1. Mr Willeart: Good morning, sir.
2. Mr Justice Barling: Good morning.
3. Mr Willeart: I have a tiny piece of housekeeping just to keep you in the loop. We were sent a third von Hinten-Reed yesterday, and haven’t had a chance to take proper instructions on it. What I said to Mr Brealey is I will take instructions at lunchtime and then I will indicate to him whether we are happy for that to go in or whether he has to make an application.
4. Mr Justice Barling: That’s fine. I’m not sure whether we have got it. I’m not conscious of having it, but it may be that the system has got it here.
5. Mr Brea...
for setting the rules. So the terms and the rules, and the participants in the payment system how they behave, how they need to react and respond to different matters with respect to the scheme. And I was responsible at that time for the interchange team, which was specific for setting the interchanges across Europe. So I was not responsible for the rules; I was responsible for the setting of the interchange.

Q. Correct. Very quickly, where is the MasterCard rules team? Were is that based?
A. So MasterCard’s rule team is not based in one single location. So there is different people involved from both global function as well as European functions. So I couldn’t tell you exactly where everybody amongst the team is based, where it is multiple people involved in that team, including a lot of people from Europe and including also people from product areas, different business areas, to make sure that the rules that are put forward in the scheme actually make sense both from a scheme fraud perspective and business perspective.

Q. So is there a forum that is held every now and again which sets out the scheme rules? Who decides whether to amend it, for example?
A. I’m probably not right person to ask that because I was not involved in that process.

Q. And how does that potential bank or financial institution sign up to these terms of dealing?
A. It is my understanding that when somebody becomes part of MasterCard’s scheme and is assigned a licence, that they are also obliged to the rules that MasterCard puts out there. So you become a member of the payment scheme, then you need to adhere to the rules, so that everybody else in the payment scheme understands that this new participant obeys by the rules.

Q. So you refer to the licensee has to adhere to the rules, obey the rules. So what happens if they disobey the rules?
A. There is various consequences that could be. Of course, in first place this participant will be notified of that.

Q. Notified of the breach?
A. Of the breach, indeed. And of course it is like in any breach of rules, at a certain point in time there could be consequences for that entity. But, again, I was not responsible for managing that process, I was not responsible for setting the rules.

Q. At paragraph 12, just so that you can refresh your memory, you say: "It is the combination of all these rules which determine the allocation of responsibilities between the issuers and acquirers."

So the issuers and acquirers, by signing up to the terms of dealing, adhere to MasterCard’s allocation of responsibilities?
A. Yes. Just to put it into a perspective, so what I refer to in my witness statement is the fact to interchange, we might come to that, is a balancing mechanism where the objective of this balancing mechanism is to maximise the volumes, transactions and usage of the payment scheme. And in order to do that we need to maximise at one site, on the site where the card is issued to the cardholders. The issuers of this card, at the same time, need to maximise the participation of the merchant in this eco-system.

Q. Mr Willeart, I do apologise, but that is in your statement, that is your evidence. But if you could concentrate on answering my questions I’m posing --
A. Sorry, I will get to the point.

So one of these rules relates to the fact that who is paying in case, for instance, if there is a fraud on the card. The rules specifies that the issuer in many cases will be responsible for covering the fraud, so the issuer has a cost for that and the interchange needs to take that into account. There is a balance in the system. And that’s where, for instance, in a practical way this refers to.

Q. So you refer to costs of the issuers. So if one goes, for example, yes, if you just keep your finger in your witness statement but if you go to tab 1 of this bundle.
A. Yes.

Don’t lose your witness statement, but if you go to tab 1 of the bundle, which is the witness statement of Mr Sidenias, page 11, paragraph 31, you have mentioned at paragraph 12 of your witness statement the allocation of responsibilities as regards fraud.

But I take it from your evidence that the MasterCard terms of dealing also set out the allocation of responsibilities for the actual credit write-offs, fraud losses, fraud investigation cost, collections, funding costs and processing costs? Have you seen paragraph 31?
A. Yes, I see paragraph 31.

Q. At paragraph 12, you say there’s an allocation of responsibilities, and you highlighted fraudulent transactions. And I’m just asking you whether the MasterCard terms of dealings also sets out allocation of responsibilities relating to the six items at paragraph 31.
A. I wouldn’t be able to answer if they were specifically in the rules because, again, I was not responsible for setting the rules. But typically in a payment scheme where it is a bank issuing cards, the costs for fraud...
investigation and so on are borne by the issuing side.

That's why they recover the costs.

Q. Let's put it another way: your team sets the multilateral interchange fee, correct?

A. Correct.

Q. When you are setting the multilateral interchange fee you have regard to these six items?

A. We use multiple components to define the right balance and the right level of interchange, of which one of the components is the cost components. And this is what is referred to in this witness statement of Mr Sidenius.

Q. So the answer is yes, you will have regard to these six items?

A. Yes, we will get information in terms of the costs that issuers in the market on average bear for driving the payment scheme.

Q. This is an area where you may be asked further questions. Have you still got your finger in your witness statement? Keep your finger in your witness statement and just flip to C2, tab 2, page 40, paragraph 67. You have got those two.

Q. You say at paragraph 10: "The interchange terms on which acquirers and issuers deal together can either be agreed by an acquirer and issuer with each other (a bilateral agreement) or can be set by MasterCard in a particular country."

"Fallback interchange fees. Fallback interchange fees only apply in ...(Reading to the words)...as their name would suggest."

Now, you were the general manager for the Nordic and Baltics. You are now the general manager for France, as I understand it. Before we get to what Mr Douglas says about the UK, are there any examples of bilaterals in Europe?

A. Absolutely there are examples of bilaterals. Just to be very clear and the mechanism, how interchange works, it is in the first place the promise that a cardholder, in every market where it goes and wants to pay, the system works. And the issuer knows what he will get as a cost and what he will get as a revenue to accept the transaction. At the same time the merchant knows what the costs and revenues are associated with the transaction.

That is the basis. That is why we have a fallback balancing mechanism. Then MasterCard allows between the issuers and acquirers to make bilateral agreements around what is the level of interchange which they will agree. So in some markets this is applied and used, in some other markets it is not applied and used, and in some European markets, for instance, like the Swedish market is a good example, bilaterals are used.

Q. And as I understand it, is it Austria, the debit card?

A. I'm not aware of bilaterals in Austria. But there are multiple examples where it exists and there are multiple examples where it does not exist.

Q. You have given Sweden there and you say there are multiple examples. Can you assist the Tribunal with any other examples or countries in Europe, for example?

A. I can give you an example. Sweden is a market where there is a lot of bilateral existence. For instance, also in the Baltic markets there are examples of bilateral interchange fees.

Just to clarify, perhaps also on the bilaterals, that the level of the bilaterals can sometimes be higher than the multilateral interchange fees, sometimes can be lower. This is a commercial, or a negotiation between the two parties in the system.

Q. I asked you to just go to Mr Douglas' witness statement C2, at tab 2 of C2, paragraph 67, page 40. So this is in a world of no multilateral interchange fee in the UK.

He says: "MasterCard would have had to persuade its issuers and acquirers to enter into bilateral agreements setting bespoke interchange fees to apply to the transactions between them. I believe that a sufficient number of bilateral agreements could have been entered into to deal with this given the limited number of major issuers and acquirers in the UK market."

Then he goes on to say about Maestro and rates. But just concentrating on those two sentences, is that something that you would agree with?

A. Within the market domestically in the UK, if there is a limited number of participants, issuers, acquirers, I think indeed it is possible that those issuers and acquirers would be able to agree amongst themselves about what is the level of interchange that both parties seem to need to make the system work. That is domestically set.

Of course, it is impossible for every single acquirer and issuer in the UK market to do this across the world with all transactions. On a limited scale it is possible. Just to clarify, that possibility exists and there's nothing stopping in MasterCard rules for issuers and acquirers in the UK market to do that.

Q. On that point, it existed, if you just -- have you got bundle E3.10? Go to page 4068, bottom right.

A. This is the same bundle?

Q. It is the scheme rules. It is bundle E3.10. The terms
Q. Okay. You can put that bundle away, I won’t refer to that again.

If you go to paragraph 24 of your statement, please, to pick up that you started to make. I slightly cut you off. But you say there that there are multiple factors which are considered when setting interchange fees. And you start off with cost data, yes?

A. Correct.

Q. And you say at paragraph 26, I’m just focusing on cost data at the moment, so it is the first heading that you refer to in 24. Just focusing on that.

At paragraph 26, if you could just look at paragraph 26, at a basic level the scheme must ensure that all the participants involved in it can cover their costs.

What do you mean by that? Costs of what?

A. I mean, that is a payment system. This is a two-sided system. This is at the one hand the issuing bank distributing the cards and they will incur costs for distributing these cards. They need to recruit new cardholders, they need to score credits, for instance, on this new cardholder, they have costs to process the transaction.

At the same time, also on the acquiring side that deal with the merchants that have a relationship with the merchants, they also have costs. So there is the overall set of costs to make the payment system work. That is the costs I refer to.

Q. So keeping that paragraph 26 in mind, then going to paragraph 31, and again just focusing on costs, you say that:

"MasterCard, in attempting to balance the costs of the issuers and acquirers ...

