

# OPUS 2

## INTERNATIONAL

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

Day 3

January 27, 2016

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1 Wednesday, 27th January 2016  
 2 (10.30 am)  
 3 Opening submissions by MR BREALEY (continued)  
 4 MR JUSTICE BARLING: Good morning, Mr Brealey, Mr Hoskins.  
 5 I think you know that we have now made the order, or  
 6 it is in the process of being perfected, for  
 7 confidentiality ring. The terms are pretty clear, but  
 8 I mean just to remind people that in accordance with its  
 9 terms, although the names are listed of the current, as  
 10 it were, candidates, I think you are still in the  
 11 process of pruning them, but even when they remain there  
 12 they won't be in the ring until they have signed the  
 13 undertaking.  
 14 MR BREALEY: I have just signed something.  
 15 MR JUSTICE BARLING: Yes. Probably a cheque. So, right.  
 16 MR HOSKINS: Can I say something about confidentiality  
 17 before we --  
 18 MR JUSTICE BARLING: Yes.  
 19 MR HOSKINS: Which is just Mr Smith referred yesterday to  
 20 the fact that we have a set of rules and they were all  
 21 blue. That's an error.  
 22 Apparently, what has happened is we had indicated to  
 23 Mishcons documents we claimed were confidential, and  
 24 where we were claiming part of a document was  
 25 confidential, those redactions have been made. But it

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1 has not always been picked up where we claim something  
 2 is confidential, so the whole thing should be in blue  
 3 paper. I'm afraid that is a process that's currently  
 4 being corrected. But the rules are not confidential.  
 5 MR SMITH: Right. That's very helpful.  
 6 MR HOSKINS: They are published on our website. Sorry for  
 7 that. I'm struggling with it as well. I understand it  
 8 has been corrected. It is not ideal, but let's be  
 9 honest, everyone has had to do an awful lot of work to  
 10 try to get that right, so we will have to live with it.  
 11 But I apologise for the practical difficulty it is  
 12 causing.  
 13 MR JUSTICE BARLING: Right, well.  
 14 MR BREALEY: So for half an hour probably max, if I could  
 15 just tidy up a little bit on the ex turpi causa, going  
 16 back over some of the exchanges yesterday and just try  
 17 and put it in order.  
 18 I don't think we need to change our skeleton  
 19 argument, but it may well be on reflection I need to  
 20 emphasise a few points as a result of the exchange.  
 21 Two general points. One is certainly a general  
 22 point, which is that Lord Sumption stated at  
 23 paragraph 62 of Bilta, as the Tribunal probably knows,  
 24 he says the ex turpi causa doctrine is:  
 25 "... a perplexing mass of inconsistent case law."

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1 So the perplexing mass of inconsistent case law,  
 2 I don't believe the three judgments of the Supreme Court  
 3 have necessarily clarified much.  
 4 But the second general point, which is something  
 5 I do want to emphasise because it is teased out from the  
 6 exchange we had yesterday, is that of course the  
 7 application of the doctrine of ex turpi causa is  
 8 primarily a matter of English law. There is no euro  
 9 public policy as such. Ex turpi causa is domestic law,  
 10 I don't say English law, but domestic law but of course  
 11 with certain euro principles mixed up.  
 12 I think that is important to state as a general  
 13 point before I go to some of the cases. But when one  
 14 comes to, for example, attribution, the starting point  
 15 and probably the end point is English law, but what the  
 16 ECJ says will be of some assistance. And I think that  
 17 is something that we hadn't teased out sufficiently in  
 18 the skeleton.  
 19 With those two general points in mind, that as  
 20 a matter of English law it is a bit of a mess, but  
 21 secondly, ex turpi is a matter of domestic public  
 22 policy, could I go to volume I7.1. It is the Servier  
 23 case at tab 25.  
 24 So we can just highlight the passage that I think  
 25 Mr Smith was putting to me yesterday about how the

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1 Supreme Court has approached the doctrine of ex turpi  
 2 causa, and it is at tab 25, page 771, paragraph 22.  
 3 Clearly we can't go through it all, but basically  
 4 what Lord Sumption has said up to paragraph 22 is that  
 5 Tinsley v Milligan applies.  
 6 At 22, he says:  
 7 "However, it does not follow that the court should  
 8 be insensitive to the draconian consequences which the  
 9 ex turpi causa principle can have if it is applied too  
 10 widely. The starting point in any review of the modern  
 11 law must be that we are concerned with the principle  
 12 based on the application of general rules of law and not  
 13 on fact-based evaluations of the effect of applying them  
 14 in each individual case."  
 15 I just pause there. That bit is sometimes not  
 16 applied by other law lords. They do say that in certain  
 17 circumstances it is fact specific, particularly when it  
 18 comes to attribution.  
 19 We just pass on that:  
 20 "However, the content of the rules must recognise  
 21 that within the vast and disparate category of cases  
 22 where a party in some sense founds his claim upon  
 23 an immoral or illegal act, there are important points of  
 24 principle."  
 25 Then we get I think what was being put to me

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1 yesterday, which is the three-pronged test:  
 2 "The application of the ex turpi causa principle  
 3 commonly raises three questions. What acts constitute  
 4 turpitude for the purpose of defence? What relationship  
 5 must the turpitude have in relation to the claim? And  
 6 on what principles should the turpitude of an agent be  
 7 attributed to his principal, especially when the  
 8 principal is a corporation?"  
 9 I think those were the kind of three-pronged tests  
 10 that we were debating about yesterday.  
 11 Again, so we are not into euro territory here, we  
 12 are clearly focusing on domestic law principles. Now,  
 13 there was no question of attribution in Servier, but  
 14 Lord Sumption does give some guidance on the meaning of  
 15 turpitude, and this is what we picked up in our  
 16 skeleton. And essentially it starts -- just to flag the  
 17 point, if one goes essentially over the page to  
 18 page 773, right at the bottom of paragraph 25, I'm not  
 19 going to go through the whole of 25, but one sees, for  
 20 example, the last three lines of paragraph 25, the  
 21 reference to competition law.  
 22 Therefore, a breach of competition law can in  
 23 principle constitute an act of turpitude. However, he  
 24 goes on, at paragraph 29 over the page, at page 774,  
 25 page 15 of the judgment:

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1 "It is right to add that there may be exceptional  
 2 cases where even criminal and quasi-criminal acts will  
 3 not constitute turpitude for the purpose of the  
 4 illegality defence."  
 5 He refers to a case:  
 6 "This applies in particular where the act in  
 7 question was not in reality the claimant's at all."  
 8 Without going into it in too much detail, what he is  
 9 saying here, and one sees it in the sentence "in such  
 10 cases":  
 11 "The fact that liability is strict and the claimant  
 12 was not aware of the facts making his conduct unlawful  
 13 may provide a reason for holding that it is not  
 14 turpitude at all."  
 15 We will come onto a further passage in a moment, but  
 16 having flagged that competition law can constitute  
 17 turpitude, Lord Sumption is recognising that imposing  
 18 strict liability, because breach is an objective test,  
 19 imposing strict liability may constitute injustice, and  
 20 it does not really fall within the category of  
 21 turpitude.  
 22 So when one goes over the page, still continuing  
 23 with paragraph 29, really, again, I rely on the whole  
 24 paragraph, but it is, say, ten lines up from the bottom.  
 25 If one takes the conclusion halfway down and then goes

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1 ten lines up, just after all the cites of the cases,  
 2 Lord Sumption says:  
 3 "The application of the exemption for the cases of  
 4 strict liability [which competition law is] may require  
 5 a court to determine whether the claimant was in fact  
 6 privy to the illegality to the extent an inquiry into  
 7 the claimant's moral culpability may be necessary in  
 8 such cases before his act can be characterised in law as  
 9 turpitude. This may be a difficult question, but it is  
 10 not a question of degree. The conclusion will be  
 11 a finding that the claimant was aware of the illegality  
 12 or that he was not."  
 13 Then he is saying it is a long way from what some of  
 14 the law lords have been saying, that *Tinsley v Milligan*  
 15 give judges a certain discretion.  
 16 Certainly he is flagging there competition law may  
 17 constitute strict liability, which it does. It is  
 18 an objective test. But he is saying there that there  
 19 may be cases where strict liability is not appropriate,  
 20 and that is why we have mentioned that in paragraphs 482  
 21 to 485 of our skeleton and why we refer to the judgment  
 22 of Mrs Justice Asplin in the *Tesco v MasterCard* case.  
 23 Just very quickly to go to that, that's at tab 27,  
 24 the *Tesco v MasterCard* case. And really, I just want to  
 25 highlight for the Tribunal's note the two main

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1 paragraphs. So we are at tab 27, *Tesco v MasterCard*.  
 2 The first is really, if one goes to page 840 of the  
 3 bundle, this is in the section one sees on the left-hand  
 4 side, 839:  
 5 "Does the maxim of ex turpi causa apply to the  
 6 claim?"  
 7 This is in the context of the submissions being made  
 8 there.  
 9 (iii):  
 10 "Does the maxim of ex turpi causa apply to the  
 11 claims?"  
 12 At paragraph 62, right at the bottom of page 840:  
 13 "Lastly, Mr Railton says that if he is wrong about  
 14 this and that the infringement here is a quasi-criminal  
 15 ... and if so, to the extent that negligence or  
 16 intentional ... that there is such mens rea, it would  
 17 also be ...(Reading to the words)... 29 of his judgment  
 18 [that's in *Servier v Apotex*] that there may be  
 19 exceptional cases where even criminal or quasi-criminal  
 20 conduct will not constitute turpitude."  
 21 This is the submission that is being made about  
 22 whether you need to be privy to the facts and be aware  
 23 of the unlawful conduct.  
 24 The judge picks it up at paragraph 80. Again,  
 25 remembering this is a strike-out application at 844, it

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1 is the last page of the judgment.  
 2 Paragraph 80:  
 3 "Does the maxim apply to the claims?"  
 4 That is in the context of the arguments which it has  
 5 been making, where her ladyship said:  
 6 "Once again, in my judgment the MasterCard  
 7 defendants cannot show that the relatively low threshold  
 8 necessary in order to avoid summary judgment strike out  
 9 has been met. I consider it more than merely arguable  
 10 that in order to fall within the category of  
 11 quasi-criminal ...(Reading to the words)... negligent  
 12 conduct. Lord Sumption himself referred to Safeway  
 13 Stores as an example of such conduct, a case in which  
 14 the company had been personally held liable for a fine.  
 15 I regard it more than merely arguable that it is  
 16 necessary to establish whether the claimants and each of  
 17 them have their requisite state of knowledge."  
 18 Maybe that is something that this Tribunal is going  
 19 to have to decide, and clearly we will make further  
 20 submissions on this issue in closing. So we are looking  
 21 at how the domestic court is trying to grapple with the  
 22 meaning of turpitude.  
 23 That, we say, is right: it has nothing to do with  
 24 European law as such, because European law is not  
 25 imposing rules of domestic public policy on Spain,

1 Germany, France or the UK. So that is just a question  
 2 of turpitude.  
 3 If I can come to attribution, which has really vexed  
 4 I think everybody. Going through, again, the judgments  
 5 last night, none of the Supreme Court cases seem to be  
 6 particularly illuminating to the specific facts of this  
 7 case, where you have a sister company suing a third  
 8 party and the third party saying that that claim is  
 9 barred because of the acts of another sister company.  
 10 One doesn't really get a flavour of that from these  
 11 judgments. I will, for example, just go to the three  
 12 situations that Lord Sumption referred to in Bilta.  
 13 Bilta is at tab 26. It is one just before Tesco's.  
 14 So Bilta is at tab 26, page 814 of the bundle. I'm  
 15 just going to refer to a few paragraphs here just to try  
 16 to tease out a few principles. One is kind of an almost  
 17 a negative principle. At 84 of Bilta, again another  
 18 judgment by Lord Sumption, paragraph 87. This is  
 19 concerning attribution:  
 20 "There are three situations in which the question of  
 21 attribution may arise. First, a third party may sue the  
 22 company for a wrong, such as fraud, which involves  
 23 a mental element. Secondly, the company may sue either  
 24 its directors for breach of duty involved in causing it  
 25 to commit the fraud or third parties acting in concert

1 with them or, as in the present case, both. Third, the  
 2 company may sue a third party who is not involved in the  
 3 directors' breach of duty for an indemnity against its  
 4 consequences."  
 5 I mean, if it is anything it is the third one, but  
 6 even the third one doesn't really grapple with the sort  
 7 of attribution that we are concerned with here. So when  
 8 one is going through the judgments, it is about the  
 9 analysis of a corporation, a company. It doesn't act on  
 10 its own, it has to act through the directors or it has  
 11 to have the mind or will. And the usual question is, if  
 12 the directors have been naughty, the extent to which  
 13 that naughtiness can be attributed to the company.  
 14 So that is a negative proposition. What I would  
 15 like to do, however, is draw two things from Bilta. The  
 16 first is from paragraph 7 of the judgment, which is the  
 17 judgment of Lord Neuberger. I would like to emphasise  
 18 two things that we get from Bilta. This is at page 786  
 19 of the judgment, under the heading "Attribution":  
 20 "So far as attribution is concerned, it appears to  
 21 me that what Lord Sumption says in those paragraphs is  
 22 effectively the same, in effect, to what Lords Toulson  
 23 and Hodge say in their paragraphs.  
 24 "Both judgments reach the conclusion, which may  
 25 I ...(Reading to the words)... then the wrongdoing or

1 knowledge of the directors cannot be attributed to the  
 2 company as a defence to a claim brought against the  
 3 directors by the company's liquidator in the name of the  
 4 company and on behalf of its creditors for the loss  
 5 suffered by the company as a result of its wrongdoing."  
 6 Paragraph 7:  
 7 "Even where the directors were the only directors  
 8 and shareholders of the company."  
 9 I emphasise the next few words:  
 10 "And even though the wrongdoing or knowledge of the  
 11 directors may be attributed to the company in many other  
 12 types of proceedings."  
 13 Now, why do I say that's important? It is important  
 14 because there are instances where the acts of directors  
 15 may be attributed to the company for other purposes, but  
 16 when it comes to the doctrine of ex turpi causa, the  
 17 courts are looking at it with a different lens, and we  
 18 would say with a stricter lens, because the turpitude is  
 19 barring the claim, barring the remedy. So one has to be  
 20 careful, in other words, that just because you say  
 21 someone is an economic unit, then you have the  
 22 sufficient attribution.  
 23 I'm just going to develop that very briefly. So  
 24 I said there were two points. First is that it is  
 25 a rule of domestic public policy, but secondly, we see

1 that Lord Sumption gets some guidance from Meridian  
2 Global at a paragraph 92.

3 If we jump from paragraph 7 to paragraph 92, here we  
4 are looking at the extent to which the acts of an agent  
5 can be attributed to the acts of the principal. Again,  
6 it is only a paragraph and it is not that illuminating,  
7 but what we get from all these judgments is that  
8 Meridian Global seems to be fairly well accepted.

9 But he says at paragraph 92, 816:

10 "The technique of applying the general rules of  
11 agency and then as an exception for cases directly  
12 founded on a breach of duty to the company is a valuable  
13 tool of analysis, but it is no more than that. Another  
14 way of putting the same point is to treat it as  
15 illustrating the broader point made by Lord Hoffmann in  
16 Meridian Global that the attribution of legal  
17 responsibility for the act of an agent depends on the  
18 purpose for which the attribution is relevant.

19 "Where the purpose of attribution is to apportion  
20 responsibility between a company and its agents so as to  
21 determine their rights and liability to each other, the  
22 result will not necessarily be the same as it is in  
23 a case where the purpose is to apportion responsibility  
24 between the company and the third party."

25 Again, we are slightly in uncharted territory, but

13

1 clearly when one sees, and we will hand up -- I do not  
2 think it is necessary to go through it now -- I'm not  
3 sure it is in the bundle -- but a copy of Meridian. We  
4 do see the Privy Council, Lord Hoffmann, at  
5 paragraph 23 -- I don't know if we want to hand it up  
6 now -- but paragraph 23:

7 "It was therefore not necessary in this case to  
8 inquire into whether ...(Reading to the words)... will  
9 of the company, but their Lordships would wish to guard  
10 against being understood to mean that when a servant of  
11 a company has authority to do an act on its behalf,  
12 knowledge of that act will for all purposes be  
13 attributed to the company.

14 "It is a question of construction in each case as to  
15 whether the particular rule requires that the knowledge  
16 that an act has been done or the state of mind in which  
17 it is done should be attributed to the company."

18 Again, and we will hand this up, but to a certain  
19 extent there are references there which say: are you one  
20 and the same person? This is why we say the economic  
21 unit point is important to attribution.

22 Again, just to emphasise the two cases that I went  
23 to yesterday, if one could just -- I know we went  
24 through them yesterday and I will only spend three or  
25 four minutes on it, but it is bundle I7, it looks like

14

1 17. Tab 6. We saw yesterday paragraphs 96 to 100. It  
2 is bundle I7, looks like 17. This is the Aristrain  
3 case, C-196/99P.

4 So the inquiry as a matter of domestic law is to  
5 work out whether the act of the Bank should be  
6 attributed to the Supermarket. That's essentially what  
7 we are trying to ...

8 Clearly we would say that 96 to 100 appears relevant  
9 in that inquiry. So in other words, domestic law may  
10 consider how EU law would treat the attribution of  
11 responsibility when it comes to a breach.

12 98:

13 "The court of first instance is wrong to rule that  
14 it is impossible to impute to a company all the acts of  
15 a group even though that company has not been identified  
16 as the legal person at the head of that group with  
17 responsibility for coordinating the group's activities.  
18 The simple fact that the share capital of two separate  
19 commercial companies is held by the same person or the  
20 same family is insufficient in itself to establish that  
21 those two companies are an economic unit, with the  
22 result that under community competition law the actions  
23 of one company can be attributed to the acts of the  
24 other and that one can be held liable to pay a fine.."

25 Again, we see the word "attributed" in

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1 paragraph 100:

2 "The contested decision states no reasons in that  
3 regard, and even contains an internal contradiction  
4 since it suggests that ...(Reading to the words)... must  
5 be attributed to both companies."

6 We see the word "attributed" in Aristrain, and as we  
7 saw again yesterday in the judgment of Jungbunzlauer,  
8 which was at tab 9. Again, at paragraph 126 we see the  
9 word "attributed".

10 So if it is the case, so one is looking at the  
11 jurisprudence of the CJEU and if it is the case that one  
12 sister has decisive influence over the other sister, so  
13 that the second sister is not acting independently in  
14 the market, then one can see that if the naughty sister  
15 acts in a wrongful way, a naughty way, that that act of  
16 naughtiness may be attributed to the person who is  
17 controlling her. And it may well be that if the concept  
18 of economic unit was put to the Supreme Court, they may  
19 say, well, there are four situations where you would  
20 attribute, the three that Lord Sumption referred to and  
21 then circumstances in which you can attribute  
22 responsibility.

23 But the reason I want to emphasise these two cases  
24 is because they do emphasise decisive influence/control.  
25 We would say that is the benchmark for attributing any

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1 act of the Bank onto the Supermarket. If Mr Hoskins  
 2 wants to go further and come up with some other notion  
 3 that says, well, the Supermarket is one economic unit  
 4 with the Bank, then one would have to look very closely  
 5 to see whether those other circumstances were, as  
 6 a matter of English law, sufficient to attribute  
 7 responsibility to the Supermarket for the purposes of  
 8 turpitude.

9 That's why I don't think that we emphasised enough  
 10 that you have got to go back to domestic principles just  
 11 to double check that when EU law says you are part of  
 12 the same economic unit, that is sufficient for the  
 13 purposes of domestic law.

14 But we can see that if the two sisters are  
 15 an economic unit because Sainsbury's Supermarkets is  
 16 exerting that the requisite degree of control in  
 17 Aristrain, then we can see that the Supreme Court would  
 18 probably say that the act of the Bank would be imputed  
 19 onto the Supermarket.

20 MR JUSTICE BARLING: Assuming they are the same unit, but  
 21 for the purposes of the EU case law, so that, for  
 22 example, as a matter of EU law they would have been  
 23 a party to the infringement, let's assume that follows,  
 24 where are you on sort of turpitude and whether things  
 25 are sufficiently naughty in this case?

