

OPUS 2

INTERNATIONAL

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

Day 4

January 28, 2016

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1 Thursday, 28th January 2016
 2 (10.30 am)
 3 Opening submissions by MR HOSKINS (continued)
 4 MR JUSTICE BARLING: Good morning, Mr Hoskins.
 5 MR HOSKINS: Good morning, sir. I hope, if nothing else,
 6 Messrs Rochet and Wright aided your insomnia last night.
 7 MR JUSTICE BARLING: Yes, I slept very well. No, we've read
 8 it carefully.
 9 MR HOSKINS: You've read it, so I will be brief. If we can
 10 start, therefore, in bundle E3.6, tab 130A.
 11 If I can pick it up at point 6, you will see that
 12 the first paragraph on that page begins:
 13 "Given the obvious importance ..."
 14 It is the second sentence of that paragraph:
 15 "The point of departure from the existing literature
 16 is to model credit cards explicitly. An existing
 17 literature model's price determination and payment cards
 18 networks initiated by Schmalensee, Rochet and Tirole
 19 with the earlier date, and Wright. The models in this
 20 literature have essentially focused on the choice
 21 between payment cards, which could just as well be debit
 22 cards, and cash or cheques. We contribute to this
 23 literature by extending the models to allow a separate
 24 role for the credit functionality of credit cards
 25 thereby allowing us to discuss credit card interchange

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1 fees specifically."
 2 This is very important in this case because
 3 hopefully you have picked up from our skeleton, because
 4 of the Maestro experience, MasterCard has very little
 5 presence in the debit card market, which means that
 6 credit cards make up over 99% of the value of this
 7 claim. So it is the credit card MIF that really matters
 8 in this case.
 9 Going on:
 10 "In our model, credit cards can be used for two
 11 types of transactions: Ordinary purchases for regular
 12 convenience usage for which cash or a debit card are
 13 assumed to provide identical benefits, and for credit
 14 purchases where credit is necessary for purchases to be
 15 realised.
 16 "Credit purchases include a range of different types
 17 of purchases, such as unplanned purchases, impulse
 18 purchases and large purchases for which the consumer
 19 does not have the cash ...(Reading to the words)... of
 20 payment facilitates the transaction."
 21 So two types of transaction.
 22 Then, you have read this, so I'm not going to read
 23 it all out, but the top of point 7:
 24 "Since consumers do not internalise retailers' cost
 25 savings from avoiding direct provision of credit and

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1 since merchants cannot distinguish the type of consumer
 2 they face, there is also a case for setting a relatively
 3 high interchange fee so that consumers that wish to rely
 4 on credit are induced to use credit cards when it is
 5 efficient for them to do so. For this reason, to
 6 maximise consumer surplus, including the surplus of cash
 7 customers, may require setting an interchange fee which
 8 induces excessive usage of credit cards for ordinary
 9 purchases."
 10 So you set the level to encourage the use for credit
 11 purchases accepting that it might lead to a degree of
 12 inefficiency for ordinary purchases.
 13 Then the next paragraph -- I pick it up at the
 14 second sentence:
 15 "The theory suggests one of two possible caps will
 16 maximise consumer surplus. Depending on the relative
 17 costs and benefits of the different instruments, the cap
 18 should either be based on the issuer's costs to avoid
 19 excessive usage of cards for ordinary purchases ..."
 20 That's akin to what the Commission did in the 2002
 21 Visa decision and it is akin to Dr Niels' adjusted cost
 22 benefit approach:
 23 "... or on merchant's net avoided costs from not
 24 having to provide credit directly, so that consumers use
 25 their cards efficiently for credit purchases. Since

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1 evaluating which of the two options gives higher
 2 consumer surplus is informationally very demanding,
 3 a conservative regulatory approach would be to cap
 4 interchange fees using the maximum of these two levels,
 5 which is likely to be the latter option."
 6 So that is the merchant's avoided costs for
 7 providing their own credit:
 8 "In our model this always raises consumer surplus
 9 ...(Reading to the words)... will sometimes result in
 10 the best outcome for consumers. In contrast, using
 11 issuer costs to regulate interchange fees is
 12 realistically only likely to give a lower bound of
 13 possible interchange fees that maximise consumer
 14 surplus."
 15 They are saying for credit cards, two options.
 16 There are informational difficulties and nobody before
 17 you is suggesting the avoided cost to merchants of
 18 providing their own credit.
 19 What Dr Niels is suggesting is the issuer's cost
 20 methodology proposed here. That is one of the
 21 methodologies that Rochet and Wright say is appropriate
 22 for credit cards. They do not suggest the MIT is
 23 appropriate for credit cards, and they say using that
 24 issuer's cost approach is likely to give a MIF which is
 25 the lower bound of the best interchange fee.

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1 So where does that leave us? The Commission formal
 2 decisions they have adopted, exemption decisions,
 3 commitments etc, and EU regulation are based on limited
 4 data which I think is now generally accepted to be
 5 pretty much insufficient for purpose. That is the old
 6 national bank studies. In addition, those Commission
 7 decisions in the regulations rely on an academic theory,
 8 that's Rochet and Tirole, which I showed you yesterday
 9 on its face says that it will give too low a figure for
 10 MIF if welfare is one of the policy objectives. And
 11 I showed you that it is, and which Rochet, one of the
 12 authors of Rochet and Tirole, now says isn't suitable
 13 for credit cards, which, in our submission, means that
 14 what the CAT should do is to assess the evidence which
 15 it has before it to produce a more robust proxy. And we
 16 say you are in a position to do that. You will have the
 17 evidence, you will hear the evidence.
 18 But what this shows is that MIT isn't fit really for
 19 this purpose according to its own creator, and certainly
 20 even if one were to do a MIT to try to get a grip, to
 21 get an idea of how you wield the broad axe, it needs
 22 adjustment because the Rochet and Tirole does not take
 23 account of the specificities of credit cards.
 24 One little point that crops up, and this is not an
 25 ideal place to take it but I will take it now, is

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1 Mr Brealey's free rein point. He says you need to have
 2 objective criteria, so he is talking about in the past,
 3 and we will see, I will come to it, the way in which
 4 MasterCard set its MIF had certain characteristics.
 5 I can't remember if they are all confidential or not,
 6 but it was based largely on cost surveys and certain
 7 other factors with them taken into account. I will come
 8 back to that.
 9 He said that's not acceptable because he showed you,
 10 I think it was in the Visa decision that the exemption
 11 was premised on the basis that there would be objective
 12 criteria applied for the future in order to grant
 13 an exemption.
 14 But there's really nothing in that point because
 15 MasterCard did predominantly seek to base its MIF on
 16 costs, and actually what we see from the evidence is it
 17 set the actual level of the MIF below the level of the
 18 costs that were indicated by the EDC cost studies. So
 19 it wasn't taking the costs and then using other factors
 20 and pushing the MIF up, it was taking the cost studies,
 21 taking other facts into consideration and pushing the
 22 MIF down from what would be justified by the costs.
 23 The best place I can show you that is in our
 24 skeleton argument. It is paragraphs 86 and 76. So that
 25 is bundle A, tab 2 at page 190. The numbers are

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1 confidential so I have to be a bit careful here. But
 2 paragraph 86 gives you the results of the cost studies
 3 and you will see the percentages there, blue
 4 confidential.
 5 If you compare those with the weighted average rates
 6 actually charged, which are at paragraph 76, and it is
 7 the credit card figures we are interested in, you will
 8 see the substantial reduction.
 9 MR JUSTICE BARLING: Yes.
 10 MR HOSKINS: So 86 and 76(a).
 11 PROFESSOR JOHN BEATH: I can't actually see it, it is too --
 12 MR JUSTICE BARLING: It is very ...
 13 MR HOSKINS: What can I do? Can I hand up a tab with the
 14 number written on it and you can pass it along? (Pause)
 15 PROFESSOR JOHN BEATH: Okay, that's fine.
 16 MR HOSKINS: Thank you.
 17 MR JUSTICE BARLING: We will adjust our skeletons
 18 between us.
 19 MR HOSKINS: The second point is, for the exercise we are
 20 currently engaged in, which is looking backwards to
 21 determine what the exemptable level of the MIF would
 22 have been, it doesn't actually matter how MasterCard set
 23 its actual MIF because what, of course, we are engaged
 24 in is looking with the benefit actually of material that
 25 MasterCard didn't have at the time, because we are going

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1 to go and look, for example, at the Commission's 2015
 2 survey, with the Rochet and Wright article etc.
 3 So what survey was actually doing is, with the
 4 benefit of looking backwards and seeing whether the
 5 MasterCard level was above or below what is now
 6 determined to be the exemptable level of the MIF.
 7 For our purposes it doesn't matter how MasterCard
 8 got there. Even if it did that and stuck its finger in
 9 the air, as long as the answer comes out in the right
 10 place, that's enough.
 11 The reason why objective criteria is important in
 12 exemption decisions is of course it is forward looking.
 13 What the Commission is saying is "We will give you
 14 an exemption, but you have to do the following going
 15 forward". But we are engaged in a purely ex-post,
 16 looking backwards exercise. It doesn't matter how
 17 MasterCard has got there historically as long as it got
 18 to the right place. So it is really just a red herring,
 19 that free rein point.
 20 I have been through a lot, so let me do an interim
 21 conclusion. We still have a little bit to go on
 22 exemption and take stock of where we are. First of all,
 23 we say the Tribunal is free to make up its own mind
 24 about the exemptable level of the UK domestic MIF and it
 25 doesn't have to necessarily use a MIT to do so. We saw

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1 that, for example, in recital 50 of the 2014 Visa
 2 decision. I took you to that yesterday. But the quote
 3 from it, the relevant bit of the quote is:
 4 "National courts are well placed to assess MIFs set
 5 by local members domestically."
 6 You will see that again in the 2015 Commission
 7 study. It says: we are doing this, but national courts
 8 and regulators are well placed to look at domestic MIFs.
 9 So you have actually been invited to do so by
 10 the Commission.
 11 In the real world, second point, the MIT will tend
 12 to underestimate social welfare. We saw that in the
 13 2008 Rochet and Tirole article. And social welfare is
 14 one of the objectives of EU competition law, we saw I
 15 think it was paragraph 33 of the Commission's 101(3)
 16 guidelines.
 17 Third point, in order to take account of credit
 18 purchase, in order to take account of the specificities
 19 of credit cards, what Rochet now says is that MIFs
 20 should be based on issuer costs or merchant's net
 21 avoided costs from not having to provide their own
 22 credit.
 23 Using issuer costs to regulate interchange fees,
 24 according to Rochet and Wright, is realistically only
 25 likely to give a lower bound of possible interchange

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1 fees. In any event, whether we are looking at MIT or
 2 issuer's costs, the Commission has never sought to
 3 calculate a MIT-MIF in its formal decisions on the basis
 4 of the 2015 survey data. We will come to the survey.
 5 That's next on our list. But the figures that it is
 6 arrived at, all the way up to the regulation, are based
 7 on the national banks' studies, not on its Deloitte's
 8 surveys.
 9 So our submission is the Tribunal is free to, and
 10 should, make up its own mind on the exemptable level of
 11 the MIF based on the evidence before it.
 12 Can we turn now to the 2015 Commission survey. It
 13 is bundle E3.10 at tab 202. You have seen from the
 14 previous Commission material we have looked at that
 15 the Commission instructed Deloitte's to carry out
 16 a merchant cost study for it and then it produced this
 17 report setting out some updated views on the MIT in
 18 light of that survey.
 19 If we can pick it up at page 429.4, "Executive
 20 summary and conclusions". Again, if I can do that,
 21 asking you to read, because it will save time. If you
 22 can read paragraphs 1 to 3 and then I will pick up some
 23 points.
 24 Points to note, paragraph 2, the last sentence:
 25 "The study can therefore serve as a basis for debate

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1 and further research."
 2 This is the not the final word, it is an invitation
 3 for further consideration and that's what I'm inviting
 4 you to do.
 5 Paragraph 3, final sentence:
 6 "Obviously, if and to the extent that parties
 7 disagree with this and other methodological choices
 8 discussed in the report, or wish to argue that certain
 9 elements are not applicable for their specific case,
 10 they would have to bring forward arguments and/or
 11 further evidence."
 12 That, of course, is what we are doing before you.
 13 Again, the Commission is recognising that that is
 14 something that's acceptable, indeed one would say
 15 encouraged, because we are trying to push forward what
 16 has been a pretty rudimentary treatment of the
 17 assessment of the acceptable level of MIFs up to date.
 18 Then paragraphs 4 to 5. Again, if I could ask you
 19 to read those. This raises certain reliability issues
 20 about the data here.
 21 The points to note there are that because of the
 22 difficulties of compiling information, you will see at
 23 the bottom of paragraph 4, the second last sentence:
 24 "It was decided to focus the cost measurement only
 25 on large merchants in ten countries with the highest

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1 retail turnover in the EU. Eventually this represents
 2 a trade-off between precision of data and sample size
 3 and representativeness. Furthermore, the data
 4 collection did not manage to reach the target number of
 5 replies. Several ...(Reading to the words)... to
 6 justify their refusal to participate."
 7 This is one of the principal issues between the
 8 experts if one is to use a MIT-MIF, because Dr Niels
 9 suggests that because the 2015 survey data is limited
 10 only to large merchants, it is appropriate to make some
 11 adjustments to try to deal with that fact.
 12 Mr von Hinten-Reed suggest the adjustments are
 13 unnecessary. I will come and I will detail the specific
 14 differences between the experts, but as we are going
 15 through the survey I think it is useful to flag them up
 16 as well.
 17 Then if I could ask you to read paragraphs 6 to 8,
 18 which deal with the timescale to be adopted in
 19 a calculation and the split between fixed and variable
 20 costs. It is the perennial problem of the shorter the
 21 timescale, the more costs you exclude, the longer the
 22 timescale, the more costs you include in taking it into
 23 consideration.
 24 MR JUSTICE BARLING: 6 to 8?
 25 MR HOSKINS: 6 to 8.

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1 Just to note that the appropriate timescale for
 2 calculating a MIT-MIF is another principal issue between
 3 the economists because Dr Niels believes that a longer
 4 timescale is more appropriate than the one that
 5 Mr von Hinten-Reed suggests.

6 Paragraph 13, if I could ask you to read that,
 7 please. So what the Commission is concerned with here
 8 is that, for the purposes of gathering the data, it was
 9 the merchants themselves who allocated cost to fixed
 10 variable. And given the Commission itself recognised
 11 a problem of self selection bias, you immediately see
 12 the problem.

13 What the Commission did was a third type of
 14 analysis, which was to use an econometric technique, and
 15 the strength of it, you will see mid-way down,
 16 paragraph 13:

17 "The first econometric techniques are capable of
 18 identifying fixed and variable costs without relying on
 19 the merchant's views."

20 That is one advantage of it.
 21 Then at the bottom of the page:

22 "Second, econometric techniques allow for testing
 23 and accounting for different sources of heterogeneity
 24 across merchants ..."

25 So accounting for differences:

13

1 "... and therefore allow a richer modelling of the
 2 cost functions."

3 As always in the real world it is not perfect. It
 4 is fair for me to point that out:

5 "It is worth mentioning that the econometric
 6 estimations were constrained by the availability of data
 7 ... (Reading to the words)... potential imperfect
 8 modelling."

9 So there are problems on both sides.

10 Ultimately you are going to have to decide which is
 11 the most robust if you want to do a MIT-MIF approach,
 12 but there are problems on both sides.

13 Again, this is a principal issue between the experts
 14 because Dr Niels believes that the econometric technique
 15 is the best way to address various issues, including the
 16 subjective nature of allocations fixed and variable
 17 costs by experts.

18 It also allows one to take account of a longer
 19 period of time, and Mr von Hinten-Reed disagrees.

20 Then paragraphs 19 to 22. I don't need you to read
 21 the detail of this, but this is where one sees that
 22 the Commission presents a number of different MIT-MIF
 23 analyses based on different approaches.

24 Scenario 1 is what is called the short-term
 25 approach, and neither of the experts in this case

14

1 advocate a short-term approach. A medium-term approach,
 2 which it called scenario 2, you will see in
 3 paragraph 20, five lines up from the bottom:

4 "In the medium approach, scenario 2 ..."

5 That's Mr von Hinten-Reed's preferred approach.

6 And then thirdly, the econometric approach. That's
 7 Dr Niels' preferred approach if one does a MIT-MIF.

8 We don't need to go into the details just now, it is
 9 simply the existence of those three approaches I want to
 10 draw to your attention.

11 Then next I would like to go to paragraph 23:

12 "The report finally explores the possibility to
 13 obtain figures which would describe the whole merchant
 14 population, not only large merchants ... (Reading to the
 15 words)... Taking this into account and after careful
 16 consideration, the Commission therefore considers that
 17 without further data from small merchants it is not
 18 possible to draw reliable conclusions from the study
 19 concerning the level of indifference of all merchants."

20 That is important because remember from the Rochet
 21 and Tirole article, which is the genesis of MIT-MIF, it
 22 said one had to look at the average merchant.

23 So the Commission itself accepts that this exercise,
 24 not possible to draw reliable conclusions for level of
 25 indifference of all merchants.

15

1 Dr Niels suggests a means of taking account of this
 2 issue and Mr von Hinten-Reed doesn't agree with it. It
 3 is another source of disagreement between the experts.

4 But the experts do agree that one has to have a one
 5 size fits all MIF. So it is not the case, nobody is
 6 advocating that MasterCard and/or Visa have to have
 7 different MIFs for different merchants. And one can see
 8 immediately how that would not be practical because the
 9 four-party scheme does not deal directly with merchants.

10 So they both agree it is a one size fits all, it is
 11 an average.

12 Then paragraphs 24 to 26, the conclusion:
 13 "All results need to be considered taking into
 14 account certain caveats. The results therefore are
 15 merely a first attempt to consistently apply the MIF."

16 So if you want to apply a MIT-MIF, the Commission is
 17 welcoming, encouraging such an exercise.

18 25:

19 "Nonetheless, DG Competition believes these results
 20 are based on a precise and complete data set providing
 21 valuable cost information."

22 You can form your own view on that as we go through
 23 the case, how reliable and robust this is, having seen
 24 what the Commission itself says about the data set:

25 "There are still areas of improvements. In

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1 particular, two areas can be identified: the evaluation
 2 of a representative acquiring margin and ...(Reading to
 3 the words)... merchant's costs."
 4 I'll skip a sentence:
 5 "More difficult is the ...(Reading to the words)...
 6 proved to be a difficult task, while using information
 7 of large merchants to approximate the cost of small
 8 merchant is a questionable exercise."
 9 I have already flagged up that issue between the
 10 experts. Is it better to do something to try to address
 11 that, or to do nothing and just take all the large
 12 merchant data as the basis?
 13 So I have already sort of flagged up what the issues
 14 are for the Tribunal to decide on the MIT-MIF, but let
 15 me just set them out.
 16 If you wish to apply MIT-MIF -- and I'm going to
 17 come onto in a minute why we say you shouldn't, and we
 18 have already seen quite a lot of why we say it is not
 19 appropriate. But if you want to do this exercise, you
 20 have to decide whether you are going to apply it as
 21 suggested by Dr Niels or by Mr von Hinten-Reed or,
 22 indeed, you may decide to take an amalgam of the two.
 23 You might like some of the suggestions of Dr Niels, but
 24 not others.
 25 But the principal issues for you to decide are

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1 identified and discussed in our skeleton at
 2 paragraphs 229 to 278, and I'm not going to go through
 3 the skeleton now, but that's where you will find this
 4 written out.
 5 First issue, on what basis should the assessment of
 6 costs as fixed or variable be carried out? On the basis
 7 of the categorisations supplied by the merchants who
 8 took part in the survey, ie their own categorisation of
 9 costs as fixed or variable. That's Mr von Hinten-Reed's
 10 approach. Or on the basis of an econometric technique,
 11 which is Dr Niels' approach.
 12 Second issue, should the MIT be applied so as to
 13 take account of the fact that the information in the
 14 2005 Deloitte's survey only related to large merchants?
 15 Third point, should the MIT be applied so as to take
 16 account of online transactions? Fourth point, should
 17 the MIT be applied so as to take account of the fact
 18 that credit cards provide benefits to merchants but cash
 19 does not, for example, by allowing sales to be made that
 20 would otherwise not happen? And you will have seen that
 21 category recognised in the Rochet and Wright article.
 22 And that's what they say characterises credit cards.
 23 They don't just deal with ordinary transactions where
 24 you have cash or debit cards, there are functions they
 25 perform for the consumer which wouldn't otherwise be

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1 available if you only had cash or debit cards.
 2 Let me come to the costs-based approach, which is
 3 actually where the economic literature has got to for
 4 credit cards. It is Rochet and Wright. Because
 5 although Dr Niels has produced a MIT-MIF estimate,
 6 Mr Brealey says it is not. It is. It is a MIT taking
 7 account of the problems I have identified, that the
 8 Commission has identified. But he has serious
 9 reservations about using a MIT at all, just like Rochet
 10 and Wright do for credit cards.
 11 If you can go to his first report, it is D3, tab 3.
 12 At page 311, at 6.9 to 6.18. I was going to ask you to
 13 read it now, but if you are happy I can just leave it in
 14 your notes. I'm in your hands. If you are finding it
 15 helpful to build this up by accretion -- I would rather
 16 you read it now, I do not want you to --
 17 MR JUSTICE BARLING: We will read it now.
 18 MR HOSKINS: Hopefully this helps because there's so much
 19 paper and this shows you which bits of paper matter.
 20 MR JUSTICE BARLING: Feel free to sit down if you want to.
 21 MR HOSKINS: Thank you. (Pause)
 22 I'm going to come back to this in a minute, so if
 23 you can keep it out once you have finished reading it.
 24 For these reasons, Dr Niels' preference is for
 25 an adjusted cost benefit balancing approach, which is

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1 essentially the type of issuer's costs approach which we
 2 saw in Rochet and Wright.
 3 Dr Niels says: no, can't use this at all. But if
 4 one is to apply a cost-based approach, then there is one
 5 main issue of principle between the experts and that --
 6 MR JUSTICE BARLING: Do you mean Mr von Hinten-Reed?
 7 MR HOSKINS: I'm sorry, Mr von Hinten-Reed. I'm sorry.
 8 There is one main issue of principle between the
 9 experts if one is to adopt this approach, and that is
 10 whether the provision of credit is of any benefit to
 11 merchants or not.
 12 Mr von Hinten-Reed asserts that the provision of
 13 credit is of no benefit to merchants and therefore
 14 should be wholly excluded from the calculation. And one
 15 sees that, for example, at D2.1, tab 3, page 547,
 16 paragraph 615.
 17 If you could read 615, the point is clear in that.
 18 He says "exclude costs relating to provision of credit".
 19 Hopefully you will immediately see the problem with
 20 that approach when one thinks of the Rochet and Wright
 21 article. The whole reason why a cost-based approach is
 22 appropriate is because of the specific benefits that
 23 credit cards bring, ie they allow transactions in
 24 addition to ordinary transactions.
 25 So if one accepts that the cost-based approach is

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1 appropriate because of the features of credit cards, it
2 then makes no sense to exclude any of the costs that
3 relate to those particular features. That's one of the
4 troubles with Mr von Hinten-Reed's approach.

