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IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS
OF ENGLAND AND WALES
QUEEN'S BENCH DIVISION
COMMERCIAL COURT

Claim No. CL-2015-000471

IN PUBLIC

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 23 February 2018

Before :

MR JUSTICE PHILLIPS

- -

Between :

SAINSBURY'S SUPERMARKETS LTD

Claimant

- and -

(1) VISA EUROPE SERVICES LLC
(2) VISA EUROPE LTD
(3) VISA UK LTD

Defendants

- -
- -

Mark Brealey QC, Derek Spitz and Sarah Love (instructed by **Morgan, Lewis & Bockius UK LLP**) for **the Claimant**
Dinah Rose QC, Daniel Jowell QC, Brian Kennelly QC, Daniel Piccinin and Jason Pobjoy (instructed by **Milbank Tweed Hadley & McCloy LLP and Linklaters LLP**) for **the Defendants**

Hearing dates: 14-17, 21-24 and 28-30 November, 1, 6-9, 12-15 and 19-21 December 2016; 11-13, 16-19 and 23-25 January; 1, 22-24 and 27-28 February, 1 March and 30 November 2017

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Approved Judgment

(PUBLIC VERSION WITH COMMERCIALLY CONFIDENTIAL MATERIAL EXCISED)

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Mr Justice Phillips:

INTRODUCTION

1. In a previous judgment in these proceedings, handed down on 30 November 2017[1], I concluded that Visa's UK MIFs do not restrict competition within the meaning of Article 101(1) and have not done so at any time during the period covered by Sainsbury's claim. That conclusion meant that Sainsbury's claim failed at that first hurdle, rendering it unnecessary to consider Visa's contention that the UK MIFs in any event were and would be exempt under Article 101(3).

2. However, and as anticipated in that judgment, the parties have asked that I nonetheless determine what levels of UK MIFs (if any) would or could have qualified for exemption under Article 101(3) on the basis that (contrary to my conclusion) the UK MIFs did (and still do) restrict competition within the meaning of Article 101(1) and (as I have already found) are not objectively necessary. Such determination would, on that basis, be relevant to:

   (i) whether Visa's UK MIFs (or any of them) were exempt and therefore lawful during the relevant claim period, providing Visa with a further defence to all or part of Sainsbury's claim; and

   (ii) if any or all of Visa's UK MIFs were not exempt and lawful, the level of Interchange Fees Sainsbury's could lawfully have been charged, Sainsbury's claim for damages being for the amount paid to Acquirers above such lawful level.

3. Both parties addressed the question of exemption on the basis that the benefits and burdens of UK MIFs are to be compared and contrasted with the no-MIF/default SAP counterfactual. Neither party invited me to consider, for these purposes, a counterfactual in which Issuers and Acquirers are assumed to negotiate Bilateral Interchange Fees.

4. This further judgment should be read as following on from my previous judgment, in which I set out the relevant background and defined a number of the terms used both above and below.

ARTICLE 101(3) ISSUES

5. The rationale for granting exemption to certain restrictive agreements, otherwise prohibited under Article 101(1), is explained in paragraph 33 of the Article 101(3) Guidelines as follows:

> "*The aim of the Community competition rules is to protect competition on the market as a means of enhancing consumer welfare and of ensuring an efficient allocation of resources. Agreements that restrict competition may at the same time have pro-competitive effects by way of efficiency gains. Efficiencies may create additional value by lowering the cost of producing an output, improving the quality of the product or creating a*

[1] [2017] EWHC 3047 (Comm).

> *new product. When the pro-competitive effects of an agreement outweigh its anti-competitive effects the agreement is on balance pro-competitive and compatible with the objectives of the Community competition rules. The net effect of such agreements is to promote the very essence of the competitive process, namely to win customers by offering better products or better prices than those offered by rivals. This analytical framework is reflected in Article [101(1)] and Article [101(3)]. The latter provision expressly acknowledges that restrictive agreements may generate objective economic benefits so as to outweigh the negative effects of the restriction of competition.*"

6. Paragraph 34 of the Article 101(3) Guidelines summarises the application of the exception as follows:

> "*The application of the exception rule of Article [101(3)] is subject to four cumulative conditions, two positive and two negative:*
>
> *(a) The agreement must contribute to improving the production or distribution of goods or contribute to promoting technical or economic progress,*
>
> *(b) Consumers must receive a fair share of the resulting benefits,*
>
> *(c) The restrictions must be indispensable to the attainment of these objectives, and finally*
>
> *(d) The agreement must not afford the parties the possibility of eliminating competition in respect of a substantial part of the products in question.*
>
> *When these four conditions are fulfilled the agreement enhances competition within the relevant market, because it leads the undertakings concerned to offer cheaper or better products to consumers, compensating the latter of the adverse effects of the restrictions of competition.*"

Although Article 101(3) refers to the "production or distribution of goods", it is clear that it also applies to the provision of services: see §48 of the Article 101(3) Guidelines.

7. It is apparent from the above that exemption will only be granted to restrictive agreements which give rise to <u>net</u> economic benefits or increases in value: to the extent that a restriction simply benefits one group at the expense of the other (a "zero sum game"), that restriction is not generating an efficiency, but merely transferring value which already exists in the economy. For example, the fact that accepting a payment card enables Merchants to win business from competitors who do not accept that card (referred to as "Business Stealing") is a benefit for the accepting Merchants but not, in itself, for the economy as a whole: their competitors suffer an equal and

opposite loss, achieving no more than transferring business from one to the other with no net gain. Although Popplewell J in *Asda v MasterCard* considered Business Stealing to be a benefit which justified exempting an element of the MasterCard MIFs (§316 to 328), Visa did not so contend in these proceedings.

