Interchange Fee Litigation in the English Courts: The Consequences of the Court of Appeal's Recent Judgment [1]

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Several years of litigating unlawful multilateral interchange fees ("**MIFs**") in the English Courts[2] reached a pivotal point in July, following a much-anticipated judgment handed down by the Court of Appeal ("**CoA**") (the "**CoA Judgment**").[3] The CoA Judgment resolves two decisions of the High Court and one by the Competition Appeal Tribunal (the "**CAT**"), in which conflicting conclusions had been reached as to whether MasterCard's and VISA's MIFs were an infringement of competition entitling retailers to damages. As explored in this article, alongside this long-running issue, the CoA Judgment resolves a number of legal principles which should serve as a useful wider precedent for competition damages cases, including the legal test for assessing whether there has been pass-on of any overcharge by a claimant.

Background

MasterCard and VISA operate a four-party payment card system with rules governing the relationship between participants. At its simplest, in MasterCard's and VISA's four-party system, retailers pay the MIF to their bank (the "**Acquiring Bank**") when customers use a debit/credit card issued by their bank (the "**Issuing Bank**")) to pay for goods/services. The claims brought before the English Courts relate to MIFs set by MasterCard/VISA on UK transactions prior to implementation of the Interchange Fee Regulation in December 2015 (the "**IFR**").[4] The IFR set a maximum MIF payable on debit/credit card transactions; Member States may impose lower caps for domestic transactions.

In the years pre-IFR, MIFs attracted attention from both national and international competition regulators. In July 2002, the European Commission (the "Commission") accepted commitments from VISA to reduce its MIFs applicable to European Economic Area ("EEA*") cross-border transactions. In 2010, further commitments were made by VISA in relation to its EEA cross-border debit MIFs and, in 2014, in relation to its EEA cross-border credit MIFs. With regard to MasterCard, in December 2007 the Commission issued an infringement decision in relation to its EEA MIFs, finding that they were unlawful in the period dating back to May 1992 (the "2007 Decision").[5] The 2007 Decision withstood attempted appeals by MasterCard to the General Court of the European Union in May 2012,[6] and an appeal to the Court of Justice of the European Union ("CJEU") in November 2014.[7]

In 2012, claims were brought by various retailers in the English Courts against MasterCard and VISA for competition damages on the basis of Article 101 of the European Treaty and the UK Competition Act 1998.[8] The claims related to both follow-on claims for MasterCard's EEA fall-back MIFs[9] (relying upon the 2007 Decision) and stand-alone claims in relation to UK MIFs, relying upon an argument that the principles of the 2007 Decision on EEA fall-back MIFs could be read-across as applying equally to domestic MIFs. Thus, unlike in a typical follow-on claim for damages, in the standalone claims, all elements of a damages action had to be established by the retailers. As noted below, the claims that are the subject of the judgments to date relate to the UK MIFs. Claims have also been brought against MasterCard in relation to 17 EEA countries (including the UK) and Switzerland which are awaiting also pending.[10]

Recapping the First Instance Judgments

In a very unusual turn of events reflective of the potential exposure of MasterCard/VISA, what are effectively the same claims were taken to trial three times:

(i) Sainsbury's v MasterCard.[11]

Sainsbury's brought its claim against MasterCard in December 2012, which was transferred to the CAT in December 2015.[12] It was the first Article 101 interchange case to go to trial. In July 2016, the CAT ruled in favour of Sainsbury's, finding that the MIFs were a restriction of competition. Specifically, the CAT found that, in a counterfactual world without the MIF, bilateral agreements would have been entered into by the Issuing and Acquiring Banks. Sainsbury's was awarded in excess of £68m in damages. However, neither the retailer nor MasterCard had submitted evidence on bilateral agreements being the appropriate counterfactual, and this ultimately became one of the focal points of MasterCard's appeal. The CAT also addressed the competing arguments of whether the MIF had been passed on by Sainsbury's to its customers and found that, whilst in practice there may have been some pass-on of interchange fees by Sainsbury's as part of its overhead costs, in the absence of any evidence of a direct and identifiable causal link between the fees and ultimate prices charged by Sainsbury's, pass-on was not established as a matter of law.