17

1 I can't remember now whether that's dealt with or  
 2 not in your skeleton. It might be.  
 3 MR BREALEY: First of all, I will just say it would  
 4 depend -- in a moment I will try and articulate what we  
 5 say MasterCard have to prove.  
 6 MR JUSTICE BARLING: Yes.  
 7 MR BREALEY: But the straight answer to my Lord's question  
 8 is that it would depend upon the basis upon which the  
 9 bank and the supermarket were regarded as a matter of  
 10 European law as one economic unit.

11 So let's assume for the sake of argument that today  
 12 we see that the European Court has departed from  
 13 Aristrain and said you don't need decisive influence or  
 14 more control, it is sufficient (inaudible) that you can  
 15 just simply impute knowledge, that the common  
 16 shareholding, it is two sister companies, part of the  
 17 same group, you can impute knowledge. So they get rid  
 18 of Aristrain, and simply because you are a member of  
 19 a whole group, you are one economic unit. Let's assume  
 20 for the sake of argument that is how euro law pans out.

21 I would say that paragraph 7 of Lord Neuberger,  
 22 well, that might be sufficient for you to be technically  
 23 in breach of article 101, but when it comes to  
 24 identifying turpitude and attribution for the purposes  
 25 of this public policy test, it would not be sufficient.

18

1 Because we submit, and it seems to be -- this is what  
 2 you get from these cases -- the agent must be under the  
 3 directing mind and will of the company, or that the  
 4 company is somehow controlling the agent in order for  
 5 the act of the agent to be imputed to the principal. It  
 6 must be more than just you are in the same class, you  
 7 are a member of the same -- it must be more than you are  
 8 just a member of the same group.

9 MR SMITH: Obviously you have quite rightly made the point  
 10 that questions of attribution are extremely difficult,  
 11 and so perhaps we need to devise a way of parking those  
 12 questions.

13 Can we, in order to discuss the other two elements  
 14 that comprise an illegality defence, assume that  
 15 Sainsbury's and Sainsbury's Bank are actually just one  
 16 company, in other words, a single legal entity is  
 17 carrying on both the operations of the Supermarket and  
 18 the operations of a Bank, so we don't have to worry  
 19 about attribution acts or anything like that, we know it  
 20 is the same entity doing both? And then approach the  
 21 question of turpitude and the relation of turpitude to  
 22 the claim that has been brought without having to worry  
 23 too much about these very difficult questions of  
 24 attribution?

25 MR BREALEY: Sure. I will do that.

19

1 I will do that in the context of what and then  
 2 hopefully I will finish on this and then I will just  
 3 mention turpitude and Lord Sumption's third.  
 4 But can I articulate what we say about attribution.  
 5 I would like to say what MasterCard prove, and I think  
 6 it is in a different order to Lord Sumption.  
 7 So attribution first. We submit that the question  
 8 here is: should the act of the Bank be attributed to the  
 9 Supermarket?

10 We would say that involves two considerations. I'm  
 11 still on attribution. The first consideration is  
 12 whether the Supermarket has decisive influence over the  
 13 Bank, and the second consideration, which should not be  
 14 forgotten, is that the Supermarket must have decisive  
 15 influence over the Bank in respect of the restrictive  
 16 agreement.

17 So if it was proved that the Supermarket had  
 18 decisive influence over the Bank-- this is not the case,  
 19 but over pay of the Bank's employees -- this is not the  
 20 case but if it was -- that would not be sufficient to  
 21 attribute the act of the Bank, when it includes  
 22 a naughty agreement, onto the Supermarket.

23 I think we get that from the cases, but we get that  
 24 from the Hydrotherm v Andreoli case that we saw  
 25 yesterday. So even on the economic unit point, you have

20

1 to be at one for the purposes of the agreement.  
 2 MR JUSTICE BARLING: It has to be a decisive influence in  
 3 respect of the MIF or just be part and parcel of the  
 4 scheme?  
 5 MR BREALEY: This flows to quite a few of the conditions.  
 6 We would say the MIF, why the MIF? Because as  
 7 Mr Hoskins was I think submitting yesterday, or  
 8 I accepted, the scheme in itself is not anything to do  
 9 with turpitude. The scheme as a general concept is  
 10 a good thing. So one would have to highlight the  
 11 restrictive agreement.  
 12 That's the whole thrust of Mr Hoskins' submission on  
 13 objective necessity. The scheme is a great thing --  
 14 MR JUSTICE BARLING: You can't be a member of the scheme  
 15 without submitting to the rule about the MIF.  
 16 MR BREALEY: Precisely. That feeds into significant  
 17 responsibility. So that is the attribution.  
 18 Now, I will take Mr Smith's point that there is now  
 19 one economic unit, how does that then feed into the  
 20 other conditions? Well, having seen that the act of the  
 21 Bank is attributed to the Supermarket, one still has to  
 22 identify Lord Sumption's first condition and the most  
 23 obvious one is whether it is turpitude.  
 24 I don't want to go over old ground, but clearly  
 25 Lord Sumption and Mrs Justice Asplin saw that a breach

21

1 of competition law could in principle constitute  
 2 turpitude. But whether it is turpitude for the purposes  
 3 of the ex turpi causa principle depends on, as she said  
 4 at paragraph 80:  
 5 "I consider it more than merely arguable that it is  
 6 necessary to establish whether the claimants,  
 7 ie Tesco's, had the requisite state of knowledge."  
 8 So that is an inquiry that we will have to look at  
 9 in the evidence. But whether, even if technically one  
 10 economic unit, Supermarket, is in breach of article 101,  
 11 whether it had sufficient knowledge if Lord Sumption is  
 12 right and Mrs Justice Asplin, her instinct is right.  
 13 So that would be the question on turpitude. The  
 14 last condition Lord Sumption referred to is, what  
 15 relationship does the turpitude have to the claim. That  
 16 was his third condition. I have tried to work through  
 17 this, but it seems to me that that condition is very  
 18 closely related to the overriding condition imposed by  
 19 European law on this doctrine, that of significant  
 20 responsibility.  
 21 So whether significant responsibility is a fourth  
 22 condition, because we know from *Courage v Crehan* that  
 23 significant responsibility is an overriding condition  
 24 that is imposed on the national doctrine of ex turpi  
 25 causa. So why? Because it was put to the European

22

1 Court that the strict application of the doctrine in  
 2 *Tinsley v Milligan* precluded Mr Crehan's claim, and the  
 3 European Court said no, only if Mr Crehan is  
 4 significantly responsible.  
 5 So we know that the ex turpi causa doctrine is  
 6 a matter of national law, but just as with the passing  
 7 on defence, European law has a little bit to say about  
 8 the strict application. And so whether Lord Sumption's  
 9 third condition "What is the relationship between  
 10 turpitude and the claim", is a free-standing condition  
 11 to significant responsibility, personally I haven't  
 12 quite worked out yet. But I think it is quite closely  
 13 related.  
 14 It may well be that what is the relationship of the  
 15 turpitude to the claim is no more than saying: are you  
 16 founding your claim on the unlawful agreement? If that  
 17 is all that Lord Sumption is saying, then there would be  
 18 a fourth condition: even if you are doing that, as in  
 19 *Courage v Crehan*, are you significantly responsible?  
 20 And are you significantly responsible for the breach of  
 21 competition law? And that's essentially what we are  
 22 looking at.  
 23 It is not the fact that you have just signed up to  
 24 what -- it could be a very benign or proactive scheme,  
 25 a credit card scheme -- are you significantly

23

1 responsible for the breach?  
 2 MR JUSTICE BARLING: On which you rely.  
 3 MR BREALEY: On which you rely.  
 4 MR SMITH: I think, whether it is a third or a fourth  
 5 element, but it seemed to me that when Lord Sumption was  
 6 talking about the relationship between the turpitude and  
 7 the claim, he was taking as given that there might be  
 8 a wrongful act of turpitude for which the actor, the  
 9 claimant, bore significant responsibility, but which was  
 10 nevertheless so unrelated to the claim that it fell out  
 11 of account.  
 12 MR BREALEY: Right.  
 13 MR SMITH: And that is in itself one of these very vexed  
 14 questions, whether it has to be literally an element of  
 15 the cause of action you are advancing which involves  
 16 illegality, or whether it is broader than that, but the  
 17 third stage, it seemed to me from *Apotex*, was that by  
 18 that stage he was accepting that there was both a level  
 19 of wrongfulness that triggered the public policy  
 20 interest, and attribution of that wrongfulness to the  
 21 claimant, but that the other question was: was it  
 22 sufficiently attached or detached? Which is in  
 23 itself --  
 24 MR BREALEY: That's why, heaven forbid I disagree with  
 25 Lord Sumption, but if you apply significant

24

1 responsibility for the breach upon which you rely and  
 2 you say that is the third condition, it is difficult to  
 3 see what you get from the fourth condition because what  
 4 you are trying to see is whether it is detached. And it  
 5 is difficult to see that if you have been significantly  
 6 responsible for the breach on which you rely, how you  
 7 can then go on to say it is detached. But that's why  
 8 I kind of --  
 9 MR SMITH: There may be an elision.  
 10 MR BREALEY: Yes. That is all I have to say.  
 11 I was trying just to kind of clarify what was a long  
 12 day yesterday. It has been helpful.  
 13 The last thing that I just would like to do before  
 14 I leave it to Mr Hoskins, and I don't make any  
 15 submissions on it, MasterCard have in their skeleton  
 16 handed up kind of some flowcharts about the damages  
 17 which, frankly, again we will have to sort out probably  
 18 with Dr Niels. We certainly don't agree the charts and  
 19 we do not agree that when they say it is agreed, it is  
 20 agreed, if you see what I mean.  
 21 MR JUSTICE BARLING: We can't believe anything anymore.  
 22 MR BREALEY: There are sort of shadings which say that  
 23 Dr Niels and Mr von Hinten-Reed agreed, and  
 24 Mr von Hinten-Reed says he does not agree.  
 25 MR JUSTICE BARLING: So we don't agree the charts.

25

1 MR BREALEY: We certainly do not agree the charts. If  
 2 I could just hand up our own chart.  
 3 MR JUSTICE BARLING: Is it you don't agree the accuracy, or  
 4 you don't agree -- sorry, I haven't got in mind what  
 5 the --  
 6 MR BREALEY: We don't agree --  
 7 MR JUSTICE BARLING: Do they say they are agreed? The range  
 8 of damages, if, on the basis of the MIF of -- the first  
 9 chart is on the basis of scenario 1. Is it the figures  
 10 that aren't agreed, or is it the --  
 11 MR BREALEY: We can't replicate the figures.  
 12 MR JUSTICE BARLING: You can't replicate the maths, as it  
 13 were?  
 14 MR BREALEY: No. I'm looking at the scenario 1. I think  
 15 Mr von Hinten-Reed -- just looking on the left  
 16 "Effective competitive dynamics, volume migration to  
 17 Amex only".  
 18 MR JUSTICE BARLING: I can't remember if this is  
 19 confidential or not.  
 20 MR HOSKINS: We have been told this is all confidential to  
 21 Sainsbury's.  
 22 MR JUSTICE BARLING: You haven't said anything yet.  
 23 MR BREALEY: Right, sorry. I'm grateful --  
 24 MR HOSKINS: It makes it quite difficult to deal with.  
 25 MR JUSTICE BARLING: That's why I thought I would interject.

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1 MR BREALEY: It is not yellow. I'm confused.  
 2 I mean, I have -- I think the experts have tried to  
 3 get together, and I think I would urge them again to get  
 4 together to try to see if they can get --  
 5 MR JUSTICE BARLING: If it is just maths, it ought to be  
 6 capable of being ironed out, oughtn't it?  
 7 MR BREALEY: It is. The lighter green Mr von Hinten-Reed  
 8 does not agree.  
 9 MR JUSTICE BARLING: He doesn't agree that they represent  
 10 his views?  
 11 MR BREALEY: Yes.  
 12 MR JUSTICE BARLING: Right, okay.  
 13 MR BREALEY: And that it should affect the damages. But he  
 14 can't replicate the numbers.  
 15 MR JUSTICE BARLING: Right.  
 16 MR BREALEY: Very often these are helpful because it gives  
 17 a range, but at the moment Mr von Hinten-Reed has  
 18 some --  
 19 MR JUSTICE BARLING: Problems with the numbers.  
 20 MR BREALEY: I think he has been in contact with Dr Niels  
 21 and they are going to be a few weeks away --  
 22 MR JUSTICE BARLING: That applies to all scenarios does it,  
 23 one to four?  
 24 MR BREALEY: Yes. That percentage in the left-hand column  
 25 is disputed so far as the damages is concerned.

27

1 Ultimately, we do not agree with the numbers.  
 2 MR JUSTICE BARLING: Right. Anyway, all will become clear  
 3 in due course.  
 4 MR BREALEY: All will become clear when they try and sit ...  
 5 what they have done, and I guess this is also  
 6 confidential so I won't go through at the moment in open  
 7 court, in opening, the range of damage estimates. All  
 8 I will do is just indicate to the Tribunal what actually  
 9 is happening.  
 10 If one looks at the MIT MIF and goes across, the  
 11 first percentage is the calculation made by  
 12 Mr von Hinten-Reed applying a MIT.  
 13 MR JUSTICE BARLING: This is the one you have just  
 14 handed up?  
 15 MR BREALEY: Yes. I think there are some notes, I don't  
 16 know whether it is on two sheets.  
 17 MR SMITH: It is on the back.  
 18 MR BREALEY: We will try and get it on two sheets, I think.  
 19 And you have the notes. But one is the MIF that we say  
 20 is correct. The other is the Commission MIF, and the  
 21 other is the bottom of Dr Niels' range, the low scenario  
 22 from his table 9.2. So all that's happening there is  
 23 you have got three calculations relating to three  
 24 different MIFs.  
 25 Then below the MIFs you have the way of

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1 calculating -- and again, I'm told this is confidential,  
 2 but we will tease this out -- at least two ways of  
 3 calculating compound interest.  
 4 MR JUSTICE BARLING: Yes.  
 5 MR BREALEY: Then on the left-hand side, you have the  
 6 degrees of pass-on.  
 7 As I said yesterday, MasterCard now say there is  
 8 a 100% pass-on and that leads to the bottom right figure  
 9 that they say we are entitled to. Whereas if you adopt  
 10 what MasterCard have been arguing for the last 15 years,  
 11 zero pass-on, you end up with a figure in kind of red  
 12 shading on the left-hand side. But that's just to give  
 13 the Tribunal an indication of --  
 14 MR JUSTICE BARLING: So that is the rival version of  
 15 those --  
 16 MR BREALEY: It is totally rival, because if you take the --  
 17 MR JUSTICE BARLING: Yes, some of them. Where should we put  
 18 that, then? At the end of your skeleton?  
 19 MR BREALEY: If you could, my Lord, thank you.  
 20 And that concludes my opening. I don't know whether  
 21 that's convenient, unless there are some questions from  
 22 the Tribunal?  
 23 MR SMITH: Yes, Mr Brealey, one question.  
 24 Yesterday in the course of your submissions you were  
 25 discussing the various lawful MIFs, and you of course

1 call it the MIT MIF, and Mr Hoskins has his alternative  
 2 proxy for what was a lawful MIF.  
 3 We wondered whether a proxy for a lawful MIF  
 4 mightn't be the MIF that was actually charged in the  
 5 case of debit cards, because that would, as I understand  
 6 it, exclude the cost of providing credit to customers,  
 7 but would include essentially everything else. So we  
 8 thought we would float that with you.  
 9 There's no need to respond now.  
 10 MR BREALEY: I'm very grateful for that. I do see that  
 11 point, yes.  
 12 MR JUSTICE BARLING: I have just lost sight at the moment  
 13 whether part of your case is, or you are prepared to  
 14 tolerate some additions that only apply to credit cards,  
 15 such as an element of the cost of sort of purchaser  
 16 default. I can't remember whether that was something --  
 17 MR BREALEY: Well, the answer to that would be probably no  
 18 for the reasons that Mr von Hinten-Reed set out at  
 19 length and we have tried to put in the skeleton, but  
 20 obviously look at it. But to a certain extent in his  
 21 calculation he looks at transaction costs and an element  
 22 of fraud. So there is an element of fraud there.  
 23 MR JUSTICE BARLING: Yes.  
 24 MR BREALEY: But when it comes to default, again, without  
 25 going into the cross-examination, but you do get a sense

1 from MasterCard, where they emphasise the competitive  
 2 nature of the UK market and the issuing banks came along  
 3 and threw money at people who couldn't afford to pay and  
 4 there were defaults, the question is -- and they got  
 5 interest from it and then they defaulted. So why should  
 6 it be that the merchant should pay for the sins of the  
 7 banks who are, on one view, irresponsibly lending?  
 8 You take that and then you actually analyse it under  
 9 article 101(3). So that is just more or less a forensic  
 10 point. Then you analyse it under 101(3), and say: what  
 11 are the efficiencies that are being achieved which merit  
 12 exemption under 101(3)? The guidelines I saw, the "what  
 13 is the link two efficiencies from the MIF".  
 14 MR JUSTICE BARLING: So Mr von Hinten-Reed didn't come down  
 15 in favour of any of that?  
 16 MR BREALEY: No. The reason --  
 17 MR JUSTICE BARLING: I have just forgotten that.  
 18 MR BREALEY: The reason for that is that, as I say, when one  
 19 looks at the guidelines and how the European Court has  
 20 said, so is the MIF indispensable for efficiency gain?  
 21 When you actually analyse it, the answer to that must be  
 22 no, we say. There is no efficiency gain that results  
 23 from the MIF.  
 24 MR JUSTICE BARLING: I couldn't remember now, maybe you  
 25 showed us a diagram of a shaded area, quite what the

1 shaded area included and what it didn't include. Don't  
 2 worry, I can look it up.  
 3 MR BREALEY: That shaded area is purely and simply the  
 4 transactional benefits.  
 5 MR JUSTICE BARLING: Right. Yes.  
 6 MR BREALEY: It is a little bit more than that. It is the  
 7 benefits of accepting the card and, as I understand it,  
 8 it is primarily transactional benefits, but there may be  
 9 an element of fraud there because you are saving  
 10 elsewhere on fraud --  
 11 MR JUSTICE BARLING: That's probably what I might have been  
 12 thinking of, but there might be something else.  
 13 MR BREALEY: There is a something else and that's why when  
 14 you take out the humongous bit of the cost of credit,  
 15 really, it matters.  
 16 But I take the point about the debit card and I will  
 17 discuss that with Mr von Hinten-Reed.  
 18 MR JUSTICE BARLING: Thank you very much, Mr Brealey.  
 19 MR BREALEY: Thank you.  
 20 (11.30 am)  
 21 (A short break)  
 22 (12.00 pm)  
 23 Opening submissions by MR HOSKINS  
 24 MR HOSKINS: I would like to do three things in my opening  
 25 submissions. First of all, identify what are the

1 questions you need to consider with some degree of  
2 specificity, and in doing so I will follow the structure  
3 of the questions that we set out at paragraph 441 of our  
4 skeleton argument. You will see we have already adopted  
5 a structure.

6 It is A, tab 2, page 295. So that is the structure  
7 I'm going to follow, but obviously developing those  
8 points.

9 MR JUSTICE BARLING: Right.

10 MR HOSKINS: There is an awful lot of stuff in this case and  
11 unless one gives oneself a structure you get lost quite  
12 quickly, so that is the structure we propose.

13 The second thing I would like to do is establish the  
14 relevant legal principles, where it is relevant. The  
15 third thing I would like to do is identify what the  
16 differences are between the parties, and that can  
17 include on the evidence, whether it be factual or  
18 expert, we say X, Sainsbury's say Y. But for obvious  
19 reasons I'm not going to try to enter too much into the  
20 fray of the evidence, I'm just trying to identify the  
21 lines between the parties because one never knows what  
22 will happen with live witnesses.

23 So those are the three things I would like to do.

24 For a bit of variety, so you don't have to listen to  
25 me the whole time, you will be glad that Mr Cook is

1 going to deal with compound interest and ex turpi causa,  
2 and he will also deal with the association of  
3 undertakings issues because there is a certain degree of  
4 crossover between them. So at the appropriate moment  
5 you will be hearing from Mr Cook.

