

OPUS 2

INTERNATIONAL

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

Day 20

March 11, 2016

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1 Friday, 11 March 2016
2 (10.34 am)
3 HOUSEKEEPING
4 MR JUSTICE BARLING: Morning, Mr Brealey.
5 MR BREALEY: Morning.
6 MR JUSTICE BARLING: Morning, all. You have had a busy few
7 days.
8 MR BREALEY: I would say that.
9 MR JUSTICE BARLING: Caught up on sleep, I hope? No?
10 MR BREALEY: No, that is next week.
11 MR JUSTICE BARLING: Just a couple of points on the
12 timetable. I am afraid we need to rise at 4 today. If
13 you feel you would like an extra quarter of an hour, we
14 can easily take a shorter lunch.
15 MR BREALEY: I am sure we have time.
16 MR JUSTICE BARLING: Then the other thing, I think, just to
17 make clear, is that at the moment we are sort of
18 pencilled in, I think, to Wednesday, aren't we?
19 MR BREALEY: Yes.
20 MR JUSTICE BARLING: If we did have to sit on Thursday, we
21 could only sit until lunchtime, just so you know, and we
22 can't sit Friday.
23 MR BREALEY: I would have thought the four days should be
24 sufficient.
25 MR JUSTICE BARLING: I would have thought so, but just in

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1 case, that is the position.
2 Closing submissions by MR BREALEY
3 MR BREALEY: Just reflecting on that, what I would like to
4 do in my final slot, as it were, is highlight certain
5 points of principle that may not have been so clear to
6 the Tribunal, and then I think I would quite like to
7 follow the logic of our closing. Obviously I am not
8 going to read it out but drawing, you know, attention to
9 the main points, but at the same time responding to
10 Mr Hoskins and MasterCard's skeleton.
11 I will not go to too many documents. As you have
12 requested, we have tried to put it in the text.
13 MR JUSTICE BARLING: Yes. Thank you. Thank you for that.
14 MR BREALEY: We will go to a few, and with all promises,
15 sometimes they just get postponed for a moment. The
16 very first issue I want to go to is regulatory context.
17 I would like to go to a few documents, but after that
18 I will kind of basically go through the closing.
19 MR JUSTICE BARLING: Yes. Right.
20 MR BREALEY: But there is one point, one quite important
21 point, that I would like to nail at the beginning which
22 does involve going to just a few documents.
23 MR JUSTICE BARLING: Okay.
24 MR BREALEY: So this point is the issue of credit write-offs
25 which is quite a big chunk of MasterCard's MIF, credit

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1 write-offs and debt collection. It is relevant,
2 obviously, to debt collection, but it is also relevant
3 to the regulatory context.
4 What I would like to do -- and I will be flipping
5 between our closing and MasterCard's closing -- I would
6 just like to refer the Tribunal to how MasterCard put
7 this credit write-off, or the set of costs at
8 paragraph 350 of its closing, that is page 116.
9 Just to flag where I am going, I am going to have
10 a look at paragraph 350 of MasterCard's closing, and
11 paragraph 15 of ours. This is in the regulatory context
12 section, but it is important for the exemption.
13 I want to flag the issue and then I want to go
14 through certain documents.
15 This is paragraph 350 of their closing, their
16 skeleton. In section 5 of this first report, Dr Niels
17 conducted a cost-based analysis which he referred to as
18 the "adjusted benefit cost balancing approach". We have
19 called that the "issue as cost approach".
20 This is important:
21 "This uses the same subset of costs used by the
22 Commission in 2002, and by MasterCard throughout the
23 claim period, and considers the extent to which
24 merchants should contribute to costs associated with
25 credit. Dr Niels concludes it would be reasonable but

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1 conservative to attribute at least a quarter/half of
2 those issues as costs to merchants."
3 But the bit I want to take issue with, and I will
4 come on to it, is that it is simply incorrect to say
5 that the same subset of costs were used by the
6 Commission in 2002. That is the bit that I want to
7 highlight.
8 So if we just put their skeleton away and go to our
9 paragraph 15, this is where we deal with the -- so what
10 MasterCard are referring to there, obviously, when it
11 says, "the Commission in 2002", is the Visa exemption.
12 As we did before, we referred to the Visa II exemption
13 decision, so, paragraph 15, we set out the background.
14 It allowed Visa, until 2002, to base its MIF on three
15 categories of cost: the cost of processing transactions;
16 the cost of providing a payment guarantee; and the cost
17 of the Free Funding Period funding period.
18 Now, it is quite important to define what we mean by
19 the cost of the Free Funding Period funding period.
20 These three categories of costs were, at the time,
21 perceived by the Commission as a proxy for the cost of
22 issue as to providing credit. Then we go on, as we did
23 in opening, that this exemption decision should have put
24 MasterCard on notice that its four-party system would
25 not be a joint service, that it was likely to be

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1 considered a restriction of competition, not objectively
 2 necessary, and then:
 3 "As to exemption, it was unlikely that MasterCard
 4 would receive an exemption on subjective criteria ..."
 5 I will come on to that bit later on, and then there
 6 was a doubt about whether the Free Funding Period
 7 funding period, now let's call that the 28-day period:
 8 "... the Free Funding Period funding period would be
 9 accepted in a domestic context."
 10 We have seen this time and time again throughout the
 11 trial. That is footnote 44:
 12 "This warning was particularly relevant to the
 13 UK market, where banks earn considerable sums from
 14 interest".
 15 Then, again, we will come on to that, but we know
 16 all about that, the Free Funding Period funding period
 17 and the interest.
 18 The third is new:
 19 "The exemption did not exempt any costs relating to
 20 credit write-offs, bad debts. The Visa exemption
 21 related to the cost of Free Funding Period funding, not
 22 to credit write-offs."
 23 This is quite important, because that is big chunk
 24 of MasterCard's MIF.
 25 If we could remind ourselves what we are talking

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1 about here, we need to go to Bundle E3.6, tab 126, so
 2 this is the E3.6, tab 126, which is the infamous, or
 3 famous, Edgar, Dunn cost study that relates to 2007
 4 data. If you remember, Mr Sidenius said it should be
 5 regularly updated, and it hasn't been. But this is the
 6 2008 cost study, so this is the basis upon which
 7 MasterCard are setting the MIF.
 8 If one goes to internal page 12, which is 2508.1.
 9 Again, I know this is old ground but it is quite
 10 important, so 2508.1. The figures, I understand, are
 11 confidential, but the categories are not:
 12 "Actual credit write-offs ..."
 13 We get a percentage:
 14 "Collections department, percentage, fraud, and
 15 fraud investigation."
 16 But I emphasise, "credit write-offs, collections
 17 department". If one goes a bit further on to internal
 18 page 16, so bundle page 2512, internal 16, the actual
 19 credit write-offs, so the cost category relating to
 20 actual credit write-offs and balances on accounts,
 21 uncollectable, and then collection, so that is
 22 essentially the write-off, that is actual credit
 23 write-offs. And then collections, at the bottom, the
 24 cost of monitoring/managing the collection of
 25 outstanding and past debt. Costs include rental, space

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1 costs, collection costs on delinquent accounts, costs of
 2 letters, telephone calls to cardholders whose payments
 3 are due, amortisation of equipment, but quite a lot in
 4 actual credit write-offs and collections, all of which
 5 MasterCard are putting a chunk onto the merchant.
 6 I will not go through it, but just for the
 7 Tribunal's note, I cross-examined -- well, I mean,
 8 I asked Mr Sidenius to expand on these. This was at
 9 Day 11, internal pages 36-40. So Mr Sidenius expanded
 10 on these various descriptions at Day 11, internal
 11 page 36. So that is what we are talking about. We can
 12 put E3.6 away.
 13 Then we go to Mr von Hinton Reed's second report
 14 at D2.1. Again, we have been through this before, but
 15 it does assess -- this is his famous table, 8.1 and 8.2.
 16 It starts on page 550. It starts at paragraph 637.
 17 This is his Table 1, which we have been through this
 18 opening, and with the witnesses, but one sees there the
 19 headings, and we see that the credit write-offs --
 20 I think Table 8.1 is confidential, but Table 8.2 is not,
 21 but you see the significance of credit write-offs in
 22 itself, and of collections department. That is in
 23 Table 8.1. In 8.2, it gets all lumped together with the
 24 funding costs,
 25 I am showing you this table to highlight the fact

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1 that the credit write-offs is a significant proportion
 2 of MasterCard's MIF, and one sees there at
 3 paragraph 639, we will come to it in a moment, Dr Niels,
 4 and this is in the skeleton at 350, MasterCard's
 5 skeleton at 350, Dr Niels argues that at least
 6 25 to 50 per cent of the cost of credit benefits should
 7 be included in the MIF, so he is saying that a quarter
 8 to a half of that credit write-off should be offloaded
 9 onto the merchant.
 10 Now, I think we can put that away, but if one
 11 remembers in opening I took the Tribunal to this
 12 because, basically, if you take out the credit
 13 write-offs and the funding, you actually get to the
 14 0.2 per cent, which is various ways to skin a cat, but
 15 it comes around to 0.2 per cent if you take this Free
 16 Funding Period funding and credit write-offs.
 17 So that is the HR2.
 18 If I go to, now, D3, tab 3, which is Dr Niels'
 19 report --
 20 MR JUSTICE BARLING: Sorry, this is my fault for not reading
 21 it carefully enough, but in the credit -- the 28-day
 22 Free Funding Period funding wasn't part of that, or was
 23 part of that?
 24 MR BREALEY: The 28-day funding is a completely separate
 25 head. I mean, we could go --

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1 MR JUSTICE BARLING: No, no, don't worry, but I just wanted
 2 to be sure that that -- I didn't think it was, but yes.
 3 MR BREALEY: This is why I want to emphasise the point that
 4 it is simply wrong to say that MasterCard are using
 5 credit write-offs that were used by the Commission in
 6 2002.
 7 MR JUSTICE BARLING: Yes. Okay. So which one was it now?
 8 MR BREALEY: D3, tab 3, and it is page 307. This is the
 9 paragraph at 307, 589. This is the paragraph I took
 10 Dr Niels to. This is the paragraph that is referred to
 11 in paragraph 350 of MasterCard's skeleton. And these
 12 four lines are essentially the sole justification that
 13 we got from Dr Niels as to why he was offloading 25 to
 14 50 per cent of credit write-offs onto merchants.
 15 I asked him what did he base it on and he said, "It is
 16 a value judgment". That is Day 16, page 118. Day 16,
 17 page 118.
 18 So this is just a value judgment that he thinks that
 19 25 to 50 per cent of credit write-offs should be
 20 offloaded onto the merchants.
 21 So that is the part of the report that is referred
 22 to there, and we say that is simply, in itself, not
 23 a sufficient basis to offload a quarter to half of these
 24 credit write-offs.
 25 Why am I going to this? Again, I can put all of the

1 reports away, and I am now going to the Visa exemption
 2 certificate which is at E1, tab 2.
 3 Paragraph 350 at MasterCard's closing says:
 4 "This uses the same subset of costs used by the
 5 Commission in 2002."
 6 Simply wrong. When we get to the Visa exemption
 7 decision, E1, tab 2, just to put -- you know, why did we
 8 get to these costs in the first place? So why did we
 9 get to this subset of costs? If one remembers from the
 10 openings, a long time ago now, but I refer the Tribunal
 11 to recital 13, which is on page 21, 13, and 80.
 12 MR JUSTICE BARLING: 13 and 18?
 13 MR BREALEY: 1-3 and 8-0.
 14 So, 1-3, this is at page 21, so why did we get to
 15 the costs in the first place? It is because the
 16 Commission objected to Visa having a Free Funding Period
 17 rein, a Free Funding Period rein to set the MIF about by
 18 reference to what it thought was the competitive level,
 19 which is fundamental to how MasterCard have also set it,
 20 but recital 13:
 21 "As from its introduction, the MIF set by the Visa
 22 EU board has been set as a percentage of net ...(Reading
 23 to the words)... has been Free Funding Period to set the
 24 MIF at any level it considers appropriate, independently
 25 of any specific services provided by issuing banks to

1 the benefit of acquiring banks."
 2 It is very important to MasterCard's counterfactual.
 3 Recital 80, at page 32, "Prior to the
 4 modifications", so the Commission didn't like this Free
 5 Funding Period rein, this ability to set the MIF at any
 6 level it wanted just so it could be competitive with
 7 another system, so:
 8 "Prior to the modifications described above in
 9 section 323 ..."
 10 We will come on to that in a moment:
 11 "... the Visa MIF was considered ..."
 12 This is recital 80:
 13 "Prior to the modifications described above
 14 ...(Reading to the words)... as not satisfying, in
 15 particular, the second condition of Article 81.3,
 16 notably because the Visa EU board was Free Funding
 17 Period to set the MIF at any level it wished,
 18 independently of the cost of the specific services
 19 provided by issuing banks for the benefit of merchants."
 20 Pausing there, we have got all the witnesses from
 21 MasterCard, Dr Niels saying that MasterCard sets the
 22 MasterCard MIF by reference to what it perceives to be
 23 competition from Visa, and right back here, in the
 24 statement of objections, Visa was being told, "You just
 25 cannot do that, you cannot set the MIF simply at any

1 rate that you want. It has to be by reference to
 2 certain objective criteria".
 3 That is how, in 2002, we got to the subset of costs,
 4 these costs, which the Commission then departed from
 5 very soon after this, but this is early days. But when
 6 we go to the objective criteria, we see this at
 7 recital 21, so you cannot have a Free Funding Period
 8 rein, you have got to have some sort of objective
 9 criteria.
 10 Now, this is where I am getting to the punchline on
 11 the credit write-off point, so recital 21,
 12 "Objectivity":
 13 "Under the modified scheme ..."
 14 So Visa was forced, even in these early days, to
 15 modify its scheme so it couldn't just have this Free
 16 Funding Period rein:
 17 "... Visa will use three categories of issuer's
 18 costs involved in applying Visa payment services, an
 19 objective criterion under which to assess the Visa
 20 ...(Reading to the words)... the cost of processing
 21 transactions, the cost of Free Funding Period funding
 22 period ..."
 23 That is the 28 days:
 24 "... and the cost of providing the payment
 25 guarantee."

1 If one looks at the footnote, footnote 15, you have
 2 debit cards, and then, three lines down:
 3 "For credit cards, it corresponds only to the cost
 4 of any time difference between payment to the acquirer
 5 and the time when either payment must be made by the
 6 cardholder or the balance of the credit card bill rolled
 7 over into the extended Credit Facility to which a rate
 8 of interest is applied. It does not include any costs
 9 arising from the grant of extending credit to
 10 cardholders."

11 We say it is quite clear that the credit write-offs
 12 were not included in Visa.

13 And I need to go to a blue document, which I will --
 14 obviously we are in open court so I will have to do it
 15 quite delicately -- to show the Tribunal how MasterCard,
 16 after its infringement decision -- sorry, I need to
 17 first of all go to the infringement decision. I am
 18 jumping ahead of myself.

19 So we can put E1 away, and before I get to the blue
 20 document, we need to go to the infringement document,
 21 E2.2. So Visa did not have the cost of credit, but
 22 MasterCard did. It had the credit write-offs and the
 23 collections. So we will see how the Commission treated
 24 this credit write-off. So this is E2.2, page 1204,
 25 page 202 of the decision, 1204 of the bundle,

1 paragraph 742, where the Commission is looking at
 2 whether the Free Funding Period funding and the credit
 3 write-offs could be exempted:

4 "While merchants may benefit through enhanced
 5 network effects on the issuing side this does not
 6 necessarily offset their losses which result from paying
 7 off inflated merchant fees."

8 A key issue in this case:
 9 "The Commission has therefore reviewed ...(Reading
 10 to the words)... MasterCard, in practice ..."

11 Then I understand that is --

12 MR JUSTICE BARLING: Well, we will read that.

13 MR BREALEY: Then:

14 "As set out in detail ...(Reading to the words)...
 15 that are not related to services which sufficiently
 16 benefit merchants."

17 So the first bit:

18 "It remains unproven that merchants benefit from
 19 bearing the financial burden of issuers for the
 20 provision by issue as to cardholders of a so-called
 21 'free funding period'."

22 So this is where, even on the Free Funding Period
 23 funding period, as we know, the Commission was taking
 24 objections, and we see footnote 891, where the
 25 Commission refers to that footnote 44 of the Visa

1 decision. So that first bit is the Free Funding Period
 2 funding. Then moreover, in this little indent of 742:

3 "The Commission doubts that merchants sufficiently
 4 benefit from bearing the financial costs of issuers
 5 writing-off bad debts and collecting debts from
 6 cardholders."

7 So it wasn't exempted in Visa, MasterCard is trying
 8 to offload this item on to merchants, and the Commission
 9 is saying it doubts that merchants sufficiently benefit
 10 from bearing the financial cost of issuers writing-off
 11 bad debts and collecting debts from cardholders.

12 Again, we know, we have seen it, but annex 6 was the
 13 Oxera study, which I called in opening "the
 14 Mr Micawber's principle", where, again, the Commission
 15 rejects the study.

16 Go to page 1244 very quickly, 1244, where the
 17 Commission is looking at both the Free Funding Period
 18 funding and the credit write-offs. 1244. This is annex
 19 6, where it rejects the very study that Dr Niels still
 20 relies on. Paragraph 8:

21 "In particular, the study does not distinguish
 22 between the timing of consumers spending net changes to
 23 total consumer spending ...(Reading to the words)... and
 24 spending more in the current period they must repay
 25 their debt thereafter. Everything else equal,

1 cardholders must reduce their spending in the future."

2 Something which Mr Sidenius accepted:
 3 "If credit holders cannot generate ...(Reading to
 4 the words)... cannot be spent tomorrow."

5 Clear stuff. Paragraph 9:

6 "The study, moreover, does not even distinguish the
 7 provision of the interest Free Funding Period and the
 8 extension of credit more generally. Issuing banks
 9 ...(Reading to the words)... at no point the study
 10 considers why a MIF would be necessary for the extension
 11 of credit through credit cards, rather the study limits
 12 itself exclusively to analysing the effects of
 13 ...(Reading to the words)... to cardholders and the
 14 MIF."

15 But again, this is where, in annex 6 -- and we will
 16 come on to an exemption -- where is the link between the
 17 MIF and the extension of credit?

18 The Commission clearly rejected any notion of
 19 offloading the debt collection and the credit write-offs
 20 onto the merchants. Then, if I could take the Tribunal
 21 to one last document on this? That is at 3.4, tab 90A.

22 So, after the Visa exemption decision which didn't
 23 have credit write-offs, after MasterCard was told, "No
 24 justification for credit write-offs as debt
 25 collections", what happened?

1 This document at 90A, if the Tribunal remembers,
 2 this is something that Mr Koboldt was responsible for,
 3 so this is after the infringement decision. We see it
 4 is dated 19 May 2008 at the top left, and at 90B -- if
 5 you remember, I took Mr Koboldt to this. This is where
 6 the European Commission says, you know, "You still
 7 haven't substantiated any efficiencies, any link between
 8 the MIF and the efficiencies", so this is where the
 9 Commission rejected this paper,
 10 But the reason I want to go to this paper is to see
 11 what MasterCard was proposing to the Commission in order
 12 to get some sort of clearance or exemption from the
 13 Commission. In order to see that, if one goes to
 14 internal page 38, almost to the end of this document --
 15 it is a long bundle number, but it is 2039A.38, it might
 16 be better to go to internal 38. And then it is blue, so
 17 I will ask the Tribunal just to read paragraph 69, which
 18 is under the section 3.5.
 19 I actually can't understand why this is
 20 confidential, but ... it relates to something many, many
 21 years ago.
 22 If one then goes to the table on the right-hand
 23 side, this is quite important. You see the table, you
 24 have "Merchant", you have "Stakeholder benefits", and
 25 then, if I could ask, maybe you can see "Net bad debt

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1 write-offs"? So if one goes --
 2 MR JUSTICE BARLING: Yes, "Net bad debt write-offs".
 3 MR BREALEY: Then you see what is --
 4 MR JUSTICE BARLING: -- excluded. That is the bit, isn't
 5 it?
 6 MR BREALEY: That is the bit.
 7 So what you are getting is, these credit write-offs
 8 were not used by the Commission in 2002, contrary to
 9 what is said at 350. They were rejected by the
 10 Commission in the 2007 infringement decision. You can
 11 see how MasterCard then, when faced with, "What am
 12 I going to do?" -- to the extent to which it proposed to
 13 ditch certain -- the credit write-offs --
 14 MR JUSTICE BARLING: Mr Brealey, somebody wants to give you
 15 something.
 16 (Pause)
 17 You get the Free Funding Period funding.
 18 MR BREALEY: Yes. So we have got two more headings which
 19 are excluded, Ms Love is right to tell me.
 20 MR JUSTICE BARLING: What do you mean?
 21 MR BREALEY: The cost of funds, extended credit funding.
 22 MR JUSTICE BARLING: Yes.
 23 MR BREALEY: Thank you.
 24 One sees MasterCard's reaction to the sort of
 25 alleged benefit to the merchant that it was --

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1 essentially, I mean, it was proposed to ditch it, and
 2 yet in these current proceedings is, again, pursuing an
 3 argument that credit write-offs should be loaded onto
 4 the merchant.
 5 Now, they are quite entitled to do that, but what
 6 they are not entitled to do is what they have said in
 7 paragraph 350, that it was somehow sanctioned by the
 8 Commission in 2002, and that somehow -- you know, "If
 9 only we could go back to the 2002 days", or whatever --
 10 it was not sanctioned in 2002, it was specifically
 11 rejected in 2007, and it was proposed to be ditched in
 12 2008.
 13 MR JUSTICE BARLING: Yes.
 14 MR BREALEY: So that is credit write-offs.
 15 MR JUSTICE BARLING: I mean, the Free Funding Period funding
 16 period seems to be -- you are not too fussed about that,
 17 are you?
 18 MR BREALEY: Absolutely we are.
 19 MR JUSTICE BARLING: Are you? The Free Funding Period
 20 funding period?
 21 MR BREALEY: Yes. Well, there are two reasons. The first
 22 is one is the link between the MIF and the Free Funding
 23 Period funding period. We are going to have to come on
 24 to this.
 25 The question is very much a MasterCard question.