5 Dr Niels, on the other hand, just to show you very
6 quickly what his approach is, it is back in his first
7 report. So that is D3, tab 3, this time at page 305.

8 I'm sorry, 307. It is paragraph 5.89.

9 MR JUSTICE BARLING: Same report.

10 MR HOSKINS: Page 307, paragraph 5.89.

11 MR JUSTICE BARLING: Thank you.

12 MR HOSKINS: "Given the important benefits that merchants
13 derive from these costs", that is the costs of providing
14 credit, "in my opinion it would be reasonable but
15 conservative to attribute at least 25% or 50% of these
16 issuer costs to merchants."

17 He doesn't attribute all the costs, he says:

18 "... reasonable but conservative to attribute at
19 least 25% or 50% ..."

20 That's a point, clearly, that's going to have to be
21 explored in cross-examination with both experts, but it
22 won't surprise you to learn that we submit that
23 Dr Niels' approach is clearly preferable.

24 I'm almost done with exemption, but I want to finish
25 up with just focusing on this point about some aspects

21

1 of the nature of credit card use. You have already seen
2 Rochet and Wright's view. Let me just flag up some
3 aspects. Again, these are bound to come up in the
4 cross-examination.

5 MR JUSTICE BARLING: Can we put D3 away?

6 MR HOSKINS: We can put that away, sir. We will come back
7 to it at some stage.

8 First point is we say that credit cards clearly do
9 provide benefits to merchants. As we explained in the
10 factual background section of our skeleton, long before
11 any credit card schemes came into existence, merchants
12 offered customers credit. Think back to all those
13 Western films you used to see where everyone would go to
14 the general store and get things on credit. It has been
15 around a long time. It's been around for centuries.

16 The reason merchants did that is because they
17 recognised they would benefit from doing so. They also
18 must have recognised that the benefits of doing so
19 outweighed the costs of doing so. What's true then,
20 that is the reason why this started happening, it
21 remains true today.

22 From the outset as well, when payment systems did
23 come into existence, merchants had been willing to
24 accept credit cards despite these having higher MSCs
25 than debit cards. And the difference, the basic

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1 difference between a credit card and a debit card is the
2 provision of credit to the customer.

3 If the addition of that credit facility provided no
4 benefit at all to the merchant, the merchants would
5 never have begun to accept credit cards. But they did.
6 We say just as the genesis of the initial decision to
7 give credit and then the acceptance of credit cards
8 despite higher costs, it was all done because it was
9 beneficial to merchants. That remains the same today.
10 Retailers accepted credit cards throughout the period of
11 the claim because they benefit from doing so. The
12 benefits of accepting credit cards outweigh the costs.
13 To be honest, that's not really in dispute.

14 The case is we don't want to pay so much for
15 accepting credit cards, not that we pay so much that
16 they are loss-making. That is not put. And it wouldn't
17 be correct. We know that the benefits to Sainsbury's
18 and, indeed, many other retailers, substantially exceed
19 the costs involved in accepting MasterCard because
20 Sainsbury's and other retailers are willing to accept
21 American Express, but American Express is significantly
22 more expensive, has been significantly more expensive
23 than MasterCard throughout the relevant period.

24 You can see the relevant costs of MasterCard and
25 American Express. I'm sorry, I probably was too quick.

23

1 It is in Dr Niels' first report, D3, tab 3 at 368.
2 Page 368, figure 7.3.

3 So figure 7.3:

4 "Actual blended ...(Reading to the words)... at
5 Sainsbury's."

6 The red is Amex, the blue is MasterCard.

7 And you will see the differential in the different
8 respective costs to merchants of Amex and Sainsbury's.
9 We know, it is in the evidence, that Amex is less widely
10 accepted than MasterCard and Visa.

11 So if a merchant decides to accept Amex, it must be
12 because it believes the benefits outweigh the costs.
13 The costs of Amex are materially higher than the costs
14 of MasterCard, so it must follow that the benefits of
15 accepting MasterCard outweigh the costs of doing so.

16 Put it another way, Sainsbury's must believe that it
17 will have higher sales through accepting American
18 Express than through not accepting American Express. It
19 must believe it will have more sales through accepting
20 MasterCard than not accepting MasterCard.

21 I'm going to come back to Dr Niels, so let's put him
22 on one side. Second point is that what
23 Mr von Hinten-Reed says in relation to this is he says,
24 well, that's just transaction stealing. By offering
25 credit, a merchant merely obtains a transaction that

24

1 would otherwise have taken place at a competitor who
2 doesn't accept credit cards.

3 But with respect, that's a bad point, and the reason
4 it is bad is explained by Dr Niels at page 297 of this
5 first report at paragraph 5.49. So we are at D3, 3,
6 page 297, paragraphs 5.49 to 5.53, if I could ask you to
7 read that, please.

8 You see the point, the decision to accept or not
9 accept a particular type of credit card is just part of
10 the competitive process. Just as much about decisions
11 on opening hours with the costs that entails, about
12 provision of parking, advertising spend; it is just part
13 of the competitive process because if you don't accept
14 credit cards, then you will lose some sales to
15 competitors who do.

16 MR JUSTICE BARLING: It is an odd thing to call it, I must
17 say, "business stealing" because that's what
18 competition is.

19 MR HOSKINS: Precisely.

20 Third point, again, let's stay in Dr Niels and we
21 will go over the page to 299 at paragraph 5.59. If
22 I could ask you to read that, please.

23 This relates to a category of sales, nothing to do
24 with transaction stealing. This is a category of sales
25 that wouldn't take place at all absent a credit card and

25

1 provision of credit, and those are sales where the
2 cardholder ultimately defaults.

3 Therefore, there's a situation where a customer who
4 ultimately cannot pay for the purchase means that it is
5 a purchase that would not have taken place otherwise,
6 because the purchase could not have taken place without
7 the provision of credit. So it generates additional
8 sales which would not otherwise have happened.

9 If the merchants provided credit themselves, they
10 would get the benefit of these sales, but they would
11 bear the costs themselves of the default.

12 By making credit available to customers through the
13 acceptance of credit cards, the merchant gets the
14 benefit of the incremental sale and, under the current
15 MasterCard scheme, gets default protection. But default
16 protection has a cost.

17 If we go to page 291 of this report, you will see
18 table 5.1:

19 "Results of EDC pay later credit card cost studies
20 for the UK."

21 So these are the cost studies that were done for
22 MasterCard that it used to set the MIF. But we are just
23 here looking at the results of those cost studies. This
24 is confidential. So I have got to be a bit careful
25 with it. But you will see the costs involved in

26

1 cardholder default are those under the heading "Credit
2 write-offs".

3 You will see the percentage figure. You will have
4 in your mind the various sorts of percentages that are
5 around for suggested level of MIFs. But the simple
6 point is, we say, there's no justification for saying
7 that merchants should get the benefit of these sorts of
8 additional sales without making any contribution to
9 those costs.

10 Just staying on this table, on the first day of the
11 trial, this is transcript Day 1, page 167, line 25,
12 Mr Brealey sought to portray the key aspects of the
13 dispute between MasterCard and Sainsbury's about the
14 cost-based approach as being about whether it was
15 appropriate to take account of the interest free period,
16 also referred to as the free funding period. And you
17 will be aware of that, that it's normally 28 days, the
18 28-day period a cardholder has to pay off the credit
19 card before interest starts to accrue.

20 But let's look again at the EDC costs study, so
21 table 5.1. The costs of the interest free period are in
22 as the funding costs, and you will see the percentage
23 for that. You will see that that percentage means --
24 I can't even say it -- it is a certain percentage of the
25 total costs. I can't say it. I will have to ask you to

27

1 do the arithmetic.

2 MR JUSTICE BARLING: Funding costs?

3 MR HOSKINS: Funding costs. You will see the total ad
4 valorem interchange costs at the bottom, and you will
5 see how much of it is made up of funding costs.

6 We say really that Mr von Hinten-Reed's approach
7 should fail unless he can persuade you that no account
8 should be taken of these relevant costs, including
9 default costs, whatsoever because he excludes them.

10 MR SMITH: Mr Hoskins, this debate, in a sense, drags us
11 into why cardholders use cards and which sort of cards
12 they use in preference to other forms of payment. And
13 obviously we are getting a lot of speculation about
14 that.

15 Isn't there some sort of survey evidence or data
16 done by someone, possibly MasterCard, which gives us
17 insight into what actually cardholders think when they
18 are --

19 MR HOSKINS: Think about what, sir? Sorry, so I can answer
20 your question.

21 MR SMITH: For example, we have been talking about why it is
22 that credit may be advantageous to cardholders and
23 whether one might use a credit card rather than a debit
24 card, and it occurred to me that some insight into
25 cardholders' thinking might assist us in working out

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1 whether, as Mr von Hinten-Reed suggests, all the
2 provision of credit does is enable one to buy now but
3 pay later and that in the medium term aggregate demands
4 stay at the same level, or whether there are other forms
5 of thinking on the part of cardholders which might
6 assist us.

7 MR HOSKINS: There's all sorts of surveys, and we see some
8 of the issues, for example, about whether over a long
9 term credit cards generate more sales than etc, etc.
10 Whether there's that particular type of evidence, I'm
11 not sure. I don't think, if there is, that it is before
12 the Tribunal.

13 The reason why we get to where we are by looking at
14 it through the rubric we are in because we are in 101(3)
15 territory, we are also in what's the exemptable level of
16 the MIF for overcharge territory. Lots of people have
17 looked at this over the years. It is pretty clear
18 people have decided that the best way to try and look at
19 this is through an appropriate proxy. The proxies on
20 the table, through learning and experience, are MIT-MIF,
21 and I have explained that, issuers' costs, and there was
22 the cost of merchants writing their own credit.

23 The way it has come before this Tribunal, because of
24 the accretion of learning experience, is it is MIT-MIF,
25 or it is costs, or you could do both and see, take

1 a view on the broad axe.

2 But in a sense I'm not trying to completely reinvent
3 the wheel, and I don't think we do have the evidence.
4 It might exist, but it is not before the Tribunal, I'm
5 pretty sure. There is evidence that would go to that
6 sort of issue, but sort of indirectly through costs in
7 relation to credit write-offs are a certain
8 percentage etc, so you know -- whether you call that
9 a cardholder, use that as an advantage, I can make
10 a purchase I can't pay for and never pay for.

11 So there is an aspect of that in these sort of cost
12 studies etc. But terms of what you are asking me, which
13 is go out and say to cardholders "What are the features
14 of a credit card you value? Is it the 28-day period?
15 Is it the fact you can default?" probably does exist,
16 but I don't think --

17 MR SMITH: Not before us, anyway.

18 MR HOSKINS: Mr Cook points out, for example, we have
19 a figure for the credit write-offs and we have some
20 figures for the extent to which customers will roll
21 over, ie not pay off the card within 28 days. There is
22 figures in relation to that, but they tend to be cost
23 figures, how much is it costing, rather than subjective.

24 But we know that some cardholders do this, so
25 whether one needs to say subjectively is this something

1 good? We know people use credit cards and roll over and
2 pay the interest. We know that people use credit cards
3 to buy something they don't currently have money for and
4 then they discover, or they know already when they make
5 the purchase, they are not going to have it in 28 days'
6 time, but they want things. We know all these things
7 happen, but we don't have that subjective evidence --

8 MR SMITH: It just crossed my mind in terms of the
9 transaction stealing point that there might well be
10 a class of transaction where, because of the monetary
11 amount involved, you would want to pay by way of card,
12 but that the nature of the purchase is actually a luxury
13 and not a necessity. So you actually wouldn't buy that
14 particular good but for having a credit or debit card.
15 But if we don't have it --

16 MR HOSKINS: I had this yesterday, you both put points to
17 me. One of my favourite ones against me. And I sort of
18 discouraged you both from going beyond the evidence,
19 because part of the trouble with this case is you have
20 seen how people have grappled with these problems over
21 the years. I could start speculating with you about
22 things that help me and you could start speculating with
23 me about things that don't help me etc, but I'm trying
24 to make this as objective as I can.

25 That's why the exercise I'm currently engaged with

1 is on the evidence we have, what are the particular
2 issues that arise. And I'm encouraging you, can't stop
3 you, to find on the evidence rather than -- and I accept
4 it's part of decision-making, you can go and speculate
5 and say "We think it is fair to assess on the basis --
6 you may well end up doing that. But I'm really keen to
7 try to say let's stick to the evidence before us and be
8 as objective as possible, and that may work in my favour
9 or against me at the end of the day but I'm trying to
10 keep it manageable for that reason.

11 MR JUSTICE BARLING: I don't know whether you are leaving
12 table 5.1 now, but I wasn't quite sure, were you
13 intending to make any comment? As well as drawing
14 attention to the funding costs percentage, are you
15 making a relative point as between that and credit
16 write-offs, or were you simply pointing to the fact that
17 funding costs are at that percentage?

18 MR HOSKINS: No, the point was that Mr Brealey focused on
19 funding costs as being the important cost in relation to
20 credit cards, and I'm saying actually it's not the
21 feature that's the most important.

22 MR JUSTICE BARLING: These EDC cost studies, I can't
23 remember now because it is some time since I read this,
24 is that in dispute, or are these generally --

25 MR HOSKINS: I'm not sure, because our evidence -- because

1 one of our witnesses goes into quite a lot of detail
 2 about how these cost studies were produced, and he will
 3 be cross-examined --
 4 MR JUSTICE BARLING: It is not obvious yet.
 5 MR HOSKINS: It is not obvious if they are agreed, no.
 6 The fourth point in this, and one gets this from
 7 paragraph 5.56 of Dr Niels' first report, so that is
 8 page 299, which is an obvious point really, but one sees
 9 it in the last sentence there, is that credit cards
 10 bring expenditure forward. So it is the net present
 11 value of cash points a transaction is made on a credit
 12 card, and whilst the cardholder doesn't have to pay
 13 within a 28-day period if they want to be interest free
 14 or later, indeed, they've got the benefit of credit,
 15 you'll have seen that the acquirer and the merchant get
 16 the money effectively immediately within 24 hours, or
 17 whatever it is, but the receipt of the cash by the
 18 merchant is brought forward.
 19 Another way to look at it is whether the merchant
 20 itself had offered credit, it wouldn't get paid later,
 21 but under this system it would get the money effectively
 22 immediately.
 23 These points I have been going through are aspects
 24 of the points that Rochet and Wright make about credit
 25 cards. They are not exactly the same, but I'm saying

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1 that Rochet and Wright recognise the benefit of credit
 2 cards beyond debit cards and cash. And this exercise is
 3 about saying yes, and here are some confirmatory
 4 examples and some further things for you to think about
 5 when you come to consider what's the appropriate way to
 6 consider a MIF for credit cards.
 7 Let me conclude on this point, which is what is the
 8 acceptable level of the MIF. Main points are these: if
 9 necessary, by which I mean if we ever get to the
 10 acceptable level of the MIF because we say there is no
 11 restriction, the Tribunal should wield the broad axe so
 12 as to arrive at the best estimate you can of the
 13 exemptable level of the MIF.
 14 As I said earlier, if the actual MasterCard UK
 15 domestic MIF during the period of the claim is lower or
 16 equal to the Tribunal's estimate, then the MIF will
 17 benefit from the exemption or there will be no damages
 18 because there is no overcharge. It is the same point.
 19 But there's obviously a legal distinction there.
 20 Sainsbury's doesn't get any damages.
 21 If the actual MasterCard UK domestic MIF during the
 22 period of the claim is higher than the Tribunal's
 23 estimate, then the actual MIF will not benefit from the
 24 exemption and the difference between the actual MIF and
 25 the Tribunal's estimate will represent the overcharge.

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1 If you get to this stage -- we say you don't -- if
 2 you get to the stage you of course will have the
 3 subtraction sum to do. And at page 274 of Dr Niels'
 4 first report, there is table 4.1 which sets out his
 5 calculations of the weighted average MasterCard MIF for
 6 transactions at Sainsbury's during the period of the
 7 claim.
 8 I must confess I'm not sure if this is agreed or
 9 not, but it is useful to know that so you know what
 10 figures you are working from when you need to calculate
 11 an overcharge, what figures you are dealing with.
 12 I'm about to move on if we get to damages
 13 calculation, what's involved in that. So that is
 14 probably, if it suits you a --
 15 MR JUSTICE BARLING: Yes, we ought to take a break. Are you
 16 going to say anything at all about the -- I think it is
 17 the Commission's point and others -- about the need to
 18 take account of the credit income, you know, the
 19 interest? But anyway --
 20 MR HOSKINS: Well, my point on that is Rochet and Wright.
 21 MR JUSTICE BARLING: They just say they haven't taken
 22 account of it. Somewhere I read that in their report,
 23 they say "Bear in mind our model doesn't include any ...
 24 Anyway.
 25 MR HOSKINS: You have put a marker down. I'm not intending

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1 to say anything about it now.
 2 MR JUSTICE BARLING: At this stage, okay.
 3 MR HOSKINS: I will take the point on board.
 4 MR JUSTICE BARLING: We will take a break.
 5 (11.40 am)
 6 (A short break)
 7 (11.50 am)
 8 MR HOSKINS: I'm now moving to a part of the case which we
 9 say you should never get to, but I have to deal with it,
 10 which is damages calculation.
 11 MR JUSTICE BARLING: Yes.
 12 MR HOSKINS: So if the Tribunal finds that the MasterCard UK
 13 domestic MIF applied during the period of the claim was
 14 a restriction, and finds that there was an overcharge,
 15 then you are into a quantum exercise.
 16 I'm going to deal with exemplary damages separately,
 17 for obvious reasons. But in relation to compensatory
 18 damages, the Tribunal would have to determine the
 19 following issues. First of all, what is the appropriate
 20 damages counterfactual? Secondly, to what extent, if
 21 any, did Sainsbury's pass on the overcharge in the MIF
 22 to its own customers? Thirdly, if Sainsbury's did pass
 23 on some or all of the overcharge, did this cause it to
 24 lose any sales? It is the so-called volume effect.
 25 Fourthly, what account needs to be taken of the change

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1 in corporate tax rates during the period of the claim?
 2 Fifth, what account needs to be taken of the fact
 3 that Sainsbury's would have received less benefits from
 4 Sainsbury's Bank -- I will explain that when we get to
 5 it -- if the MasterCard MIF had been lower during the
 6 period of the claim?
 7 Then, sixth, is Sainsbury's entitled to compound
 8 interest or simple interest? If it is entitled to
 9 compound interest, on what basis should it be
 10 calculated?
 11 There are issues tucked in and around those, but
 12 those are the main ones.
 13 So dealing with the first issue, the appropriate
 14 damages counterfactual, for your notes it is addressed
 15 at paragraphs 304 to 314 of our skeleton argument.
 16 I don't need you to turn that up now.
 17 As you are well aware, according to the basic
 18 principle of tortious damages, the claimant is entitled
 19 to be put into the position that he would have been in
 20 had the wrong not occurred, and therefore it is
 21 necessary to compare what actually occurred with what
 22 would have occurred if the wrong had not happened. So
 23 we are back into counterfactual issues.
 24 This raises three issues between the parties. The
 25 first issue is: what is the appropriate damages