8. It is not in dispute that the Scheme as a whole gives rise to several net economic benefits which would be capable of being "efficiencies" for the purpose of Article 101(3), including some or all of the following aspects:

   (a) Payment card transactions are acknowledged to be more efficient (and therefore cheaper) for Merchants than cash transactions. Card transactions are quicker at the point of sale (all the more so in the case of "contactless" cards), reduce the need for back office functions such as cash management, till reconciliation, counting and sorting and do not require collection and cash banking services. Merchants' labour costs are reduced and certain third party charges are avoided, including bank charges;

   (b) Card usage may result in fewer payment transactions than would have been required by purchasers using cash (referred to as the "ticket lift" effect), resulting in further costs savings;

   (c) Payment cards permit or greatly facilitate transactions at a distance, such as internet and telephone purchases;

   (d) Credit cards provide a period of free credit to cardholders (removing the need for Merchants to do so);

   (e) Issuers provide a guarantee of payment, taking the loss where a card is used without authority of the cardholder, benefiting both the cardholder and the Merchant, and also paying credit card transactions where the cardholder fails to pay the Issuer; and

   (f) Some or all of the above may contribute to an increase in aggregate sales by Merchants.

9. Such efficiencies, however, would arise even if the Scheme did not provide for MIFs (the no-MIF/default SAP counterfactual): they are inherent in any payment card scheme (for which, it must be assumed at this stage, a MIF is not objectively necessary). The questions which arise, therefore, are:

   (a) whether the UK MIFs contribute to the achievement of cost or qualitative efficiencies beyond those which would be generated by the Scheme in any event, that is to say, whether the first condition of Article 101(3) is satisfied;

   (b) whether, if and to the extent that UK MIFs do contribute to additional or greater efficiencies, "consumers" receive a fair share of such benefits, that is to say, whether the second condition of Article 101(3) is satisfied; and

   (c) whether the UK MIFs are indispensable to the achievement of any efficiencies to which they contribute, or whether they could reasonably be achieved by

other less restrictive means, that is to say, whether the third condition of Article 101(3) is satisfied.

It is common ground that the fourth condition of Article 101(3) need not be considered: it is not suggested that the UK MIFs have the effect of eliminating competition.

10. Visa's case as to the mechanism by which its UK MIFs contribute to increased net efficiencies, in satisfaction of the first condition, is as follows:

(a) The receipt of an Interchange Fee for each transaction incentivises Issuers to take steps to stimulate card use by their customers so as to increase the number of transactions and thereby revenue;

(b) Each Issuer makes its own commercial decision as to how to stimulate such usage, utilising one or more of the following six "channels" to a greater or lesser extent: (a) increasing rewards (e.g. airmiles or cashback); (b) increasing investment in innovation (such as Contactless payments); (c) better credit terms (such as lower interest rates on credit card balance payments or lower fees); (d) more liberal application of the payment guarantee (by more readily accepting a transaction was unauthorised); (e) promotion of e-commerce (by limiting the extent of online-security); and (f) issuing debit cards to "marginal" customers;

(c) The steps taken to stimulate card usage, by making card payments more attractive to customers, has the desired effect of increasing the number of card transactions by causing customers to switch from cash (and historically from cheques) to cards, each transaction which switches giving rise to the efficiencies and benefits of payments under the Scheme outlined above; and

(d) Certain of the benefits provided to cardholders to encourage usage also increase the efficiencies derived from transactions which would in any event have been paid for by card ("Always-Card" transactions).

11. Visa further contends that:

(a) The effect of the above process is that value is transferred to cardholders (in the form of the MIFs paid by Merchants, via the benefits Issuers decide to bestow on cardholders to obtain that revenue) so as to bring the benefits cardholders receive from card transactions into closer alignment with that which Merchants receive from such transactions (but which would not otherwise factor in Cardholders' decision-making), thereby "internalising the externalities" and making the market more efficient;

(b) So long as the burden of the UK MIFs on Merchants does not exceed the total benefit they create for consumers (TUS), the fair share condition is also satisfied: in other words, a MIF set at a level which is no higher than the benefit generated would be exempt; and

(c) There is no other mechanism reasonably capable of achieving the above results, thereby satisfying the indispensability condition.

12. Sainsbury's disputes each element of Visa's case, arguing that the UK MIFs do not contribute to any objective net efficiencies and that, to the extent that any such efficiencies are created (i) Merchants (which Sainsbury's contends are the relevant "consumers") do not receive a fair share of them and (ii) Visa cannot show that the same efficiencies could not be generated by lower levels of MIF.

The burden of proof

13. Article 2 of Regulation 1/2003 provides that a party "*claiming the benefit of [Article 101(3)] shall bear the burden of proving that the conditions of that paragraph are fulfilled*".

14. It is accordingly clear, and not in dispute, that Visa bears the burden of proving that the UK MIFs satisfy the conditions of and are therefore exempt under Article 101(3).

15. If, however, Visa is unable to prove that all the UK MIFs were exempt throughout the claim period, the more difficult question arises (at least in theory) as to which party bears the burden of proving the lower level of MIFs which would have been exempt for the purposes of calculating Sainsbury's damages.

16. Visa contends that, as the burden is on Sainsbury's to prove its loss, which Sainsbury's claims to be amount it paid in Interchange Fees in excess of what would have been an exempt and lawful level of MIF (the "Overcharge"), it is for Sainsbury's to prove that level. Visa points to the fact that Sainsbury's pleaded its claim on that basis, expressly claiming damages in the amount of payments in excess of specified levels above which, Sainsbury's asserts, the UK MIFs would not have been exempt.