6 Let me plunge in: restriction of competition or, as  
7 we would say, no restriction of competition.

8 Our submission is that in the particular  
9 circumstances of the UK market, during the period of the  
10 claim, the MasterCard domestic UK MIF was either  
11 objectively necessary or it was not a restriction of  
12 competition that falls or fell within article 101(1).

13 There is a certain common legal base to both those  
14 questions, but one of the things I want to do is  
15 disentangle what the principles are in relation to each  
16 of those questions.

17 I start with what we say is the prize evidence in  
18 the case, which is the evidence in relation to Maestro.  
19 Because what the Maestro experience shows us is that the  
20 commercial impact of a material difference in the level  
21 of interchange fees offered by different payment card  
22 schemes was dramatically demonstrated by what happened  
23 in relation to Maestro.

24 Let me just show you the evidence that is before the  
25 Tribunal on that. First of all, can you go to

1 bundle C2, tab 2. This is a witness statement of  
2 a MasterCard witness, Mr Douglas. You have probably  
3 read it already, but just to refresh your memory in  
4 relation to paragraphs 28 to 37 of that witness  
5 statement, that's at page 29.

6 (Pause)

7 To summarise, paragraph 28, early 2000s, healthy  
8 competition in the debit card market in the UK.  
9 Paragraph 29, the bilateral rates, because there was  
10 a bilateral system, but in practice they were set at the  
11 level of the MIF. Paragraph 30, due to particular  
12 commercial background, MasterCard did not have power to  
13 set the MIF rates for Maestro; it was stuck with rates  
14 set by someone else. Paragraph 31, in the early to  
15 mid-2000s that meant that the Switch/Maestro/MasterCard  
16 debit interchange rate was significantly lower than  
17 Visa's. Paragraph 35, that disparity resulted in  
18 a collapse of the Maestro market share to below 3%.

19 Paragraphs 36 and 37, MasterCard tries to do  
20 something about it by launching its own debit card  
21 product, but it was too little too late. But that's  
22 important. I'll come back to it when I come to credit  
23 cards.

24 When it sticks at 3%, the reason it stuck at 3% is  
25 because MasterCard was able to launch a product with

1 a higher MIF to match Visa, and we will submit that's  
2 why it retained any market share at all. But I will  
3 return to that point when I come to credit.

4 Just to keep showing you what the evidence is on  
5 this, if we could go to bundle D3, tab 3, this is the  
6 first expert report of Dr Niels. If you could turn to  
7 page 265.

8 Again, I simply want to refresh your memory about  
9 looking at paragraphs 386 to 389, which includes  
10 something called box 3.1. But you will see it, there's  
11 a lot of drawn ... because it relies on Mr Douglas'  
12 evidence.

13 Then for a graphic illustration of what happened to  
14 the market shares, so if you can turn to page 249, you  
15 will see figure 3.3, which just plots the market shares  
16 for debit cards in the UK. And MasterCard are dark blue  
17 at the bottom and you will see the cliff that they  
18 fall off.

19 I should say this figure is reproduced in our  
20 skeleton argument at A, tab 2, page 172, and that's the  
21 one I showed you I think on the first day of the trial.  
22 But this is the same table.

23 Note the dates of the effect. A reduction begins,  
24 2004, there is a little plateau and then it really goes  
25 downhill after 2008 because it takes time for banks to

1 switch. There is a degree of lag and that's why one  
 2 sees that shape.  
 3 But what's important is that the cliff post-dates  
 4 the Commission's 2002 Visa decision; the cliff  
 5 post-dates the Commission's MasterCard decision in 2007.  
 6 One theme I will keep coming back to, but it is  
 7 important to remember, is that when one looks at the  
 8 General Court and the Court of Justice's judgments, they  
 9 are effectively a judicial review of the MasterCard 2000  
 10 decision.  
 11 So Mr Brealey was positing "I wonder if this could  
 12 have been before the Commission?" Well, it certainly  
 13 wasn't before the Commission because the cliff  
 14 post-dates the decision, nor could it have been before  
 15 the General Court or the Court of Justice because they  
 16 have to review the legality of the decision on the basis  
 17 of the material that was before the Commission.  
 18 So we say that the Maestro experience in the UK  
 19 proves that if there is a material difference in the  
 20 level of interchange fees offered by competing payment  
 21 card schemes, the scheme offering the lower level will  
 22 suffer a catastrophic loss of market share. Mr Brealey  
 23 beat the drum and said "We don't accept this, we are  
 24 going to challenge this", well, that's fine, you can do  
 25 that in cross-examination. But there's no factual

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1 evidence from Sainsbury's to challenge the relevance of  
 2 what happened in relation to Maestro and why it  
 3 happened, as Mr Douglas explains, as Dr Niels explains.  
 4 So the fight on that basis will have to be trying to  
 5 poke a hole through our witnesses in cross-examination  
 6 because they don't have their own factual evidence about  
 7 what happened in relation to Maestro.  
 8 So the Commission has never considered the UK MIF at  
 9 all, nor has it considered this evidence specific to the  
 10 UK market. The only decision in relation to the UK MIF  
 11 there has ever been was by the OFT, and you will be  
 12 aware that that case collapsed when the OFT tried to  
 13 change its case and the decision was overturned by  
 14 the CAT.  
 15 There is a question of, well, to what extent, then,  
 16 is the Tribunal bound by the Commission decision? We  
 17 have set out the legal principles on the effect of  
 18 Commission decisions in the statute and in the  
 19 regulation. That's paragraphs 114 to 123 of our  
 20 skeleton argument, bundle A, tab 2, page 198.  
 21 Our submission is that while the Tribunal of course  
 22 may well be assisted by reference to the Commission  
 23 decision, it's not bound by it. Mr Brealey accepted  
 24 that yesterday. The reference is transcript Day 2,  
 25 page 16.

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1 So we say that the Tribunal's task is to determine  
 2 the particular issues raised before it on the basis of  
 3 the evidence presented to it, including the Maestro  
 4 experience. Let me come back to the mechanics of what  
 5 happened this Maestro. Why did a difference in  
 6 interchange fees produce such a dramatic effect?  
 7 We need to go back to Mr Douglas' witness statement  
 8 for this. So that is C2, tab 2, page 29. I'm sorry,  
 9 I'm going to pick it up at page 25. You will see at  
 10 paragraph 13, the heading:  
 11 "How banks decide which scheme's card to issue."  
 12 If you can refresh your memory on paragraphs 13  
 13 to 15, paragraph 18 and paragraph 20. So that is 13  
 14 to 15, 18 and 20.  
 15 MR JUSTICE BARLING: Thank you.  
 16 (Pause)  
 17 MR HOSKINS: So that is the evidence about the importance of  
 18 rate of interchange fees offered in terms of issuing  
 19 banks choosing which cards to issue, ie competition  
 20 between payment card schemes to get issuers to issue  
 21 their cards.  
 22 An important point at paragraph 21:  
 23 "This intense focus on ...(Reading to the words)...  
 24 not cross-border rates since between 98% and 99% of card  
 25 transaction volumes in the UK were generated by domestic

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1 transactions."  
 2 This is a crucial difference between this case and  
 3 the Commission decision because the Commission decision  
 4 deals with, dealt with, intra EEA MIFs only and you  
 5 don't have the same competitive dynamic for cross-border  
 6 MIFs as you do for purely domestic MIFs.  
 7 Mr Brealey sort of rattled his shield, he is going  
 8 to challenge this, fine. Let's see what  
 9 Mr von Hinten-Reed said about this dynamic, his first  
 10 report, that's D2, tab 2, paragraph 513. Again, if  
 11 I can invite you to refresh your memory, paragraphs 513  
 12 to 523. (Pause)  
 13 There are two particularly important points made by  
 14 Sainsbury's expert here in relation to competitive  
 15 dynamics. The first one is the last sentence of  
 16 paragraph 516:  
 17 "As noted by the Commission, issuers are members of  
 18 both the Visa and MasterCard schemes and are therefore  
 19 likely to choose whichever of the two brands of cards  
 20 offers the highest interchange fees, competition between  
 21 the schemes, based on the interchange fees offered."  
 22 And 520:  
 23 "In competing for issuers to issue their cards, Visa  
 24 and MasterCard have a very strong incentive to increase  
 25 interchange fees."

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1 The schemes compete between themselves through the  
2 interchange fees they offer. That's Sainsbury's expert  
3 evidence and it confirms the competitive dynamic that  
4 I am talking about. The level of the MIF is a critical  
5 driver of competition between payment systems.

6 What's the significance of the fact that competition  
7 in this case puts an upward pressure on the MIFs?  
8 Because of course one thinks of the classic example of  
9 competition putting a downward pressure on prices of  
10 whatever, but here competition has the opposite effect.

11 Well, take a step back. It is not unusual for  
12 undertakings to compete by seeking to offer more  
13 attractive financial offers than its competitors. The  
14 classic example is an auction.

15 PROFESSOR JOHN BEATH: Yes, it is an auction for customers.

16 MR HOSKINS: An auction is by definition a fantastic example  
17 of competition, but what's the effect of an auction?

18 You get a higher price. That's why people have them.

19 And this isn't me giving evidence, but it is  
20 anecdotal and you will put whatever weight on it you  
21 want, but a very good example of competition leading to  
22 higher prices is demonstrated by the position in  
23 relation to live football rights. Because in relation  
24 to live football rights what happened to many years is  
25 Sky bought them all and this was seen to be

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1 a competition problem. I'm not going to go into pay TV,  
2 seeing everyone's faces.

3 So the Commission said "This is not good for  
4 competition because Sky is buying all the rights every  
5 time", so you have to actually set up a system where  
6 people can bid for the rights and not one person can buy  
7 all the rights. And that's what happened, and look  
8 what's happened: The most recent auction has created  
9 this astronomical uplift in the fees the television  
10 companies are paying for the rights. And again, forgive  
11 me if this is me giving evidence -- treat it as  
12 anecdotal -- I sit at home and watch, and the prices I'm  
13 paying as a consumer to watch Arsenal lose to Chelsea  
14 every season have gone up. But that is the effect of  
15 a competitive process that the Commission has insisted  
16 on, that it pushes prices up.

17 So one cannot simply say that because some sort of  
18 mechanism, here a competitive mechanism, results in  
19 a higher price, there is a competitive problem.

20 A higher price, a level of price is not in itself  
21 a competition law issue. It might be a reason why  
22 a regulator gets concerned and sees whether it should  
23 apply competition law or, indeed, regulation, but a high  
24 price for a high level is not in itself a competition  
25 law issue. What competition law is concerned about is

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1 the mechanics by which a particular price is reached.

2 If one looks purely at a concern with the level of  
3 prices, as I have submitted, it is not a competition  
4 concern per se but it can be a regulatory concern. And  
5 that's actually now what's happened in relation to MIFs,  
6 as we know. Because we have had regulation, 2015/751  
7 has been adopted.

8 If we can look at that. It is in bundle I1 at  
9 tab 6. You will see under the bold heading before we  
10 get to the formal recitals, there is:

11 "The European Parliaments ... the Council of the  
12 European Union, having regard to the treaty on the  
13 functioning of the European Union, in particular  
14 article 114(1) thereof ..."

15 Article 114 has nothing to do with competition, it  
16 is the legal basis for harmonisation for internal market  
17 purposes. So this is a harmonisation piece of  
18 legislation.

19 Recitals 1 and 7. 1:

20 "Fragmentation of the internal market is detrimental  
21 to competitiveness growth and job creation within the  
22 Union ...(Reading to the words)... of an integrated  
23 market for electronic payments with no distinction  
24 between national and cross-border payments is necessary  
25 for the proper functioning of the internal market."

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1 7, I will ask you to read it rather than have me  
2 canter through it, if that's all right.

3 MR JUSTICE BARLING: Sorry, which bit do you want us to  
4 read?

5 MR HOSKINS: Recital 7.

6 MR JUSTICE BARLING: Yes.

7 MR HOSKINS: So you see it is the classic reason for needing  
8 EU harmonising legislation, otherwise there would be  
9 a disparity in legislation between member states.

10 Recitals 10 and 11 are interesting because they  
11 recognise and accept the competitive dynamic I've  
12 described of schemes competing by offering higher  
13 interchange fees. So if I can ask you to read 10  
14 and 11, hopefully that point will leap out at you.

15 So the Commission accepts the dynamic I'm  
16 describing. The need for harmonisation, indeed the  
17 relationship between harmonisation and competition law,  
18 you will see that in recitals 12 to 14. Competition law  
19 hasn't worked so we are going to adopt a regulation. It  
20 is without prejudice to any competition law issues that  
21 may arise. That's 12 to 14.

22 The solution, recital 18: all debit and credit card  
23 based payment transactions shall be subject to maximum  
24 interchange fee rate.

25 20 then tells us how the Commission has gone about

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1 coming up with a rate, the so-called merchant  
2 indifference test. I will take you through other  
3 examples, but here is the first example we have seen of  
4 the MIT being used as a proxy.

5 The Commission isn't going through every limb of  
6 101(3), but you will see from the language of recital 20  
7 that it reflects what one finds in the 101(3)  
8 conditions. But The Ommission, we will see, has on  
9 a number of occasions said if it is an appropriate proxy  
10 you don't have to go through 101(3). That's the way we  
11 satisfy ourselves.

12 Then those limits, pan-European limits, you find  
13 given effect to in articles 3(1) for debit cards and  
14 article 4 for credit cards. Then there's a particular  
15 concern, and it is something you will have seen in the  
16 evidence, that's strongly shared by MasterCard about,  
17 well, what about Amex and what about other three-party  
18 schemes?

19 There is a solution in the regulation. You see it  
20 at recital 28. This is important because, again, the  
21 experts continually clash on the extent to which it is  
22 relevant to look at Amex.

23 What the Union has decided in the regulation is  
24 that:

25 "To acknowledge the existence of implicit

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1 interchange fees that contribute to the creation of  
2 a level playing field, three-party payment card schemes  
3 using payment service providers as issuers or acquirers  
4 should be considered as four-party payment card schemes  
5 and should follow the same rules as ...(Reading to the  
6 words)... to all providers."

7 Then there is a transitional period. That level  
8 playing field is given effect to by article 1(5).

9 So it is not all three-party schemes, but it is  
10 where they use licensees to issue and acquire, for  
11 example, Amex GNS scheme in --

12 MR JUSTICE BARLING: The 3.5 scheme.

13 MR HOSKINS: Correct.

14 MR JUSTICE BARLING: This would apply to Amex here?

15 MR HOSKINS: Then article 2(18), it is the same point we  
16 have seen in the recitals, you see how the definition of  
17 three-party payment card schemes are treated as  
18 four-party schemes where there are 3.5 schemes, if I can  
19 mix numerals.

20 Then the implementation date is at article 18(2).  
21 The common caps applied from 9th September 2015. Now,  
22 the difference between a regulatory approach such as  
23 this and a competition law approach is that the Maestro  
24 problem doesn't arise under the regulatory approach.  
25 The trouble with competition is if you go after one

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1 person but not the other, you create the Maestro  
2 problem. With the regulation, everyone has the same  
3 rule in relation to MIF at the same time. Therefore, no  
4 Maestro problem. All payment service providers are  
5 subject to the same limit at the same time, including  
6 certain third party schemes.

7 Neither side, interestingly, has actually said the  
8 easy answer for you is take the rates here and apply  
9 them to the UK. The reason we say that is really two  
10 reasons: first of all, the case you are considering is  
11 a competition case. You have the Maestro problem. So  
12 what you have here is a regulatory solution which  
13 applies the same rate to everyone at the same time, and  
14 I will come on to the crucial point between us, which is  
15 the proper counterfactual as a matter of law.

16 But our submission is if we are right in our  
17 counterfactual as a matter of law, then you can't simply  
18 go to this and say "There you are, 0.3 and 0.2". But  
19 there is another problem, which is this is  
20 a pan-European level, and as we will see when we go  
21 through the materials, including some of the Commission  
22 materials, it is quite clear that the Commission  
23 contemplates that there can and should be specific  
24 consideration for particular domestic markets.

25 You will have seen from the evidence there is

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1 a great deal of discussion about the differences between  
2 different member states, for example, credit cards are  
3 far more prevalent in the UK etc. So this is not, I'm  
4 afraid, an off-the-shelf answer, and neither party is  
5 suggesting it is, that you simply say "Aha, here is  
6 a regulation, it is 0.3 and 0.2, that's the answer".  
7 And that's the reason we say it is not. Sainsbury's  
8 haven't specified, and they equally do not say "Simply  
9 take this off the peg".

10 Let me then switch to the law. As I have said in  
11 relation to restriction of competition, the Tribunal has  
12 to consider two questions. First, was the UK MIF  
13 an ancillary restraint? Was it objectively necessary.  
14 Alternatively, if it was not an ancillary restraint, was  
15 a restriction of competition within the meaning of  
16 article 101(1)? That's almost tautologous, but you can  
17 have restrictions that don't fall within 101(1).

18 The legal framework. I will come onto exemption  
19 later, but on this issue is the MasterCard judgment of  
20 the Court of Justice of the European Union. Essentially  
21 we have had it bottom up because Mr Brealey took you in  
22 detail to the Commission decision, took you to the  
23 general law, but what matters on the law is what the  
24 Court of Justice said, so let's go to the Court of  
25 Justice. It is in bundle E1, tab 19.

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1 First of all, I'm going to deal with objective  
 2 necessity. What is the test for objective necessity?  
 3 One finds that in paragraphs 78, 86 and 89 to 94 of the  
 4 judgment. So it is 78, you will see the heading, this  
 5 is dealing with objective necessity:  
 6 "The General Court carried out an assessment of the  
 7 objective necessity of the MIF before addressing the  
 8 question as to whether those fees produced  
 9 anti-competitive effects. In those circumstances, it is  
 10 appropriate to examine the plea concerning the ancillary  
 11 nature of the MIF before addressing possibly restrictive  
 12 effects."  
 13 This is what we are dealing with.  
 14 At 86, you get the arguments of the parties:  
 15 "The appellants [so including MasterCard] submit  
 16 that the General Court misapplied the test of objective  
 17 necessity over restriction. Instead of applying the  
 18 test under which a given limitation on commercial  
 19 autonomy is...(Reading to the words)... applied in its  
 20 judgment an incomplete test according to which  
 21 a restriction is objectively necessary only if without  
 22 it the main operation is incapable of functioning."  
 23 So that was MasterCard's argument to the Court of  
 24 Justice.  
 25 Then the court's analysis is to be found at

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1 paragraphs 89 to 94. I think, as long as you are happy  
 2 with this, if you could read 89 to 94, then I will make  
 3 submissions on it.  
 4 MR JUSTICE BARLING: Yes, we will read those.  
 5 MR HOSKINS: It is really for the shorthand writers as well,  
 6 so they don't have any gabbling at speed.  
 7 (Pause)  
 8 Is it a high test? Oh yes, it is. We don't shy  
 9 from that.  
 10 Paragraph 91:  
 11 "It is necessary to inquire whether that operation  
 12 would be impossible to carry out in the absence of the  
 13 restriction in question."  
 14 The fact that the operation is simply more difficult  
 15 to implement or even less profitable without the  
 16 restriction concerned is not sufficient.  
 17 Paragraph 93, the last sentence of it:  
 18 "The objective necessity test concerns the question  
 19 whether, in the absence of a given restriction of  
 20 commercial autonomy, the main operation would be likely  
 21 not to be implemented or not to proceed."  
 22 I will come back to that because that actually is  
 23 an echo. It is obviously a reflection of one of the  
 24 classic and early community cases on ancillary  
 25 restraint, which is Société Technique Minière, or STM,

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1 which is from something like 1963, which dealt with  
 2 ancillary restraints necessary to break into new  
 3 markets.  
 4 I will come back to that in a bit. I put down that  
 5 flag now that what you see here is the court saying in  
 6 2000, and whenever this was, I forget -- 2014 -- what it  
 7 was basically saying in 1963 about ancillary restraints:  
 8 The main operation would be likely not to be implemented  
 9 or not to proceed.  
 10 But it is a high test. I don't shy from that.  
 11 That's the test for objective necessity. What's the  
 12 relevant counterfactual to see whether that test is  
 13 satisfied? If we look at paragraph 96 you get the  
 14 arguments of the parties. Again, if you could read  
 15 that.  
 16 (Pause)  
 17 The big point from that is that the argument that  
 18 was being made is that, in relation to objective  
 19 necessity, the Commission relied on a counterfactual,  
 20 a prohibition on ex-post pricing, which MasterCard said  
 21 would never in fact have occurred. Then the findings of  
 22 the court on this begin at 105, but if we could pick it  
 23 up at 108:  
 24 "Irrespective of the context or aim...(Reading to  
 25 the words)... counterfactual is used."

