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

Day 22

March 15, 2016
MR HOSKINS: What I would like to do over the next day or so
is really is to build on what I did in the opening, because first and foremost I want to set down a framework for the case.
We did that in the opening and it is the same framework in closing, but hopefully that gives you a framework for the case.

I will develop all of these, but it seems to me these four points, which really are uncontroversial, in

you are interested in and I will try and pre-empt them. I am going to go to restriction of competition -- sorry, actually I need to keep going.

If you go to page 14 of the closings, just to make some comments on the status of the EU proceedings: do they bind the Tribunal; do they not; what weight do they have?

If I can pick that up at page 16, which is our response to the Tribunal’s second question about the relevance of Crehan, and you have seen that Crehan chimes with what we were saying in opening but it is a good, pithy way of encapsulating, and two particular aspects, Lord Bingham at paragraph 11:

"Community law does not go to the length of requiring national courts to accept the factual basis of a decision reached by a Community institution when considering an issue arising between different parties in respect of a different subject matter."

Then Lord Hoffmann at paragraph 69:

"The decision of the Commission is simply evidence properly admissible before the English court which, given the expertise of the Commission, may well be regarded by that court as highly persuasive. As a matter of law, however, it is only part of the evidence which the court will take into account. If, upon an assessment of all the evidence, the judge comes..."
By the conclusion that the view of the Commission was
wrong. I do not see how, consistently with his judicial
oath, he can say that as a matter of deference he
proposes nevertheless to follow the Commission."
You will have your own views. You have heard
a welter of evidence, evidence that the Commission
didn't have the benefit of, evidence which
the Commission didn't have the benefit of
cross-examination on, so you are in a much better
position, to be frank, than anyone who has looked at
this before, because of the nature of the process we
have just finished.

What we say is the Tribunal is not bound by
the Commission decision but it is entitled to have
regard to it. The Tribunal is bound by the legal
principles established by the Court of Justice and by
the General Court insofar as it wasn't overturned by the
Court of Justice. Because Mr Brealey repeatedly took
you to the Commission and the General Court, but quite
often didn't follow through the story with the Court of
Justice. As I will show you when we go to that, the
Court of Justice actually didn't follow the Commission
in the General Court in some really important legal
matters which are fundamental in this case.

That is on the law. Really you have to look
absolutely the whole process. What did the Court of
Justice say? Because that's where you find what the law
is. But on the facts as well, when you are potentially
looking at the Commission decision, what one has to has
to remember is that the general courts and the Court of
Justice were reviewing the legality of a particular
competition decision and effectively it was a judicial
review. That's the nature of what the courts were
doing. Therefore, they had to judge the legality of
the Commission decision on the basis of the facts that
were available, because that's the nature of a judicial
review. It wasn't a trial like this was, it was

a judicial review, and that's important for a number of
reasons, but the most important reason, of course, is
that the Commission was dealing with an intra-EEA MIF
and I think it is pretty much common ground that
a threat to the life of a payment scheme is going to be
much greater, whatever the right answer is, but the
threat is much greater when you are looking at the
necessity of a domestic MIF as compared to an intra-EEA
MIF, just because of the proportions in which they make
up the scheme.

Again, when you are looking at the Commission,
that's something very important to bear in mind. And
you will understand the submission, this Tribunal has
heard and seen a great deal of evidence that is specific
to the UK, which the Commission didn't have. I know
Mr Brealey kept saying it mentions the UK but that's not
the same as the process that we have had in the last 7
weeks, and we submit that you can and should make up
your own mind on the factual basis of what you have
heard, rather than some sort of an inferential approach
as to what the Commission might or might not have heard
or known about the UK. That's clearly not a very
satisfactory basis.

Page 18 of the closings deals with the broad axe and
I do not think there is much dispute about that. I will
come obviously to the issue of exemption against
exemptible level, which you debated with Mr Brealey at
a appropriate time, and how the broad axe fits into
that, but in terms of the principles I understand it is
not pushed back on.

Before I begin on restriction of competition, if you
go back to page 8 of the closings, because that
summarises what our main points are on restriction. So
I will just identify what they are and then I will
develop them orally.

The first point, paragraph 7; as you know, we say
the realistic counterfactual is that if MasterCard's
domestic MIF were assumed to be zero or very low, ie
0.15, we say Visa and Amex would have maintained their
actual rates or would have maintained their rates at
such a high level that large amounts of switching would
have occurred.

On objective necessity, as we will see, we say both
the economic experts accepted that in that
counterfactual MasterCard would have been forced out of
the UK market over time. That's why we say domestic MIF
was objectively necessary.

If you reject that -- sorry, before we do that. To
further develop it, what's happened actually during the
hearing is the Tribunal has suggested two further
counterfactuals. One is that acquirers would take steps
to keep MasterCard afloat for the general good of the
market and for acquirers, and I will deal with that, our
submission is not borne out by the evidence but we will
come to the detail of that; and the second
counterfactual that's been floated is that merchants, if
they sold MasterCard at zero or low, would turn towards
Visa and put pressure on Visa to bring its rates down,
and it must be a logic of the suggestion by the Tribunal
that it would come down to such a level that switching
would not occur, therefore not objectively necessary,
and again I will deal with that in detail when we come
to it.
If you are against us on that, so the objective necessity point then we move to: is there a restriction within the meaning of Article 101(1)? And the test there is you are looking at what competition was in the actual and comparing it to what it would have been in the counterfactual. That wasn’t really touched on by Sainsbury’s at all in their oral closing submissions, but I obviously intend to deal with that in our submissions. Our conclusion is that for either of those reasons objective necessity are not a restriction. That actually determines the case, because there is no restriction, there is no right to damages.

That is the broad framework and now I need to go into the detail of that. I pick this up, it is page 20 of our closing submissions. Quite a lot of this early material was covered in opening so I can take it quickly.

We have the definition of the ancillary restraints principle. There is no dispute about that. We have the test for objective necessity. It is a high test, I accepted that in opening. Would it be impossible for the scheme to operate without a domestic MIF? In its opening submissions Sainsbury’s suggested that this argument, our objective necessity argument, is a 101(3) argument not 101(1), but that’s wrong, with respect, because the argument we are putting forward is not that the scheme would have been smaller or less profitable without the UK MIF, our case is the scheme would not have been able to continue without the MIF.

And that’s absolutely consistent with the case law. Now, whether we establish that or not is a matter for you, but it is not a 101(3) question, it is clearly from the case law a 101(1) question. We now come to page 22, paragraph 64, identifying the relevant counterfactual. Again, this hasn’t been challenged in terms of this level of the legal test. The counterfactual must be realistic. As I pointed out in opening, there is a difference to what the Court of Justice said is you can have different counterfactuals for different purposes and the court itself applied different counterfactuals for objective necessity and for restriction of competition. This is paragraph 64(c) of the closing. Because in relation to ancillary restraint, what the court said is the test -- the counterfactual is not one that would arise in the absence of the MIF, but it can include a counterfactual of a realistic situation that might arise in the absence of the MIF.

What does that mean? Well, one way, we submit, of understanding what that distinction -- because clearly the distinction has been drawn -- what it actually means is that the Tribunal, for ancillary restraint, is not asking what MasterCard would have done absent the MIF, but it is asking what could have been done by the operator of a scheme to allow the MasterCard scheme to continue to operate. I will come onto that. It is another point. It is to allow the MasterCard scheme to continue to operate, not a general four-party scheme, and that’s why it is objective necessity.

The question isn’t the factual one: what would MasterCard have done absent the MIF? The question is: what could MasterCard have done absent the MIF to keep the scheme afloat? That’s why it is objective.

In terms of restriction of competition, again I’m not really sure there’s any dispute between us about what the test is. It is just that Sainsbury’s didn’t really engage with this bit of the analysis. It is the O2 Germany case, so this is paragraph 65 of the closings. The most important point of it, it is paragraph 65(d) of the closings, paragraph 73 of O2, we have set out the short quote. Again, we saw it in opening. What the courts of first instance said in that case is:

“That is necessary to consider what the competition situation would have been in the absence of the agreement.”

So again, you are comparing state of competition in the actual with state of competition in the counterfactual in order to assess whether the MIF is a restriction of competition or not.

Again, when looking at the relevant counterfactual we saw the case law in opening, you have to look in the actual context in which the agreement operates or would not exist in the counterfactual. You have to look at the legal context. You will see it in -- we set it out at 66(b):

“In that regard it is necessary to take into consideration the actual context in which the relevant agreement exists, and in particular the economic and legal context in which the undertakings concerned operated, the nature of the goods or service affected, as well as the real conditions of the functioning and the structure of the market or markets in question.”

Again, you are looking at the real context. That is perfectly clear from the case law. Then, paragraph 167 of MasterCard. This is at the top of page 24:

“The counterfactual must be based on the assumption that the scheme rules which are not challenged, such as the honour all cards rule, would remain unchanged.”
Again, I don’t think there is any dispute between  
the parties that that is the case.  

Then, as I flagged up when I looked at objective  
necessity, the difference when one comes to looking at,  
is there a restriction of competition, is one is looking  
at an appropriate counterfactual for assessing  
restriction of competition, as one that would have been  
likely to arise in the actual market or markets in  
question.

So it is much more a factual enquiry than a more  
objective enquiry that one has for objective necessity.  

Paragraph 68 of the closing, it is really the point  
I have already made, you have to look at the relevant  
economic and legal contexts when you are taking account  
of the counterfactual. But 68(a) is important.  

This is bullets, it doesn’t have quotes round it,  
but it is pretty much a quote from MasterCard, but  
I have taken you to it already:  

"The alleged restriction of competition must be  
considered within its actual context. It is therefore  
necessary to take into account any relevant factor,  
having regard in particular to the nature of the  
services concerned as well as the real conditions of the  
functioning and the structure of the markets in relation  
to the economic or legal context in which the  

coordination occurs, regardless of whether or not such  

a factor concerns the relevant market."

We will come onto that because it is clearly  
an important theme. We say at each turn, even if we are  
looking primarily at a restriction on the acquiring  
market, at each stage of the analysis it is quite clear  
from the case law that you have to take into account  
what’s happening in the issuing market as well. This is  
the first place one sees in it terms of identifying the  
counterfactual, the Court of Justice makes it quite  
clear.

That’s a theme I’m going to be coming back to.  

In Sainsbury’s closing submissions, it made a number  
of legal points about the assessment of the  
counterfactual. If you can go to their closings, so  
that is bundle B1, it is internal page 73 of their  
closings -- sorry, no, that’s the bundle number. Give  
me a second. No, I’m right. Sorry. Internal 73,  
bundle 230.

You see at the bottom of page 73 there’s that  
heading "Objective necessity" not subjective necessity:  
"CJEU emphasised the objective nature of the  
necessity. As the Commission stated in its Costs of  
Cash survey, a restriction of competition may fall  
outside the scope of Article 101 if it can be shown that  
it is objectively necessary for the existence of  
an agreement of that type or that nature."

Then Sainsbury’s say:  
"Thus, the focus is not on the need for one person  
of that type to survive vis-a-vis another person of the  
same type, the focus is on the type generally and  
whether the restriction is necessary for that type of  
operation to function."

This is part of Mr Brealey’s submission that you  
don’t look at what Visa is doing when you look at the  
counterfactual. He says you take it in a vacuum, what  
would a four-party need to work? That is paraphrasing,  
but that’s effectively what he said.

A number of problems with that. It is just not  
right. These are the reasons why.

First of all, he seeks to create a legal principle  
which should be of considerable importance from some  
wording taken from the Commission’s 2015 cost survey  
that wasn’t even directly dealing with that legal  
question. The reference for that -- I don’t want to  
take you to it now because you can look it up -- it is  
E3.10, tab 202, page 4307 at paragraph 52. But if you  
go to that quote, it is just taken completely out of the  
context for which it is now being relied on. It is not  
a discussion of this particular legal point. It is not  
a discussion of the particular point Mr Brealey seeks to  
obtain from it.

In his oral submissions Mr Brealey also referred to  
the Court of Justice in MasterCard on this. If we can  
look briefly at that. It is E1. If you can keep the  
Sainsbury’s closing submissions handy, I need to come  
back to that in a second. E1, tab 19, at page 428. It  
is paragraphs 163 to 166 of the judgment. 163:

"As is apparent from paragraph 108 of the present  
judgment, the same counterfactual hypothesis is not  
necessarily appropriate to conceptually distinct issues.  
Where it is a matter of establishing whether the MIF had  
restrictive effects on competition the question of  
whether without those fees that by the effect of  
prohibiting ex-post pricing and open payment systems  
such as the MasterCard system could remain viable is not  
in itself decisive."

That is what Mr Brealey took you to. But 164:

"By contrast, the Court should to that end assess  
the impact of the setting of the MIF on the parameters  
of competition..."

So you are looking, by definition, at competition at  
the relationship with competitor, not in a vacuum:  
"... such as the price, the quantity and quality of  
the goods and services. Accordingly, it is necessary,
in accordance with the settled case law, to assess the
competition in question [so a relative relationship]
within the actual context in which it would occur in the
absence of those fees."

Then 165 is a recitation of the standard case law,
looking at actual context, economic legal effects etc.
That judgment doesn't support the proposition
Mr Brealey seeks to get from it, that you look at the
viability of a scheme in a vacuum. Quite the contrary.
It confirms application of the existing case law has to
be realistic, has to take account of actual context, has
to take account of competition. So has to take account
of what Visa is doing.

Then, back to the Sainsbury's closings, please.
That's internal 74, paragraph 186. There is a reference -- a reliance on -- this is looking at their
point which is: if one is looking at the legality of
what MasterCard is doing one, should assume that Visa, because it is similar, is also acting unlawfully.
Again, probably put a bit crudely but you recognise the
point.
Two points are made. First of all they rely on the
OFT decision. Well, the brief point there is that OFT
decision was effectively withdrawn by the OFT because
they couldn't support it, and was put to death by the
CAT, it was quashed. So one doesn’t really get much out
of that. Then, in relation to British Airways, it simply doesn’t support the proposition for which it is put. They have set out the paragraph they rely on at
187 of their closings:
"Where, as in this case, the Commission is faced
with the situation where numerous factors give rise to
a suspicion of anti-competitive conduct on the part of
several large undertakings in the same economic sector,
the Commission is even entitled to concentrate its
efforts on one of the undertakings concerned ...
"Concentrate its efforts, ie investigate, one of the undertakings concerned:
"... while inviting the economic operators which
have allegedly suffered damage as a result of the
positively anti-competitive conduct of the other
undertakings to bring the matter before the national
authorities."

This has nothing to do with the proposition
Mr Brealey is putting, which is you must assume Visa is acting unlawfully in order to consider whether
MasterCard was acting unlawfully. What it is actually
dealing with is the Commission’s discretion to pursue
investigations against some undertakings but not others
involved in the same conduct.

It says nothing about the appropriate counterfactual
to be adopted in this case. Mr Brealey sought to seize
on the word "suspected" or "suspicious" in that
paragraph to say there is a legal principle that if
an undertaking is suspected of operating unlawfully,
then one can and should assume it is operating
unlawfully for the purposes of the counterfactual.
Nothing to that effect in the paragraph. But,
equally, the presumption of innocence applies just as
much, if not more strongly, in other areas of EU
competition law, and that’s simply not an appropriate
basis to act but certainly no support for it in case law.

