the claim that they wanted to advance against the directors and say: you acted in breach of a director's duties. Clearly right in the sense that that it is a breach of your duty to enter into an illegal agreement which gets your company fined a lot of money. So they were suing them for breach of contracts of employment, directors' duties, and that was the claim said to be barred by ex turpi causa.

And what they wanted to say was the infringement was by, or the wrongdoing was by the directors and therefore we wanted to sue for it. They said no, the wrongdoing

was yours, the company's, and it can only be yours, the company's, because only an undertaking can commit an infringement of competition law.

It was one that completely didn't address Lord Sumption's third proposition. That was the issue. If they had been in Lord Sumption's third proposition, then it may well be ex turpi causa would not have applied, and that was actually where the first instance judgment, which I believe was Mr Justice Flaux, the Court of Appeal differed from him on that particular issue. He said it was arguable that the claim was not barred by ex turpi causa, but the Court of Appeal disagreed with him.

MR SMITH: Thank you.

MR COOK: I will hand up in relation to association of undertakings, mostly because it involves going through a number of parts of -- it is all right. Have I handed it up?

MR JUSTICE BARLING: Yes, you have.

MR COOK: Then I got asked questions. So this addresses the association of undertakings issue response to Mr Brealey's complaint that we hadn't done so.

My intention has not been to go through it line-by-line with you because large parts of it are simply -- unfortunately, it involves a fairly detailed

analysis of bits of the Commission decision, but to set out for the Tribunal's assistance that of Sainsbury's, what we say the propositions are, and therefore why MasterCard says it is no longer an association of undertakings.

The starting point, MasterCard acknowledges, it has to acknowledge, it doesn't agree with it, that it was an association of undertakings until 19th December 2007 because that's the period covered by the Commission decision, and that was upheld.

We also accept as a matter of logic, even though we are not formally bound to, that that finding is one the Tribunal is going to follow, any court would follow, and unless and until there has been a sufficient change that the Commission's reasoning as approved by the Court of Justice is no longer applicable.

What we say is that sufficient changes had taken place by June 2009 that we were no longer an association of undertakings after that date. We advanced, as you will have seen, a sort of cascade of dates. We say we have made a certain number of changes, that is good enough. If not, we have made some more, some more, and we get to today and say we are certainly not an association of undertakings.

But in order to trace whether we made enough

changes, we need to look briefly at the Commission's reasons and those which were then upheld by the Court of Justice so I can tell you what the changes were and why we say they are good enough.

The Commissioner's decision is at bundle 2.2, E2.2. If you start at paragraph 50 in the introduction section, this is by way of a factual background section and it is setting out the facts. And the Commission then goes on to draw some conclusions from them.

I should say factually MasterCard doesn't necessarily agree with all of these propositions. They, however, are the ones that the Commission found the Court of Justice upheld, so those are the ones the Tribunal should proceed on.

I would simply like to say, one isn't normally asserting as facts these propositions. They are simply ones that the Commission found.

So paragraphs 50 to 57 set out a number of factual propositions about what was happening with MasterCard during those periods, and what I have sought to do in my hand-up is sort of summarise in a one-line sentence the points the Commission is making as taken from these various paragraphs.

Unless the Tribunal would like me to do so, it wasn't my intention to take you to every paragraph

underlining the words we rely upon for the moment. It is just showing you the key propositions that we say are relevant.

I mean, just to briefly summarise what the Commission does in these seven or eight paragraphs, it focuses on the fact that following MasterCard's international public offering on the New York Stock Exchange in May 2006, MasterCard abolished most of its regional boards, but it did not abolish the European regional board. And up until May 2006, the European regional board had been the one that took effectively all major decisions in relation to Europe, including setting, among other things, the intra EEA MIF, the cross-border MIF that was the subject of the Commission decision. And following the IPO, that power was taken away from it.

So MasterCard itself started setting the EEA MIF, rather than the European board. And one of the issues was, effectively, had we done enough that we were no longer an association of undertakings? And we said interchange is no longer a collective issue, it is done by MasterCard which is now owned by its shareholders.