Which is what you just referred to:

"... wants to ensure that issuers are not paying too large a proportion of the total costs, since this will make the scheme uncompetitive ...(Reading to the words)... from cardholders.”

What do you actually mean by that?

Could you just explain how paragraph 26 and the first sentence of paragraph 31 act out?

A. This I think goes back to the principle of the four-party scheme that I mentioned. It is costs on the issuing side to recruit cardholders, to manage that; it is costs to recruit merchants and manage and process the transactions on the merchant’s side.

Various studies and theories have been developed and measured those costs in this eco-system, and it has been found that the costs on the issuing side far outweigh the costs on the merchant side. So in order to make the...
a product, it needs to be competitive in the market. So if you launch a product you need to make sure that the product you provide to the issuer can compete in the market with other products. So if you are making a standard product you need to be able to compete with alternative products for the issuers, for instance. It could be Visa in this case. If you are making premium product you need to make sure that from a consumer perspective the benefits that are given to the consumer, the insurances, the rewards, that they are competitive with what the issuer could do as an alternative. For instance, issuing an Amex card. So competition is a very important part of setting interchange as well.

Q. Keeping that competition, that competitive element in mind, I just want to take you to three paragraphs of your witness statement. Again, keeping the competitive situation in mind, the first sentence is paragraph 30 and then I will take you to all three and then I will ask you the question. In 30, you say: "The costs incurred are not necessarily the defining factor in the rates set by MasterCard." All you have to do is say yes or no, because otherwise we will lose ourselves.

But that's your evidence: that the costs incurred are not necessarily the defining factor in the rates set by MasterCard. Then at paragraph 35, you say, again this is your evidence, a vital factor when setting rates is the rates of MasterCard's main competitors. Correct?

A. Mmm.

Q. Then if you go back to paragraph 17, you say that: "To assess and set interchange fees, the interchange fee team researches the relevant payment market looking at market trends." And "If necessary, will request a cost study." I take it from that that sometimes you don't actually request a cost study.

So keeping those three statements in mind, the logical implication of that, those three statements, is that you may raise an interchange rate that is not based on cost?

Can I have a yes or no answer to that and then you can --

A. Am I allowed to put the context?

Q. I will ask you the question, then you can say anything you want, but I would like an answer to the direct --

MR HOSKINS: I think he should be allowed to answer it the way he wants.

MR BREALEY: No, I would like to --

MR HOSKINS: I think he should be allowed to answer it the way he wants.

MR BREALEY: I would like to ask the direct question and then you can say anything you want to clarify it.

The logical implication of that is that you may raise an interchange rate that is not based on cost? Yes or no, and then you can say whatever you want. A. I would say no. And I would say that the -- in setting the interchange for a specific product always different factors will be taken into account.

What I mean is in the first place a cost basis will be taken into the account. In the first place. And we always will take -- look at what is the cost basis. It does not mean that at every point in time a new cost exercise needs to be conducted because that is a very complex process, but an element of the cost is always taken into account.

Secondly to that, it might not be the determining factor for setting interchange. You might very well have an interchange which is below -- set below a certain cost level to make the balancing. But if that results in a product that is not competitive, it doesn't work in the market, the issuer is not able to issue the product because you have set the wrong interchange and it cannot compete on the issuing market, then you have got the wrong interchange. It is one of the factors.

Next that there's also a third dimension which is important, which is the evolution of the market, for instance, new technology. If we are talking about contactless transactions, if we are talking about chip cards to improve the security, we will use interchange to drive the innovation in the market.

So there is multiple aspects to setting of the interchange of which the cost and competition are important ones, but they are not the only one.

Q. That is not quite what I asked you. You do take into consideration costs, I accept that. I asked you, and I will ask it again: do you ever raise an interchange rate which is not based on cost? Is the increase ever made with, for example, a competitive situation in mind?

A. That is possible. It is very well possible that you have an interchange which is higher than the cost rate because of a competitive reason, though those cases are very, very exceptional. But theoretically it is possible.

Q. I had understood that MasterCard's evidence regarding the Maestro is that it just was that: they wanted to increase the Maestro rate in order to be competitive
1 with Visa?
2 A. I think that is a very short (inaudible) summary of why
3 their rate needs to be increased. But I understand that
4 it is essential in the market to have a product that is
5 competitive. So if the rate is not competitive that is
6 a good reason to increase it, yes.
7 Q. Mr Willeart, there are thousands of documents in this
8 case and, forgive me, but one document seems to be
9 missing and that is the precise calculation by the
10 interchange fee team of the UK MIF.
11 Can you assist the Tribunal with why that is?
12 A. I cannot answer on the specific document because I was
13 not --
14 Q. It is not annexed to your statement, for example?
15 A. No, exactly. So I would say that, and I think what you
16 are hinting at is, is there one precise formula where
17 you magically pump in all the information and the
18 interchange comes out? No. An interchange is
19 a balancing mechanism and you need to take various
20 inputs into account to set the right level of
21 interchange.
22 There are other examples, for example if the Central
23 Bank sets a interest rate, they are also using a
24 mechanism in the market to balance. So it does not
25 necessarily require one specific formula.

26 So this, typically where you are balancing two
27 different market sides, it does not mean necessarily
28 there is a specific formula for saying "This is now the
29 right level of interchange".
30 Q. There is no document that MasterCard can produce to the
31 Tribunal or to the experts in this case which will allow
32 them to assess in some detail how the interchange team
33 arrived at a certain level throughout this claim period.
34 A. I would disagree with that. I think MasterCard
35 typically put a very robust methodology in place. We
36 set interchange levels, taking the different components
37 into account. That was surely the same case for the UK
38 interchange where at the one end there was taken a cost
39 basis as an input, which was a cost study performed
40 typically by Edgar Dunn, it was outsourced to have
41 an independent company to look at what are the costs in
42 the market. Secondly, we would look at different
43 research. What is the trends in the market. How we
44 drive people from cash to electronic payments. And of
45 course there was a (inaudible) done from competition,
46 and there is various documents from every single time
47 that MasterCard set an interchange, there was a thorough
48 process done that took multiple months, was
49 independently done and came to a conclusion in a
50 document that was presented for approval independently
51 by MasterCard.
52 So I would disagree. There was a very robust
53 process and there was documentation to prove it, as in
54 the various documents.
55 Q. Have you exhibited any calculation to your witness
56 statement?
57 A. I have not in my witness statement given any statement
58 about exact level of interchange in UK.
59 Q. No.
60 A. So I did not feel I would need to submit annexes on what
61 is the level of interchange. But I am sure that the
62 court can have access to the pages and documents, if it
63 has not got it already, that defined how the rate in the
64 UK was set.
65 Q. And with detailed calculations of the costs, the
66 competitive situation, the market conditions, every
67 single factor that was taken into account to arrive at the
68 certain level of interchange fee for the UK, you
69 think that such a document exists, do you?
70 A. There are typically interchange documents, EIC
71 documents, which are a proposal and which state -- which
72 are a summary for a committee to review.
73 Q. Correct, they are a summary. I am not sure I need the
74 exhibit to your witness statement. We get a minute
75 saying this is what it should be, but I'm asking you
76 whether there are any documents which would allow us to
77 verify how it has been calculated?
78 A. So in preparation of this document there are various
79 materials made, calculations made to come to this
80 conclusion and this is the end result, which is a study
81 that were done to come to the conclusion. For instance,
82 if there is a cost component and a cost study done,
83 there is a lot of work done, data collected from various
84 parties in the market, in this case I'm referring to
85 studies done by Edgar Dunn, they collect those
86 informations and they produce an end report. The result
87 of this end report is produced in the interchange
88 proposal, which is the EIC document.
89 So there is a process and there is a summary to come
90 to a conclusion.
91 Q. Yes, Mr Willeart. We have lots of Edgar Dunn reports,
92 we have lots of EIC reports, we have nothing in the
93 middle. We have no detailed calculations from your
94 interchange team which would allow us to verify how you
95 have gone from Edgar Dunn to what the EIC has
96 sanctioned.
97 A. I would say the different inputs are clearly laid out in
98 the document, and the logic and how a rate was proposed
99 is clearly laid out in this document. So I'm not
100 sure -- as I mentioned, there is no one formula that
101
will make up this is the level of interchange, but the
 logical conclusion, how you get to the level of
 interchange, is clearly explained in this document.
 Q. Anyway, for today’s purposes you are not able to assist
 the Tribunal in how the interchange fee team arrived at
 the UK MIF? Except in a very vague terms.
 A. I would disagree with that. I think to me what
 I explained is that interchange committee took into
 account the various cost components, took into account
 the competitive level in the market and took into
 account the different factors to come with the rate
 proposal. And that was what was used, and in this case
 for the UK interchange team it was done before I became
 responsible, for the same process applied when I was
 responsible.
 MR SMITH: Mr Willeart, a few moments ago you used the
 analogy of the Bank of England interest rate setting.
 Now, as I understand that process, there is a regular
 meeting, a monthly meeting, at which the rate is
 reviewed. And I anticipate before that meeting the
 are briefing documents circulated, they are read, the
 Committee assemblies, they discuss, make a decision and
 then after the decision minutes are published for the
 public as to how the conclusion has been reached.
 Is that the sort of process that MasterCard adopts?