I'm moving on to page 25 of our closings. We can put away the Sainsbury's closings for the moment. Let me start with the parties' proposed counterfactuals.
I will come on to the ones that the Tribunal has floated
after I have dealt with these ones, if that's okay.
As you know, Mr von Hinten-Reed's analysis in his written opinion -- he tried to shift a bit orally, but
in his written opinions -- was based on the assumption
that if the MasterCard MIF had been low or zero, then
the Visa MIF would have been low or zero. But that wasn't really based on any factual analysis, it was
an assumption on his part. That's the way it was put in
his report.
As you know, Dr Niels thinks that if MasterCard's
domestic UK MIF had been low or zero Visa would have
remained high, and indeed he thinks the same of Annex
Let me deal first of all with Mr von Hinten-Reed's
suggested counterfactual and why we say it is simply not
realistic, which is what the case law requires.
First of all -- this is at page 26 of our
closings -- as a matter of regulatory control, Visa did
not have any regulatory obligations imposed upon it in
respect of the level of its domestic UK MIF at any stage
during the period of the claim. We have set out what
constraints were imposed on Visa, but none of them
concerned a UK domestic MIF. So no formal regulatory action taken against them.
The second question is regulatory incentive, if one
likes, the threat of regulatory action during the
period. But as a matter of regulatory incentive, at no
stage during the period of the claim did Visa or
MasterCard feel obliged, by virtue of a regulatory
decision taken against the other competitor, to
immediately follow suit. We have given the two examples
at 73(a) and (b). When the Commission adopted its 2002
Visa decision, which exempted Visa's consumer intra-EEA
MIF -- so Visa's EEA MIF was effectively coming down
from what it had been -- MasterCard didn’t drop its own intra-EEA MIF so as to bring it into line with the new Visa MIF, it maintained its position, and that led to the Commission decision and all the court proceedings. So far from feeling constrained by regulatory threat, MasterCard carried on doing what it was doing. Equally, in 2009 we had the adoption of the Commission’s 19th December 2007 decision relating to MasterCard’s intra-EEA MIF, which brought the level down even further. So MasterCard was then below Visa, and Visa didn’t immediately drop its debit or credit intra-EEA MIFs. Indeed, it didn’t drop its credit card MIF until it gave commitments to the Commission in 2013. And the Commission decision originally was 2007. So the idea that regulatory threat would have meant something happening in the short-term simply isn’t borne out by the facts of this case.

MR SMITH: Mr Hoskins, in the UK, the only proceeding was the OFT’s quashed proceeding against MasterCard, there was no parallel proceeding against Visa by the OFT?

MR HOSKINS: Nothing that led to a formal decision.

MR JUSTICE BARLING: When did they introduce the new debit card, the new MasterCard, roughly? About the same time?

MR HOSKINS: It kept 3% of the market that way. MR SMITH: Until the regulation came into effect, did it stay at 8p?

MR HOSKINS: It wasn’t. But, as we saw, MasterCard retained its own MIF at a time when MasterCard was substantially lower and at a time that MasterCard was disappearing from the market.

The third question is: what about commercial choice? What would Visa, in this countercultural -- MasterCard is at low or zero -- what would Visa have done as a matter of commercial choice? Here Maestro is important. Page 28 of the closings. We have got an annex which sets out the Maestro story in more detail but just for this purpose, what you see is prior to 1st January 2007 there was a differential between Maestro and Visa Debit, 6.6 basis points. 2004/2005, HBOS move from Switch, the predecessor to Maestro, to Visa Debit. Around July 2006 Visa announced that it was going to put its interchange fee up from 6.5p per transaction to 8p per transaction. As we know from the evidence, Maestro didn’t respond because MasterCard didn’t set the rate and the body that did, including issuers and acquirers, couldn’t agree to raise the Maestro MIF. What that did was it increased the differential between Maestro and Visa Debit to 9.2 basis points. Now, what that shows is that in a situation in which MasterCard’s interchange fees were materially lower than Visa’s, far from reducing its fees, Visa put its foot on the pedal and raised its interchange fees, because they wanted issuers to migrate to Visa.

Then, of course, we know what happened subsequently is HSBC and RBS subsequently decided to switch. At page 29 of the closing you will see the way the market share went. We have seen that before. But what we know is that what Visa actually did was it retained its higher MIF whilst Maestro’s market share collapsed. It didn’t drop the rate -- for whatever reason; out of commercial choice, out of pressure from acquirers or out of pressure from merchants -- it kept its foot on the pedal and watched Maestro exit the market, and nobody stopped it doing it, not a regulator, not acquirers, not merchants.

That shows that when faced with a competing card with materially lower MIFs, Visa did not choose to lower its own credit card MIF, it chose to raise it. It is important -- I know there is a dispute on Maestro about what’s the precise reason why HSBC and RBS switched, to what extent was it the differential in the MIFs, and to what extent was it reduced functionality on the part of Maestro; but, important for this part of the story, that doesn’t matter, the question of why they switched. What matters for the purposes of this part of the story is that Visa maintained and then raised its own MIF at a time when MasterCard was substantially lower and at a time that MasterCard was disappearing from the market.

MR JUSTICE BARLING: Was it substantially lower for MasterCard’s new debit card?

MR HOSKINS: It wasn’t. But, as we saw, MasterCard retained 3% of the market.

MR SMITH: MasterCard’s rate for its debit MasterCard was the same, at 8p.

MR HOSKINS: Yes, as I just said.

MR SMITH: I am with you.

MR HOSKINS: It kept 3% of the market that way.

MR SMITH: Until the regulation came into effect, did it stay at 8p?

MR HOSKINS: I would need to check that, sir.

We would need to check that, sir, I don’t know the answer off the top of my head. But in a sense what’s most important for this present purpose is the period from just before 2004/05 when HBOS switches, so the early 2000s, we have a differential of 6.6 basis points. You can take it up until the point when HSBC and RBS switch if you like, you have got that period, and what you see is again Visa putting its foot to the floor, not the opposite.
MR HOSKINS: Another point that was made by Sainsbury's --

MR JUSTICE BARLING: June, thank you.

common ground, Amex maintained that differential. That

charged in respect of MasterCard and Visa. Again,

evidence relating to the claim period.

have retained a material difference. Either will do.

Let me break it into periods. First of all, the

evidence relating to the claim period.

During the period from 2006 to 2009, Amex's merchant

discount rate was significantly higher than the MSCs

charged in respect of MasterCard and Visa. Again,

common ground, Amex maintained that differential. That

was despite the fact it had lower acceptance etc. That

is just Amex's business model. That's what it does.

You will hopefully remember this because we saw it in

cross-examination. If we can go to B, tab 11. This is

some of the information provided in response to the

Tribunal's questions. That was at page 152 of the

bundle.

Hopefully you will recognise that table because

I took Mr von Hinten-Reed to it in cross-examination.

What this shows is that whilst during the period 06/09

Amex had a materially higher merchant discount rate than

Visa and MasterCard's MIFs, three-party schemes, which

of course in the UK is primarily Amex, increased its

market share from 8% to 14%. So they almost doubled

their market share in that three-year period.

Again, what does that tell us? Far from seeking to

lower its merchant discount rates to levels similar to

the MIFs offered by MasterCard and Visa, Amex chose to

maintain a high differential in order to grow its market

share.

And nobody stopped it. It wasn't subject to

competition regulation. It didn't deal with acquirers,

save in relation to 3.5. And merchants weren't saying,

"Hang on, you have got a large differential so we are

not going to deal with you or we are going to stop

accepting you". The facts are what they are; the market

share went up despite the large differential.

You will remember from the evidence, this is

paragraph 94 of our closings, that MasterCard was only

able to stem the flow of market share to Amex by

offering higher MIFs on its MasterCard World card, some
time around 2009 and 2010, and that not only arrested
the rise in Amex market share at the expense of the
three-party schemes, it actually clawed some of it back.
We set out that evidence at paragraph 94.

What we say is the evidence relating to the claim
period therefore confirms that Amex was able to, and
did, maintain a material differential with MasterCard's
MIF in order to grow its business, same as Visa. It is
the same business, it is the same commercial imperative.
And nobody was apparently able to stop it. Whether
people tried, we don't have the evidence, but what we
know is it didn't work, because we see the dramatic rise
in market share.

Let's move into the evidence relating to the
regulation. This is paragraph 96 of the closings, and
what Sainsbury's has brought up in the course of the
trial is its negotiations with Amex in 2014 and 2015.
As we know, it related in a certain -- it is
confidential so I will try and tread carefully --

merchant discount rate at a certain level, but you will
note there was still a substantial differential between
the rate negotiated and the rate of 0.3 allowed for by
the regulation. It didn't bring it down actually
anywhere near close to what Visa and MasterCard are now
constrained to apply.

Let's look a bit closer at these negotiations.

First of all, because what we are looking for of course
is a counterfactual that applied during the claim period
which is before the regulation, what Sainsbury's say is,
"Look, we had these negotiations in 2014 and 2015, this
is evidence of what would have happened in the
counterfactual in the claim period". One of the points
we make is no, no, no, no; this is looking at what is
happening when the regulation is on the stocks and about
to come into force, therefore it is not relevant when
you are trying to identify a counterfactual for the
actual claim period. So it is a bit convoluted but
that's why we end up in this place.

But the negotiations with Amex, 2015, take place
against the backdrop of the impending adoption and
implementation of the interchange fee regulation. If we
can look at the regulation, it is at E1, tab 21.
You have seen this in opening. If you go to
page 450 you will see Article 1 is "General provisions".
Then over the page, Article 1(5):

"When a three-party payment card scheme licences other payment service providers for their issuance of card-based payment instruments or the acquiring of card-based payment transactions or both, or issues card-based payment instruments with a co-branding partner through an agent, it is considered to be a four-party payment card scheme."

That is Amex’s GNS, 3.5. So for the purposes of the regulation it is considered to be a four-party payment card scheme.

But Amex get a little time off, potentially:

"However, until 9 December 2018 in relation to domestic payment transactions, such a three-party card scheme may be exempted from the obligations under chapter 2 provided that the card-based payment transactions made in a member state under such a three-party payment card scheme do not exceed on a yearly basis 3% of the value of all card-based payment transactions made in that member state."

Of course, that’s a disincentive to grow market share for three years. Because if you grow your market share and it did. At this time, when the negotiations are taking place, it actually has a disincentive, a regulatory, legislative disincentive, not to increase its market share.

You will see that Dr Niels was asked about this. It is at the top of page 33 of our closings. He explained the effect of these changes when cross-examined. If I could just ask you to read that quote to yourselves. Paragraph 100. (Pause).

You don’t need an expert economist to tell you that. It is clearly right. That’s one reason why looking at what happened in 2015 does not tell you what the realistic counterfactual would have been in the period of the claim when the regulation was just a bright light in someone’s eye for most of the period. It is just not part of the actual counterfactual. The second point is, even if one thought it were relevant to look at these negotiations for a counterfactual in the period of the claim, look at the result. MasterCard and Visa now 0.3, and you see what the negotiated rate was.

I’m now at the bottom of page 33 of our closing submissions. It is the evidence relating to Australia, because you will remember that in his written reports Mr von Hinten-Reed relied heavily, and indeed in his cross-examination kept going to Australia. That was his lifeboat whenever the going got tough.

But the truth is Australia was driven by aggressive surcharging by Australian merchants. And the evidence we had from Sainsbury’s own witnesses was that surcharging was neither desirable nor feasible for UK retailers. We have set out the evidence in detail at paragraph 103.

I’m not going to read it all out. There you have it. Surcharges just isn’t on the table in the UK.

The second point about Australia -- this is page 36, paragraph 105 of the closings -- is that under the Australian regulation, the caps imposed on MasterCard and Visa were weighted average caps. What that meant is that MasterCard and Visa were free to set higher interchange fees for premium cards to compete directly with Amex. And they did so. We have seen that competing with a four-party scheme.

So in this UK scenario MasterCard would not be able to set competitive premium interchange rates, and that’s why Australia doesn’t help you, because in the UK you have MasterCard down here, you have Amex here, switching. Mr von Hinten-Reed’s world of Australia, you have MasterCard and Visa here, Amex here, less switching. But it doesn’t help you, Australia. I don’t like taking the point that so-and-so didn’t put something in cross-examination to someone, and you get ridiculous ones where people say, “You didn’t put this document”, or this line, but Australia wasn’t put at all to Dr Niels as an appropriate counterfactual. It literally did die a death during Mr von Hinten-Reed’s cross-examination.

Page 37 of the closings. Sainsbury’s argued that if MasterCard were zero or low, Visa would definitely have come down to the same level because of the threat of damages, because they know that if they didn’t come
down, they would have had to have handed over all the money in any event in damages. Again, that was killed in cross-examination because it is based on the unrealistic assumption that every person who was entitled to bring a claim would successfully do so against Visa.

Again, we have set out the cross-examination on that point at 109. It was accepted by Mr von Hinten-Reed. But, equally, again let’s stay in the real world. During the period of the claim, neither MasterCard nor Visa reduced their UK MIF to 0.15 or anything approaching it because they were worried about the risk of damages. MasterCard fought its corner in Europe. Visa stood its ground as well. It was only when the regulation came in that you saw those drops in the UK. So that threat of damages is simply not part of the realistic counterfactual. The final point on this Sainsbury’s proposed counterfactual is, of course, they have got the point: well, unless you assume that Visa are acting unlawfully as well, and therefore treat them as coming down to low or zero, you can’t prove that MasterCard are acting unlawfully. The artificiality of that is plain on its face, and I think I have dealt with that already; Mr Brealey’s reliance on the OFT, his reliance on British Airways etc. It simply doesn’t tally with the intellectual case law, which is: look at competition, look at the actual context, look at something that’s realistic. You simply cannot adopt the sort of artificial construct which requires you to assume that Visa are acting unlawfully. It is completely inconsistent with the case law.

That is why we say the realistic counterfactual has to be, if MasterCard is low or zero, Visa maintains, Amex maintains. It doesn’t have to be exactly the same level but at or around the same level. That’s what we say is quite clear from the evidence. So let’s take that counterfactual. We are low, everyone else high, what happens? That’s ancillary restraint. This is page 40 of the closings. I could take this quickly because it is really familiar to you now.

118, it is common ground between the parties that the level of the UK MIF is a very important driver of competition. We set out the evidence; it is Mr von Hinten-Reed’s own first report that that comes from. Second point, top of page 41, it is also common ground between the economic experts that in a counterfactual in which MasterCard’s domestic UK MIF was low but Visa and Amex’s remained at their actual level for any sustained period, MasterCard would have been driven out of the market, the UK market. Mr von Hinten-Reed accepted that expressly in cross-examination. So you look at 121, we set out what the actual differentials were during the period. Then you remember, hopefully, I took Mr von Hinten-Reed, you remember I took him to part of our skeleton. It is A, tab 2, at page 211(e).

Remember, I wanted to show him what the differential would be in the counterfactual of us low, Visa and Amex the same. Then I put it to him that if that was the position, MasterCard would be driven out of the market, and he said he accepted that was yes, as long as that applied over the period of the claim. We have set out the extract. Bottom of page 41 onto page 42. But that’s absolutely fundamental. I invite you just quickly to read that extract at 42.

MR JUSTICE BARLING: Which page are we reading? We are reading the bit on --

MR HOSKINS: It is the cross-examination.

MR JUSTICE BARLING: Right.

MR HOSKINS: Yes. (Pause).

Dr Niels agreed. So you have got agreement by the experts on what would happen in the counterfactual I have identified as the realistic one. There is another practical importance, of course, as --
Mr Hoskins: Sir, as you accepted, but more expert than you.

We will look at the factual evidence. My point is a simple one. I’m sorry if it is going to be too blunt, it is probably too blunt already. If you want to say there is an alternative counterfactual other than the one that has been considered by the parties, it has to be based on the evidence, and that’s the process I’m going through to show you what the evidence is. You are not surprised, the punchline is going to be I don’t think either of your two counterfactuals are actually supported by the –

Mr Justice Barling: You are assuming we have got two counterfactuals.

Mr Hoskins: They are potential ones. I am not going to stick my head in the sand. You put a certain form of questioning, and you are going to ask me the same questions again. You have a completely open mind and that’s why I’m here to persuade you one way or the other, but you have floated two possibilities and I want to address them.

My point is any counterfactual has to be based on the evidence, has to be supported by the evidence, and I doubt that’s going to be controversial between us.

I’m also reminded, in terms of this particular point about what would have happened in the differential of us here and everyone else there, of course all our factual witnesses say we would have been driven out of the market. So it is not just the economists.

Mr Justice Barling: If it had remained like that?

Mr Hoskins: If it had remained, correct. That’s what the experts say but, again, as a sort of adjunct to what you have just put to me, it is also confirmed, if you think about the sorts of sums that were involved in this counterfactual play. It is paragraph 125 of the closings. We give you an example.

Taking 2011 as a mid-point during the claim period, total UK purchases on UK MasterCard credit charge cards amounted to in excess of £82 billion. Even based on the level of exemptible UK MIF proposed by Mr von Hinten-Reed, this means UK banks issuing MasterCard would have together received over £500 million per annum of additional revenue from moving their business to Visa and over £800 million per annum from moving to Amex.

If you want some facts -- would they really have done it? Yes, they would, because it is worth, to the industry, 500 million. Which is pretty compelling. It is not peanuts.

Closings 126. It is the Australia point.

