IN THE COMPETITION APPEAL TRIBUNAL 1517/11/7/22

Salisbury Square House
8 Salisbury Square
London EC4Y 8AP

Monday 24 March – Friday 4 April 2025

Before:

The Honourable Justice Michael Green
Ben Tidswell
Professor Michael Waterson

Merchant Interchange Fee Umbrella Proceedings

A P P E A R AN C E S

Matthew Cook KC, Sonia Tolaney KC & Owain Draper on behalf of Mastercard
(Instructed by Jones Day and Freshfields
LLP)

Daniel Jowell KC, Jessica Boyd KC, Isabel Buchanan, Ava Mayer & Aislinn Kelly-Lyth
on behalf of Visa (Instructed by Linklaters LLP and Milbank LLP)

Kieron Beal KC, Philip Woolfe KC, Reuben Andrews, Flora Robertson & Oscar Schonfeld on behalf of
the SSH Claimants

Thursday, 27 March 2025

(10.30 am)

MR COOK: Good morning, sir.

THE CHAIRMAN: Good morning.

MR COOK: I call Ms Webster.

THE CHAIRMAN: Yes.

MS RACHEL WEBSTER (affirmed)

THE CHAIRMAN: Thank you, Ms Webster.

Examination-in-chief by MR COOK

MR COOK: So Ms Webster, do you have hard copies of your reports in front of you?

A. I do.

Q. Good, okay.

I think also we were going to prepare a cheat sheet for you in relation to the names of the three acquirers. Has that been --

A. I have just written them down --

Q. Okay, good.

A. -- based on the labelling from yesterday.

THE CHAIRMAN: Yes. So we are going to stay in open court for the time being?

MR COOK: We are at the moment, I understand, sir, but I think my learned friend says we are going to be in closed quite rapidly.

THE CHAIRMAN: Oh, okay.

MR COOK: It was more just making sure there is a document that is handwritten in front of Ms Webster, I wanted to make sure I had observed what it was before anyone else asked.

THE CHAIRMAN: All right, yes.

MR COOK: So Ms Webster, if we could go to your first report, which is in the bundle at {RC-F1.3/2/1}, and if we could go to {RC-F1.3/2/197} of that, which is your expert declaration. If we could then turn over the page {RC-F1.3/2/198}, is that your signature?

A. Yes.

Q. Are there any corrections you would like to make to that?

A. No.

Q. Does that still represent your full and complete professional opinion?

A. Yes.

Q. Thank you very much.

If we could also have up -- then turn up on the screen {RC-G1.2/1/1}, please -- sorry, {RC-G1.2/2/1} it will be.

Again, is this your reply report in these proceedings?

A. Yes.

Q. If we could turn on that, please, to {RC-G1.2/2/149}, is

that your signature?
A. It is.
Q. Are there any corrections you would like to make to this report?
A. No.
Q. Does that represent your full and complete professional opinion?
A. Yes.
Q. If we could also have up on screen {RC-Q5/4/1}, please.
These are some charts that you have prepared by reference to acquirer B data, and we are in open, so we should refer to them on those terms, and -- well, firstly, can you confirm that these -- that there are no corrections you wish to make to them and these represent your full and complete professional opinion?
A. They do.
Q. Please could you just tell the Tribunal what these graphs show, in your opinion?
A. Yes. So my team produced these charts following the response that we received to the experts' questions, it was a response from acquirer B, which we received the day of submission of our reply reports. In that -- in those responses, acquirer B confirmed, or set out the treatment of how they classified UK-EEA transactions following Brexit, and my understanding of that response

to the experts' questions was that from January 2021, UK-EEA transactions would no longer be recorded as intra-regional transactions in the data -- in their data. So my team produced an analysis of transactions in the intra-regional categorisation within acquirer B's data and that is what this -- these charts show.

So the first charts show, for both standard contracts and contract type called -- am I allowed to say? It is not ... PTC, that is the totality, I understand, of non-cost-plus contracts for acquirer B. It shows a drop off in the volume of transactions from sort of between 7.5 and 10 million.