And the Commission went through, and I have tried to summarise them, various points, factually at this stage, where it is just simply setting out the material that it

then relies upon to say that we were still an association of undertakings.

It then went on at paragraphs 58 to 62 to identify another key factual background point at this stage it relied upon, which is the role of national fora of member banks. And that was where you would have local banks who would make decisions. In the UK, for example, up until 2004, it was the UK banks collectively that set the UK MIF, and from 2004 onwards MasterCard took that power away from them.

The Commission focused in paragraphs 58 to 62 on the fact that there continued to be national fora across Europe making national decisions on issues like domestic interchange fees.

What we have at the bottom, just over the page, in my hand-up, paragraph 5, are just summarised what effectively you say are the key aspects of the factual background that the Commission relied upon at this stage.

Firstly, that the European board, which was a board made up of members, or largely of members appointed by European banks, decided all key issues in Europe other than interchange fees. That those powers could not be taken away from the European board by MasterCard's global board without the consent of what were called

class M directors, and those were bank-appointed directors. So appointed by the banks.

There was a class M director that was appointed by the European banks which sat on the global board and on the European board. They said that was an important flow of information between the European board and the global board, and then the powers for national fora to coordinate their business including by deciding on domestic interchange fees.

The Commission's key reasoning on association of undertakings is then at paragraphs 350 to 367 of the decision. In those paragraphs, in the bundle at 1104, the Commission lists -- I believe it is six points which it relies upon as the basis for its conclusion that MasterCard remained an association of undertakings even after the IPO.

I'm going to focus on a couple of those; this is not a matter of me cherrypicking. No doubt it will be said that it is, but the reason why I'm emphasising a couple when the Commission lists six is because that's what happened in the course of the Court of Justice process whereby effectively the reasoning became narrowed down. And in the General Court and in the Court of Justice it became focused on two particularly of those. Therefore, I'm going to focus on those two, not the ones that fell

away to some extent.

The two particular factors at paragraph 354 was the fact that MasterCard carried on to operate in a decentralised manner in Europe, and that was based on the European board maintained as the decision-making body. That is based on the fact that the European board carries on deciding all matters other than interchange, the Commission concluded.

So it said, can we see that at 359, key decision-making powers remain vested in bank-constituted bodies, in particular the European board and national fora.

And developing that point which is dealt with at paragraph 359 to 367, the Commission concluded, or it rejected at 364, MasterCard's suggestion that the European board had few remaining powers.

The Commission said, actually, the powers that remained were effectively all significant ones other than interchange.

At 365, it again rejected MasterCard's submission, it said the European board was plainly subservient to MasterCard's global board and said, effectively, based on past practice, it was highly unlikely the global board was going to use its powers to overrule and more importantly the powers were drafted in a manner that

fully protected the interests of the European banks and this was the role of the class M shareholder; which meant, as I summarised a moment ago, that the powers couldn't be taken away without the European banks agreeing to it through that class M shareholder.

It then went onto conclude at paragraph 381 to 393 that the intra EEA MIF was still adopted in the banks common interests. At 382 it suggested that the banks had resolved to delegate these powers, ie the powers of setting interchange fees, to a small number of bank delegates on the European board and after the IPO to the global board.

The conclusion was that the banks had delegated their powers to MasterCard to set, and again while we disagree with the proposition that we are an association of undertakings up until today's date. In the context of the ex turpi causa case, again, it is important to bear in mind that language at least in relation to the first few years of the claim where we do accept we were an association of undertakings, but the basis of the claim against us was our powers were delegated to us by the banks.

We don't agree with that analysis as a matter of fact, however, it is what the Commission found, what my learned friend relies upon. At 383 it concluded that

there was a clear and pronounced commonality of interest among the banks. I draw the Tribunal's attention to paragraph 385, which said:

"That MasterCard also ignores the fact that until 31 December 2004 the no acquiring without issuing rule obliged every acquirer also to carry out an issuing activity."