Mr von Hinten-Reed accepted that Australia doesn’t help
us on this because in Australia Visa and MasterCard were 1
subject to regulation at the same time, so you don’t 2
have the disparity that we are considering. 3

Fourth point. In his second report, 4
Mr von Hinten-Reed considered what would happen if the 5
only way that an acquirer could obtain payment from 6
an issuer was by means of a bilateral agreement. This 7
was his: no payment moves to the acquirer absent 8
a bilateral agreement. And that’s the hold-up problem. 9
His evidence is the scheme collapses. So that doesn’t 10
work either.

So a system, “no payment to acquirer unless 11
bilateral” doesn’t work because of the hold-up problem, 12
it collapses. Because the issuers hold out the charge 13
too much.

PROFESSOR JOHN BEATH: Sorry, could I just ask you to say 14
a bit more about that? Because it seems to me that if 15
you are thinking about bilateral agreements, it matters 16
whether these are agreed ex-ante or ex-post. The 17
hold-up problem arises in an ex-post situation but if 18
you have a set of bilateral agreements that are 19
enshrined in contract, there can’t surely be a hold-up 20
because there is a right, through contract law, to 21
ensure that the amounts that have been agreed ex-ante to 22
be handed over are in fact handed over.

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1 MR HOSKINS: I was about to come to it, absolutely. In that 1
situation -- because if you take out the scheme, the 2
current scheme is you can have bilaterals, but if no 3
bilateral the MIF applies. That’s the current 4
situation. Absent that, you would have a system that 5
didn’t actually provide any rules for interchange. We 6
talked about the blue pencil. If you just take those 7
two out, what are you left with is you are left with 8
a system, a very uncertain system of people -- you would 9
either have to say there was either some sort of implied 10
contract, which might well be difficult because you 11
would be asking yourselves exactly the same question 12
because to get an implied term in a contract is it 13
necessary for the contract to operate? Very similar to 14
a ancillary restraint-type issue.

The only way I can think, but I think it might work 15
the other way, is a quantum valebat-type situation,
where you would be trying to evaluate what value of 16
services the issuer provided. But that would be odd,
because in this case you would presume it would be 17
issuer actually holding money back and saying “I’m 18
entitled to hold this” or “I’m holding this", whereas 19

a quantum valebat, made by the acquirer, the acquirer 20
would be saying, “You have charged me too much”, and you 21
would have to plead some sort of implied term of 22
contract in breach of it.

But the short point is, imagine a scheme which is 23
set up without any rules on how much an acquirer is to 24
pay an issuer, the point is nobody would join that 25
system, because of the legal uncertainty. Because there 26
is no clean legal answer in contract or restitution 27
absent a scheme rule.

The only way I can think, but I think it might work 28
the other way, is a quantum valebat-type situation,
where you would be trying to evaluate what value of 29
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because in this case you would presume it would be 30
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is no clean legal answer in contract or restitution 40
absent a scheme rule.

The only way I can think, but I think it might work 41
the other way, is a quantum valebat-type situation,
where you would be trying to evaluate what value of 42
services the issuer provided. But that would be odd,
because in this case you would presume it would be 43
issuer actually holding money back and saying “I’m 44
entitled to hold this” or “I’m holding this", whereas
service fee, as applicable. The corporation has the right to establish default interchange fees and default service fees ... it being understood that all such fees set by the corporation apply only if there's no applicable bilateral interchange fee or service fee agreement between two customers in place. The corporation establishes all fees for interregional transactions and intraregional transactions ...’

The rest is not relevant. So you will have to apply a blue pencil to remove the default fees and only contain reference to bilateral fees.

What this seems to be saying, but do correct me if I'm wrong, is that a transaction settled between customers only gives rise to the payment of the appropriate fee if (a) it is a default fee or (b) it is bilaterally agreed.

If you strike a line through the default and say it doesn't exist, isn't there simply a right to deduct only where there is a bilaterally agreed fee, and otherwise, when there is a transaction entered into with a merchant, communicated into the system, and the system settles, the settlement is at 100% with no discount? I'm wrong, is that a transaction settled between two customers in place.

The blue pencil test is a very mechanical one. That is the effect of it, is default applies if absence of bilateral agreement, issuer gets no payment. We are assuming that in this situation, absent paragraph 135 of the closings.

The blue pencil point, because you can still put the point to me in an ancillary restraints/objective necessity scenario, one isn't hidebound by having to blue pencil to say is it objectively necessary or not? You can still put the point to me, which is: what is the position -- I think the way you put it during the questioning, so if it has moved on apologies if I have got it wrong, but the position is: no payment absent bilateral. Which means that if the issuer wants money it has to enter into a bilateral, and if it doesn’t, it won’t get any money. So it is the flip side of the Mr von Hinten-Reed collapsing scenario.

MR SMITH: That net figure moves to the acquiring bank, who also retains the difference between the interchange fee and the merchant service charge, and the net/net figure is passed down to the merchant.

MR SMITH: That net figure moves to the acquiring bank, who also retains the difference between the interchange fee and the merchant service charge, and the net/net figure is passed down to the merchant.

MR SMITH: That net figure moves to the acquiring bank, who also retains the difference between the interchange fee and the merchant service charge, and the net/net figure is passed down to the merchant.

MR SMITH: So he doesn’t get 100%, he gets whatever it is, 97.5 or more. So blue pencil is showing my Common Law contractual traditions too much; what we are talking about is a form of rules here which somehow, without doing too much violence to the provisions of 8.3, is removing the default but allowing the bilateral to remain, without saying what the bilateral is.

MR SMITH: In that situation, assuming no bilateral, we have the right to establish interchange fees and default service fees. It begins that all fees set by the corporation apply. So put a line through all of that and you are left with only if there is no applicable bilateral interchange fee or service fee agreement between two customers in place.

The blue pencil test is a very mechanical one. That is the effect of it, is default applies if absence of bilateral agreement, issuer gets no payment. We are assuming that in this situation, absent paragraph 135 of the closings.

I see the basis for self-help here, that the issuing bank could say: well, my services are worth 5%. I'm not sure I see the basis for self-help here, that the issuing bank could say: well, my services are worth 5%.

MR SMITH: I do apologise.

MR SMITH: That’s helpful, because we are in the same place. We are assuming that in this situation, absent bilateral agreement, issuer gets no payment.

MR SMITH: That’s helpful, because we are in the same place. We are assuming that in this situation, absent bilateral agreement, issuer gets no payment.

MR SMITH: That’s the point. Remember, we are looking at an counterfactual that applies in a situation where MasterCard would have this rule, Visa and Amex would still have a MIF and would still be setting it high; subject to the point I’m going to come onto about what commercial pressure would do, but let’s take this in stages.

MR SMITH: Indeed, but before we move on to that it would be very helpful to know if this construction of 8.3 is
MR SMITH: What I'm really putting to you is, which is... MR HOSKINS: Yes. MR SMITH: It is a different analysis. MR HOSKINS: That's my point. MR JUSTICE BARLING: Surely we are not doing a blue pencil test. MR HOSKINS: That is my submission, which is the blue pencil test. MR SMITH: There may be a distinction without a difference here. What I'm trying to work out is, on our counterfactual, where the MIF is excluded, eliminated, and the need then to posit in the counterfactual the rule against an ex-post facto negotiating or is that in fact -- MR HOSKINS: It is a different analysis. MR SMITH: It is a different analysis. MR HOSKINS: Yes. MR SMITH: What I'm really putting to you is, which is right? In other words, is it the case -- and it is really just a question of law -- that on the true understanding of the rules, if you take away the default, there's no entitlement to deduct or, conversely, if you take away the default, it is a free-for-all? MR HOSKINS: Sorry, you are asking me to look at the particular rules as they are and imagine that one blue pencil the whole of that wording. MR SMITH: The Chairman is right that we should lose the phrase "blue pencil". MR HOSKINS: That's why I said: are we discussing -- sorry to ask again, but it will help me answer the question. Are we discussing a potential scheme in which the rules are the issuer cannot deduct unless there is a bilateral? That's what I understood to be the issue. That's what I was prepared to address. One gets there simply because in the context of objective necessity one is asking: is there another way in which the scheme could operate, which wouldn't make it impossible for it to operate, other than the MIF? MR SMITH: When one is discussing the counterfactual, the counterfactual is what would happen if this default is removed. And one ought -- but again do correct me if I'm wrong -- to do the least possible violence to the rest of the scheme rules in order to understand how this would work in the counterfactual. MR HOSKINS: Indeed, they are supposed to remain in place, according to the case law, so that's why the honour all... cards rule is assumed to be valid. Yes, absolutely. MR SMITH: Indeed. What I'm asking is, taking away this default but keeping everything else, what is the position for us to feed into the counterfactual? Is it, on the one hand, no deduction? Or is it, on the other hand, a free-for-all -- MR HOSKINS: It's a matter of statutory construction where they are in there, it will just be a free-for-all, which would clearly have problems because nobody -- that scheme would not be viable. Let me take that. A free-for-all would not be viable, because nobody would sign up to that scheme if you were left with, for example, quantum valebat-type issues. That is unworkable. MR SMITH: Indeed, because one can see that both cardholders and merchants, to say nothing of the banks in between, but simply the cardholders and merchants would say the scheme is not fit for the purpose. The whole point is that this is a convenient way of paying the merchant. MR HOSKINS: Yes. Then flip side, as a contractual question really, is, if those words weren't there, would the members be entitled to enter into bilateral agreements? Would the scheme allow that? If it didn't expressly allow it, if that makes sense. I don't know. It is a really difficult question.

You would have to go through the scheme rules and look for objective pointers as a matter of contractual construction of whether that was allowed or not. But it is a really detailed exercise of contractual construction to get to the answer, and I have not done it. MR SMITH: Okay, well thank you.

MR HOSKINS: You would probably have to fall into, certainly, implied terms. It would be first of all a question of whether as a matter of statutory construction was this excluded by the rest of the contractual rules; and if it weren't expressly excluded, you would then be looking to see, is it necessary to put something in place to allow the contract to operate? Then that probably takes us back into the question of competition law, which is: what is it that's necessary? Is it sufficient, for example, to have a rule, issuer doesn't receive absent bilateral, or do you indeed need some sub-default such as a MIF? I think, through that contractual analysis, it brings us back to that question, just because of the similarity between the test of implying a term into a contract and indeed the competition law here, which is something which is necessary to allow the contract to operate, because that's actually, fortuitously, the same.
question, although for a different purpose in each case.

MR SMITH: You see why we are asking the question? It is not in theory what one could have as a scheme, because I entirely accept that one could have either a scheme that was zero deduction or a scheme that was the issuing bank deducts what it thinks its services are worth. Either, no doubt, is possible, although one might have views as to its viability. But because one needs to import into the counterfactual as much of the real world as remains when one has taken away the provision that is said to be restrictive of competition, it does seem to matter what, as a matter of construction, the answer is, as opposed to how one might build the scheme apart from that.

MR HOSKINS: The way I have approached it, this may be a practical way rather than a sort of perfect way, is what one knows is the scheme operates with the MIF because that’s the way it has operated for years. What’s then been done is a number of different counterfactuals have been proposed: could the scheme operate with this or could it operate with this, could it operate with this? And the way -- again to put it crudely -- we have approached this is to say no, it can’t operate with that or that or that, and then by a process of elimination, so therefore it must need the

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MIF. Whereas yours is a different approach, and it is a more perfectionist approach, which is to say: absent this, what would be the proper contractual construction? 

MR SMITH: Then, what would be the consequences given that construction? Exactly. What I’m in a sense putting to you is, how much of the “real world” can we import into our counterfactual world to make, as it were, the hypothetical exercise that we are undertaking as narrow and as tightly framed as possible?

MR HOSKINS: I think it’s difficult, because when one is asking what would happen absent the MIF, one has to almost -- as everyone has done it -- well, could you put this in its place? And a number of different possibilities have come up and then one has to look at each of them. Because it is quite difficult just theoretically, philosophically, to come up with an approach which wouldn’t require you to say: what about this, what about that? Because otherwise you are just in a bit of a vacuum.

MR SMITH: That’s what I’m trying to avoid.

MR HOSKINS: I will be honest, I haven’t attempted that sort of contractual broad sweep. What I have done -- maybe this is my sort of defendant outlook, if you like -- is it works with a MIF, these are the other things that
MR SMITH: One point one might say of the no deduction rule.

MR HOSKINS: Yes.

MR JUSTICE BARLING: I think we'd better give the transcript.

MR HOSKINS: Substantial migration is the basis of both.

MR SMITH: But the broad factual argument you're making is.

MR HOSKINS: Yes.

MR SMITH: Let's suppose I'm an issuing bank who signed up

MR HOSKINS: Certainly in the evidence in the Commission.

MR SMITH: That, I think, was something the OFT discussed in

MR SMITH: Before you move on, just as

MR SMITH: An adjunct to the debate we had before the break, you

MR SMITH: Will recall the discussion that the Tribunal had

MR SMITH: Yesterday with Mr Brealey about the nature of the

MR SMITH: Restriction of competition arising and whether the

MR SMITH: Words, what was pernicious was not so much how high the

MR SMITH: MIF was, but the fact that there was a MIF at all at any

MR HOSKINS: Yes.

MR SMITH: One point one might say of the no deduction rule

MR HOSKINS: There may be a difference, because for

MR SMITH: It is premised on us exiting the market.

MR SMITH: For restriction of

MR SMITH: Competition, I might need less to establish not

MR SMITH: A restriction of competition. Because if, for example,

MR SMITH: In the restriction you reject the argument objective

MR SMITH: Because you say MasterCard would not have

MR SMITH: Been forced out of the market but it would have

MR SMITH: Remained, albeit at a very low level, say 3%, that could

MR SMITH: Still lead to a conclusion: no restriction of

MR SMITH: Competition. Because instead of having a situation of

MR SMITH: Competition with vibrant MasterCard, vibrant Amex,

MR SMITH: Vibrant Visa, you have MasterCard limping there, you can

MR SMITH: Immediately see where I would go with that submission.

MR SMITH: So there is that distinction. Objective necessity

MR SMITH: Is more black and white.

MR SMITH: More black and white, yes. So there is more
MR HOSKINS: Yes. In terms of my approach, if one takes
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MR JUSTICE BARLING: It might be argued that although
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I think you are probably right to say that the rule that
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says you can’t deduct, you have to pass-on 100% if you
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don’t agree, has the same effect as a zero MIF. It
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probably isn’t a zero MIF --
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MR HOSKINS: It is sometimes called at par clearing.
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MR JUSTICE BARLING: Yes. It is difficult to see how that’s
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a restriction to competition.
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MR HOSKINS: It means the issuers can’t charge.
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MR JUSTICE BARLING: Unless they are in agreement.
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MR HOSKINS: They’ll all start by charging zero, absent
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bilateral agreements. That’s why it has the same effect as
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a zero --
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MR SMITH: Yes, but the focus is on the payment system.
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What it is saying is that the cardholder’s payment of
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£25 will reach, unimpaired, the merchant, he will
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receive £25, unless there is an agreement to which
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everyone in the chain consents, so the deduction can be
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made. Because we have been focusing on the scheme rules
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but, of course, there are also going to be contracts
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between the cardholder and the issuing bank, and the
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merchant and the acquiring bank, and again one would
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register a degree of surprise if there wasn’t a rule
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along the lines of the money moves to the payee absent
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an agreed deduction.
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MR HOSKINS: Yes, but I mean the crucial thing is what’s the
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contract or what are the rules that apply between the
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issuing and the acquiring banks. Yes, I understand of
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course there would be provisions in that chain, but
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what’s in the middle is what we are discussing.
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MR SMITH: Indeed, but the middle will be drafted with
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a view to what the ends expect.
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MR HOSKINS: Yes, but what they expect is it depends --
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I think it is tail wagging dog territory. Because at
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the moment what the cardholder or merchant expects is
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the result of what the issuers and the acquirers are
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doing as between each other.
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MR SMITH: Which is on the basis of an agreement, but it
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happens to be a default.
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MR HOSKINS: Yes. In terms of my approach, if one takes
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this scenario as a possible scenario, which is issuer
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can’t deduct any payment absent a bilateral, let’s take
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that and see where it leads us, because it also then
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raises the question that Mr Justice Barling put to me,
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which is the caveat in all this is: would Visa and Amex
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have maintained high levels throughout the period?
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Actually, through your questioning there is two elements
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to this and they face different ways.
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The first way that comes out of the questioning is,
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in this situation, if MasterCard had a rule, issuers
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can’t deduct absent a bilateral agreement -- and
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remember, this is a counterfactual where Visa and Amex
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have stayed high -- would acquirers agree to pay
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a sufficiently high level to MasterCard because they
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want to keep MasterCard in the market, because it suits
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them to have MasterCard and Visa and Amex rather than
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just Visa and Amex? That’s the first way it is put.
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The problem with that one is the evidence doesn’t
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support it. This is page 46 of our written closings.
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You have got Mr von Hinten-Reed and he was asked this
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question twice. The first time he said, “I prefer not
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to assist you”. That is the extract at 46 onto 47. On
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the second occasion his evidence was that, in his
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opinion, bilateral negotiations could not produce
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an interchange fee in excess of 0.15% and in any event
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he doubted whether the extra cost of negotiating
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bilaterals would make that worthwhile at all. But of
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course, the problem with that in this analysis is we are
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in a world -- so he is assuming that if you had this
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rule and bilaterals came in to fill the gap, they would
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not be higher than 0.15, and in this world Visa and Amex
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are still up here at their actual levels, so that
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migration happens.
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So Mr von Hinten-Reed’s take on ‘would acquirers
step in to keep MasterCard afloat?’ doesn’t work,
because he puts a ceiling of 0.15 in his approach.
MR SMITH: Yes, but that’s more a point against the 0.15
level than bilaterals.
Q. I’m just dealing with his evidence and I will come on to
deal with --
MR SMITH: Indeed, but in terms of his evidence, he was
treating the 0.15, which is his computation of the MIT,
was he regarding the MIT-MIF as a constraint on
bilateral negotiations.
MR HOSKINS: Or was he saying -- I actually understood it
differently. I understood that he was saying that
because all the benefit merchants get from credit cards
is saving the costs that would arise if you were dealing
with cash instead.
You may be right. It was not entirely clear. But
I wasn’t sure he was saying this is a sort of legal
point, but it makes more sense as an analysis if you
want to try to unpick what he was saying, if he says it
is 0.15 because that was all acquirers would be willing
to pay on behalf of merchants, because he thinks that’s
all the benefit merchants get from accepting credit
cards.
MR SMITH: Except the MIT analysis is an analysis entirely
provoked by the Commission's investigation, and one that
Sainsbury's, for instance, had never done apart from at
the behest of the Commission.