In other words, are there regular reviews of what the
 MIF should be for a particular market, monthly or
 however, or is it a more ad hoc process?
 A. I would say it is -- there are multiple changes that can
 happen and when there is a review required. For
 instance, when there is a new product being launched in
 the market, that will be taken into account. There is
 going to be a meeting with the business people and the
 product teams in MasterCard to understand what they are
 trying to achieve in the market, what is the competitive
 situation, what is happening in the market trends.
 That information will be collated, and of course
 together with the interchange team, will be reviewed and
 a proposal for how the interchange should be set is
 developed. So such process indeed exists.
 And there is multiple ways it can exist. It can
 start with the interchange team reviewing the rates. It
 can come from business needs. It can come also from,
 for instance, a new technology in the market and there
 is a change required. It can also be that competition
 has made a change.
 So there is, I would say there is a very regular
 discussion with market teams about what’s the level of
 interchange, what are the various products that need to
 be issued. And all that typically results in

an interchange proposal if there is a change required to
the setting, and that would then go to the -- through
the approval process.
 So there is a similar type of approach, not
necessarily every week, but there is a similar type of
methodology approach.

MR SMITH: Correct me if I’m wrong, it is perhaps not
regular in terms of a monthly set date.

A. Correct.

MR SMITH: But perhaps more triggered by something
happening, whether it be a new product or a new
technology or a sense that the competitive situation in
the market may have changed requiring a review.
 So would it be fair to say that the review of the
MIF requires some form of external trigger to produce it
rather than it being done on a time set basis?

A. Definitely external factors will trigger it, but also
internal factors; we will look at the evolution of the
products in the market.

To give you one example, at some point in time we
observed that the premium product, which were competing
with Amex, we had launched the world product in the UK
market, became very successful in the market. We
expected more world products to come into the market, so
we proactively took the decision to lower the

interchange across products in order to manage the cost
in the system for the merchant and for the acquirers in
the system.
 So this was a case, for instance, where there was
not necessarily any external competitive situation.
 There was more, let’s say, a proactive approach from
MasterCard side to look at what is going to be the
future evolution of the average interchange in the
markets and do we need to take any action.
 So that was one occasion. But you are right, there
is multiple ways you can be proactive. Sometimes it is a
new product.

MR SMITH: Thank you, Mr Willeart.
 Thank you, Mr Brealey.

PROFESSOR JOHN BEATH: I have a supplemental question. I’m
still trying to get to grips with what goes on in your
team’s mind as you are generating this MIF, because the
way you describe it you have some hard information,
I presume that’s what EDC provide, hard information, it
maybe based on some judgments of players, but it’s hard
information. Then you also have soft information, which
is all this stuff about, you know, what the market is
like and so on.
 Now, when you bring these things together you have
to have a baseline to start from. So is the baseline
the cost information and you then have a judgmental factor? Because, you know, thinking about the Bank of England MPC process that’s exactly what it would be. There is hard data on the economy, and then you think about expectations and things of that sort. Is that actually the way your team ends up with “This is today’s MIF”?

A. It is a very good question. I’ll try to explain it. So I would say -- in the first objective I would say that the product that you put in the market, let me assume that we would be setting the rate for a new product from MasterCard that would be launched, of course the first objective would be to ensure that the product is competitive in the market. So that is the first objective. Then what you would do is you would look at the cost information -- PROFESSOR JOHN BEATH: But if it didn’t cover the costs. I mean, if to be competitive it didn’t cover the costs, would you simply withdraw the product?

A. If so you would, let’s say, need to set an interchange rate would be higher than the costs in order to be competitive, then I think no. So you could still go ahead. But, for instance, let me make a concrete example. The premium product. We get a study from Edgar Dunn that says the cost in the market on average is 100 basis points on average. Then we want to compete with Amex. So we say, well, Amex gives the issuers on average, let’s say, 160. So if I’m going to launch a product at 100, it is never going to be able to compete, no issuer in the market will launch this.

So I can actually make -- set an interchange rate which is competitive with Amex, say I put it at 140 because Amex has a different acceptance. So we look at 140 as a competitive rate, but then I would look at the overall costs in the market and then make an estimate how much of these products will be issued in the market. And I will look at the total costs in the market of all MasterCard products for merchants: Standard products, premium products. And the average of that, I would try to ensure that that is below the cost level, so that on average the merchant does not necessarily have an increase, or will not be above the cost. But that does allow me within this average to set some products at the higher rate to compete and some at the lower level. That is why the average is a very important mechanism for setting this interchange.

MR BREALEY: That was a very helpful answer of the thought process that you go through, but we don’t seem to have any details or minutes of the interchange fee team which would give us a clue as to how you go about that thought process; is that correct? Do you have minutes of the interchange fee team?

A. There were minutes of the meeting made which noted to the decisions taken on each of the proposals. Q. But not why? Not detailed calculations?

A. Again, to me if I look at the proposals, read the proposals, I think the logic in the proposals is quite clear and follows the same logic as I explained.

There is not a difference and the proposal is clear to how a rate was set, what was taken into account. The minutes did not go further than the discussion and the proposal, that is true.

Q. Well, let’s look at an example that you give in your witness statement, which is the development and the repricing of the DMC proposition, which you refer to at paragraph 42.

You say “I was therefore tasked with developing and repricing the DMC ...” That is the debit MasterCard proposition: “... in an attempt to grow its volumes in 2010/11.” You say that essentially you wanted to establish debit MasterCard as a superior debit product offering towards issuers, correct?

A. Correct.

Q. 43, the strategy was essentially to increase the functionality of the debit MasterCard, and link it to the premium segment. Again, at 44:

“In terms of functionality, we sought to relaunch debit MasterCard mandating PayPass functionality.”

That was the increase in functionality, but it was also a correlation with the increase in interchange rates because you say that in order do that, you wanted to increase the interchange rates to persuade issuers to issue MasterCard debit cards.

So in 43 and 44, you are looking at increasing functionality and increasing interchange rates to persuade issuers to take that card.

Could you expand on that? Why are you increasing the rates in order to persuade the issuers to take the DMC which has increased functionality?

A. I think it comes back to the essential point that if we set and launch a new product in the market, it needs to be competitive. And it needs to be competitive in terms of the proposition to the cardholder so the issuers can have an attractive product to distribute in the market. That is the essentials.
What we found is when DMC at that time, when it was launched, and it is no secret, was not gaining a lot of traction in the market. If you look at our market share in the UK market, it was very low.

When we looked at the position of DMC versus the competitive product of Visa, we did not find there was sufficient appeal to pick up this product. So the strategy of the product in the market team at that time was to revamp, relaunch it and make something that was more appealing and also more adjusted to the time.

At that time it was the coming of contactless, so that needed to be a default proposition. We wanted to make sure that cardholder had a secure product, so we would put zero liability for cardholders in the product. Then we refreshed the interchange setting. Two objectives: first of all because we made a more appealing product, it was also higher cost for the issuers to put contactless on there, to put the zero liability insurance on there.

Also because we found the product, and in this case the interchange, had not made a difference for issuers to issue the product. So there was a change in product construct that justified us to change the interchange setting for that product.

Q. Okay. Also at paragraph 42, at the same time as you are establishing debit MasterCard as a superior debit product with increasing interchange rates to persuade issuers to take them, this is the third bit in 42, you are confirming Maestro has entry level debit product.

A. I think this is in the context, when we look at the debit product that MasterCard wanted to offer to issuers, we say we are going to offer product which is superior versus Visa, with contactless on there, with insurances on their superior product. But we also want to make sure that when we have a range of products in the market there is a product which has less functionality, which has less benefit around the product, if you wish. So that is where Maestro was positioned at the time.

Q. You gave evidence of what I call the Maestro story, 36 to 41. Can I just confirm your knowledge of it.

A. 2009.

Q. So this is after --

A. Correct.

The reasons for the portfolio losses in debit... and there are multiple factors that influenced HSBC and RBS’s decision to migrate their debit portfolios from MasterCard, notably overall economics, acceptance and marketing."

I took Mr Douglas through this and he accepted that all these were contributory factors to the loss of RBS and HSBC, yes?

If you weren’t around at the time, then you obviously can’t give direct knowledge of it, can you? But from your reading of historic documents or talking to people, were you aware of the limited functionality of Maestro? Were you aware?

A. What I was aware of is that -- this was mentioned, I think it was also mentioned on Monday. There was the famous less acceptance for the Maestro product. I think that is one of the topics.

Q. If you just pause there. If you look at the second product strategy:

"The UK was still Maestro-based providing strong UK acceptance, but inconsistent throughout Europe and little across other global markets with the US representing a key acceptance gap."

Were you aware of that?

