No. 02-6074(L)

Consolidated with Nos. 02-6076, 02-6078

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

FINAL VERSION

UNITED STATES OF AMERICA,
Plaintiff-Appellee,
v.

VISA U.S.A., INC., MASTERCARD INTERNATIONAL, INC., and
VISA INTERNATIONAL, INC.
Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR THE UNITED STATES

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STATEMENT OF ISSUES

1. Whether Visa's Bylaw 2.10(e) and MasterCard's Competitive Programs Policy (CPP), which prohibit member/owner banks from issuing general purpose cards on the only networks not controlled by banks, constitute unreasonable restraints of trade in violation of Section 1 of the Sherman Act, 15 U.S.C. § 1.

2. Whether the district court abused its discretion by ordering repeal of Bylaw 2.10(e) and the CPP, and a transition period during which member banks entering into issuing arrangements with American Express or Discover may terminate existing agreements with Visa or MasterCard committing them to maintain a certain percentage of their general purpose card business in the United States on that association's network.

3. Whether the district court abused its discretion in including Visa International in the decree.

COURSE OF PROCEEDINGS

1. On October 7, 1998, the United States sued Visa USA Inc. (VUSA), Visa International Corp. (VINT) (collectively, Visa), and MasterCard International Inc. (MC), alleging two violations of Section 1 of the Sherman Act, 15 U.S.C. § 1. A61. Visa and MasterCard are joint ventures (or "associations") created, owned, governed, and operated by their thousands of member banks. *United States v. Visa U.S.A. Inc.*, 163 F. Supp. 2d 322, 327 (S.D.N.Y. 2001) ("Op.") (SPA158, 163).

Visa and MasterCard's business is to provide network services to their member/owners which, in turn, issue credit and charge cards[1] to consumers and provide card acceptance services to merchants.

Count I of the Complaint challenged the governance practices of Visa and MasterCard, under which member banks with representatives on the Board of Directors and/or governing committees of each association are permitted to issue substantial numbers of cards on the other association's network. The government alleged that because of this "dual governance," Op. 327-28 (SPA163-64), the conflicted directors "have a reduced incentive to invest in or implement competitive initiatives that would affect their other card product, and as a result the Visa and MasterCard associations have failed to compete with each other by constraining innovation and investments in new and improved products." Op. 328 (SPA164).

Count II focused on Visa's Bylaw 2.10(e) and MasterCard's Competitive Programs Policy (CPP) (together, the "exclusionary rules," Op. 329 (SPA165)).

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[1]"A charge card requires the cardholder to pay his or her full balance upon receipt of a billing statement from the issuer of the card. . . . A credit card permits cardholders to pay only a portion of the balance due on the account after receipt of a billing statement," Op. 331 (SPA167), and incur interest charges on the balance. Debit cards, which "promptly access money directly from a cardholder's checking or deposit account," are not a type of credit or charge card. *Id.*

These rules permit member banks to issue credit and charge cards on both the Visa and MasterCard networks,[2] but prohibit them from issuing cards on the only two other major general purpose credit card networks, which are not controlled by banks: American Express (Amex) and Discover. Op. 329 (SPA165). Plaintiff contended that the exclusionary rules restrained competition among credit card networks and credit card issuers, and thereby harmed consumers.

2. The district court held a 34-day bench trial, Op. 330 (SPA166), during which it heard live testimony from 37 witnesses, and admitted depositions of 122 other witnesses and 1418 exhibits. Following the close of evidence, the parties submitted 741 pages of proposed findings of fact and conclusions of law; and another 241 pages responding to each others' proposed findings and conclusions. A920, 1151, 32-33, 36.

The district court issued 157 pages of findings of fact and conclusions of law, with detailed citations to the record—especially to defendants' documents and the testimony of their current and former executives. SPA158. The court analyzed the government's claims under the rule of reason, beginning by defining

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[2]The exclusionary rules also permit member banks to issue cards on the Diners Club and JCB networks. Op. 379-80, 381 (SPA215-16, 217).

two product markets: (1) general purpose cards,[3] and (2) general purpose card network services. Op. 335 (SPA171). The court found that defendants have market power in the network services market—the market in which the associations operate. Op. 340 (SPA176). Although the court found that the government had not sustained its burden with respect to Count I, it held that the exclusionary rules challenged in Count II "weaken[ed] competition and harm[ed] consumers" and that the defendants had failed to establish any procompetitive justification. Op. 329-30, 399-400 (SPA165-66, 235-36).