MR HOSKINS: I'm not going to go too far into defending
Mr von Hinten-Reed, for obvious reasons, but that was
his position on acquirers, and it wouldn't work to keep
a MasterCard scheme aloof in this counterfactual, is
the short point.

MR SMITH: No.

MR HOSKINS: Everyone gets to...

MR SMITH: Clearly, if he is right and a bilateral is
constrained at an upper limit of 0.15, then your point,
that a Visa MIF of an order of magnitude higher than
that, well there's no difference between a bilaterally
agreed 0.15 and a default of zero.

MR HOSKINS: Yes. Then Dr Niels was asked about this and
his point really was that he said, as a matter of his
opinion, that he thinks because acquirers are competing
with each other, what they would actually do is they
would take the benefit of no deduction, rather than
unilaterally reaching a decision that it is better for
the common good to offer to pay more. We have set out
his evidence on this, but you get that in particular
from the extract at page 49 and the long extract at 50
to 51, where he was asked this question a number of
times. But you will see for example, on page 50, the
passages in bold really flag this up.

Dr Niels:
"Yes, so I think individually no acquiring would
really be so enlightened to say, well, we do want the
scheme to provide, especially if there are competing
schemes out there, so I'm going to be a bit more
generous and allow this particular issuer to charge more
than zero if I can actually get away with zero."

He basically repeated that point. That was very
much his position.

MR SMITH: Indeed, but on this particular question don't we
really have to go and put ourselves into the shoes of
Mr Coupe and Mr Rogers.

MR HOSKINS: That's where I'm coming. I'm just about to go
into those shoes. Absolutely.

The question, and I said there's two sides to it,
the first one is: would the acquirers step in and agree
bilateral agreements that would allow MasterCard to bring its MIF
back up? The other side is: well, if that's not going
to work, flip the other way, would merchants turn their
gaze not on MasterCard but to Visa and say, "If
MasterCard is down at this level, we are going to make
you come down to this level?" That's a commercial
pressure point.

In order to do that, of course, the merchants would
have to threaten something or do something to get
negotiating power, and one of the possibilities that was
put in the questions to Mr Brealey is that in this
counterfactual Visa might refuse to -- sorry --
retailers might refuse to accept Visa Credit cards
whilst continuing to accept Visa Debit cards, and say:
we are not going to accept Visa Credit cards unless and
until you bring your MIFs down because MasterCard are
low.

Our submission is the evidence does not support that
counterfactual, for a number of reasons.

First of all, go back to the Maestro experience,
because Maestro's MIFs were materially lower than Visa's
debit over a period of years, and up until 2007 when
MasterCard brought in its own debit card product, so
2000 to 2007. Merchants didn't negotiate lower
Visa Debit MIFs. They didn't turn round to Visa and
say: you must drop your rates because Maestro is at the
bottom. It didn't happen. That is just as a question
of fact. You have seen what happened to the market
shares, so it didn't happen.

Second point is, in my submission it is not
surprising that didn't happen because, to use the
language of the case law, it is unrealistic to suggest
that merchants would have ceased to accept Visa Credit
cards in this scenario or indeed that they could
credibly have threatened to stop accepting Visa Credit
cards. The reason why they are is because accepting Visa
cards, Visa Credit cards, is simply far too beneficial
to merchants. Even at the higher level in this
scenario, the higher level of Visa MIF, it is still far
too beneficial to them to either stop accepting them or
to credibly threaten to stop accepting them.

Let me give you some figures to put flesh on that.
Can we go to B1, tab 12. Sainsbury's closing
submissions. Again, they were asked to provide various
figures in response to questions by the Tribunal. It is
appendix 2. B1, 12, appendix 2. It is memorandum from
CEG setting out Sainsbury's merchant services charges.
Page 464.

MR SMITH: Ours don't have bundle numbering. (Pause).
MR JUSTICE BARLING: First version of appendix 2.
MR HOSKINS: It is table 5 of that. It is internal page 6.
sorry.

MR JUSTICE BARLING: Thank you. Table 5 you want, MSC paid
on Visa Debits.

MR HOSKINS: That is the one, and Visa Credit card
transactions.
MR HOSKINS: Exactly. You get the annual sales and then you
MR JUSTICE BARLING: We can read them anyway.
MR HOSKINS: Remember that what we are positing here is
MR SMITH: We are looking at the older version.
MR JUSTICE BARLING: Yes, that is table 11, I think.
Page 8.
MR SMITH: We are looking at the older version.
MR JUSTICE BARLING: Table 5. Tab B.
MR HOSKINS: It should be Visa Credit card transactions
MR SMITH: It is the average transaction value I'm looking
at.
MR JUSTICE BARLING: The credit is --
MR HOSKINS: You're right, in absolute volumes debit cards
are used more, but you will see what the average
transaction value is on credit, people buy more on
credit cards per each transaction. There are more
transactions on debit, but each transaction on average
is worth less. When you are looking at the volume in
value, these are weekly figures.
MR SMITH: Maestro too is quite high.
MR HOSKINS: That is correct. That is the point, I made
this point in cross-examination. I will come back to
this, because it is one of the reasons why I say
merchants benefit from accepting credit cards over debit
cards. People spend more on credit cards. Sainsbury’s
figures show that.
Again, this is another reason why we say is it
realistic that someone like Sainsbury’s would say,
"Actually, we are just going to stop accepting your
cards’? The answer is no. That is the second reason,
because they make more on accepting credit cards than
they do on accepting debit cards.
MR JUSTICE BARLING: I suppose that might be a dynamic if
you had a -- you are postulating that over a period of
very high.
Remember, when looking at this, trying to put this
in some sort of context, accepting Visa Credit cards
gave Sainsbury’s higher profits than accepting
Visa Debit cards. I will show you that again, because
it is something I have shown you. E9.1, tab 12 at
page 560. Again, this may well be confidential so
I won’t read it out.
There is a little table at the bottom. The table
details approximate weekly volumes in values by
the main card types. You will see the ATV, the average
transaction value, on a Visa Credit card and
a Visa Debit card and you will see the difference.
MR JUSTICE BARLING: You are comparing the average
transaction value on the MasterCard?
MR HOSKINS: No, I’m comparing Visa Credit with Visa Debit,
because we are imagining a situation where they say: we
are not accepting credit any more but we will carry on
with debit”, and hopefully it is obvious, you will see
one of the reasons why we say that wouldn’t be something
commercially they would do, because if the transactions
were going to switch to debit rather than credit, you
will see the impact it is going to have.
MR SMITH: Debit is far larger than the credit, but the
credit is still significant.
about seven or eight years this kind of differential
would be maintained, and you say, well, the merchants
couldn’t credibly even threaten to do something along
those lines. But I suppose that this is a differential
that would apply across the board to all merchants and
so all merchants would be in the same position of having
to start different --
MR HOSKINS: That is my next point.
MR JUSTICE BARLING: Yes, and --
MR HOSKINS: That is a point in my favour. Can I explain?
MR JUSTICE BARLING: It might be. I’m just thinking -- you
say that wouldn’t give them any more clout, though.
MR HOSKINS: What you have to remember is that when you are
looking at the commercial decision of a retailer to stop
accepting Visa Credit cards, somebody has to do it
first. Imagine you are Sainsbury’s and you are saying,
"Okay, we are making a lot of money, even with a Visa
MIF at this level. Look at the level of sales, look at
the average transaction value, higher on the credit
card. Look at MasterCard. We can get them down a bit,
we will stop accepting them.” What did Tesco and Asda
do?
MR JUSTICE BARLING: To do it, yes. Of course you would be
sticking your neck out, but you were saying they
couldn’t make a credible threat. And what about the
MR HOSKINS: I have one other point to go to, which is

There is a question by Mr Justice Barling:

MR SMITH: I think it is common ground that Mr Perez's

He responds with a different point, which is his

Well, their response is roughly -- and you have

I mean, it is pretty unclear what's being driven at,

If you talk about something being organised through

I have now finished my submissions on it, subject to

MR SMITH: I think it is common ground that Mr Perez's

you have a small amount of time to do it and to

you would welcome their customers with open arms, because

that is why I was so aggressive -- apologies --

Mr von Hinten-Reed was asked by the Tribunal about this.

The Telegraph to say: if you do not reduce your MIF, we

the British Retail Consortium or whatever, you have my

but what I take from that is he says people wouldn't

you are doing is switching from -- you have been waiting

that basically you have to go to Visa because your

Mr von Hinten-Reed was asked by the Tribunal about this.

Mr Rogers would do in this counterfactual world?

Mr Rogers would do in this counterfactual world?

the way in which I would play it would be simple.

Visa to drop its MIF, we saw it actually raised its MIF

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MR SMITH: I think it is common ground that Mr Perez's

you would rather have the customers.

collectively? No, they wouldn't. You see how

cut-throat the supermarket business is. You see how low

Visa Credit cards, "Come into our stores". It is

with Visa Credit cards, "Come into our stores". It is

the same as the expert economic evidence on acquirers,

would they do something individually but thinking

Mr von Hinten-Reed was asked by the Tribunal about this.

It is quite interesting to see how far he was

prepared to go. It is transcript Day 12, page 57,

It is the UK. It is a large differential. Acquirers,

It didn't happen in Maestro. It didn't happen.

it showed the one thing that has happened is Mr Coupe wasn't asked

so what's the response of a retailer or a group of

They would collect the money from customers, they wouldn't

Mr von Hinten-Reed -- part of the trouble is because --

they are not a criticism of anyone, because the case has

Visa to drop its MIF, we saw it actually raised its MIF

Mr von Hinten-Reed was asked by the Tribunal about this.

It is quite interesting to see how far he was

prepared to go. It is transcript Day 12, page 57,

the things that has happened is Mr Coupe wasn't asked

about this, because it wasn't something that was being

raised by Sainsbury's. We don't know. But

I have one other point to go to, which is

you have a small amount of time to do it and to

complain. It doesn't necessarily mean that you

surcharge, or you don't accept Visa cards, but you can

certainly put something in the Guardian or The Times or

the Telegraph to say: if you do not reduce your MIF, we

will do exactly that.

I mean, it is pretty unclear what's being driven at,

but what I take from that is he says people wouldn't

surcharge, people wouldn't stop accepting cards. He

seems to be suggesting that somehow you flag your

intentions to everyone else. But again, if Sainsbury's

puts an advert in the newspaper, Tesco and Asda think:

fantastic, the sooner you do it the better.

If you talk about something being organised through

the British Retail Consortium or whatever, you have my

point, it didn't happen in Maestro and that was the same

scenario.

I have now finished my submissions on it, subject to

the question you are about to ask me.

MR SMITH: I think it is common ground that Mr Perez's

description of how issuers would evaluate a move to

a new and different card scheme was quite compelling.

They would take the first step to do it because it would be

crazy, because Asda and Tesco are probably not going to

follow, they are just going to say to all the people

with Visa Credit cards, "Come into our stores". It is

the same as the expert economic evidence on acquirers,

would they do something individually but thinking

collectively? No, they wouldn't. You see how

cut-throat the supermarket business is. You see how low

the margins are. If someone jumped first, the rest

would welcome their customers with open arms, because

the MIF is actually such a small part of what they do

that they would much rather have the customers.

Mr von Hinten-Reed was asked by the Tribunal about this.

It didn’t happen in Maestro. It didn’t happen.

MR HOSKINS: It didn’t happen in Maestro. It didn’t happen.

It’s the UK. It’s a large differential. Acquirers,

merchants, regulators did nothing, put no pressure on

Visa to drop its MIF, we saw it actually raised its MIF

during the relevant period, and MasterCard all but

exited the market, and it just clung on by its nails

because it introduced a new product in 2007.

That’s why I was so aggressive -- apologies --

earlier. I was talking about a counterfactual. It has

to be based on the evidence; and the evidence here is

Maestro on that. Then it is bolstered by the evidence

on the amount of money that accepting Visa Credit cards

is worth to these retailers.

I think you are ad idem in the sense that nobody

would take the first step to do it because it would be

crazy, because Asda and Tesco are probably not going to

follow, they are just going to say to all the people

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that they would much rather have the customers.

Mr von Hinten-Reed was asked by the Tribunal about this.

It didn’t happen in Maestro. It didn’t happen.
MR SMITH: Secondly, this was clear from the evidence,

MR HOSKINS: Yes, Mr Smith.

MR SMITH: Let’s assume for the sake of argument that you

are right and in our counterfactual world MasterCard’s

ability to set a default is eliminated but no one else’s

is and they carry on as before, both Amex and Visa. So

their MIFs or rates are materially higher, I put it no

more than that, than that of MasterCard.

Let’s put ourselves in the position of Mr Coupe and

Mr Rogers and try to think how Sainsbury’s would analyse

that, first of all, Sainsbury’s is a significant player

in the merchant markets, someone acquirers will listen
to, card issuers and indeed schemes will listen to,
because they are a very, very big operator. That would
be uncontroversial, I take it?

MR HOSKINS: I only assuming stopping nodding because I want to see

where this is going before --

MR SMITH: I thought you might be, Mr Hoskins.

MR HOSKINS: I will shout if I disagree.

MR SMITH: Secondly, this was clear from the evidence,

Mr Coupe and Mr Rogers are both pretty sophisticated
people, they will take not necessarily an immediate
short-term view but they will take a medium to long-term
view, they will take a strategic look as well as
a short-term look.

With all those facts in the pot, what are they going
to do when they see MasterCard at zero and Visa at
rather more than zero? The short-term view would be to
say, “I’m going to pressure my acquiring banks to keep
the merchant service charge as absolutely low as
possible and eliminate a significant portion of my
credit card or debit card base. I will still have to
pay a high level to Visa --

MR HOSKINS: Sorry, I did not understand that last bit.

MR SMITH: Sorry. By not agreeing a bilateral, by sticking
to the default of zero, which is what Dr Niels
suggested, you achieve a saving on a significant portion
of your card expenses, the MasterCard side. But the
Visa side, of course, stays at the level as before.
That’s what we have postulated.

MR HOSKINS: Yes.