19

1 The Free Funding Period funding period, everyone says is
 2 a benefit.
 3 MR JUSTICE BARLING: You say -- why? How do you know?
 4 MR BREALEY: First of all, how do you calculate? Again,
 5 what is the efficiency gain from the Free Funding Period
 6 funding period? And what, then, having identified the
 7 Free Funding Period funding period, how is that linked
 8 to the MIF?
 9 MR JUSTICE BARLING: Well, I mean, let's just think about
 10 it. Working backwards, you could say that -- leave
 11 aside 101(3), leave aside that, but working backwards to
 12 say credit write-offs, apart from the Free Funding
 13 Period funding period, are remunerated, and all that
 14 revenue goes to the -- that is the issue. They get that
 15 revenue from the credit -- sorry -- from the extension
 16 of credit. I am not talking about write-offs as such,
 17 I am talking about the extension of credit.
 18 MR BREALEY: I take my card in and I don't pay for 28 days.
 19 MR JUSTICE BARLING: Yes, well that is the Free Funding
 20 Period funding period, but if you decide to roll it
 21 over, if you are a revolver, then there is the revenue
 22 in relation to that. I know it is not a write-off,
 23 but ...
 24 The Free Funding Period funding period is slightly
 25 different. There is no revenue coming in directly in

20

1 relation to the Free Funding Period funding period,
 2 because, by definition, it is Free Funding Period.
 3 MR BREALEY: But the bank, to a certain extent, has to
 4 notionally borrow money in order to somehow fund it.
 5 MR JUSTICE BARLING: Yes. So if there was no question of
 6 any benefit to merchants by reason of someone having
 7 a credit card which included that Free Funding Period
 8 funding, but if it was absolutely clear there was no
 9 benefit -- but there is at least a debate going on,
 10 isn't there, and there is some evidence about that, as
 11 to the benefits to merchants of credit cards.
 12 Q Does it? I mean, the question -- you are absolutely
 13 right. The question that everyone has to answer is:
 14 what is the incremental sales that the Free Funding
 15 Period funding period -- it is not the scheme as such,
 16 it is how does the MIF lead to incremental sales, and
 17 what are those incremental sales?
 18 MR JUSTICE BARLING: Well, I am not sure the MIF leads to
 19 the incremental --
 20 MR BREALEY: Well, that is why it falls down.
 21 MR JUSTICE BARLING: Another question might be -- it might
 22 be the wrong question, but another question might be:
 23 what is the legitimacy of seeking to charge the merchant
 24 something in respect of the Free Funding Period funding
 25 period?

21

1 MR BREALEY: Again, a very general question, and one has to
 2 focus, again, back to 101(3). I have said, and I am
 3 cited in the closings saying that these schemes are
 4 a fantastic thing, which they are, and merchants benefit
 5 from them, but as the European Court, the Commission,
 6 have consistently said, that is not the test.
 7 MR JUSTICE BARLING: No, but I was trying to look at it in
 8 a rather wider way than just the 101(3). I was
 9 thinking, you know, in general terms, what could be said
 10 to be the justice of --
 11 MR BREALEY: In general terms, if I ditch the analysis of
 12 the MIF leading to efficiencies, the justice of it is:
 13 okay, you are now going to charge me for the Free
 14 Funding Period funding period. Why, when you obtain all
 15 this interest anyway?
 16 MR JUSTICE BARLING: But they don't, by definition, get the
 17 interest in respect of any Free Funding Period funding
 18 period.
 19 MR BREALEY: No, but the same cardholder. So you are
 20 divorcing the relationship, as it were. You are taking
 21 the 28-day period and saying, "It is a terrible thing",
 22 but then hiding the interest bit.
 23 So when you are saying, "I need to put some of the
 24 cost onto the merchant of the 28-day period, because it
 25 would be unfair", the reply from the Commission and the

22

1 European Court is, "Well, why is it unfair when you are
 2 earning so much interest from the cardholder?"
 3 MR SMITH: Can't you just put it the other way around, and
 4 say the issue that it is notionally borrowing, it can
 5 extend credit to the cardholder, and the cardholder
 6 ordinarily would pay interest on that, if you disregard
 7 the 28-day Free Funding Period. But if you say, well,
 8 because it makes a scheme work better for whatever
 9 reason, you give the cardholder a 28-day period, you see
 10 that as a cost to the issuing bank because what you are
 11 therefore doing is foregoing the interest they would
 12 otherwise receive from the cardholder and the question
 13 really is; to whom is that a benefit?
 14 MR BREALEY: And again, I come back to -- clearly, the
 15 28-day period could be a benefit, certainly to the
 16 cardholder, and it could be a benefit -- as a general
 17 proposition -- I mean, I agree, but we are not just
 18 talking about general benefits. We are talking about
 19 a collective price agreement which is resulting in, and
 20 we will come on to it, an inflated MIF, and one is
 21 trying to work out whether that can be exempted, and
 22 essentially, the questions that have been put to me are
 23 quite -- you know, Dr Niels' point, which is that you
 24 look at it in the round and justice and costs, but
 25 without analysing it from the perspective of 101(3).

23

1 MR JUSTICE BARLING: I'm not saying you shouldn't do that at
 2 some point but I think it was going a step back from
 3 that, just to see what the rationale might be, or even
 4 looking at the question of exemption, and -- in looking
 5 at the cost stacks that might be relevant to that
 6 question. But, as I understood it, you don't exclude
 7 the likelihood that the Free Funding Period funding
 8 period, leave aside credit in general, but the Free
 9 Funding Period funding period makes the product a more
 10 attractive product to cardholders?
 11 MR BREALEY: Well, to cardholders in particular.
 12 MR JUSTICE BARLING: Yes.
 13 MR BREALEY: But, you know, if one looks at it generally,
 14 I take a loan out from Barclays Bank for £500 to finance
 15 my lifestyle for the next two weeks or three weeks or
 16 whatever, and I go into shops and I use the cash
 17 spending that money. I don't pay any fee for extended
 18 credit. The relationship is between the borrower and
 19 the bank. I go into a shop and I buy something with
 20 a cheque, I might have credit with the bank, I might not
 21 have to pay it back, but a merchant doesn't pay some
 22 sort of 28-day funding fee because I have an overdraft
 23 with the bank.
 24 That is where the European Court is coming from.
 25 I write a cheque, I have got an overdraft, I have got

24

1 credit, and you might say, "Well, that is a benefit to
 2 everybody".
 3 MR JUSTICE BARLING: People like cards, generally speaking,
 4 more than they like going to the bank to arrange a loan,
 5 and therefore -- they, you know, find it convenient to
 6 pay in that way.
 7 MR BREALEY: I don't think anybody in the room disagrees
 8 with the proposition, but the question is -- again, one
 9 has to come back to 101(3). How does the level of the
 10 MIF -- we know it has gone down from, say, 0.9 to 0.3,
 11 so what has happened to any incremental spend? Nothing
 12 has happened. There is no evidence to it. Nothing has
 13 happened, except that the cardholders may not get so
 14 many rewards, which is what the Commission and the
 15 European Court say, "Well, that is what happens", but
 16 when it comes to the benefit to the merchant, they are
 17 still making sales, people are still using their credit
 18 cards; and one has to focus in on what is the efficiency
 19 gain of the MIF, and --
 20 MR SMITH: Mr Brealey, doesn't that depend on exactly what
 21 you define as the context? We had this debate with
 22 Mr von Hinton Reed, where we put the example of the two
 23 cinemas, and what he was doing, quite clearly, was
 24 focusing on the acquirer market and saying, "Looking at
 25 the acquirer market, one has got to see in what way has

25

1 the merchant benefited by credit cards over the cash?"
 2 This is how he was justifying the benefit of credit
 3 cards in that very narrow confine.
 4 But doesn't the answer to the question become
 5 different if one says, "Well, let's look more broadly at
 6 the three inter-related markets that Dr Niels
 7 identifies, the issue of the acquirer and the --
 8 MR BREALEY: That is fair case.
 9 MR SMITH: No, of course, but the answer, then, becomes
 10 different to 101(3), certainly.
 11 MR BREALEY: And my reply to that is, again, one has to --
 12 I think one has to -- look at how to properly interpret
 13 101(3). Let's assume that it is the acquiring market
 14 which is affected, but the issuing market is not
 15 affected -- distortion of competition -- the only market
 16 which has been restricted is the acquiring market, so
 17 the merchant, category of merchants is the category that
 18 is being affected.
 19 You then go to paragraph 85 of the guidelines which
 20 is based on the jurisprudence of the court, and you have
 21 to say to yourself, "Is that category of person that is
 22 affected by the restriction of competition any worse
 23 off?"
 24 So the merchants must be no worse off when one is
 25 looking at the conditions of 101(3).

26

1 So it is not just sufficient to say, and this has
 2 been the battle for the last ten years, to say, "Well,
 3 the merchants can essentially subsidise the
 4 cardholders". One has to rein back to the question,
 5 paragraph 85, I think it is 85 of the guidelines: the
 6 category of person, consumer, who is affected by the
 7 restriction of competition, must be no worse off. It is
 8 your cinema example.
 9 MR SMITH: Yes, but the difficulty is that you see things
 10 only by way of increasing the aggregate market of spend
 11 through credit cards, but why can't we see simply the
 12 fact that one can pay by credit card as a benefit for
 13 the cardholder? Why is that left out of account?
 14 MR BREALEY: Well, it is a benefit to the cardholder. That
 15 is not left out of the account, so when one is looking
 16 at the first condition of 101(3), you are looking at
 17 benefits generally.
 18 MR SMITH: Right.
 19 MR BREALEY: But then, and, again, this is -- we are
 20 applying Article 101 here, so you say, "It creates
 21 benefits" -- as long as you can identify them, and we
 22 say they haven't identified them, but let's take what
 23 you are saying to me, that we have identified them, now
 24 you have to apply the second condition of Article 101(3)
 25 which says that the category of consumer that is

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1 affected by the restriction of competition, that is the
 2 merchant, cannot be any worse off.
 3 That is why you come back to the transactional
 4 efficiencies, because you have the 0.2 per cent which is
 5 represented by the transactional efficiencies, and you
 6 can say, "Well, the merchants should pay that, that
 7 0.2 per cent". That still benefits the cardholders. It
 8 is still a payment of money from the merchants to the
 9 issuers, and the issuers can give that to the
 10 cardholders. And that is why the MIF actually works,
 11 because the MIF creates benefits, efficiencies, to
 12 cardholders and merchants.
 13 But when it comes to the second condition, you are
 14 saying: is the category of merchants any worse off? No,
 15 because the transactional savings they are making up
 16 for, by the 0.2 per cent, and that money goes to the
 17 issuers.
 18 But if you then say, "Right, I am going to go beyond
 19 the 0.2 per cent and I am going to charge them
 20 0.9 per cent", now you say, "Well, they are worse off.
 21 Now what is the benefit they are getting for that
 22 difference, that 0.5?"
 23 MR SMITH: So just to be clear, let's suppose, subjectively
 24 speaking, a large merchant like Sainsbury's values cards
 25 and is prepared, in its own mind, to pay more than the

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1 MIT-MIF, that doesn't have any bearing, you would say,
 2 on what is acceptable. That is a different question
 3 altogether: what, in the market, exercising its own
 4 judgment, Sainsbury's might be prepared to pay.
 5 MR BREALEY: I think MasterCard, it is their case, you
 6 cannot have MIFs for different categories of merchant,
 7 because it would be, they say, unworkable, and so they
 8 actually do say, "You have to look at the merchants as
 9 a whole", but the fact that Sainsbury's may be prepared
 10 to pay more or less -- I mean, there may be an argument
 11 for saying that Sainsbury's should be a lot less, and
 12 that the small corner shop, that we buy our papers from,
 13 should be paying a lot more, but MasterCard and
 14 Sainsbury's are not putting forward that case to the
 15 Tribunal. And it is not, obviously, in the interchange
 16 fee regulation, it is one size fits all. That is why
 17 you look at merchants in the aggregate.
 18 MR JUSTICE BARLING: I expect you are coming on to
 19 restriction, but, I mean, this question of the adverse
 20 effects on the party affected, which is, as you put it,
 21 is the merchants by the MIF, does that -- we don't get
 22 into exemption until there is a restriction?
 23 MR BREALEY: No.
 24 MR JUSTICE BARLING: So, remind me, because I am sure this
 25 is -- and it has just slipped my mind, but do you say

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1 that a MIF of even a fraction of a penny, or even
 2 pound-zero, is still a restriction that needs exemption,
 3 or does the characterisation of the MIF as a restriction
 4 on competition depend on the level of the MIF?
 5 MR BREALEY: Neither, really, because we are at the 101
 6 restriction stage. We are not really at level. We are
 7 looking to see whether the process of competition is
 8 being affected.
 9 MR JUSTICE BARLING: By the existence of a MIF at any level?
 10 MR BREALEY: Yes. So, for example, the scheme rule says
 11 that the banks will not compete, and they are entitled
 12 to set a common price. That is a restriction -- we will
 13 come on to it -- because, as we know, competition law
 14 will interfere when competitors have, you know, an
 15 agreement as to a common cost.
 16 So it doesn't matter whether it is a penny, £10,
 17 whatever, what competition law is saying is that,
 18 "I don't like the fact that the competitive process has
 19 been distorted. You should be competing on an
 20 individual basis, not on a common basis".
 21 So in a cartel, for example, like a cement cartel,
 22 it is no defence for the cartelist to say, "Well, we
 23 only rigged the price by 2 per cent. You know, I can
 24 understand, OCMA, if we had increased it by
 25 100 per cent, but, you know, it was a pretty marginal

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1 cartel at the end of the day". That has never worked.
 2 MR JUSTICE BARLING: This is another point; is it your
 3 argument -- I know it is on the pleadings, but I wasn't
 4 sure to what extent you were pursuing it, are you saying
 5 this is a restriction by object?
 6 MR BREALEY: No. I mean, it is not on the pleadings and we
 7 have not run the case, but it is pretty close to it, and
 8 the reason it is pretty close to it is because it has
 9 been said to be a restriction by effect for so many
 10 years that at some point you have to say, "Well, is it
 11 a restriction by object?"
 12 I hear sniggering, but that is actually how object
 13 restrictions are identified. So if you go into the
 14 101 guidelines, you know, why is there an object
 15 infringement? Because price-fixing is, by its very
 16 nature -- we have decided it so many times that it is an
 17 obvious restriction. That is why price-fixing
 18 agreements tend to have as their object a distortion of
 19 competition, because of previous case law. And I would
 20 say we are not far off on object infringement.
 21 MR SMITH: Well, Mr Brealey, I think you do plead that it is
 22 an infringement by object. You have said very little
 23 about in your submissions; that is why we are a little
 24 puzzled.
 25 MR JUSTICE BARLING: We have got to work out whether we have

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1 to decide it. At some point we need to know if it is
 2 part of your case.
 3 MR BREALEY: If you are pushing me, then I would say it was
 4 an object infringement.
 5 MR JUSTICE BARLING: It is?
 6 MR BREALEY: Yes.
 7 MR JUSTICE BARLING: An object restriction?
 8 MR BREALEY: I am not, at this stage, going to say that it
 9 is not. I have just said it is an extremely close
 10 thing. They have had -- 2002, supplemental statement of
 11 objections prior to that. I think the Tribunal would be
 12 perfectly entitled, in all consciousness, to say,
 13 "Enough is enough. You know, both Visa and MasterCard
 14 have lost every single time". They have got a new
 15 statement of objections; again, it is a restriction ...
 16 I haven't emphasised it because we say that it is
 17 clear that it is a restriction by effect, but
 18 I certainly couldn't stand up here and say, "It is not
 19 a restriction by object".
 20 At the end of the day, it is a price-fixing
 21 arrangement between competitors on a national basis. If
 22 one tries to figure any other example where a nationwide
 23 agreement that fixed a common cost which is paid by
 24 somebody else -- sorry, Professor Beath is going to tell
 25 me that --

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1 MR SMITH: No, no, I am merely identifying the part of your
 2 pleading where you quite properly plead it as an object
 3 infringement, which is paragraph 39 of the amended
 4 Particulars of Claim.
 5 MR BREALEY: Well, I don't resile from it.
 6 MR SMITH: That remains Sainsbury's' position?
 7 MR BREALEY: I don't resile from it. But I do say that it
 8 is absolutely plain as a pikestaff that it is
 9 a restriction by --
 10 MR JUSTICE BARLING: But is it your case that the MIF is
 11 a restriction by effect, regardless of level?
 12 MR BREALEY: Yes.
 13 MR JUSTICE BARLING: So even if it was fixed at nought, it
 14 would still be a restriction by effect?
 15 MR BREALEY: Well, I understand what you are saying.
 16 I mean, if a cartel that says, "I am not going to have
 17 a price rise, I am not going to ..."
 18 I mean, that is a difficult one, obviously, but it
 19 still distorts the competitive process. You are still
 20 not -- I mean, Mr Willcart, for example, accepted that
 21 there would be instances where interchange fees could go
 22 the other way. And in my submission, if you take the
 23 interest payments, so banks are earning a fortune from
 24 these credit cards and the way that they earn this
 25 fortune is through merchants accepting these credit

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1 cards, there is, in theory, or, if not, a possibility,
 2 that interchange fees should be -- issuers should be
 3 paying merchants to accept it. So this is not this
 4 case, but if you are asking me on a hypothetical, you
 5 know, if the banks got together and said, "It will be
 6 a zero MIF", and that precluded interchange fees going
 7 the other way, one could see, well, yes --
 8 MR JUSTICE BARLING: The reason I ask you, because it links
 9 to 101(3) to some extent, but I just want to -- because
 10 you say that you only look at the adverse -- the adverse
 11 effect is on the merchants, and when you are looking at
 12 the second criterion in Article 101(3), I think that is
 13 the way --
 14 MR BREALEY: Can't be any worse off. Yes.
 15 MR JUSTICE BARLING: Yes. But of course, bearing in mind
 16 what we have heard about the skewed nature of the
 17 four-party system --
 18 MR BREALEY: And it is skewed.
 19 MR JUSTICE BARLING: -- and assuming there are benefits to
 20 both sides, you know, there are benefits for merchants
 21 as well, and so the fraud -- you know, they are being
 22 protected against fraud in the MasterCard system --
 23 MR BREALEY: And fraud is included in the MIT-MIF --
 24 MR JUSTICE BARLING: And defaults, and so on, so there are
 25 benefits to merchants, so why is it, therefore, said

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1 that the effects of this restriction can only be felt on
 2 the merchant side? Because if you had a very low MIF
 3 that didn't cover the costs, for example, of the
 4 benefits, the admitted benefits to merchants, then there
 5 would be effects -- the cardholders would, in effect, be
 6 subsidising the merchants, so why wouldn't they be
 7 affected by it?
 8 MR BREALEY: I am not sure that that logically follows. You
 9 have got a situation where you have a price-fixing
 10 arrangement which is offloading costs onto merchants,
 11 and they have no possibility of negotiating out of it.
 12 MR JUSTICE BARLING: Yes. Acquirers do, arguably, but not
 13 merchants directly; indirectly perhaps.
 14 MR BREALEY: So where is the -- again, one has to focus on
 15 who is being affected by the restriction.
 16 MR JUSTICE BARLING: Exactly. Now, if the level of the MIF,
 17 which is the restriction on competition, doesn't
 18 actually cover the admitted benefits that merchants get
 19 through defaults, fraud, and so on, even
 20 transactional -- so if the level is so low that those
 21 costs are, in effect, lumped on the issuers and their
 22 customers, namely cardholders, aren't they also affected
 23 by the restriction on competition? Why should you only
 24 look at the MIF insofar as it affects merchants? Why
 25 can't you look at it insofar as it affects the other

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1 side of the market where appropriate?
 2 Because this is a balance thing. I think everyone
 3 seems to agree this is a balancing mechanism, and if the
 4 balance goes the other way then the cardholders are
 5 losing out, or the issuers are losing out.
 6 MR BREALEY: I think you have to take it in stages, don't
 7 you? As the European Court said, that analysis is
 8 a 101(3) analysis. It is not a restriction of
 9 competition analysis. So the European Court says, quite
 10 clearly, that if you are trying to persuade me about
 11 benefits to cardholders, that is a 101(3) analysis, not
 12 a 101(1) analysis. So, yes, merchants are the affected
 13 group, they are the ones that are getting the common
 14 cost, that the banks are putting this cost onto the
 15 merchants.
 16 The banks are not putting the cost onto the
 17 cardholders. The banks are putting the cost onto the
 18 merchants.
 19 MR JUSTICE BARLING: I wasn't -- well ...
 20 MR BREALEY: So you have identified the affected group by
 21 the restriction of competition, the acquiring market.
 22 There has been no analysis from MasterCard that the
 23 acquiring market is not the relevant market to be
 24 looking at. The acquiring market has been the market in
 25 the Visa -- the two decisions, it has been upheld by the

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1 general court. So you are looking at the acquiring
2 market which is the affected market by the restriction
3 of competition.