17. In *Asda v MasterCard*, Popplewell J accepted MasterCard's contention to the same effect, holding that the burden of proving the overcharge, and therefore the "exemptible" level of the relevant MIFs, was on the Merchants. Popplewell J stated:

> "297… *The Claimants do not establish that the extent of their loss is the full amount of the MIF merely by establishing that the MIFs as set were unlawful. The extent of their loss is measured by the extent of MasterCard's tortiously unlawful activity, as required by the principles of causation. It is for the Claimants to establish the extent of their loss by reference to the extent of the unlawfulness. Put another way, their loss is to be measured not by the amount of the MIF they were required to pay, but the amount of the MIF they were unlawfully required to pay.*
>
> *298. The position is no different from that of any claimant tortiously induced to pay a price for goods or services, for example by tortious misrepresentation. He does not prove his loss at the total amount paid for the goods or services merely by establishing the tortious inducement and the fact of payment; he must prove that he was induced to pay more for the goods or services than he otherwise would in the absence of the tort, usually by proving he has paid more than the market value, the difference being the measure of his loss: see for*

> *example McGregor on Damages 19th edn. at paragraph 47-055. If he makes no attempt to do this he has not proved his loss. In this case, the market value of the services for which the Claimants have had to pay by indirectly bearing the MIF can be treated as that which MasterCard could lawfully have charged by setting an exemptible MIF. It is for the Claimants to establish as their measure of loss the difference between this market value and their actual payment.*"

18. Popplewell J recognised (at §302) that the result of his conclusion in this regard was that the opposing parties would each be carrying the burden of proof, simultaneously, on issues which arose under Article 101(3), albeit for different purposes. Popplewell J gave practical effect to that theoretical distinction by first determining the levels at which MasterCard's MIFs were exempt (resolving any areas of doubt in favour of the Merchants) and then increasing those figures by 10% to arrive at "exemptible" levels of MIFs for the purpose of calculating the Merchants' damages, reflecting that doubts arising in calculating those levels should be resolved in favour of MasterCard.

19. I respectfully take a different view. In these proceedings Visa has advanced arguments and adduced large amounts of factual and expert evidence in an attempt to prove that its UK MIFs, set at differing levels over the claim period, were all at or below a level it can show to be exempt. To that end it has sought to demonstrate the numerous efficiencies it asserts are caused by the UK MIFs, seeking to place a value on each of them and adding them together to reach the level it claims to be or to have been exempt: Sainsbury's (and the Arcadia claimants) adduced evidence to the opposite effect. Even if the burden of proof is strictly on Sainsbury's in relation to its damages claim, that burden is to prove the level of exemption which Visa would have been able to demonstrate during the claim period. Sainsbury's can discharge that burden by pointing to the result of that very exercise carried out in these proceedings. In my judgment, I can and should reach a decision, on the extensive evidence before me, as to what levels of MIFs can be shown by Visa to be exempt (if any), those levels necessarily being the same for both exemption and for the assessment of damages. As both sides have adduced evidence as to what is, essentially, the same ultimate issue, I do not see any merit in applying a percentage "discount" to the outcome based on an assessment of that evidence to reflect a theoretical difference in the burden of proof.

20. If, contrary to the above analysis, it is necessary for me to determine where the burden of proof lies as to exemption for the purposes of calculating Sainsbury's damages under Article 101(1), I would have found that that burden is on Visa for the following reasons:

    (a) Once it is established that the restrictive agreement in question is not exempt and is therefore unlawful and void, the loss falls to be calculated on the basis that there was no restriction unless there could have been an alternative agreement which would have been exempt. In my judgment, the burden of proving such alternative agreement and its entitlement to exemption must be on the defendant, the party seeking to rely on it. The situation is not analogous to a party to a sale of goods contract proving its loss by establishing the market price of the goods it should have received: that is the immediate measure of loss caused by the breach of contract. Establishing an alternative exempt

agreement has more in common with demonstrating that damages could have been mitigated or that there was contributory negligence, in respect of which the burden is on the defendant. It is recognised that the burden of proving facts going to avoid or abate liability in damages will be on the defendant: see *McGregor on Damages* 20th Ed. at §52-002 and §52-003;

(b) Requiring a claimant to prove what level of restriction would have been exempt would significantly undermine the enforcement of competition legislation through private claims in national courts. It would entail that such claimants would not be awarded full compensation for damage caused by restrictions set at unlawful levels and defendants would not be held to account for the full extent of their wrongdoing; and

(c) Placing the burden on the claimant would be to require a party to prove a series of negatives, namely, that alternative agreements at an infinite range of lower levels would not be exempt. The burden would produce particularly bizarre results if a defendant to a claim under Article 101(1) did not defend the claim or simply put the claimant to proof of its damages: it is difficult to see how the claimant could be expected to set about proving the exempt level of MIFs if no basis for exemption was advanced in the first place.

21. I therefore approach the task of considering what level of UK MIFs (if any) would satisfy the conditions of Article 101(3) on the basis that the burden of proof in that regard is on Visa for all relevant purposes.

The standard of proof

22. The parties agree that the usual civil standard of proof applies, namely, whether Visa has established on the balance of probabilities that its UK MIFs at a particular level are or were exempt.

23. The question arises, however, as to the relationship of that standard of proof with the requirement under EU law that the claim that a restrictive agreement creates efficiencies must be founded on detailed, robust and compelling analysis and that assumptions and deductions be based on empirical data and facts (see *the MasterCard Commission Decision* at §690).