MR SMITH: So in the short-term you can achieve a saving on
a significant portion of your credit card transactions
portfolio. But Mr Coupe and Mr Rogers, would they be
unaware of the likely move away from MasterCard in the
MR HOSKINS: Because the differential between the Maestro and a vibrant Visa Debit. They just let it happen. That's the evidence.

MR SMITH: Well, up to a point. I mean, in a sense, if we have to look at the facts, the fact is that the level of Maestro's transactions which Sainsbury engaged carried very high through to 2015. So in a sense the perception that Sainsbury's might have had of a Maestro collapse would be --

MR HOSKINS: But we are using Sainsbury's as an example. This has to be all retailers, because we are talking about a situation -- remember, we are talking about a situation in which there is a differential in the MIFs, in a scenario where we are low, everyone else high, and the evidence is -- and I don't think this is contested -- left unchecked, we fall out the market. So the question is will someone -- or, sorry, will some group step in to avoid that happening? Would acquirers step in to stop that happening? Would retailers step in? So when we talk about Sainsbury's, we use that because we have evidence on them. But the truth is, would a sufficient number of retailers put pressure on the acquirers to bring it down? We don't know. We don't have the evidence save for Maestro, which didn't happen.

MR JUSTICE BARLING: Why shouldn't you give us your best shot on whether we should take judicial notice that a situation -- remember, we are talking about a situation which there is a differential in the MIFs, in a scenario where we are low, everyone else high, and the evidence is -- and I don't think this is contested -- left unchecked, we fall out the market. So the question is will someone -- or, sorry, will some group step in to avoid that happening? Would acquirers step in to stop that happening? Would retailers step in? So when we talk about Sainsbury's, we use that because we have evidence on them. But the truth is, would a sufficient number of retailers put pressure on the acquirers to bring it down? We don't know. We don't have the evidence save for Maestro, which didn't happen.

MR HOSKINS: We are. We have to. Because we are being asked to speculate not just on one but on three different counterfactuals, which does involves speculation and can, at times, involve taking judicial notice of things. I think what Mr Smith is asking you is to take -- maybe whether it is appropriate to take judicial -- we obviously have the Maestro evidence but, as you know, Sainsbury's case is that that's totally different, it is another --

MR HOSKINS: But not on this point, with respect. That's a distinction that doesn't matter in this context.

MR JUSTICE BARLING: Why shouldn't you give us your best shot on whether we should take judicial notice that commercial people act rationally, and in a hypothetical situation, which didn't happen, so we have no direct evidence as to what happened or would happen, we just have to speculate --

MR HOSKINS: But you do have evidence in this case, sir.

You have the evidence of Maestro --

MR JUSTICE BARLING: We don't have any -- because we didn't have a situation with a zero MasterCard MIF on a credit card and a Visa remaining indefinitely at a high level.

MR HOSKINS: You did, sir. Actually the position in Maestro is less extreme than the counterfactual we are considering.

MR JUSTICE BARLING: Because it's--

MR HOSKINS: Because the differential between the Maestro MIF and the Visa Debit MIF was less than we are currently considering in the counterfactual, by several orders of magnitude. That's the paragraph of our skeleton I took you to at E.

So you did absolutely have that situation of a differential in the MIFs. But it is greater in the counterfactual we are considering, so any effect would be greater. But nobody stepped in, watching what was happening to Maestro. You have seen Sainsbury's figures and others will have the same. You have seen every week how many transactions are being done on Maestro, how many are being done on Visa Debit. I think we saw some of the figures actually when we were going through it.

They would see every week Maestro plummeting. But they didn't go into a star chamber and say, "Look what's happening, this is bad for us in the long term because we would actually would prefer to have a vibrant Maestro and a vibrant Visa Debit. They just let it happen."

MR SMITH: I mean, it is a question really of joining the dots, isn't it? You are saying that if the MIF differential continues unchecked, this rival scheme to Visa, the only rival scheme to Visa, will exit the market, with the result that all of the merchants will end up paying those MIFs that Visa chooses to set, with no competitive check whatsoever. That was the reason we put to Dr Niels the question about supply chains and what a sophisticated entity in the market would do with a view to protecting its supply chains.

MR HOSKINS: That's why I asked him whether that supply chain analysis would apply equally to payment schemes, and he said no. Because a supply chain benefits the particular retailer who is funding it. His example, I think, was a bottling plant or something--

MR SMITH: It was Tesco's bottling plant.

MR HOSKINS: But that's someone investing in someone staying in the market directly for their own benefit. Whereas the example we are considering here, where it goes on the evidence, is people not doing something that immediately benefits them, but something that benefits the greater good. So you can't just leap, in our submission, from that bottling plant example, immediate benefit to Tesco's, to the scenario we are contemplating. Indeed, Dr Niels in re-examination was
MR HOSKINS: Sorry, the figures, for example, if one takes Table 8 is Maestro acquisitions through the MasterCard exit, we saw that.

MR SMITH: You see? Table 8 is Maestro acquisitions through WorldPay.

MR HOSKINS: Yes, but that's -- I see. I'm sorry.

MR SMITH: From 07/08 there is a spike that is not consistent with the general shape of the graph, but then a quick plummeting thereafter.

MR HOSKINS: No, but you are missing table 11, because Sainsbury's switched acquiring bank.

MR SMITH: No, well if you -- one would have to check what WorldPay.

MR HOSKINS: We are looking at billions and millions. 2009/2010 and compares the figures on table 11, they are still substantially less by an order of magnitude, are they not?

MR HOSSINS: No, it is not because they want to harm other people. The evidence -- as I say, I don't -- the point you just put to me, I say, is not supported by the evidence. See Maestro. See the expert economists when you asked them a similar point about acquirers.

MR JUSTICE BARLING: We will see you at 2 o'clock.

MR SMITH: Yes. My main point is the evidence and my main point is Maestro and my main point is the expert economists. So it is economics and effects.

MR JUSTICE BARLING: Shall we give you a rest then?

MR HOSKINS: I'm fine, but we should give everyone else a rest. Thank you.

MR JUSTICE BARLING: We will see you at 2 o'clock.
In the counterfactual there is Visa and Amex, no MasterCard, or a severely wounded MasterCard. Therefore, less competition.

If you take a scenario where you have at par clearing, subject to bilaterals, which is issuer receives nothing absent bilateral, you have still got, we say, a zero MIF, because that is what at par clearing is; it is default rule of zero but it’s still a common floor for merchants, and indeed for issuers as well.

So we would say on the issuing market, probably worse -- at least worse in the counterfactual but certainly no better.

Just to take account of the scenario: what if merchants were to put pressure on Visa to bring their rates down? Well, what we have got -- you will understand my submission, but let’s take the Amex share up, it was bang into the regulation. In the counterfactual we are imagining, there is no regulation, so that is a scenario we have got of merchants going to Visa, effectively, and saying, “We want to pay less”.

Visa would be in a stronger position than Amex was in 2015 because there is no regulation.

In addition, you must remember that Amex is a far less attractive proposition to most retailers than Visa. It is accepted in less places. It is used for groceries, I don’t say it is never used for groceries. I pay for groceries with Amex. But it’s a less attractive proposition, partly because the retailer pays more to accept Amex.

But look what happened in that scenario? Did Amex come down to 0.3 in the negotiations with Sainsbury’s? No, it didn’t. The actual figure is confidential, but it’s still a very substantial difference. If you are applying your add on to the counterfactual, if you like, of merchants putting pressure on Visa, you then have to ask the question: what effect would that have on Visa? How far would it come down? Would it come down to the same level as MasterCard? Our submission is probably not, because it’s still a very substantial difference.

So we would say on the issuing market, probably worse -- at least worse in the counterfactual but certainly no better.

Just to take account of the scenario: what if merchants were to put pressure on Visa to bring their rates down? Well, what we have got -- you will understand my submission, but let’s take the Amex share up, it was bang into the regulation. In the counterfactual we are imagining, there is no regulation, so that is a scenario we have got of merchants going to Visa, effectively, and saying, “We want to pay less”.

Visa would be in a stronger position than Amex was in 2015 because there is no regulation.
question of what the exemptible MIF would have been in
order to determine what loss, if any, Sainsbury's had
suffered?
In deciding whether the actual MIF fulfilled the
criteria for exemption, the burden of proof is on
MasterCard, and it is for MasterCard to show that the
four conditions of Article 101(3) are satisfied.
If the Tribunal finds that the actual MIF should not
benefit from an exemption, Sainsbury's doesn’t
immediately have a right to claim damages for any loss
that it can show it has suffered. There’s no
presumption of loss because a MIF is at a level which is
above the exemptible level. The claimant still has to
prove loss. Because the tortious principle, and it is
perfectly compatible with EU law, is claimant is
entitled to be put in the position as if the wrong had
not occurred. So if, for example, there had been 100%
pass-through, then you don’t suddenly say you have got
a right to claim the whole overcharge, you have actually
got to go on and see what loss has actually been
suffered. So there isn’t, as Mr Brealey appeared to
got Mr von Hinten-Reed saying here and you have got
Dr Niels in this case is that there is an exemptible
level doesn’t satisfy 101(3), there is an automatic
right to damages, because the way the case has been
brought by the claimant is there is an exemptible level
of MIF. So you are looking for that counterfactual.
What would the exemptible level have been?
We say this is exactly the same sort of exercise
that you have in cartel damages cases, because if it is
established that there was a cartel, the question then
is: well, what would the price have been absent the
cartel?
There’s no automatic assumption that the whole of
the price paid during the cartel period is itself
recoverable. In order to establish loss, the claimant
has to show what the overcharge is. They can’t simply
say: I have paid a price and the price is unlawful.
So we say that at this stage, when you are looking
at what the exemptible level of the MIF would have been,
that’s part and parcel of the task of establishing
whether there has actually been any overcharge as
a result of unlawful conduct. It is part and parcel of
the task of damages assessment. It is nothing to do
with granting an exemption. That simply doesn’t enter

There are a number of points about the task of
damages assessment that the Tribunal would have to
undertake if we get to this stage.
First of all, for this purpose, when you are trying
to identify the exemptible level of the MIF, having
decided that the actual MIF is not to be exempted, then
it is quite clear that what you are seeking to identify
is what the lawful level of MIF would have been.
That is nothing to do with granting an actual
exemption, because let’s assume you come up with
a lawful level of MIF at 0.4. You do not then grant
an exemption at 0.4, because that MIF never existed.
The reason why I say that -- what you are not doing as
part of this exercise is you are not saying, “Shall we
grant an exemption at a certain level?” What you are
doing is saying, “What’s the exemptible level of the
MIF?” in order to determine whether Sainsbury’s have
suffered a loss, and how much.
Secondly, the evidence of Mr von Hinten-Reed and
Dr Niels in this case is that there is an exemptible
level of a MIF.
The actual question that’s before you is, you have
got Mr von Hinten-Reed saying here and you have got
Dr Niels saying here, you may say it is somewhere in the
middle etc, but both experts say there is an exemptible
law.
MR JUSTICE BARLING: You say the significance of that being
that the burden of proof is shifted as to what that
exemptible level is, as I understood it anyway. That
is, once you failed on, if you fail on, exemption, then
exemptible level passes over to Mr Brealey.

MR HOSKINS: They have to establish loss. So just that if
it is a widget cartel case, a claimant who turned up in
court without any evidence on what the lawful level
of -- the level of the MIF -- sorry, the price of the
widget would have been absent the cartel, they wouldn't
win, because the court wouldn't say: you are entitled to
the whole price.

MR JUSTICE BARLING: That is a bit different, possibly,
because here you would have an unexempted overcharge.
Here you have what you say is a restriction of
competition. You say that there is no -- I think you
say that in principle there is no distinction, even if
it is a zero MIF.

MR HOSKINS: It is not a MIF. What you don’t have
an exemption for is a MIF at a certain level.

MR JUSTICE BARLING: Yes.

MR HOSKINS: If we are proceeding on the basis that there is
an exemptible level of the MIF, which is the evidence
before this Tribunal.

MR JUSTICE BARLING: It is not quite like a cartel case.

MR HOSKINS: I understand. It is a simplified comparison.

MR JUSTICE BARLING: It seems that, at first sight, it is
a bit counter-intuitive that, you having failed, on this
hypothesis, to establish that you have done something
lawful, therefore the assumption is you have charged
what is, in effect, an unlawful price, they then have to
prove what would have been a lawful price in order to
recover anything.

MR HOSKINS: I will go back to my widget cartel. We charged
a price of 10p per widget due to a cartel. That’s not
exemptible, because it was a naked horizontal
price-fixing cartel. So we charged an unlawful price.
Can the claimant turn up and simply say: absent the
cartel, the widget would have cost nothing? Clearly
not.

When the sides turn up and the claimant turns up and
says, “I think the price absent the cartel would have
been X”, the defendant says, “It would have been Y”, who
is the burden of proof on? In that context, actually it
would be on the claimant because they are proving their
loss.

MR SMITH: But in weighing these various factors as to what
is exemptible, the exemptible level is, whether it can
be exempted, one of the things we need to take into
account are the criteria for exemption, and the fact
that the burden would be on you to establish that, were
push to come to shove in the counterfactual world.
MR HOSKINS: But we are removed, in a sense, from this. I understand. We are removed from this exercise, because we have heard all the evidence and you are deciding what the exemptible level is. So you could take it one stage of difficulty further and say: well, because this is an unclear area, we are going to give the benefit of the doubt to the claimant rather than the defendant.

In my submission that wouldn’t be the correct approach, because the job for you is to apply the four criteria and decide what the exemptible level would be. Because you are not granting an actual exemption.

MR SMITH: Sure, but suppose --

MR HOSKINS: Can I just try -- this might help at least to understand what I’m saying. Maybe you won’t like it but let me hopefully clarify the point.

The really interesting point arises, which is what if -- we are looking at whether the actual MIF should have an exemption, and the answer is no. Then you look at the question: what would the exemptible level of MIF have been? And using the broad axe you decide that the spread of possible exemptible MIFs actually would cover up to the level of the actual MIF. That really is where it becomes important, if you get to that stage.

What my submission would be, so you see where we are coming from, is that you could say, in that circumstance, MasterCard has failed to prove its entitlement to an exemption for the actual MIF, but as a matter of quantification Sainsbury’s has not established any loss. Again, it is a bad one because it is not a complete fit, but this is the one that popped into my head when I was trying to see, well, why would that be right.

It is a bit like a crime has been committed and there is a criminal prosecution which fails and then there is a civil action that succeeds. Now it is not perfect, because you have different standards in criminal and civil law, but you can see how the same act can give rise to one conclusion in one legal context and in another.

I think I’m a bad lawyer, because I know lawyers are supposed to get excited about burden of proof issues. My impression is – I have never sat on that side of the bench – the truth is you have all the evidence before you, and if you ask yourselves the question what was the exemptible level of the MIF, with all the evidence before you, it is not going to turn on the question of who bears the burden of proof. Because you have more than enough evidence in this case to come to your own conclusion on what the exemptible level is.

MR SMITH: Suppose we take a view that there is an exemptible MIF, and we have in mind a range, and at the upper end we are confident that it wouldn’t be exempted, at the lower end we are confident that it would be, and we are just not sure in our minds where in the range it works. We have established sort of to our satisfaction that the probability of exemption increases the lower you go.

At that point, don’t we have to take into account the burdens that do lie on your client with regard to establishing exemption, and we should say, well, we should err towards the lower range of that end rather than the --

MR HOSKINS: I think it depends how you ask the question. Because if, in your example, you have a range and you think the upper level wouldn’t merit an exemption, then it shouldn’t be in your range. I think you are looking for the range of MIFs that you believe would get an exemption. Once you have identified that range, then if you are applying the broad axe -- which helps Sainsbury’s in many ways because they are not required to prove loss to the nearest pound and pence, the broad axe generally helps the claimant -- but what kicks in then is generally that the courts, without a legal rule, that the courts have generally said: if we are applying the broad axe in order to allow some recovery, you err on the side of under-compensation.

Our submission would be, first of all, identify the range where you think, on the balance of probabilities, it would satisfy the exemption criteria. Then, in terms of assessing what the overcharge was, you err on the side of under-compensation.

MR JUSTICE BARLING: You say that in establishing that range we have to -- I know you say, and you may well be right about this, but most cases don’t turn on the burden of proof, most issues don’t -- but technically, in establishing that range, you say the burden is on Sainsbury’s to establish --

MR HOSKINS: No, in terms of establishing -- we have to -- if one starts from the basis that there is an exemptible level of MIF, then yes, the burden is on Sainsbury’s.