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1 counterfactual? Mr von Hinten-Reed's position is that
 2 the appropriate damages counterfactual is to assume that
 3 if the wrong had not occurred, both MasterCard and Visa
 4 would have applied the same MIF, ie the lower MIF that
 5 Mr von Hinten-Reed identifies.
 6 I'm not sure if that figure is confidential, because
 7 I think it was referred to in opening. It would make
 8 life easier if I could say it.
 9 Can I just consult Mr Brealey. (Pause)
 10 MR BREALEY: Excuse me --
 11 MR HOSKINS: Do you want to take instructions? Sorry about
 12 this. It's just I will always have to use quite
 13 a longhand every time I refer to it.
 14 MR JUSTICE BARLING: The shorthand is both Visa and MIF
 15 would have applied the same MIF?
 16 MR HOSKINS: Exactly, the lower MIF.
 17 MR BREALEY: At the moment I'm told it is, but I shall
 18 find out.
 19 MR HOSKINS: That's fine. I wondered if I could
 20 short-circuit this.
 21 Dr Niels considers that the appropriate damages
 22 counterfactual -- this is all sounding very familiar,
 23 I am sure -- is one where MasterCard's MIF -- on this
 24 basis we're in damages territory, so it is the one which
 25 Mr von Hinten-Reed suggests, but Visa's MIF at the

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1 actual level that's applied. It is a similar debate.
 2 But the reason it is significant in this context is
 3 as follows. We have got the Maestro evidence, which
 4 tells us if there was that material difference in the
 5 MIFs MasterCard would have lost a large part of its
 6 business to Visa and Amex. Transactions which actually
 7 took place in the real world using MasterCard therefore,
 8 in the counterfactual world, would actually take place
 9 using Visa or Amex.
 10 In our damages counterfactual, the Visa MIF and Amex
 11 merchant costs are higher and therefore there's no loss.
 12 Is that sufficiently clear?
 13 I'm sorry, yes, it is not no loss, it is less loss,
 14 and I will explain that now. Because what Dr Niels has
 15 done is he has modelled the effect on the damages claim
 16 by Sainsbury's under his counterfactual, and as a result
 17 of the switching effect this analysis is based on the
 18 fact that in the counterfactual there would be a switch
 19 from MasterCard to Visa and Amex. But that will take
 20 a period of time, and during that period of time in the
 21 counterfactual world there will still be some
 22 transactions that take place on the MasterCard lower
 23 MIF, as opposed to the higher Visa and Amex MIFs, and
 24 that will have a damages value.
 25 We can see Dr Niels' calculation on this is -- again

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1 back to his first report, so it is D3, tab 3 and he
 2 deals with it at paragraph 7.38 to 7.50, which begins at
 3 page 364. But you can see the conclusion he reaches on
 4 this at page 369. Actually, go to page 368. If I could
 5 ask you to read paragraph 7.50.
 6 Then if you go over the page to table 7.3, you see
 7 that the effect of this switching exercise is that
 8 Sainsbury's total damages, which are in the region of
 9 200 million-odd, that's what they claim, would be
 10 reduced to 55 million-odd by this effect. So it is
 11 a substantial issue.
 12 So we hear a familiar issue of what's the
 13 appropriate counterfactual. As I have already submitted
 14 in relation to the previous counterfactuals, we say that
 15 the only basis upon which the Tribunal can find
 16 a restriction at all, that's what I submitted yesterday,
 17 is to adopt a legal fiction which ignores the reality of
 18 the market. That's my submission. By definition, if we
 19 get to this stage you have rejected that submission.
 20 However, what we see from the Court of Justice
 21 judgment in MasterCard is you can have different
 22 counterfactuals for different purposes. Horses for
 23 courses. Counterfactuals for courses.
 24 Our submission is that if the Tribunal is prepared
 25 to find a restriction on the basis of a legal fiction,

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1 it would be doubly harsh, doubly unfair, if it were then
2 also to assess damages on the basis of a legal fiction
3 rather than on the basis of what actually would have
4 occurred.

5 So don't damn us twice. You can adopt
6 counterfactuals for appropriate purposes. If you decide
7 that Mr Brealey's submission on restriction is
8 an attractive one for legal policy reasons or whatever,
9 it doesn't require you then to simply read across when
10 you come to a damages calculation.

11 The second point on the counterfactual. Assume you
12 are against me on the counterfactual and you decide to
13 assess damages on the basis of Mr von Hinten-Reed's
14 counterfactual. So that is his counterfactual is
15 MasterCard and Visa at the lower level, but Amex stays
16 at its actual level. It would then be necessary to take
17 account of the loss of business that would have
18 occurred, the switching that would have gone to Amex, to
19 MasterCard. Therefore, transactions in the real world
20 took place on the MasterCard MIF and the counterfactual
21 would take place, some of them, on the Amex merchant
22 fee, which is higher. So, again, that would go to
23 reduce the damages.

24 We have actually seen it before, but I would like to
25 show it to you again for this purpose, bundle D2, tab 2,

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1 page 211, paragraph 441.
2 MR JUSTICE BARLING: Yes, I see that.
3 MR HOSKINS: It is the 5%. I will show it to you again
4 because it comes up again in this context. Dr Niels
5 says actually the switch would have been much higher.
6 That is the dispute between the experts on this point
7 and that's obviously something that will be examined in
8 cross-examination, but I flag that up as the issue.

9 What would the switch to Amex have been under
10 Mr von Hinten-Reed's damages counterfactual? The third
11 point on the damages counterfactual is this: again, if
12 the Tribunal chooses to assess damages on the basis of
13 Mr von Hinten-Reed's counterfactual, then it will be
14 required to consider what MasterCard would have done if
15 it had been limited to setting the UK MIF at the level
16 suggested by Mr von Hinten-Reed. And Visa is in the
17 same boat.

18 MR JUSTICE BARLING: Sorry, did you have the reference to
19 Dr Niels' -- you said it would be much higher. Do you
20 want to give it --

21 MR HOSKINS: I will get it from the skeleton. I will ask
22 Mr Cook to look it up and I will shout it out once he
23 has found it.

24 If MasterCard had been constrained to adopt the
25 lower level of MIF during the period, what MasterCard's

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1 evidence is is that it would have been compelled to make
2 other changes to the scheme rules. For example, changes
3 to the payment guarantees that were offered in respect
4 of fraud and cardholder default. It would have had to
5 reduce the costs of the system because the MIF was
6 lower. It would have to have introduced different rules
7 about the timing of payment to the merchant. So rather
8 than having immediate payment, there would be
9 potentially some delay.

10 The argument is that these changes to the system
11 would have had disadvantages to the merchants in the
12 counterfactual, which would have to be taken account of
13 if you are assessing damages, and put in the position
14 you would have been if the wrong had not occurred. You
15 have to look at what the reduced benefits would have
16 been to merchants under the scheme, and the extra costs,
17 therefore, they would have to bear under the Sainsbury's
18 counterfactual.

19 The evidence about the changes that MasterCard would
20 have had to make to its scheme in light of a low or zero
21 interchange fee, if I just give you the references.
22 First Douglas, paragraphs 60 to 70, bundle C2, tab 2,
23 pages 38 to 41. First Perez, paragraph 17 to 52,
24 bundle C2, tab 5, pages 80 to 90. First Tittarelli,
25 paragraphs 5 to 55, bundle C2, tab 6, page 93. First

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1 Willeart, paragraphs 78 to 87, bundle C2, tab 7.

2 MR JUSTICE BARLING: C2, tab 7 where?

3 MR HOSKINS: Page 136.

4 So in the counterfactual world, a merchant would
5 have to bear increased costs relating to fraud,
6 cardholder default, timing of payment etc, and those
7 would have to be taken into account in the damages
8 calculation.

9 This is me trying to simplify the flowchart. I'm
10 going to move to pass-through now.

11 Pass-through. There is no dispute between the
12 parties that pass-through is legally relevant. I don't
13 need to go to it now, but at paragraphs 315 to 324 of
14 our skeleton argument, we explain that English law
15 requires the court to take account of the extent to
16 which any loss has been passed on to customers in the
17 assessment of damages.

18 That is the British Westinghouse case.

19 I know there is debate about the precise basis in
20 English law about pass-through, but in our submission,
21 British Westinghouse is a sound legal basis for
22 recognising the principle. But equally, it would just
23 be an aspect of you have put the victim in a position he
24 would have been had the wrong not occurred, and
25 therefore you take account of benefits, but

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1 British Westinghouse is one of the ways in which you can
 2 explain why pass-through is available in English law.
 3 Paragraph 287 of the Sainsbury's skeleton argument
 4 accepts that it is open to prove Sainsbury's has passed
 5 on the overcharge to its own customers, ie they accept
 6 that pass-through is relevant to quantification in
 7 English and, indeed, EU law. So the debate between the
 8 parties is not about whether pass-through is legally
 9 relevant, but what is the test for pass-through.
 10 What I would like to do to show you what the test
 11 actually is is to, I'm afraid, revisit as quickly as
 12 possible the authorities which Mr Brealey showed you to
 13 show you what propositions you should take from them.
 14 The first proposition that comes from those
 15 authorities is that national rules may ensure the remedy
 16 granted to a claimant who has been injured by a breach
 17 of EU law is not unjustly enriched. In the absence of
 18 EU rules governing such unjust enrichment, national law
 19 may be applied provided that it complies with the
 20 principles of equivalence and effectiveness.
 21 We don't need to go to them, but I will give you the
 22 references for the proposition. Case 68/79, Hans Just,
 23 paragraph 26, bundle I.4, tab 2, page 523. Also case
 24 C-453/99, Courage v Crehan, paragraphs 29 to 30,
 25 bundle I.4, tab 5, page 97.004.

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1 The second proposition one gets from the case law is
 2 this. National rules relating to pass-on may not apply
 3 legal presumptions or rules of evidence which place the
 4 burden on the claimant to prove that pass-on has not
 5 occurred.
 6 That's the San Giorgio case, and I do need to go
 7 that because there are some aspects of it I would like
 8 to show you that you didn't see with Mr Brealey. It is
 9 I.4, tab 3.
 10 What I would like to show you is actually what
 11 San Giorgio was about because you need to put the
 12 judgment in context. First of all, if we could pick it
 13 up at paragraph 2 on page 69.
 14 We see that the case was about the fact that
 15 San Giorgio, the plaintiff, was required to pay health
 16 inspection charges which were levied contrary to
 17 community law. And the reason why this case raised
 18 an issue that went to the Court of Justice, one sees
 19 from paragraphs 4 to 5, is because the claim went
 20 through the national courts, and in Italian law there
 21 was a provision which is set out at paragraph 4 of the
 22 judgment:
 23 "The state finance administration relied on
 24 article 10 of the particular law."
 25 It is the second part of the quote citation from the

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1 law.
 2 This is legal provision:
 3 "The charge is presumed to have been passed on,
 4 whenever the goods in respect of which the payment was
 5 effected have been transferred even after processing
 6 transformation ...(Reading to the words)... in the
 7 absence of documentary proof to the contrary."
 8 So you see it was a very onerous legal presumption
 9 of pass-on. Pass-on presumed unless documentary
 10 evidence to the contrary and San Giorgio complained that
 11 that particular legal provision was contrary to
 12 community law.
 13 Then you come to the paragraphs that you saw with
 14 Mr Brealey, so I will take them quickly. Paragraph 12
 15 I don't think you saw, but it sets out just the standard
 16 community right to restitution, national law, principles
 17 of equivalence and effectiveness.
 18 You see at paragraph 14 the court's reasoning for
 19 saying that such a presumption is not acceptable:
 20 "Any requirement of proof which has the effect of
 21 making it virtually impossible or excessively difficult
 22 ..."
 23 So it is an aspect of the principle of
 24 effectiveness:
 25 "... to secure the repayment of charges levied

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1 contrary to community law would be incompatible with
 2 community law. That is so particularly in cases of
 3 presumptions and ...(Reading to the words)... have not
 4 been passed on, or are special limitations concerning
 5 the form of the evidence to be adduced, such as the
 6 exclusion of any kind of evidence other than documentary
 7 evidence. Once it is established the levying of the
 8 charge is incompatible with community law, the court
 9 must be free to decide whether or not the burden of the
 10 charge has been passed on wholly or in part to other
 11 persons."
 12 There is no legal or evidential presumption of the
 13 sort that's considered in San Giorgio at play in the
 14 present case. We are inviting you to decide on the
 15 basis of all the evidence before you whether there is
 16 pass-on or not.
 17 The third proposition that comes from the European
 18 case law is that the question, and we have just seen it
 19 in San Giorgio, whether an overcharge has been passed on
 20 in each case is a question of fact to be determined by
 21 the national court, which may freely assess the
 22 evidence.
 23 So you see that, paragraph 14 of San Giorgio. You
 24 also saw it in Comateb at paragraph 25, bundle I.4,
 25 tab 4, page 88. Mr Brealey sought to try to put

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1 a restriction on the ability of the Tribunal, of courts
 2 generally, to assess the evidence freely, which is
 3 clearly the principle, by saying "Ah, this is
 4 an exception, it must be interpreted restrictively". He
 5 is trying to suggest somehow your ability to freely
 6 assess the evidence had to be done through some sort of
 7 restrictive framework. But let me show you why that's
 8 wrong.
 9 It is the Weber's Wine World case, I.4.4, tab 6. It
 10 is paragraphs 95 and 96. They are on page 125 of the
 11 bundle. You will see that what the court says there is:
 12 "As the exception, ie the pass-on, is a restriction
 13 on a subjective right derived from a community legal
 14 order, it must be interpreted restrictively. Thus, in
 15 the Bianco case the court held in particular that even
 16 though indirect taxes ...(Reading to the words)... final
 17 consumer and in commerce are normally passed on in whole
 18 or in part, it cannot be generally assumed that the
 19 charge is passed on in every case", ie the strict
 20 interpretation means you can't have general
 21 presumptions, general evidential presumptions.
 22 But even within a need to interpret it restrictively
 23 it is quite clear, as the court goes on to say:
 24 "Consequently, the question of whether an indirect
 25 tax has or has not been passed on in each case is

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1 a question of fact to be determined by the national
 2 court, which is free to assess the evidence adduced
 3 before it."
 4 There is no restriction on your freedom to assess
 5 the evidence. The restriction of interpretation means
 6 you can't have general presumptions of evidence or law,
 7 but it does not curtail the requirement on the national
 8 court or Tribunal to freely assess the evidence
 9 before it.
 10 Of course, for example, evidence as to economic
 11 theory, which one has from both Dr Niels and
 12 Mr von Hinten-Reed, is not a legal or evidential
 13 presumption. It is part of the evidence which the court
 14 may freely assess. I'm not sure Mr Brealey went quite
 15 this far, but there were shades of it. You cannot say:
 16 EU law forbids me from looking at economic theory when
 17 freely assessing where there is pass-through because the
 18 economic theory is just part of the relevant evidence.
 19 And of course, Dr Niels makes it quite clear we are not
 20 relying on economic theory to say there is a presumption
 21 that you must follow. It is simply part of the overall
 22 evidence that's before you and he makes that quite
 23 clear, and he accepts that.
 24 MR JUSTICE BARLING: I think the point he majored on was
 25 this granted directly part.

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1 MR HOSKINS: Which I'm coming to now.
 2 The fourth principle, we say, that comes out of the
 3 case law is that acts unrelated to the wrong upon which
 4 the claim is based cannot be relied upon so as to
 5 establish unjust enrichment. That's my definition, if
 6 you like, of what an indirect pass-through would be:
 7 acts unrelated to the wrong upon which the claim is
 8 based cannot be relied upon so as to establish unjust
 9 enrichment.
 10 Let me explain why I put it that way by reference to
 11 the Lady v Kid case, I.4, tab 9. Again, you need to see
 12 what the case is about because all that Mr Brealey has
 13 done is cherrypicked the word "direct" and sought to
 14 imbue it with meaning.
 15 If you pick up the judgment at page 199 of the
 16 bundle, at paragraph 1:
 17 "The reference for a preliminary ruling relates to
 18 the interpretation of community law and recovery of
 19 amounts wrongly paid."
 20 Then paragraphs 3 and 4:
 21 "By law number 840, the Kingdom of Denmark
 22 introduced a business tax known as the employment market
 23 contribution."
 24 Then paragraph 4:
 25 "In return for the introduction of the Ambi,

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1 a number of social charges of employers had been
 2 abolished."
 3 So A legislative change where a new law is
 4 introduced and certain other laws are abolished at the
 5 same time.
 6 The argument that the state ran was because of the
 7 different legislative provisions that had been adopted.
 8 Even though the new law imposed an unlawful charge, you
 9 got a benefit, because we changed other laws at the same
 10 time which favoured you, and we can rely on that to say
 11 you have not suffered any loss. And that's what the
 12 court was dealing with when you see the judgment.
 13 Mr Brealey took you to it at page 203, and in particular
 14 paragraphs 19 and 20. When the court refused to allow
 15 the State to rely on that argument and said in
 16 paragraph 20:
 17 "The direct passing on of the tax wrongly
 18 ...(Reading to the words)... levied in breach of
 19 European Union law," that's what it was talking about.
 20 Denmark could not rely on other law changes which
 21 were beneficial to traders to argue that a trader would
 22 be unjustly enriched if it were repaid payments made
 23 pursuant to a different unlawful law.
 24 You were also taken to Accor, which doesn't really
 25 add very much because it simply cited that paragraph

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1 from Lady & Kid. I will confess it is very difficult to
 2 get to grips with what was actually happening in Accor.
 3 It is all about particular provisions of company tax etc
 4 in France, but our submission, to keep it simple, is it
 5 doesn't add anything to the definition of "direct".
 6 Our submission is that the domestic law on passing
 7 on is entirely consistent with EU law, including the
 8 statement in Lady & Kid that only direct passing on can
 9 lead to unjust enrichment. And the quickest way I can
 10 make good that point is by reference to our skeleton
 11 argument. So that is bundle A, tab 2, paragraphs 317
 12 to 320. That's where we refer to the
 13 British Westinghouse case.
 14 If I can ask you just to refresh your memory on what
 15 the law said in that case. It is paragraph 319. If you
 16 could quickly read the quotes there, please. This is
 17 the domestic law.
 18 So what one sees in English law, the principle is,
 19 one sees it in different language, but for example, it
 20 is said that we are an injured party that takes action
 21 quite naturally arising out of the circumstances in
 22 which it was placed by the breach in the ordinary course
 23 of business. That can be taken account of in
 24 quantification. That's direct. Would that action form
 25 part of the continuous dealing with the situation with

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1 which it found itself and was not an independent or
 2 disconnected transaction? The court should take account
 3 of it in quantification. That's direct.
 4 "Any benefit arising from the action should take
 5 into account assessment of damages in those
 6 circumstances."
 7 It is all direct.
 8 That is the whole point. English law is the same as
 9 EU law. That's why I put it the way I did. The
 10 proposition is to put it from the other perspective that
 11 acts unrelated to the wrong upon which the claim is
 12 based cannot be relied upon so as to establish unjust
 13 enrichment. But related acts can. They are
 14 sufficiently direct in domestic law in the UK.
 15 What, really, Sainsbury's is trying to do here is it
 16 just picks the word "direct" out of the Lady & Kid
 17 judgment and then tries to play a semantic game with it.
 18 But let's look, because what one gets is we get
 19 a labelling by Mr von Hinten-Reed of what he considers
 20 to be direct and indirect pass-on. And if we can just
 21 briefly look at that at D2, tab 2, page 380. Part of
 22 this is confidential.
 23 It is paragraph 1169. You see he says:
 24 "I define 'direct pass-on' as any increase in retail
 25 prices resulting from an increase in cost."