24. In my judgment the distinction being drawn is between (a) real links to real efficiencies, capable of being observed and demonstrated on the facts by evidence (in other words, requiring empirical data), and (b) theoretical or logically assumed links and efficiencies based on broad economic or logical analysis, opinion or anecdotal evidence, perhaps sound in theory but possibly failing to take into account one or more of the many factors which arise in highly complex interactions in the real economy. I see no difficulty in this court determining whether the former has been proved on the balance of probabilities. That test is capable of accommodating varying requirements as to what is expected to meet the standard: contract terms must be "certain", allegations of fraud must be "distinctly proved" and it is often said that "cogent" evidence is required to rebut certain presumptions. In the case of Article 101(3), it is recognised that robust analysis and cogent evidence will be required to establish, on the balance of probabilities, that a restrictive agreement in fact and in the real world (as opposed to in theory) gives rise to pro-competitive effects.

25. The above analysis does not differ significantly from that of Popplewell J in *Asda v Mastercard* at §305 in relation to the standard to which Visa must prove exemption. On the other hand, I do not agree with the view expressed by Popplewell J at §307 that the court should use a broad brush and err on the side of under compensation in calculating damages, but that to some extent is a function of the different conclusion I have reached as to the burden of proof on that issue, as set out above.

The first condition: do the UK MIFs contribute to benefits or efficiencies?

The test for whether the first condition is satisfied

26. The Article 101(3) Guidelines explain (§51) that all efficiency claims must be substantiated so that the following may be verified:

> "*(a) The nature of the claimed efficiencies;*
>
> *(b) The link between the agreement and the efficiencies;*
>
> *(c) The likelihood and magnitude of each claimed efficiency; and*
>
> *(d) How and when each claimed efficiency would be achieved.*"

27. Letter (a) is directed at verifying that the claimed efficiencies are objective in nature: see §52 of the Guidelines.

28. As for letter (b), the Guidelines at §54 emphasise that the claimed efficiencies must normally be direct, further stating:

> "*Claims based on indirect effects are as a general rule too uncertain and too remote to be taken into account. A direct causal link exists for instance where a technology transfer agreement allows the licensees to produce new or improved products or a distribution agreement allows products to be distributed at lower cost or valuable services to be produced. An example of indirect effect would be a case where it is claimed that a restrictive agreement allows the undertakings concerned to increase their profits, enabling them to invest more in research and development to the ultimate benefit of consumers. While there may be a link between profitability and research and development, this link is generally not sufficiently direct to be taken into account in the context of Article [101(3)].*"

29. Letters (c) and (d) allow the decision-maker to verify the value of the claimed efficiencies. The Guidelines, at §55, emphasise that:

> "*Given that Article [101(1)] only applies in cases where the agreement has likely negative effects on competition and consumers ... efficiency claims must be substantiated so that they can be verified. Unsubstantiated claims are rejected.*"

30. In further general remarks, the Guidelines make the following points:

> "*56. In the case of claimed cost efficiencies the undertakings invoking the benefit of Article [101(3)] must as accurately as reasonably possible calculate or estimate the value of the efficiencies and describe in detail how the amount has been computed. They must also describe the method(s) by which the efficiencies have been or will be achieved. The data submitted must be verifiable so that there can be a sufficient degree of certainty that the efficiencies have materialised or are likely to materialise.*
>
> *57. In the case of claimed efficiencies in the form of new or improved products and other non-cost based efficiencies, the undertakings claiming the benefit of Article [101(3)] must describe and explain in detail what is the nature of the efficiencies and how and why they constitute an objective economic benefit.*"

The MasterCard Commission Decision's approach to the first condition

31. The Commission considered MasterCard's contention that its EEA MIFs contributed to objective net efficiencies, summarising MasterCard's case as follows:

> "*688. The central efficiency claim of MasterCard rests on the alleged capacity of the MasterCard MIF to help the scheme to maximise system "output" by balancing cardholder and merchant demands. This effect is then said to contribute to other efficiencies, such as sales for merchants; improved cash-flow for merchants; improved security and back-office operations for merchants; payment guarantee for merchants against cardholder default; payment guarantee for merchants against fraud; new sales channels; an alternative, cardholders' ability to defer payment for goods and services over a convenient period; increased personal security for cardholders, fraud protection for cardholders, increased competition in both issuing and acquiring, lower costs through economies of scale and increased innovation.*"

32. It is apparent that MasterCard was asserting that its EEA MIFs contributed to similar efficiencies as those identified by Visa in these proceedings as summarised above. MasterCard was also contending, as does Visa, that the effect of its MIFs was to align the benefits to Cardholders and Merchants of card payments so as to increase (and thereby maximise) card usage and so increase the efficiencies resulting from such usage.

33. The Commission rejected that contention in the following terms:

> "*689.… it cannot just be assumed, as MasterCard does, without detailed economic and empirical analysis, that a MIF maximises the overall benefits of a system to merchants and*

> *cardholders "by reducing costs, increasing services levels and contributing to overall economic welfare". The mechanism may overburden one side of the scheme with (artificial) costs while not yielding any positive effects on scheme growth and overall efficiency.*
>
> *690. Hence, whether a MIF should be paid by acquirers to issuers or vice versa, and whether it should be set at a certain amount or at zero, cannot be determined in a general manner by economic theory alone. A claim that an interchange fee mechanism creates efficiencies within the meaning of Article [101(3)] therefore must be founded on a detailed, robust and compelling analysis that relies in its assumptions and deductions on empirical data and facts. Apart from MasterCard's general assertion that balancing of the demand of cardholders and merchants leads to a better performance of the MasterCard system, is inherent and indispensable to the operation of a four-party payment card system, contributes to overall economic welfare and therefore "undoubtedly" fulfils the first condition of Article [101 (3)] no such analysis and empirical evidence was provided to the Commission.*"

34. The Commission further stressed the need for empirical evidence at §695:

> "*... In the context of the first condition it has to be ascertained that the restrictive effects are offset by efficiencies. In this context the undertakings concerned must demonstrate whether a MIF generates the positive effects which the underlying model claims to achieve, here: an increase of system output and possible related efficiencies. To the extent that objective efficiencies cannot be established empirically, they cannot be balanced with the restrictive effects. Some form of convincing empirical evidence on the actual effect of a MIF on the market is therefore required.*"

35. The Commission accordingly found that MasterCard's EEA MIFs did not meet the first condition of Article 101(3) and so did not qualify for exemption. That approach and conclusion was upheld both by the General Court and by the CJEU.