Assume it wasn’t common ground, there hadn’t been evidence, common ground between the parties, that there was an exemptible level of MIF, then the burden would be on us to show there was an exemptible level, and that would probably fold the two questions together. But once you have a situation where both parties before you are saying there is an exemptible level of MIF, one side says X and one side says Y, then I would say the burden is on them to show what the exemptible level is.
PROFESSOR JOHN BEATH: Sorry, in order to show that Y is right rather than --
MR HOSKINS: Yes, to show what the extent of their loss is.
MR SMITH: You have mentioned, quite rightly, on several occasions that both economists agree not as to the level of exemptibility but that there ought to be an exemptible level.

You are not going so far as to say that we simply take that agreement as read and assume our quest for the exemptible level? We presumably have to apply the legal test to the facts that the economists have brought before us and reach a conclusion as to exemptibility first and then go on to --

MR HOSKINS: I agree with that. Because if you have two expert reports that you thought, that’s fine, but they are completely wrong in law, it wouldn’t help you. But you will see the submission and you have read the clauses, but Mr von Hinten-Reed thinks on his view of the law it is satisfied, and we say on our view of the law it is satisfied, but I agree you would have to satisfy --

MR SMITH: We have to apply the legal test first and then go from there.

MR HOSKINS: Yes. But that is applying a legal test to facts that have been established on the balance of probabilities. It is a purely legal exercise, and if a burden of proof doesn’t come into that then we are dancing on the head of a pin.

MR SMITH: Yes, we are going into an interesting and possibly unnecessary debate about what is a question of fact and what is a question of law, but yes, we have to apply the law to the facts.

MR HOSKINS: Even a characterisation of facts is generally characterised as, for example, as an error of law in judicial reviews.

I was trying to make your job easier, at least at some stage.

Can I move into the four criteria then. I pick it up at page 66 of our closing submissions. Both in the opening and in the closing we have referred to the 101(3) guidelines. For example, if you see paragraph 202, what the guidelines do say:

"Each case must be assessed on its own facts and the guidelines must be applied reasonably and flexibly."

Yes, you have to bring robust evidence etc, but it is not an impossible burden. It is not intended to be. Because that itself would be bad for competition. If nobody could ever prove a 101(3) case, then matters that should be exempted will not be exempted. So it is odd, there is a bit of hard and soft in the regulation.
We will come to that: agreed that when it comes to the first condition, you

"Even if this Tribunal finds that the UK MIF was not necessary to allow this scheme to operate, so not objective necessity, the scheme will still generate relevant benefits within the scope of the first condition to the extent that the UK MIF allows the MasterCard scheme to be larger and therefore generate more benefits than a scheme without a MIF, or indeed a scheme with a smaller MIF."

In other words, benefits which arise from the MasterCard scheme that would not arise in the absence of a MIF satisfy the first condition. I will develop that, but that’s the nub of what we say.

First question, arising this took up quite a lot of time yesterday, benefits on what markets? Because there are three markets in play here: there is the intersystems market, competition between payment schemes; there is the issuers’ market; there is the acquiring market.

In our submission, it is absolutely plain as a matter of law that the Tribunal is not limited to considering benefits arising solely on the acquiring market. You are looking at efficiencies on the other markets as well. We have referred to Compagnie Maritime Belge. That is set out almost verbatim, so we have given you the reference to the passage, but what that case says is:

"All the advantages on both consumer markets in the MasterCard scheme, including therefore on the cardholder’s market, could, if necessary, have justified the MIF."

Then 242:

"Thus, where, as in the present case, restrictive effects have been found in only one market of a two-sided system, the advantages flowing from a restrictive measure on a separate but connected market also associated with that system cannot be in themselves be of such a character as to compensate for the disadvantages resulting from that measure in the absence of such proof of the existence of appreciable objective advantages attributable to that measure in the relevant market."

I will come on to that, because that is the next stage. Because, sir, what you can’t do is look at all the benefits. Here, if you are looking at a restriction on the acquiring market, the fact that there are lots of benefits in the issuing market, if there were none on the acquiring market, that would not be enough.

I will come to take that in a bit more nuanced way as to what you have to have on the acquiring market. At this level, first condition, ‘are there efficiencies?’, you are looking at both markets. That’s quite clear from the case.

MR SMITH: In terms of efficiencies, simply as a matter of logic, you can’t rely upon the benefit that you relied upon at the 101(1) stage, namely the collapse of the market, because by definition you will have rejected that submission if you get to 101(3).

MR HOSKINS: Exactly. As I put it in paragraph 206, what
I’m about to do is identify a large number of what we say are benefits from the MIF. The argument is going to be -- again, I will take you to the evidence, but what the MIF allows the scheme to do is compete with other schemes and extend its market share; and the more people that use credit cards, the more people that benefit from the benefits, whether it be cardholders and/or merchants. In fact, it is both. This has moved away at this stage from --

MR SMITH: I thought that was your position. I just wanted to be clear.

MR HOSKINS: Page 70 of the closings, “Benefits to merchants”. Now, poor Mr Brealey’s fantastic thing quote comes back again, but let’s look at the benefits to the merchants, the evidence that credit cards benefit merchants, and also the evidence that the value of those benefits exceeds the costs to merchants.

At 216 of the closings you have got the point we made in our opening oral submissions. When you look at how credit cards came into being, long before any credit card schemes existed, merchants offered customers credit. It has a value to merchants. They did that.

Why offer credit? Because it was an advantage to do so. And they must have decided that, by definition, the benefits of accepting credit outweighed the costs to them of doing so, otherwise nobody would have done it.

It makes me think of those old westerns, where people are going into the general store and putting it on the slate. It has been around for centuries; merchants offer credit because they think it has an overall benefit for them.

The second point, this is 217, merchants were willing to accept credit cards when they were introduced, despite the fact they had higher costs to them than debit cards. So in that world a few decades ago, when there were just debit cards, somebody comes in with credit cards, the merchants didn’t go: no, no, no.

You see the success of the schemes. It has been incredibly successful.

If the addition of the credit facility provided no benefit to the merchant at all, merchants would have no reason to accept anything other than debit cards.

Mr von Hinten-Reed accepted in his cross-examination, we have set it out, that each merchant which accepts cards must consider the value of doing so is greater than the cost to them of doing so.

He had a different point then, which we will come to. But he accepts that for individual merchants you accept a credit card because you think the benefits to you outweigh the costs.

Third point, 218, the benefits that merchants receive from accepting credit cards is apparent from the evidence of expenditure at Sainsbury’s. That’s the table I took you to this morning, you remember the average transaction value, where you saw the difference for MasterCard credit and Maestro and for Visa Credit and for Visa Debit. We have given you the reference there, but it is that little table. People spend more on credit cards than they do on debit cards.

Paragraph 220 -- it is in yellow so I can’t read it out -- you will see the comparison there is between the extra spend on the average transaction value between credit and debit and what MIF is being incurred. You will see that the benefits quite substantially outweigh the detriment to Sainsbury’s by accepting credit cards, by an order of magnitude.

The fourth point, this is at 221, the substantial benefit which Sainsbury’s, and indeed all other retailers, we say, receive from allowing its customers to buy on credit is confirmed by the significantly higher payments that Sainsbury’s agreed to make to American Express. Again, a lot of this is in general, so I have to be careful. But the point is this: for the first eight years of the claim period, Sainsbury’s was willing to pay American Express an average MSC that was much higher or materially higher than the MasterCard and Visa fees. Why? Because they thought it had a benefit.

I could get into the debate this morning about: did they drag Amex down to the level of Visa and MasterCard? No, they didn’t. We have said enough on that, but in passing I will note that.

Then in B we have the point that even with this 2015 negotiation, with the regulation putting the cold hand on Amex’s shoulder, you will see the level of the negotiated fee between Sainsbury’s and Amex compared to the 0.3 that MasterCard and Sainsbury’s have. Why is Sainsbury’s willing to pay that to Amex? Because it thinks there is a benefit in doing so.

Fifth point at 222. There is, of course, further evidence in relation to the substantial benefits which Sainsbury’s believe it receives from credit cards in the Sainsbury’s Bank payment story, because Sainsbury’s Supermarkets was willing to pay Sainsbury’s Bank large sums to offer more attractive cards, because it thought that would lead to greater sales in its stores.

So again, cogent evidence that Sainsbury’s believed that credit cards have a substantial advantage for it, to the tune of the level of the payments that it was making.

Sixth point at 224. This is actually
MR JUSTICE BARLING: The merchant gets it the next day.

MR HOSKINS: It is an advantage of a store card. It is the

MR JUSTICE BARLING: That is an advantage over a store
cardholder uses the card to make a payment, what happens
issuers, unlike debit card issuers, have no current
another way. Let me see if I can break this down.

MR HOSKINS: Mr von Hinten-Reed’s case.

That’s a meal that might not otherwise have been taken.

So there is the net present value point. That is

a benefit.

Merchants benefit from the free funding period in
another way. Let me see if I can break this down.

In relation to the free funding period, credit card

account relationship with the cardholder. So, when the

cardholder uses the card to make a payment, what happens

in the current system is that the merchant gets the
money immediately, but the cardholder has 28 days to
pay. But in a debit card world, the money is lifted
immediately from the cardholder’s account.

What a four-party credit card scheme could do is it
could say, rather than pay the merchant immediately, we
will pay the merchant in 28 days’ time when we actually
receive the money.

But that’s not what happened. So the free funding
period has a flip. It gives the customer 28 days to pay
but, equally, part of the system is the merchant gets
the money immediately, they are not required to wait 28
days. So in terms of net present value, it’s money in

the pocket for the merchant.

MR JUSTICE BARLING: That is an advantage over a store
charge card, which would presumably -- no, sorry. No.
They would pay later -- yes, that’s just a credit card
but you have to pay the full amount.

MR HOSKINS: It is an advantage of a store card. It is the
advantage of old-fashioned -- if I went back to my
Wild West store, you could have credit, but that
merchant wouldn’t get the money immediately.

What actually happens under the four-party scheme --

MR JUSTICE BARLING: The merchant gets it the next day.

MR HOSKINS: Exactly.

That is merchants. I am not pretending that is
an exhaustive list, but there is a serious -- I put it
there is overwhelming evidence of material benefits to
merchants. I leave the hyperbole at that.

Then one looks at cardholders as well, because we
are to look at both sides. This is paragraph 229 of the
closing.

Mr von Hinten-Reed accepted again, in
cross-examination -- we give there the references --
cardholders benefit from short-term flexibility of the
credit provided by credit cards, they benefit from the
interest-free period, they benefit from the ability to
make online purchases and they benefit from the
availability of rewards.

For Mr Brealey rewards are a vicious circle, but in
our submission they are a virtuous circle, because
rewards encourage cardholders to use their cards. How
do they use their cards? By spending money with
merchants. It is a virtuous cycle, not a vicious cycle.

In terms of the first condition, what are the
benefits of credit cards, those are the benefits.

I will come on -- I know the legal test is benefits
flowing from the MIF, and I have given you a flavour of
that, it is because the MIF increases the use of credit
cards, but I will come to that, and I am going to do

MR HOSKINS: Mr von Hinten-Reed acknowledged that merchants
do benefit from the fraud guarantee and the cardholder
default guarantee, because they get the money in any
event.
that under one of the other conditions. I haven’t forgotten that. Let’s go to the second condition, which is a fair share for consumers. First of all, we have set out the exemption guidelines at paragraph 85. This is this notion of: is social welfare relevant or not? In our submission it clearly is. One sees that most clearly really in 85 of the exemption guidelines: “The concept of fair share implies that the pass-on of benefits must at least compensate consumers for any actual or likely negative impact caused to them by the restriction of competition. It allows the overall objective of Article 81 to prevent anti-competitive agreements. The net effect of the agreement must at least be neutral from the point of view of those consumers directly or likely affected by the agreement. If such consumers are worse off following the agreement, the second agreement is not fulfilled. The positive effects of the agreement must be balanced ...(Reading to the words)... valuable products, and thus to more efficient allocation of resources.” That is a clear, we say, description of social welfare. As I will show you, to unlock social welfare certain legal criteria have to be fulfilled and that’s

the next heading, “Which consumers?” In our submission, it is quite clear again from the law that when you are looking at which consumers benefit, you are looking at merchants who accept payment cards, you are not looking at merchants who do not accept payment cards. This is one of the real flaws in Mr von Hinten-Reed’s analysis, where he looks at all merchants. That is quite clear again, we say, from the exemption guidelines. We have set it out at 234, paragraph 84: “The concept of consumers encompasses all direct or indirect users of the products covered by the agreement ...” Here it is users of MasterCard. It is merchants who accept MasterCards and cardholders who accept MasterCards. It does not include merchants who do not accept MasterCards. Not surprisingly, if you think through the logic. Then you follow that quote through: “... including producers that use the products as an input, wholesalers, retailers and final consumers, ie natural persons who are acting for purposes which can be regarded as outside their trade or profession. In other words, consumers within the meaning of Article 101(3) are the customers of the parties to the agreement and the subsequent purchasers.” The parties to the agreement here are the issuing and acquiring banks and MasterCard itself, and the subsequent purchasers are the cardholders on one side and the merchants on the other. Those are the consumers who have to have a fair share; cardholders who have MasterCard, merchants who accept MasterCards.

That’s also, we say, clear from the Court of Justice in MasterCard. If we go back that, that’s E1.19. It is page 437, paragraphs 235 to 237. You have read these before but it is in particular from the language of 237: “It follows from this that in the case of a two sided system such as the MasterCard scheme ...” Sorry, I should pick it up -- if you see in 236 the final sentence says: “Furthermore, under Article 81.3 EC it is the beneficial nature of the effect on all consumers in the relevant markets.” It is not all consumers; it is all consumers in the relevant markets. So in the relevant issuing markets and the relevant acquiring markets, they must be taken into consideration.

That follows through in 237: “It follows from this that in a case of a two-sided system such as the MasterCard scheme, in order to assess whether a measure which in principle infringes Article 101(1) can fulfil the first condition it is necessary to take account of the system of which that ...(Reading to the words)... advantages flowing from that measure, not only on the market in respect to which the restriction has been established but also in a market which includes the other group of consumers associated with that system.” I understand that this is talking about the first condition, but the language is clearly of the consumers associated with the MasterCard system on the issuing side and the acquiring side, which is what the guidelines tells us we should do. Mr von Hinten-Reed’s analysis is based on the assumption that as a matter of law, under Article 101(3), all merchants must be shown to benefit from the MIF. That is why he kept going on about, for example, business stealing and he excludes it. But he was absolutely wrong to do so as a matter of law. I’m afraid he has just got the law wrong. That’s important because, of course, as soon as you realise what the law actually is, then business dealing becomes highly
relevant; because insofar as a merchant who accepts
a MasterCard credit card steals, obtains a purchase from
someone else who does not, that is a relevant
efficiency. And it is also part of the fair share for
that merchant under the second condition.

The final question on this second condition is 'how
much benefit?', which is an important point. This is
paragraph 239 of the closings. I have just put that
judgment away and I'm going to have to go back to it.

Sorry. E1.19. What the legal position is -- before
I take you there, it is paragraph 248, I think that is
at page 438.

If you could read 248, that's the quickest way to
take it. (Pause).

Again, what we say, the case law is quite clear.
For the second condition, fair share, it is not
necessary to find that each group of consumers,
merchants and cardholders, should benefit equally from
the benefits, provided that merchants do enjoy
appreciable objective advantages. Merchants have to
enjoy the MIF as well as cardholders, but not to the
same extent as them.

Equally, within that group of merchants -- if you
could take up 13 at tab 8, it is a case that you have
been referred to but I don't think you have seen

Shaw and Falla, which is one of the beer cases.

It is paragraph 163 at page 315. You should read
the paragraph, but it is the final sentence that is
really the important one:
"From the point of view of the grant of
an individual exemption, it is not material that the
benefits produced by the notified agreements do not
entirely compensate the price differential suffered by
a particular tied lessee. If the average lessee does
enjoy that compensation, it is therefore such as to
produce an effect on the market generally."

What this is saying is we know that merchants must
enjoy the benefits as well as cardholders, but not to
the same extent as them, and equally you don't have to
show that each individual merchant benefits from the
same level of efficiencies as all other merchants. You
are looking at the merchants who accept MasterCard in
aggregate or the average of them.