4 Yes, you can then look at the benefits to
5 cardholders and merchants in 101(3), and that is what
6 the European Court said. So MasterCard made this very
7 argument to the European Court. It said, "You have to
8 look at all the benefits of the scheme", and the
9 European Court said, "Well, if you are talking about
10 benefits to cardholders, you are not the category of
11 consumer affected by the restriction of competition, you
12 can look at the benefits to the cardholders but it has
13 to be in the context of 101(3)".

14 MR SMITH: Aren't you slightly putting the cart before the
15 horse there? Because you said it is obvious that you
16 said the merchant is the affected party, that the
17 acquirers are the -- but isn't the first step to
18 establish precisely what the counterfactual is, so that
19 you can actually test who the affected parties are? So
20 isn't the first step on our road to say, well, what,
21 exactly -- if one removes the offending provision, and
22 the provision is anti-competitive effect we are testing,
23 what, exactly, would the test look like if one applies
24 a scalpel and removes that provision?

25 So it is no default MIF, as I understand it, is your

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1 position. Now, does that mean that you simply treat the
2 scheme as one where no price is set?

3 MR BREALEY: Well, I think, as you know, with our case, and
4 it has been the case that the Commission -- it has been
5 the case that MasterCard, as I understand it, have
6 advocated, that -- competition law has bitten on the
7 common agreement on price, the multilateral interchange
8 fee. It is an agreement between competitors on a cost.
9 And that is, if it is not object, it is effect, it is
10 a restriction of competition.

11 So that MIF now goes, and, as a lot of the questions
12 that you have been asking to the witnesses, the experts,
13 what then takes its place? You know you cannot have
14 a common agreement, so now the issue is that the
15 acquirers have to do it on a bilateral basis. And the
16 evidence of Mr von Hinton Reed, and, as I understand it,
17 MasterCard, submitted to the Commission on European
18 Court, is that you can have a system of bilaterals but
19 it would collapse, and then, so says the European Court
20 you would have an ex post pricing rule which would
21 prevent it from collapsing. Mr von Hinton Reed says if
22 you have the ex post pricing rule, you would then get
23 the negotiation, and it would be roughly the same as the
24 transactional benefits.

25 MR SMITH: Yes, but let's call it the "collapse point",

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1 because doesn't that require us to understand exactly
2 how the scheme is going to work, absent the removed MIF?

3 Now, as I understand it, the case that is put by
4 MasterCard, was put by MasterCard, in front of the
5 Commission, was that there was no obligation on the part
6 of the issuing banks to pass anything on to the
7 acquiring banks at all. So one could have a situation
8 where I, as a cardholder, go to Sainsbury's and spend
9 £100; I am extended credit to that extent because it is
10 a credit card I have used, but effectively I owe my
11 issuing bank £100. The issuing bank, call it
12 a MasterCard, may or may not pass some or all of that
13 £100 over to the acquiring bank, who then may or may
14 not, perhaps, pass it on to the merchant.

15 Now, that, it seems to me, is a rather extraordinary
16 state of affairs. It does seem to me that unless you
17 have an agreed interchange fee, whether that be
18 multilateral or bilateral, the issuing bank, as part of
19 the settlement process, needs to pass the price over to
20 the other side.

21 Now, obviously, that is something which we will need
22 to discuss with MasterCard, but in terms of how the
23 scheme operates, if that is right, you don't need an
24 ex post rule against pricing, because the hostage
25 situation doesn't arise, but it does seem to be a rather

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1 material element, in understanding how the
2 counterfactual works, to appreciate whether or not an
3 issuing bank does have this rather extraordinary power
4 to extract what it likes absent a remit, or whether it
5 doesn't.

6 MR BREALEY: Well, all I can say is that that has been
7 canvassed repeatedly for the last ten years to the
8 Commission, and to the court. It has been canvassed by
9 Mr von Hinton Reed. And it has always been -- and one
10 is looking at this objectively, from a scheme
11 perspective -- that the MasterCard would adopt a scheme
12 rule which would prevent it from collapsing.

13 MR SMITH: I mean, even if one puts a blue pencil through
14 the default MIF, doesn't one have to ask the question:
15 what would happen if, in that counterfactual, an issuing
16 bank decided to hold on to a defined portion of the
17 £100? If the acquirer then says, "Well, hang on
18 a minute, you have decided to deduct half of it, I would
19 like a counter for that", what would the answer be?

20 MR BREALEY: I am not sure that was counterfactual, but
21 I can tell you what I think the answer is, is that if
22 I am Sainsbury's or I am any other merchant and someone
23 uses a credit card in my shop, and I find out that I am
24 only going to be paid 5 per cent of the value of that
25 product that I have just sold, I am never going to

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1 accept that credit card again. And I think the simple
 2 answer to that question is that the merchants would just
 3 say, "I am not going to have this type of credit card in
 4 circumstances where I part with this £100 product and
 5 I am only going to get £5 from the issuing bank". The
 6 merchants would not accept it.
 7 MR SMITH: I would think that the cardholders would be as
 8 cross because they would be losing £100 and it would all
 9 be lost in the middle. What I am suggesting to you, and
 10 it seems to me it is a legal point, not a point for the
 11 economists, but what I am suggesting to you is that,
 12 before saying, "This is a terrible system and we will
 13 ditch it", the merchant might actually look at the chain
 14 of contracts between itself and the cardholder and say,
 15 "Well, can this possibly be right?"
 16 And it does seem slightly odd that one is simply
 17 accepting the assertion that this is what would happen
 18 without actually testing what the chain of contracts
 19 between cardholder and merchant would actually dictate.
 20 MR BREALEY: I mean, I see the point. You will have to take
 21 it in stages, I think. You are, at the moment, faced
 22 with a situation where you have a collective price
 23 agreement which is setting an inflated floor, and the
 24 issuers and MasterCard and Visa have the ability to keep
 25 on raising the price and price and price. So if, for

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1 example, the merchants lose this case, and it is
 2 accepted that MasterCard can operate a MIF, they can
 3 have as many premium cards as they want, any high
 4 exchange fees until the pips squeak, as it were.
 5 So you do have a situation, at the moment, according
 6 to the Commission, the court, the evidence in this case,
 7 where you are getting ever-increasing higher fees. We
 8 know now that they have been regulated but they were
 9 ever-increasing. And the question, I think, which is
 10 being put to me is: well, what would be in its place?
 11 As I understand it, the evidence from both
 12 economists is that what would happen -- and the
 13 witnesses -- and I can go to that now if it would
 14 assist. I think if I just --
 15 MR JUSTICE BARLING: You may be coming to it in the ordinary
 16 event.
 17 MR BREALEY: I can just deal with it, if one -- I mean,
 18 obviously Mr Smith has looked, but it is paragraph 159
 19 of our skeleton, where this is what we are putting
 20 forward as the alternative to the MIF which is having
 21 ever-increasing interchange fees. So we say that --
 22 this is 159:
 23 "The MasterCard witnesses, Willcart and Douglas,
 24 consider that, in the absence of the MIF, interchange
 25 fees would have to be agreed on a bilateral basis."

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1 We say:
 2 "This has been the argument advanced by MasterCard
 3 and the economists for a long, long time."
 4 Then we refer to the evidence in cross-examination.
 5 So we have the answer in the second paragraph:
 6 "There is a limited number of participants, issues
 7 and acquirers. I think it is possible that those
 8 participants, issuers and acquirers will be able to
 9 agree amongst themselves about what is the level of
 10 interchange to make the system work. That is
 11 domestically set. Of course, it is impossible for every
 12 single acquirer in the world, but on a limited scale it
 13 is possible."
 14 So this was the evidence that appeared to be given
 15 by the MasterCard witnesses on a domestic basis. So
 16 then you have the issue as to whether, on that basis,
 17 you would have collapse, and this is something that, as
 18 Mr Smith knows, has been argued time and time again, and
 19 we have set out what the Commission said about the
 20 collapse.
 21 It went to the highest level in Luxembourg, so that
 22 was what the Commission says at page 64. It went to the
 23 highest level in Luxembourg. And the CJ -- this is
 24 paragraph 163 -- says:
 25 "In paragraphs 95 and 96 in the judgment under

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1 appeal, the General Court correctly considered that some
 2 issuing banks might hold up acquirers who are bound by
 3 the honourable cards rule. It could be solved by
 4 a network rule that is less restrictive to competition
 5 than MasterCard's current solution."
 6 And I emphasise "less restrictive", because that is
 7 what the restriction of competition counterfactual is
 8 about:
 9 "The alternative solution would be a rule which
 10 imposes ...(Reading to the words)... in the absence of
 11 a Bilateral Agreement."
 12 Then over the page we get a statement from the
 13 European Court saying:
 14 "It is not only plausible but, indeed, likely."
 15 So we adopt what the Commission, the General Court,
 16 and the main court has said, that this is what would
 17 replace the MIF. And there is evidence which says that,
 18 in the case of the bilaterals, there would be --
 19 Sainsbury's would have leverage and would be able to put
 20 pressure on the acquirers in its negotiations with the
 21 issuers.
 22 Then, at 165, we have set out the evidence that we
 23 thought was relevant to -- which is the exchange that
 24 you had, sir, Mr Smith, between Mr von Hinton Reed.
 25 Basically, his evidence is that, in the absence of the

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1 MIF, what will happen, system of bilaterals, and you
 2 will probably end up round about 0.15 per cent.
 3 According to the European Court, that would be "less
 4 restrictive of competition".
 5 We have not come to court saying that there can't be
 6 an exemption to avoid this, but we don't have to prove
 7 that. That is for MasterCard to prove that. But we do
 8 say that there is a system out there which can replace
 9 a common pricing agreement, which, on any view, is
 10 imposing higher and higher costs onto merchants.
 11 MR SMITH: Yes. I suppose what I am testing is whether the
 12 ex post pricing rule is actually a necessary part of the
 13 counterfactual, or whether it is, in fact, perhaps,
 14 a desirable clarification of what is no more than the
 15 existing position.
 16 MR BREALEY: I can well see the sense in that, that you may
 17 not need it because, in the system of bilaterals, it
 18 would work, and they have just got to be grown-ups.
 19 I can see that. But if they are not going to be
 20 grown-ups, and the issuers are going to misbehave, you
 21 could see that you would need this rule just as some
 22 sort of back-up. Because I think it was put to one of
 23 the witnesses, you know, "Why would you want the system
 24 to collapse? Surely you would just get on with it and
 25 do the right thing?"

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1 But the bottom line is, it is independent evidence
 2 from Mr von Hinton Reed but it is consistent with what
 3 has been before the regulators for the last ten, fifteen
 4 years, which -- this MIF, this multilateral pricing
 5 agreement, has resulted in higher and higher costs for
 6 the merchants. We can come on to the benefits in
 7 101(3), but if one adopts -- and you may have seen it,
 8 but I will come on to it after coffee -- I need
 9 a coffee, I have lost my train of thought now!
 10 MR JUSTICE BARLING: Shall we have a break? You collect
 11 your train of thought and we will have a short break.
 12 (11.53 am)
 13 (A short break)
 14 (12.09 pm)
 15 MR JUSTICE BARLING: Mr Brealey, just to go one step back to
 16 make sure we have understood what it is, by object, the
 17 restriction is a MIF at any level. Is that the way it
 18 is put? You said it wasn't related to the level.
 19 MR BREALEY: Whether it is object or effect doesn't matter.
 20 Object or effect -- a restriction -- I will show the
 21 passage right now, but competition law is about
 22 protecting the competitive process.
 23 MR JUSTICE BARLING: Yes.
 24 MR BREALEY: Competitors do not get together to agree
 25 a common cost.

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1 MR JUSTICE BARLING: Right.
 2 MR BREALEY: Whether that is object or effect, that is
 3 a distortion of the competitive process, and it is no
 4 defence, in my submission, for a cartel to say,
 5 "Well, we all clubbed together in a smoke-filled room,
 6 but it either failed, it only led to a 1 per cent
 7 increase, or a 100 per cent increase".
 8 MR JUSTICE BARLING: So your case is that the MIF,
 9 regardless of level, is a restriction by object and/or
 10 effect?
 11 MR BREALEY: And/or effect.
 12 MR JUSTICE BARLING: Just leave aside object.
 13 MR BREALEY: Yes. Leave aside object.
 14 MR JUSTICE BARLING: When we look at a restriction by effect
 15 of, say, a very low, or zero MIF, I just want to get
 16 a feel in very rough and ready terms of how you would
 17 say that that has the effect of restricting competition.
 18 MR BREALEY: Because they are no longer competing between
 19 themselves.
 20 MR JUSTICE BARLING: On the --
 21 MR BREALEY: But they have agreed a common price of zero.
 22 MR JUSTICE BARLING: How does that have the --
 23 MR BREALEY: Well, I mean this is kind of a hypothetical
 24 because it hasn't really been the subject of evidence,
 25 but there may be all sorts of reasons why the banks

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1 should not get -- it may well be, for example, that
 2 Sainsbury's could say, "Well, on a system of
 3 bilaterals", as I said earlier, "It may well be that
 4 I will get paid for accepting credit cards".
 5 You know, this is hypothetical here, and that is why
 6 it is the competitive process. You know, "I account for
 7 X percentage of retail, I am very important to" --
 8 MR JUSTICE BARLING: "I am a big retailer."
 9 MR BREALEY: "I am a big player. A small corner shop" --
 10 MR JUSTICE BARLING: "You want me to accept your cards so
 11 you have to pay me for it."
 12 MR BREALEY: "You have to pay me for it. You earn a lot of
 13 money from me ..."
 14 I am just throwing back the hypothetical that you
 15 have --
 16 MR JUSTICE BARLING: Yes.
 17 MR BREALEY: But the key answer is it is a distortion of the
 18 competitive process. And I have never, for example,
 19 come across where, you know, in a cartel, they have
 20 said -- well, it may not have had any effect, so you
 21 cannot claim damages, but it has distorted competition,
 22 because it has distorted the competitive process.
 23 That is --
 24 MR JUSTICE BARLING: And on the acquirer market, you
 25 subscribe to that, the Commission's approach, that this

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1 is -- we are looking at competition only on the acquirer
 2 market?
 3 MR BREALEY: Yes. I mean, we have nailed our colours to the
 4 acquiring market for very good reasons. It is not just
 5 a question of following what the Commission has said.
 6 There are very good reasons that Mr von Hinton Reed sets
 7 out in his expert report, the snip test, the
 8 substitutability, the competitive constraints, all the
 9 classic market definition tools that are open to us.
 10 And when you apply the guidance on market definition,
 11 you have to come down, really, on the fact that the
 12 acquiring market is one market.
 13 There are other markets, I mean -- and I don't
 14 actually think that Dr Niels disagrees with that.
 15 I mean, he is quite cagey. He says, "Our three markets,
 16 but you have to look at them together", to which we say,
 17 "Well, you can. If you accept that the acquiring market
 18 is distorted", which we say it is, "You can look at all
 19 the three markets in 101(3)". I am going to show you
 20 that in two seconds.
 21 MR SMITH: Two short questions, Mr Brealey.
 22 First of all, and I think I know your answer to
 23 this, looking simply to 101(1), even if it were
 24 contended that the default interchange fee were, as it
 25 were, the perfect fee that would have been agreed

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1 bilaterally, you would still say that was a distortion
 2 on competition because it hadn't been agreed
 3 bilaterally, it had been imposed by default?
 4 MR BREALEY: Yes.
 5 MR SMITH: Secondly, if one has a default MIF, it obviously
 6 is fixing the price on the issuing side as well, so
 7 would you agree that the issuing market is also being
 8 distorted because there is no negotiation there?
 9 MR BREALEY: Sorry, can you ask me that again?
 10 So the question has been put to me that --
 11 MR SMITH: Well, the MIF, obviously, is a default, and what
 12 you are saying is that it is fixing a price where there
 13 ought to be a competitive process, but that price is
 14 fixed not simply for the acquiring banks, but is also
 15 fixed, by definition, for the issuing banks. So does it
 16 follow, is my question, that there is a restriction, or
 17 distortion of competition, both on the acquiring side,
 18 and on the issuing side?
 19 MR BREALEY: And the reason that there would be a distortion
 20 on the issuing side?
 21 MR SMITH: Is precisely the same reason as on the acquiring
 22 side: the price is being fixed, not negotiated.
 23 MR JUSTICE BARLING: There might have been, as you said,
 24 a price going the other way, so why would it therefore
 25 be any different?

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1 MR BREALEY: Yes. I mean, I tend to accept that. The only
 2 reason I hesitate is that -- where is the restriction on
 3 the issuing side? The issuing banks have got together
 4 to impose a cost on the merchants, so is it being put to
 5 me that that must automatically mean there is a -- so
 6 let's assume, for the sake of argument, they have
 7 50 per cent of the costs on the merchants, but there is
 8 no -- the reason I hesitate is that there is no set fee,
 9 vis-à-vis issuers and cardholders, so the issuers are
 10 not agreeing between themselves that they will charge
 11 cardholders anything, as opposed to -- but they are
 12 agreeing to charge merchants, acquirers, something. So
 13 you have issuers and the acquirers, are all part of the
 14 same scheme, and they all sign up to a default MIF which
 15 is going to impose a common cost on merchants. There is
 16 no agreement to impose a common cost on any cardholders.
 17 MR SMITH: So, on that basis, it all turns on the fact that
 18 the acquiring banks pass the cost on fully to the
 19 merchants?
 20 MR BREALEY: And they do.
 21 MR SMITH: I appreciate that, but that is the reason, you
 22 say, why it is a restriction on one side of the market
 23 and not a restriction on the other side?
 24 MR BREALEY: Correct. And, really, when one thinks about
 25 it, it is the issuers who say, "I have all these costs";

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1 the acquirers are quite, you know, not neutral about it,
 2 but, you know, they are not going to soak it up, and
 3 they just pass it on, which is what happened in
 4 Australia, and the evidence in the case is that they do
 5 pass it on. It is not in their interest to accept the
 6 costs, and the effect is that they just pass it on to
 7 the merchant.
 8 And the issuers know that. The issuers know that it
 9 is going to be passed on to the merchant.
 10 But there is no agreement -- that is why I just
 11 hesitated -- no agreement between the issuers to impose
 12 any sort of common cost on cardholders. But, as the
 13 European Court and the Commission say, basically, the
 14 relationship between the cardholder and the issuer, that
 15 is that, and that should get sorted out between
 16 themselves.
 17 MR SMITH: Right. So, to be absolutely clear, then, the
 18 restriction on competition is a combination of the fact
 19 that there is a default price set for the interchange
 20 fee, and that that default price as set is 100 per cent
 21 passed by the acquiring bank to the merchant?
 22 MR BREALEY: Well, I kind of resist the 100 per cent.
 23 I mean, if it was 95 per cent, I mean, there is
 24 absolutely no way, in practice, that the acquirers are
 25 going to make a loss on their acquiring services, which

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1 they would do if they absorbed the costs that are being
2 put on to the merchant. That is why the acquirers are
3 pretty neutral about it. They say, "Okay, if this is
4 what the scheme is, we will pass it on", and that is,
5 indeed, exactly what happens. They just don't have the
6 same self-interest to absorb it. And that is what has
7 happened, you know, we saw in Australia, and we've been
8 seeing for the last ten years, the Commission saying it
9 gets passed on. It becomes a floor. That is the second
10 anti-competitive vice. It becomes a floor because of,
11 in general terms, the neutrality of the acquirer.

12 Shall I move on just to quickly explain in the
13 skeleton where I am coming from on this a little bit?
14 So if one goes to page 50 of the skeleton, of the
15 closing, which is paragraph 117, this is essentially to
16 pick up the point. So paragraph 117, page 50, the
17 primary aim of 101.

18 MR JUSTICE BARLING: Just pause for a moment, Mr Brealey.
19 I do apologise.

20 (Pause)

21 Thank you. Yes?

22 MR BREALEY: My Lord, it was page 50, 117.

23 So, again, to a certain extent we have gone to this
24 in opening but I think it is important just to
25 re-emphasise it, and I will go just to a couple of

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1 passages in the European Courts. So, restriction of
2 competition contrary to 101. We set out two legal
3 principles here. The first is protecting the
4 competitive process. The courts and the Commission have
5 emphasised this time and time again. And, for example,
6 paragraph 118, the quote there:

7 "A general principle underlying Article 101, which
8 is expressed in the case law of the community courts, is
9 that each economic operator must determine independently
10 the policy which he intends to adopt on the market."

11 So again, I just re-emphasise the point, which is
12 that you have a cartel, they all get together in
13 a smoke-filled room, it doesn't matter whether the
14 cartel was a failure, whether it was half a success,
15 a massive success, they have distorted the competitive
16 process.

17 It may be that when a claimant wants to sue them in
18 damages, it can't show any loss because the cartel was
19 a complete failure, but it doesn't alter the fact that
20 Article 101 has intervened. And, we have seen time and
21 time again, companies have been fined massive amounts of
22 money, even though they have said that the cartel didn't
23 work. So I can't emphasise enough this process of
24 competition.