Visa's case that the UK MIFs caused or contributed to objective benefits

36. Visa's case is, fundamentally, the same as that advanced by MasterCard to the Commission, relying on the same economic theory as to how the same efficiencies are created: the MIF transfers value from Merchants to Cardholders, via Issuers, so as to balance the two sides of the market and thereby increase the Scheme's output and its beneficial effects. Visa contends, however, that its case (unlike that advanced by MasterCard) is based on more than mere theory, but is supported by evidence which proves that its UK MIFs do contribute to demonstrable and measurable benefits.

37. Visa's case as to the link between the UK MIFs and the creation of additional efficiencies involves two stages: (i) that the MIFs incentivise Issuers to take steps (or

greater steps) to stimulate usage of Visa cards which they would not otherwise take (or take to that extent); and (ii) that the steps so taken do indeed increase card usage, and the efficiencies of transactions which would have been card transactions anyway.

(i) MIFs as an incentive to Issuers to further stimulate card usage

38. The immediate difficulty with assessing whether and to what extent Issuers are incentivised by the prospect of revenue from MIFs is that Issuers in any event generate substantial revenues from their card issuing businesses, in particular in the form of interest on credit card balances (in the case of revolvers), interest on overdrafts on personal current accounts and other facilities (to which debit card usage contributes) and fees (card fees, currency fees etc). Whilst no financial data was provided, there was evidence indicating that Interchange Fees constitute somewhere in the region of 10% to [***redacted text***] of the revenue Issuers receive from their card issuing businesses:

    (a) In the *MasterCard Commission Decision* (footnote 829) it is asserted that in the UK issuing banks generate only 10% of their revenues from Interchange Fees, referring to data from 2000 set out in the European Card Review of March 2007;

    (b) Craig Evans, Managing Director of New Customer Acquisition at Barclaycard, confirmed orally that Interchange Fees constituted about 14% of Barclaycard's revenue; and

    (c) [***Redacted text***]

39. It follows that Issuers are in any event, in general terms, seriously incentivised to maintain and increase card usage in order to earn revenues other than Interchange Fees and would continue to be so in their absence. The question therefore arises as to whether and to what extent the MIF incentivises Issuers to take steps they would not otherwise take. It is by no means obvious or inevitable that receiving extra revenue in the form of MIFs increases such incentive in general: Issuers deprived of that revenue might decide to increase stimulation of usage to replace the lost revenue with other forms of card revenue and might be concerned that reducing stimulation would risk further reducing their revenues. Conversely, an increase in Interchange Fee revenue from existing business may cause an Issuer to decide that it is unnecessary to incur costs (or greater costs) necessary to stimulate increased business. It is all a matter of the cost-benefit analyses undertaken by sophisticated enterprises with multiple overlapping considerations as to how to maximise overall profit in the short, medium and long term.

40. A further difficulty with Visa's case in this regard is that its theory does not entail that Issuers are incentivised at any point in time by MIF revenues on existing volumes of transactions. To the extent that Issuers already receive Interchange Fee revenue on existing volumes of transactions, they have no need to incur <u>greater</u> costs to obtain that revenue. Any incentive to stimulate additional usage is limited to the amount of Interchange Fees the Issuers hope to receive from that extra volume. By way of example, if Visa introduced a MIF on a card product which did not previously have

one, Issuers would automatically receive the resulting Interchange Fee revenue on its continuing business: Issuers would not have to do anything extra to obtain that revenue, so it would not provide an additional incentive. The incentive, if any, would only be to obtain increased MIF revenue from increased sales.

41. Further, it would seem logical that the expenditure would be less than the additional revenue anticipated, the basic incentive being to *profit* from increased MIF revenue. The interrelationship between existing Interchange Fee revenue, expenditure and anticipated increased Interchange Fee revenue is unexplained and opaque at best.

42. Having expressed those concerns as to the theory behind Visa's case that the MIF incentivises Issuers to stimulate card use, I turn to consider what evidence there is of an actual link in the real world.

43. Visa did not adduce any financial or other empirical data (from Issuers in general or any particular Issuers) demonstrating any relationship between (a) card business revenues generally, (b) Interchange Fee revenues and (c) the costs of use of the 6 "channels" by which usage might be stimulated. Such evidence would seem to be exactly the sort of robust empirical data referred to by the Commission as being required to demonstrate a link between MIFs (and in particular, movements in MIFs) and expenditure on stimulation. Issuers are members of the Scheme, shareholders in Visa UK and have a clear and sizeable financial interest in assisting Visa in these proceedings, so it is safe to infer that if it was possible to demonstrate the alleged linkage with data, the same would have been adduced in evidence.

44. For example, if Visa's theory holds good in the real world, it should have been possible to adduce empirical evidence that, once Issuers knew that (i) MIF levels would be reduced following amendment to the CBA Rules on 31 December 2014 and/or (ii) MIFs were to be capped from 9 December 2015 (when the IFR came into force), they did <u>in fact</u> lower their costs and expenditure in relation to the 6 "channels", or at least budgeted to do so over the coming years. No such evidence was adduced.

