

MORE FIRSTS FOR COMPETITION LITIGATION - CAT AWARDS SAINSBURY'S DAMAGES OF £68.6M (PLUS COMPOUND INTEREST) AGAINST MASTERCARD

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Legal Briefings - By **Stephen Wisking**, **Kim Dietzel** and **Molly Herron**

On 14 Jul the UK Competition Appeal Tribunal (**CAT**) issued its judgment in the damages claim brought by Sainsbury's against MasterCard. The CAT found that MasterCard's setting of UK multilateral interchange fees (**MIFs**) for its payment cards infringed the Article 101 TFEU/Chapter I prohibition on anti-competitive agreements, and awarded damages of £8.6m, plus interest.

Significantly, this is: the first time the CAT has awarded damages in an Article 101 TFEU/Chapter I claim; the CAT's highest award of damages to date; and its first judgment in a 'stand-alone' competition claim. The case is the first in which a UK court has given judgment on the crucial question of the passing-on 'defence', with the CAT setting a relatively high bar for defendants wishing to invoke this. It is also the first competition case in which compound interest has been awarded.

The CAT's approach is likely to have a significant impact on future damages actions and settlement negotiations. The effect of the decision on on-going MIFS litigation by other retailers - and a threatened £19bn consumer class action - remains to be seen.

This case comes as part of a huge increase in the private enforcement of competition law in the UK courts in recent years. The prospect of competition claims being brought - whether or not public enforcement action has been taken by the competition authorities - is now a key risk which businesses must take into account when dealing with their customers and competitors.

1. BACKGROUND

MIFs

The case relates to the MIFs established by MasterCard under the MasterCard payment scheme which Sainsbury's was required to pay for MasterCard credit and debit card transactions. In simplified terms, a MIF is a form of interchange fee charged by the bank which issued the card to the consumer (**the issuing bank**), and paid by the retailer's (or other merchant's) bank (**the acquiring bank**) for processing a payment card transaction. This transaction fee will be charged by the acquiring bank to the merchant. An interchange fee can either be agreed bilaterally between individual banks, or set by the payment scheme operator (MasterCard in this case) multilaterally (a MIF). Unless the merchant chooses to impose a surcharge on the consumer for paying by card, the merchant would bear the fee and the cardholder would pay the same price for the goods or services he/she purchased irrespective of the mode of payment.

Interchange fees have been subject to much regulatory scrutiny in various jurisdictions (and are now subject to EU legislation as to their level). The European Commission previously investigated the MasterCard scheme for cross-border MIFs (which apply when a card issued in one Member States is used in another Member State). It found that this restricted competition in breach of Article 101 TFEU, and that - at the level the MIF was set - this could not be justified under the Article 101(3) TFEU efficiency exemption. This infringement decision was upheld on appeal by both the General Court and the Court of Justice.

Sainsbury's damages claims

In 2012, Sainsbury's launched a damages action, claiming that MasterCard's UK MIFs (for cards issued in the UK and used in the UK) breached Article 101 TFEU and/or the Chapter I prohibition¹, and that this breach has caused it loss.

Sainsbury's brought its claim in the High Court, but this was transferred to the CAT in December 2015 following the coming into force of legislation which extended the CAT's jurisdiction to cover stand-alone claims (not reliant on the infringement decision of a competition authority), and allowed claims to be transferred between the High Court and the CAT.

Other private MIFs litigation

Hundreds of other retailers/merchants (including Arcadia, Tesco, John Lewis, Ocado, Dixons, Deutsche Bahn and Hertz, to name a few) have brought separate claims in the High Court and/or CAT against MasterCard (and in some cases against Visa) in respect of MIFs. The most advanced of these claims (which were in trial) have been stayed pending judgement in this case. In addition, on 5 July Walter Merricks, an ex-lawyer who previously led the UK Financial Ombudsman Service, announced that he intended to launch a £19bn opt-out class action in the CAT against MasterCard on behalf of UK consumers under the new competition collective redress regime, on the basis that merchants had passed on the allegedly overcharged MIFs to customers in the form of higher prices for goods and services.

2. CAT JUDGEMENT

The CAT issued its judgement on 14 July 2016.

INFRINGEMENT

Notwithstanding the Commission decision on cross-border MIFs, the CAT did not consider that it was bound by the conclusions of the Commission (and the EU Courts), as that case dealt with different facts. The CAT therefore had to determine whether the settling of the UK MIF infringed Article 101 TFEU.