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1 That is a sort of cost plus type situation.
 2 Then I will leave you to read his indirect pass-on,
 3 because part of it is said to be confidential. It is
 4 difficult to see how on earth it could be confidential,
 5 but I will do what I'm told.
 6 MR JUSTICE BARLING: Yes.
 7 MR HOSKINS: I say that if we make good that form of
 8 indirect pass-on, then clearly as a matter of domestic
 9 law it must be taken into account, see
 10 British Westinghouse. And clearly as a matter of
 11 community law, your taking into account is not precluded
 12 because it is sufficiently direct.
 13 MR JUSTICE BARLING: You say what he describes as indirect
 14 is good enough for you?
 15 MR HOSKINS: Exactly. Don't play with the language, that's
 16 why they have set up a semantic game. Take direct from
 17 Lady & Kid, then the expert says: this is what I call
 18 direct, this is what I call indirect. So what? The
 19 legal principle is quite clear that this is legally
 20 relevant if we make good the point on the facts.
 21 I make the point about the broad axe. You already
 22 have my submission that the broad axe should be applied
 23 to the quantification of damages. It allows you a broad
 24 discretion in the assessment of damages. I took you to
 25 the cases where both Mr Justice Rimer and the

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1 Court of Appeal both felt it was appropriate when
 2 wielding the broad axe to err on the side of
 3 under-compensation. And when you come to look at
 4 pass-through, it is simply part of the quantum
 5 calculation so it must also be subject to the broad axe
 6 and it must also be subject to the need to err on the
 7 side of under-compensation.
 8 Sainsbury's skeleton suggests otherwise.
 9 Paragraph 295 suggests that if the court is unable to
 10 determine the actual rate of any pass-on, then the
 11 pass-on defence must fail.
 12 Well, that's patently nonsense, I'm sorry. It is
 13 flatly inconsistent with the broad axe, and if you
 14 applied that logic to pass-on, we can only benefit from
 15 pass-on if we prove the actual rate, then you would have
 16 to apply the same exacting standard to Sainsbury's when
 17 trying to prove the overcharge. And good luck with
 18 that, given the economic evidence before the court. So
 19 that is hopeless.
 20 Sainsbury's skeleton, paragraph 288(c), suggests
 21 that:
 22 "Any uncertainty as to whether the overcharge has
 23 been passed on benefits Sainsbury's."
 24 No authority is cited in support of that
 25 proposition. And you have my submissions on the need to

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1 err on the side of under-compensation if you are
 2 wielding the broad axe.
 3 US law. Mr Brealey tries to pray in aid the policy
 4 decision that has been taken in US law to exclude
 5 pass-through and to limit claims in federal anti-trust
 6 law to direct purchasers. I was passed a note to point
 7 out, while Mr Brealey was making these submissions, that
 8 Sainsbury's itself was an indirect purchaser because the
 9 acquirer is in the middle and the MIF is only passed on
 10 to the MSC, which made me smile. But there is a better
 11 argument which is that US policy is irrelevant in
 12 English law and is said to be so by the Chancellor,
 13 Sir Andrew Morritt.
 14 I will show you Emerald Supplies v British Airways.
 15 It is 12.2, tab 13, at page 1762. This arises out of
 16 the air cargo litigation. Page 1762, it is
 17 paragraph 37. You see that Hanover Shoe was raised in
 18 the context of this particular issue. It was about the
 19 ability to bring collective action, and the issue was
 20 whether you could have a collective action where your
 21 direct and indirect purchasers, who clearly had a
 22 tension between who would actually get any pot at the
 23 end of the day. And Hanover Shoe was brought before the
 24 court and swiftly dismissed by the Chancellor at
 25 paragraph 37:

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1 "The judgment of the US Supreme Court in United
 2 ... (Reading to the words)... was a policy decision not
 3 open to the courts in England.
 4 "For that reason alone, it demonstrates that the
 5 problems the claimants ... (Reading to the words)...
 6 anticipate are better dealt with by Parliament than by
 7 stretching the use of a particular CPR rule to
 8 accommodate cases such as this."
 9 So you shouldn't allow US policy decisions to infect
 10 your application of the pure domestic law which we have
 11 in British Westinghouse. Put it out of your mind.
 12 What evidence do we have in this case? Well, we
 13 have set out a summary of the evidence upon which we
 14 rely. Our skeleton argument, paragraphs 325 to 346. It
 15 won't surprise you to know I don't intend to add
 16 anything to that at this stage, but one point I do want
 17 to just quickly knock on the head is this.
 18 For obvious reasons, and I would have done the same,
 19 Mr Brealey took great delight in saying "Look at what
 20 MasterCard submitted on pass-through in the past". Two
 21 points in relation to that. First of all, retailers are
 22 in a far better position to judge whether they have
 23 passed-through MSCs and retail costs or not.
 24 You will see in the evidence that they did say
 25 generally they did pass through MSCs. So retailers are

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1 far better placed than MasterCard to know whether they
 2 have passed through or not.
 3 The second point is what MasterCard did was it was
 4 making submissions and producing reports it had
 5 commissioned in order to put to regulators who were
 6 going to make decisions. And having heard the evidence
 7 from MasterCard, or submissions from MasterCard, and the
 8 evidence saying "We believe there is pass-through", and
 9 having heard the submissions of MasterCard saying "No
 10 pass-through", the retailers say "We do pass through",
 11 the regulators have invariably agreed with the retailers
 12 that they do pass through.
 13 So when one is looking at, well, MasterCard made
 14 submissions, they were not accepted by regulators, and
 15 I will give you one example of that.
 16 EU Commission. Can we go to our skeleton again,
 17 bundle A, tab 2, page 263. So you will see there that
 18 MasterCard hasn't actually got far with these
 19 submissions because they weren't accepted. The
 20 Cruickshank Report passed through. The OFT passed
 21 through. The Commission passed through.
 22 If you look in particular, this is leading to the
 23 regulation, 340(d):
 24 "The EU's proposal for the regulation. Such
 25 interchange fees paid by acquiring payment service

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1 ...(Reading to the words)... MSCs, which merchants in
 2 turn pass onto consumers. Thus, high interchange fees
 3 paid by merchants result in higher final prices for
 4 goods and services which are paid by all consumers."
 5 (e):
 6 "The Commission's impact assessment leading to the
 7 regulation", the same.
 8 These costs are passed on by merchants to consumers.
 9 And the preamble to the regulation itself, so the final
 10 reasons for its adoption, the justification for its
 11 adoption, recital 10:
 12 "Interchange fees remain part of the fees charged to
 13 merchants by acquiring ... (Reading to the words)...
 14 incorporate those card costs, like all their other
 15 costs, in the general prices of goods and services."
 16 So the EU has decided it is appropriate to regulate
 17 the level of MIFs because they are passed through by
 18 retailers leading to higher retail prices.
 19 So with respect --
 20 MR JUSTICE BARLING: That would mean you could never really
 21 get any damages in this situation.
 22 MR HOSKINS: This is just one of the aspects of evidence.
 23 Again, I'm going nowhere near --
 24 MR JUSTICE BARLING: "Incorporating them generally in costs,
 25 like all other costs", is that really what is being

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1 spoken of?
 2 MR HOSKINS: Sir, we will come to that. My point here is
 3 Mr Brealey has had his fun with MasterCard's
 4 submissions.
 5 MR JUSTICE BARLING: Yes. You are having your fun now.
 6 MR HOSKINS: What we will do, we have a number of heads of
 7 evidence, this is one of them and you will decide at the
 8 end of the day, looking at all the evidence in the
 9 round, whether we have established the indirect/direct
 10 pass-through in Mr von Hinten-Reed's category.
 11 That's it.
 12 The next heading in the flowchart, for your
 13 decision-making, is "Volume effects". Now, remember
 14 that this only arises if you have found there has been
 15 some pass-through, because then the issue is to what
 16 extent has this resulted in lost sales for Sainsbury's?
 17 MR JUSTICE BARLING: Yes.
 18 MR HOSKINS: Given this is a bit of a cul de sac, I will
 19 deal with it very quickly. It is dealt with in our
 20 skeleton argument at paragraphs 349 to 356.
 21 There is a large measure of agreement between the
 22 experts as to how any volume effect should be assessed.
 23 There are three points of dispute. First of all, the
 24 experts disagree about the counterfactual to be applied,
 25 and it is our old friend. Secondly, the experts

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1 disagree about the level of switching that would have
 2 taken place to Amex under Mr von Hinten-Reed's
 3 counterfactual. Another old friend. Thirdly, they
 4 disagree about the extent to which it is possible that
 5 consumers might switch to a lower priced product, but it
 6 might have a higher margin.
 7 I won't dwell on the detail of that, I just flag it
 8 up as the third issue between you. The point to retain
 9 in your mind is that you can have lower price products
 10 with higher margins. And our submission is that
 11 Sainsbury's does and is able to flex the way it prices
 12 to control its margins, so it can make better margins on
 13 lower priced products. And I will explain in closing
 14 why that can have an effect on the volume effect.
 15 The next heading is "Tax". Since the decision of
 16 the House of Lords in -- amazingly, I don't think it is
 17 in the bundle among all the authorities -- British
 18 Transport Commission v Gourley, it is 1956, Appeal Court
 19 185:
 20 "... it has been necessary to take account of the
 21 impact of taxation when assessing damages."
 22 I know why it is not in the bundle, it is because it
 23 is not an issue between the parties.
 24 Both experts say you should take account of tax, and
 25 nobody denies that. The reason why it is important here

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1 is the level of corporation tax has changed over the
 2 period. The experts agree that the impact of taxation
 3 reduces the size of Sainsbury's claim in the present
 4 case.

5 This is confidential, but I will show you
 6 Mr von Hinten-Reed's position. So that is the most
 7 conservative position for our purposes. It is the
 8 addendum to his second report, so it is D2.1, tab 6 at
 9 page 763. This is all confidential, so I will tread
 10 carefully.

11 If you look on page 764 at table 4.5, you can see
 12 that his calculation of the effect of taxation, you will
 13 see the figure at the bottom of that table:

14 "Total pre-tax damages, including tax effect," which
 15 actually means not taking account of the tax change.
 16 And you will see the figure there and then the figure
 17 above is total post-tax damages, and you will see the
 18 figure there.

19 So you will see that it makes a sizeable difference
 20 to the claim, and obviously that has to be taken into
 21 account.

22 MR JUSTICE BARLING: Sorry, where was the second one?

23 MR HOSKINS: Sorry, table 4.5.

24 MR JUSTICE BARLING: I have got that.

25 MR HOSKINS: The last two figures, there is a difference,

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1 what he calls total pre-tax damages.

2 MR JUSTICE BARLING: Yes.

3 MR HOSKINS: And total post-tax damages.

4 MR JUSTICE BARLING: Yes.

5 MR HOSKINS: The difference between them --

6 MR JUSTICE BARLING: The language is slightly counter
 7 intuitive because --

8 MR HOSKINS: It is.

9 MR JUSTICE BARLING: -- the one that is said to include the
 10 tax effect doesn't.

11 MR HOSKINS: It is because of what he is calling -- the
 12 easiest way to understand it is score out the words, or
 13 ignore the words "including tax effect". You will see
 14 "total pre-tax damages", "total post-tax damages", and
 15 you get a lesser sum once you take account of the tax
 16 changes.

17 MR JUSTICE BARLING: That level, in principle it is agreed
 18 that it reduces.

19 MR HOSKINS: You will see it has a material impact on the
 20 level of damages.

21 MR JUSTICE BARLING: Yes.

22 MR HOSKINS: The maths can hopefully be worked out this side
 23 of the room.

24 MR JUSTICE BARLING: Yes. Are your rival figures to be
 25 found somewhere?

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1 MR HOSKINS: Well, we have put our figures, in --
 2 particularly it is in our flowcharts, and I will come
 3 to that.
 4 MR JUSTICE BARLING: In your flowcharts.
 5 MR HOSKINS: I think there may be a problem with one of
 6 them, which we are currently investigating.
 7 MR JUSTICE BARLING: Right.
 8 MR HOSKINS: That's why I said the flowcharts are
 9 illustrative.
 10 MR JUSTICE BARLING: Yes.
 11 MR HOSKINS: I'm hoping we will be able to, this side of the
 12 bench, spare you from having to do the maths. As you
 13 have seen, it is what I'm trying to do. I am trying to
 14 put you in a position where, if you are having to try to
 15 calculate damages, have a decent stab at it.
 16 We are going to keep the addendum we have just
 17 looked at out. The next heading is:
 18 "The effect a lower MIF would have on the benefits
 19 to Sainsbury's from Sainsbury's Bank."
 20 Again, this is an agreed deduction:
 21 "Sainsbury's Supermarkets benefited from the fact
 22 that Sainsbury's banks offered Nectar points to its
 23 MasterCard holders which could be used to make purchases
 24 in Sainsbury's."
 25 If the MasterCard MIF had been lower, the Nectar

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1 points offered by Sainsbury's Bank to its cardholders
 2 would also have been lower, and therefore there would
 3 have been less purchases in Sainsbury's as a result.
 4 There would have been less Nectar points to use for
 5 purchases in Sainsbury's Supermarkets.
 6 So the experts agree there is a need for a deduction
 7 for that reason, but they disagree as to the amount of
 8 the reduction.
 9 Again, just to show you the level of figures. It is
 10 in the addendum to Mr von Hinten-Reed's second report,
 11 so it is the one we have just looked at. This time it
 12 is at table 4.7, 4-7 on page 765.
 13 MR JUSTICE BARLING: Same page, yes.
 14 MR HOSKINS: You will see again the figures are
 15 confidential, but the table --:
 16 "Total damages before including the impact of Nectar
 17 awards."
 18 Then:
 19 "The impact of Nectar awards."
 20 Then:
 21 "Total damages excluding the Nectar awards."
 22 MR JUSTICE BARLING: It should be --
 23 MR HOSKINS: Again, it is slightly difficult language.
 24 Again, you will see the value of the Nectar awards on
 25 the reduction that has to be made according to

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1 Mr von Hinten-Reed.
 2 MR JUSTICE BARLING: Including the impact of --
 3 MR HOSKINS: If you take the middle figure, you will see the
 4 value of the deduction.
 5 MR JUSTICE BARLING: Yes.
 6 MR HOSKINS: As I say, there is a dispute as to the amount.
 7 You get the counter position from fourth Harman, D3.1,
 8 tab 7. You can get his figure from paragraph 2.25 on
 9 page 650. This is where he sets out in a table his
 10 calculation of the benefits that would be lost to
 11 Sainsbury's Supermarket of the lower MIF. So D3.1,
 12 tab 7, page 650.
 13 MR JUSTICE BARLING: Yes.
 14 MR HOSKINS: He sets out in the rows his calculation of the
 15 benefits that would be lost, and the figures for
 16 comparison to compare with Mr von Hinten-Reed is in the
 17 total row. It is the final one under the column
 18 "Difference GB pounds million". You will see the
 19 figure.
 20 MR JUSTICE BARLING: Yes.
 21 MR HOSKINS: Which I'm not allowed to say.
 22 MR JUSTICE BARLING: Yes.
 23 MR HOSKINS: But that's the dispute. There is to be
 24 a deduction --
 25 MR JUSTICE BARLING: But it is a higher --

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1 MR HOSKINS: Exactly. It is just the exact amount.
 2 Sir, I'm conscious that if we get to this stage, you
 3 wielding your broad axe have to come up with a figure in
 4 pounds and pence. One could have a situation where, for
 5 example, you delivered a judgment, we all went away to
 6 consider it and came back and argued about the pound and
 7 pence, but it is probably not an attractive prospect to
 8 anyone. So what we have tried to do is see if there is
 9 a way in which we can help you come up with the pounds,
 10 hence our flowcharts that we appended. They are
 11 illustrative; they don't include everything.
 12 For example, they don't include the Nectar card
 13 benefits, if I can use that shorthand, we just looked
 14 at. They are not in the flowcharts. They also don't
 15 include the extra costs that merchants would have had to
 16 bear because MasterCard would have changed its scheme if
 17 the MIF had been lower. So it would have changed the
 18 fraud protection rules, the default payment
 19 guarantee etc.
 20 It doesn't take account of that, so the illustrative
 21 figures still have a couple of chunks taken out of them.
 22 But we put them forward at this early stage to see if
 23 there's a way in which we could help you, and say, look,
 24 if you find this helpful we are happy to refine them.
 25 The other side said can we have the calculation and

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1 we said of course, because it seems to us if we can come
 2 up with some sort of collaborative charts that's even
 3 better if that assists you. I must admit the
 4 Sainsbury's flowchart wasn't very helpful because
 5 there's so much missing from it. It gave you a sort of
 6 here is the highest figure, here is the lowest figure.
 7 It is not even actually the lowest figure, because the
 8 lowest figure is zero. Even if we are doing quantum
 9 there is a restriction. But if you find it useful,
 10 happy to take it further. Happy to take it further with
 11 Sainsbury's, and if you have got any indications that
 12 you want to give us at any stage as to what you would
 13 find useful in relation to the charts, obviously we will
 14 do what we can.
 15 That is why we put them forward. This isn't really
 16 an advocacy exercise at all, those charts. It is just
 17 supposed to be seeing if we can help.
 18 MR JUSTICE BARLING: Well, we are duly grateful, thank you.
 19 MR HOSKINS: Compound interest, Mr Cook is going to deal
 20 with. So I will just put a marker down for that. You
 21 can slot it in.
 22 The last point I need to deal with with you is
 23 exemplary damages. Sainsbury's claim for exemplary
 24 damages is explained very half heartedly in its
 25 skeleton, paragraphs 429 to 438. It was not dealt with

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1 at all in opening, so I will make the usual forensic
 2 point, which is that I'm not sure whether this is being
 3 pursued and whether or not their heart is in it. What
 4 I would like to do is kill it at best, then we won't
 5 have to waste any more time on it.
 6 The law on exemplary damages, and in particular its
 7 application in the context of competition law, has of
 8 course been considered by the Tribunal in two recent
 9 cases, Cardiff Bus and Albion Water.
 10 Cardiff Bus is at 1.6, tab 11, at page 352. If
 11 I can ask you to pick it up, paragraph 448. It sets out
 12 some of the general principles established by the law in
 13 relation to exemplary damages. For example, we see the
 14 object of exemplary damages is to punish and deter. At
 15 the bottom of that page, exemplary damages are a remedy
 16 of last resort which are not to be encouraged. And at
 17 the court's inderence, discretion towards exemplary
 18 damages must be cautiously exercised.
 19 You see at paragraph 451, they are well known, there
 20 are three categories of cases where exemplary damages
 21 can be potentially granted, and we are in the second
 22 category, or rather we are dealing with the second
 23 category. We say we are not in it.
 24 Sainsbury's says:
 25 "Conduct calculated to make a profit which may well

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1 exceed the compensation payable to the claimant."
 2 That second category, the contents of it, is defined
 3 at paragraph 461 of the Tribunal judgment. You will see
 4 the reference to Rookes v Barnard. It actually has two
 5 limbs, so the claimant has to show two things. It has
 6 to show, first of all, a cynical disregard for
 7 a plaintiff's rights, and secondly, it has to show
 8 a calculation that the money to be made out of the
 9 wrongdoing would probably exceed the damages at risk.
 10 Then paragraphs 480 to 490 analyse what is meant by
 11 the first limb of the test, "cynical disregard of the
 12 claimant's rights". I would like to draw your attention
 13 in particular to paragraph 484:
 14 "On the face of it, Lord Devlin's second category is
 15 specifically aimed at the punishment and deterrence of
 16 such calculated risks. Yet we consider that, unless we
 17 are compelled to by higher authority, to impose an
 18 undertaking is an exposure to exemplary damages in all
 19 cases where a company proceeds with conduct despite
 20 there being a known risk of an infringement of the
 21 chapter 2 prohibition would be wrong."
 22 490:
 23 "We consider that it will only be in those cases
 24 where an undertaking is aware that its proposed conduct
 25 is either probably unlawful or clearly unlawful that

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1 a risk can be classed as unacceptable. Whether the risk
 2 is in fact unacceptable will, in addition, depend on all
 3 the facts of the case, including for example any
 4 expected pro-competitive effects of the conduct that
 5 ... (Reading to the words)... by following a different
 6 course of action with less serious anti-competitive
 7 effects."
 8 I'm probably not doing justice to the detail of the
 9 judgment, but at least one of you is very familiar
 10 with it.
 11 Albion Water, same bundle, behind tab 11A. If we
 12 can pick it up at paragraph 231. And 233, you will see
 13 that, not surprisingly, what the Tribunal did in Albion
 14 Water was to adopt the approach of the Tribunal in
 15 Cardiff Bus when dealing with the first limb, cynical
 16 disregard. That's Albion Water, 231 to 233. But then
 17 considered the second limb, calculated to make a profit,
 18 that is at #356 to 365.
 19 If I can draw your attention to 362:
 20 "Dwr Cymru had well in mind the economic advantages
 21 that could be gained and it recognised that if it could
 22 justify such an approach, that was likely to protect its
 23 existing revenue."
 24 363:
 25 "However, the case law cited above shows that it is

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1 necessary for there to be some additional evidence not
 2 only that the defendant was motivated by the desire to
 3 make a profit or avoid a loss of revenue, but that there
 4 had been some weighing up or balancing of the likely
 5 gain against the likely loss in terms of having to pay
 6 compensation to the claimant."
 7 364:
 8 "In the present case, there is no evidence before us
 9 that Dwr Cymru or anyone else in Dwr Cymru weighed
 10 the risks of going ahead with the first access price
 11 against the likely downsides."
 12 365:
 13 "We recognise the point made that if it had turned
 14 its mind to the question of whether any benefit would
 15 outweigh compensation, it would have realised that the
 16 maximum compensation payable to Albion would be a subset
 17 of the money they made in the interim," ie it would have
 18 made more money. "We do not regard that as an
 19 ...(Reading to the words)... thought about it."
 20 Then the conclusion at 366:
 21 "We have concluded that Albion's claim for exemplary
 22 damages must fail on two grounds."
 23 If I can just ask you to read (a) and (b), please.
 24 We deal with the application of the evidence, the facts
 25 of this case, in our skeleton argument, paragraphs 390

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1 to 410. But let me just encapsulate the main points.
 2 We say the application for exemplary damages is
 3 hopeless. We rely on the points in the skeleton, but
 4 let me just take it shortly. In relation to the first
 5 limb, cynical disregard, there is no basis in the
 6 evidence to support a finding that MasterCard acted with
 7 cynical disregard of Sainsbury's rights. This is not
 8 a case where MasterCard sought to conceal its conduct.
 9 It notified the domestic UK MIF to the OFT in 2000. And
 10 the OFT's infringement decision was unsustainable and
 11 was overturned by the Tribunal.
 12 The Commission has never considered the legality of
 13 the UK domestic MIF. On the contrary, as I have shown
 14 you, the Commission has indicated that national courts
 15 and competition authorities are best placed to consider
 16 the legality of the domestic MIF.
 17 Of course what we have in the UK is the Maestro
 18 experience. It is a particular characteristic of the UK
 19 market. It has not previously been considered by any
 20 court or regulator. Whether you agree with my
 21 submissions or not, I hope you will at least see, I hope
 22 you will agree with me, but I hope you will agree that
 23 the point, the argument we are making is a strong one,
 24 whether you like it or not.
 25 But this is not a case where MasterCard is simply

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1 putting up a hopeless or artificial legal argument to
 2 justify conduct over a period of years. This is
 3 a genuine and strong legal argument. We go back to the
 4 counterfactuals: what would MasterCard have done?
 5 Because it has been said it should pay exemplary damages
 6 for cynical disregard. If MasterCard had lowered its
 7 credit card MIF during the period of the claim, it would
 8 have lost the market share. Forget the context of that
 9 about objective necessity, restriction etc. Just on
 10 exemplary damages, has MasterCard acted with cynical
 11 disregard due to the need to compete with Visa by having
 12 the level of MIF it had? This is clearly not a case
 13 that satisfies the first limb.
 14 On the second limb, equally, there is no evidence to
 15 show that MasterCard ever addressed its mind to whether
 16 the likely profit it would make from setting the UK MIF
 17 at the level it did would exceed any potential damages.
 18 You have seen from Albion that that's necessary.
 19 An actual addressing the mind to that issue. So we will
 20 see, but in our submission, really we hope not to hear
 21 from exemplary damages again because there's nothing
 22 in it.
 23 You have Mr Cook to entertain you after lunch.
 24 MR JUSTICE BARLING: We look forward to that.
 25 MR HOSKINS: Unless you have any further questions?