A. Well, I have a slightly different view from the way it is written here, because if I look across Europe,
Maestro and especially -- Maestro is a very strong brand and a strong product. If I look at the Dutch market, for instance, all of the Dutch cards are Maestro cards. In Germany, 80 million cards in Germany has as a brand on there, Maestro. Why do they have it? Because it allows them to cards they use outside of Germany. Q. Pausing there. Can you flip back to page 4857 and let's look at the figures that were available at the time. So what HSBC and RBS had, when they were making their decision whether to go with Visa or not. 4857. This is another MasterCard document, debit MasterCard. A new choice. You see 4857. We call this the 10 million versus the 23 million point. So the figures at the time that these two banks were making these decisions, we see the acceptance. I think one of the witnesses -- I don't know whether it was Mr Perez, I can't remember now. I think it was Mr Perez yesterday accepted that where you see the figures for MasterCard, you can take equivalent figures for Visa because they have a similar reach. But you see there: acceptance 23 million locations worldwide for, say, Visa, but only 10 million locations worldwide for Maestro. I would suggest to you that that is a humongous difference in acceptance.

A. For sure I'm not going to debate the figures here. I fully follow you there is a big gap in numbers, but I also just want to put in perspective that Maestro is exactly the brand taken by many banks across Europe to give their cardholders access outside. So the level of acceptance, where it is, could be that in at small remote locations in the US there is not a Maestro, but if you travel to New York, travel to the key points, there is Maestro acceptance. So the overall numbers might be lower too, but surely 80 million German Maestro travellers also travel to the US. I agree there is a difference in numbers, but there is also an important factor about where the acceptance is. But I do agree with you that there is a difference in numbers --

Q. Quite a significant --

A. There is a significant difference in numbers, absolutely. But the important part is where is acceptance gap. The important piece.

Q. One of the reasons for the significant difference in numbers was the limited functionality of Maestro.

A. I think you accept that. For example, we have just seen it was sporadic. Let me put it as neutrally as I can.

Q. In the US it could not be used for e-commerce at the time. It had limited functionality.

That is one of the reasons you were charged with establishing a superior DMC, correct?

A. I think you need to take the time perspective. So I do understand there is, and there is, a difference in acceptance of the product. I'm not going to debate that.

Q. And is it due to functionality?

A. I would say at that point in time there is different functionality of Maestro online versus, for instance, a Visa card online at the time.

But let's put it in perspective at that time. E-commerce transactions, we are talking the period 2005/2006, e-commerce transactions were a very small proportion at the time. So if you take different perspectives about what happens, to me the interchange component is a very critical aspect.

I'm not saying that the other doesn't play a role, but the interchange one, let's not forget the gap in interchange between Visa card and a Maestro card, and just make the numbers. If you make the numbers, the card was 10 basis points difference. 10 basis point, if you take a portfolio of 5 million cards -- I'm just making an example here -- about £8,000 spent makes on a yearly basis about £40 million difference for a bank if they issue a Maestro card and they issue a Visa debit card.

I think that's also an element that we should not ignore because that's a key factor for me.

Q. It is, but if I'm a cardholder and I have a Maestro and I go to Los Angeles and I can't use my Maestro card, I may go to another bank that will offer me a card that I can primarily use in the UK but also gives me that ability abroad. You would accept that?

A. No, I understand that acceptance is a key part. But I'm also saying that acceptance on key locations was there, because the Germans also travel to the US. And it might be that in outside locations, in Texas and wherever, there is a lower acceptance, but if you go to the key airports, key cities in the US, there was Maestro acceptance. There is no problem.

There is 80 million Germans, all the Dutch. This was a cross-border brand. The reason of existence of Maestro in Europe is the fact that it allowed domestic schemes in Europe to give international acceptance. So surely it worked for the Germans, so it cannot have been that bad that it totally didn't work for the UK market.

Q. But I think you have accepted that there was --

A. A difference --

Q. -- a difference in functionality between Maestro and the
MR JUSTICE BARLING: Are you saying that's less important in Germany because it is a cash economy?

A. I would make a difference between now when e-commerce is significant, but let's not forget this was happening in 2005/2006 when the banks took the decision, e-commerce was a very small proportion at that time. We were at the start of the e-commerce period.

Q. The banks made their decision not in 2005/2006. They made their decision in the last quarter of 2007.

A. Exactly.

MR BREALEY: With respect, they gave the decision in the last quarter of 2007.

MR JUSTICE BARLING: Sorry, Mr Brealey, we have been interrupting you. Shall we have a short break then?

Mr Willeart, feel free to stretch your legs but do not talk to anyone.

(11.40 am)

(A short break)

(11.50 am)

MR BREALEY: So Mr Willeart, just concluding on this and we were looking at paragraph 42, 43, 44, the launch of what you call the superior debit MasterCard. And I think we have established that your evidence is that the launch of the superior debit MasterCard merited higher interchange fees because of its functionality, correct?

It is what you say.

A. It needed to be a competitive product and functionality was one of the aspects, yes.

Q. So if you get higher interchange fees because of increased functionality, logically, I would suggest to you, an inferior product should attract lower interchange fees. It is a question. An inferior product should logically attract lower interchange fees?

A. It depends on the context, the specific context of the market, what product was the competition at that time. I cannot answer that as a theoretical hypothetical scenario.

Q. You can’t answer a straight question? You think it depends?

A. It depends on the context because the product in all cases needs to be competitive, so I don’t know in your scenario what is the competitive situation. If the inferior product is competing with another inferior product which has a higher interchange then it is a different situation.

Q. Let's see if we can get this straight. So on the MasterCard, I think it is accepted that it was not as good as the competing Visa product. You would accept that?

A. Correct.
Q. If it is inferior to the competing Visa product you say that you need higher interchange fees in order to make that inferior product competitive with a Visa product, correct? Competitiveness seems to be the key element here.

A. It needs to be a competitive product, yes.

Q. So in other words, I think you talked about the 10 basis points. It would be MasterCard’s intention to increase the interchange fee of the Maestro product simply to compete with the superior Visa product, correct? To make it competitive in terms of the amount of money the issuers are going to receive.

A. That could have been one of the scenarios, yes.

Q. So in essence, the effect of your evidence is that had MasterCard increased the Maestro interchange rate, they would have been asking merchants to pay issuers to retain an inferior product? Correct? Logically it follows.

A. I think -- I mean -- I'm not sure I follow the context.

Q. I think you do follow me. The whole thrust of this evidence that you give at 36 to 41 is that if only we could have increased the interchange fees we could have made the Maestro as competitive with Visa and retained the two accounts.

That's the thrust of what you are saying, and what account would have 13 million locations, less than if the person in Tottenham took the Visa card to use worldwide, correct?

A. I don't understand why the acceptance in the US has a difference for the acquirers in the UK in terms of the costs for the transaction of the card.

Q. It has a difference for the cardholder, doesn't it?

A. For the cardholder, there is a difference, I understand, yes.

Q. Yes. But I don't understand what is the difference for the cost of a transaction in the UK. I don't understand that.

Q. All I'm putting to you that had MasterCard increased the rate by 3p or 4p, on your evidence, your evidence is, if you only had been able to do that, you would have retained the accounts for three, four, five years, how long the period was, you would have retained the accounts, the customers in the UK who had Maestro cards would have had an inferior product?

A. In the UK the customer would have a similar product as the Visa product because the acceptance was the same.

Q. You also mention Amex.

A. Yes.

Q. About how you are going to lose market share if only you could compete with Amex.

Is this the evidence -- we are looking at essentially paragraphs 46 to 56 -- are you giving this evidence with your interchange fee hat on, or what? Or your experience as the general manager of France, the Nordics? Where is the experience coming from?

A. Probably my witness statement has elements of both, I am sure.

Q. So if you go to -- I don't know what bundles -- have you got E --

A. I have bundle E3.12.

Q. I think we will not need that. You will need to put that away and go to E3.13.

So we won't go at length through all the Amex documents, we have been through it with the witnesses, but I will take you to this one, E3.13, tab 249. Before we delve into this document, let's just go to the front -- is this blue? (Pause)

Then I'm afraid I can't...

MR JUSTICE BARLING: This is the document that we went into camera.

MR BREALEY: Let's see if I can --

MR JUSTICE BARLING: It depends on how extensive your cross-examination --

MR BREALEY: I will do my best.
MR JUSTICE BARLING: See how we get on.

MR BREALEY: This is confidential to MasterCard so I will take you to various passages, you can read it and then ... (Pause)

I'm going to show you this document in the context of your evidence where you say that you need higher interchange fees to compete with Amex, correct? And just let's get some base rules from the evidence that you have given on the interchange fees, how you set them.

Do you accept that the bilateral interchange fee is a cost set by MasterCard?

A. It is a balancing mechanism by MasterCard, correct.

Q. If I can call it the MIF, that the MIF sets a proportion of the issuer's costs. I think you have accepted that.

So the MIF sets a proportion of issuers' costs?

Q. A. The MIF balances the costs from the issuers to the acquirers, correct, yes.

Q. I'm just taking this from your evidence.

This is not necessarily in your evidence, but I put it to you that the effect of that is that there is no competition between acquirers and issuers as to the proportion of issuers' costs because it is a common cost. Do you agree with that?

A. Yes.

Q. But you say that this fixed common cost is necessary to stimulate interbrand competition from a competitor, here Amex, correct?

A. Yes.

Q. Whilst it may restrict intra-brand competition -- do you understand the --

A. Can you --

Q. Intra-brand competition? Intra-brand competition is competition in the focal product, say MasterCard. So there is no competition in the MasterCard interchange fee.