25 The second principle is -- again, we are familiar

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1 with it -- concerned with balancing pro-competitive
2 effects with anti-competitive effects. This is where we
3 say that, very often, Dr Niels goes wrong. It is
4 relevant to this two-sided market, the interaction
5 between the two sides.

6 We have set out in paragraphs 120 and 121 some of
7 the quotes from the case law. Could I ask the Tribunal
8 to go to Bundle E1? Because in the short adjournment
9 I went back to the judgments, and I just want to --
10 because of the questions to me about this two-sided
11 market, 101(1) and 101(3) -- remind the Tribunal about
12 the relevant passages.

13 Strangely enough, it is paragraph 181 in both
14 judgments. I don't know how could possibly happen, but
15 it is paragraph 181 in both judgments.

16 The General Court is at tab 15, and the relevant
17 page is 341. That whole page is quite illuminating,
18 because you see at paragraph 172, at the top, where the
19 Commission took the view that:

20 "The four-party bank card system operated in three
21 separate markets ... in an acquiring market, and relied
22 on the restrictive effects of the MIF on the acquiring
23 market."

24 So, again, we do see these three markets but
25 different considerations apply to all three:

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1 "We see this single service in joint demand. The
2 European Commission ..."

3 And Mr von Hinton Reed goes into more detail as to
4 why the acquiring market is the relevant market for
5 today's purposes and for the infringement decision.
6 Paragraph 181 is where I just want to emphasise, because
7 this is the point that was being made to me, so, again:

8 "With regard to the criticism by MasterCard
9 concerning the failure to take the two-sided nature of
10 the market into consideration, it must be pointed out in
11 that context the applicants highlight the economic
12 advantages that flow from the MIF. Thus, in essence,
13 the applicants state the MIF enables the operation of
14 the MasterCard scheme to be optimised ...(Reading to the
15 words)... merchants benefit from the MIF."

16 That is all the things which have been put to me:

17 "The applicants also complain the Commission
18 overlooked ...(Reading to the words)... the advantages
19 conferred on cardholders."

20 Now, the General Court says:

21 "Such criticisms have no relevance in the context of
22 a plea relating to the infringement ...(Reading to the
23 words)... may be weighed."

24 And just to show you how the main court dealt with
25 this, again, that was at tab 19. Again, it is

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1 paragraph 181, page 430. The CJEU refers to the
 2 relevant points:
 3 "In the light of that finding, the General Court
 4 therefore correctly concluded...(Reading to the
 5 words)... that the criticisms presented to it in
 6 relation to the two-sided nature of the system had no
 7 relevance in the context of a plea relating to
 8 infringement of Article 101 so far as entailed the
 9 taking into account of economic advantages under that
 10 paragraph. The General Court...(Reading to the
 11 words)... only in the context of the analysis
 12 under 101(3)."
 13 One of the questions that the Tribunal has asked
 14 concerns the House of Lords Courage v Crehan, which we
 15 have dealt with, but I think that both sides are agreed,
 16 even MasterCard, that when it comes to rulings by the
 17 courts on the proper interpretation of Article 101, then
 18 they are basically binding unless the Tribunal want to
 19 refer the issue back.
 20 And I would submit that this is an example of how
 21 the European courts are interpreting 101. They are
 22 saying that if you are going to make arguments that
 23 there are economic advantages to cardholders, then that
 24 should be properly interpreted, or properly analysed
 25 under 101(3) and not 101(1). If, I would imagine --

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1 if -- you are with me on the acquiring market. If the
 2 Tribunal is going to throw it open and say that there is
 3 just is a single market, which has been argued for by
 4 MasterCard for the best part of ten years and rejected,
 5 then it may be different, but we have just seen there
 6 that there are three markets here, and the acquiring
 7 market is a market that has been distorted, and that is
 8 the market that the retailers are complaining about,
 9 because they are paying a high fee, which has been
 10 collectively agreed, and if you want to argue that there
 11 are benefits flowing from that restriction of
 12 competition, that is a 101(3) analysis.
 13 So those are the two principles in ...
 14 I have got to deal with counterfactuals. I would
 15 like to highlight paragraph 127 of our closing, because,
 16 in my respectful submission, this, actually, goes to the
 17 heart of the case. Something that I referred to in
 18 opening but it concerns the "very radical" approach to
 19 Article 101. We say at 127:
 20 "Before setting out the reasons why MasterCard's
 21 co-ordination on the UK MIF infringes 101, it is helpful
 22 just to step back and consider what the Tribunal was
 23 faced with. It was faced with an industry and
 24 nationwide co-ordination between MasterCard and most
 25 retail banks in the UK, pursuant to which MasterCard

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1 fixes the level of a cost for a service which nearly
 2 every retailer in the UK pays ..."
 3 I can put:
 4 "... and the retailer has no practical ability to
 5 challenge such cost, and a significant beneficiary is
 6 MasterCard, which channels the majority of the funds in
 7 the direction of the issuing banks to retain business
 8 with them."
 9 I don't believe that that is, in any shape or form,
 10 over-egging it. I would imagine that MasterCard could
 11 well accept that definition.
 12 129:
 13 "It should come ..."
 14 So we say that it should come as no surprise that
 15 the Commission and various regulatory bodies have wanted
 16 to scrutinise that, but 129:
 17 "It should come as no surprise because Dr Niels
 18 candidly accepted in cross-examination that the notion
 19 that Article 101 did not apply to scrutinise such
 20 behaviour was ..."
 21 And this is his words:
 22 "... 'very radical'.
 23 "And he said:
 24 "'Now I am taking a very radical view that
 25 Article 101 should not apply. I think, in a way, yes,

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1 I am, because I do not think this is really a
 2 restriction of competition'."
 3 Now, why is that radical? Why I emphasise that is
 4 because of the Maestro story, which we set out at 130.
 5 And, again, that statement was in the context of
 6 MasterCard's Maestro story, and we would say, on the
 7 evidence, on any view, the Maestro debit card was an
 8 inferior -- on any view, the Maestro debit card was an
 9 inferior product to the MasterCard debit card. We have
 10 evidence to this which we shall refer to at some point:
 11 "... having less functionality and less acceptances
 12 worldwide. On MasterCard's own case, had it been able
 13 to pay issuers more, MasterCard would have been able to
 14 retain the issuers' business. That would have meant
 15 merchants paying a higher fee to incentivise issuers to
 16 continue to issue cardholders with an inferior debit
 17 card, all this through the mechanism of a collective
 18 price arrangement between MasterCard and the banks."
 19 If one is saying that that is not a restriction of
 20 competition within the meaning of 101, then I don't know
 21 what is, but if it is not, it is very radical. I would
 22 say almost heresy, but I will live with "very radical".
 23 Again, why is it radical? Again, if I just
 24 re-emphasise the first three lines of 131, so:
 25 "Dr Niels argues against the proposition that the UK

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1 MIF ...(Reading to the words)... element of the market
 2 knows best, that the UK MIF has been set to support
 3 skewed pricing structure of four-party scheme."
 4 Just pausing there, and we can skip the rest, but go
 5 on to the last paragraph of this section at 136, so what
 6 does that actually mean? It means that -- what is
 7 "Dr Niels' market knows best"? It does lead to the
 8 extreme proposition that all issuers in the UK would be
 9 legally free to collude and fix any level of interchange
 10 fee that is ultimately payable by merchants.
 11 That is why we say that is a very radical -- and
 12 I haven't even come to the three vices yet, which I need
 13 to emphasise, because it is relevant to Mr Hoskins' and
 14 MasterCard's counterfactual, but it is an extreme
 15 interpretation. And, you know, the Tribunal is faced
 16 with an interpretation that has been put on Article 101
 17 by the Commission for the best part of ten years,
 18 endorsed by the European Courts, was endorsed by the
 19 OFT, and the OFT has been investigating it, endorsed by
 20 Sainsbury's. And you compare that pedigree with the
 21 very radical approach that is being advocated by
 22 MasterCard, again, in my respectful submission there is
 23 only one conclusion: don't go down the very radical
 24 road.
 25 MR SMITH: Mr Brealey, just to be clear as to why it is

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1 radical, is it radical because one is looking at three
 2 markets when one should only look at one?
 3 In other words, let's suppose that MasterCard is
 4 correct, that if one has a no MIF situation, so that the
 5 interchange fee absent Bilateral Agreement is nil, and
 6 let's suppose, and I know this is contentious, let's
 7 suppose that Visa's interchange fee stays at the MIF
 8 rate, which is materially higher than MasterCard, such
 9 that on the issuing side there is a flood away from
 10 MasterCard towards Visa. Now I know all this is
 11 contentious but let's assume that. Are you saying that
 12 because the only relevant market is the acquiring
 13 market, that we don't look at these consequences until
 14 we get to 101(3)? Is that your position?
 15 MR BREALEY: No. You do look at it, and it has been looked
 16 at, and we will come on to, in two seconds, how it has
 17 been looked at, and essentially the answer to that
 18 question is that both parties rely, more or less, on the
 19 same evidence for different purposes.
 20 So we look at the MasterCard system, and then we
 21 look at competition with Visa, intersystem
 22 competition -- we are going to come on it in a moment,
 23 but I will flag it now. So you look at the kind of
 24 distortion of competition with MasterCard, then you look
 25 at Visa, and we say that competition with Visa actually

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1 exacerbates the competition for the MasterCard card. So
 2 you are looking at the upward pressure because of the
 3 intersystem rivalry, and that exacerbates the distortion
 4 of competition.
 5 They look at it, the same evidence, the upward
 6 pressure, and they say, "No distortion of competition",
 7 and at the end of the day the Tribunal is going to have
 8 to decide which way you go. But ironically, both
 9 parties are emphasising the upward pressure, the
 10 intersystem competition. And we will come on to it in
 11 a moment, but, again, I just talked about the pedigree
 12 of whose interpretation is to be preferred, the
 13 regulators, Mr von Hinton Reed, I mean, have said that
 14 this upward pressure, this intersystem competition, has
 15 just led to merchants paying higher and higher fees, and
 16 they haven't accepted, if it has ever been run, I think
 17 it probably has, this notion that the schemes would
 18 collapse. And the reason, the obvious reason, is
 19 because you are looking at the two together. But even
 20 if you were to look at the three markets, you are still
 21 ending up with a situation where issuers, who bear
 22 certain costs, are offloading those costs onto
 23 merchants.
 24 MR SMITH: Right. So I think what you are saying is that
 25 the difference between MasterCard and Sainsbury isn't

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1 which facts we should look at, but rather the
 2 appropriate inferences and implications of those facts?
 3 MR BREALEY: Yes.
 4 MR SMITH: So, forgive me, this is a rather basic question,
 5 but why are we having all this debate, then, about
 6 looking at one market rather than three? It seems that
 7 you and Mr Hoskins are both looking at what would happen
 8 on the issuing side of the market. You are drawing
 9 radically different conclusions --
 10 MR BREALEY: Again, one has to get to be quite careful. If
 11 you are looking at 101(1), so we are not in 101(3) --
 12 MR SMITH: We are definitely 101(1) territory. Absolutely.
 13 MR BREALEY: We have never said that you don't look at the
 14 competition from Visa. So the counterfactual is you
 15 will look at the competition from Visa. The reason
 16 I hesitate on 101(3), of course, is because you have to
 17 identify who has been affected in the relevant market in
 18 order to work out whether there are efficiencies, so you
 19 have to be certain of your market in 101(3).
 20 You have to be certain of your market in 101(1), but
 21 there is no doubt you are looking at competition between
 22 MasterCard and Visa to determine the nature of the
 23 restriction of competition, whether there is a breach of
 24 101(1).
 25 MR SMITH: Right. So sticking to 101(1), we should be

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1 looking at effects across all three markets in order to
 2 determine whether there is a restriction of competition?
 3 MR BREALEY: No.
 4 MR SMITH: No?
 5 MR BREALEY: Because what we are looking at is the
 6 competition between MasterCard and Visa saying that we
 7 need these high interchange fees in order to essentially
 8 pay the banks to retain our business. Possibly --
 9 I mean, there is no evidence necessarily of this, that
 10 goes to the issuing bank's pockets, the extent to which
 11 it goes down to the cardholders is a bit of a moot
 12 point, we have never really established whether it
 13 actually goes to the cardholders, to what extent, but
 14 that upward pressure leads to a greater distortion in
 15 the acquiring market. So, I said it doesn't matter, the
 16 three markets, but we still do come back to the
 17 acquiring market, because this nature of intersystem
 18 competition greatly exacerbates the distortion of
 19 competition in the acquiring market.
 20 MR SMITH: That, of course, is on your case, but then, to go
 21 back, let's suppose we take the view that the MasterCard
 22 contention as to what would happen is, in fact, the
 23 correct one, that the inability on the part of
 24 MasterCard to set a MIF in competition to Visa
 25 effectively causes the MasterCard system to fail.

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1 I know that is contentious, but that is a factor that is
 2 relevant in determining the anti-competitive effect of
 3 the default MIF.
 4 MR BREALEY: Yes, and we are going to come on to that,
 5 subjective necessity. They have been running this
 6 argument for -- and it is a restriction of -- but it is
 7 primarily an objective necessity, and they have been
 8 running this argument for years. And the answer is that
 9 it is a relevant --
 10 MR SMITH: The answer is that it fails on the facts, or the
 11 inferences we should draw from the facts, rather than
 12 being out of court for another reason.
 13 MR BREALEY: It fails on the law and it fails on the facts.
 14 Why does it fail on the law? It is because -- well, we
 15 will come on to it in a moment, but you cannot have
 16 a situation where you have -- I mean, to take another
 17 position, two cartelists, and we know very often that
 18 claimants only sue one or two, they don't sue all 50 or
 19 all 20, and you sue one cartelist and the cartelist
 20 says, "Well, I would have gone out of business had
 21 I stopped being part of this cartel. You have suffered
 22 no loss, there is no restriction of competition.
 23 I would have failed".
 24 So there is a real deep -- and we will come on --
 25 this is the OFT v British Airways case that we will

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1 touch on, but there is a deep legal point here as well
 2 as a factual point, as to circumstances where, if you
 3 have players in the same market operating the same
 4 practice, which is arguably unlawful, the extent to
 5 which one can say, "Well, it is not a restriction of
 6 competition because I would fail if I didn't have this
 7 conduct which is allegedly unlawful".
 8 MR SMITH: Yes, that is -- it's no criticism, but that is
 9 moving on to a slightly different point as to whether we
 10 apply the same assumption regarding the MIF to Visa, as
 11 we do to MasterCard, and that, as it were, is a detail,
 12 an important detail in the counterfactual world that we
 13 are looking at on the interissuer competition side.
 14 MR BREALEY: Yes.
 15 MR SMITH: I quite understand why you are suggesting the
 16 same --
 17 MR BREALEY: There are other reasons why the objective
 18 necessity is wrong in law. Another one is that it is
 19 objective necessity, it is not subjective necessity. So
 20 ultimately, with the greatest of respect, I think the
 21 Tribunal has been hoodwinked, to a certain extent, on
 22 this, and the reason is that MasterCard are asking the
 23 wrong question. The question that they are asking, and
 24 asking the Tribunal to answer, is a question -- for
 25 example, Mr Perez wakes up on a Monday and says, "What

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1 is going to happen if I reduce my interchange fees from
 2 0.9 to 0?" And they go around, they have the board
 3 meeting, and the board of MasterCard say, "Well, we are
 4 going to go out of business".
 5 Now, that is the question that really is being asked
 6 of the Tribunal, but we are not necessarily dealing with
 7 that question. We are in a competition case, and one is
 8 applying objective necessity, ancillary restraints
 9 doctrine, which has been defined and interpreted by the
 10 European Court. The only reason they are saying this is
 11 because they are relying on -- it is in their
 12 skeleton -- the ancillary restraints doctrine. And
 13 I will show you in a moment that the ancillary
 14 restraints doctrine is based on an objective test: would
 15 a scheme of this nature fail?
 16 Now, once you realise that you are not just looking
 17 at the scheme in question, but you are looking at all
 18 four party schemes, you quite soon realise that what
 19 I have called "the circular argument" just doesn't --
 20 their argument doesn't work.
 21 MR JUSTICE BARLING: So we look at it in a watertight
 22 compartment. We don't have to consider whether Visa is
 23 out there or anyone else when we look at whether this
 24 would be --
 25 MR BREALEY: I have got various, hopefully, strings to my

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1 bow, arrows in, whatever, my sling, but the answer to
 2 that question is yes. It is an objective necessity
 3 test.
 4 I mean, what you have to realise is that you are
 5 disapplying Article 101 to a collective price fixing
 6 agreement, and the European Court has said, "It has got
 7 to be something special in order to take it outside
 8 of 101". And what the European Court is looking at is:
 9 is it necessary for a four-party scheme? Is a MIF
 10 necessary for a four-party scheme? Answer: no, because
 11 they can charge the cardholders ...
 12 So, as soon as you look at it generally, all
 13 four-party schemes, this question of Mr Perez on the
 14 Monday morning in the board meeting, it is not the right
 15 question. I have other arguments, but --
 16 MR JUSTICE BARLING: So, because of bilaterals, even if
 17 there are thousands of players -- are theoretically
 18 possible, in a four-party scheme ---
 19 MR BREALEY: Yes.
 20 MR JUSTICE BARLING: That, effectively, answers the
 21 question, because that would work just as well, or
 22 certainly it wouldn't render it impossible.
 23 MR BREALEY: No, but the real -- it is almost a self-serving
 24 argument, is that we need the MIF -- we can't have
 25 bilaterals because Visa haven't got bilaterals. They

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1 have still got the MIF. And Visa have got a MIF at
 2 1 per cent, 0.9, and we are only going to get
 3 bilaterals, according to Mr Brealey, which the
 4 negotiations are going to be circa 0.2, and there is
 5 going to be a difference, but as soon as you look at it
 6 of the nature or type, the objective necessity, not
 7 subjective necessity, you quickly realise you can have
 8 a system of bilaterals, you can have no MIF, you can
 9 charge the cardholders, and we will see, this is what
 10 the European Court have said, but it is, in the context
 11 of having just -- having seen that there is a distortion
 12 of the competitive process and the three advices, there
 13 is a flaw, there is an inflated flaw, it is not the
 14 right answer. We are in a competition case, and --
 15 sorry.
 16 MR SMITH: That was very helpful. Just so that I have got
 17 it clear in my mind, looking, first, at objective
 18 necessity, we have, as it were, the four-party scheme on
 19 our laboratory slab and we look at it and we say, "Well,
 20 if we excise this particular aspect, the default MIF,
 21 will it or will it not work on almost a theoretical
 22 level".
 23 MR BREALEY: Well, it is a functional level, theoretical
 24 level. Yes.
 25 MR SMITH: On the restriction of competition side, we have

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1 a rather more broad input of facts, and there we are
 2 looking at consequences across at least two markets, but
 3 three markets, and there we are differing, both as to
 4 what the factual consequences in those markets are,
 5 where both parties are presenting different inferences
 6 that should be drawn, and there is this difference, you
 7 say it is a legal point, as to whether the same shoe
 8 should fit Visa as MasterCard, but there is no other
 9 difference between the parties in terms of the factual
 10 material that we should be taking into account in
 11 reaching our conclusion as to restriction of
 12 competition.
 13 MR BREALEY: Save that, I mean, the answer is, "Yes", but
 14 obviously we disagree with MasterCard on the facts,
 15 because what they have said, essentially, is they have
 16 relied solely on the Maestro, you know, "If we don't
 17 have this we will plummet to 0.3 per cent", and we say,
 18 you know, that was Dr Niels' evidence, both for Amex and
 19 for Visa, and we say that is not a very solid basis
 20 to --
 21 MR SMITH: I quite understand that, Mr Brealey. Helpfully,
 22 you have made that clear. Yes.
 23 MR BREALEY: If I could, then -- I have done kind of the
 24 very radical interpretation that MasterCard have.
 25 Could I go to -- and again, I will not -- well,

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1 paragraph 137 of the closing.
 2 MR JUSTICE BARLING: Yes.
 3 MR BREALEY: I do want to just emphasise the three vices, as
 4 I have called them, and one of the reasons I want to
 5 emphasise it is because the passages that we quote are
 6 relevant to the exchange I have just had, which is the
 7 intersystem competition. It is not correct that we
 8 don't take it into consideration. We just see it
 9 differently, and so does the Commission.
 10 MR JUSTICE BARLING: We are in 101(1) now, aren't we?
 11 MR BREALEY: We're still in 101(1).
 12 MR JUSTICE BARLING: We have got rid of objective necessity.
 13 MR BREALEY: Well, we haven't, unfortunately. I will come
 14 back to it. I just want -- I will do it quickly.
 15 MR JUSTICE BARLING: Don't worry, I just want to be sure
 16 what we are talking about. That is all.
 17 MR BREALEY: Sorry, we are not in objective necessity yet.
 18 MR JUSTICE BARLING: No.
 19 MR BREALEY: And the reason is that when you are look at
 20 objective necessity, as we have seen from the guidelines
 21 and from the jurisprudence, you are asking the question,
 22 "Is this restriction ..."
 23 MR JUSTICE BARLING: -- outside the scope?
 24 MR BREALEY: Yes. So it is an ancillary restraints
 25 doctrine. You have identified this restriction and now