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1 MR JUSTICE BARLING: No, we will see you at 2 o'clock.
 2 MR HOSKINS: Thank you very much.
 3 (1.00 pm)
 4 (The short adjournment)
 5 (2.00 pm)
 6 MR HOSKINS: Don't worry, I just have one reference to
 7 give you.
 8 MR JUSTICE BARLING: Oh yes.
 9 MR HOSKINS: It is the evidence from Dr Niels to show that
 10 the switching from MasterCard to Amex would be more
 11 than 5%.
 12 MR JUSTICE BARLING: We left a space for that somewhere,
 13 right.
 14 MR HOSKINS: It comes up, for example, in the damages
 15 counterfactual and I took you to Mr von Hinten-Reed. It
 16 is at paragraph 144/141.
 17 MR JUSTICE BARLING: Yes.
 18 MR HOSKINS: Anyway, the counter figure for switching to
 19 Amex is first Niels, paragraph 7.27 and then there is
 20 a diagram called 7.2 and it is bundle D3, tab 3 at 362.
 21 It is not a figure as such, it is a graph that plots the
 22 switch.
 23 MR JUSTICE BARLING: Thank you very much.
 24 MR HOSKINS: Mr Brealey has a housekeeping point.
 25 MR JUSTICE BARLING: Right.

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1 Housekeeping
 2 MR BREALEY: It was just the witnesses we were debating, and
 3 I just need to get that sorted if I could to let people
 4 know.
 5 So next week we have Monday as a non-sitting day.
 6 MR JUSTICE BARLING: Hang on, let's just ...
 7 MR BREALEY: No witnesses. It is not a non-sitting day, but
 8 no one is coming to give evidence.
 9 MR JUSTICE BARLING: So --
 10 MR BREALEY: So it is a holiday or a non-sitting day.
 11 MR JUSTICE BARLING: We can just chat among ourselves?
 12 MR BREALEY: Read?
 13 MR JUSTICE BARLING: So not sitting because no witnesses.
 14 MR BREALEY: And the same applies to Tuesday morning.
 15 That's the 2nd. Then in the afternoon, I will be
 16 calling Mr Brooks. On Wednesday morning I will be
 17 calling Hannah Bernard. In the afternoon will be
 18 Mr Rogers. Thursday is, of course, free for the palace.
 19 Then Friday morning is Mr Coupe, and then that's the end
 20 of my evidence. Then Mr Scott Abrahams will be
 21 Friday pm. That is the start of the defendant's
 22 witnesses.
 23 Mr Hoskins has been very helpful but he was going to
 24 let me know at some point tomorrow or the day after the
 25 order of his witnesses.

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1 MR JUSTICE BARLING: In the following week after that.
 2 MR BREALEY: The following week.
 3 MR JUSTICE BARLING: Right. Good. Thank you for that.
 4 MR HOSKINS: Can I just make three very brief observations
 5 on that.
 6 We have lost a day because we had three days
 7 scheduled for cross-examination; we have now got two.
 8 I think that should be sufficient. I just want to make
 9 the point so that if we are squeezed for time --
 10 MR JUSTICE BARLING: You have some credit in the bank, you
 11 mean?
 12 MR HOSKINS: That's it. What a good boy I have been ... In
 13 relation to Mr Brooks, I may well not be the whole
 14 afternoon with him, so I don't want you to be
 15 disappointed if we all pitch up on Tuesday afternoon and
 16 we are not here for the whole afternoon. It may well go
 17 shorter than the half day.
 18 MR JUSTICE BARLING: So be it.
 19 MR HOSKINS: In relation to Mr Rogers, it is the opposite
 20 problem. If I'm not finished with him on Wednesday
 21 afternoon, and I think this is right, he would need to
 22 be able to come back for a bit of Friday potentially, or
 23 we would need to sit a bit late. But I don't want to
 24 lose that time with Rogers if --
 25 MR JUSTICE BARLING: You do not think it is appropriate to

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1 have Ms Bernard standing by in case you are short with
 2 Mr Brooks? You don't think there's any point in that?
 3 MR HOSKINS: It is not my --
 4 MR JUSTICE BARLING: I was just throwing that out.
 5 MR HOSKINS: To be fair, we have discussed ... (Pause)
 6 MR BREALEY: I will certainly do my utmost to find out
 7 whether she is available.
 8 MR JUSTICE BARLING: It is just it sounds as though
 9 Mr Hoskins has reason to believe he doesn't need two
 10 hours, or two hours and a quarter with Mr Brooks. If it
 11 is significantly shorter than that in all probability,
 12 like if it is only an hour, I don't know, it might be
 13 worth thinking about if it is --
 14 MR BREALEY: She is no longer employed at --
 15 MR JUSTICE BARLING: I see. So is she is not here anyway.
 16 MR BREALEY: I would have to go back and just check, that's
 17 the only thing.
 18 MR JUSTICE BARLING: The danger would be if Mr Hoskins takes
 19 longer than he thinks, she will have to come back.
 20 I will leave it with you.
 21 MR HOSKINS: I do flag that Mr Rogers may have to come back
 22 on Friday on that basis. I will try and avoid it.
 23 MR JUSTICE BARLING: If you get squeezed with Mr Rogers,
 24 yes.
 25 MR HOSKINS: In relation to order of our witnesses, we are

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1 having to just make sure, because the days have slipped
 2 a little bit when they can all fit in, but we will
 3 obviously let you know as soon as possible.
 4 MR JUSTICE BARLING: Thank you very much. That would be
 5 helpful.
 6 Mr Cook, you are taking over.
 7 Opening submissions by MR COOK
 8 MR COOK: I am, sir.
 9 Sir, I have been left to deal with three issues: the
 10 issue of compound interest or interest, ex turpi and
 11 association of undertakings.
 12 And I will try not to use the afternoon as a target.
 13 Once I have done those issues, I hope I will sit down,
 14 but hopefully that will be some time before the end, but
 15 I will see how matters progress.
 16 MR JUSTICE BARLING: Sure.
 17 MR COOK: Dealing firstly with the issue of interest. Now,
 18 Mr Brealey skipped over the issue of interest on Tuesday
 19 saying -- and it is the transcript from Day 2, page 119
 20 to page 120 -- that the economists were agreed that
 21 interest should be compounded, it was just a question of
 22 rates.
 23 Now, we obviously hope we won't get to the issue of
 24 interest, but if we do Sainsbury's case faces rather
 25 more fundamental difficulties than Mr Brealey would

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1 suggest.

2 The starting point for interest is the statutory

3 power to award interest, which is section 35A of the

4 Senior Courts Act 1981. And under this provision

5 a claimant can only claim simple interest, and the

6 conventional practices of the courts has been to award

7 interest, at least in pounds, by reference to the Bank

8 of England base rate plus 1% or sometimes 2%.

9 And whatever the commercial criticisms that may be

10 levelled about awarding simple rather than compound

11 interest, that is the only approach permitted by

12 statute.

13 Now, Sainsbury's rather optimistically suggest in

14 its opening, paragraph 389, that if the Tribunal awards

15 simple interest pursuant to the Senior Courts Act, it

16 should do so at a rate of 5% above the Bank of England

17 base rate. That doesn't reflect the conventional

18 approach adopted by the courts which, as Sainsbury's

19 itself describes in paragraph 62 of its particulars of

20 claim, is to reflect the cost of the borrowing of

21 claimants in general by using a rate of 2% above the

22 Bank of England base rate. So the 5% simply at the

23 moment, it is a swing, it is not going anywhere.

24 Now, MasterCard accepts that the statutory power to

25 award interest is not the end of the story in than

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1 following the decision of the House of Lords in *Sempra*

2 *Metals*, it is open for a claimant to recover compound

3 interest where it can claim and prove that it suffered

4 actual loss on this basis.

5 However, this is a claim for damages and it must be

6 pleaded and proved as an actual loss. Now, I was going

7 to deal with the extracts from the cases from our

8 skeleton argument which sets out the relevant passages,

9 rather than taking you through to a number of

10 authorities.

11 So if I could ask you to turn to that written

12 openings, paragraph 359.

13 MR JUSTICE BARLING: Yes.

14 MR HOSKINS: We set out at 359 quotes from three of their

15 Lordships in *Sempra Metals*, firstly, and just for the

16 Tribunal's reference *Sempra Metals* is in the bundles at

17 bundle I5, tab 1A.

18 MR JUSTICE BARLING: Yes.

19 MR COOK: As I said, I am going to deal with it from the

20 extracts that we have quoted for the moment.

21 The first quote is from Lord Hope. He says:

22 "I also agree with Lord Nicholls that the loss on a

23 late payment of a debt ...(Reading to the words)...

24 compound interest [I emphasise the next words] the

25 claimant must claim and prove his actual interest losses

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1 if he wishes to recover compound interest as is the case

2 where the claimants for a sum that includes interest

3 charges."

4 So he must claim and prove his actual interest

5 losses.

6 Then we have extracts from Lord Nicholls

7 paragraphs 94 and 96 of the judgment, who concludes:

8 "The house should hold in principle that it is

9 always open to a claimant to plead and prove his

10 ...(Reading to the words)... payment of a debt."

11 We accept that is a principle that applies in

12 relation to tortious damages as well, as we see from the

13 next extract from Lord Scott.

14 He then goes on to say:

15 "But an unparticularised and unproved claim simply

16 for damages will not suffice. General damages are not

17 recoverable. The Common Law does not assume that delay

18 in payment of debt will of itself cause damage. Loss

19 must be proved."

20 Finally, Lord Scott at paragraph 132 of the

21 judgment:

22 "Interest losses caused by a breach of contract or

23 by a tortious wrong ..."

24 Obviously we are in that territory at least in terms

25 of the cause of action being advanced:

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1 "... should be held in principle to be recoverable,

2 but subject to proof of loss."

3 Which is the key point I emphasise.

4 He goes on to address a number of other ones. These

5 are all making clear it needs to be our particularised

6 and proven case for an interest claim on a compound

7 basis.

8 And going on in our written opening at

9 paragraph 360, we can see from the judgment of

10 Mr Justice Teare in *JSC BTA v Ablyazov*, 2013, the

11 Tribunal's reference, that is in bundle I5, tab 2, we

12 can see how these requirements have been followed in

13 practice by the courts. Again, we have the relevant

14 extract at paragraph 360 of our opening.

15 Now, Mr Justice Teare accepted at paragraph 4 that

16 following *Sempra Metals*, the claim could be brought for

17 compound interest, but he noted that the house

18 emphasised the need for such damages to be pleaded and

19 proved.

20 Rather than reading out those two lengthy

21 paragraphs, if I could ask the Tribunal just to read the

22 two of them to themselves. Then I will emphasise the

23 final sentence of paragraph 18 to the second extract.

24 MR JUSTICE BARLING: Right.

25 MR COOK: So it's the final sentence which said:

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1 "In the absence of a specific plea of actual
2 interest losses, the remedy ...(Reading to the words)...
3 This is clear guidance for trial judges which I must
4 follow."

5 We say again the Tribunal should follow it. It is
6 therefore simply wrong for Sainsbury's to suggest, as it
7 does at paragraph 389 of its written opening, that it is
8 open to the Tribunal to award Sainsbury's compound
9 interest at an conventional, commercial rate.

10 That's simply not correct. There is no basis for
11 the award of compound interest at some general
12 commercial rate. In order to take itself outside the
13 statutory provision, section 35A, Sainsbury's must plead
14 and prove its actual interest losses.

15 Now, in terms of Sainsbury's pleaded case, we see
16 this at paragraph 61 and 62 of the particulars of claim,
17 which is bundle B, tab 2, and it is at page 31. There
18 are two paragraphs in which Sainsbury's sets out its
19 case.

20 In paragraph 61, Sainsbury's starts by asserting
21 that it is entitled to complete compensation, whether
22 for lost return on investments, additional finance costs
23 or for interest losses incurred. Now, that's correct in
24 principle. We don't disagree with it, but only if it
25 can plead and prove those losses. And of course, there

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1 they are raising three possible grounds of loss.

2 At paragraph 62 we then have the actual pleading on
3 the basis on which Sainsbury's says it would have
4 suffered loss, and it says:

5 "Over the period of its claim, Sainsbury's undertook
6 substantial capital expenditure, including investments
7 in new ...(Reading to the words)... In the absence of
8 the allegedly unlawful UK MIFs, Sainsbury's would have
9 reinvested a substantial portion of the sums claimed
10 above in its business thereby generating further
11 profits."

12 That is an assertion they would have made more
13 profits:

14 "Secondly, and/or Sainsbury's would have needed to
15 borrow less."

16 So that is reduction in borrowing:

17 "And/or raise less equity capital than it did to
18 finance its capital expenditure and operations."

19 That is an argument that it would have issued less
20 shares to its shareholders and therefore received less
21 equity capital.

22 So, at that stage, it raises three possible grounds
23 of loss: reduction in profits, reduction in borrowings
24 and reduction in equity capital. So money advanced by
25 shareholders. It doesn't tell us which of these are

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1 meant to have happened or the extent of the loss said to
2 have been suffered as a result.

3 We say Sainsbury's factual evidence is similarly
4 lacking in any detail at all. We have set out at
5 paragraph 362 of our written opening two extracts from
6 the evidence which we say are the critical extracts,
7 from the evidence of first Mr Coupe, and secondly
8 Mr Rogers.

9 If I could ask the Tribunal to read those because
10 they are confidential and so I can't read them out loud.

11 Without trespassing on issues of confidentiality, we
12 say that this evidence, and in particular the evidence
13 of Mr Coupe, suggests that Sainsbury's may well not have
14 suffered any interest rate loss at all. He raises the
15 possibility the money may have been spent in a way which
16 would not have resulted in an interest cost arising.

17 What is, however, quite clear, we say, is this
18 evidence falls in far short of identifying any specific
19 loss by Sainsbury's based on which Sainsbury's can say
20 it suffered a compound interest loss. And we say that's
21 simply the end of the story in relation to anything
22 other than statutory damages. It has not identified
23 a specific loss and it's not pleaded and proved that
24 loss.

25 Now, Sainsbury's tries to fall back on its expert

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1 evidence, and in particular on the evidence of

2 Mr Reynolds, in order to fill that hole. However, all
3 Mr Reynolds does is look at the weighted average cost of
4 capital and not even at the claimant, but at
5 Sainsburys plc, the parent.

6 With respect, that does not work. Mr Reynolds
7 cannot identify the loss which Sainsbury's Stores
8 Limited actually suffered without evidence, which I have
9 said is simply not there, but as a result of the UK MIF
10 Sainsbury's Store Limited in fact increased its funding
11 by the amount of the overcharge, and that this
12 additional funding was obtained at J Sainsbury plc's
13 weighted average cost of capital, if anything it would
14 have been Sainsbury's itself borrowing at whatever its
15 actual costs were, not some weighted average across
16 everything it did in the business. And without any
17 evidence, how the money was actually borrowed and
18 without the evidence of the increases in the rates of
19 that specific borrowing, Mr Reynolds is not looking at
20 actual losses, he is looking at some hypothetical broad
21 measure. And that's simply, as the case law shows, not
22 adequate for a claim of compound damages under Sempra
23 Metals.

24 We say that is simply the end of the matter and it
25 shouldn't be necessary ultimately for the Tribunal to

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1 get into what are undoubtedly complicated issues of
 2 disagreement between the experts about weighted average
 3 cost of capital versus average debt costs, incremental
 4 debt costs and matters of the kind, and within each
 5 calculation the appropriate way to calculate each of
 6 them.

7 If and when it becomes appropriate to get into those
 8 matters, they are confidential matters which will need
 9 to be dealt with in camera, so I'm not going to develop
 10 them any more today. We obviously rely upon the
 11 evidence of Mr Harman in relation to those and if it
 12 becomes necessary we will invite the Tribunal to accept
 13 his evidence. But we say fundamentally, and the reason
 14 why we have opened this today, is to make clear that
 15 there is a fundamental and very high threshold that
 16 Sainsbury's has to satisfy to persuade the Tribunal that
 17 it's appropriate to award Sempra Metals compound
 18 interest. And we say they come nowhere near to
 19 discharging that particular measure, and coming back to
 20 statutory measure that's the measure applied for all
 21 damages claims up until Sempra Metals, and it continues
 22 to be what courts throughout the land do on a day-to-day
 23 basis.

24 That is the issue of interest. Turning to the issue
 25 of ex turpi causa. Of course if the Tribunal concludes

1 there is a breach of article 101, then MasterCard relies
 2 upon that principle to say the claim is simply cut off
 3 at its knees.

4 Now, Mr Smith, as you rightly observed on Tuesday,
 5 what we are doing is combining both English law and
 6 European law principles there. We rely upon the English
 7 doctrine of ex turpi causa subject to the restriction on
 8 that doctrine imposed by the European Court in
 9 *Courage v Crehan*, namely the requirement for significant
 10 responsibility. Although I would say it is extremely
 11 open to doubt, particularly in the light of the approach
 12 taken by the Supreme Court in *Apotex*, whether that
 13 requirement actually adds anything to English law or
 14 whether it is simply a different formulation of exactly
 15 the same principles.

16 I am not sure in the end it is necessary for the
 17 Tribunal to worry about that too much. My submission
 18 would be that the English law principles on significant
 19 responsibility are broadly the same test.

20 We then rely upon what was originally a European law
 21 concept, but under the Competition Act 1998 is
 22 an English law concept, the concept of an undertaking in
 23 order to show the claimant in this case was party to the
 24 infringement and therefore falls within the ex turpi
 25 causa doctrine.

1 Now, Mr Smith, you raised the issue of attribution
 2 under English law principles. There obviously are
 3 circumstances under English law in which the actions of
 4 one party, often an employee or an agent, can be
 5 attributed to another party. We say we are simply not
 6 in that territory at all. Under competition law, it is
 7 an undertaking which commits an infringement.
 8 Therefore, we say the relevant question is whether
 9 Sainsbury's stores was part of an infringing
 10 undertaking.

11 Now, before I get into the detail of these issues,
 12 I would just like to put the point we are addressing in
 13 context. Since December 2012, Sainsbury's stores has
 14 been bringing the present claim against MasterCard
 15 contending that the UK default MIF is set at
 16 an excessive and consequently unlawful level. And
 17 Sainsbury's internal documents show, as you might
 18 expect, that that claim was in contemplation for some
 19 time before it was launched.

20 However, throughout the claim period, including from
 21 September 2012 when it was commenced, onwards and right
 22 up until today's date, Sainsbury's Bank, which was at
 23 least 50% owned by the Sainsbury's group throughout the
 24 claim period and has been 100% owned for the past two
 25 years, has issued MasterCard credit cards to all of its

1 credit card customers and continues to do all of its
 2 MasterCard credit card business on the basis of the
 3 default UK MIF, demanding that acquirers pay it the very
 4 charge which Sainsbury's stores is, in front of you
 5 today, saying is excessive and unlawful.

6 It is also clear on the evidence that no attempt has
 7 ever been made by Sainsbury's Bank to change that.
 8 There is no suggestion that Sainsbury's Bank has ever
 9 tried to agree bilateral agreements which would have
 10 reduced interchange fees to what Sainsbury's stores
 11 contends is the lawful level.

12 Bear in mind it is important to emphasise it is
 13 a default interchange fee, it is not compulsory, people
 14 are free to contract out of it. There is no indication
 15 that they have they have made any attempt to do so.

16 To put the scale of that in context, I would ask the
 17 Tribunal to turn to Mr Abrahams' witness statement.
 18 Mr Abrahams is the current employee of MasterCard
 19 formerly employed by Sainsbury's stores. And that's in
 20 bundle C2, tab 4.