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1 Because we use a counterfactual both for  
 2 an objective necessity and for restriction of  
 3 competition. But regardless of what you are using the  
 4 counterfactual for:  
 5 "It is important that that hypothesis is appropriate  
 6 to the issue it is supposed to clarify and that the  
 7 assumption on which it is based is not unrealistic."  
 8 That's clearly one of the main battlegrounds.  
 9 I will make submissions to you in a little bit about why  
 10 our counterfactual is in accordance with the law and is  
 11 realistic. I will show you why and Mr Brealey's is not.  
 12 Then 111, this is dealing particularly with the  
 13 counterfactual for objective necessity:  
 14 "The alternatives on which the Commission may rely  
 15 in the context of the assessment of the objective  
 16 necessity of a restriction are not limited to the  
 17 situation that would arise in the absence of the  
 18 restriction in question, but may also extend to other  
 19 counterfactual hypotheses based inter alia on realistic  
 20 situations that might arise in the absence of that  
 21 restriction.  
 22 "The General Court was therefore correct in  
 23 concluding in paragraph 99 of the judgment under appeal  
 24 that the counterfactual hypothesis put forward by  
 25 the Commission could be taken into account in the

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1 examination of the objective necessity of the MIF  
 2 insofar as it was realistic and enabled the MasterCard  
 3 system to be economically viable."  
 4 Now, the language is difficult in its nuance, but  
 5 hopefully it will become clearer when we come to what  
 6 the counterfactual is for the restriction of  
 7 competition. And the crucial difference, one sees it  
 8 already coming in the language of 111, for a restriction  
 9 of competition, you have to consider what would in fact  
 10 have arisen in the absence of the restriction, whereas  
 11 for an objective necessity, the counterfactual is not so  
 12 limited. It still has to be realistic, but it can be  
 13 a counterfactual that might arise insofar as it is both  
 14 realistic and enabled the system to be economically  
 15 viable.  
 16 I will flesh out what that difference means as best  
 17 I can because it becomes a bit clearer in the case law.  
 18 But you will see the court is trying to draw  
 19 a distinction and you will see the language it uses to  
 20 draw a distinction.  
 21 MR JUSTICE BARLING: You say in 111 that the court isn't  
 22 there saying that it is realistic, that the Commission  
 23 is right to say it is realistic. Are they saying that  
 24 they were right to take it into account insofar as it  
 25 was realistic and that was something the Commission

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1 thought it was?  
 2 MR HOSKINS: I'm going to come onto what the court said  
 3 about whether it fulfilled the condition, whether it was  
 4 a realistic counterfactual which enabled MasterCard to  
 5 be economically viable. But at the moment I'm just  
 6 looking at what the test is, and then that's the next  
 7 stage is, well, what did the court find in relation to  
 8 that particular proposed counterfactual on objective  
 9 necessity.  
 10 But what we say is that what this shows us,  
 11 paragraph 111 shows us, is that the counterfactual for  
 12 objective necessity must be realistic and must enable  
 13 the MasterCard system to be economically viable.  
 14 Let me switch from objective necessity, the law on  
 15 objective necessity, to what the law is on restriction  
 16 of competition. Again, I will do it in two steps.  
 17 First of all, what is the test, and secondly, how you  
 18 identify the relevant counterfactuals.  
 19 First of all, what is the test. Mr Brealey referred  
 20 to the O2 (Germany) case. I would like to take you to  
 21 that. It is in bundle I3 at tab 9.  
 22 I'm not going to go into all the facts of the case,  
 23 I don't think I need to, but just to see what the court  
 24 was considering. If we go to page 349, you will see  
 25 that this section of the judgment is in italics, is

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1 concerning the first plea, alleging that there is no  
 2 restriction of competition and that the competitive  
 3 situation has been insufficiently analysed.  
 4 Then the findings of the court in relation to that  
 5 plea begin at page 353 of the bundle, paragraph 66:  
 6 "In order to assess whether an agreement is  
 7 compatible with the common market in the light of  
 8 article 81(1), it is necessary to examine the economic  
 9 and legal context in which the agreement was concluded,  
 10 its object, its effects and whether it affects  
 11 intra-community trade taking into account the particular  
 12 economic context in which the undertakings operate, the  
 13 products or services covered by the agreement and the  
 14 structure of the market concerned and the actual  
 15 conditions in which it functions."  
 16 I'm going to labour that, I make no apology for it.  
 17 And this formulation, one finds it again and again  
 18 in the relevant case law. This is a standard type of  
 19 language that one finds cut and pasted into judgments  
 20 dealing with the same issue.  
 21 68:  
 22 "Moreover, in a case such as this, where it is  
 23 accepted that the agreement does not have its object as  
 24 the restriction of competition, the effects of the  
 25 agreement should be considered, and for it to be caught

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1 by the prohibition it is necessary to find that those  
 2 factors are present which show that competition has in  
 3 fact been prevented or restricted or distorted to  
 4 an appreciable extent."  
 5 Again, it is the same point I'm labelling:  
 6 "The competition in question must be understood  
 7 within the actual context in which it would occur in the  
 8 absence of the agreement in dispute."  
 9 71:  
 10 "The examination required in the light of  
 11 article 81(1) consists essentially in taking account of  
 12 the impact of the agreement on existing and potential  
 13 competition and the competition situation in the absence  
 14 of the agreement."  
 15 Those two factors being intrinsically linked. So  
 16 that is where the counterfactual comes in in order to  
 17 determine where there is a restriction of competition  
 18 you have to look at the state of competition as it is  
 19 with the restriction and the state of competition as it  
 20 actually would be without the restriction.  
 21 73:  
 22 "In order to take account of the two parts which  
 23 this plea actually contains, it is therefore necessary  
 24 to examine, first, whether the Commission did in fact  
 25 consider what the competition situation would have been

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1 in the absence of the agreement, and second, whether the  
2 conclusions which it drew from its examination of the  
3 impact to the agreement and competition are sufficiently  
4 substantiated."

5 So you have to consider what the competition  
6 situation would have been in the absence of the  
7 agreement.

8 Here that would be in the absence of the MIF, the  
9 MasterCard MIF, because that's the agreement we are  
10 looking at. So that is what we say the court has to do  
11 here, the Tribunal has to do here: it has to consider  
12 what the competition situation would have been in the  
13 absence of the MasterCard MIF.

14 You have seen already to an extent O2 deals with  
15 what the relevant counterfactual is, but it is also  
16 considered by the Court of Justice in the MasterCard  
17 judgments. So I can go back to that. That was E1,  
18 tab 19.

19 If we can pick this up at paragraph 127. This was  
20 an argument that was put by Royal Bank of Scotland.  
21 I acted for Royal Bank of Scotland in this case, not  
22 MasterCard, not that that makes any difference.

23 127:

24 "RBS maintains that in relying on general  
25 considerations and assumptions, the General Court erred

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1 in law on its assessment of the existence of a  
2 restrictive effect on competition. First of all, in  
3 assessing whether an decision has a restrictive effect  
4 on competition, the Commission should have considered  
5 what the actual counterfactual hypothesis would have  
6 been in the absence of the MIF. By not penalising that  
7 omission and by thus relying solely on the economic  
8 viability of the ...(Reading to the words)... rather  
9 than on any consideration of the likelihood of such  
10 a prohibition actually being adopted, the General Court  
11 erred in law by confusing the legal conditions for  
12 objective necessity and those for effects on  
13 competition."

14 So that was our submission, and we relied on O2  
15 because what the General Court had done was it just took  
16 the test for objective necessity and applied the same  
17 test to restriction of competition. And we said that's  
18 wrong, see O2. And the court agreed with us, agreed  
19 with the Royal Bank of Scotland. That's paragraphs 161  
20 to 169.

21 Again, that's quite a long passage. Could you read  
22 that to yourself, please? 161 to 169. (Pause)

23 Royal Bank of Scotland was right, the General Court  
24 had committed an error of law by eliding the appropriate  
25 counterfactuals for objective necessity and restriction

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1 of competition.

2 Just to unpick that, paragraph 163:

3 "The same counterfactual hypothesis is not  
4 necessarily appropriate to conceptually distinct issues.  
5 Where it is a matter of establishing whether the MIF  
6 have restrictive effects on competition, the question  
7 whether without those fees that by the effect of  
8 prohibiting ex-post pricing open payment systems such as  
9 the MasterCard system could remain viable is not in  
10 itself decisive."

11 So the objective necessity test is not the same as  
12 the restriction of competition test.

13 164:

14 "By contrast, the court should, to that end,  
15 assessing a restriction of competition, assess the  
16 impact of the setting of the MIF on the parameters of  
17 competition, such as the price, the quantity and quality  
18 of the goods or services. Accordingly, it is necessary  
19 to assess the competition in question within the actual  
20 context in which it would occur in the absence of those  
21 fees."

22 The MasterCard MIF fees.

23 166:

24 "It follows from this that the scenario envisaged on  
25 the basis of the hypothesis that the coordination

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1 arrangements in question are absent must be realistic.  
2 From that perspective it is permissible where  
3 appropriate to take account of the likely developments  
4 that would occur on the market in the absence of those  
5 arrangements."

6 Having seen that, can I invite you just to go back  
7 to 111, which you read before, because I think the court  
8 is making the same distinction there. But once one has  
9 seen the passages we have just seen, I think that  
10 distinction the court is trying to make between, for  
11 objective necessity, a realistic hypothesis that might  
12 arise, and for a restriction of competition, a realistic  
13 competition that would on the facts arise absent the  
14 MIF. That is the distinction they are trying to draw.

15 And the test is therefore more difficult to satisfy  
16 for objective necessity than for restriction of  
17 competition.

18 There is one really important point that comes out  
19 of paragraph 167:

20 "In the present case, the General Court did not in  
21 any way address the likelihood or even plausibility of  
22 the prohibition of ex-post pricing if there was no MIF  
23 in the context of its analysis of the restrictive  
24 effects of those fees. In particular, it did not  
25 address the issue as to how [this is the important bit]

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1 taking into account in particular to which the  
2 obligations to which merchants and acquiring banks are  
3 subjects under the honour all cards rule, which is not  
4 the subject of the decision at issue, the issuing banks  
5 ...(Reading to the words)... settlement of bank card  
6 transactions."

7 So what this tells you is that when you are carrying  
8 out the analysis, whether it is objective necessity or  
9 restriction of competition, you have to carry out the  
10 analysis taking the scheme as you find it.

11 The only thing that can switch between the  
12 counterfactuals is the alleged restriction. So, for  
13 example, here in both counterfactuals, whether it is  
14 objective necessity or restriction of competition, so  
15 the counterfactual for each, you have to assume that the  
16 honour all cards rule exists in each because it is not  
17 challenged.

18 We submit that must go for the rest of the scheme.  
19 For example, insofar as the scheme provides for  
20 guaranteed payment in event of default, or in event of  
21 fraud, you have to take the scheme as it finds it  
22 because they are not alleged to be restrictions of  
23 competition by Sainsbury's.

24 So the counterfactual, whatever it may be, and  
25 I will come to that, has to take the scheme as it finds

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1 it, and the only thing that changes, as you are looking  
2 at the scheme, with UK domestic MIF, MasterCard domestic  
3 MIF, or a scheme without UK domestic MasterCard. And  
4 that's crucial, 167, for that reason.

5 It is 12.59 and that would be a good place for me  
6 to stop.

7 MR JUSTICE BARLING: Good. Thank you very much.

8 MR HOSKINS: Thank you.

9 (1.00 pm)

10 (The short adjournment)

11 (2.00 pm)

12 MR HOSKINS: Good afternoon.

13 MR JUSTICE BARLING: Mr Hoskins.

14 MR HOSKINS: The next point I wanted to look at on the law  
15 relates to restriction of competition, as opposed to  
16 objective necessity.

17 What I want to show you is as a matter of law, when  
18 you are considering where there is a restriction of  
19 competition, so when you are comparing the actual  
20 position that existed with the counterfactual, you have  
21 to take account of competition in both the issuing and  
22 acquiring markets.

23 That's not a market definition point. This assumes  
24 that there is a relevant market in acquiring and there  
25 is a separate product market in issuing. But even if

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1 they are separate markets in that sense, for the  
2 competition analysis, you still have to look at both of  
3 them.

4 MR JUSTICE BARLING: Is that because even when you are  
5 looking at the effect on competition in the acquiring  
6 market, isolating that, you still have to look at --

7 MR HOSKINS: No. It is when you are looking at O2, you are  
8 looking at the actual state of competition with the MIF,  
9 what the state of competition would be without the  
10 MIF --

11 MR JUSTICE BARLING: But on which market?

12 MR HOSKINS: Let me show you the case and I think it will  
13 answer your question.

14 It is the MasterCard case again, so we are in E1.19.

15 (Pause)

16 Paragraphs 177 to 179. Again, if you could please  
17 read those. Actually, 176 to 179. You get the argument  
18 in 176. (Pause)

19 You see from 177 the court says:

20 "In order to determine whether coordination between  
21 undertakings must be considered to be prohibited by  
22 reason of the distortion of competition which it  
23 creates, it is necessary to take into account any factor  
24 which is relevant."

25 Then we get the recitation of the factors that we've

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1 seen before.

2 Final words:

3 "... regardless of whether or not such a factor  
4 concerns the relevant market."

5 Then in 178, the Court of Justice notes that the  
6 General Court found that there was an interaction  
7 between the issuing and acquiring markets. So even  
8 although the General Court was focusing on the acquiring  
9 market, it was established that there was an interaction  
10 between the issuing and acquiring markets.

11 Then what the Court of Justice tells us in 179:

12 "In those circumstances, the economic and legal  
13 context of the coordination concerned..."

14 Let's call it the O2 point, if you like. That is  
15 looking at the (inaudible) factors, each of the  
16 counterfactuals:

17 "... includes the two-sided nature of MasterCard's  
18 open payment system particularly since it is undisputed  
19 that there is interaction between the two sides of that  
20 system."

21 So when you are considering where there is  
22 a restriction of competition, you have to take account  
23 of the relevant factors in issuing and acquiring markets  
24 to judge whether there is restriction of competition.  
25 You are not just looking at the acquiring market.

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1 MR JUSTICE BARLING: Yes, but it seems to be on the premise  
2 that what you are looking at is the restriction of  
3 competition on the relevant market, namely the acquiring  
4 market.  
5 MR HOSKINS: Do you mean to find whether there is  
6 a restriction of competition?  
7 MR JUSTICE BARLING: Yes.  
8 MR HOSKINS: Sorry, yes. But in order to determine that,  
9 you need to look at both.  
10 MR JUSTICE BARLING: Because there's a linkage.  
11 MR HOSKINS: That is correct. This is a Pyrrhic victory,  
12 actually both of these points were, because whilst the  
13 Court of Justice agreed with the banks, with Royal Bank  
14 of Scotland and Lloyds, about the law, it then in the  
15 circumstances of the case said it didn't help them.  
16 So here we see 180 to 181.  
17 "In the present case, the arguments essentially put  
18 before the General Court, which are not contested in the  
19 present appeal, did not include the argument now  
20 advanced."  
21 According to which, in order to assess a restriction  
22 of competition in its proper context it is necessary to  
23 take into account the two-sided nature of the system in  
24 question.  
25 So the court agreed with the law. And that's quite

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1 a good summary in 180 of what the legal position is, but  
2 said "But you didn't raise it before, so you can't win  
3 on it now".  
4 So this point wasn't live in relation to the 07  
5 decision. So what we get from the EC judge: this is the  
6 principle, ECJ didn't have to apply it because it hadn't  
7 been raised at the right time, if its raised before you  
8 then that is the principle you have to apply.  
9 This is really important because when Mr Brealey  
10 says this argument, the Maestro argument, is a 101(3)  
11 argument, he is wrong because of this. Because what  
12 this tells us, remember the O2 restriction of  
13 competition, what's the actual state of competition that  
14 existed with the domestic MasterCard UK MIF? Compare it  
15 with the counterfactual that would have existed absent  
16 the MasterCard domestic UK MIF and see what the state of  
17 competition is. Is there a restriction of competition  
18 when you compare those counterfactuals?  
19 And that's in order to determine whether there is  
20 a breach of 101(1). We are not talking here  
21 about 101(3), because 101(3) is about where you have  
22 a restriction which produces benefits and then you have  
23 to consider whether the benefits justify an exemption.  
24 We are not talking about benefits flowing from  
25 restriction here. We are talking about MasterCard's

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1 ability to compete without its domestic UK MIF. That is  
2 a 101(1) point, and that's what this judgment tells us.  
3 MR SMITH: This necessity of taking into account the  
4 two-sided nature of the system, which is quoting from  
5 paragraph 180, the silent assumption is that this is  
6 a feature arising out of a two-sided market.  
7 If you have got a single market, you've simply  
8 stolen the market definition of what is the market we  
9 are talking about, and you look at the effect on  
10 competition in that context.  
11 MR HOSKINS: Yes.  
12 MR SMITH: Whereas here, do correct me if I'm getting this  
13 wrong, you are saying that you have two markets and you  
14 need to be aware of the fact that they are both there,  
15 so you define one market, you define the other one.  
16 How does one deal with a situation where there is  
17 a restriction on competition in market A, one side, but  
18 not in market B, or maybe even beneficial in market B?  
19 How do you trade the two off?  
20 MR HOSKINS: I will come to what my submission is. I will  
21 tell you. I would rather take in sequence --  
22 MR SMITH: I'm sorry, of course.  
23 MR HOSKINS: This is complicated stuff. I'm trying to make  
24 it as simple as possible and I will get confused if  
25 I don't take it in stages. But what I will come to is

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1 I'm going to apply these principles in this case and  
2 I will put the point to you.  
3 But in a sense this is precisely what the Court of  
4 Justice had because remember the Commission in the  
5 General Court had found relevant market, acquiring  
6 market, restriction in acquiring market. Question: is  
7 this a restriction for the purposes of 101? And what  
8 the Court of Justice is saying is in order to answer  
9 that question, you have to look at the issuing and the  
10 acquiring market.  
11 MR JUSTICE BARLING: Forgive me, I want to be absolutely  
12 sure about this. So the argument that they said wasn't  
13 raised was not an argument related to the definition of  
14 the relevant market?  
15 MR HOSKINS: No.  
16 MR JUSTICE BARLING: It was the question of what you could  
17 take account of?  
18 MR HOSKINS: Yes.  
19 MR JUSTICE BARLING: When deciding whether there was  
20 a distortion on the acquiring market?  
21 MR HOSKINS: Correct. This is all on the premise that there  
22 is a separate relevant market in acquiring, there is  
23 an alleged restriction in the acquiring market.  
24 MR JUSTICE BARLING: Separate market because relevant market  
25 has the baggage of being the market you are looking at

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1 to see whether there is a distortion of competition on  
 2 which --  
 3 MR HOSKINS: Yes, the classic "What are the relevant product  
 4 markets?" And the Commission found an acquiring market  
 5 and an issuing market, but as Mr Smith has just noted,  
 6 as the court tells, these are actually linked and  
 7 because they are linked the court says you have to look  
 8 at both to see whether the restriction in one of them  
 9 contravenes 101.  
 10 MR JUSTICE BARLING: Yes, it is part of the context --  
 11 MR HOSKINS: Yes, which we saw, for example, in O2.  
 12 PROFESSOR JOHN BEATH: Yes, you need to worry about if you  
 13 do something, what's the knock-on effect in that other  
 14 market to work out the overall ...  
 15 MR HOSKINS: That is right, absolutely.  
 16 Another aspect of this is of course, Mr Brealey  
 17 repeatedly said that MasterCard's argument in this  
 18 respect is about its profitability. But as I hope is  
 19 clear, our argument isn't taking away the (inaudible) to  
 20 make less money; our argument is that it would drive us  
 21 from the market, objective necessity, or it would  
 22 restrict our ability to compete in a material way.  
 23 I will come to those two distinctions.  
 24 It is not simply about how much money we make. It  
 25 is about whether we exist as a viable four-party scheme,