So it is now the case that somebody can be licensed to be just an acquirer or just an issuer. Up until 31 December 2004, you could be just an issuer, but if you wanted to have an acquiring business you also needed to do some issuing as well and that was the rule. But we abolished that on 31 December 2004, but the Commission effectively at that stage were saying, firstly, you only abolished it in 2004 and they went on to say, as a result, almost all acquirers are at the same time issuers and their interest in high interchange fees for the issuing part of their card business is common.

At that stage it was saying, well, you have had this rule in place and while you have abolished it, the effect is still that most acquirers have very large issuing businesses.

MR SMITH: I thought, maybe it is my misreading, that the no acquiring/issuing rule was present in the 2014 rules

that we looked at in bundle --
MR COOK: I hope not because as far as I'm aware MasterCard undertook to remove that in 2004.
MR SMITH: We better check.
PROFESSOR JOHN BEATH: Yes. I think we saw something that implied that the acquirers under new rules were a subset of the set of issuers.
MR COOK: E3.10 is our 2014 rules.
PROFESSOR JOHN BEATH: It was all blue paper.
MR SMITH: Yes, it is bundle E 3.10.
MR COOK: None of this is confidential, it is published on our website.
MR SMITH: Yes, the rule I was thinking of was rule 3.1 at page 4068 of bundle E3.10.
MR COOK: I will take instructions on that. My understanding is that's not a: no acquiring without issuing rule. That would simply be, if you have the right to issue, you must ensure you have issued a sensible number to have the right. But I will take instructions in relation to that. My understanding is the Commission records that the express provision about acquiring not issuing was abolished.
MR SMITH: Do take instructions. What it says is:
"Each principal and association licensed to use the MasterCard ...(Reading to the words)... MasterCard based

on such criteria as the corporation may deem appropriate from time to time."
MR COOK: If you give me a moment, I can probably take instructions straightaway.
The likely explanation for that is what we are looking at is MasterCard global rules. If you see underneath it says, "Modifications to this rule appear in..."
MR SMITH: Then there is a European section.
MR COOK: "... among other European regional section", and I would have to chase through to check.
MR SMITH: Because there are additional rules.
MR COOK: Yes. I can find that. If you go to page 4191. Rule 3.1:
"The rule on this subject does not apply in relation to the EEA."
MR SMITH: That explains it. Thank you very much.
MR COOK: You are quite right to identify what is indeed the no acquiring without issuing rule as such, but not in relation to the EEA.
Fortunately we have abolished the rule as the Commission recorded, but nonetheless the Commission was saying effectively it had only been abolished recently and there was a hang over effect. At that stage most acquirers had very big issuing businesses.

It was concluded as a result of that that therefore there was still a commonality of interest between acquirers and issuers and the interests of the high interchange fees was common.
At 388 there was the conclusion. Again MasterCard would certainly disagree with, but it is the conclusion which is that the global board still takes decisions on a MIF virtually on behalf of the banks. Again I would say that's relevant to the significant responsibility point. That is the case my learned friend advances, that we are doing things on behalf of the banks, including Sainsbury's Bank.
Then, 389, the conclusion is that the global board still takes account of the concrete bank's interest in setting the level of relevant interchange fees and then after the passage in bold:
"The European banks are still represented on the global board [that is through the class M director] and can thereby express their views on interchange related issues."
They were saying there was still a representative there. Those were the key aspects of the Commission's decision. If I can turn now to the Court of Justice decision, which is at E1, tab 19. The section of the Court of Justice's decision dealing with

association of undertaking is paragraphs 48 to 77, although the initial sections are simply dealing, obviously, with the arguments of the parties and we come to the important paragraphs at paragraphs 66 to 77.
Again I have sought to summarise in my hand up what we say the key aspects to the Court of Justice's decision process were. At paragraph 66 it says:
"There is a paragraph in paragraph 259 of the judgment under appeal that, in relying first on the retention of the bank's decision-making power within MasterCard and second on the existence of commonality of interest between that organisation and the bank's ...(Reading to the words)... association of undertakings."
As I said that's why I focused upon only some of the Commission's original six reasons because by this stage the European Court, it has been narrowed down to effectively in front of the General Court and now in the Court of Justice, two principal ones: the retention of the bank's decision-making powers within MasterCard and the commonality of interest between the organisation and banks on the issue of interchange fees.
Paragraph 68 then addresses the fact that MasterCard continued to operate in Europe as an association of undertakings in which the banks participated

collectively in all essential elements of decision-making and the General Court concluded that the Commission had been right to conclude the MIF reflected the bank's interest to the commonality of interest.