A. Okay.

Q. So there is a distortion of competition, a common fixed cost, MasterCard. But you say that that restriction of competition intra-MasterCard, you need it in order to compete with Amex?

A. What I'm saying and what I mean is that you need to be competitive with Amex, and for that purpose MasterCard has multiple products, premium products to compete with Amex, and other products that compete with standard products, yes.

Q. It's what the economists like Dr Niels and Mr von Hinten-Reed --

A. It's complex --

Q. Call intra and inter-brand competition. I thought you might know that.

That is in the context of your evidence here. This document, you can see what it is. It is a -- I am sure I can say this, a steering committee. Do you know whether you were on the steering committee?

Q. A. I was not on the steering committee, no.

Q. So you have never seen this document?

A. I have never seen this document.

Q. Do you get access to these sorts of documents? I mean, this is essentially a commercial document giving the state of play of the market and of the competitors. Do you ever get access to this sort of stuff?

A. Could be that I get access to this, but this is not necessarily systematic.

Q. When you signed your statement, when it was prepared for you, did you have these sorts of documents? Were these sort of documents shown to you?

A. No.

Q. If you go to page 5319, I think it is 5319, we have seen this before, do you agree that MasterCard has a significant acceptance advantage over Amex?

A. Yes, I agree with that, but you need to nuance a little bit.

We are talking about the premium markets. So it is important always to look about the premium market in

specific. So if you look at the market in total and look at acceptance, for a premium cardholder, the acceptance in a small village in the north or in the south is less important than the acceptance in a high street location in London.

So while these figures are market averages, you of course would need to look into, from a premium perspective, what is the acceptance and what is level of acceptance, but of course there is a difference in acceptance, I do agree with you there.

Q. At paragraph 55 of your statement, I think you are, throughout really you also are referring to the Amex GNS offering.

If you go back to 5318, at the bottom you see it says:

"The Lloyds Duo."

You see the second bullet point, there was evidence from someone from a bank in these proceedings saying that the Lloyds Duo was complex and customers did not really understand the two-card concept.

Would you agree with that? Is that your experience?

A. Unfortunately, I can't comment a lot on the market experience, but I understand that it was not, let's say, potentially as successful as they may have wished.

I have not been very close to that specific product ...
Q. Again, this has been debated at length, but in fairness show it to you. If you go to page 5327, you see that that is dealing with what we have referred to publicly as the experience in Australia. Are you aware of the Australian experience--

A. I'm not aware in detail of the Australian experience.

Q. If you go over the page, which is page 5328, the penultimate bullet point, which says "meaning".

A. Which page? It is page 5328.

Q. I'm sorry, page 5328, with the fourth bullet point: "Meaning that..."

A. Are you aware that that was the experience in Australia?

Q. I guess -- I'm not aware of the details in the Australian market, but I think the key point is to understand in this context how did MasterCard compete in that market.

A. If MasterCard was able to compete with the premium interchange rate, I would expect Amex to gain share.

Q. If MasterCard was to issue a card at the premium interchange rate, I would expect them to be able to compete and defend their position. My understanding is that there was a premium interchange for MasterCard at that time in the market. But... A. I believe there is an average of what MasterCard was expected to respect, and an average is important because it allows you to set premium interchange to compete with Amex and to set a lower rate, and then you respect the average. I think that's the essential element for the Australian case.

Q. So you have or you have not studied Australia?

A. No, I have not studied, but I understand that there has been an average interchange which is respected.

Q. If you were aware of it you don’t feel you should have dealt with it in your witness statement?

A. I'm not.

Q. Should you not have dealt with this in your witness statement? You are coming to this Tribunal, it was for the court, saying that it was almost certain that you would lose premium business. I'm suggesting to you that you haven't really been shown all the documents which would better inform you as to whether that's correct or not. Would you accept that?

A. I have not seen this document.

Q. Are you aware of what is happening in the UK, the market intelligence about how Amex is responding to the 0.3% cap?

A. No, I'm not.

Q. But I do suggest to you that the concerns that you or MasterCard have about losing market share to Amex, if you did read all documents and gained the market intelligence, would be misplaced. I have to formally put that to you.

Do you accept that you would like to gain more market intelligence in order to say that it is certain that you would lose the premium business to Amex?

A. I would say that the Amex is a significant threat in the premium space to MasterCards. I mean, both when I was working on the interchange side, both as I'm working as a general manager, I see we are competing with Amex in the market. So I'm very comfortable in saying that, yes.

Q. Sorry, are you saying that you would not wish to look at more market intelligence before making statements that MasterCard will lose its premium business? Are you saying that you would not want to be better informed?

That you can make this statement on the few documents that you have seen?

A. I'm saying that I have seen, I have seen and...
So to revenue streams in – for taken into account used and then put the different A. setting the interchange fee? have never interest

A. I’m not aware in specific terms and I would assume that, of course -- I understand it is a significant component of their revenues, I fully understand that. If you ask about specifics, I’m not aware to give you an exact amount.

Q. But you have been head of the MasterCard interchange fee for the UK, and so I take it from your evidence that you have never really considered interest payments when setting the interchange fee?

Q. Where is cards which had – charge cards where there was no credit card components, being cards that had revolving aspects or where there was an interest case, and there is cards which had -- charge cards where there was no interest attached, if you wish to --

Q. Mr Willeart, sorry to interrupt. Are you referring to the two reports that Mr Sidenius is going to refer to tomorrow? Have you looked at those, is that what you are meaning?

A. I mean to that exactly.

Q. You mean those two reports?

A. I mean exactly this.

Q. In 2002 one is a draft. We will have to ask him tomorrow because we don’t know whether they have been submitted to the OFT, the European Commission. We are at a complete loss. But you are getting your knowledge from those two reports, you are not getting your knowledge of interest from anything that you have done during your time at the interchange fee?

A. No. For sure we also looked at the overall market and how issuers can make, let’s say, can compensate costs that they face. In terms of some markets there is card fees in the markets, like a market like France, for instance, you have high card fees, which is not the case in the UK market. In the UK market you have some banks which have interest and you have some other banks that don’t have an interest income.

So definitely I’m aware of that and that’s definitely something that we took into account.

Q. If you go to page 5313, you will see at 5313 that MasterCard’s analysis, which comes from Datamonitor, which I understand is a public group, and the Boston Consulting Group analysis, where you see on the right-hand side the billions of pounds that credit cards generate for issuers, correct?

A. Yes.

Q. If you go to 5315, you will see a significant proportion of credit card customers are revolvers, that is to say they pay interest. 5315.

A. Yes.

Q. Now, did you ever follow the European Commission’s infringement decision of 2007?

A. What do you mean with follow?

Q. Did you read it?

A. I did not read it of course.

Q. Have you ever been told about its implications?

A. Of course I understand that there was a procedure ongoing with the European Commission, yes.

Q. And did you see the General Court’s judgment? Have you seen that in your --

A. I have not read it, no.

Q. So in your role as head of interchange fee, you have never been educated as to the implications of the Commission’s decision and the judgments of the European Court?

A. I understand that there was a proceeding ongoing with the European Commission, yes.

Q. Have you ever been told by MasterCard that interest from credit cards should be taken into account when fixing an interchange fee? Are you aware of that?

A. I have not been aware of that, no. But of course all the revenue sides that the bank can take into account, like, for instance, card fees, also interest fees, we looked at those market elements as part when we reviewed the markets. So --

Q. Have you ever carried out an exercise where you have
MR JUSTICE BARLING: Mr Hoskins, perhaps it would be more expedient if we asked some questions ourselves and then Mr Brealey can come back if he needs to, and then you can --

MR HOSKINS: It saves me bobbing up twice, potentially.

MR JUSTICE BARLING: Yes.

Questions by THE TRIBUNAL

MR SMITH: Mr Willeart, I have got what I fear are some rather basic questions on the operation of the MasterCard system. If you don't know the answer, please don't worry, just say so.

I think I will be avoiding discussion of information that's confidential, but if we do stray into confidential territory perhaps you will say.

Just to begin with, some terminology. MasterCard obviously is a four-party system, and I'm going to describe the four parties in my questions as customer issuing bank, although I know it can be a financial institution, acquiring bank and then merchant, and then participating in this scheme respect the rules, there is no necessarily exceptional or limited. When we are talking about commercial agreements, MasterCard can engage with commercial agreements, and what it does is it gives financial incentives to issuing banks to distribute and promote the card basis in the MasterCard brand.

You mentioned specifically about exclusivity, and I can talk a little bit about that as the general manager, I have been, for the Nordics and now for France. We typically do not have agreements where we are exclusive working or, if you wish, locking in a customer with MasterCard. What we are doing is we are providing a financial incentive and in return, of course, we are asking that this bank drive the volumes, drive the spend.

What happens if the bank decides halfway through, okay, I want to get rid of MasterCard, I want to work with Visa or somebody else? They can fully do that. There is not a protective measure in that contract, but they will not get the benefits of the contract. They might agree with another scheme, a new contract.

So that is typically the practice that we make the agreements. We make a financial agreement, the bank will benefit from some financial incentives, could be a discount on the pricing, could be an additional financial incentive linked to the performance of the card portfolio.