3. The court's opinion addressed relief and proposed a decree, but invited further comment on the remedy. Op. 407-11 (SPA243-47). The parties and amici subsequently provided the court 42 pages of comments on the final judgment, another 72 pages responding to each others' comments, followed by sur-reply comments by Visa USA. A1682-1766. On November 29, 2001, the district court issued a further opinion on remedy and modified its final judgment (FJ). 183 F. Supp. 2d 613 (S.D.N.Y. 2001) ("Remedy Op.") (SPA260). The Final Judgment orders Visa USA and MasterCard to repeal their exclusionary rules; enjoins all three defendants from "enacting, maintaining, or enforcing any by-law, rule,

[3]"General purpose cards" include credit and charge cards, but exclude in-store credit cards (e.g., Sears cards) and debit cards. Op. 331 (SPA167).

policy or practice that prohibits its issuers from issuing general purpose or debit cards in the United States on any other general purpose card network"; and, for a period ending two years after exhaustion of appeals, permits member banks that enter into agreements to issue American Express or Discover cards to terminate any existing "dedication" agreements[4] with Visa or MasterCard. FJ § III (SPA268-69).

4. Visa USA and MasterCard jointly moved to modify the Final Judgment under Rule 59(e), FED. R. CIV. P., alleging denial of due process. A46. They also moved separately for the district court to stay its judgment pending appeal. On February 19, 2002, the district court denied as "wholly without merit" defendants' motion to modify the final judgment, granted their requests for a stay, and entered the Final Judgment. A51, 1918, 1919-20. These appeals followed.[5]

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[4]Some member banks have signed agreements with Visa or MasterCard committing them to maintain a certain percentage of their general purpose card volume, new card issuance, or total number of cards in force in the United States on that association's network. In return for such "dedication," the member banks receive discounts on network fees and, often, large cash payments from the association. Op. 368-69 (SPA204-05).

[5]Although the United States does not agree with the district court's decision regarding Count I, it has not appealed from that decision.

STATEMENT OF FACTS

A. Overview Of The Payment Card Industry

"General purpose" cards are the most popular form of payment cards. Unlike "proprietary" cards (e.g., Macy's cards), which are accepted at only one merchant, general purpose cards are accepted at "numerous, unrelated merchants." Op. 331 (SPA167). Appellants control the two largest of the four major network brands of general purpose cards:[6] Visa (47% of U.S. general purpose card transaction dollar volume in 1999), MasterCard (26%), American Express (20%), and Discover (6%). Op. 341 (SPA177).[7] This appeal is about the rules adopted by the members of Visa and MasterCard that preclude member banks from also issuing American Express or Discover cards, thereby limiting competition among providers of network services.

General purpose card networks "provide the infrastructure and mechanisms through which general purpose card transactions are conducted, including the

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[6]Diners Club is an additional brand of general purpose card. Citicorp, the largest individual issuer of Visa/MasterCard cards, also owns the Diners Club network and issues all Diners cards in the United States. Op. 379 n.19 (SPA215).

[7]When measured by several other appropriate criteria, Visa's and MasterCard's shares are even larger. *See* M.Katz Dir. ¶¶ 165-71 & Fig. 20 (T3092-96, 3260-61). (At trial, each testifying expert presented written direct testimony. This brief cites to such testimony in the form "[Expert] Dir. ¶ __." Each expert was subject to live cross-examination.)

authorization, settlement, and clearance of transactions." Op. 338 (SPA174). Networks play "a major role in determining the overall quality of the brand, encompassing system-level investments in brand advertising, the creation of new products and features and cost-saving increases in the efficiency of the electronic backbone of the networks." Op. 333 (SPA169).

"Issuers" evaluate card applications and issue cards to consumers, set terms for those cards (e.g., annual fees, interest rates charged for carrying a balance), and own the consumer's account. Although networks provide product platforms (e.g., parameters for platinum cards), issuers add features that appeal to their customers. "Acquirers" sign up merchants to accept one or more brands of cards.

In a typical general purpose card transaction, when a customer presents her card to a merchant as payment for goods or services, the merchant

> electronically presents the card transaction data to an "acquirer" . . . for verification and processing. The acquirer presents the transaction data to the association (*e.g.*, Visa or MasterCard) which in turn contacts the issuer (*e.g.* MBNA) to check the cardholder's credit line. The issuer then indicates to the association that it authorizes or denies the transaction; the association relays the message to the merchant's acquirer, who then relays the message to the credit card terminal at the merchant's point of sale.

Op. 332 n.4 (SPA168). After verification, the acquirer pays the merchant the amount of the charge, less the acquirer's processing fee—known as the "merchant discount"—usually expressed as a percentage of the value of the transaction.

Thus, the higher the merchant discount, the less the merchant actually receives in payment. The average merchant discount in a Visa/MasterCard transaction is approximately 2%. Op. 332 (SPA168).

To illustrate, when a customer uses her Visa card to purchase $100 worth of clothing from a merchant, the merchant ends up with about $98 in cash from the acquirer. For the merchant, the transaction is now complete.

After paying the merchant, the acquirer turns to the issuer of the card for reimbursement. The issuer pays the acquirer the full value of the transaction (in this example, $100), less the "interchange fee." Assuming an interchange fee of 1.4% (which is the average interchange fee in a Visa/MasterCard transaction, Op. 332 (SPA168)), the issuer pays the acquirer $98.60, leaving the acquirer with net revenue of $0.60 on the transaction. The issuer, which bears the risk of nonpayment, bills the cardholder for the full value of the transaction ($100). The cardholder then has a number of days to pay the statement in full without accruing finance charges; interest is charged on unpaid balances at the issuer's interest rate.