Paragraph 69:

"Taken together these two factors [or those two factors] summarised at paragraph 259 of the judgment under appeal effectively explained why, according to the General Court, the setting of the MIF by MasterCard continued to operate, notwithstanding the changes from the IPO, as an institutionalised form of coordination, the conduct of the banks."

Then it talks about the fact that the European banks retained decision-making powers in many other key respects other than interchange.

Again it is the focus upon those two factors, the European bank still having decision-making powers and the commonality of interests. At paragraph 71 it records that -- it is three lines up from the bottom:

"After the IPO there were indications that the organisation is in reality continuing to take account of concrete banks' interests in setting the level of the MIF."

Finally, the key paragraph, paragraph 72:

"In those circumstances, it was open to the General Court to find in the particular circumstances of the case, and taking into account the arguments expounded before it, that both the bank's residual decision making powers after the IPO on matters other than the MIF, the commonality of interest between MasterCard and the banks were both relevant and sufficient for the purposes of assessing whether MasterCard was an association of undertakings and the appeal was rejected on that point."

Those are the two, commonality of interest and European bank's decision-making powers, which are the important points which the courts concluded were sufficient at that time.

MasterCard then gives evidence to what's taken place since 2007. Of course the court judgment is 2014, it is only looking at the position up until 2007. We set out in paragraphs 8, 9 and 10 of my note the key evidence we rely upon to say matters have moved on significantly since December 2007.

Paragraph 8, I refer to the evidence of Mr Perez, who is President of MasterCard Europe, dealing with changes in MasterCard's governance since 2006 and the reference I have given there for his statement is at bundle C2, tab 5 and the relevant paragraphs.

Again, I will just emphasise what I say is the significant evidence, that between September 2008 and June 2009 MasterCard withdrew all of the specific authorities previously granted to the European board. Since June 2009 the European board has had no powers. Again, we say, that's one of the key aspects -- probably the key aspect the Commission relied upon for the fact that the European board kept all the powers other than interchange, it concluded. Since June 2009 the European board has had no powers.

Paragraph 8 of his evidence:

"Pursuant to the terms of MasterCard's charter, in June 2008 all shares of class M stock ceased to exist and the concept of a class M director was therefore removed."

Again the class M director point was the fact there was a bank appointed director, which sat on the global board and therefore could pass-on the views of the banks in relation to interchange. That concept of the class M director was removed in June 2010.

Then paragraph 11 records the fact that we took away the power of the UK banks to set the UK MIF in 2004. The residual decision-making powers were removed in April 2014 and the position in relation to the UK is also addressed by Mr Douglas who was a member of

MasterCard's UK executive management team from 2009 to 2014 in his statement, bundle C2, tab 2.

The key paragraphs are 71 and 72 summarise what we say the key evidence is, that Mr Douglas explains the banks had very few residual powers to set scheme rules prior to 2014 and that those residual powers were removed in April 2014.

The other evidence we rely upon is that of Dr Niels, who has analysed changes in the UK acquiring market. I've given the reference there to Dr Niels' report. This shows what has happened, particularly in 2009, as a result of banks selling off their acquiring operation, so most of the key acquirers in the UK are now stand alone businesses not owned by big banks. Not true of all of them. Barclays still has a very significant acquiring business, but as Dr Niels shows there:

"The majority of the UK acquiring market since 2009 have been held by acquirers who don't have an issuing business at all."

Again the commonality of interest point that the Commission made based on the residual effects of the no acquiring without issuing rule, we say, in relation to the UK, that is unwound by 2009.