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1 you are saying, "Well, it should fall within 101 but is
 2 it absolutely necessary for this pro-competitive aim?"
 3 if it is, we all know that it falls outside.
 4 MR JUSTICE BARLING: Yes.
 5 MR BREALEY: So the three vices. Now, I emphasise this --
 6 so the impact on the competitive process.
 7 Now, let's just see, again, whether we just blindly
 8 ignore, in MasterCard's counterfactual, Visa. Is it
 9 a realistic -- that you just ignore Visa?
 10 So paragraph 140, the impact on the competitive
 11 process. So this is the first of the three vices.
 12 So the Commission has, for over 20 years, objected
 13 to the price co-ordination between competitors reflected
 14 by multilateral interchange fees.
 15 Now, the Visa II decision, the Commission stated:
 16 "The MIF is an agreement between competitors which
 17 restricts the freedom of banks individually to decide
 18 their own pricing policies and distorts the conditions
 19 of competition on the Visa issuing an acquiring market.
 20 Both these activities are affected by the MIF and the
 21 Visa member banks".
 22 Pausing there, the same banks that are part of the
 23 MasterCard scheme, basically:
 24 "...are thus competitors as concerns their agreement
 25 ...(Reading to the words)... on price competition at the

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1 acquiring and issuing level since the MIF agreement will
 2 fix a significant part of ...(Reading to the words)...
 3 revenues respectively".
 4 MR JUSTICE BARLING: They seem to have changed their tune
 5 now because now they are talking about both levels
 6 distorting competition, aren't they? This is rather
 7 different from the way that they put it --
 8 MR BREALEY: In Visa II they do say it is a restriction on
 9 the issuing market, but when we are looking at the
 10 101(3), you have got to compartmentalise them, and in
 11 Visa II they looked -- when they were looking at
 12 exemption, they are looking at the acquiring market.
 13 So the reason I emphasise that passage is that, you
 14 know, you could swap Visa and MasterCard there, which is
 15 essentially what happens, so that is the first vice
 16 which applies equally to Visa. It is Visa and the
 17 issuing acquiring banks. Then you get the de facto
 18 minimum price.
 19 So, that co-ordination is exactly the same in the
 20 MasterCard infringement decision, paragraph 4.1.
 21 Then the de facto minimum price:
 22 "Again, in the Visa II decision, the MIF, moreover,
 23 has its effect ...(Reading to the words)... because it
 24 creates an important cost element, approximately
 25 80 per cent, which is likely to constitute a de facto

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1 flaw for the freeze charge to merchants since the Visa
 2 acquiring bank would make a loss on its acquiring
 3 activity".
 4 So is it really being suggested that in
 5 a counterfactual one is going to ignore all this? Then
 6 at 144 we get exactly the same:
 7 "MasterCard does not contest the myth...(Reading to
 8 the words)... sets is flaw".
 9 So so far we have exactly the same considerations
 10 applying to MasterCard and to Visa. Then we get to --
 11 now we are coming to the intersystem competition, and
 12 reverse competition, upwards pressure on MIFs.
 13 I will do that, then I will take -- I will go
 14 slightly out of my script because I think it is
 15 important when we look at this, we will also look at
 16 what the European Courts say, but 146, 147 and 148 is
 17 all about the competition between MasterCard and Visa,
 18 so just before the quote on 146:
 19 "The Commission, in the MasterCard infringement
 20 decision, described the upward pressure on interchange
 21 fees as follows".
 22 I will come on to that in a moment, but we will see:
 23 "However, as set out in section -- the forces of
 24 intersystem competition do not sufficiently ... it is
 25 referred to the evidence, the level of Visa's

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1 interchange fee".
 2 This is in the context of a MasterCard infringement
 3 decision.
 4 I think we will go to the passages in the -- and
 5 then again in the interchange fee regulation at 148:
 6 "Interchange fees are subject to reverse
 7 competition, meaning that competition between card
 8 schemes to attract issuers leads to ever-higher
 9 interchange fees".
 10 What I will do --
 11 MR JUSTICE BARLING: What I was going to suggest was if
 12 there is something you are going to take us to, given
 13 the time, do you want to tell us and we will read it
 14 over the lunch?
 15 MR BREALEY: Sorry, I had not noticed the time.
 16 MR JUSTICE BARLING: It is okay. We will read it over
 17 lunch.
 18 MR BREALEY: If I could, then? So this is on the
 19 competition between schemes, and it is the Commission
 20 decision which is at E2.2, page 1134.
 21 MR JUSTICE BARLING: Page 1134? Yes.
 22 MR BREALEY: There you will see, and I will just quickly do
 23 it after lunch, the Commission, but also could you take
 24 Bundle E1 which is the courts, so it is that page of
 25 E2.2, and then the courts is E1, tab 15, that is the

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1 General Court, at paragraph 136, and the main court,
 2 tab 19 at paragraph 176. Then it will make it easier
 3 just to --
 4 MR JUSTICE BARLING: Well, if we have a look at that over
 5 the break.
 6 MR BREALEY: There you will see that basically the
 7 Commission and the courts looking at the implications of
 8 this intersystem competition.
 9 MR JUSTICE BARLING: Right.
 10 MR SMITH: Mr Brealey, in return, can I leave you with
 11 a question?
 12 MR BREALEY: You can.
 13 MR SMITH: Obviously, the agreement whose anti-competitive
 14 effect we are testing is this default myth, but at the
 15 stage of testing we have not reached a conclusion
 16 whether it is anti-competitive or not. The whole point
 17 about excising it with a scalpel and working out what
 18 would happen in the counterfactual world without that
 19 default is to see whether it is or isn't
 20 anti-competitive.
 21 MR BREALEY: Just pausing there, whether there is any --
 22 whether there is a greater restriction of competition.
 23 MR SMITH: Yes. I am using, "Anti-competitive", as
 24 a shorthand.
 25 MR BREALEY: That is the purpose of the counterfactual, to

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1 see whether there is a greater restriction of
 2 competition.
 3 MR SMITH: Indeed, which is itself a shorthand for the
 4 101(1) test.
 5 MR BREALEY: Yes.
 6 MR SMITH: But one isn't presuming the restriction on
 7 competition, one is testing to see whether it exists or
 8 not.
 9 Now, on that basis, it surely is wrong to presume an
 10 anti-competitive outcome, in other words, to presume
 11 a restriction, given that the whole point is to create
 12 an analytical framework where you are testing whether or
 13 not there is going to be restriction or not as a result
 14 of this provision, and if that is right, isn't it wrong
 15 in principle to make the same presumption as regards
 16 a wholly separate scheme, namely the Visa scheme?
 17 I mean, I quite understand as between members of the
 18 same cartel that you would presume the deletion of the
 19 allegedly restrictive provision, but here we are talking
 20 about a scheme that is entirely separate, albeit in
 21 operation similar, so my question is; why do we apply a,
 22 "One shoe fits all", test in relation to a scheme that
 23 is self-standing and separate from the scheme under
 24 consideration here?
 25 MR BREALEY: Okay, and the reason is that if there is

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1 a suspicion that other players in the market, in the
 2 same economic sector, practising the same -- having the
 3 same practices, it would be wrong for the Tribunal to
 4 simply regard Visa as an angel, and blindly ignore the
 5 fact that, too -- you don't have to make a finding, but
 6 it would be wrong just to simply assume that
 7 0.9 per cent of the Visa is lawful. I will come back to
 8 that.
 9 MR JUSTICE BARLING: But wrong to assume that it would
 10 remain at 9 per cent but as I understood what you were
 11 saying in opening, and also in cross-examination, is
 12 that you were saying that we -- or implying that we
 13 should have regard to, in this counterfactual, so what
 14 would be likely to happen, how Visa would be likely to
 15 react to, as it were, MasterCard reducing its MIF to
 16 zero or very low, and we should judge that on the basis,
 17 amongst other things, of how they would see the
 18 regulatory risks.
 19 MR BREALEY: Correct, and I adopt both. I say if you look
 20 at the OFT v British Airways, it would be wrong, as soon
 21 as you get that suspicion that they are doing something
 22 wrong, you shouldn't be looking at them as a perfectly
 23 valid counterfactual. If I am wrong on that, I fall
 24 back on the cross-examination and all the factual
 25 evidence that has been heard as to whether the Tribunal

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1 can, in fact, decide that the banks would have migrated,
 2 everything that my Lord has just put to me, so I am
 3 doing it at two levels. I am doing it at a more
 4 legalistic level, which is to what extent should you
 5 have regard to Visa and is it a valid counterfactual at
 6 all when there is a suspicion that a fellow cartelist or
 7 someone operating the same scheme is doing this very
 8 same thing, so you just stop there, and if you don't --
 9 if you are not with me on that I fall back on the
 10 evidence in the case, and I say that in a competition
 11 case like this where MasterCard has just -- you know, it
 12 is a restriction of competition, will there be the
 13 migration of banks, will Visa accept the migration, all
 14 the things that we were -- I have been asking the
 15 witnesses about, and my Lord has been asking the
 16 witnesses about, so it is at two levels. One is a more
 17 general legalistic level, one is they lose on the facts
 18 as well.
 19 MR SMITH: But you are not saying, just to be clear, you are
 20 not saying that we should, just because we are presuming
 21 no MIF for MasterCard, we should automatically presume
 22 no MIF for Visa. What you are saying instead is that we
 23 should, in the counterfactual, build in this sense of
 24 regulatory risk, or regulatory concern, that someone in
 25 Visa's position would have, given all the facts of the

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1 case.
 2 MR JUSTICE BARLING: I thought you were saying that, in
 3 fact. I thought that was your legalistic point. In
 4 other words, I thought that was your primary point, is
 5 that we should assume that Visa will have no -- will
 6 drop to the same level, but if that is not right, you
 7 then turn to the evidence and the regulatory risk and
 8 try and work out what they would probably do.
 9 MR BREALEY: The two are aligned, but basically, as soon as
 10 the Tribunal has a suspicion that Visa is in the same
 11 boat as MasterCard --
 12 MR SMITH: We apply exactly the same counterfactual.
 13 MR BREALEY: Correct.
 14 MR SMITH: Right. Okay. I had misunderstood your first one.
 15 so your primary position -- I understand your secondary
 16 position but your primary position is that we should say
 17 it is a no default MIF for MasterCard and it is a no
 18 default MIF for Visa and we should work out the
 19 consequences on that basis.
 20 MR BREALEY: Basically you just cannot have a situation
 21 where MasterCard on a Monday morning can say, "I will go
 22 bust", and Visa on a Monday afternoon will say, "I will
 23 go bust", when they are operating exactly the same
 24 activity, so if you have a suspicion that one follows
 25 the other, and we will see what Dr Niels said as well,

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1 you should cut it short and not go into the evidence.
 2 I would say but even if you do go into the evidence,
 3 given the regulatory risk, given the perception that
 4 Mr Perez talked about, you will not get the migration
 5 that MasterCard says.
 6 MR JUSTICE BARLING: Because you submit on that basis we
 7 should assume that Visa would follow suit, or certainly
 8 bring their MIF down to --
 9 MR BREALEY: Is it really realistic that the same banks are
 10 going to just swap the name -- having been told, the
 11 same banks, having been told that the MasterCard scheme
 12 is unlawful, are just going to go across the doorway and
 13 have a different name on it?
 14 MR JUSTICE BARLING: And sign up with Visa. Yes.
 15 MR SMITH: I suppose there is a question, though, I mean,
 16 let's suppose we are not with you on the first
 17 hypothesis, that the same shoe fits both schemes, and
 18 let's suppose, in our counterfactual world, Visa is
 19 rather bullish as regards the regulatory risk, and so
 20 when MasterCard has its MIF removed, and effectively the
 21 default is zero, and Visa doesn't, and it maintains its
 22 rates as before, the next question must be; will there
 23 be this flood of banks away from the MasterCard scheme.
 24 MR BREALEY: Now there are two questions. the first is
 25 whether that flood is going to cause a collapse, and

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1 then you are into objective necessity, and the second
 2 is -- I am sorry about the time -- but what is the
 3 analysis here? What MasterCard are -- and I say that
 4 there is no restriction of competition, because again,
 5 on a restriction of competition counterfactual, you have
 6 got to ask yourself a question; I have got this
 7 restriction, arguably of competition because it is
 8 within the scheme, it is what we call "the intra-brand
 9 competition restriction", how is that going to be
 10 affected, vis-à-vis Visa? And what you are looking at
 11 is whether there is a lesser restriction of competition,
 12 or greater restriction of competition. That is what
 13 a restriction of competition counterfactual is looking
 14 at. "I have got this restriction of competition and now
 15 I want to work out whether it is a greater". The bottom
 16 line is it would be wrong, in my submission, for the
 17 Tribunal to ignore the restriction of competition within
 18 MasterCard on the basis that it just helps them to
 19 compete with somebody else, so even assuming Visa was
 20 lawful, nothing wrong with it whatsoever, again, just
 21 stand back and think about it. You have a cartel, and
 22 a cartel says, "Well, I quite like this cartel to
 23 compete with this person over here". This person is
 24 quite efficient, it has got there on its own merit, but
 25 the cartelists get together and say, "Well, you know,

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1 if" -- and we will come on to MasterCard's
 2 counterfactual, it says that competition would be
 3 reduced, the counterfactual says, "I need this cartel
 4 otherwise I can't properly compete with this person".
 5 Now, that is another dense question that this
 6 counterfactual is being put forward. This is right at
 7 the end of my -- of the analysis, but even if you find
 8 against me on everything else, you have still got to ask
 9 the question; is it really a proper interpretation of
 10 101(1) to allow a situation -- of a price-fixing cartel
 11 to say, "It is not a restriction of competition because
 12 I quite like this cartel to compete with this third
 13 party".
 14 MR SMITH: Could we not simply put ourselves in, let's say,
 15 Sainsbury's' position, and we know from the data that
 16 you helpfully provided us yesterday, that over the years
 17 the Visa credit card MIF was about 0.8 as an average,
 18 a blend of all the various cards, credit cards. Now,
 19 let's suppose that that remained the rate throughout the
 20 claim period. Wouldn't Sainsbury's simply use the Visa
 21 rate as a cost to it, and as an input into negotiating
 22 a different interchange, bilateral interchange, with
 23 MasterCard? In other words, it would use that as one of
 24 the inputs into working out what a better price would be
 25 for it with MasterCard.

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1 MR BREALEY: Maybe. What you are putting to me is --
 2 MR JUSTICE BARLING: In the counterfactual this is?
 3 MR SMITH: Yes, in the counterfactual.
 4 MR BREALEY: In the counterfactual, Visa is at 0.8.
 5 MR SMITH: Visa is at 0.8, what Sainsbury's would be in
 6 a position, indirectly through its acquirers, would be
 7 saying to MasterCard, "Well, we now need to negotiate
 8 a price. That price, obviously, has got to be lower
 9 than Visa's", query what it will be, but something will
 10 be agreed with the MasterCard organisation, the issuing
 11 banks participating there, and that would, in itself,
 12 have an effect on Visa over time. I mean, in a sense,
 13 what I am putting to you is that there will be -- even
 14 assuming the Visa rates remain unchanged, there will be
 15 an interplay between those rates and whatever is
 16 hypothetically agreed with MasterCard.
 17 MR BREALEY: I think to a certain extent that is what
 18 Mr von Hinton Reed was saying, which is that you cannot
 19 just assume that everybody is going to go to Visa, there
 20 will be some retailer complaints that -- bilaterally
 21 they will be playing people off.
 22 MR SMITH: I appreciate it is a very different context but
 23 we saw something like that with the Amex/Sainsbury
 24 negotiations. I know Amex is a different beast
 25 altogether, but nevertheless, one saw a certain hard

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1 negotiation on the part of Sainsbury with --
 2 MR BREALEY: That actually does come back to what I just
 3 mentioned about being kind of -- the last point, the
 4 last bit of the jigsaw, which is that
 5 a counterfactual -- a restriction of competition
 6 counterfactual is about whether there is a greater or
 7 lesser restriction of competition, hence what the
 8 European Court said about the hold-out, the introduction
 9 of that new scheme rule results in a less restriction --
 10 there will be a less restrictive competition, so it is
 11 not just -- you don't -- MasterCard don't just get home
 12 on a restriction of competition counterfactual, because
 13 they say that, "I can't compete as well as I can, absent
 14 the cartels, with the cartel".
 15 So, what you are putting to me is an example of how
 16 it could pan out. It may be to the detriment of
 17 MasterCard, but it is not a greater restriction of
 18 competition. It is just the cartel can't operate any
 19 more and has got to -- the market has got to sort itself
 20 out.
 21 MR JUSTICE BARLING: We will peruse those bits you told us
 22 about. We will say we will start at quarter past.
 23 (1.18 pm)
 24 (Luncheon adjournment)^sp
 25 (2.15 pm)

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1 MR BREALEY: If I could just finish off on just where we
 2 were, I think we were basically at paragraph 146 of the
 3 closing submissions.
 4 MR JUSTICE BARLING: Yes.
 5 MR BREALEY: I am grateful for you taking the time to read
 6 the decision and the judgments. If I could just quickly
 7 go to those so that I can just emphasise what is going
 8 on, the decision is at E2.2, and we need to go to
 9 page 1134. This relates to MasterCard's repeated
 10 emphasis that we have to look at the absence of the MIF
 11 in the actual context in which it would happen.
 12 MR JUSTICE BARLING: Yes.
 13 MR BREALEY: At 1134, section 72.4:
 14 "Intersystem competition increases anti-competitive
 15 effects in downstream markets."
 16 Paragraph 467 is the one that we cite at our
 17 paragraph 146, where it is talking about upward
 18 pressures on interchange fees, but I would also ask the
 19 Tribunal to note section 7.2.4.2, recitals 469 and 470.
 20 Again, this is a MasterCard infringement decision, and
 21 it is squarely looking at the effect of intersystem
 22 competition between MasterCard and Visa:
 23 "In its Visa II decision, the Commission expressed
 24 the concern that competition between Visa and MasterCard
 25 creates upward pressures on the level of the MIF since

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1 most banks are members of both Visa and MasterCard and
 2 therefore are likely to issue whichever of the two
 3 brands of card has the higher interchange level and
 4 brings them most revenue. There is empirical evidence
 5 that MasterCard's board has repeatedly increased
 6 possible interchange fee rates to align rates with those
 7 of Visa."
 8 I said earlier on that there is -- you have got
 9 almost the same story, and then one has got to work out
 10 what the implications are. I want to come on to the
 11 judgment in a minute, but clearly, the Commission has in
 12 mind the fact that these two competing schemes want to
 13 play off each other and, you know, outbid each other.
 14 And it is not saying, "Well, if I reduce the MasterCard
 15 MIF to zero they are going to go out of business", the
 16 actual analysis is, "I have got to do something about
 17 this restriction of competition, and I am looking at
 18 Visa at the same time". Unquestionably they are looking
 19 at Visa at the same time. They are looking at
 20 competition from Visa between Visa and MasterCard
 21 I will not go through it, and I am sure that the
 22 Tribunal has it, but I want to concentrate on Visa, but
 23 of course, at page 1174, just to flag it, because I want
 24 to continue on the Visa story, but at 1174 you have
 25 quite a detailed analysis, section 7.3.4.6, about how,

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1 in the absence of the MIF, MasterCard can still compete
2 with Amex.

3 So that section is the Commission's analysis about
4 Amex. And you will see there certain references to
5 Australia. But if I could concentrate on Visa, as
6 I say, at recital 469, the Commission is looking at the
7 state of competition in its actual context. So, if
8 I could put that -- the decision -- away, and just turn
9 up the judgment.

10 It is actually slightly odd, some of the arguments.
11 First, to the General Court, which is at tab 15. And
12 I gave you the key paragraph, but just to put it in
13 context -- so this is at tab 15 -- could I first go to
14 paragraph 87? Because it is important to see what the
15 passage that I asked the Tribunal to note -- you know,
16 what is the analysis here? It is clearly the analysis
17 of the counterfactual. So this is page 330 of tab 15,
18 and here at paragraph 87:

19 "It is clear from the settled case law that in
20 examining the restrictive effects on competition under
21 101, account should be taken of the actual conditions in
22 which an agreement, a decision by an association,
23 produce their effects. In particular, the economic and
24 legal context in which the undertakings concerned
25 operate, the nature of the product services, in other

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1 words, the real operating conditions and the structure
2 of the market concerned."

3 All the things that Mr Hoskins and MasterCard
4 emphasised in opening. So that is what they are looking
5 at. So, that is paragraph 87. That goes back -- if you
6 go to the old purple books in 1966, you know, the
7 Consten and Grundig, Technique Miniée, this is not new,
8 this is settled case law.

9 If you then go to paragraph 129, at 335, this is
10 under the heading, "The complaints relating to the
11 assessment of competition in the absence of the MIF".
12 So, page 335, paragraph 129, just above 129 we see,
13 under the heading, "The complaints relating to the
14 assessment of competition in the MIF" -- so we are
15 looking at the actual conditions of competition that
16 would arise in the absence of the MIF:

17 "Again, the applicants and a number of Interveners
18 submit that the Commission failed to fulfil its
19 obligation ...(Reading to the words)... would occur in
20 the absence of the MIF."

21 They raise two complaints. The first complaint is
22 at paragraph 130, which we can ignore, and the second
23 complaint is over the page, at paragraph 135, so this is
24 in "The complaints relating to the assessment of
25 competition in the absence of the MIF". Two complaints,

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1 and I am looking at the second complaint at 135. Now,
2 the applicant, that is MasterCard:

3 "A number of Interveners complained that the
4 Commission failed to establish that elimination of the
5 MIF would raise the level of competition. That
6 complaint can be divided into four sets of objections."