Q. Just to avoid the double negative point, non-cost-plus is basically blended?

A. Yes. Yes. So --

Q. So what do you take, therefore, from that graph?

A. So this -- these graphs seem to me to be consistent with the response that we received from acquirer B saying that there had been a reclassification of UK-EEA transactions because there is this sudden fall off in the volume of such transactions, of intra-regional transactions, from January 2021. What they don't -- these charts don't show is sort of where those transactions have been reclassified, and I don't think we know the answer to that question, but clearly they're

no longer within the intra-regional classification.
Q. So in relation to anything that is left in intra-regional, what are your views in relation to that?
A. So it would mean that whatever transactions are left, they're clearly a small subset of the transactions that were there, and -- well, it could mean that they are not UK-EEA transactions that are left. I think that's one point we don't know, and it's not possible to discern that from the data. Even if they were UK-EEA transactions that somehow have been left, I wouldn't think that they -- well, I would be concerned that they may not be representative of the full set of intra-regional -- sorry, UK-EEA transactions, which would be the ones that one would wish to analyse for a purpose of pass-on for a Brexit event.
MR COOK: Thank you very much, Ms Webster.

Cross-examination by MR WOOLFE

THE CHAIRMAN: Mr Woolfe.
MR WOOLFE: Good morning, Ms Webster.
A. Good morning.
Q. Now, we are going to actually start off with some matters of economic theory. We spent a long time in Trial 2A on your benchmark case, we will not be spending anything like that length of time today.
I am sorry, Professor Waterson.

Can we go, please, to {RC-F1.3/2/50}.

Here, you form your expectations of economic theory based upon the same benchmark case which you relied upon for the purpose of Trial 2A, did you not?

A. Yes.

Q. You recap your four cumulative conditions, you say they are cumulative at paragraph 4.20. So can we just go over the page, please, to {RC-F1.3/2/51}. Rather than me read it out, perhaps if you and everybody else can just read those paragraphs, (a), (b), (c) and (d), but those are your four conditions.

Now, as I understand, the two conditions --

THE CHAIRMAN: Do you want to just give us a chance to read it?

MR WOOLFE: Sure.

(Pause).

The two conditions that you query whether they apply in the context of acquirer pass-on are the first condition, which is commonality of interchange fees and out-of-market constraints, and the second, which is merchants -- the degree to which merchants' price sensitivity changes in response to price. I just want to take those in turn, but you essentially think the conditions (c) and (d) you have here are fulfilled; is that right?

A. Yes.
Q. Now, in terms of the first condition, which is commonality of costs and out-of-market constraints, I think when we looked at this in Trial 2A you agreed this is essentially about inelasticity of demand; is that right?
A. Yes, I think it combines inelasticity in market demand, which is, if there is no out-of-market constraint, then I would expect market demand to be inelastic, and it combines that with a commentary on the degree of competitive intensity. So if one were to find that there is a material out-of-market constraint, then the intensity of competition within the market becomes important.
Q. Right. But your evidence is that if there is not a significant out-of-market constraint, so market demand is inelastic in that sense, the intensity of competition is not so important; that is your view?
A. That's correct.
Q. Now, if we turn to what you actually query about this, can we go to {RC-F1.3/2/52}, please, paragraph 4.25. You seem satisfied, essentially, there that MIFs are a common cost --
A. Yes.
Q. -- to all acquirers. So the aspect of your first point

that you are querying is set out at 4.26, which is whether or not acquirers faced a material out-of-market constraint?

A. Yes.

Q. Which you essentially interpret as being whether or not merchants could start doing something else other than accepting cards?

A. Yes.

Q. Now, is it -- I think it is also fair to say on this section of your report, and you explain below, that you are essentially drawing a distinction between the situation post-2015 on the one hand, where you more or less accept this condition is fulfilled, and the situation during the Merricks claim period on the other; is that right?