Then we come to the third condition, which is
indispensability. I pick this up at page 80 of the
closing submissions. The point is not: does the
MasterCard system generate benefits? The question is:
does MIF generate benefits? That's the test. Again,
that comes from the Court of Justice in MasterCard as
well.

In looking at this, paragraph 245, we have set out
again an extract from the exemption guidelines,
paragraph 75. When looking at indispensability what the
guidelines say, it's halfway down paragraph 245:
"Undertakings invoking the benefit of Article 101(3)
are not required to consider hypothetical or theoretical
alternatives. The business judgment of the party should
not be second-guessed. The authority or court should
only intervene where it is reasonably clear that there
are realistic and attainable alternatives. The parties
need only explain and demonstrate why such seemingly
realistic and significantly less restrictive
alternatives to the agreement would be significantly
less efficient."

Again, as I said, sometimes the language in the
guidelines is very hard but sometimes it is more
practical, and this is one of those areas.

Again, if you go then to 247, which is taken from
the guidelines, and our restriction, in our context, is
the MIF. What the guidelines say is the MIF is
indispensable if its absence would eliminate or
significantly reduce the efficiencies that follow from
the agreement or make it significantly less likely that
they will materialise. The assessment of alternative
solutions must take into account the actual or potential
improvement in the field of competition by the
elimination of a particular restriction or
an application of a less restrictive alternative.

In short, third condition, the MIF will satisfy the
third condition if more efficiencies are produced with
the MIF than would be the case without the MIF.

It's not all or nothing. It's does the MIF
contribute to the benefits of the scheme, does it
increase them? If it does, it's relevant.

What's the evidence of indispensability in this
case? This is paragraph 250 of the closing submissions.
The evidence in this case establishes that -- this is
the point I started with -- the MIF is:

(1) A critical aspect of competition between payment
schemes.

(2) It encourages increased use of payment cards;
(b) cardholders receive higher benefits from card use in
a system with a MIF than they would if there were no
MIF.

(3) Merchants benefit from the MIF because the MIF
allows a payment scheme to attract more cardholders, who
in turn use their cards to make purchases from the
merchants who accept them, and increased card use is a
benefit to merchants.

Then we set out the evidence, but I'm not going to
go through it in detail because we just don’t have time, 1 but I take each of those points and we have given you 2 the evidence that supports them. 3
251. The MIF increases competition between schemes 4 and increases use of payment cards. 5
We have given you the evidence, and 6
Mr von Hinten-Reed accepted those principles in 7 cross-examination. We have seen the quotes. 8
254 onwards deals with the increasing number of 9 cards. 254, in cross-examination, Mr von Hinten-Reed 10 agreed that MasterCard set the MIF at a level designed 11 to maximise the number of MasterCard cards. Again, we 12 have set out all the evidence there. 13
255, the MIF allows cardholders to receive higher 14 benefits. Again we have set out the relevant evidence, from 15 Mr von Hinten-Reed’s own report and cross-examination. 16 You see at 256 he accepted cardholders would like to 17 get rewards and he accepts that rewards are financed by 18 the MIF.
19
257. In cross-examination Mr von Hinten-Reed 20 accepted that low cost balance transfers, low 21 interest-free periods, credit card access to less 22 affluent customers, higher rewards on cards had all 23 developed as a result of competition between card 24 issuers and the intersystem market. 1
We say, therefore, all that evidence, I will leave 2 you to look at the detail, but what it confirms is if 3 there were no MIF, such benefits to cardholders would be 4 reduced. It is obvious from the evidence.
5
If one is looking at the fact that MIF increases 6 benefits to merchants, I have just dealt with 7 cardholders -- at 259 there is a typo I should correct, 8 it says the MIF increases benefits to merchants.
9
First, the MIF increases card use, thus producing 10 a corresponding increase in the benefits which, it 11 should say “merchants” obtain from the use of cards. 12
Again, you have got the evidence of 13 Mr von Hinten-Reed accepting those points. Then at 260; 14 “Reduced use of payment cards would lead to 15 increased use of alternative payment means, such as cash 16 or cheques, which would be more expensive for 17 merchants.”
18
That is Mr von Hinten-Reed’s case. That’s all he 19 was prepared to admit. 20
Then, third at 261 you have got the evidence about 21 Project Forward, Project Porsche etc, where the 22 MasterCard was -- I have to be careful because a lot of 23 that was confidential, but you will see the final 24 sentence at 261/262. It is not marked but I just want 25 to be a bit sensitive about it.

MR SMITH: Mr Hoskins, just going back to your 1 paragraph 258, where you begin to enumerate the benefits 2 if there were no MIF, the countervailing factor you are 3 assuming there is that there will be a MIF of zero; is 4 that right? What I’m trying to work out is what you are 5 gauging the benefits against.
6
MR HOSKINS: It is that, but it is also the higher the MIF, 7 the more the benefits are.
8
MR SMITH: Right.
9
MR HOSKINS: There is clearly a breaking point, but the 10 difficulty is we don’t know what it is. But in terms 11 of -- I mean, for example -- this is not a complete 12 answer. I was trying to put it in context. You heard 13 the evidence, on the EDC study, the 2008 one, if one 14 took the level of all the costs, and I will come to this 15 when I do the adjusted cost/benefit analysis, the MIF 16 was actually set substantially below the total costs 17 that were assessed there.
18
Yes, the argument is not just some MIF is better 19 than no MIF, generally speaking there is an increasing 20 level of benefits, but I accept at some stage there must 21 be a break point and that’s when merchants would 22 actually turn round and say, “I’m sorry, we are not 23 accepting credit cards anymore because we are not 24 anymore receiving more benefits than it is costing us”.

MR SMITH: So something of a sliding scale.
MR HOSKINS: Yes.
MR SMITH: Or an upward demand curve.
MR HOSKINS: Yes.
MR SMITH: Subject to your limit, the greater the MIF, the 1 greater the benefits to all concerned.
MR HOSKINS: Yes. To all concerned, absolutely.
MR JUSTICE BARLING: I think all we are looking at now is 1 under the heading of indispensability, but in terms -- 2 I was going to ask, but I think you have partially 3 answered it, maybe fully answered it: in terms of where 4 you fit -- how you fit the level of a MIF as opposed to 5 the existence of a MIF into those four criteria -- 6 MR HOSKINS: I’m going to come to that, because you are 7 absolutely right that is then the next question, if 8 you like. It is what I have just been discussing with 9 Mr Smith. Because it is all very well to say a MIF 10 creates these extra benefits. The trouble is you have 11 got to decide what level of MIF. I’m going to come to 12 that as a separate question, because obviously that is 13 a big issue. I just want to finish the four conditions.
14
MR JUSTICE BARLING: What I’m asking is: should we look at 15 fair share or is it under 7?
MR HOSKINS: I put it under indispensability. I appreciate
there is not a neat compartment. I have tried to identify the issues and I've put them under the conditions, but I fully accept you can look at them as having interactions. I hope I'm covering all the points, but I accept you may say they may have some relevance to other headings.

If I can finish on this bit. Page 88. Again, the case isn't a very difficult one to follow. We have got the evidence. It is not just me telling a story, we have set out in detail the evidence.

262, on page 88. It is clear from the evidence that more efficiencies are produced with the MIF, and that's on both sides, issuing and acquiring, than would be the case in the absence of the MIF.

The existence of a MIF brings significant benefits to intersystem competition, merchants and cardholders.

Then, as you see at 264, the crucial question is then what level of MIF satisfies indispensability?

Which in a sense is the $6 million question, but I will come to that after the short break.

Let me finish the fourth condition, because I can do that quickly. No elimination of competition. You see that at 266. We see that condition is clearly satisfied, because the existence of the MIF hasn't led to the elimination of competition in the payment systems.
I need to go back and refresh my memory, but from memory you don’t get that sort of debate within, for example, the exemption guidelines about needing to identify a counterfactual in the same way you do. It does seem to be more a sort of crude approach in some respects, which is look at the system with or without the measure that has been found to be a restriction, rather than look at it with or without restriction, and look at what the actual counterfactual would have been. I could be wrong about that, but that’s my recollection.

MR SMITH: I suppose what I was getting at was looking at a number of the benefits that you have articulated going to merchants as a result of a credit card scheme, they need to be funded, but in a sense those benefits accrue whether they are funded by a multilaterally imposed interchange fee or a bilaterally agreed interchange fee, assuming those two to be the same.

MR HOSKINS: My point is they are always going to get more benefits with the higher MIF, because you will have more cardholders. Because the higher the MIF, the more the rewards. That is what we are told. The more rewards, the more cardholders. The more cardholders, the more purchasers and the retailers using credit cards. We know, for example, average spend on a credit card is higher than a debit card, etc. The more cardholders, the more transactions in which the merchant gets the money earlier. The more cardholders, the more transactions in which the merchant gets money he wouldn’t have got at all because the cardholder turned out not to have the money to pay for it, etc.

It is not binary in that sense. It is the whole thing creates more cardholders, which is good for merchants. Because the more people come into their shops and buy things, the better for merchants.

MR SMITH: Right. I appreciate you would say there’s no loss in this case, but I think what you are saying is that even if the bilaterally agreed interchange fee was at the level of the MIF imposed during the claim period, a higher MIF could still be exempted.

MR HOSKINS: If the bilateral was at the actual -- yes, that’s possible.

MR JUSTICE BARLING: I’m afraid I don’t quite follow you, because all the benefits you just referred to could be available if bilaterals are in place --

MR HOSKINS: It depends on the level --

PROFESSOR JOHN BEATH: Generally, they are called the interchange fee. We don’t use this word “MIF”, it is just whatever the price is agreed --

MR HOSKINS: Yes. The higher the interchange fee, the more the benefits.

PROFESSOR JOHN BEATH: Yes.

MR JUSTICE BARLING: Yes. Subject to your point about an absolute limit, higher the MIF or how much -- in the EU analysis we had how much increases as the interchange fee increases, and assuming those two to be the same.

MR HOSKINS: A MIF rather than a BIF.

MR JUSTICE BARLING: A MIF rather than a BIF.

MR JUSTICE BARLING: We will have a short break.

MR HOSKINS: We are going to come onto the tests which have been applied to try to identify, rather than actually just in practice squeezing merchants until they break, after you have the adjusted cost benefit analysis, you have the MIT-MIF. That is an attempt. That’s what has been done by the Commission, by the EU legislature and the regulation etc. That is their attempt to come up with an answer to the indispensability question of how much MIF or how much -- in the EU analysis we had how much interchange fee, but for 101(3) the question is how much MIF?

MR JUSTICE BARLING: We will have a short break.

(A short break)

MR HOSKINS: We are going to come onto the tests which have been applied to try to identify, rather than actually just in practice squeezing merchants until they break, as we say at 267, both the expert economists agree, and this is a quote from the joint experts’ statement:

"This is just too much, we are not going to pay"
MR JUSTICE BARLING: You accept that, do you? Sorry, this

MR HOSKINS: Equally, over the page, in the 2015 survey, I
didn't see any passages in opening, it says it is intended
to serve as a basis for debate and further research, and
the survey is merely an attempt to consistently apply
the MIT.

Again, a green light to you or anyone else in your
position to actually take the matter forward, to take
the learning forward.

So when one looks at what the Commission has done,
flashing light, it is 2008 Rochet and Tirole, which
Rochet says is not suitable for credit cards, and

Central Bank studies generally, except for 2015.

275, the Rochet and Tirole article. You have the
problem, the article makes it clear on its face that the
test discussed therein does not provide a comprehensive
test for the calculation of acceptable MIFs, and it
would suggest suboptimal results from the point of view
of social welfare.

The way I say that the law on the second condition
interacts with this is if you show that merchants are no
worse off, so that is the second condition test, so the
benefits they receive means they are no worse off in
a position with the MIF than absent the MIF, then you
are into 101(3). As long as the benefits that merchants
get is enough to make them neutral -- I actually say it
takes them way beyond that, there are actually far more
benefits, and cardholders are also taken into account --
when you are actually coming to assess what the
exemptible level of the MIF would be, you can and should
take account of social welfare as well. Because that is
what the guidelines tell us, that competition law is
concerned not just with the benefit to merchants and the
benefit to cardholders, but also with social welfare.

But in order to get into 101(3) you have to show
that merchants benefit enough.

MR JUSTICE BARLING: You accept that, do you? Sorry, this
MR HOSKINS: For the second condition?

MR JUSTICE BARLING: We needn't worry about anything else.

MR HOSKINS: It is a sort of necessary trigger.

MR JUSTICE BARLING: Because Mr Brealey said that "no worse

MR HOSKINS: I'm not sure that the case law is absolutely

MR JUSTICE BARLING: You say both for fair share.

MR HOSKINS: -- both sides.

MR SMITH: In a sense, although they are part of the

MR HOSKINS: Yes.

MR SMITH: It is really a question of the merchant benefit

MR SMITH: It is a peculiarity not so much of two-sided

MR HOSKINS: That seems to me quite a good example to show

MR JUSTICE BARLING: Yes.

MR HOSKINS: Fair share. Yes. But then you are taking

account of all the benefits when you are looking at the

first condition.

MR JUSTICE BARLING: Yes, for merchants.

MR SMITH: As you said, it might be difficult if on one side

there was a disbenefit and on the other side there was

a benefit, and the law may be unclear here, but here you

are saying that cardholders benefit and merchants

benefit.

MR HOSKINS: That's my case, yes.

MR SMITH: And in a sense the cardholder case isn't really

being heard here, because no one is saying they don't

benefit.

MR HOSKINS: Yes.

MR SMITH: It is really a question of the merchant benefit

and whether it is a fair share and so on.

MR HOSKINS: Yes.

MR SMITH: In a sense, although they are part of the

equation, they are a rather silent part for the purposes

today.

MR HOSKINS: Particularly when you come to set what the

exemptible level of MIF is, you have to take account of

the benefits to cardholders and merchants. They are

both relevant.

I took you to the exemption guidelines which clearly

refer to social welfare as being one of the objectives

of competition law. I was trying to think of another

example which makes it here that competition law is

concerned with social welfare and not just the position

of individual parties.

It is the GlaxoSmithKline I think is quite a good

equation. This is done on the hoof, so I don't have the

reference for it. It is a well-known case.

GlaxoSmithKline established or stated the principle,

which has been stated a number of times, that EU

competition law protects the process of competition, not

individual competitors.

MR JUSTICE BARLING: Yes.

MR HOSKINS: That seems to me quite a good example to show

that you are not just looking at, for example, merchants, it is a much broader scope. But, yes, for

fair share merchants have to get enough of the benefit

for 101(3) to be opened up, but once the gateway is

opened up, you are looking at the benefits that a MIF

creates for merchants and cardholders and social

welfare.

We then move on to 280, because the Rochet and

Wright article, it was published twice, so it is 2009

and 2010, but it is the same article. You have the
point, I took you to it in opening, that
Professor Rochet has said that his tourist test in 2008, yes for debit cards, but no for credit cards. Precisely because of the sorts of benefits that we have been discussing, and we set out the quotes from 281. I have taken you to them and we have set them out again. But credit has a benefit for merchants and therefore that should be taken into account.

Interestingly, this is at page 94 at (c), this is a summary of what’s concluded but what the Rochet and

Wright article concludes is that:
"As a result, a conservative regulatory approach
would be to cap interchange fees for credit cards based on retailers’ net avoided costs from not having to provide credit themselves, and that using issuer costs to regulate interchange fees is only likely to give a lower bound of possible interchange fees."

We say that’s very important because, of course, we come on to do our costs analysis. But what Rochet and Wright tells us is that that’s actually the lower bound for credit cards.

Then we come onto the MIT-MIF and, as you know, there are various differences between the experts about how it should be applied. This is 282 of the closing.

The first point is that Dr Niels says that the costs data used to calculate the MIT-MIF should be based on the Commission’s econometric models, long run econometric models, not its medium term calculation, which is what Mr von Hinten-Reed prefers, and Dr Niels says that is for two reasons. First, because it takes proper account of all costs which may vary over time, and equally, it avoids the need to rely on the merchant’s own subjective costs allocations.

I will develop these. Those are the two reasons he said he prefers econometric to the medium term data. The second point of difference between the experts is this question: the Commission survey only had data for category 6 to 8, the large merchants, what should you do about that to get to the average merchant?

The third point really has two in it, which is that cash, according to Dr Niels, isn’t an appropriate comparator both for face-to-face transactions that will only take place if credit is available, and also for online purchases. He says, well, it is not fair to look at cash because that’s not a real comparator, and that is the dispute.