Article 101(1) TFEU

Taking each limb of Article 101(1) TFEU in turn:

- The CAT found that the MasterCard scheme amounted to an agreement between undertakings - i.e. MasterCard and the member banks - as well as (at least up to a certain point in time) a decision of an association of undertakings.
- The CAT found that the agreement did not have the 'object' of restricting competition (i.e. where a sufficient degree of competitive harm is presumed by the nature of the agreement), in light of various factors including: the rationale and basis for setting the MIF; the fact that MIF was a default position only; the fact that the agreement was not secret; and the fact that any harm to competition was not clear-cut without a detailed effects analysis.
- The CAT therefore considered whether the default UK MIF had the 'effect' of restricting competition by analysing the complex question of what was the relevant counter-factual. It rejected the counter-factuals put forward by both MasterCard and Sainsbury's. The CAT concluded that, absent the existence of the default MIF, the issuing and acquiring banks (and their merchants) would have bilaterally negotiated "market price" interchange fees which would have been lower than the MIF, but above zero (coming to an estimated figure for each type of card). The MIF did therefore have the effect of appreciably restricting competition, as it meant the issuing banks were unlikely to engage in such negotiations, preventing greater competition between banks on the acquiring market.
- The CAT rejected MasterCard's argument that the MIF was an objectively necessary restriction ancillary to the legitimate activity of operating the MasterCard scheme, given its conclusion that absent the MIF a viable interchange fee would have been agreed via bilateral negotiations.

Article 101(3) TFEU

The CAT rejected MasterCard's arguments that the MIF as set was justified under the Article 101(3) TFEU exemption criteria, inter alia as it did not promote economic progress and was not necessary for the operation of the beneficial MasterCard scheme.

ILLEGALITY/EX TURPI CAUSA

MasterCard argued that Sainsbury's Bank was part of the same 'single economic understanding' as Sainsbury's in competition law terms. It argued that, as Sainsbury's Bank was an issuing bank participating in the MasterCard scheme (and receiving the MIFs), it was party to any infringement, such that Sainsbury's would be barred from bringing a claim.

The CAT found that, whilst the ex turpi causa principle could apply to competition law infringements, on the facts the nature of Sainsbury's Bank's breach was not sufficiently serious to engage the principle, in particular as the breach should be regarded as "innocent" rather than intentional or negligent.

Notwithstanding this conclusion, the CAT also considered the question of whether the conduct of Sainsbury's Bank could be attributed to Sainsbury's for these purposes, in light of the EU law concept of a single 'undertaking'. On the facts the CAT held that Sainsbury's and Sainsbury's Bank (which was jointly owned by Sainsbury's parent company and a third party bank) were not part of the same undertaking, and that, even if they were, Sainsbury's Bank's conduct could not be attributed to Sainsbury's. The CAT's findings on attribution (in circumstances where Sainsbury's itself did not participate in the infringement and did not have "decisive influence" over the legal person which did) are likely to be relevant in other areas of competition litigation.

DAMAGES

Having found that MasterCard had infringed Article 101 TFEU, and that it could not rely on the illegality defence, the CAT went on to assess what (if any) damages were caused by that breach, recognising that this necessarily involves the use of a "broad axe".

Overcharge

Firstly the CAT assessed the extent of any overcharge i.e. the difference between the UK MIF actually paid by Sainsbury's and the highest lawful interchange fee that would have been paid in the counter-factual world. Unlike the position in many other competition claims (for example those relating to cartels), the CAT had already estimated the latter as part of its assessment of whether an infringement had been committed (at a level higher than that claimed by Sainsbury's). It found that Sainsbury's would have paid (the equivalent of) 0.50% in the case of credit cards and 0.27% in the case of debit cards.

The CAT therefore deducted these sums from the MIFs actually paid for the relevant period (i.e. 5 years prior to the issue of proceedings for transactions in Scotland, and 6 years for transactions in England and Wales, due to the applicable limitation rules) and computed the overcharge.

From the resulting figure the CAT deducted an amount representing the proportion of the overcharged MIFs received by Sainsbury's Bank from which Sainsbury's had benefitted.

Passing-on and mitigation

MasterCard argued that Sainsbury's could not have suffered any loss as it had passed on any overcharge to its customers in the form of higher prices. It further argued that Sainsbury's was not entitled to recover damages if it had mitigated any overcharge by cutting costs.