7 Now, in the first place, this is what MasterCard is
8 submitting:

9 "It is maintained that the Commission wrongly took
10 intersystem competition into account."

11 So what MasterCard were arguing there I really don't
12 know, but it seems to be that:

13 "The Commission wrongly took intersystem competition
14 into account ...(Reading to the words)... restriction of
15 competition, recitals", and it goes on.

16 Then we get the General Court rejecting the
17 argument:

18 "First, it must be observed that, as noted by the
19 Commission in 416-498 ..."

20 As we have seen:
21 "... that competition between the MasterCard system
22 and the other bank card schemes for the bank's business
23 resulted in upward pressure on the levels of the MIF to
24 a relevant aspect of the economic context within the
25 meaning of the case law cited in paragraph 127 ..."

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1 Which is the settled counterfactuals:
2 "Accordingly, the Commission was legitimately able
3 to take into account ...(Reading to the words)... the
4 MIF on competition."

5 Now, whether the Tribunal disagree with it, or
6 MasterCard disagree with it, that is how the General
7 Court, and the Commission, the General Court upholding
8 the Commission, were looking at the argument that, "We
9 need to play off each other. We want to outbid each
10 other". And the analysis is not in the sense that one
11 of them is going to go bust, which is essentially this
12 circular argument, the analysis is the merchants are
13 paying too high fees.

14 So we don't end there, because the CJU endorses this
15 paragraph. And so, quickly to tab 19, we see the
16 argument at paragraph 140, which is at page 425 of the
17 copy of the judgment in the bundle, but here we see --
18 and it is strange that -- this seems to be the LBG's
19 argument, so I am not sure whether this is MasterCard or
20 what, I don't know anymore, but:

21 "Next, in the light of the parties' arguments and
22 particularly the economic evidence ...(Reading to the
23 words)... importance of constraints from other payment
24 systems."

25 So here, again, it was squarely -- the "importance

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1 of constraints from other payment systems". So they are
 2 criticising the General Court which had endorsed what
 3 the Commission had said. And at paragraph 176, can
 4 I ask the Tribunal to note 176, at page 430:
 5 "As to the arguments summarised in paragraph 140 of
 6 the present judgment, it is sufficient to note that in
 7 paragraph 137 of the judgment under appeal, the General
 8 Court expressly found that the Commission was right to
 9 have taken intersystem competition into account in its
 10 analysis of the effects of the MIF."
 11 So I am still not quite sure what MasterCard was
 12 arguing in front of the courts in Luxembourg, whether it
 13 was arguing, "Well, you should not be taking intersystem
 14 competition into account", or whether, "You should", but
 15 what is absolutely quite clear is that the CJEU, the
 16 main court, endorsed what the General Court said, and
 17 the General Court endorsed what the Commission said,
 18 which was, "We are looking at intersystem competition.
 19 We are looking in a counterfactual, and our assessment
 20 is that it is leading to higher fees paid by merchants
 21 because of the upward pressure".
 22 Essentially what MasterCard is asking the Tribunal
 23 to do is to dump all that and say, "Well, we don't care
 24 about that upward pressure, that analysis. Actually,
 25 when you properly look at it, we will go bust, because

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1 it is in the nature of this intersystem competition that
 2 we need to outbid each other to compete, and if you tie
 3 one hand behind MasterCard's back, then it will go bust
 4 because Visa will take over". That is just not how it
 5 has been analysed to date.
 6 It is the same evidence but just a different
 7 economic and legal analysis, but MasterCard cannot
 8 possibly say -- they might disagree with it, may
 9 distinguish it, I don't know, but they can't possibly
 10 say that no one has looked at the absence of the MIF --
 11 and that was the heading in the General Court, the
 12 absence of the MIF -- has not looked at it.
 13 MR JUSTICE BARLING: I mean, they seem to be saying that,
 14 you know, you look at everything. In this judgment, if
 15 you look at paragraph 179 --
 16 MR BREALEY: Of the main court?
 17 MR JUSTICE BARLING: Of the one we have just been looking
 18 at.
 19 MR BREALEY: And that is, you know, what Mr Hoskins was
 20 saying in opening. We don't disagree with it. When you
 21 are looking at the counterfactual you are looking at
 22 everything. The phrase is "the economic and legal
 23 context". I emphasise, by the way, the legal context.
 24 It has to be examined in the economic and legal context.
 25 MR JUSTICE BARLING: It is my fault, but I am still not

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1 100 per cent sure about what the question is that the
 2 counterfactual is there to answer in relation to the
 3 alleged restriction which is a restriction on the
 4 acquiring market. That is the restriction you are
 5 relying on. And the counterfactual is there to see
 6 whether, absent the alleged restriction constituted by
 7 the MIF --
 8 MR BREALEY: There would be a greater restriction.
 9 MR JUSTICE BARLING: On the acquiring market?
 10 MR BREALEY: On the acquiring market.
 11 MR JUSTICE BARLING: And how, then, do you feed in what the
 12 court then says is the -- also to be taken account of,
 13 in the legal -- because it is a two-sided market and so
 14 on, there are other aspects to the market, the wider
 15 aspects -- how, in answering that question, do you feed
 16 those in? Those aspects of the legal and factual
 17 context?
 18 MR BREALEY: Well, as you have just seen. So we have seen
 19 that there is -- whether you call it a restriction of
 20 competition, because it gets quite -- there is
 21 a restriction. There are the three restrictive vices.
 22 And there is, actually, a restriction of competition,
 23 because that is restriction within -- if one thinks
 24 about it, it is a restriction of intra-brand
 25 competition, because MasterCard have 70 per cent of the

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1 market in credit cards, or 55-70, nigh on -- it is
 2 a huge market share, and so you have this massive credit
 3 card scheme company having a collective price-fixing
 4 agreement, and so distorting competition in that part.
 5 Now you ask yourself the question, "So I am going to
 6 look at it in its economic and legal context, so I am
 7 looking at the restriction on the acquiring market,
 8 MasterCard, whether you call it the whole market, but it
 9 is MasterCard, and I am looking at, in its economic
 10 context, how competition from Visa either makes it worse
 11 or better", in a sense. And, in a nutshell, what has
 12 been held to date is that competition from Visa has made
 13 it worse --
 14 MR JUSTICE BARLING: Because it has the upward pressure.
 15 MR BREALEY: -- whereas what is being submitted now, and we
 16 don't know whether it was submitted then, but what is
 17 being submitted now is that it makes competition worse,
 18 because MasterCard is going to go out of business. It
 19 is just a question of how one analyses it.
 20 I mean, I am kind of dealing with both things, so
 21 that is the -- what I wanted to say on -- I just need to
 22 emphasise the points on objective necessity which I kind
 23 of flagged. I can go straight to paragraph 180 of our
 24 closing.
 25 We have set out here four -- it is under the

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1 heading, "Relevant legal principles". If I just flag
 2 the legal principles, because it is not quite apparent
 3 because there should be numbers, so under the "Relevant
 4 legal principles" of 180, we have got four legal
 5 principles. One is impossibility of performance -- this
 6 is page 72 of the closing, para 180 of the closing, and
 7 it is under the heading, "Relevant legal principles".
 8 We have set out four. One is, "Impossibility of
 9 performance". Two is, again, our, "Low balancing of pro
 10 and anti-competitive effects". Three is "Objective
 11 necessity not subjective necessity"; and then what
 12 I call "Two wrongs do not make a right".
 13 The impossibility of performance we have seen --
 14 MasterCard don't disagree with this. You know, this is
 15 one of the legal principles that would be binding
 16 because this comes from the European Court, but I do
 17 emphasise what the court is saying here. So what the
 18 court is saying at paragraph 181, where it is a matter,
 19 right at the last line:
 20 "Contrary to what MasterCard claims ..."
 21 So that is what they were claiming there:
 22 "... the fact that the operation is simply more
 23 difficult to implement, or even less profitable without
 24 the restriction, cannot be deemed to give that
 25 restriction the objective necessary and required in

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1 order to be classified as ancillary."
 2 Just pausing there before I get to the other points
 3 on this, again, just stepping back from the analysis
 4 point of view, objective necessity is quite a high
 5 hurdle. It is an impossibility. We see that
 6 hit, "impossibility". The mere fact that you are making
 7 less money, or you are less profitable, ie you are less
 8 competitive, is not sufficient for you to escape
 9 Article 101. That is what they are saying there. Just
 10 because you come to court and you say, "This restriction
 11 is necessary for me to make more money, I will be less
 12 profitable without it", means that you don't escape 101.
 13 It has to be impossibility.
 14 So here is my point; how can it be the case, when
 15 MasterCard come to its restriction of competition
 16 counterfactual, to say, "There is no distortion of
 17 competition and therefore I escape because I am less
 18 profitable"? There is something not quite right about
 19 the analysis, so --
 20 MR JUSTICE BARLING: By "less profitable", are you equating
 21 that with the Maestro-type scenario?
 22 MR BREALEY: Yes, "I can't compete as well".
 23 So, we know we have 101, the restriction of
 24 competition. Is that restriction of competition -- does
 25 it fall outside of Article 101 completely, because of

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1 the objective necessity? So the argument is run. It
 2 does fall outside 101 because -- this is what they have
 3 been arguing -- "I would be less profitable. I would
 4 lose my Maestro business, part of it, to Visa. I would
 5 be less profitable". So they lose that argument on
 6 objective necessity. The European Court says, "Less
 7 profitable is not good enough, you have got to show
 8 impossibility", to which MasterCard say, "All right, we
 9 accept that principle, I will bin objective necessity.
 10 I think we will go out of business but I accept that".
 11 But then they say, "Well, actually, there is no
 12 restriction of competition in my restriction of
 13 competition counterfactual because I would be less
 14 profitable".
 15 You can see how it is put. I mean, you can see --
 16 if one goes to paragraph 167 of their skeleton, of their
 17 closing, and again, the counterfactual -- you can almost
 18 make anything of it if you want to, just by tripping off
 19 the few words that they do. But at 167, this is at
 20 page 56, you see here, this is not their objective
 21 necessity any more, this is their assessment of
 22 restriction of competition. And you see at 169 and 170,
 23 you know, references to reduced competition, "We would
 24 be significantly reduced"; so in laymen's commercial
 25 terms that means, "I am making less profit. On less

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1 profit, I can't compete as well".
 2 MR JUSTICE BARLING: Well, they put it -- I mean, you say
 3 "less profitable", the way they put it is "forced out of
 4 the market". That is their Doomsday scenario, isn't it?
 5 MR BREALEY: If they are forced out of the market, they are
 6 in their objective necessity.
 7 If it is the same thing, I don't mind, if they are
 8 being forced out of the market, there is the objective
 9 necessity, but under this count both experts agree they
 10 will be forced out of the market, so if that is the
 11 objective necessity, I don't mind. If this is
 12 a different counterfactual that is being put to the
 13 Tribunal I certainly do mind, because what they are
 14 saying here, for example, the last sentence of 169, is:
 15 "... the competitive position would therefore have
 16 been significantly worse."
 17 MR JUSTICE BARLING: That is when they leave the market.
 18 I think 170 is the point.
 19 MR BREALEY: Maybe that's right, yes.
 20 MR JUSTICE BARLING: They are saying, "Well, even if the
 21 Tribunal were to conclude that they would have retained
 22 some presence, then the level of competition wouldn't be
 23 as good".
 24 MR BREALEY: That is absolutely right, my Lord. The point
 25 still is, having lost before the European Court

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1 saying, "Objective necessity means reduced profit,
 2 reduced competition", you then actually make the very
 3 same argument in a different counterfactual, and try to
 4 get home on that.
 5 I haven't even really got to the other -- but just
 6 as a matter of analysis, it is quite troubling. And it
 7 comes back to what I was saying before lunch, that it is
 8 quite odd -- you have a different situation, you have
 9 a cartel with a 50 per cent market share, say, quite
 10 efficient, doing quite well, acting lawfully, the other
 11 50 per cent have a cartel and they say: well, you know,
 12 we can actually do better, collectively, than
 13 individually. And competition would be reduced, or
 14 significantly reduced, if we can't have this collective
 15 price-fixing agreement.
 16 There is something quite troubling about such
 17 a submission. So that is the impossibility of
 18 performance that is the first relevant legal principle.
 19 The second is the balancing of pro and
 20 anti-competitive effects. The reference to
 21 paragraph 183 to the Visa, I will just go to it, it is
 22 E1, tab 2, recital 59, page 29. So there should have
 23 been a reference there, E1, tab 2, recital 59, page 29.
 24 I would like just to emphasise the thirdly,
 25 "Objective necessity not subjective necessity".

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1 I meant, when I was in the main court's judgment, to go
 2 to paragraph 163, but we can see what the main court --
 3 I am sorry to go around, but at paragraph 178 of the
 4 skeleton, if we could just go back a few pages, we do
 5 have the quote. I meant to take the Tribunal to it, but
 6 we do have the quote, so we are looking at:
 7 "As the court stated ..."
 8 At paragraph 163:
 9 "... is whether the co-ordination ..."
 10 Hold on. Sorry. I will go back even more --
 11 MR JUSTICE BARLING: "Could remain viable"? There is
 12 another one.
 13 MR BREALEY: Yes, absolutely. So an open system such as
 14 MasterCard system could remain viable. I have been
 15 caught out by the words "such as", before, but I still
 16 read that:
 17 "An open system such as MasterCard ..."
 18 It is looking at it generally, not just MasterCard.
 19 That is the main court. But when we go back to
 20 objective necessity, not subjective necessity, at 184,
 21 if we could just quickly go to --
 22 MR JUSTICE BARLING: Back to the judgment?
 23 MR BREALEY: No, we have been through that, but E3.10, which
 24 is the Commission's cost of the survey on the cash. At
 25 4307 -- I did take, I think, Dr Niels to this, but

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1 at 4307, paragraph 50, 253, is, in my submission, quite
 2 a neat summary of the logic underlying Article 101 and
 3 its proper interpretation. So I did take him to this.
 4 So:
 5 "Competition law analysis under 101 ..."
 6 50 is the -- all agreements. 51 is:
 7 "In MasterCard, the Commission concludes that it
 8 infringed 81 by restricting competition between
 9 acquiring banks, de facto floor."
 10 We have seen all that. Then 52 is the objective
 11 necessity:
 12 "Restriction of competition may fall outside
 13 ...(Reading to the words)... via their respective
 14 customer groups."
 15 And this is quite fundamentally important, because
 16 you are trying to work out whether the effectiveness of
 17 Article 101 is -- you know, you are looking at whether
 18 Article 101 will not be applied to a system of pricing,
 19 collective price-fixing, and you are not looking at the
 20 subjective position of the cartel saying, "I need this
 21 cartel to compete with this other person in the market".
 22 You are looking at it in a more general level, on an
 23 objective level, "Is this scheme of a type or nature?"
 24 And there is good reason why you are looking at it
 25 from an objective level, not a subjective level, because

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1 otherwise the effectiveness of 101 is going to be
 2 seriously undermined.
 3 That is the third legal principle.
 4 The fourth is the two wrongs do not make a right.
 5 I don't know if the Tribunal wants to go back to --
 6 I mean, I have been to it a few times, but it is the
 7 OFT's passage in the British Airways, just to -- the
 8 quotes are here, but, again, I do refer to it in the
 9 damages counterfactuals, so maybe we should just have
 10 a look at it.
 11 So this is the fourth legal principle, and this is
 12 E1, tab 3, at page 224. We were trying to work out
 13 before lunch -- I was talking about kind of a legal
 14 approach and then the factual approach, and this is how
 15 the OFT looked at it, I think, from a legal position,
 16 without even looking at the facts, really.
 17 I mean, you would have to -- obviously, it is not in
 18 a vacuum, but you are not examining whether the banks
 19 are going to migrate or Visa is going to accept them,
 20 you are looking at it at a far more holistic level. So,
 21 again, at 224, this is back, I think, in 2003 -- well,
 22 the decision is 2005. This argument has been rehearsed
 23 quite a lot, so:
 24 "... must be set by reference to competitive
 25 constraint."

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1 So this is at 224. And again, 186 of the decision,
 2 224 of the bundle, the same argument is being made:
 3 "We need this MIF in order to compete with Visa ..."
 4 And:
 5 "MasterCard submit that failure to recognise the MIF
 6 is indispensable to the scheme as any outcome would
 7 place the scheme at a competitive disadvantage.
 8 "The MIF must be set by reference to competition
 9 provided by other payment card schemes, particularly the
 10 Visa scheme. The Visa scheme must be able to set, and
 11 if necessary vary, the amount of the MMF MIF to respond
 12 to competition".
 13 Again, we saw this earlier on this morning, the
 14 Commission just not buying this at all.
 15 At 639 the OFT's response:
 16 "In essence, this argument suggests that the cost of
 17 additional features ..."
 18 ie the costs being offloaded onto the merchants:
 19 "... can be recovered through the MIF, irrespective
 20 of how peripheral these features ...(Reading to the
 21 words)... of these costs is necessary."
 22 This is why I say it is a bit of a public policy
 23 legal point here:
 24 "On this basis, otherwise unlawful conduct would
 25 become lawful if others also engaged in it. The OFT

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1 cannot accept this as a justification for the recovery
 2 of the costs."
 3 So they are not actually, as we have done in this
 4 trial, analysed or cross-examined Mr Perez, trying to
 5 work out whether banks would migrate -- and we can go to
 6 the British Airways, but to a certain extent I set it
 7 out in paragraph 187. That is all we need to -- so they
 8 refer to the British Airways case:
 9 "Whereas in this case the Commission is faced with
 10 a situation where numerous factors give rise to
 11 a suspicion of anti-competitive conduct on the part of
 12 several large undertakings in the same economic sector,
 13 the Commission is even entitled to concentrate its
 14 efforts on one of the undertakings concerned while
 15 inviting the economic operators which have allegedly
 16 suffered damage as a result of the possible
 17 anti-competitive conduct to bring the matter before the
 18 national authorities."
 19 So, in other words, the regulator can choose one
 20 person, and that person can't say, "Well, I am going to
 21 go bust because you are just taking me out", the
 22 regulator is entitled to say, "There are other
 23 players operating the same practices, and you cannot use
 24 as a justification the fact that other people are
 25 carrying out the same practice".

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1 MR SMITH: Mr Brealey, looking at paragraph 639, the
 2 penultimate sentence indicates the OFT doesn't accept
 3 that it would be unworkable, complex or burdensome to
 4 use an alternative approach to set the MIF, so they
 5 clearly are of the view that, actually, there is some
 6 alternative open to MasterCard.
 7 MR BREALEY: Yes.
 8 MR SMITH: Do we know what that alternative was?
 9 MR BREALEY: I will find out. I think it is the bilaterals
 10 again, but I think we have to be careful on the OFT's
 11 counterfactual, because if you remember they got into
 12 a mess about it.
 13 MR JUSTICE BARLING: They got into trouble. Yes.
 14 MR SMITH: You mean the appeal to this Tribunal?
 15 MR BREALEY: Yes.
 16 MR SMITH: Yes, but it just seems to me, looking at 639 on
 17 its own terms, that there is a qualification to the
 18 public policy point that they are taking, which is that
 19 there was also an alternative approach.
 20 MR BREALEY: Well, I read it as a kind of "Further,
 21 alternatively".
 22 Further, alternatively, I don't accept that it would
 23 be unworkable --
 24 MR JUSTICE BARLING: They seem to be discussing -- I may
 25 have got this wrong but they seem to be discussing how

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1 you calculate the MIF rather than whether you have
 2 a MIF, so you could have calculated it on a different
 3 basis, and you mention, you know, by reference to
 4 certain costs. Alternative approach.
 5 MR BREALEY: The whole case is similar to what -- in the
 6 European Commission, which is similar now. I mean,
 7 I would, with respect, disagree, that the point being
 8 made in the argument -- and we did ask for the
 9 submissions, we have not got them -- but the point being
 10 made is that, "I, MasterCard", this is 637, "I,
 11 MasterCard, need to allow my issuers to recover these
 12 costs in order so that MasterCard can compete with
 13 Visa".
 14 MR JUSTICE BARLING: Yes. Yes. That is the point they are
 15 dealing with.
 16 MR BREALEY: That is the point they are dealing with,
 17 "Otherwise we are at a competitive disadvantage".
 18 Exactly the same issue that is being raised in this
 19 case, thirteen years on, or whatever.
 20 The regulator is troubled by that because everybody
 21 knows that you have got two four-party schemes in the
 22 UK. They are both being investigated. In, you know,
 23 Europe you have the Visa exemption which talks about the
 24 restriction of competition we have already referred to,
 25 and yet we come back to the -- it is a deeply

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1 unattractive argument for MasterCard to say, "We need
 2 these costs to compete with Visa", and Visa saying, "We
 3 need these costs to compete with MasterCard", lo and
 4 behold we both win.
 5 MR JUSTICE BARLING: But it would be -- I mean, the OFT
 6 appear to be possibly, here, falling into the trap
 7 that Mr Smith mentioned earlier, which is that --
 8 assuming that something is unlawful. If you assume it
 9 is unlawful, of course, it is very undesirable to
 10 have -- but if you --
 11 MR BREALEY: Or do you assume it is lawful? That is what is
 12 being said. But, on that point, that is why I pray in
 13 aid what the court says in British Airways, where it
 14 talks about a suspicion of anti-competitive conduct. In
 15 our closing we have referred to the suspicion.
 16 And as I said earlier on, if one applies the British
 17 Airways case, so you have a sector, and everybody is
 18 operating the same practice in this economic sector, and
 19 there is a suspicion of anti-competitive conduct, then
 20 you can go against one, and, as I say, it is no
 21 justification to say, "Well, others are doing it, others
 22 are pursuing this same conduct", if that is a suspicion.
 23 You know, that is the words in the judgment, hence,
 24 "suspicion". You don't have to assume, you don't have
 25 to prove. I am just taking the words that the European

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1 Court has said, which is, "If you have a suspicion, then
 2 it would be no justification".
 3 If you are not with me on that, then we have delved
 4 into the facts which we are going to go through and have
 5 a look at in a moment.
 6 Essentially, it is a matter of impression, whether
 7 the impression that one gets is, "Can this really be
 8 right? Visa and MasterCard have -- are the only
 9 four-party -- they have both been investigated, both
 10 been found to have distorted competition on the
 11 acquiring market, both given undertakings, both
 12 commitments, both been regulated in the same way. When
 13 it comes to someone claiming damages, they are told,
 14 "Well, you just forget Visa". And if my respectful
 15 submission it would be wrong, as a matter of principle,
 16 simply to assume -- assume -- that Visa is acting
 17 lawfully, where there is clearly a suspicion that it
 18 would not be.
 19 Again, I come back to the cartel. We all know
 20 that -- you know, you have ten people in a cartel, I am
 21 the claimant, I sue one person in the cartel, the other
 22 nine are not party to the private proceedings, is it
 23 right for the one cartelist to say, "Well, if you find
 24 me guilty of an infringement I would go out of business
 25 and therefore there is no restriction of competition".