So, first of all, the econometric model against the medium term model. I say that gives rise to two issues; taking account of all costs that vary over time, and the relying on the merchants’ own subjective data.
because it is not the sort of thing they normally do.

Yes, they are absolutely dealing with costs all day, but not analysing whether they are fixed or variable.

You see that, what the Commission said itself, 295, it is the quote from paragraph 13 of its own survey.

Econometric techniques are capable of identifying fixed and variable costs without relying on a merchant’s view.

That is why we go there.

But is this really a problem? Let’s look at the extent to which relying on merchants’ views would actually be something to be concerned about.

296, the survey. One cannot entirely rely on potential self-selection bias.

At 297, as we see, the split is crucial for the determination of an application of the MIT.

298, if it is fixed rather than variable you get a lower MIF.

At 299 it is the point again, it is challenging for retailers or merchants’ finance departments, it is not what they normally do.

We have the answers from Mr von Hinten-Reed at 300.

This was really quite striking, because he had, of course, been shown, as we discovered during the course of cross-examination, Sainsbury’s own response or proposed response to the Deloitte’s survey. What he said at 300(c), in Mr von Hinten-Reed’s view:

"Sainsbury’s response to the survey was horribly wrong. Horribly.”

Then (d):

"I should state categorically I was asked whether they should send this submission in and I said no, because I was not happy about some of the supporting evidence.”

(e) Sainsbury’s had submitted its response to the Deloittes survey even after Mr von Hinten-Reed had told them it was not fit for purpose.

You will see the exchange, sir, with yourself. The point is simply this one: if even a large and well-resourced company like Sainsbury’s submitted an assessment of its fixed and variable costs that was horribly wrong and not fit for purpose, it is highly likely that many other merchants would have done the same.

It is not a great advert for relying on the merchants' own data. Because Mr von Hinten-Reed looked at the Sainsbury's submissions and said: it is rubbish, you shouldn’t send it in.

Paragraph 302, there’s also the clear problem, a risk of bias, that the merchants that participated in the Deloittes survey were told of the purpose of the survey, and Mr von Hinten-Reed very fairly accepted, well, that gives rise to a risk of bias. It clearly does.

There is no need for us to allege that Sainsbury’s was biased. I’m not going to put anyone in that difficult position. We don’t have to. I didn’t question on that basis. All I need to do is make the point that clearly there was a risk of bias.

Sainsbury’s, we make no allegation about that, but it is obvious that there is a real risk, in the way the survey was set up, of bias of other people.

303, sixth point, you remember what Mr von Hinten-Reed said he did, because he thought the Sainsbury’s assessment was rubbish, so he did his own.

He went to the costs and did his own categorisation of the costs as fixed or variable. The problem with that is twofold; you are then relying on a data sample of one, rather than a hundred-odd, and Sainsbury’s is one of the largest merchants in the UK and it is not going to be representative of the average merchant. I will come onto that in more detail. But really, to say “Sainsbury’s was rubbish, so I have looked at it and I’m going to rely on this as a sample of one” is clearly unsatisfactory.

304, Mr von Hinten-Reed made the point, he said, "Econometric estimation requires assumptions to be made based on subjective judgment".

Of course, remember what we are talking about is the Commission, carrying out an econometric analysis, and it is very unlikely that the Commission will have been biased to try to produce or even subconsciously trying to produce a higher MIF, given the way it has been behaving over the last decade. So of course econometric analysis requires judgment, but the Commission, you can assume, will have been doing at the very least a neutral job to produce a MIF that was accurate.

What Mr Brealey says is there are all these problems with Dr Niels. We are not saying Dr Niels is perfect.

Dr Niels doesn’t say Dr Niels is perfect. But we are in an imperfect world and you have a choice between these two things. You have an econometric model, which does take account of costs which vary over the longer term. You have an econometric model which avoids the obvious problems of relying on merchants’ own categorisation of costs as fixed or variable.

Our submission is it is pretty obvious, in that scenario, which the preferable route is, because what Mr von Hinten-Reed offers you is his sample of one, “I have gone off and looked at the Sainsbury’s data”.

You are looking at -- whether you call it the average...
MR HOSKINS: I'm about to take you to the evidence that will base it on a sample of one is absolutely hopeless.

The second point is what do you do about the fact that the 2015 Commission survey only included large merchants, categories 6 to 8? Mr Brealey took you -- this is 307 of our closings -- to the eight classes. We have got data for 6 to 8 but nothing more.

What we know from the Commission's survey, we set it out at 308, the Commission's survey recognises, this is the last couple of lines of paragraph 4: "... it is a trade off between precision of data and sample size and representativeness."

Paragraph 23:

"The Commission therefore considers [this is at the bottom of 23] that without further data from small merchants it is not possible to draw reliable conclusions from the study concerning the level of indiffERENCE of all merchants."

That is the Commission saying that. 26:

"Collecting data from small merchants proved to be a difficult task, while using data from large merchants to approximate the cost of small merchants is a questionable exercise."

That is the Commission's view. Again, Mr von Hinten-Reed accepted that in cross-examination.

MR HOSKINS: That is correct. T13, page 126. If one goes to paragraph 312 of the closing, larger merchants are likely to have lower costs in accepting cash due to economies of scale. We have just seen Mr von Hinten-Reed accept that. It is also in Rysman and Wright, and then we give the proper reference to lines 21 to 24.

If you pick it up at 313 of the closing, we say relying solely on data in relation to large merchants is therefore likely to lead to a MIT-MIF which is too low. One gets that from Rochet and Tirole. Merchants are heterogeneous, and if that properly guides cardholders' decisions must reflect the average, not the marginal merchant benefit. This implies that the merchants who benefit least from the card, say the large retailers, are likely to fail the tourist test at the social optimum, ie you get a MIT-MIF that is just too low if you base it solely upon large retailers. Again, Mr von Hinten-Reed agreed with that statement from Rochet and Tirole in cross-examination.

MR JUSTICE BARLING: I hadn't spotted that. Why do they benefit of use from the card? It probably doesn't matter.

MR HOSKINS: It does matter. I'm going fast because it's late in the day but I'm probably going too fast, as it is late in the day. If you back to 312, larger merchants are likely to have lower costs in accepting cash due to economies of scale.

MR JUSTICE BARLING: I see. They benefit least from the card because of the comparison --

MR HOSKINS: Exactly.

MR JUSTICE BARLING: But then someone else says they're both likely to --

MR HOSKINS: No, what the Commission says is it is not clear that will be the case, because they --

MR JUSTICE BARLING: They are both likely --

MR HOSKINS: I'm about to take you to the evidence that will demonstrate that in fact it is clear that there is a major difference, on the basis of the evidence, between the levels of MIFs or MSCs you get to if you rely on the large merchant information and what you would get to if you looked at the average merchant.

If I'm going too fast, obviously you will slow me down.

I'm at page 105, paragraph 314. This is where we get to the facts. 314, the fact that the MIT-MIF will differ depending on the size of the merchant and will be lower for larger merchants is confirmed by the calculation set out in the Commission's survey.
We need to go to E3.10, tab 202, 4358. You see there is a number of -- you see what it's doing at paragraph 212:

"The tables below show the median in different thresholds for the merchants service charge in both the card-based and retail-based approach."

What's important is they calculate different MIT MSCs on different bases for categories 6 to 7 and category 8. You will see the sort of differential that one comes up with, in particular it is 12(b) for us, credit cards.

It doesn't really matter the detail of how they got there. The point is they do an exercise which is separate, MSC for categories 6 to 7 and get 0.42, and they do the calculation for size A, the largest gets 0.14. That is a dramatically different indication of how, if you are relying on just larger merchants, you will get a MIT MSC that is dramatically different and lower. We say clearly too low for the average merchant.

So what do you do? The problem matters. So what do you do to try and palliate the problem? As you know, what Dr Niels has done is to say: well, we have got categories 6, 7 and 8, the problem is we don't have 1 to 5. Again, it is not perfect but I'm more likely to get something approximating the right answer by taking categories 6 and 7 and excluding 8.

It is a simple point. He says: if you have not got the bottom half, I chop a bit off the top and I'm more likely to get something that arrives at the average.

Mr von Hinten-Reed says: no, I'm going to take 6, 7 and 8. Which, as I hope I have demonstrated already, will take you to a MIF that is going to be too low.

What Mr von Hinten-Reed did to try and justify his approach, remember he said: I did this, I took 6, 7 and 8, but then I did the sensitivity analysis to show that it is all right -- sorry, just using Sainsbury's data, and then performed a sensitivity analysis. But Sainsbury's is category 8, so it is even worse than I described.

A number of problems with that. This is at 317 of the closing. First of all, of course, again, you have got Mr von Hinten-Reed relying on a sample of one, very large, whilst Dr Niels has got a sample of 126 merchants.

You had Mr Brealey poking sticks into Dr Niels saying, "This takes out a number of merchants in the UK". Again, we are not saying it is perfect, but the exercise here is not: how imperfect is Dr Niels? The exercise for you is: which is the preferable approach, Dr Niels or Mr von Hinten-Reed, in the world of imperfection? So Dr Niels sample of 26 merchants in categories 6 and 7. Mr von Hinten-Reed, sample of one in category 8.

He then tries to justify it with his sensitivity analysis. You remember that, in his report, he had an assumption that smaller merchants would have a MIT-MIF which was twice or three times higher than large merchants, and in cross-examination he admitted he had no evidential basis for taking two and three.

Q. What the data in the Commission survey shows is that that sort of assumed differential, times two or times three, was clearly unrealistic. I took him to the survey. If we pick it up again, E3.10, tab 202, this time at page 4351. You remember I took him to this in cross-examination. This was a distribution of the estimated MIF MSCs by the number of merchants. This, by definition, is just within categories 6, 7 and 8, because that's all the Commission had. What I did was I looked at the median of the most common MIT MSC, which was 0 to 0.5, and I compared it with the median of the other results in this category. I did it in cross-examination but we set out the results in the closing at page 107, because it gives you a sense of what the differentials of MIT MSC are, even within the category of large retailers.

You will see (ii):

"Around 15% of large merchants had a MIT MSC around three times higher than the majority of large merchants."

(iii):

"Around 6 to 7% of large merchants had a MIT MSC around six times higher than the majority of large merchants."

(iv):

"Around 5% of large merchants had a MIT MSC around 14 times higher than the majority of large merchants."

Then (v):

"Around 2% of large merchants had a MIT MSC at least 20 times higher."

That is the sort of spread one is getting just within categories 6 to 8. You remember I took Mr von Hinten-Reed through that, and he confirmed that he would expect the disparity to be greater if one were comparing the large retailers with the retailers in categories 1 to 5. So he would expect a larger spread. That is the top of page 108 at (c).

In our submission, it is quite possible, indeed probable, that you are talking about differentials that might be in the order of 20-odd, not certainly of 2 and 3.
So what Mr von Hinten-Reed was then -- go and do another exercise and show us what would happen if you take higher differentials. Oxera did the same exercise and they have put their conclusions in appendix C because again I think, from memory, Mr von Hinten-Reed’s goes no higher than times 7 in the one that he redid, which is still nowhere near the ballpark spread we are seeing from the Commission’s own data. Oxera have done it with higher factors including a factor of 10 and 20. It is in appendix C so to our closings but we summarised the results at 321 and what it shows, I will pick it up in the third line, this shows that with the differential of times 20, which as I have shown is perfectly possible and indeed probable, the MIT-MIF would be 0.75 using the Commission’s scenario 2, at least 1.67 based on the Commission’s scenario 3 and 0.86 even on Mr von Hinten-Reed’s Sainsbury’s based calculation. The factor of 10, you get the equivalent figure, 0.42, 0.94 and 0.49. With respect to Mr von Hinten-Reed, his sensitivity analysis just isn’t worth the paper it is written on because it is based on unrealistic assumptions and that’s also the case indeed for his updated one, which only goes to times seven. This is paragraph 322. Mr von Hinten-Reed sought to defend his reliance on Sainsbury’s, on using Sainsbury’s data only, ie a sample of one, by saying: well, typical payment takes place at a large retailer, therefore it is reasonable to assume that the MIT-MIF obtained by such a large retailer would represent the large majority of UK sales. As we set out at 323 it is quite clear from the Rochet and Tirole 2008 article, which Mr von Hinten-Reed himself relies on, is what you are looking for is the average merchant. So even within his own world that’s not really justification for a sample of one. Therefore we say Mr von Hinten-Reed’s suggested approach is clearly unreliable, relying on Sainsbury’s sensitivity analysis, clearly unrealistic, and it will lead to a MIT-MIF which is too low. In Sainsbury’s closing, at paragraph 319, they make the point it would be unfair to impose a MIT which is too high on the very large merchants. But that’s deal with by the Shaw case that I showed you. You are not looking at the effect on each individual merchant, you are looking at the effect on the average merchant. For your note the point made in Sainsbury’s closing, paragraph 319, is dealt with in our closing at paragraph 240. Again Dr Niels isn’t saying that his approach is perfect. But we say it is better, clearly better than Mr von Hinten-Reed’s and should be preferred. Then, the final point of difference, which is: is it correct to always use cash as the relevant comparator for this calculation? First of all, online transactions. As I already said, it is common ground that cash is generally not a substitute for online transactions. So if you are not using a four-party payment scheme credit card, what are you using? What’s available? It is Amex and it is PayPal. Again, it is not that we say it is perfect but the problem you have got is that Mr von Hinten-Reed doesn’t take any account of online transactions, but yet it is clear that the MIT-MIF is intended to apply to online transactions and for all its advantages and disadvantages. At least Dr Niels has taken account of the fact that the MIT-MIF has to apply to online transactions and that in online transactions cash is not an appropriate comparator. Again, you get this very sort of stark approach from Mr von Hinten-Reed: I’m not doing anything, I’m not taking any account of this fact. It is interesting that what Mr von Hinten-Reed sort of criticises: well, why does Dr Niels go to Amex and PayPal? The reason is because those are the realistic alternatives for online transactions. He doesn’t suggest any other alternative himself, he just ignores online transactions. Again, we say neither is perfect, but Dr Niels is clearly preferable. Then the final point between them relates to this idea of increased sales resulting from the availability of credit. What we have seen is that there are certain face to face credit card purchases that wouldn’t take place absent credit. So, for example, the worker who is getting paid at the end of the week but wants to go for a nice meal couldn’t afford it unless he used credit. Transactions where something is bought on credit and then there is subsequently a default. So there are, we submit, quite clearly categories where transactions take place that wouldn’t otherwise take place if credit weren’t available. Dr Niels takes some account of them; Mr von Hinten-Reed takes no account of them. We say Dr Niels is therefore clearly preferable. I think it is important to note, this is paragraph 338, he applies a weighted approach to this. So it is a nuanced approach. It may not be perfect but there is some attempt at nuance. Whereas Mr von Hinten-Reed is simply: no account. For that basis we say, if you are going to --
you should -- I think it is worth looking at a MIF
approach -- but it should be with the proper approach,
the best approach is the one put forward by Dr Niels
rather than Mr von Hinten-Reed.
You will see the range that Dr Niels gets to,
paragraph 347. Subject to the sorts of debates we have
been having about whether you go to the lower or the
higher end of the range, for most of that range there is
then no overcharge because the comparison is between the
figures in 346A for credit cards and the range in 347.
MR JUSTICE BARLING: You won’t have time to do the adjusted
cost benefit, if you are --
MR HOSKINS: I won’t have time to finish it today.
MR JUSTICE BARLING: No. You have probably got another
5 minutes if you want?
MR HOSKINS: To be safe, I imagine we want to finish
tomorrow, and that includes Mr Brealey’s reply. So what
I’m trying to do is get to a situation where I sit down
at lunchtime. I have got to finish this and I have got
to do pass-through and then we have got Mr Cook, who
will have slightly over ... I think we agreed
Mr Brealey would have an hour in reply --
MR JUSTICE BARLING: Would it be sensible if we sit earlier?
MR HOSKINS: I think if we could start at 10.00 we would be
safe. 9.30 is an awfully long day.

MR JUSTICE BARLING: I agree. We will sit at 10.00.
MR HOSKINS: Then I will stop now and take this when we’re
fresh in the morning. Thank you.
MR JUSTICE BARLING: Thank you.

(4.25 pm)
(The court adjourned until 10.00 am on
Wednesday, 16th March 2016)
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