Although it has been widely accepted that the passing-on 'defence' exists in English law (and a number of cases have proceeded on this basis), this had not previously been explicitly accepted, nor had the scope of the defence been delineated in a final judgement. This has now been resolved, with the CAT confirming that pass-on needs to be taken into account. As the CAT notes, pass-on is in reality not a defence at all: it forms part of the principles of assessing compensatory damages. The CAT stated that this reflects the need to ensure that: (i) a claimant is sufficiently compensated, and not over-compensated, by a defendant; and (ii) the defendant is not forced to pay more than compensatory damages, when considering all of the potential claimants (i.e. including indirect purchasers who argue that an overcharge has been passed on to them).

The CAT provided important clarification on the scope of the 'defence' as follows:

- The pass-on defence is only concerned with identifiable increases in prices by a firm to its customers.
- The increase in price must be causally connected with the overcharge, and demonstrably so.
- The defence can only succeed where, on the balance of probabilities, the defendant has shown that there exists another class of - downstream - claimants to whom the overcharge has been passed on.

On the facts, having considered in detail the manner in which Sainsbury's dealt with costs and pricing, the CAT found that exactly how Sainsbury's dealt with the cost of the UK MIF (which was one of many cost items it needed to take into account) was "unknowable". The Cat found, that at a high level, Sainsbury's would have passed on to consumers what it could through higher prices, made whatever cost-savings it could, and adjusted its spending so as to return the expected profit, but it is impossible to say exactly what proportion was dealt with in which way.

The CAT held that, although a substantial amount of the UK MIF would therefore have been passed on (consistent with economic theory), this was not sufficient legally to defeat or reduce Sainsbury's damages. MasterCard had not been able to establish any identifiable increase in retail prices, still less one that is causally connected with the UK MIF. Nor had MasterCard identified any purchaser or class of purchasers of Sainsbury's to whom the overcharge has been passed on who would be in a position to claim damages.

In relation to mitigation, the CAT held that costs savings achieved by Sainsbury's cannot be regarded as a 'benefit' to be set off against the overcharge, as it would have sought to make cost savings year on year regardless of the level of the MIF and whether there was any overcharge.

The CAT therefore concluded that Sainsbury's was entitled to recover £68,582,245 in damages (a figure which was lower than that claimed by Sainsbury's, due to the CAT's conclusion on the counter-factual and the level of overcharge), plus interest.

INTEREST

Sainsbury's sought to recover compound interest under the rule in *Sempra Metals*.

The CAT found that, because the UK MIF was a cost common to Sainsbury's and its supermarket rivals, a substantial amount of the UK MIF - 50% - would have been passed on (albeit not in a manner sufficient for the passing-on 'defence' to succeed, as discussed above). In relation to this 50% no claim for compound interest could be made.

In relation to the other 50%, the CAT found that, if the overcharge had not been made, Sainsbury's would have: (i) had higher cash balances and received interest on such (20%); and (ii) required less borrowing and therefore not incurred the cost of borrowing (30%). The CAT therefore awarded compound interest in respect of 50% of the overcharge. The CAT ordered interest to be paid at the rate that Sainsbury's would have earned on its cash balances for the 20%, and at the rate that Sainsbury's would have saved by taking out less new debt for the 30%. The parties must now calculate the interest payable, which is likely to be very significant.

This is a significant ruling, as whilst compound interest is routinely claimed in competition claims, the extent to which courts would be willing to award this has been unclear. In the two previous cases in which the CAT had awarded damages (2Travel and Albion Water, both of which related to abuse of dominance) it had ordered simple interest only.

3. IMPACT OF JUDGEMENT

This judgement is highly significant, as it is the first time the CAT has issued a damages award in an Article 101 TFEU case. Although obviously specific to the facts (which are relatively unusual compared to the cartel damages claims commonly brought), it demonstrates the approach the CAT will take to assessing damages. This is particularly useful given the vast majority of competition damages claims settle before trial. Most importantly, the judgment confirms the existence of the passing-on 'defence' in English law (prior to planned legislation on this point to implement the EU Damages Directive), and what defendants will be required to prove in order to successfully raise the defence. The relatively strict approach taken by the CAT - absent any appeal - is likely to have an impact on future competition damages claims.

The parties to the other on-going interchange litigation will be considering the judgment closely to determine the impact of the CAT's findings on their cases. It remains to be seen what effect the CAT's conclusions on passin-on may have on the proposed consumer class action against MasterCard, which would depend on the overcharge (or a proportion thereof) having been passed on to consumers in the form of higher prices.

More generally, this case emphasises the UK's current very active private enforcement landscape, and that some steps have been made towards the Government's aim of establishing the CAT as the primary venue to litigation in the UK.

¹The remainder of this ebuletin refers to Article 101 TFEU only for ease of reference.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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