21 It is paragraphs 22 and 24, or more accurately the
 22 tables beneath each of them, which are confidential that
 23 I wanted to take the Tribunal to. We see at
 24 paragraph 22 and the table below it the annual
 25 interchange fee revenue that Sainsbury's Bank has

1 received on MasterCard credit cards year on year.
 2 The details of the specific numbers are obviously
 3 confidential, but the Tribunal can see the substantial
 4 scale of the sums that we are talking about.
 5 If the Tribunal compares those numbers in that table
 6 to the first row, or the first significant row in the
 7 table below paragraph 24, that row records the total
 8 interchange fee is paid by Sainsbury's stores. So one
 9 can see comparing the money in to Sainsbury's Bank
 10 versus the money paid out by Sainsbury's stores, what
 11 a substantial percentage of the interchange bill at
 12 Sainsbury's stores is offset within the group by money
 13 coming in from interchange fees revenues.
 14 What we would also emphasise is what's dealt with in
 15 the rest of table 24, which is a very substantial part
 16 of the sums being claimed. And we see that in the
 17 second substantial row in financial terms, and the third
 18 row deals with, as a percentage, what is a substantial
 19 part of the sums being claimed in these proceedings are
 20 in fact money that simply went out of Sainsbury's stores
 21 and next door into Sainsbury's Bank, its half sister and
 22 now full sister.
 23 So that is the situation. And we now are in
 24 a position where the Sainsbury's group is challenging
 25 the legality of the UK MIF with one hand while, at the

1 same time, enthusiastically participating and profiting
 2 from the UK MIF with the other hand.
 3 Moreover, a large part of that claim for damages
 4 includes money which, as far as the group is concerned,
 5 it simply paid itself. Now, there's obviously
 6 a forensic point I can make here about whether the
 7 Sainsbury's group really believed the UK MIF is
 8 unlawful, because if it really believed that, would it
 9 honestly still be continuing to charge that default
 10 interest rate fee?
 11 However, we say the problem is more profound than
 12 simply a forensic point. It means that Sainsbury's
 13 claim is barred by the principle *ex turpi causa*. Now,
 14 I will develop why we say that's the case. While I go
 15 on to explain why we disagree with a number of the
 16 points made by Mr Brealey, I would certainly echo his
 17 comments that both illegality as a general matter of
 18 English law and its relationship with a competition law
 19 concept of undertakings are undoubtedly complicated
 20 issues.
 21 In particular, many of the points the Tribunal will
 22 ultimately have to decide are ones on which there are no
 23 decided cases. The European cases are largely concerned
 24 with moving fines up the chain to find the person with
 25 the ability to pay them, the person with deep pockets.

1 Whereas the English cases to date have predominantly
 2 been in relation to jurisdiction, and therefore
 3 concerned whether or not a claim against an anchor
 4 defendant, usually a small part of a wider group, but
 5 an English company, which will therefore allow
 6 a justification for suing in England with the perceived
 7 advantage of English litigation, so people have just
 8 joined a lesser connected part of the group as an anchor
 9 defendant to allow them to bring lots of different
 10 foreign defendants here. Because those have been dealt
 11 with at a preliminary stage, as your Lordship is of
 12 course very familiar with, having dealt with it in the
 13 Dixons' matter.
 14 All that is required to show is that there is
 15 an arguable claim against those defendants, and so a lot
 16 of the cases that have addressed this have ultimately
 17 dealt with whether the point are arguable or not, rather
 18 than actually deciding them.
 19 The only other case in relation to this issue is
 20 that of Mrs Justice Asplin in *Tesco v MasterCard*, which
 21 did deal with the exactly the same issues which were in
 22 front of the Tribunal, but because it was a summary
 23 judgment application and we didn't succeed, ultimately
 24 didn't decide any of the point, she just concluded
 25 a number of matters were more than barely arguable,

1 which is the -- or merely arguable -- the words used --
 2 which is the basic non-summary judgment threshold.
 3 So that is the territory the Tribunal is in.
 4 Sir, I'm obviously conscious that I appeared in
 5 front of you in the Dixons matter dealing with the
 6 jurisdiction point, and it is right to say from
 7 a jurisdiction perspective MasterCard would prefer
 8 a narrower approach to liability within corporate groups
 9 than it does for the present purposes.
 10 Ultimately, the current law is not clear in relation
 11 to where the lines are drawn, and MasterCard in both the
 12 Tesco and Dixons cases has been trying to get some
 13 clarity. And ultimately, and unfortunately, it may fall
 14 to this Tribunal to provide that clarity at the moment
 15 is lacking in the case law, which I appreciate is not
 16 a helpful thing to be told, but that is, I'm afraid, the
 17 situation in which the Tribunal is in.
 18 We set out in paragraph 412 of our written opening
 19 the four propositions that MasterCard aims to establish
 20 in this case in order to establish *ex turpi causa*. The
 21 Tribunal will see the four of them there.
 22 I will deal firstly with what I suggest, the second
 23 one of those, is a relatively simple point -- they get
 24 more difficult after that -- which is whether or not
 25 Sainsbury's Bank was involved in any infringement.

1 Now, the basis of Sainsbury's claim against
 2 MasterCard is that the UK MIF was either the product of
 3 an agreement or concerted practice between MasterCard
 4 and its licensees, or a decision of association of
 5 undertakings, ie an association of MasterCard's
 6 licensees.
 7 Now, throughout the period of the claim Sainsbury's
 8 Banks have been licensed to issue credit cards. It is
 9 therefore one of the licensees which Sainsbury's stores
 10 contends was either party to an agreement or concerted
 11 practices with MasterCard, or on whose behalf MasterCard
 12 was making decisions about the MIF as opposed to the
 13 MIT. On either basis, we say it is more than sufficient
 14 to show that if the Tribunal concludes there is
 15 an infringement, that Sainsbury's Bank was party to any
 16 infringement.
 17 However, ultimately it is not necessary to show that
 18 Sainsbury's Bank was party to the agreement or was one
 19 of the associations of undertakings since it is well
 20 established law, and I'll hand up a copy of Provimi
 21 which refers to the European court cases showing it --
 22 Provimi at paragraph 26 -- that implemented
 23 an anti-competitive agreement itself involved a breach
 24 of article 101.
 25 So you don't have to be involved in the agreement.

1 If you implement the anti-competitive agreement by
 2 somebody else, that itself is sufficient. And there can
 3 be no doubt that Sainsbury's Bank has implemented the
 4 UK MIF.
 5 We say that's more than sufficient to show that, on
 6 any view, if there is an infringement, Sainsbury's Bank
 7 is a participant in it. Then we say that, as a matter
 8 of law, I agree this is going to be a complicated matter
 9 we are going to have to go through some of the cases in
 10 due course on, in competition law, infringements are not
 11 committed by companies, they are committed by
 12 undertakings. And we say Sainsbury's stores and
 13 Sainsbury's Bank are all part of the same undertaking,
 14 and therefore Sainsbury's stores is liable for that
 15 infringement by that undertaking.
 16 That brings me to the question which is sort of
 17 number 1 on our list, which is we say Sainsbury's stores
 18 and Sainsbury's Bank are part of the same single
 19 economic unit or undertaking. We set out the relevant
 20 case law in relation to this, what we say are the
 21 relevant points, we've set out the points, relevant
 22 paragraphs 413 to 418 of our written opening.
 23 The starting point, and this appears to be very much
 24 common ground between the parties, we then move away
 25 from our areas of agreement, is that the test for

1 identifying a single economic unit, an undertaking,
 2 requires unity of conduct on the market.
 3 This unity of conduct is said to arise in a unitary
 4 organisation of personal, tangible and intangible
 5 elements which pursue a specific economic aim on
 6 a long-term basis. For me at least, that is not
 7 a definition that is terribly helpful. What I would
 8 submit may be a more helpful definition, a more helpful
 9 way of looking at the concept, is to understand that
 10 what the Tribunal is seeking to do is determine whether
 11 companies are acting independently of each other or
 12 whether they act jointly. And that's not simply
 13 something that I'm making up.
 14 If I could ask you to turn to Sainsbury's skeleton
 15 because it sets out again, briefly, a couple of
 16 paragraphs that they agree are significant, and we do as
 17 well, although we use them for slightly different
 18 purposes, at paragraphs 461 and 462.
 19 461 deals with the Preinsulated Pipe case, and 462
 20 is the DaimlerChrysler v Commission case. Both of these
 21 cases deal with the rationale for the focus of
 22 undertakings in competition law, and the Preinsulated
 23 Pipe case, as Sainsbury's says:
 24 "The court emphasised the need to ensure that the
 25 formal separation between those companies resulting from

1 their separate legal personality could not pretend to
 2 find that they had acted jointly on the market for the
 3 purposes of applying the rules of competition."
 4 What it is really saying is sometimes companies that
 5 are connected within groups will act jointly, and
 6 therefore they are seen as undertakings. And we will
 7 come back in the extract above from Hydrotherm, which
 8 explains the logical point of why competition law
 9 doesn't worry about what separate legal entities acting
 10 jointly in certain circumstances, ie when they are
 11 within a group. But therefore, the emphasis is on them
 12 acting jointly on the market.
 13 Then at paragraph 462, the quote from
 14 DaimlerChrysler said:
 15 "The test of whether entities were part of a single
 16 undertaking is concerned with whether those entities
 17 were adopting the same course of conduct on the market."
 18 Then Uralita:
 19 "The court said the essential element is whether
 20 there is unity in their conduct on the market."
 21 This is essentially the description of the unitary
 22 organisation of personal, tangible and intangible
 23 elements. It is ultimately seeking to determine whether
 24 the companies act independently of each other, or
 25 whether they act jointly, and the rationale for that

1 distinction and the reason why competition law uses the
 2 concept of undertakings, rather than just simply, as we
 3 do in every other field, just saying companies are
 4 separate, is that you would normally expect companies in
 5 a group to work together and not fight each other
 6 because, frankly, the point of view of a group, that's
 7 simply wasted money taking business from each other.
 8 What it means is you cannot have a cartel between
 9 two members of the same group because they are
 10 controlled by the same group, and therefore you would
 11 normally expect the competition between them won't
 12 happen. So you can't have an agreement between them if
 13 it's just between members of the group, which affects
 14 competition, because there shouldn't be, it is
 15 understood that there shouldn't be, any in the first
 16 place.
 17 That is a proposition that we take -- the obvious
 18 explanation of why you use undertakings in competition
 19 law. And one can see that in the extract from
 20 Hydrotherm at paragraph 460 of the claimant's skeleton
 21 argument, matters that are familiar to the Tribunal in
 22 any way.
 23 The final sentence:
 24 "The requirement of article 101 is therefore
 25 fulfilled if one of the parties to the agreement is made

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1 up of ... (Reading to the words)... is impossible."
 2 So group companies don't normally compete and that's
 3 why they are treated as being one for the purpose of
 4 competition law. You can't have a cartel between
 5 themselves.
 6 We say what that principle also shows is that
 7 whether Sainsbury's stores is part of a single economic
 8 undertaking with Sainsbury's Bank does not depend upon
 9 whether Sainsbury's stores exercised decisive influence
 10 over Sainsbury's Bank.
 11 Now, certainly if one company exercised its decisive
 12 influence over another they would be part of the same
 13 single economic undertaking, and that's the very common
 14 way, particularly when you go up the chain of the fines,
 15 that the matters have been dealt with. Yes, the
 16 decisive influence will often be the useful way to
 17 determine, seek an economic undertaking.
 18 We say that's not the only test. What that shows is
 19 when you have a triangular arrangement, two sister
 20 companies controlled by a parent, they are all part of
 21 the same undertaking and they work together because they
 22 are controlled by the same person, and so they are not
 23 going to fight each other.
 24 But we obviously accept that common ownership is not
 25 enough. We don't start and finish and say that's the

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1 end of the story. You need to look at how their
 2 relationships work with each other. But nonetheless the
 3 fact they are jointly owned is, we say, an important
 4 factor to be considered.
 5 So what fundamentally the Tribunal has to look at
 6 when we get to the evidence is whether Sainsbury's
 7 stores and Sainsbury's Bank are companies that work
 8 together or work independently.
 9 Now, we acknowledge the shoe polish example made by
 10 Mr Justice Teare in Cooper Tire, namely that there won't
 11 be a single economic entity between two companies in
 12 a group which are involved in completely different
 13 businesses and nothing to do with each other. And the
 14 example given in that case, which related to the
 15 Butadiene Rubber cartel -- and there are no doubt people
 16 in the room who know better than I do what Butadiene
 17 Rubber is, but that was the relevant cartel. The
 18 example given was if there was a subsidiary in the group
 19 that sold shoe polish. No involvement in Butadiene
 20 Rubber at all, would that be sufficient?
 21 We accept that might well be, even if it is wholly
 22 owned and controlled outside the single economic entity,
 23 because it's simply not having anything to do with the
 24 companies that are involved in the infringement. But it
 25 is important to understand the limitations of that

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1 principle. It is because it is involved in something
 2 completely different.
 3 If you, on the other hand, had a shoe cartel and
 4 there was then a shoe polish subsidiary which operated
 5 in conjunction with the shoe company, so you actually
 6 got products that are closely related and they worked
 7 together, so you had people going out selling shoe
 8 polish and also extolling the benefits of the cartelised
 9 shoes, then in our submission, it would be that you can
 10 actually get a situation in which they are working
 11 together, they are acting in conjunction with each
 12 other, and so that may be insufficient.
 13 So we say it is not simply a question of saying do
 14 they deal in the specific products. It is about whether
 15 or not they are working together and if they are all
 16 actively part of the same relevant business for these
 17 purposes.
 18 When we come to the evidence, what we are going to
 19 submit is this is a situation where they are not looking
 20 at the shoe polish subsidiary, wholly unconnected. What
 21 we submit you will see is Sainsbury's stores actively
 22 helping Sainsbury's Bank sell financial products,
 23 including in particular sell credit cards to its
 24 Sainsbury's stores retail customers, with a structure of
 25 that credit card offering being designed to feed back

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1 into increased sales at Sainsbury's stores.
 2 We say decisions are being taken, as you would
 3 expect within a group, based on how they benefit the
 4 group as a whole, not based on whether they benefit
 5 Sainsbury's stores or whether they benefit Sainsbury's
 6 Bank.

7 So we say evidentially what you are going to see is
 8 two group companies working hand in glove for their
 9 mutual benefit, including very much in the area of
 10 credit cards, which is the essential part of the
 11 benefits that both get from it. And you heard from
 12 Mr Hoskins this morning the point about Nectar points,
 13 the benefits that arise from Sainsbury's stores. And it
 14 is common ground that without the Nectar points their
 15 sales would have been materially lower. I can't put
 16 a number on it because you will have seen those two
 17 numbers are confidential, but you were shown the two
 18 conflicting disagreement numbers this morning.

19 But those are sort the feedback loops that exist
 20 between the two, and we are going to say, when you have
 21 seen all the evidence in relation to this -- a lot of it
 22 is confidential, so I'm not going to develop it any
 23 further now and obviously these are matters that we are
 24 going to need to develop with the witnesses, but we say
 25 there is a list of key indicators at paragraphs 419

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1 to 426 of our written opening and we will need to
 2 develop these points whilst the witnesses give evidence.

3 What we say is what the Tribunal will see is two
 4 companies working hand in glove in relation to the
 5 credit card arena for their mutual benefit, and that, we
 6 say, is more than sufficient to show they are a single
 7 legal entity and consequently they are legally
 8 responsible for the infringement which, if Sainsbury's
 9 stores is right, Sainsbury's Bank has clearly committed.

10 That brings me to the issue of significant
 11 responsibility, the requirement laid down by the
 12 European Court in Courage v Crehan. I would briefly
 13 like to take the Tribunal that decision which we will
 14 find in bundle 14, tab 5.

15 Just to remind the Tribunal, and I am sure you do
 16 remember, of the facts of Courage v Crehan, this was one
 17 where Mr Crehan was the owner of a pub and Courage was
 18 the enormous brewery chain which, among other things,
 19 owned pubs and was requiring anyone who rented a pub
 20 from it to buy beer only from Courage. And that was the
 21 beer tie problem.

22 So that is what the court was focused on in dealing
 23 with this. It is paragraphs 30 to 34, the paragraphs
 24 I particularly wanted to take the Tribunal to look at
 25 the considerations that the European Court identified in

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1 relation to the significant responsibility doctrine. If
 2 I could ask the Tribunal to read 31 to 34 and I will go
 3 back to emphasise the passages which I submit are
 4 significant.

5 Sir, I would emphasise in paragraph 32 the
 6 requirements to take into account are the economic and
 7 legal context in which the parties find themselves, and
 8 based on the UK Government's submissions, the respective
 9 bargaining power and conduct of the two parties to the
 10 contract.

11 In paragraph 33, I would emphasise that:
 12 "Whether the party making the claim found himself in
 13 a markedly weaker position than the other party such as
 14 to seriously compromise or even eliminate his freedom to
 15 negotiate the terms of the contract, his capacity to
 16 avoid the loss or reduce the extent, in particular by
 17 availing himself in good time of all of the legal
 18 remedies available to him."

19 It is the availing oneself in good time of all the
 20 legal remedies we say is of particular importance in
 21 this case.

22 Then in the paragraph below obviously Sainsbury's
 23 would like to focus upon:

24 "If the sole reason is the agreement was part of
 25 a network of similar contracts which have a cumulative

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1 effect on competition."

2 Then it goes on to say:
 3 "The person controlling ...(Reading to the words)...
 4 particularly where in practice the terms of the contract
 5 were imposed on him by the party controlling the
 6 network."

7 We say that's not the position here. But we say
 8 when the Tribunal comes to -- at this stage, obviously
 9 introducing the arguments we are making, but we will say
 10 in due course that it is quite clear that the
 11 Sainsbury's undertaking does bear significant
 12 responsibility for any distortion of competition. And
 13 we say the relevant test -- and I will come to explain
 14 why -- is whether the Sainsbury's undertaking bears
 15 significant responsibility.

16 So that is a point that will be established here.
 17 We say perhaps the most significant point to bear in
 18 mind and what makes the present situation very different
 19 from Courage v Crehan is that the relevant agreement was
 20 not compulsory. Courage v Crehan, poor Mr Crehan was in
 21 a situation where he had no ability to negotiate and was
 22 compelled to accept those terms. Here we have
 23 a situation where it is not a compulsory agreement. The
 24 UK interchange fee is a default. It only applies up
 25 until the point at which somebody decides to contract

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1 out of it and they are free to do so.
 2 So MasterCard was not requiring Sainsbury's Bank to
 3 do its business pursuant to the UK MIF. It was always
 4 open to Sainsbury's Bank, and remains open to this very
 5 day, for Sainsbury's Bank to enter into a bilateral
 6 agreement with the acquirers on different terms.

7 Now, at this point I should deal with footnote 360
 8 which loomed large in Mr Brealey's submissions on
 9 day one and which Mr Brealey completely misunderstands.
 10 If I could invite the Tribunal to make sure they have
 11 reminded themselves of what footnote 360 says.

12 I am just reminding myself, footnote 360 isn't
 13 confidential.

14 MR JUSTICE BARLING: No, it is not.

15 MR COOK: I'm just checking I can discuss its terms.

16 To be clear, footnote 360 is not dealing with any
 17 counterfactual situation. It is not addressing how the
 18 world would operate if MasterCard just operated on the
 19 basis of bilateral agreements, either on its own or with
 20 a zero default MIF, or with a low default MIF or some ex
 21 post facto restriction on pricing.

22 Footnote 360 concerns the actual situation in which
 23 there was a UK default MIF at the real level that was in
 24 place throughout the period. And the point we make is
 25 a simple one, which is if an issuer like Sainsbury's

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1 Bank approached an acquirer saying "I want you to pay me
 2 less money, I want to have a lower interchange fee and
 3 we can agree on that bilaterally" then an acquirer,
 4 particularly if encouraged to do so by one of the
 5 largest retailers in the UK, Sainsbury's stores, would
 6 have of course agreed to that lower bilateral
 7 interchange fee. There would simply have been no reason
 8 for them not to do so.

9 Now, it is encouraging that point doesn't appear to
 10 be contested. But to be clear, the fact that you can
 11 agree a bilateral when the issuer proposes actively
 12 a lower interchange fee to the benefit of the acquirer
 13 and the merchant and, obviously, the acquirer and the
 14 merchant see the benefit of a lower fee, that tells you
 15 absolutely nothing about the operation of any of the
 16 counterfactuals in circumstances when issuers were
 17 positively trying to get higher fees, and acquirers
 18 would obviously try and get lower fees.

19 So the attempt to say that MasterCard is making any
 20 kind of acknowledgement of acceptance of how the
 21 counterfactual would operate based on footnote 360 is
 22 misconceived. It is dealing with the real life
 23 situation, but showing the point we say it demonstrates
 24 with a commonsense proposition, that if Sainsbury's Bank
 25 had said "Give me less money", the acquirers would have

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1 agreed to it, particularly in circumstances where, as we
 2 know, Sainsbury's stores was on -- I'm checking whether
 3 that's confidential or not -- the terms of the
 4 relationship was such that it was a pass-through of the
 5 interchange fee so that this interchange fee was
 6 automatically passed through directly to Sainsbury's
 7 stores.

8 Sainsbury's answer to the bilaterals points is to
 9 put up a witness that we will hear from next week,
 10 Ms Bernard, who says she didn't know until it was raised
 11 by MasterCard in this claim that it was open to
 12 Sainsbury's Bank to negotiate bilateral agreements.

13 With respect, that doesn't help Sainsbury's. First,
 14 Ms Bernard does not explain why, on her evidence, she
 15 didn't know about the possibility of bilaterals until it
 16 was raised in this claim. It was raised three years
 17 ago, so there have been three years of opportunities for
 18 Sainsbury's Bank to attempt to negotiate bilaterals and
 19 bring the interchange fee down to the level which is
 20 said to be lawful.