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1 The other nine are not bound, they are not bound by any
 2 judgment. The same argument can be made. How can you
 3 possibly assume that the others are guilty? They are
 4 not before the court. And yet it happens all the time
 5 that, in a stand-alone action, you are suing one alleged
 6 cartelist, but then it becomes a bit of a cartel's
 7 charter to say, "Well, I actually need to be in this
 8 cartel to compete". Or, you know, not to go out of
 9 business.
 10 MR SMITH: But that is the same cartel, whereas Visa, of
 11 course, is separate.
 12 MR BREALEY: Yes, and I am trying to work out where this
 13 goes, because, again, why is it that MasterCard are
 14 saying, "You can ignore Visa"? You are telling me,
 15 well, you cannot assume that Visa is acting unlawfully.
 16 Well, you could say the same in the cartel situation.
 17 MR SMITH: But -- no, because the test is one is attempting
 18 to ascertain the effect of an allegedly anti-competitive
 19 agreement, so you blue-pencil the pernicious, or
 20 allegedly pernicious, agreement to work out what the
 21 consequences are. And if you are blue-penciling it out
 22 in a single cartel, then obviously the blue pencil apply
 23 to say all members of the cartel.
 24 The issue we have here is that there is the
 25 MasterCard scheme and, let's assume, a Visa scheme that

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1 is, to all intents and purposes, the same, but it is
 2 separate. And what you are asking is: you are saying,
 3 "Well, assume an anti-competitive effect in the
 4 MasterCard case, and apply your scalpel to severance to
 5 see what the consequences are, but do exactly the same
 6 in respect of a similar but completely independent
 7 scheme".
 8 MR BREALEY: Well, all I am doing, actually -- I actually
 9 don't think I am doing that much. I am asking the
 10 Tribunal, in a counterfactual, to realise that Visa
 11 operates an identical scheme and has already been found
 12 to have infringed Article 101. And one has to remember
 13 that this is in a competition counterfactual. All I am
 14 doing is bringing Visa into it to show that it is
 15 exacerbating the restriction of competition, making it
 16 worse, rather than better.
 17 MasterCard are using Visa as saying, "Look at Visa
 18 over there, I need this cartel. Competition is better
 19 if I have this cartel". So they are using Visa as
 20 a mechanism to say there is no distortion of
 21 competition, and I am using Visa, with all the bells and
 22 whistles and all the baggage that Visa have got, to
 23 say --
 24 MR JUSTICE BARLING: Ignore Visa in the counterfactual,
 25 because -- assume they are the same.

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1 MR BREALEY: Assume they are the same. And I am not asking
 2 the Tribunal to find Visa guilty of anything. It is
 3 just that in the economic context they operate the same
 4 system.
 5 When one is looking at a restriction of competition,
 6 my alleged restriction of competition, are you allowed,
 7 or should you be looking at the Visa scheme and seeing
 8 how that Visa scheme impacts on the MasterCard?
 9 MR SMITH: The trouble is, how far does one take the
 10 assumption? Let's say we are with you and say: okay,
 11 well, let's assume for the sake of argument that Visa is
 12 in breach of 101(1). Do we then assume an exemption
 13 under 101(3)? If we assume an exemption under 101(3),
 14 at what level do we assume it to be?
 15 Then one has a kind of feedback effect. Because --
 16 let's suppose we assume that Visa is subject to, yes,
 17 a regulatory regime. 101(1) bites but there is a 101(3)
 18 exemption which puts the Visa MIF at a level that is
 19 materially higher than MasterCard at zero? On
 20 Mr Hoskins' case, as I understand it, there will be
 21 a flood of banks moving Visa's way.
 22 MR BREALEY: Absent the evidence in the case.
 23 MR SMITH: Of course. I am putting to you Mr Hoskins'
 24 argument. I fully accept that you say he is wrong on
 25 the facts. You can take that as read. The difficulty

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1 is, when one starts making these assumptions, I am not
 2 sure where we stop.
 3 MR BREALEY: Well, it may be that this is a matter for the
 4 evidence, but clearly I put to the witnesses the scheme
 5 is the same, or similar.
 6 MR SMITH: Yes.
 7 MR BREALEY: We know that the Commission has said there will
 8 be no discrimination between MasterCard and Visa, so we
 9 know that the exemption -- so, to answer, squarely, your
 10 point, that what MasterCard would be exempted would
 11 broadly be the same with Visa, because there would be no
 12 discrimination.
 13 Now, I don't know what Visa is going to do in autumn
 14 of this year but, you know, I can only go so far. What
 15 I can say is that all the evidence in the case has been
 16 the Commission saying to MasterCard, "We will treat you
 17 equally, no discrimination", and I will come in a moment
 18 to it, because I will come on to the damages
 19 counterfactual very quickly, but MasterCard itself
 20 saying, "Well, we see there should be a level playing
 21 field".
 22 And once you take stock of that type of evidence, it
 23 is not a great leap to then say, "Well, am I really
 24 going to reject the claim for damages on the basis that
 25 I can just ignore -- I can assume" -- I mean, this is

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1 essentially what Mr Hoskins is asking, asking the
 2 Tribunal to assume there is absolutely nothing wrong
 3 with Visa.
 4 I get criticised for saying, "Assume there is
 5 something wrong". Is it really realistic to assume that
 6 there is nothing wrong with Visa? If I could go to
 7 section H, because I just have a little bit more
 8 evidence that I would like to -- this is the damages,
 9 the compensatory damages, where we are starting to look
 10 at the evidence.
 11 So this is at page 205. I thought that I would deal
 12 with compensatory damages under Maestro stuff and the
 13 Amex stuff because it all fits into the counterfactual
 14 window all in one go.
 15 Well, we are starting to get to the evidence, but --
 16 so this is the damages Counterfactual -- so just to flag
 17 what we have done in this section, we deal with the
 18 damages calculation postulated by MasterCard, loss of
 19 Visa to Amex, so A should be just Visa, not Amex:
 20 "Damages calculation, loss of business to Amex."
 21 Then we have got two other points on Mr Harman's
 22 Section 9 and the credit. But A and B, 604 A and B, are
 23 the Visa and the Amex counterfactual.
 24 At paragraph 6.10 -- so we start with the Visa
 25 counterfactual -- Dr Niels reduces Sainsbury's damages

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1 on the basis -- lower MIF than Visa, lost market share:
 2 "The only evidence relied on is the factual decline
 3 in MasterCard's debit card transaction. It takes the
 4 debit card decline to 3 per cent and simply applies this
 5 analogy to credit cards, and, on this simple basis,
 6 MasterCard effectively wipe out the claim for the
 7 overcharge".
 8 We say it is wrong for four reasons, so we are now
 9 on damages, and to a certain extent they overlap with
 10 the previous. The first one, again, is my suspicion of
 11 unlawful conduct by Visa. Maybe this quote should have
 12 been earlier on, but again, we rely on the OFT v British
 13 Airways case at 612. At 613, Mr Perez and Dr Niels both
 14 accepted in cross-examination it was common knowledge
 15 that Visa was being investigated:
 16 "Same three anti-competitive vices...(Reading to
 17 the words)... same damages counterfactual would apply".
 18 Then we have got Dr Niels, you know, which
 19 assumption are you going to make:
 20 "Yes, I think...(Reading to the words)... forced to
 21 set its MIF lower".
 22 So again, this is from Dr Niels saying, well, his
 23 analysis would apply equally to Visa. Yet somehow there
 24 is trouble with my assumption that you cannot just
 25 assume -- or you cannot just assume that Visa is --

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1 there is nothing wrong with Visa.
 2 MR SMITH: Well, isn't there also an assumption that
 3 merchants like Sainsbury just sit back and let it all
 4 happen? We have mentioned on a number of occasions this
 5 week the possibility of a bilateral negotiation, and we
 6 put it to Dr Niels that there might be such negotiation
 7 in this case, and he suggested that that was wrong
 8 because Sainsbury's would take a short-termist view and
 9 stick, as it were, to a MIF of zero. But then it is
 10 reasonably obvious, is it not, that if one does that,
 11 there will be such a migration to Visa, assuming they
 12 keep their MIFs heartening. Wouldn't that incentivize
 13 a large merchant like Sainsbury to think: well, sticking
 14 to a zero interchange fee might be very good for us in
 15 the short run, but in the medium run we are going to be
 16 left with the very high MIF of Visa.
 17 I am obviously assuming that Visa are unaffected and
 18 untrammelled by what is happening to MasterCard.
 19 Doesn't that analysis, the commercial interests of
 20 Sainsbury, have some sort of place to play in this
 21 counterfactual?
 22 MR BREALEY: Absolutely. It is a point, I think, we make at
 23 625. What, sir, you are doing, is taking me to the
 24 facts, and I totally agree, the position of retailers
 25 cannot be ignored. It cannot simply be assumed that

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1 retailers will sit quietly back and will be prepared to
 2 pay higher fees.
 3 MR JUSTICE BARLING: You mean higher fees from Visa in the
 4 counterfactual?
 5 MR BREALEY: Yes.
 6 MR JUSTICE BARLING: Because what the retailers are faced
 7 with, then, they have -- you know, they have
 8 a substantial MSC to pay when people use their Visa
 9 cards, and they have a very considerably lower MSC when
 10 people use their MasterCard on this counterfactual,
 11 don't they?
 12 MR BREALEY: They will vote with their feet.
 13 MR JUSTICE BARLING: Well, you would have thought it would
 14 be odd if, in that situation, there weren't rumblings
 15 about, ultimately, surcharging, and/or refusing, even,
 16 if -- I mean, you would have thought that the size of
 17 that differential then, or the starkness of it, would --
 18 MR BREALEY: Well, one sees what happened with Amex.
 19 MR JUSTICE BARLING: Well, yes, in the Amex negotiation.
 20 Yes.
 21 MR BREALEY: As I think Mr von Hinton Reed said, you know,
 22 in the real world -- and I think this is what you are
 23 putting to me -- in the real world, if you are going to
 24 have a scheme that one is a 2 per cent MIF, on
 25 a bilateral, say, and one is a 9 per cent or 8 per cent,

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1 that you are not going to be very happy when,
 2 historically, it was basically similar, and you are
 3 going to start choosing the one that is cheaper.
 4 MR JUSTICE BARLING: You are going to start looking around
 5 for ways in which you can --
 6 MR BREALEY: Do it. Yes.
 7 MR JUSTICE BARLING: And equally, though, there may be some
 8 pressure on the retailer to -- you know, to do something
 9 for the -- in a bilateral negotiation. So you might see
 10 Visa, as it were, taking a more realistic view, and you
 11 might see Sainsbury's and Tesco and others saying to
 12 their acquirers, you know, "Okay, we are prepared to pay
 13 something".
 14 MR BREALEY: And I endorse all that. This is what we try to
 15 do in this section here. All I am trying to urge on the
 16 Tribunal at the moment is a deeper point, and the deeper
 17 point is, where you have two four-party schemes in the
 18 UK, both have been investigated, both have been found to
 19 infringe Article 101 because the MIF is fixed
 20 competition, and in a claim for damages, one of the
 21 schemes says, "I need that restriction of competition to
 22 compete with my rival", is the Tribunal going to ignore
 23 the history relating to Visa? That is a judgment call,
 24 obviously, for the Tribunal.
 25 MR SMITH: I quite see that, Mr Brealey. I suppose what is

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1 troubling me slightly is that if one looks at the
 2 position of Sainsbury in this counterfactual world, and,
 3 again, contrary to what you are urging us to do, we
 4 ignore the effects of Visa and just assume they carry on
 5 as before, there are a number of possibilities in the
 6 counterfactual world which suggest themselves
 7 to Sainsbury.
 8 Just looking at the figures that you helpfully
 9 provided us yesterday, we see that the Visa debit card
 10 transactions, even accounting for a lower interchange
 11 fee, amounts to 250 million over time, whereas the
 12 credit card transactions with a Visa are 88 million, so
 13 they are much smaller, and the position is the exact
 14 reverse in the case of MasterCard. And that reflects
 15 the market share information that MasterCard provided us
 16 with.
 17 MR BREALEY: Yes.
 18 MR SMITH: So one option, I simply put out there as
 19 something which springs out from the figures, is that
 20 Sainsbury could say unless Visa are realistic about the
 21 MIF they are charging, they will continue to accept Visa
 22 debit cards but they will not accept Visa credit cards,
 23 and they will negotiate something else with MasterCard
 24 that reflects the commercial realities.
 25 MR BREALEY: Absolutely.

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1 MR SMITH: So there are a number of factors which seem to
 2 come into play which don't necessarily drive one to the
 3 conclusion that MasterCard is going to go out of
 4 business, even if one doesn't make the assumption that
 5 Visa follow MasterCard down to a zero MIF.
 6 MR BREALEY: Correct. I would accept that.
 7 Basically, what is being presented to the Tribunal,
 8 as we have just seen, is that you can just look at the
 9 Maestro story and that is it. Same curve, same
 10 everything. What, hopefully, the evidence -- at least
 11 as has come out -- is to support that very thing, which
 12 is that it is a lot more complicated than that.
 13 Mr von Hinton Reed says that you cannot ignore the
 14 position of the retailers. It is not just that downward
 15 curve to 3 per cent on the basis of Maestro. And
 16 I fully endorse that. That is how key -- I have
 17 probably left that until last, but we do endorse that.
 18 But I still urge the more nuclear option, which is that
 19 you cannot assume that Visa ...
 20 Just to emphasise a few more points on the factual
 21 side of it now. I suppose we have looked at the
 22 retailers, which was our fourth point -- it went
 23 slightly out of ...
 24 If one goes to paragraph 619, "Other factual
 25 considerations", where we are essentially looking at the

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1 facts now. So, "Other factual considerations", the
 2 first point -- so it is slightly out of order, but if
 3 I can take 619 and 621 together, so 621:
 4 "In the damages counterfactual, MasterCard's MIF
 5 would be exempted at ...(Reading to the words)...
 6 counterfactual world ..."
 7 We don't have to prove beyond doubt this is going to
 8 happen; it is a counterfactual at the end of the day.
 9 But we rely on 619, where MasterCard wrote to the
 10 Commission marking-up the draft undertaking to include
 11 the following:
 12 "In view of the Commission's policy to treat ..."
 13 Is this confidential?
 14 NEW SPEAKER: Sorry, it is from "On 13 March 2009", yes.
 15 MR BREALEY: Okay, so if I can just ask the --
 16 MR JUSTICE BARLING: We will read it.
 17 MR BREALEY: Basically it matches the ...
 18 (Pause)
 19 Looking at the other factual considerations, in my
 20 submission you can, realistically, conclude that Visa
 21 and MasterCard would be broadly the same when it comes
 22 to an exemption. And that is exactly what has happened
 23 in the actual world.
 24 It is not as if it is even in the real world. The
 25 real world is they have been treated exactly the same:

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1 they are 0.2, they are 0.3. They were -- as a result of
 2 that from the competition investigations and as a result
 3 of regulations. That is the real world.
 4 The second point I rely on is this, "The greater the
 5 perception, the less risk of loss", which is teased out
 6 from what MasterCard knew, what they thought, and -- so,
 7 basically, I don't know if the Tribunal is familiar with
 8 this, but I asked the question:
 9 "My question is, you referred before the Commission,
 10 you referred to it as a ..."
 11 That is confidential?
 12 MR JUSTICE BARLING: We will just read it.
 13 MR BREALEY: It is the last four lines of Mr Perez' quote of
 14 his evidence.
 15 MR JUSTICE BARLING: Yes.
 16 MR BREALEY: "The greater ..."
 17 And that is entirely consistent with what Dr Niels
 18 said about Amex. I don't think this is confidential:
 19 "I consider that the constant threat of being
 20 designated could have affected Amex's incentives such
 21 that it did not pursue a strategy to increase its market
 22 share considerably in Australia, as being designated
 23 would have led to its charges being capped in a similar
 24 way to MasterCard and Visa."
 25 That evidence from him is absolutely consistent with

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1 what Mr Perez was saying. Again, it comes back to the
 2 debate we have been having, that if there is
 3 a suspicion, a risk, whatever it is, a likelihood, of
 4 your main competitor being designated, treated in the
 5 same way, it makes it more unlikely that you are going
 6 to lose business. It is more unlikely that the issuing
 7 banks are just going to change the name of the card from
 8 MasterCard to Visa if they know they are going to have
 9 exactly the same problem.
 10 The third point is the question of damages. You
 11 can't ignore the fact -- it is the British Airways
 12 case -- that even if -- is Visa really, realistically,
 13 going to accept all this when there is a damages claim?
 14 So, all this regulatory, private enforcement, in
 15 circumstances -- and again, one has to ask the right
 16 question. This is a competition case. It is not just
 17 Mr Perez waking up on a Monday and saying, "Boys, we are
 18 going to go down". One is looking at a counterfactual
 19 in a competition case. One has to look at the
 20 regulatory context. So we know that you look at it in
 21 the economic and legal context, and that must include
 22 the regulatory context, it must include the private
 23 enforcement context, the legal context.
 24 I don't know whether we are going to take a break or
 25 we are going to take a break? I know we are finishing

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1 at 4 o'clock.
 2 MR JUSTICE BARLING: We will have a short break.
 3 (3.25 pm)
 4 (A short break)
 5 (3.35 pm)
 6 MR BREALEY: What I intend to do before 4 is I will just go
 7 through the rest of the damages, the counterfactual,
 8 look at Maestro, look at Amex.
 9 If I could just make two points before we go on to
 10 that. We are in the damages counterfactual at the
 11 moment. The damages counterfactual, just to highlight
 12 the point, forgetting Visa for the moment, the damages
 13 counterfactual will be based on any exemption that
 14 MasterCard would have, so assuming that the Tribunal
 15 considers it a restriction of competition, and assuming
 16 the Tribunal considers there is sufficient evidence of
 17 an exemption, when you get to the damages
 18 counterfactual, that is the difference.
 19 I am going to come on to Mr Hoskins' broad axe
 20 probably on Monday, but certainly on our case, if you
 21 accept Mr von Hinton Reed's evidence on exemption, when
 22 you are looking at the damages counterfactual you are
 23 looking at MasterCard being exempted on our basis,
 24 possibly on their basis, and Visa untainted.
 25 MR SMITH: But if we are putting it in terms of a general

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1 legal test, I think it was in MasterCard's pleadings
 2 where they said that the damages is the difference
 3 between the interchange fee actually paid by Sainsbury
 4 less the highest lawful interchange fee that MasterCard
 5 could have levied.
 6 MR BREALEY: Correct. All right, but I will deal with the
 7 broad axe point now, which is that that doesn't mean to
 8 say that -- for example, it doesn't mean to say that
 9 MasterCard are not under an obligation to adduce robust
 10 and convincing evidence of exemption. There is still an
 11 obligation for them to do that. You cannot just say,
 12 "Because that is relevant to our final quantum ..." that
 13 you can adopt broad axe on exemption. Maybe I will
 14 come to that on Monday. We certainly disagree with any
 15 notion that a broad axe can be wielded at exemption.
 16 The first point is that if there is a restriction of
 17 competition, there has been an unlawful demand, and it
 18 would be -- so forget exemption, so let's assume the
 19 Tribunal says, "I don't like Dr Niels, I don't like
 20 Mr von Hinton Reed, I see there is a restriction of
 21 competition, no exemption", we would still have a claim
 22 for damages, obviously. That might be the difference
 23 between what we actually paid and what the Tribunal
 24 concluded was to be paid on a bilateral basis.
 25 MR SMITH: I suppose it is a different question in the sense