A. Yes.

Q. Because at the time you wrote this report, Merricks was still technically part of the proceedings?

A. Yes, that's right, and it's consistent with the position that I took in merchant pass-on is, given high acceptance of cards generally in the retail market, I would expect most cards to consider accept -- sorry, most merchants to accept -- consider accepting cards as a -- well, not to necessarily think that there is an alternative not to. So I -- in -- in this case, I don't

rule out that there might be some merchants for which it is a feasible option to not accept cards, but I think it's unlikely, in the period of the claim from sort of 2015 onwards.
Q. Yes, so actually, in terms of the claims, we have the CICC claims which are post-2015 --
A. Yes.
Q. -- so you accept this was fulfilled for that period?
Now, the merchant claims, the other merchant claims, some of those go back to 2011. But you would accept, would you not, that for most of the period since 2011, the merchants who actually accepted cards, they did not really have an option not to accept them, did they?
A. That -- that may be slightly strong. I don't -- I don't have a firm view on quite what the situation would have been in 2011. It may be more likely that there were some that didn't need to accept cards at that point, but I don't -- I think my conclusions are not sort of reliant on that.
Q. No, but the Merricks claim period went back to 1992 and you were saying there might be a difference if you go back that far?
A. That's right.
Q. But there is unlikely to be a substantial difference --
A. Yes, I agree.

Q. -- between 2011 and 2015?

Now, can we go, please, to {RC-J2.2/87/1}, perhaps we start on page 1 so you can see what the document is and then we will go to a page within it. You will recall we spent quite a lot of time on this document in Trial 2A.

Can we go to {RC-J2.2/87/252} within that document, please. Now, this was a graph in a sense produced by RBB to show how pass-on occurs, and we have a downward sloping demand curve and two upward sloping supply curves. There are two because we have a cost increase, so supply curve S is before the cost increase and supply curve S' is after the cost increase, yes?

A. Yes.

Q. So what we can see, at paragraph 6.30, RBB say:

"... with downward-sloping demand and upward-sloping supply, the market price will increase by less than the amount of the cost increase."

That is essentially because, as I understand it, the cost increase is given by the vertical distance on the -- on the left-hand axis, the vertical height difference between point A and point C, it is between the two points of intersection; is that right?

A. Yes.

Q. It goes on to say, this is at the bottom of the page, we might have to go over:

"The more price-sensitive -- or elastic ..."

If we go over the page {RC-J2.2/87/253}:

"... is demand, the greater the reduction in volume associated with a given price increase."

But then, can we go down to paragraph 6.32, please, they go on to say:

"... the extent of industry-wide pass-on in competitive markets will depend on the relative slopes, or elasticities, of supply and demand. The steeper/less elastic is the demand curve relative to the supply curve, the greater the extent to which the cost increase will be passed through ..."

They show two figures below. They say:

"Indeed, if the supply curve is perfectly horizontal (ie perfectly elastic), the predicted pass-on will be 100%, irrespective of the exact slope/elasticity of demand."

Would you agree with that?

A. Yes. I would note that these charts are all about market demand and supply, which may be relevant.

Q. Okay, yes, so it is about market demand and supply. But if you are thinking about the market for card acquiring, so the suppliers in the market are the acquirers and the customers are the merchants, one would expect supply

-- market supply to be pretty price elastic, would you not?
A. So what I would expect, and I think I've said this in my report, for any individual acquirer that is in the market, I expect it to have a marginal cost that it faces which is flat, so it wouldn't expect the marginal cost for each incremental merchant that they serve or each incremental transaction that they process, I don't expect the cost that they incur to go up as transaction volumes go up. So I think there would be a flat marginal cost curve.
I don't know about the supply curve in this instance, because that's about putting together all of the acquirers in the market and it might be that as more acquirers enter the market, they're entering with slightly higher costs of serving customers.
Q. But the existing suppliers -- the existing acquirers who are there could expand supply pretty easily, could they not?
A. Yes, I suppose that's right, yes, that's a fair point.
Q. In fact -- I think you accept that point --
A. Yes.
Q. -- if we go to {RC-F1.3/2/55} -- this is your third report, and I think that is a wrong reference -- no, this is right. So this is -- yes, this is your -- where

you deal with the third assumption, which is "Constant marginal cost and no capacity constraints". You mention the possibility, at 4.35, of "bottlenecks", and you say that you do not think there is -- I think, in 4.36, you make your point about marginal costs being the same, and you say at the end of that paragraph:

"In addition, I am not aware of any reasons to think that acquirers may have been unable to increase or decrease the amount of acquired volumes in response to changes in IFs and MSCs."

So you simply accept that we have got a highly elastic demand situation here -- highly elastic supply situation?

A. So I'm saying that the marginal cost curve for any individual acquirer will be flat and that may have implications for the market elasticity of supply, but whether or not it's entirely flat, I don't -- I don't know.

Q. Okay, so can we go back to the second point of your four conditions, the second one that you query. If you go back to -- if we go back to page {RC-F1.3/2/53} in this document, paragraph 4.29. This is about "Potential changes in merchants' price sensitivity in response to changes in MSCs". I think --

THE CHAIRMAN: You need to keep your voice up a little bit.

I think you are sort of tailing off a little bit.

MR WOOLFE: Thank you, sir.

So at paragraph 4.30, we need to go over the page {RC-F1.3/2/54}, you are saying that -- your assumption is about the shape of the demand curve over the relevant increment of price; is that right?

A. Yes, and the first part of this paragraph is in relation to merchant pass-on, so it relates to end consumers' willingness to shop around in response to a change in prices where that change in prices is related to a change in MSC cost that merchants face in the counterfactual relative to the factual.

Q. We went over this in Trial 2A, but your point was that because it is a relatively small increment of prices being considered, any change in price sensitivity would be small and we had a discussion about the shape and curvature of the demand curve --

A. That's right.

Q. -- but that is your point, essentially?

A. Yes.

Q. Whereas what you are saying here, at paragraphs 4.31 and 4.32, is that because MIFs are a much larger proportion of MSCs than MSCs are of services downstream, that there may be more of an issue about price sensitivity --

A. That's right.

Q. -- changing here.

But it is fair to say that in your first report, you said that this issue of price sensitivity is only a subsidiary factor, did you not?

A. I don't recall.

Q. Well, if we go to {RC-F/14/42}, this is your first report, volume 1 of your first report, and you -- sorry, 42, not 32.

THE CHAIRMAN: Is this the Trial 2A report?

MR WOOLFE: This is the Trial 2A report, yes.

THE CHAIRMAN: Okay.

MR WOOLFE: The Trial 2A first report.

THE CHAIRMAN: Yes.

MR WOOLFE: I will try and be consistent and say "first", meaning properly your first and third, meaning your first for the acquirer pass-on. I will try and do that.

We have paragraph -- starting at 3.34, you had set out the same four conditions, and you say at 3.34, referring to the commonality of cost and out-of-market constraints point, you say:

"The first of these assumptions [so that assumption] is the central determinant of the cost pass-on rate of 100% in the benchmark case."

If we go over the page to {RC-F/14/43}, paragraph 3.37, you describe all the other assumptions as ensuring:

"... that this incentive to pass-on fully ... is not mitigated or exacerbated by other relevant market [conditions]."

So it is fair to say that you do see these as being -- those three conditions as being less important in some respect?

A. Yes, I think that was particularly the case in merchant pass-on given the nature of the cost change that was being investigated.

Q. Now -- but this is setting out your benchmark case in theoretical terms, is it not?

A. Yes, but as relevant also to merchant pass-on.

Q. Can we go to your third report now, so your first report for APO, at {RC-F1.3/2/54}, and just have paragraph 4.33 I want to look at. This is where you discuss -- thank you -- how changing price sensitivity could be relevant to the rate of pass-on, and what you say is that -- you are looking at, in a sense, if the MSC decreased?