(ii) ASDA & Others v MasterCard.[13]

In October 2012, Argos filed a claim in High Court against MasterCard, and in May 2013, ASDA and Morrisons issued similar claims. After trial in January 2017, the High Court dismissed the claims, finding that: (i) the MIFs were not an infringement of Article 101(1); and (ii) the MIFs would in any event have been exempt under Article 101(3) (with the exemptible levels higher than those actually set by MasterCard). The High Court was persuaded by MasterCard's 'death spiral' counterfactual, meaning that the MIFs in the UK were objectively necessary for the scheme to operate. The Court determined it was not bound to follow either the CAT's *Sainsbury's* judgment nor the Commission's 2007 Decision. In the absence of evidence before it, the High Court determined that the VISA scheme was identical to MasterCard's and that, in a world where MasterCard would have to lower its MIFs, VISA would have to do likewise. The fact that the claims against MasterCard and VISA had been pursued separately by the same claimants, allowed MasterCard/VISA effectively to play off each other and adopt the same argument in different proceedings.

(iii) Sainsbury's & Others v VISA.[14]

Sainsbury's brought its claim against VISA in the Chancery Division in December 2013 but it was subsequently transferred to the Commercial Court to be case-managed and heard alongside claims brought by ASDA and others. In November 2017, after a 12-week trial on liability issues, the Court dismissed the retailers' claims on the basis that VISA's MIFs did not infringe Article 101(1). It also took the view that, as a matter of fact, the High Court was free to reach an alternative conclusion as to the lawfulness of the MIFs to that reached by the Commission and the EU Courts. However, in a further twist – as the matter had been covered at the trial and perhaps in anticipation of future claims/appeals – the Court issued a further judgment in February 2018 holding that, had the MIFs constituted an infringement, they would not have been exempt at any level on the basis of Article 101(3)[15].

The CoA Judgment

Permission having been granted for a combined appeal, a two-week hearing took place in late April before the CoA in which the Commission intervened. In a prompt judgment, the CoA upheld most of the retailers' appeals. The CoA made a concrete finding in respect of Article 101(1), holding that the MasterCard/VISA MIFs were an infringement of competition law, but it left open the outcome of Article 101(3) as to whether the MIFs were justified in whole or in part, and the level of any damages award. Having identified the appropriate principles to be applied (and errors made by the lower-tier Courts), it remitted the hearing back to the CAT for a combined hearing, for which the parties are only permitted to use the evidence put forward in the original trials.

(i) Did the MIF Rules restrict competition under Article 101(1)?

The CoA found that the setting by MasterCard/VISA of a default UK MIF constitutes a restriction on competition when compared to a counterfactual scenario – i.e. a world without the default MIF – where there is, instead, settlement at par (i.e. the Issuing Bank to pay the Acquiring Bank 100% of the transaction, without first deducting the MIF). This counterfactual is the same as was adopted by the Commission, and ultimately supported by the CJEU in the subsequent EU appeals. In reaching this finding, the CoA held that the MIF limited the pressure which merchants could exert on the Acquiring Banks, thus leading to a reduction in competition.

The first instance Courts had, between them, identified two other counterfactual scenarios which were overturned by the CoA:

- The CAT's conclusion that MIFs would have been agreed bilaterally between Issuing Banks and Acquiring Banks could not stand, as there was no evidence from any expert at trial to support this conclusion.
- The High Court's acceptance of MasterCard's 'death spiral' argument – which relied on the ancillary restraint doctrine that the MIF was objectively necessary – was overruled. The 'death spiral' is based on the idea that when one system is forced to lower its MIFs while its rival system continues to set high MIFs, the system with lower MIFs loses most or all of its Issuing Banks to its rival. The CoA held that the right test is to ask whether the default MIF was essential to the survival of the system itself – to which it found the answer to be clearly in the negative. This is endorsed by the fact that, even post-implementation of the IFR, the relevant MIFs that are the subject-matter of the IFR have not initiated a collapse of MasterCard and/or VISA.