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1 that what we have to do is to determine whether -- and
 2 I am on the exemption question here -- as a matter of
 3 fact, looking at all the evidence, the MIF either as
 4 set, or as it might have been set, is exemptible or do
 5 we take it at one remove and say, "Well, suppose, in the
 6 counterfactual world, the MIF had been scrutinised, what
 7 are the possibilities of a regulator exempting the MIF?"
 8 It is the former rather than the latter.
 9 MR BREALEY: It is the former. Absolutely. Otherwise you
 10 are taking -- you are assuming an exemption when they
 11 haven't met the strict conditions for exemption.
 12 MR JUSTICE BARLING: We are not exempting it, we are just
 13 arriving at what the level is.
 14 MR BREALEY: I think you are --
 15 MR JUSTICE BARLING: I have only just thrown that out
 16 because --
 17 MR BREALEY: I think you are exempting it. You have
 18 a situation where -- well, since 2007 someone has been
 19 charging a price which is, on one view, unlawful, and
 20 now -- but the person who is charging the unlawful price
 21 says, "Well, actually, it could have been exempted at
 22 roughly the same price or a lot lower". So I think the
 23 Tribunal does have to conclude -- in order to save
 24 MasterCard from paying the difference, for the sake of
 25 argument, between zero and 0.9, it has to arrive at

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1 a conclusion that the MIF was exempted, and therefore
 2 lawful.
 3 MR JUSTICE BARLING: I mean, if we grant an exemption, we
 4 grant it against all the world then, don't we, the
 5 UK MIF --
 6 MR BREALEY: Well, it doesn't bind the world, it only binds
 7 MasterCard.
 8 MR JUSTICE BARLING: Yes.
 9 MR SMITH: I suppose that was the question I was groping at,
 10 and the Chairman put it much better than I did. We are
 11 not actually talking about exemption here -- unless we
 12 exempt the rates actually charged -- but we are talking
 13 about what is the highest level that would be
 14 exemptible, looking at circumstances in the past. So it
 15 is not quite a --
 16 MR BREALEY: Well, I do disagree with that, with respect,
 17 and the reason I disagree with it is because we are
 18 coming to court -- or Tribunal, court -- and we are
 19 saying that there has been a breach of Article 101(1),
 20 and the breach of Article 101(1) has led to an
 21 overcharge. Full stop. Don't even get to exemption.
 22 Now, the burden of proof is on MasterCard to say,
 23 "Well, hey, that overcharge is not the difference
 24 between zero and 0.9, because, actually, I charged
 25 a lawful price because it would have been exempted

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1 at X". 0.3, for example, so actually, the lawful price
 2 was 0.3.
 3 MR JUSTICE BARLING: Is that a quantification damage point
 4 or causation quantification, in which -- or is it --
 5 I mean, I suppose there is a distinction -- whether it
 6 makes any difference I don't know -- between actual
 7 grant of an exemption retroactively for that period, and
 8 actually just calculating damages on the basis of
 9 a figure which we consider would be exemptible.
 10 I suppose there is a distinction in law between those
 11 two because one is just a concept of quantification of
 12 damage.
 13 MR BREALEY: I can half understand that, with respect, as
 14 long as it is not accepting Mr Hoskins' point which is,
 15 for us, in some way, to prove exemption. Or in some way
 16 it is for him not to meet the rigours that the European
 17 Court has set down for a person in his position to prove
 18 an exemption.
 19 MR JUSTICE BARLING: Because, as I understand it, your
 20 answer to his point is, you have gone as far as you have
 21 to go once you have proved the overcharge.
 22 MR BREALEY: Correct.
 23 MR JUSTICE BARLING: So, prima facie, you say that is
 24 your --
 25 MR BREALEY: I can go home.

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1 MR JUSTICE BARLING: That is your measure of loss, you say,
 2 prima facie. And if they want to go further than that,
 3 they have to show either that they either did charge
 4 a lawful -- because there was an exemption, it was
 5 exemptible, or can be exempted now, or the overcharge
 6 isn't as big because there was a level between the two
 7 points, extreme points, which was exemptible, or can be
 8 exempted now.
 9 I am just not sure whether it is, which can be
 10 exempted or is exempted. I don't know whether it
 11 matters.
 12 MR BREALEY: I mean, we have come to the Tribunal in kind of
 13 a spirit of co-operation, saying that -- we could have
 14 just had no evidence on exemption at all, but that would
 15 have been -- we would have nothing to rebut, we would
 16 have had a lot shorter hearing. But it is quite clear
 17 the burden of proof is not on us, and we realise, as
 18 a matter of practicality, that MasterCard are going to
 19 come to court, to the Tribunal, and say, "Hey, it should
 20 have been exempted at this level", and so we have come
 21 to match that. And we realise that it may be exempted,
 22 but, equally, the Tribunal -- I mean, I squarely put to
 23 Dr Niels, "Are you prepared to accept that what
 24 Mr von Hinton Reed, which is based on what the
 25 Commission has said, is in the range of possible

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1 exemptions?" and he says, "No", so it is technically
 2 possible for the Tribunal to say, "I am afraid there is
 3 no evidence -- I am not certain of any level of
 4 exemption".
 5 MR SMITH: I suppose what I am grasping at is this is not
 6 a regulatory situation where we are determining whether
 7 there has been a competition law infringement, and, if
 8 there has been, formally exempting it. What we have
 9 got, instead, is a claim for breach of statutory duty,
 10 where you are asserting that the statutory duty that has
 11 been breached is Article 101(1). There has been an
 12 infringement which you have to establish on the balance
 13 of probabilities.
 14 Now, if you succeed on that, then there is
 15 a question of what damages flow from that established
 16 infringement, and what I am getting at is: why isn't
 17 this a Chaplin v Hicks situation? Sorry, it is the
 18 beauty contest case.
 19 MR BREALEY: We had this in Enron. Yes.
 20 MR SMITH: Where what we do is we actually assess, not on
 21 the basis of balance of probabilities, binary, zero/one,
 22 but on loss of a chance; and how far does that feed into
 23 the question of, for instance, exemptability? So it may
 24 be the case that you say, "Well, in a quantification
 25 exercise you are not actually asking is it exemptible or

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1 is it not", a binary question, but you are looking much
 2 more at the one in ten chances of the lady in the beauty
 3 contest.
 4 MR BREALEY: Well, in my respectful submission, that would
 5 be a wrong approach, and the reason it is a wrong
 6 approach is because if I succeed in proving an
 7 infringement of 101(1), the charge that we have paid has
 8 been unlawfully demanded. It is an unlawful price. We
 9 are entitled to damages based on the -- what we should
 10 never have paid, which is that MIF. That MIF, that
 11 price, that has been set by reference to the
 12 price-fixing arrangement, should never have happened,
 13 and it is unlawful. It is just like the Hans Justu San
 14 Giorgia: I am entitled to that money back. It would be,
 15 in my respectful submission, a very retrograde step in
 16 that situation to say to the person who has infringed
 17 competition law in a claim for damages, "Well,
 18 I understand that you have to prove on a balance of
 19 probabilities, by reference to cogent evidence,
 20 exemption, but I am going to excuse you from that
 21 because the claimant has got a Boyes and a Hicks, a
 22 beauty parade loss of a chance". And I am not sure what
 23 the loss of a chance is. It is a breach of statutory
 24 duty, we have suffered loss, and if MasterCard want to
 25 cut down our loss by saying, "Well, the difference is

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1 not between zero and 0.9, the difference is between 0.7
 2 and 0.9", then they can do it, but they have to do it on
 3 the balance of probabilities by reference to the
 4 standard required of an exemption.
 5 MR SMITH: Does it perhaps operate at two levels? So, for
 6 instance, if Mr Hoskins is saying, as, indeed, he is,
 7 that the MIF actually charged by MasterCard was
 8 exemptible, then that is something where he bears the
 9 full burden, and if he succeeds then you recover
 10 nothing, but if he is saying the maximum lawful
 11 interchange fee was whatever level it was, that is
 12 something which moves into the area of quantification of
 13 damages, and, therefore, is much more on the
 14 Chaplin v Hicks basis than the balance of probabilities,
 15 or would you say that was wrong as well?
 16 MR BREALEY: Yes. The prima facie measure of Sainsbury's
 17 loss is the overcharge, just as in a cartel case. The
 18 parties have got together and increased, inflated,
 19 a price. All my three anti-competitive vices now have
 20 come home to roost, and there is a judgment saying there
 21 was an infringement of 101, Sainsbury's has paid an
 22 inflated price. That should never have been charged.
 23 If there was no question of exemption because, for
 24 example, just no one bothered to adduce any evidence,
 25 that would be our measure of loss.

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1 MR JUSTICE BARLING: Well, subject to, you know, other
 2 issues like whether, had that MIF not been charged, as
 3 it shouldn't have been, not a penny of MIF should have
 4 been charged on that scenario, because it was all
 5 unlawful, there was no exemption, then the question is
 6 what would have happened, and if, for example, there
 7 would have been a bilateral somewhere, then that would
 8 affect your measure of loss, wouldn't it?
 9 MR BREALEY: Yes.
 10 MR JUSTICE BARLING: Which is what you said.
 11 MR BREALEY: Absolutely right. So if you conclude that,
 12 under a system of bilaterals, it would have been at
 13 0.2 -- for the sake of argument, our difference is
 14 between 0.2 and 0.9.
 15 MR JUSTICE BARLING: Yes.
 16 MR BREALEY: Now, if MasterCard want to say, "Actually, that
 17 is not the right measure of loss because I recognise it
 18 was an infringement of 101(1), but it was not unlawful",
 19 why is it not unlawful? Well, because it was exempted.
 20 I don't mind whether it is exemptible or exempted,
 21 but -- I think the better analysis is that it was
 22 exempted. In the past, the level would have been
 23 exempted. It would have been exempted at this level.
 24 MR JUSTICE BARLING: At this level. I think Mr Smith, with
 25 great respect, is right in his distinction, isn't he,

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1 because if we can give him an exemption, it can only be
 2 an exemption for what actually happened.
 3 MR BREALEY: Yes.
 4 MR JUSTICE BARLING: We can't give an exemption for some
 5 notional -- not give an actual exemption for some figure
 6 that is different to the MIF. I am thinking aloud.
 7 I know it sounds like a proposition but I am just
 8 thinking aloud. But we clearly can give an exemption,
 9 even in a damages case, I think we can, for something
 10 that has -- you know, for something that is
 11 a restriction. Maybe it is a distinction without
 12 a difference, but if, for example, we didn't give an
 13 exemption for the MIF that was actually charged --
 14 MR BREALEY: Which I don't think you can because no-one has
 15 actually -- well, maybe that is --
 16 MR JUSTICE BARLING: Well, I think they do actually, I think
 17 they do. I think MasterCard said that that was -- but
 18 we can, nevertheless, presumably, either as
 19 a quantification exercise, quantification of damage or
 20 as a -- whichever way you put it, partly the burden of
 21 proof, we can state at what different figure than the
 22 one actually charged it could have been exempted.
 23 MR BREALEY: My big caveat is it would be fundamentally
 24 wrong as a matter of principle to accept Mr Hoskins'
 25 point. And he might be quite happy with this exchange

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1 because he says that exemptible is a loss, and
 2 therefore, the vagaries of the exemption applies just as
 3 equally to us as to him, whereas they don't. We know
 4 that in order to get an exemption, the burden is on the
 5 person who has infringed Article 101, and the burden is
 6 to prove by cogent and convincing evidence, so it would
 7 be extremely unsatisfactory if a claimant seeking
 8 damages because of an unlawful demand was -- somehow,
 9 then, the burden of proof was shifted onto the claimant,
 10 whether the burden or a standard of proof.
 11 MR SMITH: Sorry, I am groping for the answer here, so do
 12 please take it as a grope rather than an attempt to
 13 articulate what the law is, but if Mr Hoskins is saying
 14 there is no breach of statutory duty because, although
 15 Article 101(1) has been breached, the MIF, as it was
 16 charged in the past, was exemptible, ergo no breach of
 17 statutory duty, then I would suggest rather tentatively
 18 it is simply a question of burden of proof on MasterCard
 19 to establish that, because that is what the rules are
 20 under Article 101. But let's suppose that battle is
 21 lost, and, therefore, an infringement of 101 is found,
 22 because the interchange fees, as they were charged, are
 23 not exemptible. What MasterCard then say is it was
 24 exemptible at a certain level, and there is then debate
 25 about what that level is, and both parties have their

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1 submissions on that. Isn't the approach that we have to
 2 take this, that recognising that, in order to achieve
 3 exemption, one has got to meet the four criteria of
 4 101(3), which are stringent, where the burden rests on
 5 the person alleging that the exemption should pertain,
 6 these are all factors that we feed into the question of
 7 assessment of probability, but at the end of the day it
 8 is all a question of probability rather than binary,
 9 one/zero, balance of proof.
 10 MR BREALEY: Personally I am finding it very difficult to
 11 see how you can have a claim -- you are looking at the
 12 probability where you haven't come to a -- if the
 13 Tribunal hasn't come to a conclusion that the MIF is
 14 exemptible at a certain level, so they haven't satisfied
 15 their burden, how that impacts on Sainsbury's' claim.
 16 I mean, Mr Hoskins says you can wield -- we are all in
 17 the realm of damages now, broad axe, everything is up
 18 for grabs, you can almost kind of possibly, it could be
 19 exempted at this, possibly it could be exempted at that,
 20 you are talking about something that is -- they have got
 21 to make something which is unlawful, lawful, because 101
 22 has the two bits, 101(1) and 101(3) and if we succeed on
 23 101(1) there is an illegality. There is a degree of
 24 unlawfulness, and the only way they can show there is no
 25 unlawfulness -- forget about probability of damages --

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1 is to establish that the MIF would have been exempted at
 2 a certain level. That is the only way they can
 3 eradicate the tag of unlawfulness.
 4 MR SMITH: Yes, that is true, but that is what applies to
 5 the MIF as it was actually charged, and yes, if
 6 MasterCard show that there was an exemptible level at
 7 the charged at level, then your claim fails in total.
 8 What we are talking about here is the situation where
 9 you have succeeded on liability, and what we are trying
 10 to establish is what, in the counterfactual world, where
 11 it is accepted that there has been a breach by
 12 MasterCard, what the maximum lawful interchange fee
 13 would have been, so in a hypothetical world --
 14 MR BREALEY: In the hypothetical world, and in my submission
 15 you can only delve into that hypothetical counterfactual
 16 world if MasterCard has, in fact, produced robust
 17 evidence and discharged its burden of proof that at
 18 a certain level the MIF merited an exemption.
 19 MR JUSTICE BARLING: I mean, I suppose it would be odd,
 20 wouldn't it, if they had failed to prove an exemption --
 21 I think it might be helpful to talk about exemption when
 22 we talk about the actual charge, so they haven't --
 23 assume for a moment they haven't established an
 24 exemption for what they have done, and the question then
 25 is what could have been exempted. It would be odd if

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1 they, as it were, had a lesser burden when they have
 2 failed to prove an exemption, and therefore they have,
 3 in fact, acted unlawfully, but they wish to mitigate --
 4 well, it would be odd, I know they say that that is in
 5 fact the case because they say, "We are now, then, in
 6 the realm of you proving your loss", but it is perhaps
 7 slightly counterintuitive that the burden should shift
 8 at that stage.
 9 MR BREALEY: And my answer to that is; my loss is -- you
 10 take 101(1) and that is my loss, and if you want to come
 11 to court, to the Tribunal, and say that it is less than
 12 that, then you jolly well have to prove it.
 13 MR SMITH: Suppose this, it is a purely hypothetical
 14 question, where one has got the as charged for
 15 interchange fee, one obviously has a whole wealth of
 16 data as to how the market is operating, but if one is
 17 dealing with a hypothetical saying, "Well, okay, the
 18 interchange MIF at 0.9", or whatever it was, "Was
 19 unlawful, but actually at 0.5 it was lawful", but
 20 unfortunately we don't have all the wealth of data
 21 because that interchange fee was never charged, does
 22 that mean that when there is an evidential gap like
 23 that, such that, let's say for the sake of argument we
 24 can't, on the balance of probabilities, establish
 25 exemption, that means that there is no deduction from

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1 your damages at all, even though the Tribunal might
 2 think on the probabilities that there is somewhere in
 3 the scale an exemptible interchange fee.
 4 MR BREALEY: Well, again, I come back -- I don't think there
 5 is any concept, or the Tribunal should endorse any
 6 concept of a vague exemptible charge. To use your
 7 phrase, sir, it is a binary -- because otherwise, they
 8 are -- as my Lord says, they can't prove the exemption.
 9 They can't prove an exemption, so -- and they have the
 10 opportunity to come to court with all the data, they
 11 have got their economists, they have got their team, and
 12 all they then say is, "Well, we don't have to prove an
 13 exemption to eradicate the lawfulness", it is all
 14 a question of quantum and a possible exemption, so there
 15 are two possible exemptions, and you can go for that
 16 one.
 17 Come back, if they -- this is about them discharging
 18 a burden of proof to eradicate the unlawfulness, and you
 19 shouldn't be confusing the exemption and the probability
 20 of damage.
 21 The probability of damage must be based on them
 22 satisfying a correct level of MIF. it may well be that,
 23 you know, they were only 1 per cent off. I don't know,
 24 but as we know, no one has come to the Tribunal to
 25 defend the way that it was set. The way that MasterCard

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1 set the MIF was based on competition between two schemes
 2 plus Amex, and a certain element of cost which is
 3 completely and utterly outdated, and Dr Niels has not
 4 come to court to justify the way that the MIF was set.
 5 He has come up with two other methodologies to justify
 6 ex post facto the level, one of which is 0.7 as opposed
 7 to 0.8, and I would submit that that exercise has to be
 8 done on the basis that MasterCard have a burden of proof
 9 by reference to cogent evidence. It can't be laid at
 10 our door to say, "Well, all they have to do is, on the
 11 balance of probabilities save whoever, two or three
 12 exemptible MIFs and then you calculate the damages on
 13 that basis".
 14 MR SMITH: Right. So to absolutely clear, let's suppose we
 15 reach a view that the MIT-MIF that you are contending
 16 for comes within sniffing distance of exemptability, but
 17 we put its chances at 49 per cent of exemptability,
 18 rather than 51, on that basis, at 51, it is exemptible,
 19 at 49 it isn't, and you recover everything without
 20 deduction.
 21 MR BREALEY: I don't believe that the right approach to
 22 exemption is a loss of a chance, you know, a kind of one
 23 in ten. Where I think I could assist is that it is
 24 clearly open to the Tribunal to say exemption is very
 25 difficult, I have listened to a lot of data, it could be

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1 a range, I don't believe the range is huge, but I could
 2 see the range of exemption is this, because there is
 3 some doubt about the figures, and maybe that is, to
 4 a certain extent, where you are coming from, so, you
 5 know, the exemption would be, for the sake of argument,
 6 between 0.5 and 0.7 on their view.
 7 MR JUSTICE BARLING: You should get the lower part of that.
 8 MR BREALEY: Well ... well I think that is a question for
 9 the -- it is still -- well, actually, I think if they
 10 prove -- well, I don't know.
 11 MR JUSTICE BARLING: I am just reminding my colleagues of
 12 the time. But these are deep questions, anyway, and --
 13 MR BREALEY: You are telling me.
 14 MR JUSTICE BARLING: We have the weekend to cogitate over
 15 them.
 16 MR BREALEY: What I will try -- I mean, I will -- I am in
 17 the Tribunal's hands. I mean, we have only got a day,
 18 really, on Monday. I think the Tribunal knows the
 19 MasterCard and the Amex story quite well.
 20 MR JUSTICE BARLING: I wouldn't spend -- you know, we have
 21 got it in there, set out.
 22 MR BREALEY: Maybe it is better, because I have got three
 23 big topics, I have got exemption, pass-on and ex turpi,
 24 and Mr Spitz has got interest and benefits, so we have
 25 quite a lot to do.

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1 MR JUSTICE BARLING: There is a lot to do in one day. We
 2 have taken up a lot of time today, I am conscious of
 3 that, with our questions.
 4 MR BREALEY: The pass-on, and again, maybe the Tribunal
 5 could mull this over the weekend, it is in writing in
 6 some detail. Clearly it is confidential, and I can take
 7 it short by reference to various headings. I don't want
 8 to downplay the pass-on, obviously. It may well be that
 9 I will have to come back on it a little bit, but
 10 certainly on the pass-on thing that is the only area
 11 where there is deep confidentiality, and it may well be
 12 that one has read the pass-on section, then I can get
 13 a steer as to what maybe you need assistance on.
 14 MR JUSTICE BARLING: Take it for granted that we will read
 15 the pass-on section again.
 16 MR BREALEY: It is pretty straightforward.
 17 MR JUSTICE BARLING: Yes. Then you have always got reply.
 18 MR BREALEY: Not long.
 19 MR JUSTICE BARLING: Okay. Do you think there is any need
 20 for us to sit earlier or not on Monday?
 21 MR BREALEY: I probably wouldn't think that is bad idea.
 22 MR JUSTICE BARLING: Are you okay with that?
 23 PROFESSOR BEATH: I am fine with that. Start at nine if you
 24 want.
 25 MR BREALEY: Nine? Half nine? I really don't mind.

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1 MR JUSTICE BARLING: We could do 9.30 but I wonder, there is
 2 a limited -- you know, it comes to a point when everyone
 3 gets very tired if you have too long a sitting day, but
 4 if you think it would be helpful, we are happy to sit
 5 then.
 6 MR BREALEY: 9.30?
 7 MR JUSTICE BARLING: Is that all right? Okay.
 8 (4.09 pm)
 9 (The hearing adjourned to 9.30am on Monday, 14 March 2016)

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