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1 or it is about whether we are able to compete with  
 2 another four-party scheme and, indeed, a third party  
 3 scheme. It is a competition issue.  
 4 Let me come to the bit I said I would do, which is  
 5 applying the legal principles we have seen to this case.  
 6 And I will do objective necessity first.  
 7 Just to set out the argument, I'm going to take what  
 8 Sainsbury's' proposed counterfactual is for objective  
 9 necessity, because in a sense we say there isn't  
 10 a workable counterfactual. We say we can only work with  
 11 the MIF we had in the context of the UK markets. That's  
 12 why I'm going to take Sainsbury's suggestion to show why  
 13 it doesn't work. Our suggestion is there isn't  
 14 a counterfactual that works.  
 15 It is his first expert report, so it is D2, tab 2,  
 16 page 138, paragraph 93.  
 17 You see, he says:  
 18 "For objective necessity, the counterfactual is  
 19 based on no MIF or a low MIF, plus a role prohibiting  
 20 ex-post pricing or some other rule to avoid the  
 21 gun-to-the-head scenario as played out between acquirers  
 22 and issuers."  
 23 It is the hold-up problem.  
 24 Our submission, our case is that the Maestro  
 25 experience shows that if MasterCard had applied a zero

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1 or a low MIF, as suggested by Sainsbury's, by  
 2 Sainsbury's expert, then Visa would have retained its  
 3 MIFs at the higher level of the actual level they had,  
 4 and this would have decimated our market share.  
 5 We say that's putting it as simply as possible. We  
 6 say that it follows from that, if that's made out on the  
 7 evidence, that it is clear that the actual rate of UK  
 8 domestic MIF, which was applied by MasterCard during the  
 9 period of the claim was therefore objectively necessary  
 10 to allow the MasterCard credit card scheme to operate.  
 11 You remember the graphic presentation of the drop in  
 12 market share in Dr Niels' first report. It is first  
 13 Niels figure 343, but I am not going to take you to it  
 14 again just for the record.  
 15 But you remember that that showed that if -- if you  
 16 want the reference it is D3, tab 3, page 249 -- that the  
 17 market share of the debit card market from MasterCard  
 18 dropping from 3% or less.  
 19 But the scenario, the repetitive scenario in  
 20 relation to credit cards is even worse. I took you to  
 21 first Douglas, paragraphs 28 to 37. That was C2, tab 2,  
 22 page 29. You remember that what he said was that the  
 23 only reason why MasterCard retained even that tiny share  
 24 of the debit card market was because it launched its own  
 25 debit MasterCard, another separate debit product which

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1 had MIFs comparable to Visa, and that's what kept its  
 2 market share. It wasn't the Maestro with the lower MIF,  
 3 it was the new product with the MIF comparable to Visa.  
 4 That's what kept the market share.  
 5 Of course in the present case, under Sainsbury's  
 6 counterfactual there wouldn't even be that crumb of  
 7 comfort because under this counterfactual any MasterCard  
 8 debit card has a zero or low MIF.  
 9 So in our submission you can't say, look, they have  
 10 3% in the Maestro experience, that's enough, because you  
 11 don't get that here.  
 12 Second is that the switching effect in relation to  
 13 credit cards would have been even more extreme than in  
 14 the Maestro example because there was a greater  
 15 disparity, or there would have been a greater disparity,  
 16 in the level of the rates if MasterCard had lower zero  
 17 MIF and Visa had its actual MIF. The best place to see  
 18 this is from our skeleton argument. That's A, tab 2 and  
 19 it is page 210.  
 20 I have to be careful. There is some confidential  
 21 material here, so I will be careful. Paragraph 155(a)  
 22 is not confidential and that tells you under the Maestro  
 23 position what the disparity was between the Maestro MIF  
 24 and the Visa MIF.  
 25 Then (e) and (f) explain how the differential would

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1 have been materially greater if the MasterCard credit  
 2 card MIF was zero while Visa had its actual level. And  
 3 that's at (e) and (f), and you will see the magnitude of  
 4 the difference in particular at (f). So the switching  
 5 effect acknowledged by Mr von Hinten-Reed would have  
 6 been even more extreme for credit cards.

7 The third point is that in the credit card market,  
 8 unlike the debit card market, MasterCard faced  
 9 competition not just from Visa but also from Amex. If  
 10 we can look at Mr von Hinten-Reed's first report, so --  
 11 I am sorry to keep jumping around -- D2, tab 2,  
 12 page 211.

13 Paragraph 441:  
 14 "I have estimated, based on UK evidence mainly from  
 15 MasterCard disclosure, that MasterCard would lose  
 16 around 5% of its market, as measured by credit card  
 17 transactions, to Amex in a zero or low interchange fee  
 18 environment. This is consistent loss of market  
 19 share ... implicit in the estimates that BCG produced  
 20 for MasterCard for the range of likely MasterCard  
 21 revenue loss in a low interchange fee environment."

22 He is saying if Amex has its annual rates,  
 23 MasterCard has lower zero, 5% swing, he says, from  
 24 MasterCard to Amex. Put down marker, we disagree, we  
 25 say the swing would be a lot more, but I don't need that

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1 now because you take the Maestro where MasterCard is  
 2 left with 3% at the end of the day, you take the two  
 3 facts I have given you and you add on at least a 5%  
 4 swing to Amex. It is not just Visa taking, it is Amex  
 5 taking business as well. We say on that evidence  
 6 MasterCard would have been driven from the credit card  
 7 market.

8 Remember, I showed you in the MasterCard judgment in  
 9 the ECJ, there is evidence about what could MasterCard  
 10 have done and the way it could have changed the scheme.  
 11 But the ECJ makes absolutely clear in MasterCard that  
 12 the only thing you remove when you are looking at  
 13 objective necessity is the alleged restriction. So what  
 14 we are saying is that MasterCard, with an honour all  
 15 cards rule and the other features of the scheme which  
 16 are not challenged, could not have stayed in the market  
 17 with a disparity of MIF that Mr von Hinten-Reed  
 18 suggests.

19 Mr Brealey said it was crafty to talk about losing  
 20 market share because he said, well, MasterCard wouldn't  
 21 have had that market share without the MIF. I said  
 22 I would come back to Société Technique Minière, and  
 23 I want to do that now. It is at I3 at tab 1. 1966 it  
 24 is. I was a few years out.

25 If you turn, it is page 250 of the report or 007.08

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1 of the bundle. This was about restrictions in --  
 2 I think it was a distributor concessionaire agreement,  
 3 but we don't have to get into the detail of it. It is  
 4 the principle at the top of page 250 of the report, if  
 5 you could read that.

6 One of the classic early statements in competition  
 7 law, crucial words in the second line:

8 "In particular, it may be doubted whether there is  
 9 an interference with competition if the said agreement  
 10 seems really necessary for the penetration of a new area  
 11 by an undertaking."

12 So let's take Mr Brealey's optic. Let's assume  
 13 MasterCard is starting afresh, it is a new business, it  
 14 wants to set up a four-party scheme with all the  
 15 non-contested features of a four-party scheme, an honour  
 16 all cards rule etc. It looks at the market and it says  
 17 "Can I enter the market with a lower zero MIF given that  
 18 Visa has a MIF at the actual level it has?"

19 Would MasterCard have gone to the bother of setting  
 20 up the four-party scheme if it was going to get less  
 21 than 3% of the credit card markets in the UK? Possibly  
 22 nothing. The answer is obvious.

23 So that optic of Mr Brealey's, let's assume not that  
 24 MasterCard is sitting on this market share it shouldn't  
 25 have and it is going to lose, let's take his optic.

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1 Would a business enter into the counterfactual world  
 2 that Mr von Hinten-Reed describes? And the answer is  
 3 no. Such a business would not be economically viable,  
 4 to use the language of the ECJ in relation to objective  
 5 necessity.

6 So that's why we say it is objectively necessary,  
 7 and the suggestion that one gets from Sainsbury's as to  
 8 no, no, no, it would be objectively necessary, doesn't  
 9 work.

10 It hinges on what the counterfactual is. I'm going  
 11 to come to what their argument is on that. But this is  
 12 our case. So it's a case based on Visa stays as it is,  
 13 and if the Tribunal finds that that is the correct  
 14 counterfactual we say we win.

15 Bilaterals are not an answer either to objective  
 16 necessity. Can we look at Mr von Hinten-Reed's second  
 17 report at paragraph 185. That's D2, tab 3. It may be  
 18 D2.1. Sorry. It is page 456 of the bundle. Mr Brealey  
 19 confirmed this in an exchange with the Tribunal  
 20 yesterday.

21 185, first sentence:

22 "Under bilateral negotiations, under the honour all  
 23 cards rule interchange fees would be pushed so high that  
 24 the scheme would collapse."

25 So bilaterals are not a way of making four-party

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1 schemes viable if Visa has its (inaudible).  
 2 MR SMITH: You mean bilaterals without any default at all?  
 3 MR HOSKINS: Yes, that's what it is, because there's no  
 4 break in the whole MIF.  
 5 MR JUSTICE BARLING: No MIF.  
 6 MR SMITH: Thinking about this, it occurred to me that  
 7 because of the ease of switching from, let's say,  
 8 MasterCard to Visa, the simple cost of an issuer  
 9 negotiating a bilateral, even if it was very  
 10 straightforward, might be sufficiently high to  
 11 incentivise the issuer to jump ship from MasterCard to  
 12 Visa.  
 13 MR HOSKINS: Possibly. Yes. I said I don't -- that is  
 14 right. I'm not sure I have got the evidence to back it  
 15 up, but as a principle, yes. I'm just hesitating  
 16 because I'm not sure anyone has actually gone into that  
 17 as an evidential matter, but yes.  
 18 That's objective necessity. That's the very high  
 19 hurdle. Let's presume we fail on that for whatever  
 20 reason yet to be seen, but that's not the end of the  
 21 story here.  
 22 Return now to restriction of competition. If it is  
 23 not objectively necessary, is it a restriction of  
 24 competition within 101(1)?  
 25 Now, in the actual economic context that applied

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1 during the period of the claim, there was competition  
 2 between Visa and MasterCard for the credit card market.  
 3 Again, let's look at what Mr von Hinten-Reed's  
 4 counterfactual is for purposes of restriction of  
 5 competition. So that is D2, tab 2 at page 139.  
 6 Paragraph 95:  
 7 "I have established that the counterfactual for  
 8 article 101 may be no MIF or a low MIF which equates to  
 9 the additional benefits of card usage."  
 10 So no ex-post pricing rule, just zero or low MIF.  
 11 Now, again, what's the counterfactual? What's our  
 12 counterfactual? We say it is Visa would have retained  
 13 its MIF at the actual level it had during the period and  
 14 our market share would have been decimated.  
 15 MR JUSTICE BARLING: That's the same as you say for --  
 16 MR HOSKINS: It is, but the reason why it is not -- for  
 17 objective necessity, the test is higher. I have to show  
 18 it wouldn't have been economically viable, whether that  
 19 is 0%, 1% or 2%. That is the hurdle.  
 20 This, of course, is now looking at restriction of  
 21 competition. So let's just assume that our market share  
 22 falls substantially and let's just look at what the  
 23 competition would have been under Mr von Hinten-Reed's  
 24 counterfactual, because that's the exercise we have to  
 25 do. What was the actual state of competition with

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1 MasterCard UK domestic MIF at the level it was? And  
 2 then look at the counterfactual, and our counterfactual  
 3 world is: Visa stays as it was throughout the period, we  
 4 are at low or zero. And our market share therefore  
 5 tumbles.  
 6 Under that counterfactual, on the issuing side,  
 7 MasterCard would have been removed as an effective  
 8 competitor from the credit card market in the UK. Amex  
 9 and Visa would have been left as the only significant  
 10 players for credit cards. There was already no material  
 11 competition in the debit card market because of the  
 12 Maestro experience; Visa ruled the roost. So the  
 13 competitive position in the issuing market would have  
 14 been materially worse under a counterfactual without the  
 15 MIF than in the actual real world with the MIF. The  
 16 level of competition would have been materially less.  
 17 On the acquiring side, the level of competition  
 18 would be the same as it actually was because the  
 19 allegation, the vice that is said to exist in the  
 20 MasterCard MIF is that it set a floor for the MSC's  
 21 charge to merchants. I have already explained why the  
 22 actual level doesn't matter for competition purposes as  
 23 such. The real competition vice that's alleged is that  
 24 it set a floor.  
 25 But the position would have been precisely the same

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1 if MasterCard imposed a zero or low MIF, which is  
 2 Mr von Hinten-Reed's counterfactual. Because a zero MIF  
 3 is a common floor. A low MIF, at whatever level it is,  
 4 is a common floor. So the degree of competition between  
 5 acquirers in the counterfactual would be exactly the  
 6 same as it was in the real world as matters happened.  
 7 So when one has to apply the test that the Court of  
 8 Justice has told us we must apply, O2, compare the  
 9 counterfactuals and compare what the state of  
 10 competition is in each, MasterCard, Court of Justice  
 11 tells us you have to look at the effect on competition.  
 12 The relevant context is issuing in an acquiring market.  
 13 The counterfactual suggested by Mr von Hinten-Reed  
 14 means that competition in the issuing market is  
 15 substantially worse, competition in the acquiring market  
 16 is the same.  
 17 MR JUSTICE BARLING: I don't understand that. Sorry, it is  
 18 me being thick, but if you have a zero MIF and  
 19 a merchant -- can't the acquiring banks now, as it were,  
 20 compete with whatever their own merchant service charge  
 21 will be? I mean, they don't have this --  
 22 MR HOSKINS: But they can always compete on that because the  
 23 merchant service charge is made up substantially of the  
 24 MIF plus extra bits on top. They can always --  
 25 MR JUSTICE BARLING: The MIF is by far the biggest part of

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1 it. That was the whole point, wasn't it, of what  
 2 the Commission was saying? The MIF was -- I don't know,  
 3 I forget what it was, I don't know if I'm allowed to  
 4 say, but it was a very substantial part of it which  
 5 the Commission took the view that what bit that was  
 6 left, as it were, was -- because presumably once you  
 7 start paying a merchant less than, I don't know, 90% or  
 8 something, or whatever the thing might be of his sale  
 9 price, you know, he starts to get upset. So there's  
 10 only a limited amount you have got to play with,  
 11 I assume.  
 12 MR HOSKINS: But it is the same limited amount because the  
 13 MIF is just a set cost that MasterCard sets for taking  
 14 part in the system. The bit you have to play with as an  
 15 acquirer to compete are the costs above the MIF.  
 16 MR JUSTICE BARLING: But if there is no MIF or a zero MIF,  
 17 then the thing that enters the arena is surely the size  
 18 of the acquirer's own charge to his client? He can  
 19 compete as much as he wants --  
 20 MR HOSKINS: But they are trying to get the matter as low as  
 21 possible. They still have to cover their costs, because  
 22 the whole point of the MIF is that it is going from the  
 23 acquirer to the issuer to cover the issuer's costs. But  
 24 the acquirer, in terms of an acquirer being able to  
 25 compete, has its own cost issues and they are nothing to

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1 do with the MIF.  
 2 PROFESSOR JOHN BEATH: That is right. What you are saying  
 3 is that what's charged to the merchant is simply  
 4 a mark-up on the MIF?  
 5 MR HOSKINS: Yes.  
 6 PROFESSOR JOHN BEATH: And that mark-up is to cover the  
 7 costs of the acquisition side of the business and these  
 8 costs are unchanged?  
 9 MR HOSKINS: Correct. That is right.  
 10 MR SMITH: Mr Hoskins, let me make sure I have understood  
 11 this. What you are saying is that the mischief, the  
 12 anti-competitive effect that is said to occur, is  
 13 a common floor that is applicable to all acquirers and  
 14 that is passed on to the merchant market?  
 15 MR HOSKINS: Yes. The vice is that acquirers do not compete  
 16 in relation to the level of the MIF because the MIF as  
 17 in effect imposed on them by the scheme is at a common  
 18 level.  
 19 MR SMITH: You say the position is exactly the same as  
 20 regards mischief because there is still a common floor,  
 21 it is just the level of the common floor has changed.  
 22 MR HOSKINS: Yes, absolutely.  
 23 MR SMITH: And so therefore when one is sort of trading off  
 24 effects in the two markets, you say there is  
 25 a significant issue in the issuing market?

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1 MR HOSKINS: Yes.  
 2 MR SMITH: And there's no difference in acquiring market?  
 3 MR HOSKINS: Correct.  
 4 MR SMITH: Okay, I think I follow that. But let's suppose  
 5 the mischief is much more focused on the level of the  
 6 floor. I know that's not the position, but let's  
 7 hypothesise that the complaint is that the MIF is at  
 8 whatever level that the acquiring bank must pay to the  
 9 issuing bank and that really it should be set lower.  
 10 Now --  
 11 MR HOSKINS: It is not a 101 issue, sir. I'm sorry, sir, to  
 12 interrupt. Excessive pricing can be a problem, abuse of  
 13 dominance, but what 101 is concerned with is the  
 14 restriction on the ability of companies to compete with  
 15 each other because of consensus rather than competition.  
 16 But if you have a cartel and the cartel agrees "We  
 17 are going to give away our stuff because we are  
 18 humanitarian, we want to do good, we are Robin Hood", it  
 19 is still a cartel. If they are venal cartelists and  
 20 they want to make as much money as possible, it is still  
 21 a cartel.  
 22 The level has nothing to do with the 101 analysis.  
 23 It is a reason why it might attract a regulator's  
 24 attention, but actually it is irrelevant to finding of  
 25 the legality or not under 101.

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1 MR SMITH: Let me approach it another way. What I'm  
 2 interested in is in a case where there is two markets,  
 3 there is an anti-competitive effect or an effect on  
 4 competition in both.  
 5 Now, what you have presented to us is a case where  
 6 in the issuing market there is an effect and in the  
 7 acquiring market there is none because there is a floor  
 8 either which way. What I want to postulate, and I don't  
 9 really care what the effect in the acquiring market of  
 10 our hypothesising is, what I want to postulate is that  
 11 there is in fact such an effect. What is the court to  
 12 do when there is such an effect? How do you trade the  
 13 two off? How do you balance the two effects in the two  
 14 different markets?  
 15 MR HOSKINS: Assuming we are in the counterfactual -- and  
 16 let's stick to acquirer and issuer -- and there is a  
 17 negative effect, competition is worse in the acquiring  
 18 market -- not my case, but competition is better in the  
 19 issuing market in the counterfactual --  
 20 MR SMITH: Yes.  
 21 MR HOSKINS: -- you have to exercise your judgment. But it  
 22 is not this case.  
 23 MR SMITH: Okay.  
 24 MR HOSKINS: Because that's what the Court of Justice tells  
 25 you you have to do. If the detriments in the acquiring

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1 market were slight and the benefit in the issuing market  
 2 was large, overall competition is better.  
 3 You can only then exercise your judgment. That's  
 4 where the Court of Justice test leads you.  
 5 MR SMITH: What I'm wondering, though, is whether we don't  
 6 have to consider the nexus between two markets, because  
 7 if we follow the logic of what you say the effect is in  
 8 the issuing market, which is that there will be a flood  
 9 of issuing banks moving away from MasterCard and towards  
 10 Visa, won't that, because of the two-sided nature of the  
 11 market, mean that actually the MasterCard product will  
 12 be less desirable, of less interest to acquiring banks  
 13 because there will be fewer people wandering around with  
 14 a MasterCard in their pocket prepared to use it to pay  
 15 for their transactions?  
 16 MR HOSKINS: Yes, that may follow.  
 17 MR SMITH: Would that be the way in which we seek to in the  
 18 counterfactual balance the two markets?  
 19 MR HOSKINS: That is a better argument than the one I have  
 20 put. Because the competition would be worse in the  
 21 issuing market and there would be less interest in  
 22 competition in the acquiring market because nobody wants  
 23 to acquire MasterCard because nobody has a MasterCard in  
 24 their pocket.  
 25 This isn't my test. It is what the Court of Justice

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1 has said one must do.  
 2 MR SMITH: You have got to explain it to us.  
 3 MR HOSKINS: I understand.  
 4 MR JUSTICE BARLING: I'm still troubled, Mr Hoskins, by your  
 5 suggestion that levels are only to do with 101(3). I'm  
 6 still --  
 7 MR HOSKINS: Sorry, to do with ...?  
 8 MR JUSTICE BARLING: Article 101(3).  
 9 MR HOSKINS: No, they are not.  
 10 MR JUSTICE BARLING: I thought you said levels had nothing  
 11 to do with 101(1)?  
 12 MR HOSKINS: No, levels -- I interrupt, but I don't follow  
 13 you so far, sorry.  
 14 MR JUSTICE BARLING: All right. I will start again.  
 15 I thought that you were saying that the level of the  
 16 interchange fee, if it is agreed, cannot be a distortion  
 17 of competition between acquirers because by fixing it,  
 18 as it were, nothing changes between them and they can  
 19 still compete between each other in relation to their  
 20 own charge.  
 21 MR HOSKINS: Yes.  
 22 MR JUSTICE BARLING: And which they are free to fix at  
 23 whatever they choose. Am I right in saying that?  
 24 MR HOSKINS: If there is a restriction of competition --  
 25 MR JUSTICE BARLING: Yes.