45. Visa's case is, instead, advanced on the basis of what is, in my judgment, a mixture of economic theory or inference supported by opinion and anecdotal evidence. Its case as to how each "channel" is incentivised by the MIFs is as follows:

    (a) <u>Rewards:</u> Visa did not adduce direct empirical evidence that Issuers have reduced their reward programmes because of the lowering of MIF levels following the introduction of the IFR. Instead, Visa relied on Dr Caffarra's collation of news reports (and the evidence Mr Evans of Barclaycard) to demonstrate that, since the IFR came into force and MIF rates for credit cards were capped, 11 Issuers have reduced the level of rewards provided to customers for using their credit cards. On the basis of that evidence, Visa seeks to infer that there is some (undefined) degree of causal relationship between credit MIF rates and levels of credit card rewards. Such evidence (described by Dr Caffarra's as coming from a "natural experiment") is undoubtedly consistent with the existence of such a relationship and provides some support for it, but it does not prove it or demonstrate its nature or extent: it is fallacious to conclude that subsequent events are necessarily caused by earlier events. But, as appears below, that material is the <u>very best</u> evidence Visa adduced to

demonstrate a link between MIF levels and the extent to which Issuers utilise the six "channels";

(b) Credit Terms: Visa asserts that the "*same logic*" (Visa's Closing Submissions at §442) that applies to rewards also applies to credit terms. However, there were conflicting reports and hearsay evidence as to what has happened to credit interest rates (APRs) since the introduction of the IFR and the reduction in MIFs at the end of 2015. There is certainly insufficient clarity to demonstrate a pattern consistent with Visa's theory, let alone empirical evidence that there is a link between MIFs and the level of APRs;

(c) Innovation: Visa's contention is that "*MIFs…encourage innovation: they add to the collective business case of the issuer members of the scheme to adopt the new technology, as well as to the individual business cases of issuers to roll it out*" (Visa's Closing Submissions at §452). Gary Hoffman (a former CEO and Chairman of Barclaycard) and Mr Evans gave evidence that [

Redacted text

]. Further, contemporaneous documents demonstrate that [

Redacted text

]. Stephen Perry, former Chief Digital Officer of Visa Europe, [
Redacted text
]. It is therefore far from clear that MIFs incentivised innovation in the case of Contactless, the only example on which Visa relies.

(d) More liberal application of the payment guarantee: Although the payment guarantee for Cardholders is to a large extent provided for by law under the Consumer Credit Act 1974 and the Payment Service Regulation 2009, Visa contends that there is flexibility in how closely Issuers scrutinise claims under the guarantee, asserting that MIFs incentivise Issuers to apply a more liberal approach. Similarly, Visa contends that the availability of MIFs incentivises Issuers to agree to the inclusion of rules in the Scheme which guarantee payment to Merchants. Visa's case in this regard is largely, if not entirely, based on the evidence of Mr Hoffman as to what, in his opinion (drawing on his experience both as a former CEO and Chairman of Barclaycard and Non Executive director and Chairman of the Board of Visa Europe) would be likely to happen if MIFs were materially lowered or reduced to zero. His opinion as to how Issuers would be "likely" to react is, however, no more than opinion, however expert, and might more accurately be described as speculation. It was not robust empirical evidence (and did not turn into such evidence simply because it was not challenged when Mr Hoffman gave oral evidence).

(e) Development and promotion of E-commerce: Visa contends that MIFs incentivise Issuers to strike the "right" balance between online security and the need for online purchases to be as "frictionless" as possible. However, Visa's case in this regard is entirely theoretical: there was no concrete evidence whatsoever as to what steps Issuers would or would not have taken in the absence of the MIF or what the effect of those steps would be; and

(f) Issuing debit cards to marginal customers: During the claim period there was an increase in the proportion of holders of "basic" current accounts who were issued debit cards rather than just ATM cards. This was in part due to regulatory pressure and requirements, but Visa asserts that the role of MIFs in driving increased issuance is "*clear*" because "*without MIFs, issuance to these customers would have been (even) less profitable, and so it is less likely that the Government or regulators would have had such success in pressuring banks to issue debit cards to these customers*" (Visa's Closing Submissions at §512). In my judgment Visa's case in this regard is again no more than assertion based on theory and speculation, unsupported by any evidence.

46. In summary, there is in my judgment a complete absence of evidence of a real, observable and measurable link between MIFs and actions taken by Issuers to stimulate card usage. The best material that has been adduced may support some relationship between decreases in credit card MIFs and decreased levels of rewards, but its existence is a matter of supposition, there being no attempt to rule out the possibility of other causes. Even if some link was sufficiently clear, its nature and extent is not.

(ii) Stimulation of more card usage

47. If it is difficult to observe the alleged effect of MIFs on the steps taken by Issuers to stimulate card usage (including making cards more beneficial generally), it is entirely impossible to discern, let alone demonstrate, the alleged increase in card usage arising from such increased stimulation (as opposed to the pre-existing stimulation). Visa has not attempted to prove an increase in usage from any particular increase in stimulation with empirical data. Its approach is summarised in Visa's Closing Submissions as follows:

> "*526. It is impossible to quantify precisely how large a 'usage effect' those channels generate in combination. In other words, it is impossible to say precisely how much less card usage there would have been in the claim period (and into the future) if the relevant Visa MIFs had been zero during the claim period.*
>
> *527. There are, however, some clues in the evidence as to the order of magnitude of particular effects. This includes the 20% increase in credit card usage just from rewards estimated by the Australian study by Simon, Smith and West..., the 18% increase in usage in the UK caused by Contactless cited by Mr Holt... and the possibility of doubling the scale of e-commerce if online transactions could be made smoother referred to by Mr Perry... How much of those effects can be attributed to MIFs is difficult to say precisely...*"

48. Even on a broader level, it is less than clear that MIFs affect the level of card usage to any extent, by whatever channel. Sainsbury's contended that trends in card usage undermine the alleged causal link, summarising the following evidence in §278 of its Closing Submissions:

> "***First****, over the relevant period, from 18 December 2007 to date, cash use has been falling; credit card use has been* de*creasing (even though the Visa UK MIF for credit cards was, until recently, rising); and debit card use was* in*creasing (even though the Visa UK MIF for debit cards has remained broadly the same). As Mr von Hinten-Reed concludes, "the overall trend in both Visa credit and debit MIFs cannot explain the observed developments of decreasing credit card usage share and increasing debit card usage share as compared to cash."*
>
> ***Second****, the impact of falling UK MIFs on card usage from January 2015 provides what Dr Caffarra describes as a "natural experiment". Visa's UK MIFs began to fall in January 2015 when Visa changed its [CBA Rule]. Visa's UK MIFs continued to fall after the IFR came into effect in December 2015. Yet debit card use since the start of 2015 has continued to increase, while credit card use has shrunk marginally; in other words the trends described in the paragraph above have not been changed. Thus, as Mr von Hinten-Reed puts it, the data "presents a very clear message: MIFs have changed; card usage has not. The message is consistent with similar trends in Australia following the implementation of caps on MIF Levels. These data show that the MIF is not driving card usage in the UK"*."

49. Whilst empirical evidence is needed to demonstrate that a real link exists in fact, the above evidence of broad trends seems to me to be probative of the fact that there is no such link to prove. It is consistent with the fact that the card market in the UK is regarded as "mature", with the result that a large percentage of card transactions are Always-Card and that the percentage of card transactions which can be incentivised to switch from cash is relatively small. It may be that the recent success of Contactless cards has led to a large percentage of transactions switching from cash, but this is a function of the speed and convenience of the new product, not necessarily anything to do with the MIFs.

Conclusion on the first condition

50. For the above reasons I conclude that Visa has not established to the requisite standard (or anywhere close) that the UK MIFs contribute to net efficiencies by the mechanism examined above.

51. I am fortified in the above conclusion by reflecting on the huge amount of evidence, particularly expert evidence, which has been adduced by the parties in an attempt to identify and assess the value of the purported efficiencies produced by the alleged mechanism of the MIFs. Despite the volume of that evidence and the eminence of the experts, they have all ultimately engaged in (and invited me to undertake) an exercise

which involves making sweeping assumptions and the broadest of estimates, many of them requiring, in the end little more than putting a finger in the air. For example, in reaching his conclusion as to the exempt levels of MasterCard MIFs, Popplewell J was invited to make the broadest of assumptions as to the level of MIFs passed-through to Cardholders by Issuers, based on equally broad estimates of Issuers' overall profit margins (and an assumption that those margins were indicative of pass-through levels of MIF, just one income stream). Assuming pass-through of 75% for credit card MIFs and 40% for debit card MIFs, Popplewell J duly discounted his assessment of Merchant benefits by 25% in the case of credit cards and 60% in the case of debit cards (*Asda v MasterCard at* §409). I have no confidence that that type of exercise would produce anything approximating a true valuation of the allegedly pro-competitive effects of MIFs across the whole of the UK in the real economy. It would be a remarkably unsatisfactory and surprising way of assessing whether an agreement at a particular level is unlawful under a statute. In my judgment, neither EU nor UK competition law anticipates such open-textured assessment of whether an agreement is lawful: the strictures set out in the Article 101(3) Guidelines as to the approach to the proof of efficiencies speak to a far more rigorous approach.

52. I would add that, even if it was demonstrated that MIFs did incentivise Issuers to stimulate card usage and thereby increase efficiencies, I have serious doubts as to whether that alleged mechanism is sufficiently direct to satisfy the requirements of the first condition of Article 101(3). Although framed as a mechanism to balance the two sides of the card market, it can be looked at another way. Issuers are combining to impose a charge on Merchants which increases their revenues and their profits, out of which the Issuers decide to invest in improving their product by innovation and otherwise, not least so they can make yet more profit. It is unclear to me how that process differs in reality from the example given in §54 of the Article 101(3) Guidelines of a non-exempt indirect effect where "*a restrictive agreement allows the undertakings concerned to increase their profits, enabling them to invest more in research and development to the ultimate benefit of consumers*".

The second condition: do "consumers" receive a fair share of resulting benefits?

53. It was assumed in these proceedings that Merchants bear 100% of the burden of the MIFs, no point being taken as to whether any of that cost is passed-on to customers.

54. It is equally clear that, even if Visa's case as to the creation of efficiencies is right, Merchants do not receive benefits to the same value as the MIFs they pay. This is because (a) not all of the MIF revenue received by Issuers will be "passed on" to Cardholders and thereby to Merchants: Issuers will take some profit and will use some of the MIF revenue for purposes which do not benefit Cardholders such as advertising their own brand and (b) a large proportion of transactions are Always-Card, so Merchants will only gain the benefit of customers switching from cash to card in a small proportion of transactions. Visa argues that its MIFs contribute to increased efficiencies on Always-Card transactions as well, but it seems doubtful (and certainly not proved) such benefits make up for factors set out above.

55. It follows that Visa is highly unlikely to be able to satisfy the fair share condition if the reference to "consumers" in that condition is to be read as referring solely to Merchants. Sainsbury's contends that that is indeed the proper reading of the fair share condition. Visa, in contrast, argues that consumers in this context means

consumers on both sides of the two-sided market, and so includes Cardholders, the combined benefit to those consumers equating to TUS.