MR SMITH: And are there similar, you call them commercial agreements between MasterCard and acquiring banks?

A. There is agreements with acquiring banks, absolutely. That exists. There are probably less so (inaudible) agreements, but that exists.

MR SMITH: So in the case of acquiring banks it is much more likely that you have really just got the licence with MasterCard and very little on top by way of supplemental commercial agreements?

A. It depends, so I would agree that is typically what happens. But in some cases, for instance when we are deploying, let's say, contactless infrastructure, to accept contactless cards might give the acquirer an incentive to put his terminal in the market, for instance. That could be an example of that. Or to run a campaign with a merchant, for instance.

MR SMITH: Yes, I see.

To be clear, as between issuing banks and acquiring banks, there's no express agreement apart from that contained in the MasterCard scheme rules?

A. Typically not.

MR SMITH: Now, I just want to understand exactly the flow
of monies when one has a transaction using the
MasterCard payment system.
So let's suppose that a cardholder goes into a shop
in London, using his MasterCard and purchases a product
for a certain consideration. Obviously, the transaction
is processed using the merchant's equipment, the card
reading equipment, and I will come backing to that, if
I may. But let us assume the transaction is authorised
and goes through. In terms of the money flow, the money
taken from the cardholder, either from his current
account if it is a debit card or by way of the extension
of credit from the issuing bank to the cardholder if it
is a credit card.
So assuming no bilateral agreement as to
interchange, at this point the issuing bank will pass
money over to the acquiring bank --
A. Correct.
MR SMITH: -- but it will hold onto the MIF?
A. That is correct, yes.
MR SMITH: Does it hold onto anything else, for instance,
the scheme fee which I understand is payable --
A. No.
MR SMITH: It doesn't?
A. No. So the scheme fee in this case, MasterCard will
have a separate billing of its fees directly to the
issuer.
MR SMITH: I see. Thank you.
So the only thing that the issuing bank holds onto
is the MIF?
A. Correct.
MR SMITH: And it passes the net amount over to the
acquiring bank?
A. Yes, that is correct.
MR SMITH: And the acquiring bank then deducts a further
amount, representing the cost of its services to the
merchant?
A. That is correct.
MR SMITH: And passes what one could call the net net amount
to the merchant?
A. That is correct.
MR SMITH: Again, there's no deduction for the MasterCard
scheme fee, that's separately accounted for?
A. No, absolutely, that is correct.
MR SMITH: Just assist me on this. The MasterCard scheme
fee, obviously paid by both acquiring bank and issuing
bank, but separately from the £10 transaction that I'm
hypothesising, is that a flat fee or is it ad valorem,
or does it depend?
A. It is typically linked to the drivers. So they are
linked from the issuing bank to the number, volume of
the transactions typically.
Also fee for the number of cards they have in the
portfolio, but typically it is the volume, the turnover
on the card which drives that.
MR SMITH: Now, going back to this chain of payments,
I presume that there is a dovetailing of the provisions
in the MasterCard scheme with the arrangements at either
end of the scheme, in other words, with the issuing bank
to the cardholder and with the acquiring bank and the
merchant, authorising these deductions.
And just to expand on that before you answer.
Looking at the relationship between the merchant and the
acquiring bank, the agreement between those two entities
will define what the acquiring bank is allowed to
deduct, and that's the merchant service charge?
A. The acquiring banks make their commercial agreement with
the merchant, absolutely.
MR SMITH: Equally, at the end other end when you look at
the relationship between the issuing bank and the
acquirer, there will be some form of provision whereby
the cardholder agrees that his account, whether it is
his current account or his credit account with the bank,
can be debited with the amount of the transaction?
A. Correct.
MR SMITH: And would I be right in thinking that in terms of
the deductions that, say, the issuing bank can make when
paying the acquiring bank, it is only entitled to make
agreed deductions, it can't make the deductions that it
feels on any one day able viable to make?
A. Absolutely.
MR SMITH: These are stipulated.
A. Absolutely, that is my understanding.
MR SMITH: So the only deduction that an issuing bank can
make is either the MIF, or if there is a bilateral
agreement, the amounts stipulated in the bilateral
agreement?
A. Correct.
MR SMITH: Now, just help me -- if you don't mind can we
confirm this to the UK in terms of the size of issuers
versus acquirers in the UK. We have heard from other
witnesses that there are perhaps 20 or so acquirers in
the UK. Does that fit with your understanding?
A. Yes, that could be the case.
MR SMITH: But you are sounding quite tentative. It is not
perhaps your --
A. It seems to me a lot. It could be that it was a lot at
that time. Typically there is a bit of consolidation in
the market, so it could be that it's less now than it
was 20 -- over time, yes.
MR SMITH: So 20 feels a higher figure to you?
A. Yes.
MR SMITH: In terms of the number of issuing banks, can you help us on how many issuing banks might be issuing cards in the UK?
A. Maybe 20 as well. 20 as well.
MR SMITH: Right. That’s helpful.
Now, we have established that there isn’t a direct agreement between the issuing bank on one side and the acquiring bank on the other side. It is the umbrella agreement that constitutes the scheme rules.
So how exactly does the payment stream work? We have obviously got millions of transactions a year done with MasterCards, and somehow one has got to ensure that the £10 in my hypothetical example moves from the cardholder account into the account of the merchant.
That’s what the interchange system does; am I right?
A. So in this case there is different -- I mean, I need to explain a little bit.
When there is a transaction happening, at some point in time the transaction is authorised, the merchant -- the cardholder pays it. The merchant at that point, where there is a transaction which is authorised by the issuer, he says, okay, I’m willing to accept this transaction. Then what happens during certain cycles during the day, there is an exchange of information in terms of how much is the specific amount and specific additional information is exchanged between the issuer and the acquirer. Then the issuer and the acquirer, they hold accounts to settle against each other. So there is a sort of compensation made every day, for instance, where the issuer and acquirer will settle their accounts.
That is the way it works. So at some point in time, at the end of the day, as an example, the issuer and acquirer will net out and one owes the other and they will make the payment. So that happens in this case, this is happening. If the transaction is processed by MasterCard, MasterCard offers its service to the customers to make these settlements. This is settlement services.
MR SMITH: So essentially MasterCard keeps a running account?
A. Correct. Every bank member has a settlement account, correct.
MR SMITH: Each bank member as a member. And you net off the transactions as against each participating bank and the net figure is paid on a regular basis?
A. That is correct.
MR SMITH: Is that daily?
A. My understanding is it is daily.
Sweden operates on a basis of bilaterals whereas in the UK the evidence we are having is that they are actually 
very rare.

A. I think there is various reasons, I think the historical reasons why the banks in Sweden have agreed to use bilateral. I think there was a bit of the common market practice, and my understanding also was that this was done under, let’s say, the support and the supervision of the local competition authorities to complement a bilateral agreement system. Which does not mean that there was no fallback, but they implemented a bilateral system.

In other markets it happens, the customer is told it doesn’t need to do so, to set these bilaterals, and it relied on the multilateral interchange fee, because it felt that going to bilaterals would not change the outcome and the multilateral interchange fee was the right level.

But I would say in most of the cases there was a multilateral interchange fee. If you look across Europe, it is the most commonly used.

MR SMITH: In general terms it is a MIF?

A. Exactly, and there is a few exception countries, if I can say so.

MR JUSTICE BARLING: Maestro was bilateral in fact even in the UK.

A. Yes.

MR JUSTICE BARLING: Mainly it was on the basis of a bilateral agreement.

A. That was my understanding as well, correct. Even MasterCard didn’t set those bilateral rates because they were agreed, but my understanding is, well, that wasn’t a bilateral...

MR JUSTICE BARLING: Yes.

MR SMITH: As I understand it, it is a less common scenario now than it was in the past, but can I ask you what happens when the issuing bank and the acquiring bank are the same legal entity? So we have exactly the same person at both ends, or not quite the ends but both ends of the chain.

In that case do the issuing bank and acquiring bank go through the interchange system or does the entity simply deal with it itself?

A. It depends a little bit. Most of the cases they do not go to the interchange system because it is as we call it an on us transaction. It is a transaction where the issuing and the acquiring entity is the same, so it remains --

MR JUSTICE BARLING: It is "on us", isn’t it?

A. Exactly. That typically does not go through the interchange system.

MR SMITH: So in effect the bank will settle with itself because it’s got the data at both ends that it can work out --

A. That is correct.

MR SMITH: -- the position on its own?

A. Yes.

MR SMITH: The last area I wanted to ask you about was about acquiring banks.

Now, acquirers, would it be the case that they attempt to acquire transactions not just for MasterCard but also for Visa and American Express?

A. Absolutely. So acquirers typically want to have the relationship, and the biggest possible relationship, with all the payment transactions that a merchant offers.

So typically in the first place Visa, very clearly, and then with Amex of course it depends if they are entitled to get an Amex licence, if they are entitled to capture those transactions.

MR SMITH: One can see the business sense. If I’m an acquiring bank I want to be able to say I can process all kinds of transactions, you choose which ones you want me to process for you.