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1 MR HOSKINS: -- a relevant one that falls in 101, then you  
 2 get to the question of the exemptable level.  
 3 MR JUSTICE BARLING: Yes, that's what I thought.  
 4 MR HOSKINS: But you only get to that question, so the level  
 5 becomes relevant if the MIF is a relevant restriction of  
 6 competition.  
 7 MR JUSTICE BARLING: Yes, but you are saying that the MIF  
 8 can't be because it is fixed, it is the same for all of  
 9 them. And therefore, there is no question --  
 10 MR HOSKINS: In the counterfactual it is fixed.  
 11 MR JUSTICE BARLING: At the same level because it is zero,  
 12 zero level.  
 13 MR HOSKINS: Yes.  
 14 MR JUSTICE BARLING: I appreciate that, but I wasn't sure  
 15 whether you were saying at whatever level, whether it is  
 16 zero in the counterfactual or whether it is the current  
 17 level, or the level that Sainsbury's complain about, it  
 18 can't be a distortion for the same reason.  
 19 MR HOSKINS: On my case, the actual level of the MIF is  
 20 irrelevant to the 101(1) --  
 21 MR JUSTICE BARLING: I thought that's what I started by  
 22 saying.  
 23 MR HOSKINS: And I agree with you. I didn't understand the  
 24 question.  
 25 MR JUSTICE BARLING: I'm sorry, that is my fault.

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1 MR HOSKINS: That was me being slow. Yes, that is the logic  
 2 of the submission.  
 3 MR JUSTICE BARLING: So you really attack the whole concept  
 4 that is the basis of the Commission's decision, which is  
 5 that by setting a positive floor, presumably there was  
 6 an effect on competition between acquirers? Forget the  
 7 actual level, but by setting some level that is more  
 8 than zero, I don't know what they said about zero, but  
 9 by setting some level above zero, there was a distortion  
 10 because it set a floor, and you question that?  
 11 MR HOSKINS: The Commission decision had three vices.  
 12 Mr Brealey called them the three vices. I have still  
 13 got two answers. One is the Commission isn't dealing  
 14 with the UK specific market. And the second point is  
 15 that when one comes to look at what 101(1) is about,  
 16 that's why I have taken you painstakingly through the  
 17 Court of Justice in MasterCard, because forget what  
 18 the Commission saying, with respect, we have the Court  
 19 of Justice telling us what the legal principles are.  
 20 And whatever the Commission says, one has to go by what  
 21 the Court of Justice says. And my submission is simply  
 22 based on what I -- I may not have made it clear, but if  
 23 you go away and put the cold towels around your head it  
 24 is perfectly clear, in my submission, what the Court of  
 25 Justice is saying. And the level of the MIF -- it is

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1 the auction example we talked about earlier.  
 2 If 101(1) is about the level of our price, you  
 3 couldn't have auctions.  
 4 MR SMITH: Just going back to the Commission decision. You  
 5 say that the mischief aimed against is a floor-setting  
 6 MIF, but I'm wondering really whether the Commission  
 7 wasn't saying: we are opposed to a MIF set at this  
 8 particular level --  
 9 MR HOSKINS: The Commission was saying that.  
 10 MR SMITH: You are saying that's simply wrong.  
 11 MR HOSKINS: I'm saying it is not supported by the laws as  
 12 set out by the Court of Justice, and any competition  
 13 law. Just because the Commission says something doesn't  
 14 mean it is right.  
 15 We have already established you are not bound by it.  
 16 What you are bound by is the law. So if you are  
 17 satisfied, and I have not seen any attempt to do it yet,  
 18 that the level of the MIF is a problem for 101(1), then,  
 19 you know, go ahead, if you find that's the law. But  
 20 nobody has actually put forward a case to you yet to say  
 21 that 101(1), the level itself, is a problem.  
 22 The law, in my submission, has to be based on the  
 23 lack of consensus between acquirers in terms of the  
 24 charge of the MIF to merchants. That's what 101(1) is  
 25 about, not about the level they happen to charge.

1 MR SMITH: Okay, going back though to the Commission, I hear  
 2 what you say about what the Commission says may not  
 3 necessarily be the law, but just to try to understand  
 4 the reasoning in the Commission's decision, would you  
 5 agree that they were concerned with the level of MIF,  
 6 which is why they approached it in terms of their  
 7 counterfactual with an ex post facto negotiation band so  
 8 you could effectively have a MIF of zero?  
 9 MR HOSKINS: Yes. The reason why the Commission got  
 10 interested in this was because there was lots of  
 11 complaints that the MIF was too high, and that's why  
 12 they came in and that's why when they are running  
 13 a competition case they have to get to a situation where  
 14 the MIF is law. And that is the way the Commission came  
 15 at it.  
 16 MR SMITH: That's the way they approached it.  
 17 MR HOSKINS: But please remember that the Commission at  
 18 legal analysis was found to be flawed in at least two  
 19 respects by the Court of Justice. And I have shown them  
 20 to you.  
 21 MR SMITH: I'm with you. I want to be clear first of all  
 22 what the Commission reasoning was, and I think we are  
 23 clear about that.  
 24 MR HOSKINS: Yes, it is one of the three vices Mr Brealey  
 25 recognises --

1 MR SMITH: Also, to be clear, I think it is clear on the  
 2 transcript, you are saying that's simply wrong in terms  
 3 of competition law.  
 4 MR HOSKINS: Legal analysis.  
 5 MR JUSTICE BARLING: One of the things they alleged, but  
 6 they didn't make a final decision of course, was that  
 7 this was price fixing and it was therefore a by object  
 8 infringement. In the end, of course, they didn't. You  
 9 took issue, your clients took issue then.  
 10 MR HOSKINS: They were not my clients then.  
 11 MR JUSTICE BARLING: Your current clients took issue with  
 12 it. I'm not absolutely sure, and certainly it has not  
 13 been -- the accelerator hasn't been pressed very hard by  
 14 Mr Brealey --  
 15 MR HOSKINS: I think it has disappeared down a hole. We  
 16 dealt with it in our skeleton argument.  
 17 If you go to Carte Bancaire and you see what the  
 18 test is for object, it has to be screamingly obvious.  
 19 Seven weeks, half of it on quantum. But it is trite,  
 20 but you have seen the issues involved here. You  
 21 understand why Sainsbury's has basically pulled away  
 22 from objective necessity. It's got no legs.  
 23 The proof of that in a sense is in the arguments  
 24 I have just made. Because an object case is so obvious  
 25 you don't need to look at the context, but --

1 MR JUSTICE BARLING: Forget object for the moment.  
 2 MR HOSKINS: That is a dead parrot.  
 3 MR JUSTICE BARLING: Well, Mr Brealey hasn't leapt to his  
 4 feet, but again, I will obviously put the cold towel  
 5 round my head on this, but if you reach the stage where,  
 6 if there is an economic and commercial limit to  
 7 a merchant service charge simply because merchants won't  
 8 tolerate something beyond a certain level being  
 9 deducted, and if 90%, say, for the sake of argument of  
 10 that commercial limit is taken up in a fixed charge, why  
 11 doesn't that affect the ability of acquirers to compete?  
 12 MR HOSKINS: There is no evidence to that effect. Nobody is  
 13 suggesting that. It has not been suggested.  
 14 MR JUSTICE BARLING: I thought there was a general  
 15 subscription to the reasoning of the Commission by  
 16 analogy in the --  
 17 MR HOSKINS: I will meet that point when the evidence is  
 18 brought forward, but with respect, this is the point,  
 19 this is part of the trouble, if you keep going back to  
 20 the Commission. You can cherry-pick bits, and  
 21 I understand -- hang on -- and of course you are going  
 22 to refer to it, I understand. But that's why I sort of  
 23 painstakingly showed why you are not bound by  
 24 the Commission decision.  
 25 Mr Brealey accepts that, that's a matter of law, and

1 that's why I laid store on the Maestro example because  
 2 when you are talking, for example, about the levels etc,  
 3 and I will come to it when I come to deal with why our  
 4 counterfactual is the correct one, ie Visa being actual  
 5 rather than Visa being low, the vice, if it be one, of  
 6 a MIF being too high, in the UK context competition law  
 7 can't deal with it because there is not restriction of  
 8 competition for the reasons I've explained and will  
 9 further develop when I come to why their counterfactual  
 10 doesn't work.

11 So if the policy concern is levels too high, what do  
 12 you do? You adopt a law that applies to everyone to  
 13 avoid the Maestro problem. That's what you need and  
 14 that's what's been done.

15 I'm not running a case in which I say the level in  
 16 this is relevant, MasterCard can do what it wants, Visa  
 17 can do what it wants, nobody can stop them. Regulation  
 18 will step in. The issue you have to decide is, given  
 19 the specifics of the UK market and the Maestro evidence,  
 20 does competition law bite? And that's what we are  
 21 dealing with. It is a much narrower issue. It is  
 22 a different framework of analysis.

23 So can you be concerned about level? Yes. Does it  
 24 get you home on a competition case in the UK  
 25 specificities? No.

1 Let's switch, because all the arguments I have put  
 2 to you so far are our arguments based on our  
 3 counterfactual, which is Visa staying as it is while we  
 4 are at low or zero.

5 This is really, when it comes to the difference  
 6 between the parties on objective necessity, restriction  
 7 of competition. This is the big issue between the  
 8 experts and the way they put together their expert  
 9 reports, for example, on this issue because Dr Niels  
 10 adopts our counterfactual, Mr von Hinten-Reed adopts the  
 11 other, and then they sort of go like that from each  
 12 other.

13 Let's look at what Sainsbury's position is. It is  
 14 explained at first von Hinten-Reed, so that is D2,  
 15 tab 2. It is page 71 of the bundle. It is  
 16 paragraphs 89 to 91.

17 If I can invite you to read that, you will see what  
 18 the position is. I'm told there are two 89s, and I have  
 19 gone to the wrong one, I'm very sorry. There is  
 20 another 89, and the relevant one is at 138. I'm so  
 21 sorry.

22 MR JUSTICE BARLING: Page 138?

23 MR HOSKINS: Page 138 of the bundle.

24 MR JUSTICE BARLING: So we want 89 --

25 MR HOSKINS: Still 89 to 91. (Pause)

1 That's the difference. He explains, he gives  
 2 an explanation of why he has adopted that approach in  
 3 his second expert report. So that is D2.1, tab 3 at  
 4 page 461. It is paragraph 210 to 214.

5 You see it is really the point Mr Brealey made  
 6 orally which is: it is not fair, we can't catch you  
 7 unless we have this counterfactual. Such  
 8 a counterfactual would clearly be unrealistic as it does  
 9 not facilitate the assessment of whether there has been  
 10 an infringement of competition law, so that it is not  
 11 fit for purpose.

12 But, with respect, it is the Sainsbury's  
 13 counterfactual that is wrong as a matter of law because  
 14 it is that counterfactual which is contrary to the  
 15 principles which are set down in the consistent case law  
 16 of the CJEU, including the MasterCard judgment, which  
 17 I showed you.

18 According to the case law, a counterfactual must be  
 19 realistic and it must take account of the actual  
 20 conditions in which the market functions. And  
 21 an assumption that Visa would have dropped its credit  
 22 card MIFs to the same level as a MasterCard MIF, at zero  
 23 or low, neither reflects reality, nor does it take  
 24 account of the actual market conditions in which the  
 25 MasterCard system functions.

1 It actually creates a whole new market, because in  
 2 the credit card market you have got Visa, MasterCard and  
 3 Amex, and they are actually asking you to make  
 4 assumptions in relation to two of them. The only person  
 5 that's left in the real world is Amex. But it goes  
 6 further than that. Let's look at it as a matter of  
 7 regulatory constraint.

8 What was Visa faced with in terms of regulatory  
 9 constraint? Well, first of all, it was under no  
 10 obligation in respect of the level of its domestic UK  
 11 credit card or debit MIFs during the period of the  
 12 claim. The first time there is a legal constraint is  
 13 when the regulation comes in at the end of last year,  
 14 because the Commission decisions, commitments etc,  
 15 exemption decisions never relate to the UK MIF.

16 You get the history if you want it. It is our  
 17 skeleton argument at paragraphs 90 to 111. It is highly  
 18 artificial, therefore, to assume that Visa would have  
 19 been subject to specific action by the Commission or the  
 20 OFT during the period of the claim when in fact it  
 21 was not.

22 So you can't get to this counterfactual, we say. It  
 23 is just not realistic to assume somehow that there's  
 24 regulatory constraint on the Visa because there wasn't.

25 But also it is clear, we know -- and I will show you

1 the facts -- that Visa didn't feel obliged by any  
 2 regulatory threat. Mr Brealey said, well, the heat was  
 3 on and all of this, of course it would have gone down to  
 4 MasterCard. But actually what we see from what actually  
 5 happened is that they didn't, in light of any potential  
 6 regulatory threat, slavishly follow MasterCard or vice  
 7 versa or, indeed, what the Commission did to MasterCard  
 8 or vice versa.  
 9 If we can go to our skeleton for this, it is  
 10 bundle A, tab 2, page 191. That's 191 of the bundle.  
 11 Let's see what actually happens when the authorities did  
 12 step in. Paragraphs 93 and 94. In 2002, Visa offered  
 13 undertakings to the Commission in relation to the level  
 14 and setting of its intra EEA MIF. You have seen that.  
 15 That's culminated in the 2002 Visa decision. What did  
 16 MasterCard do? Did it follow it? No.  
 17 Paragraph 94:  
 18 "MasterCard did not agree with the Commission's  
 19 analysis, which Visa had not tested because it offered  
 20 undertakings."  
 21 MasterCard did not offer the same undertakings. We  
 22 went to court and that's what led to the 2007 Commission  
 23 decision and the appeals that followed.  
 24 But also, paragraphs 100 to 101, what happened at  
 25 the end of that process when MasterCard was dealt with,

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1 by that time the exemption, the Visa exemption had  
 2 expired, so Visa was sort of floating. It had been  
 3 subject to Commission regulation, so MasterCard has  
 4 the Commission decision against it.  
 5 And 100:  
 6 "MasterCard offered temporary undertakings to  
 7 the Commission in relation to intra EEA MIFs."  
 8 And that was 0.3% credit card, 0.2 for debit cards.  
 9 What did Visa do? Did it follow that? No, it  
 10 didn't.  
 11 Paragraphs 102 and 103:  
 12 "Visa didn't offer commitments in relation to debit  
 13 cards ..."  
 14 This is all intra EEA and member states other than  
 15 the UK:  
 16 "... until 2010."  
 17 So about a year later.  
 18 And over the page, 104, visa didn't offer  
 19 commitments in relation to credit cards until 2013. So  
 20 that is about four years after the MasterCard intra  
 21 undertakings. And that's six years roughly after the  
 22 adoption of the Commission decision against MasterCard.  
 23 You have seen the graph in Dr Niels' statement.  
 24 Imagine a gap of four or six years before Visa is forced  
 25 to fall into line. The damage is done and MasterCard's

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1 market share has been decimated. So as a matter of  
 2 fact, it is not enough to say: well, the Commission was  
 3 all over Visa about this, because the facts show that  
 4 Visa fought its own corner when it suited it, MasterCard  
 5 did the same. They didn't slavishly follow each other,  
 6 nor did the authorities seek to coordinate the action  
 7 against them.  
 8 That's the regulatory position. As a matter of  
 9 commercial choice, what did Visa do when faced with  
 10 a situation in which MasterCard's UK Maestro debit card  
 11 MIF was low, or materially lower? As a matter of  
 12 commercial choice did Visa follow it or did it maintain  
 13 the high one and drive MasterCard from the market? No  
 14 surprise. Visa retained its higher MIF because it wiped  
 15 the floor with MasterCard as a result.  
 16 So Sainsbury's proposed counterfactual has no basis  
 17 in either the regulatory reality of what happened during  
 18 the period of the claim, nor commercial reality. It is  
 19 a wholly artificial construct which rather than  
 20 reflecting the actual structure of the UK market during  
 21 the period of the claim, paraphrasing the legal  
 22 requirement, it expressly ignores it. It re-writes the  
 23 reality and it is therefore inconsistent with case law.  
 24 Really Sainsbury's approach is nothing more than  
 25 a legal fiction which it claims is necessary for the

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1 effective application of competition law. But it is not  
 2 correct to say that it is not possible to assess whether  
 3 there has been an infringement of competition unless you  
 4 adopt their counterfactual.  
 5 My submissions show that it is entirely possible to  
 6 apply competition law, but you get to the conclusion  
 7 where there is no infringement. It is not that it  
 8 renders competition law inapplicable, it just means you  
 9 don't show an infringement. What really Sainsbury's are  
 10 saying is: unless you adopt our counterfactual, we can't  
 11 show a restriction. But that's not the test.  
 12 MR JUSTICE BARLING: Mr Hoskins, we need to take a break  
 13 fairly soon, so just choose --  
 14 MR HOSKINS: I'm aware of that, and I have got about two or  
 15 three minutes left and then I'll stop, if that's okay.  
 16 There's another problem with Sainsbury's suggested  
 17 counterfactual, which is that it requires one to assume  
 18 that Visa's MIF was unlawful during the period of the  
 19 claim. And what they are actually saying is you have to  
 20 assume the very thing that they are trying to prove  
 21 against us also applied to Visa.  
 22 So there is a presumption of innocence problem  
 23 potentially in relation to Visa, which will be fairly  
 24 obvious. You can imagine Visa won't be very happy if  
 25 a judgment comes out and says: actually, we find that

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1 the MasterCard MIF is unlawful, and because it follows  
2 that the Visa MIF was unlawful, they would have been at  
3 the same level. Circularity and presumption of  
4 innocence problem.

5 That is the problem. You have to effectively assume  
6 illegality on the part of Visa in order to establish  
7 illegality on the part of MasterCard.

8 As I said, this isn't an argument that leads one to  
9 say there is no legal mechanism to deal with a concern  
10 about the level of MIF. But the proper way to deal with  
11 the problem is not competition law, for the reasons  
12 I have described. It is legislation. And that's what's  
13 happened in the regulation, and the reason it is the  
14 proper way is that it gets rid, for the UK, of the  
15 Maestro problem. The Maestro problem is why there's no  
16 competition law problem in the UK and the way in which  
17 it is now dealt with is by regulation which applies to  
18 everyone at the same time.

19 If the Tribunal agrees with any of this analysis  
20 leading to a conclusion of the UK domestic MIF was  
21 objectively necessary, or there is no relevant  
22 restriction on article 101(1), then that's the end of  
23 this case.

24 We should have a break and then we will come back,  
25 because if you are against me on that, we move on.

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1 (3.10 pm)  
2 (A short break)

3 (3.30 pm)  
4 MR HOSKINS: Before we get into economics, let's do a wee  
5 bit more law. Let's do a wee bit more law.

6 So I'm moving into exemption, which only arises if  
7 you find a restriction of competition. There is an odd  
8 situation which arises because the Tribunal will then  
9 have to consider what the exemptable level of the MIF  
10 was, but you will have to do that for two reasons.

11 The first reason is that if the UK domestic MIF  
12 applied by MasterCard during the period of the claim was  
13 the same or less than the exemptable level of the MIF,  
14 so if the actual one is below the exemptable level, then  
15 it is 101(3), it is exempt. And in relation to that,  
16 the burden of proof is on us, and as Professor Beath  
17 pointed out in Mr Brealey's, we already knew the tests  
18 and the guidelines is robust empirical evidence. So  
19 burden on us and robust and empirical evidence.