56. The fair share requirement is explained in the Article 101(3) Guidelines as follows:

> "*84. The concept of 'consumers' encompasses all direct or indirect users of the products covered by the agreement, including producers that use the products as an input, wholesalers, retailers and final consumers, i.e. natural persons who are acting for purposes which can be regarded as outside their trade or profession. In other words, consumers within the meaning of Article [101(3)] are the other customers of the parties to the agreement and subsequent purchasers...*
>
> *85. The concept of 'fair share' implies that the pass-on of benefits must at least compensate consumers for any actual or likely negative impact caused to them by the restriction of competition found under Article [101(1)]. In line with the overall objective of Article [101(1)] to prevent anti-competitive agreements, the net effect of the agreement must at least be neutral from the point of view of those consumers directly or likely affected by the agreement. If such consumers are worse off following the agreement, the second condition of Article [101(3)] is not fulfilled. The positive effects of an agreement must be balanced against and compensate for its negative effect on consumers. When that is the case consumers are not harmed by the agreement. Moreover, society as a whole benefits where the efficiencies lead either to fewer resources being used to produce the output consumed or to the production of more valuable products and thus to a more efficient allocation of resources.*
>
> *86. It is not required that consumers receive a share of each and every efficiency gain identified under the first condition. It suffices that sufficient benefits are passed on to compensate for the negative effects of the restrictive agreement. In that case consumers obtain a fair share of the overall benefits. The restrictive agreement is likely to lead to higher prices, consumers must be fully compensated through increased quality or other benefits. If the second condition... is not fulfilled.*"

57. In *Asda v. MasterCard* Popplewell J interpreted the above provisions as requiring that Merchants, as the consumers directly affected by the MIF (and paying higher prices as a result), must be, at least, no worse off as a result of the restriction. Sainsbury's relies upon that interpretation as supporting its case in these proceedings.

58. Visa contends that that is an incorrect reading of the Guidelines, submitting that the definition of consumers is wide enough to encompass consumers on both sides of the two-sided market in question, Merchants and Cardholders both being affected by the restrictive agreement. Visa further emphasises that the Guidelines focus on the overall

benefits to society as a whole, consistently with the policy underlying Article 101(3), namely, to ensure that there is an overall increase in pro-competitive efficiencies. In other words, Visa's case is that Merchants can be made worse-off if, overall, the market is made more efficient, although it accepts that Merchants must receive at least some benefit, even if not fully compensated.

59. Visa further submits that, contrary to Popplewell J's analysis, this very point has been decided by the Court of Justice in the *MasterCard CJEU Decision*. In §240 to 243 of that decision the CJEU explains that where there is a restriction in one market, benefits received from the restriction on another connected market could be taken into account in determining whether benefits compensated for burdens, but only if appreciable objective advantages could also be shown on the relevant market.

60. The difficulty arises in determining whether, at this point of its judgment, the CJEU was addressing only the first condition of Article 101(3), as initially appears to be the case from the wording of §240, or whether it is also taking into account the fair share requirement. It is far from clear which is the correct answer. Popplewell J considered that the CJEU was only considering the benefits requirement.

61. However, the position appears to be sufficiently clarified in §247, where the CJEU stated:

> "*As regards the appellant's argument that the General Court did not explain why the first two conditions in Article [101(3)] could not be satisfied on the basis only of the advantages the MIF produce for cardholders, it is sufficient to refer to paragraphs 240 to 245 of the present judgment.*"

62. It is apparent from that wording that the earlier paragraphs did indeed take into account the need to satisfy the fair share requirement. I therefore agree with Visa that the CJEU has indeed decided that both Cardholders and Merchants qualify as consumers for the purposes of the fair share requirement and that benefits accruing to cardholders can therefore be taken into account in determining whether benefits at least equal the disadvantage of the MIF. However, there must be at least some objective advantages for Merchants, even if less than the burden they suffer. This reading is further confirmed in the next paragraph (§248), in which the CJEU affirmed that "*merchants had to enjoy the MIF 'as well as' cardholders, and not 'to the same extent' as them*".

63. That analysis is indeed more consistent with the policy of maximising overall economic efficiency and has the attraction of applying the same broad approach to assessing the fair share requirement whether it is positive or negative: both Cardholders and Merchants are in a very real sense the consumers affected by MIFs, and either group may bear the burden of paying it depending on whether it is positive or negative.

64. It follows that I would not have held that the fair share requirement was, in itself, a legal and logical barrier to Visa establishing an exempt level of MIF. The difficulty, as I have explained above, is in proving that the MIFs contribute to any benefits. I shall not attempt to consider whether, if Visa had been able to establish such benefits, those benefits would have met the fair share requirement.

The third condition: is a MIF indispensable for the attainment of the benefits?

65. If, contrary to my conclusion above, Visa's case as to how the MIF contributes to efficiencies by incentivising the stimulation of card usage is both sound as a matter of economic theory and demonstrable by empirical data, it is readily apparent that the MIF is an essential element of the alleged mechanism.

66. Sainsbury's and the Arcadia claimants advanced arguments as to alternative means of incentivising cardholders or generating benefits which arise more generally under the Scheme, such as Merchants issuing their own rewards (in the form of discounts, "green stamps" or the like), surcharging customers who pay in cash or providing store credit. None of those proposed alternatives seemed to me to be a remotely reasonable alternative. I accept that, if Visa's case was otherwise valid, UK MIFs at some level would, effectively by definition, be indispensable.

Conclusion on Article 101(3)

67. For the reasons set out above, I determine that if (contrary to my previous decision) Visa's UK MIFs have at any time restricted competition within the meaning of Article 101(1), they were not exempt under Article 101(3) and would not have been exempt at any level.

68. That is not to say that the Visa Scheme does not provide substantial benefits to Merchants which merit (in the broadest sense) the payment of fees to Issuers who provide Visa cards to their customers. My conclusion is directed solely to the question of whether the imposition of such fees produce pro-competitive benefits which would outweigh the restrictive effects of the MIFs if, contrary to my previous decision, MIFs do constitute a restriction of competition under Article 101(1).