21 It is quite clear on the evidence there's no
 22 suggestion that any attempt to that effect has ever been
 23 made. To this day, Sainsbury's Bank is charging the fee
 24 that is said to be unlawful. We say it is quite clear,
 25 therefore, that even on the best case on the evidence,

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1 that there is a significant responsibility for actively
 2 pursuing the infringement that is said to have taken
 3 place.

4 Secondly, even if it is the case that Ms Bernard
 5 didn't know the details of the MasterCard scheme,
 6 frankly, there were people at Sainsbury's Bank who dealt
 7 with the credit card on a day-to-day basis who would
 8 have done. But even if the ignorance was more general,
 9 it would mean that the claimants, Sainsbury's, the
 10 undertaking made no attempt to consider the legal
 11 options available to it.

12 But Crehan makes very clear you must avail yourself
 13 in good time of the legal options available to you.
 14 A policy of Nelsonian blindness just is not good enough.

15 In terms of the legal options, it is also important
 16 to emphasise, as we make clear because we identify
 17 a number of factors at paragraph 433 to 438 in our
 18 submissions, that of course this claim is only commenced
 19 in December 2012 and they are trying to sue going back
 20 to December 2006. So, again, legal remedies were not
 21 pursued in good time. They were pursued six years after
 22 the start of the claim period.

23 So if they wanted to alter the position, they could
 24 have done so six years earlier. And there is no
 25 suggestion that any of the matters on which their claim

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1 is based emerged at some later stage. And there were
 2 obviously, in other MasterCard claims, attempts to say
 3 people didn't know matters and those failed in front of
 4 the Court of Appeal.

5 Sainsbury's has never taken that line of saying it
 6 didn't know all of the important matters on which it
 7 bases its case, and therefore it could and should, in
 8 the context of the Crehan doctrine, have pursued those
 9 legal remedies if it was concerned about the matters it
 10 now raises. That indicates, therefore, it has
 11 significant responsibility under the terms of that test.

12 Sainsbury's also make a single-line assertion at
 13 paragraph 512 of their written opening submissions.
 14 They say Sainsbury's Bank could not have entered into
 15 bilateral agreements with acquirers when it was
 16 an affiliate licensee. Again, that doesn't get it off
 17 the hook for the last couple of years because it has
 18 been a primary licensee. But again, no explanation is
 19 given for that proposition and it simply is not correct.

20 Sainsbury's also argue that the MasterCard scheme
 21 rules discourage bilaterals. To be clear, we don't
 22 agree with that contention. The provision they quote is
 23 about forcing parties into bilateral agreements.
 24 MasterCard say you should not force people into
 25 bilateral agreements. That doesn't alter the fact that

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1 it was always open to Sainsbury's Bank to propose and
 2 try and negotiate a bilateral agreement down to what it
 3 contends would have been a lawful level of interchange
 4 fee. It didn't even make the attempt.

5 So we say it is quite clear that the Sainsbury's
 6 undertaking has happily implemented what it contends is
 7 the unlawful MIF when it always had the option not to do
 8 so. And we identify a number of other points that,
 9 again, we are going to be developing with the witnesses.
 10 Paragraphs 433 to 438 of our written opening.

11 That brings me to the English law principles, and in
 12 particular I was going to go to the Supreme Court
 13 decision of Servier v Apotex and the three questions
 14 identified by Lord Sumption. And that's bundle 17.1 at
 15 tab 25.

16 It is paragraph 22. The Tribunal has of course
 17 already been taken to this by Mr Brealey, which sets out
 18 the three questions identified by Lord Sumption. He
 19 gave the leading judgment, which were the application of
 20 the ex turpi causa principle commonly raises three
 21 questions. What acts constitute turpitude for the
 22 purpose of this defence? 2, what relationship must the
 23 turpitude have to the claim? 3, on what principles
 24 should the turpitude of an agent be attributed to his
 25 principal, especially when the principal is

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1 a corporation?

2 So turning to those three questions. In relation to
 3 the first one, it is clear from paragraph 25 of
 4 Lord Sumption's judgment and previously from the
 5 decision of the court at first instance and in the
 6 Court of Appeal in Safeway v Twigger, that a breach of
 7 competition law is serious enough to engage the ex turpi
 8 causa principle.

9 That doesn't seem to be in dispute. Now, at
 10 paragraph 29 of the judgment, Lord Sumption goes on to
 11 refer -- and, again, Mr Brealey took you to this in his
 12 opening -- to the principle that where there is a strict
 13 liability infringement, where there may be a recognised
 14 exception where the claimant was not privy to the facts
 15 making his act unlawful. You see that four or five
 16 lines down in that paragraph.

17 It is about ten lines down, I apologise:

18 "In such cases, the fact the liability is strict and
 19 that the claimant is not aware of the facts making his
 20 conduct unlawful may prove a reason for holding that it
 21 was not turpitude at all."

22 Then Lord Sumption goes on at the bottom of
 23 paragraph 29, which is a very long paragraph, to explain
 24 what the test is in relation to the application of the
 25 exception for cases of strict liability.

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1 He says:

2 "It may require a court to determine whether the
 3 claimant was in fact privy to the illegality. To that
 4 extent, an inquiry into the claimant's moral culpability
 5 ... (Reading to the words) ... as turpitude. This may be
 6 a difficult question, but it is not a question of
 7 degree.

8 "The conclusion will be a finding that the claimant
 9 was aware of the illegality or that he was not. It is
 10 a long way from the kind of value judgment implicit in
 11 the search for a proportionate relationship between the
 12 illegality and its legal consequences of the claim."

13 So ultimately, the Tribunal at this stage will be
 14 making a binary decision. Either there was sufficient
 15 knowledge of the facts, or there wasn't. It is not
 16 a value judgment about whether the punishment fits the
 17 crime. Illegality to some extent as always had perhaps
 18 a clear bright line approach to matters, and the
 19 Tribunal is not concerned with does it fit the crime,
 20 the question is whether there's sufficient knowledge
 21 under the strict liability principle.

22 We say there's simply no possible escape, and my
 23 learned friend took you to this principle and suggested
 24 he might rely upon it. We say there's simply no
 25 possible escape by reference to this principle. As

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1 a starting point, we would say that the proposition
 2 described as arguable by Mr Justice Aikens at
 3 paragraph 31 is correct, namely that legal entities that
 4 are part of one undertaking have no independence of mind
 5 or actions of will, they are to be regarded as one.
 6 It was described as arguable at that point. We say
 7 it is the correct principle. But even if that's not the
 8 case, there's no scope if the claimant was here to argue
 9 that either Sainsbury's stores or Sainsbury's Bank were
 10 unaware of the relevant facts. Everyone knew, it was
 11 very, very overt what MasterCard were doing. There was
 12 an Office of Fair Trading investigation into it, the
 13 Competition Appeal Tribunal proceedings in relation to
 14 it all before the start of the claim period.
 15 So Sainsbury's stores knew that of course the
 16 Sainsbury's Bank was issuing MasterCard's credit cards.
 17 It was doing it pursuant to the UK MIF. This is not
 18 a situation where one party can say "I have simply no
 19 idea my sister company was doing this, I didn't know
 20 about it at all". All of the key facts were well known,
 21 so we're not in the kind of territory where they can
 22 escape in relation -- on that basis.
 23 The second question or principle identified by
 24 Lord Sumption was the question of the relationship of
 25 the turpitude to the claim. This issue is one which we

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1 say is not going to be of practical relevance in this
 2 claim. We say what it does is it relates to the
 3 question of whether the wrongdoing is connected to the
 4 basis of the claim.
 5 To give the Tribunal an example, if I'm a burglar
 6 and I go and buy a glass cutting tool for the sake of
 7 breaking into people's houses, and in breaking into
 8 someone's house, I injure myself, in those circumstances
 9 my illegality, the fact that I'm a burglar, is closely
 10 connected to the fact I want to sue for cutting myself
 11 with my glass cutting tool. My illegality is connected
 12 to my cause of action.
 13 If, on the other hand, I'm a burglar and I buy
 14 a sandwich for lunch because I'm hungry, the fact that I
 15 happen to be a burglar in the rest of my time doesn't
 16 mean that my illegality is connected to the fact that
 17 I would quite like some lunch. That's simply all it is
 18 doing: is there a connection between the two? And we
 19 say that's the proposition that it is dealing with.
 20 Here we say it is quite clear that the turpitude
 21 directly connects you to the claim. The turpitude is
 22 participating in the UK MIF, charging acquirers the UK
 23 MIF, and that's directly connected to the subject matter
 24 of the claim, which is the UK MIF.
 25 So the second principle we say is clearly going to

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1 be met here. It is not particularly an application in
 2 these circumstances.
 3 The third principle is one of attribution. We say
 4 that's not relevant again in these circumstances. As
 5 the Court of Appeal held in Safeway v Twigger, the basis
 6 of liability under competition law is not vicarious
 7 liability, it is the undertaking itself which commits
 8 the infringement.
 9 So we don't have to attribute the acts to a third
 10 party. It is if you are part of the undertaking, you
 11 commit the infringement, then we say that's the end of
 12 the story. There's no need for attribution, you
 13 yourself are responsible for the actions of the
 14 undertaking of which you are a part.
 15 Those, sir, are the reasons why we are going to say
 16 the ex turpi causa principle applies if the Tribunal
 17 concludes that there was wrongdoing on the part of
 18 MasterCard. And obviously a number of those factual
 19 points which we will be developing with the witnesses
 20 and then we will develop in closing.
 21 Unless I can assist you, that was ex turpi causa.
 22 MR JUSTICE BARLING: Yes.
 23 Shall we have a break now? You have something else
 24 to do?
 25 MR COOK: I have association of undertakings to do. It

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1 might be a sensible moment to have a break.
 2 MR JUSTICE BARLING: Let's give the shorthand writers
 3 a break. That is all you have, then.
 4 MR HOSKINS: Yes, association of undertakings.
 5 (3.00 pm)
 6 (A short break)
 7 (3.10 pm)
 8 MR COOK: Sir, since this wasn't a point that, as Mr Brealey
 9 has pointed out, we have developed in our written
 10 submissions, I do have a hand-up in relation to it on
 11 the association of undertakings.
 12 MR JUSTICE BARLING: Right.
 13 MR SMITH: Thank you.
 14 Mr Cook, before you move on to that we had one
 15 question on the role of an undertaking in the ex turpi
 16 causa defence.
 17 As I understand it, what you are saying looking at
 18 the description of that defence in paragraph 22 of
 19 Lord Sumption's opinion in Apotex, you say:
 20 "We don't need to trouble ourselves with III on what
 21 principles should the...(Reading to the words)... the
 22 attributed."
 23 Because that effectively is taken over by the
 24 European law on undertakings, which you have expounded
 25 for us.

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1 I just want to be clear as to the basis on which you
 2 say that. Do you say that because the anti-competitive
 3 claim that is being advanced by the claimant is
 4 effectively based upon European law and therefore you
 5 read across the undertaking (inaudible) any defences
 6 that are run by the defendant, or do you have any more
 7 specific authority to refer us to? I notice you
 8 mentioned Safeway v Twigger.

9 MR COOK: Yes, in relation to that -- I will look at the
 10 question again. No, it is not because it is a claim
 11 based on the European law that we say that. I mean,
 12 obviously the claim is partly based on European law, it
 13 is partly based on the Competition Act, which is
 14 a matter of English law insofar as it is meaningful to
 15 distinguish English and European law in any event.

16 No, we say that applies on the basis that the
 17 question is: is there wrongdoing committed by the
 18 claimant company? And the concept of an undertaking in
 19 competition law is undertakings commit infringements and
 20 therefore the question is: is there an infringement
 21 committed by an undertaking involving the claimant?

22 So we simply say what we are doing is saying if they
 23 are right in their allegations against us, then we will
 24 respond by saying the Sainsbury's undertaking has
 25 committed exactly the same infringement along with us,

1 21

1 and so it is not so much their claim is based on
 2 anything in particular, it is that we can retaliate with
 3 exactly the same accusation against them. And having
 4 engaged illegality, we say the ex turpi causa defence
 5 simply is triggered by turpitude illegality. So
 6 provided we can point to connected illegality by the
 7 claimant company, then we are within ex turpi causa.

8 To some extent if their claim had been -- and it is
 9 not this case at all, but if their claim had been in
 10 a different context, most of the claims aren't as
 11 connected, in a sense people aren't retaliating with
 12 exactly the same plea back to the claimant company.

13 In a lot of the cases what you are doing is saying
 14 it is a claim for breach of contract, breach of tort on
 15 a very basic level, and you retaliate with yes, but you
 16 were acting illegally.

17 So you don't need to have, you know, an exact mirror
 18 image answer. You just need to be able to say your
 19 claim contract in tort is barred by your own wrongdoing.
 20 In our case, it so happens we are in a position to
 21 advance a mirror defence, but it wouldn't need to be.

22 MR SMITH: You may say it is not an oddity, but the oddity
 23 it appears to give rise to is that one then has a scope
 24 of defence, ex turpi causa defence, that is different
 25 depending on whether the turpitude is a competition law

1 22

1 turpitude as opposed to any other turpitude.

2 In other words, if it is a competition law turpitude
 3 you can say, well, the fact that the wrong wasn't that
 4 of the claimant but of the company in the same economic
 5 entity or group, that's fine. But if it were any other
 6 area of law, you would be forced down the rather
 7 different route of the English law on attribution, as
 8 Lord Sumption puts it in III.

9 MR COOK: To some extent we would suggest it is not so much
 10 an oddity, other than it might be said the competition
 11 law, it is unusual by using the concept of
 12 an undertaking.

13 So to some extent we are looking at how illegality
 14 arises, and if illegality arises however it does, it
 15 engages the ex turpi causa principle. And the
 16 competition law principle of undertakings is often
 17 helpful to groups of companies in the sense that it
 18 allows them to do things with each other that if one
 19 adopted simply a separate legal entity doctrine would
 20 make agreements between group companies unlawful. But
 21 the flip side of that is equally it means that when you
 22 structure your arrangements so that you have separate
 23 legal personality, but in reality you are a single
 24 economic business, then both or multiple parts of that
 25 entity are responsible for the actions of that group.

1 23

1 So we say if there is an oddity, it only is the
 2 oddity arising from the fact that competition law
 3 ignores corporate personality in a way that most but not
 4 all other areas of law don't.

5 MR SMITH: Is this one of your open questions that should we
 6 get to ex turpi causa we will be forced to decide? In
 7 other words, is there any authority you can point us to
 8 to say that in a competition case, in lieu of
 9 Lord Sumption's III, we apply the undertaking analysis,
 10 or is it an open question as to whether we do that or do
 11 what Lord Sumption describes in III, even in this case?

12 MR COOK: I believe it is an open question, yes. The cases
 13 which have applied ex turpi, and the leading one is
 14 Safeway v Twigger, and that has dealt with a situation
 15 where what happened in that case was the company was
 16 liable for Safeway stores, was liable for a competition
 17 law infringement, and what it wanted to do was sue its
 18 directors and then be able to claim on their directors'
 19 insurance policies for the amount of a fine.

20 That was the case that dealt with the fact that the
 21 infringement was committed by the company, and it wasn't
 22 something for which -- they are not vicariously liable
 23 for the actions of the employees. That was a case which
 24 focused on the facts that undertakings commit
 25 infringements and that the ex turpi causa principle

1 24

1 therefore applied, but not in a circumstance in which it
 2 was being widened out beyond the single group company.
 3 It was not relevant in that circumstance.
 4 So it is right to say that Tesco was a case where we
 5 advanced a number of these arguments, and they weren't
 6 decided or said to be arguable --
 7 MR SMITH: Not helpfully decided for our purposes because it
 8 was summary judgment application.
 9 MR COOK: Yes, they weren't decided any more than some of
 10 them were said to be arguable or not.
 11 MR SMITH: Yes.
 12 MR COOK: Ultimately, it is a point where you will have to
 13 decide exactly this principle. And we can point to
 14 cases and say it points in a particular direction or
 15 not. But so far as I'm aware, nobody has applied ex
 16 turpi causa in this particular context previously.
 17 MR SMITH: If memory serves, and do feel free to take us
 18 through it if it helps, Safeway v Twigger was both
 19 Mr Justice Flaux and the Court of Appeal applied the
 20 English law rules of attribution but, as you say, in
 21 a different context to this. It was as between the
 22 company or the undertaking and its employees, rather
 23 than anything else. So we don't get much help than
 24 that.
 25 MR COOK: Oddly enough, sir, the Safeway v Twigger in the

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1 Court of Appeal is not actually in the bundles.
 2 Safeway v Twigger at first instance seemed to me, but
 3 I looked earlier Safeway v Twigger in the
 4 Court of Appeal wasn't. I have copies of it with me,
 5 which I haven't used today, but it will be sensible
 6 because we probably will have to look at it in due
 7 course if we make sure they go into the Tribunal's
 8 bundles.
 9 In the context of Safeway v Twigger and what was
 10 decided, and this was a case in which a different
 11 decision was taken at first instance and then by the
 12 Court of Appeal, what was done in the Court of Appeal to
 13 the best of my recollection was not to make a decision
 14 based on attribution, other than in the simple sense
 15 that obviously a company can only act through -- the
 16 company has no real personality, it only has legal
 17 personality, so it needs to physically act through
 18 somebody.
 19 In that case, the Office of Fair Trading have
 20 decided, if I recall, that there had been
 21 an infringement by the undertaking, by the company, and
 22 the Court of Appeal concluded that the only person who
 23 can commit an infringement of competition law is
 24 a company. Well, an undertaking, so not a company.
 25 So it wasn't a situation where you normally get with

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1 vicarious liability, where you say: my lorry driver who
 2 I employ was irresponsible, he crashed while driving,
 3 and that is a wrong committed by him as an individual
 4 which somebody can sue him for, and then they come after
 5 me as an employer saying he was driving, he was doing
 6 what he was meant to do, he was negligent, you are
 7 vicariously liable for his wrong. And that's
 8 an attribution argument.
 9 What they actually said was there isn't
 10 an attribution point here because there was no
 11 infringement by the individuals. An individual can't
 12 commit an infringement competition law like that.
 13 MR JUSTICE BARLING: They were sued by breach of directors'
 14 duties, or something like that?
 15 MR COOK: That was the claim that they wanted to advance
 16 against the directors and say: you acted in breach of
 17 a director's duties. Clearly right in the sense that
 18 that it is a breach of your duty to enter into
 19 an illegal agreement which gets your company fined a lot
 20 of money. So they were suing them for breach of
 21 contracts of employment, directors' duties, and that was
 22 the claim said to be barred by ex turpi causa.
 23 And what they wanted to say was the infringement was
 24 by, or the wrongdoing was by the directors and therefore
 25 we wanted to sue for it. They said no, the wrongdoing

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1 was yours, the company's, and it can only be yours, the
 2 company's, because only an undertaking can commit
 3 an infringement of competition law.
 4 It was one that completely didn't address
 5 Lord Sumption's third proposition. That was the issue.
 6 If they had been in Lord Sumption's third proposition,
 7 then it may well be ex turpi causa would not have
 8 applied, and that was actually where the first instance
 9 judgment, which I believe was Mr Justice Flaux, the
 10 Court of Appeal differed from him on that particular
 11 issue. He said it was arguable that the claim was not
 12 barred by ex turpi causa, but the Court of Appeal
 13 disagreed with him.
 14 MR SMITH: Thank you.
 15 MR COOK: I will hand up in relation to association of
 16 undertakings, mostly because it involves going through
 17 a number of parts of -- it is all right. Have I handed
 18 it up?
 19 MR JUSTICE BARLING: Yes, you have.
 20 MR COOK: Then I got asked questions. So this addresses the
 21 association of undertakings issue response to
 22 Mr Brealey's complaint that we hadn't done so.
 23 My intention has not been to go through it
 24 line-by-line with you because large parts of it are
 25 simply -- unfortunately, it involves a fairly detailed

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1 analysis of bits of the Commission decision, but to set
 2 out for the Tribunal's assistance that of Sainsbury's,
 3 what we say the propositions are, and therefore why
 4 MasterCard says it is no longer an association of
 5 undertakings.
 6 The starting point, MasterCard acknowledges, it has
 7 to acknowledge, it doesn't agree with it, that it was
 8 an association of undertakings until 19th December 2007
 9 because that's the period covered by the Commission
 10 decision, and that was upheld.

11 We also accept as a matter of logic, even though we
 12 are not formally bound to, that that finding is one the
 13 Tribunal is going to follow, any court would follow, and
 14 unless and until there has been a sufficient change that
 15 the Commission's reasoning as approved by the Court of
 16 Justice is no longer applicable.

17 What we say is that sufficient changes had taken
 18 place by June 2009 that we were no longer an association
 19 of undertakings after that date. We advanced, as you
 20 will have seen, a sort of cascade of dates. We say we
 21 have made a certain number of changes, that is good
 22 enough. If not, we have made some more, some more, and
 23 we get to today and say we are certainly not
 24 an association of undertakings.

25 But in order to trace whether we made enough

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1 changes, we need to look briefly at the Commission's
 2 reasons and those which were then upheld by the Court of
 3 Justice so I can tell you what the changes were and why
 4 we say they are good enough.