(ii) Notwithstanding the restriction on competition, were the MIFs nevertheless exempt from the restriction?

The CoA overturned the previous judgments dealing with Article 101(3) by setting down eight guiding principles for remittance to the CAT. Crucially, the guidance requires that there be a direct link between the restriction on competition and the resulting benefits, which must be underpinned by facts and evidence that are supported by empirical analysis and data. The CoA found that the High was wrong, in its judgment, to estimate the percentages of credit and debit pass-through without any cogent factual or empirical evidence. In addition, the "fair share" benefit must be felt by consumers as a whole – that includes both cardholders and merchants – and the resulting negative/positive effects to cardholders and merchants must be assessed separately (i.e., where one group feels only the negative effects, such effects cannot be balanced against the positive effects felt by the other group).

The CAT is, according to the CoA, better placed to make the final Article 101(3) ruling than the Commercial Court because it is a specialist tribunal, although the CAT panel will include a High Court judge as a Chairman. The parties will not be permitted to make a new case or introduce new evidence (save in respect of quantum for *Sainsbury's v VISA* and *ASDA v MasterCard*) – although the parties will be permitted to rely on evidence previously put forward in all cases (whether or not they were a party to those particular proceedings). Given the two-sided nature of the MasterCard/VISA schemes, the outcome of the CAT hearing will likely be a significant contribution into how the difficulties presented by two sided markets may be resolved; particularly in circumstances where the two markets – in this case the cardholders and the merchants – are so inextricably linked (namely (i) the value of a MasterCard/VISA card to a cardholder depends upon the extent to which it will be accepted by merchants; and (ii) the benefit that merchants gain from accepting MasterCard/VISA cards depends upon cardholders having and using those cards).

(iii) If the retailers had established a cause of action for damages, could MasterCard/VISA seek to reduce the retailer's quantum?

If MasterCard and VISA are unsuccessful in arguing that the MIFs are not fully justified, then they will have a final chance to reduce the ultimate damages pay-out. One issue in dispute was identifying which party bears the burden of proving the lawful level of MIF (assuming that the restriction is not exempt). The CoA clarified that the correct approach is to determine the answer to the issues in Article 101(3) i.e. to establish what, if any, would be the lawful level of a MIF. Assuming the MIF is not justified in whole, this level would then be used to assess damages, rather than any separate consideration of the counterfactual needing to be carried out. The CoA also confirmed that in this regard, the burden of proof in relation to the lawful level of the MIF is on the systems, and not on the merchants.

In addition, the CoA found that the CAT was right not to have reduced Sainsbury's damages for pass-on. The issue on appeal was whether the CAT in *Sainsbury's v MasterCard* was inconsistent in finding, on one hand, that MasterCard had failed to prove that the MIF had been passed-on to the merchants' customers, and there should be no reduction as a matter of law for pass-on, and that, on the other hand, Sainsbury's was entitled to compound interest on only 50% of the MIF to reflect the fact that in practice some element of the MIF would have been passed on as part of the overhead costs. The CoA held that the CAT was making economic, as opposed to legal, assumptions when restricting the level of compound interest and therefore it was not inconsistent in adopting this approach. This confirms the approach adopted by the CAT that pass-on will only be established as a matter of law where there is a sufficiently close causal connection between the overcharge and an increase in the price. MasterCard was unable to establish this in the *Sainsbury's* case.