A. Absolutely, I agree.

MR SMITH: I assume that means that there is a degree of common hardware in terms of the equipment that is at the merchant’s shop, so that one card can be processed with one piece of equipment?

A. That’s typically in the markets that we know. Here very much the case, yes.

MR SMITH: So, so far as the cardholder is concerned, the transaction looks exactly the same whether it is a Visa card, a MasterCard or an American Express card?

A. Absolutely, they put in the transaction and put in the card in the terminal and they pay.

MR SMITH: And then, at least if it is an electronic transaction, there is some communication between the merchant’s terminal and the acquiring bank?

A. Correct.

MR SMITH: But then I assume the streams diverge and one of the functions that the acquiring bank undertakes is to shunt the data that it acquires from the merchant to the appropriate system?

A. Correct. It could be Visa and MasterCard goes to the acquirer. It could be that if it is Amex transaction it goes directly to Amex, for instance. And from the acquirer it can go, for instance, to a MasterCard or to a Visa, let’s say, platform.

MR SMITH: Presumably, we mentioned the technical manuals...
MR SMITH: There is typically umbrellas of products. So under the

A. That is correct.

MR SMITH: It might be the same object but the detail is
different?

A. That is correct.

MR SMITH: And that is one of the services that an acquirer
provides?

A. Correct.

MR SMITH: Can a merchant choose, if it wants to, to use
multiple acquiring banks for its transactions?

A. Absolutely. A merchant can choose to say I want -- For
my MasterCard transaction I want to use this acquiring
bank, for my Maestro transaction I want this bank, for
my Visa cards I want to get a better deal with a
different acquirer". So they can fully choose which
acquirer they use.

MR SMITH: How, finally, can that division be sliced? You
have divided it quite logically between different
payment schemes. So you might have an acquirer, as you
say, for Visa and an acquirer for MasterCard. Can one
differentiate between debit and credit cards?

A. Yes. For instance, and I made the example of Maestro
and MasterCard, the merchant can make a specific

agreement with one acquirer to only process one brand of
product. That can happen, yes.

MR SMITH: But presumably there has to be some sort of
agreement between the merchant and his various
acquirers --

A. Typically they have multiple agreement, to decide on
which product they process. Some merchants even have
multiple acquirers for multiple products just to allow
to not be dependent on one acquiring bank.

MR SMITH: Like issuing banks, acquiring banks essentially
are selling a core product, the payment system, that
do’s’t really differentiate. Because one has the
common MasterCard system and the honour all cards rule.

In effect, the service that any MasterCard cardholder
gets is exactly the same. The card is used for payment
and the money is moved from his account to the merchant.

A. Correct.

MR SMITH: And that service will be the same whether the
acquirer is one acquirer or not?

A. Correct.

MR SMITH: In terms of the honour all cards rule, am I right
that it applies as an obligation to honour all credit
cards, and separately as an obligation to honour all
debits cards in the MasterCard scheme?

A. There is typically umbrellas of products. So under the

MasterCard product, all of the MasterCard products would
be contained for the consumer side, for instance. If
you have a premium card or a standard card, that would
be what we call all under the umbrella of the
MasterCard. At the same time, the acquirer is not able
to differentiate between I accept a card for this issuer
or from another issuer. This is what we call the all
issuer aspect of this honour all cards rule.

MR SMITH: Sorry, let me unpack that a little bit.

So one has a premium card that is created by
MasterCard and issued by banks. And one is not as
a merchant entitled to discriminate between cards of
that sort?

A. So if you are accepting a MasterCard standard, you are
also accepting a World card --

MR SMITH: I see. I suppose my question is how many
umbrellas are there? Is it the case that every
MasterCard with the MasterCard logo has to be accepted,
or is there a broad differentiation not based on issuer,
but based upon the type of card which limits the honour
all cards rule?

A. For instance, Maestro is typically a different
acceptance brand. So typically the merchant decides
which brands it accepts. Under the MasterCard umbrella
they would accept all MasterCard credit cards. Maestro

would be different, where they can select, accept or
don’t accept that product, and I understand also in
the UK the DMC MasterCard is also a separate product
that they can accept.

So there is the choice for which products they
accept or they don’t accept.

MR SMITH: I see. I can understand it more clearly from
Maestro because that was separately branded, but you are
saying that the MasterCard debit card is seen as under
a separate umbrella compared to credit cards?

A. That is my understanding.

MR SMITH: Again, that is worked out in the detail of the
MasterCard scheme?

A. Yes.

MR SMITH: Going back to this question, then, of
differentiation. How is it that an acquiring bank can
improve its position vis-a-vis merchants to provide
a better service? What can it do?

A. I’m not an acquiring bank so -- Typically they would
compete on service, they would compete on the type of
terminals they provide, technology they provide,
maintenance they provide. Of course they will also
compete on the pricing that they provide to their
merchants, and to give you an example, you have got
merchants with a presence across multiple countries. So
MR SMITH: In terms of competing on price, when one looks at the merchant service charge, I think it is uncontroversial that the interchange fee is a large part of that charge. Do you find that there are acquiring banks who are approaching MasterCard with a view to negotiating a lower MIF for transactions that they process?

A. So the MIF, that is applicable across the market, so we typically do not make a specific arrangement with one acquiring bank. No. We typically don’t do that.

MR SMITH: When you say you don’t do that, is that because no one has asked you to do that? Obviously we are all here because a large number of retailers consider that the MIF was too high and that they were having that cost passed onto them by the acquirers, although we have not heard evidence on this. But I can’t imagine that the acquirers weren’t aware of it. So it must be a significant advantage if an acquirer could say, look, my price to you, the merchant, is less because I have negotiated a cheaper deal with MasterCard. But in your experience that didn’t happen?

A. No, that typically didn’t happen. I am sure the commercial pressure from the acquiring side was there and that the sales team who took care of the acquiring side might have gotten those questions. But typically we didn’t do that because if you would give one advantage specifically to one acquiring, you create a competitive disadvantage in the market because the other acquiring would not be able to offer the same rate. So the rate in the market needs to be the same for all acquiring, otherwise if I give one acquiring the benefit then he can go off to the market with a specific benefit.

MR SMITH: So one of the things that informs the MasterCard MIF is it should be non-discriminatory?

A. Exactly.

MR SMITH: As regards acquirers.

A. Absolutely.

MR SMITH: You might differentiate between products, but you would not otherwise differentiate --

A. Absolutely, that was essential, yes. MR SMITH: So if an acquiring bank wants to try and achieve a different interchange fee, the only route, as far as you are concerned, would be the bilateral route to negotiate with the pool of issuing banks?

A. Absolutely, yes.

MR SMITH: Thank you. That was a very long line of questions, but thank you, Mr Willeart.

PROFESSOR JOHN BEATH: Just following on from that, the way we are seeing this four-party or the four-stage system, the circle of flows, we have got these two rather active people in the business: the merchants who are complaining about something and the issuers who are desperate to get profits. And there’s this very passive but crucial element, the acquirer.

Do these acquirers exert no pressure at all?

I mean, after all the MIF is supposed, does indeed, to allocate costs between -- somehow balances between acquirers and issuers. In setting that balance, you might expect acquirers to have some voice. Do they?

A. So for sure acquirers definitely did have a voice and they definitely also did -- your point about looking for influencing the MIF, getting a lower MIF. For sure, acquirers definitely are vocal. But I was not necessarily dealing directly with acquirers at the time.

But also when we set interchange fees at the time we also took that perspective into account. So it was not just there was a look at what needs to be done at the issuing side, what respect to the merchant acceptance, there was also the way that the acquirers could deal with whatever balance was put to the market.

PROFESSOR JOHN BEATH: We got this pie, the MIF, and the sharing does seem to be asymmetric.

A. Correct.

PROFESSOR JOHN BEATH: You might have thought that in a strong market, to get a share of the pie there would be rather more bargaining going on?

A. But I think that -- I mean, there was the -- you mentioned the imbalance because I think the costs were also more higher on the issuing side. I think that is the reason why there is the balancing mechanism. But --

PROFESSOR JOHN BEATH: So the acquirers are fairly happy with the way costs are balanced, are they, in the MIF?

A. Of course, being -- they are looking at their costs and they typically would like to see lower costs. So for sure they would also, at the same time that the issuer would always complain that interchange is too low, the acquirers would always complain that the interchange is too high. It is a fact in the balancing mechanism, both

MR HOSKINS: You will see it comes from first Niels, figure 33, which is D3, tab 3, page 249. That gives you the trajectory.

MR JUSTICE BARLING: Thank you very much.

MR HOSKINS: I just want to deal with two topics with you. I will deal first with Maestro, as that's what we have just been dealing with.

We know that the Maestro MIF in the UK, back in the 2000s, was set by S2, not MasterCard.

A. Mmmm.

Q. If MasterCard had been free to set the rate for Maestro in the UK during that period, what process would MasterCard have followed to determine what you describe as a competitive rate? What process would have been followed?

A. I think we would have followed the process where, as I described, we would have taken a consultation on the market to understand the costs that issuing banks and acquiring banks faced to deploy the product. So there would have been a process where there would have been consultation, in this case with an external company that collected the costs. They would do the survey in the market with the issuing banks, with the acquiring banks and they would come with a result which was the average costs to process this transaction in the market, that would result in the cost basis.