20 However, there is a second function for which the  
21 Tribunal have to investigate the exempt level of the  
22 MIF, because if the actual MIF was above the level of  
23 the exemptable level of the MIF, then the difference  
24 between the exemptable level and the actual level is the  
25 basic overcharge fee.

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1 In that regard the burden of proof is on the  
2 claimant, it is on Sainsbury's to establish the extent  
3 of its loss. So just imagine a cartel case about  
4 widgets, a follow-on damages claim. The claimant has to  
5 show what the price would have been, and the burden is  
6 on them.

7 So there is a difficult legal issue about --

8 MR JUSTICE BARLING: So who goes first? I suppose logically  
9 you do, do you, because --

10 MR HOSKINS: The more interesting issue, really, is who the  
11 burden is on. My point is this is going to fold  
12 together because we are both having to argue, we say  
13 that exemptable level is X, Mr Brealey says it is Y and  
14 it is really completely artificial to say for one  
15 purpose -- because actually, assume that by some good  
16 fortune we both said the level was the same, are you  
17 going to say there is a different standard of proof on  
18 us than there is for him?

19 MR JUSTICE BARLING: I suppose theoretically, logically, you  
20 know, the question of exemption arises before the  
21 question of damages.

22 MR HOSKINS: It does.

23 PROFESSOR JOHN BEATH: Yes.

24 MR HOSKINS: But you are not going to decide two different  
25 exemptable levels.

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1 MR SMITH: Yes. Indeed. I mean, presumably you would  
2 not --

3 MR HOSKINS: One is bad enough.

4 MR SMITH: Neither of you would be contending for one level  
5 of exemptable MIF for 101(3) purposes and a different  
6 level for damages purposes. Presumably you would both  
7 be saying that we should reach a view on the evidence  
8 and conclude with one level of counterfactual MIF?

9 MR HOSKINS: My guess theoretically you could have two, you  
10 could apply a high standard and say you failed to prove  
11 it and then move into the overcharge, and then the  
12 burden switches and then the standard is different.  
13 Probably not because it is all civil standard really,  
14 but you have the point. I don't know the answer. But  
15 I think the truth is the answer is it all comes out in  
16 the wash.

17 MR JUSTICE BARLING: Let's hope so.

18 MR HOSKINS: Let's move from the washing to the broad axe,  
19 because as we are entering into issues relating to the  
20 assessment of damages this is an appropriate time to  
21 consider the legal principles applicable to such  
22 an assessment. Both as a matter of EU and domestic law,  
23 the law is pretty clear that the court has a broad  
24 discretion as to the assessment of damages. It is  
25 sometimes called the broad axe, but I would like to show

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1 you where we get that from.  
 2 First of all, can we go to bundle E5, tab 53.  
 3 MR JUSTICE BARLING: You are on damages, not exemption now?  
 4 Or is this a crossover?  
 5 MR HOSKINS: I need to go here because when I'm looking at  
 6 exemption I'm looking at it both for 101(3) and for  
 7 a potential overcharge. And insofar as you are looking  
 8 at potential overcharge, this broad axe principle  
 9 becomes relevant.  
 10 MR JUSTICE BARLING: Right.  
 11 MR HOSKINS: Sorry, I have the wrong reference then. I'm  
 12 looking for the Commission's practical guide to quantify  
 13 harm and actions to damages. If anyone in the room  
 14 knows where it is? I'm told E5 is not right.  
 15 MR SMITH: Would it be E5.3? (Pause)  
 16 MR JUSTICE BARLING: 53 I think is in E5 --  
 17 MR HOSKINS: It is, it is E5.3. Thank you very much. And  
 18 it is tab 53 of that. I'm grateful, thank you.  
 19 So this is the Commission staff working document.  
 20 It is the Commission's practical guide on quantifying  
 21 competition damages.  
 22 If we could look first of all at paragraph 16. It  
 23 tells us it is generally very difficult to deal with  
 24 these sorts of overcharge issues, and that's what you  
 25 have here when looking at the exemptable level of the

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1 MIF for damages purposes, if we get to that.  
 2 But then footnote 15 is important:  
 3 "The limits and implications of such assessment of  
 4 a hypothetical situation have been recognised by the  
 5 Court of Justice in the context of quantifying loss of  
 6 earnings and an action of damages for the community in  
 7 the agricultural sector."  
 8 And then there is a quote:  
 9 "The loss of earnings is the result not of a simple  
 10 mathematical calculation, but of an evaluation and  
 11 assessment of complex economic data. The court is thus  
 12 called upon to evaluate economic activities which are of  
 13 a largely hypothetical nature. Like a national court,  
 14 it therefore has a broad discretion as to both the  
 15 figures and the statistical data to be chosen, and also,  
 16 above all, as to the way in which they are to be used to  
 17 calculate and evaluate the damage."  
 18 That is a quote from the Court of Justice in Mulder.  
 19 So that is EU law, assessment of damages, and  
 20 the Commission says it should apply in relation to  
 21 competition damages.  
 22 Then paragraph 17:  
 23 "For these reasons quantification of harming  
 24 competition cases is by its very nature subject to  
 25 considerable limits. As to the degree of certainty and

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1 precision that can be expected, there cannot be a single  
 2 true value of the harm suffered that could be termed but  
 3 only best estimates relying on assumptions and  
 4 approximations."  
 5 I should point out that the CAT gets an honourable  
 6 mention, footnote 16, for dealing with such issues.  
 7 I quoted this far because it is the law. I could  
 8 have come to you and said: Mr Brealey has to show great  
 9 precision. That's not the law. Of course this helps me  
 10 when we come to pass-through, as we will come and see,  
 11 but this is the law.  
 12 Then in the English courts we have Devenish, which  
 13 is I4, tab 8. The headnote, this was a follow-on action  
 14 arising from the vitamins cartel, and the claimants  
 15 sought exemplary damages, restitution in respect of  
 16 unjust enrichment and an account of profits.  
 17 We see opposite F:  
 18 "On the preliminary issue as to whether the  
 19 claimants were entitled ...(Reading to the words)... in  
 20 addition or as an alternative to compensatory damages,  
 21 the judge [who was Mr Justice Lewison] ruled inter alia  
 22 that neither exemplary damages nor a restitutionary  
 23 award nor an account of profits was available as  
 24 a remedy."  
 25 The big issue in the case was whether compensatory

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1 damages would be an adequate remedy because if not, that  
 2 could potentially trigger an account of profits or some  
 3 form of restitutionary relief. That really was  
 4 compensatory damage and adequate remedy.  
 5 What the claimant was saying was this is all so  
 6 complicated that it is not an adequate remedy. That's  
 7 rejected because of the broad axe principle.  
 8 So Mr Justice Lewison's judgment, it is paragraph 19  
 9 which I want to start at, which is on page 160. This is  
 10 where he considers compensatory damages. So he is  
 11 assessing whether compensatory damages can be  
 12 an adequate remedy.  
 13 19 says:  
 14 "Common ground at least for the purposes of this  
 15 trial of preliminary issues, the claimants are entitled  
 16 to compensatory damages."  
 17 Then he summarises the claimant's expert evidence at  
 18 that stage.  
 19 23:  
 20 "Mr Layton, who was for the claimant, put the  
 21 difficulty of proof in the forefront of his argument in  
 22 favour of the availability of exemplary damages and  
 23 a restitutionary award for a claim under  
 24 article 81(a)(c)."  
 25 A bit further down, just above G:

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1 "The important point [according to  
 2 Mr Justice Lewison] is that the difficulties on which  
 3 Mr Layton relies are not factual difficulties in the  
 4 sense that the facts necessary to amount to ...(Reading  
 5 to the words)... but evidential difficulties in the  
 6 sense that it may be difficult to prove to the  
 7 satisfaction of the court the facts that do exist or  
 8 would have existed in the no cartel world.  
 9 "It is necessary, therefore, in my judgment to  
 10 examine ...(Reading to the words)... to effective  
 11 compensation. I will do this first by looking at the  
 12 position in domestic law."  
 13 Then 27, if I could ask you to read 27.  
 14 MR JUSTICE BARLING: Yes.  
 15 MR HOSKINS: Actually, if you read between E and F, and then  
 16 you read the citation from Lord Shaw's judgment in  
 17 Watson Laidlaw, it begins below G. That is sufficient  
 18 and it will introduce you with the concept of the broad  
 19 axe, if you are not already familiar with it.  
 20 The important point is really just above B on  
 21 page 407 of the report:  
 22 "The restoration by way of compensation is therefore  
 23 accomplished to a large extent by exercising a sound  
 24 imagination and the practice of the broad axe."  
 25 Then if I could ask you to read 29 to 32, the

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1 principle of the broad axe is expanded upon.  
 2 MR JUSTICE BARLING: 29 to 32.  
 3 MR HOSKINS: Paragraphs 29 to 32.  
 4 What happened therefore was the judge said, well,  
 5 using the broad axe, compensatory damages are adequate  
 6 so you don't get the other remedies you are seeking. It  
 7 went to the Court of Appeal and the Court of Appeal  
 8 proved the first instance judgment. If we can see  
 9 Lady Justice Arden's judgment, it is 468 of the report,  
 10 174.051 of the bundle.  
 11 It is between G and H where she refers to the broad  
 12 axe and approves the wielding of it. Between G and H.  
 13 Likewise Lord Justice Tuckey at paragraph 159, it is  
 14 the last page of the report, 480.063 of the bundle:  
 15 "A judge wielding the broad axe is capable of doing  
 16 justice in such a case."  
 17 So I hope that makes your task seem a bit less  
 18 daunting than it might seem at first blush. You are to  
 19 wield the broad axe and that will hopefully make your  
 20 task easier.  
 21 There is an important aspect though because with the  
 22 benefit of the broad axe, what the courts have made  
 23 clear is that when you wield it, the court should err on  
 24 the side of under-compensation. If you like, a claimant  
 25 gets the benefit of the doubt, but then the Tribunal and

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1 the court has to be careful to err on the side of  
 2 under-compensation.  
 3 There is a very important point. I would like to  
 4 take you to those judgments. First of all, I6, tab 9.  
 5 This is a case, SPE International Limited v  
 6 Professional Preparation Contractors. It is a judgment  
 7 in the Chancery division, Mr Justice Rimer of May 2002.  
 8 If I can ask you first of all to look -- it is  
 9 pretty complicated -- at paragraph 10:  
 10 "I find against PPC on liability for infringement."  
 11 It was a patent, copyright infringement case,  
 12 I forget which:  
 13 "I find established the allegations of infringement  
 14 by copying ...(Reading to the words)... SPE's drawing."  
 15 So the defendant had breached copyright by creating  
 16 machines using someone else's plans.  
 17 Then the important bit for present purposes, 85  
 18 to 87. If I could ask you to read those.  
 19 Again, I will save you some time. 86 refers to  
 20 Watson Laidlaw; you see the broad axe is about to be  
 21 wielded at the bottom of the page?  
 22 MR JUSTICE BARLING: Yes.  
 23 MR HOSKINS: Then in 87:  
 24 "In this case my rejection of Mr Dean's evidence  
 25 means that SPE is left seriously short of material by

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1 way of proof of its loss under this head."  
 2 But he wields the broad axe to help them, but then  
 3 he says five lines up from the bottom of paragraph 87:  
 4 "That may work to SPE's disadvantage since I also  
 5 consider that I should err on the side of  
 6 under-compensation, for inadequate compensation is  
 7 better than none."  
 8 So the claimant doesn't have very strong proof, so  
 9 he wields the broad axe, but says "I'm going to  
 10 therefore err on the side of under-compensation".  
 11 That is approved later by the Court of Appeal.  
 12 That's tab 10, it's a case called Blayney (trading as  
 13 Aardvark Jewelry) v Clogau St David's Gold Mines  
 14 Limited.  
 15 It is the Vice Chancellor, as he was,  
 16 Sir Andrew Morritt at 55. If you go into the detail you  
 17 will see he approves the wielding of the broad axe. It  
 18 says at the end of paragraph 35:  
 19 "I put it that way because it is in my view  
 20 necessary to guard against over-compensation."  
 21 Just to show the reference to the Mr Justice Rimer  
 22 judgment is at paragraphs 31 to 34 of this  
 23 Court of Appeal judgment. You see he refers to SPE, he  
 24 sets out certain parts of it.  
 25 34:

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1 "In my view the approach of Mr Justice Rimer is  
 2 correct."  
 3 So two instances of the broad axe being wielded, and  
 4 both, one High Court and one Court of Appeal, the court  
 5 says yes, but you must err on the side of  
 6 under-compensation if that's the approach to be adopted.  
 7 PROFESSOR JOHN BEATH: But in the case we have looked at,  
 8 the Vice Chancellor case --  
 9 MR HOSKINS: The which, sorry?  
 10 PROFESSOR JOHN BEATH: In the case we looked at, the one to  
 11 do with the Vice Chancellor Sir Andrew Morritt, the  
 12 basis of the reasoning for not over-compensating was  
 13 there was a loss and a gain to be weighed against one  
 14 another, and that's why you would --  
 15 MR HOSKINS: Yes.  
 16 PROFESSOR JOHN BEATH: Both are going to be hard to measure.  
 17 MR HOSKINS: Yes, I understand. There are details within  
 18 the case, that's why I put it, two examples of the broad  
 19 axe being wielded, and in both instances the judges  
 20 saying "But we need to err on the side of  
 21 under-compensation".  
 22 MR JUSTICE BARLING: To be fair, he says I should guard  
 23 against over-compensation because, as Professor Beath  
 24 says, there is a set-off so that might not be quite so  
 25 helpful.

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1 MR HOSKINS: I understand.  
 2 PROFESSOR JOHN BEATH: You are not going to argue this case  
 3 that there might be --  
 4 MR HOSKINS: No, not at all. The point, I'm referring these  
 5 to you as examples of the broad axe where the court said  
 6 "But I'm going to err on the side of  
 7 under-compensation". I accept that neither of them says  
 8 "This is a legal principle", if you like.  
 9 You understand why both of them did it. I say here  
 10 is the High Court doing it, here's the Court of Appeal  
 11 doing it, you should do it.  
 12 Can I move on to how to deal with the exemption  
 13 criteria. So I'm moving out of the general approach to  
 14 assessing damages.  
 15 Article 101(3). We know there are four cumulative  
 16 conditions. What's apparent in the field of interchange  
 17 fees is that the Commission has relied on economic  
 18 proxies on a number of occasions in order to assess  
 19 exemptions and in order to find that the level of  
 20 particular MIFs has been acceptable.  
 21 It is interesting the Commission has actually used  
 22 these proxies on occasions when it wants to justify its  
 23 own approach. So, for example, when it is accepting  
 24 commitments or granting exemption to Visa, it adopts  
 25 a proxy. Actually, the only time I think -- I may be

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1 over egging it, but the most notable time it has  
 2 actually tried to do a full 101(3) analysis was the  
 3 MasterCard case where it was actually trying to reject  
 4 MasterCard's exemption. Nothing probably particularly  
 5 turns on that, save to point out when the Commission  
 6 wants to justify a level and if it is happy to use  
 7 a proxy.  
 8 Let me show the examples. First of all,  
 9 the Commission relied on the costs-based proxy, so that  
 10 is an assessment of the costs of supplying payment  
 11 services, the costs of processing transactions, costs of  
 12 providing the payment guarantee, cost of the free  
 13 funding period in its Visa 2002 decision.  
 14 If we look at -- Mr Brealey showed it to you, but  
 15 look briefly at it -- E1, tab 2. I'm sorry, is there  
 16 an E1? I'm sorry, just let me check my reference. I'm  
 17 right, E1, tab 2, page 90.  
 18 Then recitals 83 to 85. In particular 83:  
 19 "The Visa network, like any network characterised by  
 20 network externalities, will provide greater utility to  
 21 each time of user, the greater the number of users  
 22 ... (Reading to the words)... the greater the utility to  
 23 cardholders etc.  
 24 "The maximum number of users of the system will be  
 25 achieved. The Commission accepts it is not necessary to

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1 achieve," etc.  
 2 Then the last sentence:  
 3 "Given the difficulties of measuring the average  
 4 marginal utility of a Visa card payment to each category  
 5 of user, some acceptable proxy for this must be found."  
 6 84:  
 7 "To this end, Visa has, in its proposal for  
 8 a modified MIF, identified the three main cost  
 9 categories."  
 10 We see them: (a) the cost of processing, (b) the  
 11 cost of providing the payment guarantee, (c) the cost of  
 12 the free funding period.  
 13 85:  
 14 "The Commission sees no reason to contend the  
 15 relevance of these three cost categories."  
 16 Then there is some consideration under the heading  
 17 of the 101(3) criteria, but for the first two it is the  
 18 proxy that's used.  
 19 Then article 1, the exemption is granted. So in  
 20 this case the proxy is used to satisfy the first two  
 21 conditions. In the MasterCard 2007 decision,  
 22 the Commission applies 101(3), it didn't apply a proxy.  
 23 Remember then that's what the General Court -- as  
 24 I explained earlier, because it is a review of the  
 25 Commission decision, that's what then went for the

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1 General Court in the Court of Justice. And they are  
2 looking at a straight vanilla 101(3) approach. But what  
3 happened after was the Commission went back to using  
4 a proxy, but it was a different one. It was the MIT  
5 test.

6 So let's see where the Commission has used that as  
7 a proxy. The first time was in 2009, so that was after  
8 its 2007 MasterCard decision. And that was in relation  
9 to the interchange undertakings that MasterCard had to  
10 offer following the Commission decision in order to tide  
11 itself over during the appeal process.

12 If we can go first to the MasterCard undertakings,  
13 that is E3.5, tab 110, and paragraphs 1 to 8 set out in  
14 a sense the procedural history that led to the  
15 acceptance of the undertakings. But that's effectively  
16 the adoption of the decision pending the appeals,  
17 the Commission sought these undertakings to hold the  
18 position.

19 Then at paragraphs 11 to 13 MasterCard gives the  
20 following undertakings:

- 21 "(a) Interim interchange fees.
- 22 "Methodology. During the interim period, MasterCard
- 23 will use the tourist test methodology, including
- 24 a two-party interchange fee as described in MasterCard's
- 25 letter of 20th January."

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1 12:  
2 "During the interim period MasterCard will ensure  
3 the weighted average of ...(Reading to the words)...  
4 exceed the weighted average of 30BPS."

5 Then 13 is the same limit in relation to debit  
6 cards. So the methodology is tourist test or MIT. The  
7 letter -- there's actually a different letter -- the  
8 letter of 31st March is at tab 111. This is  
9 a Commission letter to MasterCard.

10 You will see in the third paragraph:

11 "As explained in your letter, calculation of these  
12 weighted average rates have been applied ... takes into  
13 account the interchange fees for all cross-border  
14 ...(Reading to the words)... including those over the  
15 internet.

16 "It is the view of the Commissioner for Competition  
17 Policy and DG Competition that the tourist test, given  
18 the specific characteristics ...(Reading to the  
19 words)... reasonable benchmark for assessing a MIF level  
20 for the purposes of article 81(3) EC treaty."

21 It is a proxy. To satisfy MIF, you satisfy 101(3).

22 Then there is a relevant Commission memo, which is  
23 in a different bundle, E1, tab 9, which relates to these  
24 undertakings again.

25 This relates to a different point because I have

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1 shown you that the Commission accepted the MIT as  
2 a proxy for 101(3). What this shows you is what  
3 information that MIT was based on, and you get that from  
4 page 3. Why are MasterCard's undertakings temporary?  
5 It is because of the appeal.

6 But then it goes on:  
7 "Commissioner Kroes notes that MasterCard's  
8 undertakings are without prejudice to a further  
9 assessment should new information come to hand. In  
10 particular, the Commission's competition department has  
11 commissioned a study with a view to collect data in  
12 order to improve the factual basis for the assessment of  
13 what level of MIF would be in accordance with the  
14 tourist test."

15 That is the Deloitte exercise that we will come to.  
16 Then bottom of that page:  
17 "How has the ...(Reading to the words)... been  
18 calculated."

19 You will see second sentence there:  
20 "MasterCard has based its calculations of this  
21 balancing fee on tourist test MIF ...(Reading to the  
22 words)... card with those of cash."