In short we say key factors the Commission relied upon, which were upheld by the Court of Justice, that

was relevant in its judgment, ceased to apply. The European Court has no powers; the class M directors ceased to have a role; the UK banks haven't had a power to set the UK MIFs since 2004; their residual powers were removed in April 2014; and acquirers, the majority of the market is held by stand alone acquirers. Based on that we say we are no longer an association of undertakings.

Obviously there's going to be a question about whether the changes we have made have been significant enough and there is a rolling process where we say, by June 2009, it was enough, if not, by June 2010, when we got rid of class M directors and, if not, it is when we got rid of the residual powers of the UK banks. That is the rolling process. That's why we say the analysis no longer applies.

It is no doubt going to be suggested that this is all very artificial. We are drawing lines between when MasterCard was an association and at some point it moves from being an association to not. We say that's very artificial. The reality is here that MasterCard has been going through a process of radical change of which the IPO was the starting point. Historically MasterCard was a members organisation. It was owned by its banks and in that period it was doing as its owners told it to

do. Since the IPO we have been owned by the general public on the New York Stock Exchange. There were class M shares held by former banks, but those were gone in 2010. So we are owned by the general public and controlled by our shareholders. We are not, therefore, owned and controlled by the banks, and we say that is a rolling process. The Commission concluded and the court upheld we hadn't done enough to be quite -- to stope being an association of undertakings in December 2007, and we say that process has been continuing as we effectively did divest ourselves of some of the residual parts of having been a members organisation and we are no longer an association of undertakings.

Really what the Tribunal needs to think about is not the artificiality of: at some point we go from being an association to not being. What the Tribunal needs to do is say: if you look at the present structure, if MasterCard had always been structured like this, could it seriously be suggested that we were an association of undertakings? It has never been suggested that American Express, which has always been a company held by the public on the Stock Exchange, is an association of undertakings and we say MasterCard has now reached that stage where it is very similar and it should not be

analysed based on its previous history and the fact that inevitably at some point, when you have a binary state of being or not being an association of undertakings, it may seem artificial to say we have moved, but if you look to analyse our structure now where not acting on behalf of the banks, we are not controlled by them, and consequently we are not an association of undertakings in that sense. Those are our submissions in relation to association of undertakings.

Unless I can assist the Tribunal further.

MR JUSTICE BARLING: The only thing is, is it all a bit academic? I mean you are all linked together by the banks, by these licence agreements via the rules, why does it matter whether you are an association of undertakings or you have just got a set of agreements that make provision for these things or even a concerted practice? Are you going to say much about that at this stage?

MR COOK: Sir, to be fair, we had not planned to say a great deal in relation to the argument about agreement to concerted practice. We don't admit it. It is a matter that my learned friend will have to prove and establish to you.

We do consider factually the analysis of the association of undertakings is wrong; MasterCard is not

acting on behalf of anybody else, it is an individual. If my learned friend persuades you that the agreement point is sufficient then --

MR JUSTICE BARLING: Don't we have to deal with it though? It is just a mechanism, isn't it, for coordination and there is no issue that you are coordinated because that's what rules are for, so why does it matter? It is a genuine question.

MR COOK: Sir, it does matter to MasterCard whether you say we are an association of undertakings. It matters in the context of, to be honest, the level of fines that might be imposed in the circumstances if we are to be treated as acting on behalf of all the banks and their turnover is brought within it. That is a point -- MasterCard challenges the idea that we are part of an association of undertakings. We don't make any admissions in relation to any other parts of the analysis. My learned friend will have to satisfy you that the concerted practice or agreement point arises.

We don't factually make any points in relation to that beyond what we said here, which says MasterCard is not acting on behalf of the banks, it is making its own unilateral decision now not because the banks are telling it to do so. So we do very much challenge the association of undertakings point and we are not making

any admissions in relation to the rest of the analysis.
MR JUSTICE BARLING: Thank you very much.
MR COOK: I think we said lunchtime on Tuesday?
MR JUSTICE BARLING: I think it is. All right. Thank you all very much and we will hope to see you then. We will start at 2 o'clock on Tuesday?
MR BREALEY: Yes, my Lord.
(4.00 pm)
(The court adjourned until 2.00 pm on Tuesday, 2nd February 2016)

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