Of course, we would also look at the same time about what is the competition in that market. So what would be competitive products to this Maestro proposition. We would also look at, if we look at the specific levels of interchange per transactions, what this -- the incentives we would like to give to stimulate the deployment of more secure technology in the market. And then we would have put together a proposal that would have set the rate that would come to this -- to take this information into account, the cost level as well as the competitive aspects, yes.

Q. You said you would look at what competitive products are. Functionality, as Mr Brealey has described it, does it play any part in this process of setting a competitive MIF?

A. If the functionality leads to higher costs for the issuing side, or other costs in their cost system then we would take it into account. We would not take into account that there would be a lower acceptance gap necessarily in the US because the domestic interchange is not supposed to deal with that. The domestic interchange is to deal with the domestic market.

Q. Then going back onto a different topic, it probably
Q. What is the purpose of this type of document, just in terms of how does it fit into the process of arriving at an interchange --
A. So the process to come to an interchange rate is typically a process that takes several months' time, where there is this phase of collecting the information from the local market, of collecting the local market cost information. Working together with the local market seems to take the input from the local issuing banks, local acquiring banks, the merchant side. And then based on this information there is a proposal made to the Committee, which is called the European Interchange Committee, that discusses, challenges, asks questions to ensure that the right balance is set. And in that committee there is multiple people, multiple functions, if you wish, represented, people from the merchant side, people from the issuing side, people from the product side, legal team, and they would discuss the proposal that has been prepared by the interchange team. And then they would either endorse it, ask questions, review it and move on. But this is, let's say, the discussion document that is proposed in the Interchange Committee.

MR HOSKINS: We see from this document, the heading is "European Interchange Committee and its proposal". Is this what you were talking about when you were talking about a proposal --
A. Absolutely.

Q. I have no idea, but have you seen this particular proposal before?
A. I have seen this proposal, yes.

Q. You have. We don't need to go into great detail, but just to give a flavour of what's taken into account and how the final decision is reached, perhaps by reference to headings in this document, can you just give a sense to the Tribunal of how this document demonstrates what you say is the logic behind the setting of a MIF rate?
A. It is very important, for instance, when we are setting a new product, premium product, for instance, we understand that you are setting a higher interchange, so you want to understand is this something that can be acceptable in the market, does this give benefit, additional sales to the merchant, one example. The other example is, for instance, when you are setting out contactless technology, if you are setting a specific rate of interchange will this rate allow merchants to deploy terminals that are capable of accepting contactless transactions. So we are driving towards more secure transactions and secure payment system, so we want to ensure that it makes sense for the whole eco-system.

Q. Why do you take, or do you take account of how acquirers might react?
A. Acquirers, of course, are very important in the eco-system as well. Just to give you one example, there is not only the economics, but there is also the technical specifications.
We can come up with a very creative rate to make a new product in the market or to deploy new technology. But if acquirers cannot implement it in the system, we can never deploy the product in the market. So all parties – it needs to work for all parties otherwise it doesn’t work.

Q. How do acquirers fit into the economic eco-system? You mentioned that when you moved on to the technical aspect.

A. We typically also looked at how, if acquirers could position this product into the market. So if they would be able to sustain this, include this new product in their pricing towards merchants. So if we introduced a new interchange fee or launched a new product and we knew that this needed to be included into the contractual agreements between the merchant and the acquirer, we tried to make sure that there was sufficient time and sufficient possibility to position this into the merchant agreements.

MR HOSKINS: I don’t have any further questions.

MR JUSTICE BARLING: Thank you. Right. Well, Mr Willeart, thank you very much indeed.

We will start again at 2.10 pm.

(1.10 pm)

(The short adjournment)

(2.10 pm)

MR HOSKINS: Good afternoon, sir. Mr Brealey bamboozled me by giving me a bit of paper to put in a file just as you walked in, so if you would bear with me.

MR JUSTICE BARLING: Keep you on your toes.

MR HOSKINS: I will gather my thoughts. Thank you.

Just to update you on the Mr von Hinten-Reed, we don’t consent to it, so there is going to have to be a little spat. But I think Mr Brealey would prefer to do that tomorrow afternoon, because obviously it’s his application. I’m happy to do it then.

MR BREALEY: Apparently it is at D2.1, tab 8.

MR JUSTICE BARLING: So we have to read it, then?

MR BREALEY: Apparently.

MR JUSTICE BARLING: I haven’t read it yet.

MR BREALEY: D2.1, tab 8.

MR JUSTICE BARLING: I suppose we need to do it now rather than when the witnesses are (...). Tab 8.

MR HOSKINS: Sir, I think Mr Brealey wants to make the application to morrow.

MR JUSTICE BARLING: Yes, I will forget otherwise to take it. D what?

MR BREALEY: D2.1, tab 8.
introduced later, it was in first Harman. And Mr Harman’s figure is that the value is about 4.4 million per annum. So that’s for a period for end of 2006 to present day, 4.4 million per annum. Then the addendum to second Mr von Hinten-Reed, which is the response to Harman as it currently stands, you will see the reference there, his total is 24.5 million. So you see the disparity is about 40 million odd against 24 million odd. That’s the current evidence before the Tribunal.

MR JUSTICE BARLING: Until this came along?

MR HOSKINS: Until this came along. So it is not that this is simply our response. What this actually is is an attempt to resile from a response. It is not that Sainsbury’s hasn’t had a chance to deal with it, it has dealt with it, but now Mr von Hinten-Reed wants to resile from the position that is in the evidence and take a different view.

MR JUSTICE BARLING: Right.

MR HOSKINS: If you have the third expert report that Mr Brealey referred you to --

MR JUSTICE BARLING: Which --

MR HOSKINS: I have it at D2, tab 8. Sorry 2.1, tab 8.

MR JUSTICE BARLING: The one that’s objected to?

MR HOSKINS: That is correct.
A. Yes.

Q. Can you confirm that that is your witness statement?

A. That is my witness statement.

Q. There should be a signature on the last page.

A. Yes.

Q. Is that your signature?

A. That is my signature.

Q. Can you confirm that the contents of this statement are true?

A. They are true.

MR HOSKINS: Mr Brealey will have some questions.

Yes, there is a confidentiality issue.

MR JUSTICE BARLING: Right.

MR BREALEY: It is all blueed, isn’t it? The whole witness statement I think is blueed?

MR HOSKINS: It is.

MR JUSTICE BARLING: Right. This is an opportune time to say that I have received a communication through my clerk from someone who I’m not sure is here today, a legal journalist, who I think travels from Brussels.

I don’t know whether she is present or not?

MISS KENNER: I have asked if we could be let known –

MR JUSTICE BARLING: Are you Miss Kenner(?)

MISS KENNER: Yes.

MR JUSTICE BARLING: Right, so you are here.

The problem is I am sure that the parties would try and give anybody who asked them as much indication as they can of when they are going to need to hear some evidence in camera, but there is an obvious problem. As you have seen this morning, because the default position is that we sit in public, not in camera, it is incumbent on counsel to do their very best to see if they can conduct the cross-examination without going into camera.

And you saw that that’s what counsel did this morning, and counsel has made attempts to do that on other occasions. But there are just some times when it becomes impossible without having to refer a witness expressly to something that is a business secret or is otherwise confidential. And even when it is possible to ask the question, there are times when the witness feels very inhibited in giving a proper and full answer.

So, I’m afraid -- can I encourage the parties, at the request of Miss Kenner and anyone else in a similar position if they do ask you, to give them the best estimate if you can, especially if they are travelling, of when a witness is likely to be heard and whether they are likely to give their evidence, or a substantial part of it -- I appreciate you can’t give an exact guarantee, and that’s the problem because the order in which witnesses are called is not always easy to orchestrate
in advance. Sometimes a witness is ill or unavailable, or there's another reason why you have to call a witness out of the anticipated order in which you were going to call them. So we do the best we can and I can assure you that we do try at all times to conduct the hearing in public, except when it is impossible to do so. This particular witness's evidence is almost entirely subject to the confidentiality ring, and so I am sorry, I know it means it is inconvenient, but that's the way we have to go. So can I ask anyone else who is not within the confidentiality ring to leave.

MR BREALEY: We are almost finished with the witnesses of fact. Just flipping through, for example, the claimant's expert reports, there's not a great deal of yellow or blue. I will have a look at the defendant's. So it may well be that we can give some indication. A lot of it is white.

MR JUSTICE BARLING: Have you been in touch, Miss, with the parties, solicitors or anyone, to ask?

MISS KENNER: I just asked on a daily basis.

MR BREALEY: I do not want to put any burden on Mischon de Reya, but I am sure that I can let people know the extent to which I am going to cross-examine on blue, but I will leave it --

MR JUSTICE BARLING: Yes. I will just encourage the parties, if they can, to try to give as much information as possible to anyone in the position of this lady, who needs to know before she buys her train ticket whether she is going to be allowed in or not. I know it is very difficult, but there we are.

Thank you very much.

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Opus 2 International
Official Court Reporters

End of in camera session
(The court adjourned until 2.00 pm on Thursday, 11th February 2016)
February 10, 2016

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

Day 10 - Redacted

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