The State of Affairs

The CoA refused permission to appeal in respect of all parties who were unsuccessful in their appeals and cross-appeals. MasterCard/VISA have, however, both applied to the Supreme Court for permission to appeal the CoA Judgment. A decision is anticipated by the end of 2018 and, pending that outcome, the remittal hearing before the CAT is on hold. The issue for the Supreme Court will be whether the applications raise an arguable point of law of general public importance.[16] In this context, therefore, it is not sufficient to point to the volume/value of claims at stake for MasterCard/VISA. It is interesting in this regard to note that the Supreme Court recently refused the Defendants' application to appeal in *iiyama*, on the basis that the issues were not of sufficient public interest.[17]

Finally, the territorial scope of the CoA Judgment is not necessarily restricted to the UK MIF, as the CoA has noted that the nature of evidence which will satisfy the standard of proof must be informed by European Union law and the 2007 Decision. In this context, the CoA stated that it is "*important to maintain a consistency of approach across Member States as to the requirements of article 101(3)*"[18] and that "*[I]t would be remarkable if the same scheme rule requiring the payment of MIFs in default of the agreement of bilateral interchange fees were held to be in breach of article 101(1) in one Member State, but not a breach of it in another Member State, whatever the factual or expert evidence might have been as to what might have happened in the postulated counterfactual.*"[19]

Conclusion

As the roller-coaster of the interchange litigation continues to its next chapter, we await the outcome of the applications made by MasterCard and VISA to the UK Supreme Court and, subject to the outcome of those applications, the remittal hearing back to the CAT. However, the principles at issue are of wider significance and practical importance to all English private enforcement cases in the competition sphere, notably as to the test to be applied to claims for which exemption is claimed under Article 101(3), the burden of proof in relation to such exemption and the assessment of loss and arguments relating to mitigation of damages and pass-on. The clarification of these principles should further assist the development of competition law and simplify private enforcement damages claims.

Footnotes

* EEA includes EU Member States in addition to Iceland, Liechtenstein and Norway.

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[2] References to “England” and the “English” are to be construed as references to England and Wales.

[3] [2018] EWCA 1536 (Civ) (4 July 2018).

[4] Regulation (EU) 2015/751 of the European Parliament and of the Council of 29 April 2015.

[5] COMP/34.579 (19 December 2007).

[6] [2012] 5 CMLR 5 (24 May 2012).

[7] [2014] 5 CMLR 23 (11 September 2014).

[8] This article will refer only to the provisions of the Treaty on the Functioning of the European Union.

[9] The EEA fall-back MIFs apply in two scenarios: (1) to all cross-border transactions between Member States; and (2) where Acquiring and Issuing Banks have been unable to agree, between themselves, a ‘bilateral’ fee or in the absence of a domestic fee set by MasterCard/VISA.

[10] *Deutsche Bahn AG & Others v MasterCard Incorporated & Others* (High Court Case No’s: HC-2012-000196 and HC-2014-000636).

[11] *Sainsbury’s Supermarkets Ltd v MasterCard Incorporated & Others* ((Case: 1241/5/7/15 (T) [2016] CAT 2 (14 July 2016)) (Court of Appeal case number C3/2016/4520).

[12] Order of Barling J dated 1 December 2015 and judgment of [2015] EWHC 3472 (Ch).

[13] *ASDA Stores Limited & Others v MasterCard Incorporated & Others* [2017] EWHC 93 (Comm) (30 January 2017 – judgment of Popplewell J) (Court of Appeal case numbers A3/2017/0892, A3/2017/0890 and A3/2017/0889).

[14] *Sainsbury’s Supermarkets Ltd v VISA Europe Services LLC* [2017] EWHC 3047 (Comm) (30 November 2017 – first judgment of Phillips J) (Court of Appeal case number A3/2017/3493).

[15] *Sainsbury’s Supermarkets Ltd v VISA Europe Services LLC* [2018] EWHC 335 (Comm) (23 February 2018 – second judgment of Phillips J).

[16] *See* UK Supreme Court Practice Direction 3.3.3.

[17] *See* UK Supreme Court permission to appeal results for June/July 2018, available here: https://www.supremecourt.uk/docs/permission-to-appeal-2018-0607.pdf (accessed 24 September 2018).

[18] *Supra* note [3] at paragraph 81.

[19] *Supra* note [3] at paragraph 157.

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