5 The Commissioner's decision is at bundle 2.2, E2.2.
 6 If you start at paragraph 50 in the introduction
 7 section, this is by way of a factual background section
 8 and it is setting out the facts. And the Commission
 9 then goes on to draw some conclusions from them.

10 I should say factually MasterCard doesn't
 11 necessarily agree with all of these propositions. They,
 12 however, are the ones that the Commission found the
 13 Court of Justice upheld, so those are the ones the
 14 Tribunal should proceed on.

15 I would simply like to say, one isn't normally
 16 asserting as facts these propositions. They are simply
 17 ones that the Commission found.

18 So paragraphs 50 to 57 set out a number of factual
 19 propositions about what was happening with MasterCard
 20 during those periods, and what I have sought to do in my
 21 hand-up is sort of summarise in a one-line sentence the
 22 points the Commission is making as taken from these
 23 various paragraphs.

24 Unless the Tribunal would like me to do so, it
 25 wasn't my intention to take you to every paragraph

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1 underlining the words we rely upon for the moment. It
 2 is just showing you the key propositions that we say are
 3 relevant.

4 I mean, just to briefly summarise what
 5 the Commission does in these seven or eight paragraphs,
 6 it focuses on the fact that following MasterCard's
 7 international public offering on the New York Stock
 8 Exchange in May 2006, MasterCard abolished most of its
 9 regional boards, but it did not abolish the European
 10 regional board. And up until May 2006, the European
 11 regional board had been the one that took effectively
 12 all major decisions in relation to Europe, including
 13 setting, among other things, the intra EEA MIF, the
 14 cross-border MIF that was the subject of the Commission
 15 decision. And following the IPO, that power was taken
 16 away from it.

17 So MasterCard itself started setting the EEA MIF,
 18 rather than the European board. And one of the issues
 19 was, effectively, had we done enough that we were no
 20 longer an association of undertakings? And we said
 21 interchange is no longer a collective issue, it is done
 22 by MasterCard which is now owned by its shareholders.

23 And the Commission went through, and I have tried to
 24 summarise them, various points, factually at this stage,
 25 where it is just simply setting out the material that it

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1 then relies upon to say that we were still
 2 an association of undertakings.

3 It then went on at paragraphs 58 to 62 to identify
 4 another key factual background point at this stage it
 5 relied upon, which is the role of national fora of
 6 member banks. And that was where you would have local
 7 banks who would make decisions. In the UK, for example,
 8 up until 2004, it was the UK banks collectively that set
 9 the UK MIF, and from 2004 onwards MasterCard took that
 10 power away from them.

11 The Commission focused in paragraphs 58 to 62 on the
 12 fact that there continued to be national fora across
 13 Europe making national decisions on issues like domestic
 14 interchange fees.

15 What we have at the bottom, just over the page, in
 16 my hand-up, paragraph 5, are just summarised what
 17 effectively you say are the key aspects of the factual
 18 background that the Commission relied upon at this
 19 stage.

20 Firstly, that the European board, which was a board
 21 made up of members, or largely of members appointed by
 22 European banks, decided all key issues in Europe other
 23 than interchange fees. That those powers could not be
 24 taken away from the European board by MasterCard's
 25 global board without the consent of what were called

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1 class M directors, and those were bank-appointed
 2 directors. So appointed by the banks.
 3 There was a class M director that was appointed by
 4 the European banks which sat on the global board and on
 5 the European board. They said that was an important
 6 flow of information between the European board and the
 7 global board, and then the powers for national fora to
 8 coordinate their business including by deciding on
 9 domestic interchange fees.
 10 The Commission's key reasoning on association of
 11 undertakings is then at paragraphs 350 to 367 of the
 12 decision. In those paragraphs, in the bundle at 1104,
 13 the Commission lists -- I believe it is six points which
 14 it relies upon as the basis for its conclusion that
 15 MasterCard remained an association of undertakings even
 16 after the IPO.
 17 I'm going to focus on a couple of those; this is not
 18 a matter of me cherry-picking. No doubt it will be said
 19 that it is, but the reason why I'm emphasising a couple
 20 when the Commission lists six is because that's what
 21 happened in the course of the Court of Justice process
 22 whereby effectively the reasoning became narrowed down.
 23 And in the General Court and in the Court of Justice it
 24 became focused on two particularly of those. Therefore,
 25 I'm going to focus on those two, not the ones that fell

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1 away to some extent.
 2 The two particular factors at paragraph 354 was the
 3 fact that MasterCard carried on to operate in
 4 a decentralised manner in Europe, and that was based on
 5 the European board maintained as the decision-making
 6 body. That is based on the fact that the European board
 7 carries on deciding all matters other than interchange,
 8 the Commission concluded.
 9 So it said, can we see that at 359, key
 10 decision-making powers remain vested in bank-constituted
 11 bodies, in particular the European board and national
 12 fora.
 13 And developing that point which is dealt with at
 14 paragraph 359 to 367, the Commission concluded, or it
 15 rejected at 364, MasterCard's suggestion that the
 16 European board had few remaining powers.
 17 The Commission said, actually, the powers that
 18 remained were effectively all significant ones other
 19 than interchange.
 20 At 365, it again rejected MasterCard's submission,
 21 it said the European board was plainly subservient to
 22 MasterCard's global board and said, effectively, based
 23 on past practice, it was highly unlikely the global
 24 board was going to use its powers to overrule and more
 25 importantly the powers were drafted in a manner that

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1 fully protected the interests of the European banks and
 2 this was the role of the class M shareholder; which
 3 meant, as I summarised a moment ago, that the powers
 4 couldn't be taken away without the European banks
 5 agreeing to it through that class M shareholder.
 6 It then went onto conclude at paragraph 381 to 393
 7 that the intra EEA MIF was still adopted in the banks
 8 common interests. At 382 it suggested that the banks
 9 had resolved to delegate these powers, ie the powers of
 10 setting interchange fees, to a small number of bank
 11 delegates on the European board and after the IPO to the
 12 global board.
 13 The conclusion was that the banks had delegated
 14 their powers to MasterCard to set, and again while we
 15 disagree with the proposition that we are an association
 16 of undertakings up until today's date. In the context
 17 of the ex turpi causa case, again, it is important to
 18 bear in mind that language at least in relation to the
 19 first few years of the claim where we do accept we were
 20 an association of undertakings, but the basis of the
 21 claim against us was our powers were delegated to us by
 22 the banks.
 23 We don't agree with that analysis as a matter of
 24 fact, however, it is what the Commission found, what my
 25 learned friend relies upon. At 383 it concluded that

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1 there was a clear and pronounced commonality of interest
 2 among the banks. I draw the Tribunal's attention to
 3 paragraph 385, which said:
 4 "That MasterCard also ignores the fact that until
 5 31 December 2004 the no acquiring without issuing rule
 6 obliged every acquirer also to carry out an issuing
 7 activity."
 8 So it is now the case that somebody can be licensed
 9 to be just an acquirer or just an issuer. Up until
 10 31 December 2004, you could be just an issuer, but if
 11 you wanted to have an acquiring business you also needed
 12 to do some issuing as well and that was the rule. But
 13 we abolished that on 31 December 2004, but
 14 the Commission effectively at that stage were saying,
 15 firstly, you only abolished it in 2004 and they went on
 16 to say, as a result, almost all acquirers are at the
 17 same time issuers and their interest in high interchange
 18 fees for the issuing part of their card business is
 19 common.
 20 At that stage it was saying, well, you have had this
 21 rule in place and while you have abolished it, the
 22 effect is still that most acquirers have very large
 23 issuing businesses.
 24 MR SMITH: I thought, maybe it is my misreading, that the no
 25 acquiring/issuing rule was present in the 2014 rules

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1 that we looked at in bundle --
 2 MR COOK: I hope not because as far as I'm aware MasterCard
 3 undertook to remove that in 2004.
 4 MR SMITH: We better check.
 5 PROFESSOR JOHN BEATH: Yes. I think we saw something that
 6 implied that the acquirers under new rules were a subset
 7 of the set of issuers.
 8 MR COOK: E3.10 is our 2014 rules.
 9 PROFESSOR JOHN BEATH: It was all blue paper.
 10 MR SMITH: Yes, it is bundle E 3.10.
 11 MR COOK: None of this is confidential, it is published on
 12 our website.
 13 MR SMITH: Yes, the rule I was thinking of was rule 3.1 at
 14 page 4068 of bundle E3.10.
 15 MR COOK: I will take instructions on that. My
 16 understanding is that's not a: no acquiring without
 17 issuing rule. That would simply be, if you have the
 18 right to issue, you must ensure you have issued a
 19 sensible number to have the right. But I will take
 20 instructions in relation to that. My understanding is
 21 the Commission records that the express provision about
 22 acquiring not issuing was abolished.
 23 MR SMITH: Do take instructions. What it says is:
 24 "Each principal and association licensed to use the
 25 MasterCard ...(Reading to the words)... MasterCard based

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1 on such criteria as the corporation may deem appropriate
 2 from time to time."
 3 MR COOK: If you give me a moment, I can probably take
 4 instructions straightaway.
 5 The likely explanation for that is what we are
 6 looking at is MasterCard global rules. If you see
 7 underneath it says, "Modifications to this rule appear
 8 in..."
 9 MR SMITH: Then there is a European section.
 10 MR COOK: "... among other European regional section", and
 11 I would have to chase through to check.
 12 MR SMITH: Because there are additional rules.
 13 MR COOK: Yes. I can find that. If you go to page 4191.
 14 Rule 3.1:
 15 "The rule on this subject does not apply in relation
 16 to the EEA."
 17 MR SMITH: That explains it. Thank you very much.
 18 MR COOK: You are quite right to identify what is indeed the
 19 no acquiring without issuing rule as such, but not in
 20 relation to the EEA.
 21 Fortunately we have abolished the rule as
 22 the Commission recorded, but nonetheless the Commission
 23 was saying effectively it had only been abolished
 24 recently and there was a hang over effect. At that
 25 stage most acquirers had very big issuing businesses.

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1 It was concluded as a result of that that therefore
 2 there was still a commonality of interest between
 3 acquirers and issuers and the interests of the high
 4 interchange fees was common.
 5 At 388 there was the conclusion. Again MasterCard
 6 would certainly disagree with, but it is the conclusion
 7 which is that the global board still takes decisions on
 8 a MIF virtually on behalf of the banks. Again I would
 9 say that's relevant to the significant responsibility
 10 point. That is the case my learned friend advances,
 11 that we are doing things on behalf of the banks,
 12 including Sainsbury's Bank.
 13 Then, 389, the conclusion is that the global board
 14 still takes account of the concrete bank's interest in
 15 setting the level of relevant interchange fees and then
 16 after the passage in bold:
 17 "The European banks are still represented on the
 18 global board [that is through the class M director] and
 19 can thereby express their views on interchange related
 20 issues."
 21 They were saying there was still a representative
 22 there. Those were the key aspects of the Commission's
 23 decision. If I can turn now to the Court of
 24 Justice decision, which is at E1, tab 19. The section
 25 of the Court of Justice's decision dealing with

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1 association of undertaking is paragraphs 48 to 77,
 2 although the initial sections are simply dealing,
 3 obviously, with the arguments of the parties and we come
 4 to the important paragraphs at paragraphs 66 to 77.
 5 Again I have sought to summarise in my hand up what
 6 we say the key aspects to the Court of Justice's
 7 decision process were. At paragraph 66 it says:
 8 "There is a paragraph in paragraph 259 of the
 9 judgment under appeal that, in relying first on the
 10 retention of the bank's decision-making power within
 11 MasterCard and second on the existence of commonality of
 12 interest between that organisation and the bank's
 13 ...(Reading to the words)... association of
 14 undertakings."
 15 As I said that's why I focused upon only some of the
 16 Commission's original six reasons because by this stage
 17 the European Court, it has been narrowed down to
 18 effectively in front of the General Court and now in the
 19 Court of Justice, two principal ones: the retention of
 20 the bank's decision-making powers within MasterCard and
 21 the commonality of interest between the organisation and
 22 banks on the issue of interchange fees.
 23 Paragraph 68 then addresses the fact that MasterCard
 24 continued to operate in Europe as an association of
 25 undertakings in which the banks participated

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1 collectively in all essential elements of
 2 decision-making and the General Court concluded that
 3 the Commission had been right to conclude the MIF
 4 reflected the bank's interest to the commonality of
 5 interest.

6 Paragraph 69:

7 "Taken together these two factors [or those two
 8 factors] summarised at paragraph 259 of the judgment
 9 under appeal effectively explained why, according to the
 10 General Court, the setting of the MIF by MasterCard
 11 continued to operate, notwithstanding the changes from
 12 the IPO, as an institutionalised form of coordination,
 13 the conduct of the banks."

14 Then it talks about the fact that the European banks
 15 retained decision-making powers in many other key
 16 respects other than interchange.

17 Again it is the focus upon those two factors, the
 18 European bank still having decision-making powers and
 19 the commonality of interests. At paragraph 71 it
 20 records that -- it is three lines up from the bottom:

21 "After the IPO there were indications that the
 22 organisation is in reality continuing to take account of
 23 concrete banks' interests in setting the level of the
 24 MIF."

25 Finally, the key paragraph, paragraph 72:

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1 "In those circumstances, it was open to the
 2 General Court to find in the particular circumstances of
 3 the case, and taking into account the arguments
 4 expounded before it, that both the bank's residual
 5 decision making powers after the IPO on matters other
 6 than the MIF, the commonality of interest between
 7 MasterCard and the banks were both relevant and
 8 sufficient for the purposes of assessing whether
 9 MasterCard was an association of undertakings and the
 10 appeal was rejected on that point."

11 Those are the two, commonality of interest and
 12 European bank's decision-making powers, which are the
 13 important points which the courts concluded were
 14 sufficient at that time.

15 MasterCard then gives evidence to what's taken place
 16 since 2007. Of course the court judgment is 2014, it is
 17 only looking at the position up until 2007. We set out
 18 in paragraphs 8, 9 and 10 of my note the key evidence we
 19 rely upon to say matters have moved on significantly
 20 since December 2007.

21 Paragraph 8, I refer to the evidence of Mr Perez,
 22 who is President of MasterCard Europe, dealing with
 23 changes in MasterCard's governance since 2006 and the
 24 reference I have given there for his statement is at
 25 bundle C2, tab 5 and the relevant paragraphs.

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1 Again, I will just emphasise what I say is the
 2 significant evidence, that between September 2008 and
 3 June 2009 MasterCard withdrew all of the specific
 4 authorities previously granted to the European board.
 5 Since June 2009 the European board has had no powers.
 6 Again, we say, that's one of the key aspects -- probably
 7 the key aspect the Commission relied upon for the fact
 8 that the European board kept all the powers other than
 9 interchange, it concluded. Since June 2009 the European
 10 board has had no powers.

11 Paragraph 8 of his evidence:

12 "Pursuant to the terms of MasterCard's charter, in
 13 June 2008 all shares of class M stock ceased to exist
 14 and the concept of a class M director was therefore
 15 removed."

16 Again the class M director point was the fact there
 17 was a bank appointed director, which sat on the global
 18 board and therefore could pass-on the views of the banks
 19 in relation to interchange. That concept of the class M
 20 director was removed in June 2010.

21 Then paragraph 11 records the fact that we took away
 22 the power of the UK banks to set the UK MIF in 2004.
 23 The residual decision-making powers were removed in
 24 April 2014 and the position in relation to the UK is
 25 also addressed by Mr Douglas who was a member of

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1 MasterCard's UK executive management team from 2009 to
 2 2014 in his statement, bundle C2, tab 2.

3 The key paragraphs are 71 and 72 summarise what we
 4 say the key evidence is, that Mr Douglas explains the
 5 banks had very few residual powers to set scheme rules
 6 prior to 2014 and that those residual powers were
 7 removed in April 2014.

8 The other evidence we rely upon is that of Dr Niels,
 9 who has analysed changes in the UK acquiring market.
 10 I've given the reference there to Dr Niels' report.

11 This shows what has happened, particularly in 2009, as
 12 a result of banks selling off their acquiring operation,
 13 so most of the key acquirers in the UK are now stand
 14 alone businesses not owned by big banks. Not true of
 15 all of them. Barclays still has a very significant
 16 acquiring business, but as Dr Niels shows there:

17 "The majority of the UK acquiring market since 2009
 18 have been held by acquirers who don't have an issuing
 19 business at all."

20 Again the commonality of interest point that
 21 the Commission made based on the residual effects of the
 22 no acquiring without issuing rule, we say, in relation
 23 to the UK, that is unwound by 2009.

24 In short we say key factors the Commission relied
 25 upon, which were upheld by the Court of Justice, that

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1 was relevant in its judgment, ceased to apply. The
2 European Court has no powers; the class M directors
3 ceased to have a role; the UK banks haven't had a power
4 to set the UK MIFs since 2004; their residual powers
5 were removed in April 2014; and acquirers, the majority
6 of the market is held by stand alone acquirers. Based
7 on that we say we are no longer an association of
8 undertakings.

9 Obviously there's going to be a question about
10 whether the changes we have made have been significant
11 enough and there is a rolling process where we say, by
12 June 2009, it was enough, if not, by June 2010, when we
13 got rid of class M directors and, if not, it is when we
14 got rid of the residual powers of the UK banks. That is
15 the rolling process. That's why we say the analysis no
16 longer applies.

17 It is no doubt going to be suggested that this is
18 all very artificial. We are drawing lines between when
19 MasterCard was an association and at some point it moves
20 from being an association to not. We say that's very
21 artificial. The reality is here that MasterCard has
22 been going through a process of radical change of which
23 the IPO was the starting point. Historically MasterCard
24 was a members organisation. It was owned by its banks
25 and in that period it was doing as its owners told it to

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1 do. Since the IPO we have been owned by the general
2 public on the New York Stock Exchange. There were class
3 M shares held by former banks, but those were gone in
4 2010. So we are owned by the general public and
5 controlled by our shareholders. We are not, therefore,
6 owned and controlled by the banks, and we say that is
7 a rolling process. The Commission concluded and the
8 court upheld we hadn't done enough to be quite -- to
9 stope being an association of undertakings in
10 December 2007, and we say that process has been
11 continuing as we effectively did divest ourselves of
12 some of the residual parts of having been a members
13 organisation and we are no longer an association of
14 undertakings.

15 Really what the Tribunal needs to think about is not
16 the artificiality of: at some point we go from being
17 an association to not being. What the Tribunal needs to
18 do is say: if you look at the present structure, if
19 MasterCard had always been structured like this, could
20 it seriously be suggested that we were an association of
21 undertakings? It has never been suggested that American
22 Express, which has always been a company held by the
23 public on the Stock Exchange, is an association of
24 undertakings and we say MasterCard has now reached that
25 stage where it is very similar and it should not be

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1 analysed based on its previous history and the fact that
2 inevitably at some point, when you have a binary state
3 of being or not being an association of undertakings, it
4 may seem artificial to say we have moved, but if you
5 look to analyse our structure now where not acting on
6 behalf of the banks, we are not controlled by them, and
7 consequently we are not an association of undertakings
8 in that sense. Those are our submissions in relation to
9 association of undertakings.

10 Unless I can assist the Tribunal further.

11 MR JUSTICE BARLING: The only thing is, is it all a bit
12 academic? I mean you are all linked together by the
13 banks, by these licence agreements via the rules, why
14 does it matter whether you are an association of
15 undertakings or you have just got a set of agreements
16 that make provision for these things or even a concerted
17 practice? Are you going to say much about that at this
18 stage?

19 MR COOK: Sir, to be fair, we had not planned to say a great
20 deal in relation to the argument about agreement to
21 concerted practice. We don't admit it. It is a matter
22 that my learned friend will have to prove and establish
23 to you.

24 We do consider factually the analysis of the
25 association of undertakings is wrong; MasterCard is not

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1 acting on behalf of anybody else, it is an individual.
2 If my learned friend persuades you that the agreement
3 point is sufficient then --
4 MR JUSTICE BARLING: Don't we have to deal with it though?
5 It is just a mechanism, isn't it, for coordination and
6 there is no issue that you are coordinated because
7 that's what rules are for, so why does it matter? It is
8 a genuine question.

9 MR COOK: Sir, it does matter to MasterCard whether you say
10 we are an association of undertakings. It matters in
11 the context of, to be honest, the level of fines that
12 might be imposed in the circumstances if we are to be
13 treated as acting on behalf of all the banks and their
14 turnover is brought within it. That is a point --
15 MasterCard challenges the idea that we are part of
16 an association of undertakings. We don't make any
17 admissions in relation to any other parts of the
18 analysis. My learned friend will have to satisfy you
19 that the concerted practice or agreement point arises.

20 We don't factually make any points in relation to
21 that beyond what we said here, which says MasterCard is
22 not acting on behalf of the banks, it is making its own
23 unilateral decision now not because the banks are
24 telling it to do so. So we do very much challenge the
25 association of undertakings point and we are not making

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1 any admissions in relation to the rest of the analysis.
 2 MR JUSTICE BARLING: Thank you very much.
 3 MR COOK: I think we said lunchtime on Tuesday?
 4 MR JUSTICE BARLING: I think it is. All right. Thank you
 5 all very much and we will hope to see you then. We will
 6 start at 2 o'clock on Tuesday?
 7 MR BREALEY: Yes, my Lord.
 8 (4.00 pm)
 9 (The court adjourned until 2.00 pm
 10 on Tuesday, 2nd February 2016)

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