23 So this is pre-Deloitte. This is an early stage.

24 Mr Brealey referred you to the figures which were  
25 reached in these discussions. He said MasterCard has

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1 done a MIT test and these are the figures it reached.  
2 But with respect, you have to bear in mind a couple  
3 of factors. First of all, we have put in evidence about  
4 how these discussions progressed. It is confidential,  
5 that is the discussion we had yesterday, so I'm not  
6 going to say it out loud now. But it is first Koboldt,  
7 which is C2, tab 3, about the nature, how MasterCard  
8 arrived at those figures. And what's very important to  
9 remember is that at this stage, first half of 2009, MIT  
10 MIF was in its infancy because the Rochet and Tirole  
11 article, which is where the Commission got the idea  
12 from, was only published in 2008.

13 MR JUSTICE BARLING: What date is this?

14 MR HOSKINS: This is all first quarter of 2009.

15 PROFESSOR JOHN BEATH: Be careful. Rochet and Tirole were  
16 putting forward that tourist test argument in discussion  
17 papers back in 2004.

18 MR HOSKINS: You are ahead of me then.

19 PROFESSOR JOHN BEATH: I think in the professional  
20 literature it was already there, and I could imagine  
21 the Commission economists were probably aware of that.

22 MR HOSKINS: Where I got that date from is where  
23 the Commission refers to the economic literature that it  
24 relies on for the MIT test, it is the Rochet and Tirole  
25 2008 article.

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1 MR JUSTICE BARLING: Were you going to give us the paragraph  
 2 for Koboldt 1 or not?  
 3 MR HOSKINS: The whole thing is the story of the  
 4 negotiations. He will be cross-examined on it by  
 5 Mr Brealey, so we will be coming to that.  
 6 But MIF was in its infancy because let's say Rochet  
 7 and Tirole had formulated the idea of --  
 8 PROFESSOR JOHN BEATH: It hadn't become mainstream.  
 9 MR HOSKINS: Exactly, and it was a long time before the  
 10 Deloitte survey, so it was based on the Central Bank  
 11 studies.  
 12 Therefore, you can't, I think, as Mr Brealey  
 13 might -- I think what he suggested was, well, look, here  
 14 is what MasterCard did to get to these interim  
 15 undertaking levels, you can rely on that. That's not  
 16 appropriate, for the reasons I have just described. We  
 17 say that's really of no evidential value in this case,  
 18 we have got far more up-to-date evidence about what  
 19 an appropriate MIT MIF should be; for example, the  
 20 Deloitte survey amongst other things. So it would be  
 21 wrong to rely on that historic interim undertaking.  
 22 The second place that the Commission used the MIT as  
 23 a proxy is its 2010 commitments decision in relation to  
 24 Visa debit cards, which related to intra EEA MIF and  
 25 certain countries, but not the UK. That's at E1 at

1 21

1 tab 13, but I think an easier way to get into it is E1,  
 2 tab 14, which is the Commission press release.  
 3 So again, you see the heading "Introduction". The  
 4 third paragraph begins:  
 5 "These commitments are offered by Visa Europe,  
 6 taking into account the Commission is currently  
 7 conducting a pilot study on the costs and benefits to  
 8 merchants."  
 9 So that is pre-Deloitte information that is being  
 10 used.  
 11 Paragraph 1.1 and 1.2 you get the figure that was  
 12 arrived at and accepted by way of commitment. But then  
 13 at 317, you get a definition of the merchant  
 14 indifference test, and there's the reference to the 2008  
 15 Rochet and Tirole article. So that is what  
 16 the Commission is relying on.  
 17 MR JUSTICE BARLING: Sorry, which paragraph is that?  
 18 MR HOSKINS: It is a definition section, and there is  
 19 a heading "Merchant indifference test involved". So it  
 20 is page 317. And they refer to the 2008 articles.  
 21 That is the source, if you like, that the Commission  
 22 is relying on for the legitimacy of using MIT as  
 23 a proxy.  
 24 MR JUSTICE BARLING: Yes.  
 25 MR HOSKINS: Then it used the MIT as a proxy again in its

1 22

1 2004 Visa decision, which was for Visa credit cards.  
 2 Again, intra EEA and certain domestic MIFs, but not the  
 3 UK. That's E1, tab 18A. 2014, I misspoke, sorry. This  
 4 is a 2014 decision.  
 5 MR JUSTICE BARLING: E1, tab 18A?  
 6 MR HOSKINS: 18A. If I can pick it up at recital 41 at  
 7 page 11 of the document, you will see again that this  
 8 MIF was based on the Central Bank's studies, not  
 9 Deloitte. It pre-dated Deloitte.  
 10 Recital 50:  
 11 "Assessment of other observations from the payment  
 12 industry.  
 13 "Domestic MIF rates set by local ...(Reading to the  
 14 words)... Therefore, the Commission is not in a position  
 15 to demand commitments on those rates. In any case,  
 16 cross-border acquiring is expected to bring MIFs down to  
 17 a comparable level domestically. In addition, national  
 18 competition authorities or national courts are well  
 19 placed to assess MIFs set by local members  
 20 domestically."  
 21 So what the Commission is saying is: we are doing  
 22 this with MIFs, but when it comes to domestic MIFs,  
 23 national courts and competition authorities are well  
 24 placed to do their own job for obvious reasons, to take  
 25 account of national conditions.

1 23

1 So you can't just take the Commission approach and  
 2 the Commission's conclusions and just transplant them  
 3 into domestic context.  
 4 Then recital paragraph 104:  
 5 "When analysing MIF levels, the MIT methodology  
 6 originally developed in economic literature ..."  
 7 The footnote references to the 2008 Rochet and  
 8 Tirole article:  
 9 "... but then further developed by the Commission to  
 10 ...(Reading to the words)... is used by the Commission  
 11 as a benchmark or proxy for assessing compliance with  
 12 article 101(3) of the treaty as a methodology that is  
 13 economically robust enough to ensure that merchants  
 14 benefit from card acceptors."  
 15 Then finally, the regulation which we have looked  
 16 at, but if we can go back to for this point. It is I.1,  
 17 tab 6. We have seen recital 20 on page 88. Sorry, it  
 18 is I.1, tab 6.  
 19 We have seen recital 20 explains that the caps to  
 20 the regulation were based on the merchant indifference  
 21 tests, and I noted that when we saw that first. The  
 22 language then reflects really 101(3), and in the  
 23 proposal that was submitted by the Commission to the  
 24 European Parliament in July 2013 in relation to this  
 25 regulation, page 16 of that proposal stated that the

1 24

1 caps were calculated on the basis of the data gathered  
 2 by the four national banks.  
 3 So even in the regulation we are still not using  
 4 Deloitte. I can give you the reference for the  
 5 proposal. It is E1, tab 17 at 381.  
 6 So the regulation is based on MIT and uses the  
 7 Central Bank's, not Deloitte.  
 8 Mr Cook is concerned to point out that the national  
 9 banks don't include the Bank of England, but I think you  
 10 have probably picked that up. He is right to be  
 11 cautious with me.  
 12 Okay, Rochet and Tirole, Professor Rochet in  
 13 particular. We have seen that the Commission has cited  
 14 the 2008 Rochet and Tirole article as the justification  
 15 for using the MIT test as a proxy for 101(3). Let's  
 16 look at it. E3.5 at tab 99A.  
 17 Page 1, the abstract:  
 18 "Anti-trust authorities often argue that merchants  
 19 cannot reasonably turn down payment cards and therefore  
 20 must accept ...(Reading to the words)... The paper  
 21 attempts to shed light on this must-take-cards view from  
 22 two angles.  
 23 "First, the paper gives some operational ...(Reading  
 24 to the words)... it analyses its relevance as  
 25 an indicator of excessive interchange fees."

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1 Then second:  
 2 "... identifies four sources of potential biases."  
 3 Pages 2 to 3, the introduction. I will try and take  
 4 this as quick as I can because you can go and put the  
 5 cold towels on if you haven't done already.  
 6 On page 3 you see the paragraph that begins:  
 7 "Second, the paper provides an alternative benchmark  
 8 for regulatory intervention."  
 9 Then at the bottom, five lines up in that paragraph:  
 10 "The paper analyses the test's relevance as  
 11 an indicator of excessive interchange fees. We show  
 12 that when issuers' margins are constant, the tourist  
 13 test is an exact test of excessive interchange fees  
 14 ...(Reading to the words)... is social welfare."  
 15 So if the criterion is social welfare, the test  
 16 indicates a MIT MIF which is too low. And the MIT MIF  
 17 in any event is based on an assumption of issuers'  
 18 margins being constant, which is not, I submit, likely  
 19 in the real world.  
 20 What is meant by "social welfare", vis-a-vis  
 21 producer welfare? There is a neat encapsulation of it  
 22 if you go to 1.1, tab 2. We are going to keep the  
 23 Rochet and Tirole out. We are going to come back to it.  
 24 There is no title page to this, but it is a work by  
 25 M Motta, 2004, "Competition Policy, Theory and

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1 Practice". It was published by Cambridge University  
 2 Press. We cite it in our skeleton.  
 3 It is pages 18 to 19 and it is the first paragraph:  
 4 "Economic welfare is the standard concept used in  
 5 economics to measure how well an industry performs. It  
 6 is a measure which aggregates the welfare or surplus of  
 7 different groups in the economy. In each given  
 8 industry, welfare is given by total surplus, that is the  
 9 sum of consumer surplus and producer surplus. The  
 10 surface of a given individual consumer is given by the  
 11 difference between the consumer's valuation ...(Reading  
 12 to the words)... of all consumers.  
 13 "The surplus of an individual producer is the profit  
 14 it makes by selling the good in question. Producer  
 15 surplus is therefore the sum of all profits made by  
 16 producers in the industry."  
 17 So social welfare, or total welfare, is the sum of  
 18 consumer welfare and producer welfare. And that's where  
 19 producer welfare or surplus is understood to be the sum  
 20 of all profits made by producers in an industry.  
 21 I hope that's a fair summary of that paragraph.  
 22 Under Rochet and Tirole's framework the social or  
 23 total welfare would refer to the aggregate surplus of  
 24 all the players involved in the four-party scheme:  
 25 Merchants, cardholders, issuing banks and acquiring

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1 banks. And Rochet and Tirole tell us that the MIT would  
 2 give a result which is too low, a false positive, if the  
 3 goal includes consumer welfare.  
 4 Which leads us to the question: is the aim of  
 5 article 101 limited to consumer surplus or does it  
 6 include social welfare? And the answer is the latter,  
 7 and you get that from the Commission's exemption  
 8 guidelines, E.1, tab 2A. I know this is tough going on  
 9 this time of day, but it is on the transcript and  
 10 hopefully you will have time to go back to it at your  
 11 leisure.  
 12 So you have seen this. Mr Brealey took you. It is  
 13 the Commission exemption guidelines. It is  
 14 paragraph 33:  
 15 "The aim of community competition rules assist to  
 16 protect competition in the market as a means of  
 17 enhancing consumer welfare and of ensuring an efficient  
 18 allocation of resources."  
 19 It is not limited just to consumer welfare.  
 20 It follows, therefore, that according to Rochet and  
 21 Tirole's own article, the MIT will produce a MIF which  
 22 is too low for the purposes of EU competition law. Of  
 23 course they weren't specifically addressing EU  
 24 competition law. That, from what they say themselves,  
 25 comparing it with what the aim of EU competition law is,

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1 on its own face will produce a result which is too low.  
 2 If we go back to the Rochet and Tirole article, it  
 3 is E3.5. It is pages 18 to 19, but again, try and take  
 4 it as quickly as possible.  
 5 On 19, you will see halfway down, there's  
 6 a paragraph begins:  
 7 "Under imperfect issuer competition, the tourist  
 8 test threshold again coincides with the ...(Reading to  
 9 the words)... interchange fee is higher."  
 10 Then I will skip a sentence:  
 11 "If competition authorities aim at maximising  
 12 consumer surplus, a cap based on the tourist ...(Reading  
 13 to the words)... That is not the case if the objective  
 14 is to maximise social welfare."  
 15 It is the point I have just made. It is spelled out  
 16 again by Rochet and Tirole.  
 17 Page 26, this is going to come up later, you will  
 18 see some equations again. The paragraph begins:  
 19 "In this case the average merchant ..."  
 20 Halfway down the page.  
 21 Then the third sentence:  
 22 "Efficiency cannot require that the tourist test be  
 23 met by all participating merchants because cardholders  
 24 must internalise the welfare of the average merchant and  
 25 not of the marginal one who values card payments less

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1 than the average merchant. Capping merchant discounts  
 2 at the convenience benefit of the most reluctant  
 3 merchants provides the cardholder with an incentive for  
 4 under-consumption of card payments."  
 5 So the important point, which we will come back to,  
 6 is the MIT test needs to be based on the average  
 7 merchant.  
 8 Then page 29, second paragraph:  
 9 "When issuer margins are constant and merchants are  
 10 homogenous ..."  
 11 You see the theoretical caveats there:  
 12 "... the tourist test is a proper and practical  
 13 policy tool."  
 14 There is a bit of a tension there, being a practical  
 15 tool when you are assuming issue margins are constant  
 16 and merchants are homogenous:  
 17 "By definition, the tourist ...(Reading to the  
 18 words)... by a non-repeat customer with enough cash in  
 19 her pocket.  
 20 "This implies that IF lies above the level that  
 21 maximises ...(Reading to the words)... aim at maximising  
 22 short-term total user surplus."  
 23 Again, very limited. There is no criticism, this is  
 24 a theoretical paper. They recognise the limitations and  
 25 the assumptions it is based on, but you will hopefully

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1 see pretty quickly that this is not actually fit for  
 2 what the Commission is then using it for. You can't  
 3 just lift this across into the real world.  
 4 Then the next paragraph begins:  
 5 "First, in the short run ..."  
 6 It is the sentence in that paragraph that begins:  
 7 "Third, merchants are heterogeneous, and an IF  
 8 ...(Reading to the words)... not the marginal merchant  
 9 benefit. This implies that the merchants who benefit  
 10 least from the card, say the large retailers, are likely  
 11 to fail the tourist test at the social optimum."  
 12 So a caveat: danger, a red flag in relation to large  
 13 retailers.  
 14 Again, you will probably already see how this is  
 15 going to be an issue because when we come to the  
 16 Deloitte survey, the data is all for large retailers.  
 17 And Rochet and Tirole themselves -- and the Commission  
 18 do, to be fair, in 2015, put a red flag up about relying  
 19 solely on large amounts.  
 20 But just to finish on the Rochet and Tirole.  
 21 Professor Beath may know; Rochet and Tirole, I don't  
 22 know if they fell out or had a difference of view  
 23 because the next time we see Professor Rochet  
 24 resurfacing he has a different partner, Rochet & Wright.  
 25 There's an article; it is published in a number of

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1 places. It is published in 2009 and 2010, which is why  
 2 I think we see references to it in different years but  
 3 it is the same one. We will look at it because what it  
 4 shows is that Professor Rochet has moved away from a MIT  
 5 test, but we will see in the 2009/2010 article he is  
 6 actually advocating a cost based approach. That's E3.6,  
 7 tab 130A. We see the title is --  
 8 PROFESSOR JOHN BEATH: 3.6?  
 9 MR HOSKINS: E3.6 tab 130A. Sorry, it is the Scottish  
 10 accent.  
 11 PROFESSOR JOHN BEATH: I was looking at blue papers.  
 12 MR HOSKINS: Turn over the page to 2562, and you will see  
 13 the heading:  
 14 "Jean Charles Rochet, Julian Wright."  
 15 Then it is at 2569A.5 is the introduction to  
 16 2569A.7. An easy way to do this, my Lord, if you are  
 17 getting tired, do you want to read this overnight?  
 18 MR JUSTICE BARLING: We could do, yes. I do suffer from  
 19 insomnia so it will be a great cure for it.  
 20 MR HOSKINS: I need you to read 2569A.5 to 2569A.7. I was  
 21 going to say --  
 22 PROFESSOR JOHN BEATH: It is the introduction you want us to  
 23 read?  
 24 MR HOSKINS: Yes, the introduction. I was going to say  
 25 I will test you on it tomorrow but probably you will

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1 test me.  
 2 MR JUSTICE BARLING: We will take your suggestion I think in  
 3 that case and take it out and ...  
 4 MR HOSKINS: There is a bit of housekeeping. If you don't  
 5 mind it might be a good time to do that now.  
 6 MR JUSTICE BARLING: Yes.  
 7 Housekeeping  
 8 MR JUSTICE BARLING: Is that to do with confidentiality  
 9 rings?  
 10 MR BREALEY: No, it is just witnesses.  
 11 MR JUSTICE BARLING: Yes.  
 12 MR BREALEY: I don't know if you have got the --  
 13 MR JUSTICE BARLING: Yes, the timetable.  
 14 MR BREALEY: The timetable. So essentially for next week,  
 15 the week beginning 1st, if we can just -- you see on  
 16 Thursday the shaded day, which is a non-sitting day but  
 17 it is reserved for continuation of witnesses?  
 18 MR JUSTICE BARLING: I don't think it is any more.  
 19 PROFESSOR JOHN BEATH: I'm afraid I have an appointment at  
 20 the Palace.  
 21 MR BREALEY: On the Thursday?  
 22 MR JUSTICE BARLING: I'm afraid it has become rather less  
 23 contingent now and is now completely a non-sitting day.  
 24 MR BREALEY: Okay. I think we need to re-group overnight.  
 25 It is just Mr Coupe, Mr Rogers were hoping to give

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1 evidence on that day. I see that's out. It may well be  
 2 that we can do it on the Friday? The reason is, I mean  
 3 they, as you may have read in the press, there is  
 4 a Sainsbury's and Argos, there is an issue, and so it is  
 5 quite important that they --  
 6 MR JUSTICE BARLING: Look, you know our position. We will  
 7 be as accommodating as we can be for other days.  
 8 MR BREALEY: If we could go into -- I will obviously talk  
 9 with Mr Hoskins but if we could have Mr Coupe and  
 10 Mr Rogers on the Friday, and I will flag that with that  
 11 with them --  
 12 MR JUSTICE BARLING: Mr Coupe and Mr Rogers you think are  
 13 likely to be Friday?  
 14 MR BREALEY: That might just eat into my cross-examination  
 15 time which is pretty healthy anyway.  
 16 MR JUSTICE BARLING: Yes.  
 17 MR HOSKINS: We have a potential -- because Mr Abrahams has  
 18 to be Friday.  
 19 MR BREALEY: Mr Abrahams has to be Friday?  
 20 MR HOSKINS: Mr Brealey and I can talk but --  
 21 MR JUSTICE BARLING: You mean he has to be not before Friday  
 22 or he has to be --  
 23 MR HOSKINS: The only time he can come in that window is  
 24 Friday.  
 25 MR JUSTICE BARLING: How would Mr Coupe and Mr Rogers be

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1 fixed if they had to go after him on say the week of the  
 2 8th?  
 3 MR BREALEY: I would have to check but they have got to --  
 4 I know they have got busy diaries but at the end of the  
 5 day they have got to --  
 6 MR JUSTICE BARLING: Speaking for myself I have got no  
 7 objection if witnesses, even if your witnesses come  
 8 after an expert -- sorry they are a witness of fact.  
 9 Unless, as it were, there is some particular reason  
 10 why Mr Abrahams should go after them, then that could be  
 11 done that way round. Have a think about it.  
 12 MR BREALEY: I will have a think about it overnight.  
 13 MR HOSKINS: I think there is a potential problem with that  
 14 because they all deal with pass through. I'm slightly  
 15 uncomfortable with reversing the order of factual  
 16 witnesses on pass through where we go first.  
 17 MR JUSTICE BARLING: Have a conversation --  
 18 MR HOSKINS: I will have a conversation with Mr Brealey. We  
 19 will try and come up with an agreement rather than  
 20 requiring you to decide it. I'm slightly uncomfortable  
 21 about that, sir.  
 22 MR JUSTICE BARLING: Okay. We will revisit that tomorrow.  
 23 Anything else?  
 24 MR BREALEY: No.  
 25 MR JUSTICE BARLING: See you tomorrow.

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1 (4.30 pm)  
 2 (The court adjourned until 10.30 am  
 3 on Thursday 28th January 2016)  
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