A. Yes.

Q. If:

"... merchants were to become less price sensitive as the MSC decreases, this would limit the extent to which a cost decrease would be passed on."

As I understand it, that would be because there is not so much incentive for acquirers to cut prices if they do not win so much new business by doing so; is that the logic?

A. I -- I don't think so. This is about how the merchants respond when MSCs are at a different level. So -- so perhaps, actually, an easier way to describe it, which I think would be responsive to your question of yesterday, sir, is, if one thinks about an increase in MIF costs, given how important MIF costs are as a proportion of MSCs, a change -- a sort of substantial change in the MIF cost could lead to a substantial change in MSC costs for a merchant, and let's say that's all pushing the price up. So what this point is saying is it could be that that higher price point, what happens is it really causes merchants to engage with, "Oh, gosh, this is actually a not insubstantial cost now, I'm going to pay a bit more attention to it and therefore I might then choose to shop around a bit more and see if I can get a better deal".

I think it's possibly the reverse of your point, Professor Waterson, about Marshall's third law. If, actually, MIFs have gone down and the MSC has become less important as a cost for merchants, they may be more inclined to sort of say, well, I don't know whether it's let sleeping dogs lie, I'm not sure if that's quite the right expression, but I don't need to pay so much attention to it, and that means less likelihood of engaging in with other acquirers as to -- to work out what savings could be made.

PROFESSOR WATERSON: I know we are in the realms of theory at the moment, but is there any evidence regarding shopping around?

A. Oh, the PSR, I think, did have quite a lot of evidence for the degree to which merchants are shopping around. I think they found that that was more likely for larger merchants, less likely for smaller merchants.

PROFESSOR WATERSON: No, I meant as opposed -- really, when the MIF went up rather than going down.

A. Oh. Not that I'm aware of.

PROFESSOR WATERSON: So this is speculation on your part?

A. Yes, that's absolutely right, and the conclusion that I draw is it could be that if -- if that price sensitivity behaves as I've just described in that example, that would point to pass-on below 100%. It could be that the alternative is that price sensitivity changes in a different way such that actually you get more than 100% pass-on. So I think I'm sort of quite clear, it could go either way. But either way there is some uncertainty therefore, and it's one of the reasons why I think in this case it's really helpful to look at

the empirical evidence, especially because we actually can look directly at the empirical evidence.
PROFESSOR WATERSON: Thank you.
MR WOOLFE: So essentially this could cut either way?
A. Yes.
Q. So simply as a matter of theory, there is no reason, as a matter of economic theory based on this, to doubt that pass-on will be high, is there?
A. I think what I'm saying is I don't -- there is some uncertainty as to quite what the pass-on would be. I can't investigate directly things like changing -- changes in merchant price sensitivity to different levels of the MSC, so I note that there's just an uncertainty, and I don't -- I can't tell you which direction it goes in, so it's not that theory points me specifically to below 100% pass-on. I'm not saying that, I'm saying let's look at the evidence.
Q. But in a situation where you have very inelastic demand at current levels and elastic market supply as well, you are going to be expecting a high pass-on rate, and this factor does not really point you, in itself, in either direction in the absence of evidence, does it?
A. This second factor points to an uncertainty which would exist even if you've got inelastic demand and quite elastic supply.

Q. Do you think that this uncertainty about price sensitivity could account for acquirers having to absorb 37% of the total cost of the MIF?
A. I mean, it's possible. I think that's why I want to look at the evidence.
Q. Now, we are going to move on to your analysis of the PSR dataset.
I am afraid at this point, sir, we are going to have to go into closed session fairly shortly, because Ms Webster's material is not, I think, marked as PSR confidential, but then we could get into some material that is, and so I think from now on, we are going to have to be in closed session.
THE CHAIRMAN: All right.
All, right, can we go into closed session. Thanks.
(In private)
(4.17 pm)
(The hearing adjourned until 10.30 am on Monday, 31 March 2025)