Visa and MasterCard are "structured as open, joint venture associations" with members that issue cards, acquire merchants, or both. Op. 332 (footnote omitted) (SPA168). At the time of trial, neither Visa nor MasterCard had stock or

stockholders.[8] Visa and MasterCard are "operated as not-for-profit associations and are supported primarily by service and transaction fees paid by their members." *Id.* Members agree to abide by each association's bylaws and operating regulations. *Id.*[9] Members also sit on the associations' boards and committees that make strategic business decisions, Op. 333 (SPA169), and they reap the financial rewards of the associations' marketplace success. Visa USA has approximately 14,000 members in the United States, including approximately 6,000 issuers. *Id.* MasterCard has approximately 20,000 global members. *Id.* Issuers are traditional banks, "monoline" banks,[10] or insurance companies or large retail corporations acting through banks, which are known collectively and generically as "member banks."

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[8]In February 2001, after the trial ended, MasterCard's board voted to convert from a cooperative association to a private, for-profit stock company. According to MasterCard's latest 10-Q quarterly report with the SEC (filed May 15, 2002), MasterCard Incorporated (designed to be the new stock-based holding company of MasterCard International Incorporated and Europay International S.A.) was incorporated on May 9, 2001 but has not yet commenced operations. *See* http://www.sec.gov/Archives/edgar/data/1141391/000095012302005127/0000950123-02-005127.txt at 1.

[9]*See* D-1586, §§ 2.03-2.04 (VUSA bylaws) (E535-49); D-3228, art. I, § 5 (MC bylaws) (E1168-70).

[10]A "monoline" bank "has no branches and specializes in banking by mail and the credit and charge card industry." Op. 328 n.1 (SPA164).

Originally, Visa and MasterCard had separate memberships. During the pendency of antitrust litigation over the exclusivity of its network, in 1976 Visa amended its rules to permit members to issue MasterCard cards, a practice termed "dual issuance."[11] Op. 345-46 (SPA181-82). MasterCard consistently favored dual issuance. *See* Op. 346 (SPA182). By 1986, "about two-thirds of the 100 largest bank credit card issuers had at least 25 percent of their cards on each system." Op. 347 (SPA183). As dual issuance became ubiquitous, the associations also came to exhibit "dual governance," with issuers on one network sitting on the Board of Directors or a decision-making committee of the other. Op. 345 (SPA181).

Count I of the Complaint alleged that dual governance was anticompetitive, but the district court held that the government had failed to prove the allegation. The government maintained that dual issuance was procompetitive, and MasterCard agreed. Op. 346 (SPA182); Defendants' Post-Trial Joint Proposed Findings Of Fact, at III-31 n.4 (Sept. 22, 2000) (MasterCard is "firmly of the view

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[11]The Department of Justice had reviewed a proposed Visa rule requiring total separation of the networks and declined to endorse separation of acquirers because of fears that such separation would retard the growth of the merchant acceptance network. *See* Op. 346 (SPA182).

that duality is procompetitive") (A1226). The district court found that dual issuance had been procompetitive. Op. 330 (SPA166).

American Express, Discover, and Diners Club "operate as 'closed loop,' vertically integrated systems. They promote their brands and operate their networks to process transactions and (unlike the associations) also issue cards and enlist merchants to accept those cards." Op. 333 (SPA169). Thus, American Express, Discover, and Diners Club compete as networks against Visa and MasterCard, and also compete as issuers against the thousands of Visa/MasterCard members. *Id.*

Visa and MasterCard set the interchange rate paid by acquirers to issuers. Op. 332 (SPA168). And although the acquirer sets the merchant discount, the association-set interchange fee is the dominant component of the merchant discount. In fact, some contracts between merchants and their acquirers provide for direct pass-through of interchange rates. M.Katz Dir. ¶ 61 (T3033). As the district court noted, neither "American Express nor Discover needs to set interchange fees because they are both the issuer and acquirer on all transactions and keep the full amount of the merchant discount fee." Op. 333 (SPA169).

In 1999, American Express's average merchant discount was approximately 2.73%, compared to Visa and MasterCard's rates of approximately 2%, and

Discover's rate of approximately 1.5%. *Id.* (citing Golub[12] (Amex) Tr. 2719:6-10 (T2283); D-0982 at AMEX0001260771 (E476); D-1683 at VUTE0001692 (E591); Nelms (Discover) Tr. 2981:2-7, 3007:22-3008:14 (T2539, 2565-66)). Because a higher merchant discount leaves less revenue for merchants, these figures mean that merchants retain more money when a customer pays with Discover than with Visa/MasterCard. Nonetheless, Discover is accepted at fewer than 90% of the locations that accept Visa/MasterCard. Op. 388-89 (SPA224) (citing Nelms (Discover) Tr. 2981:18-2982:10 (T2539-40)).

The explanation is that merchants are reluctant to accept a specific brand of card (with its associated set-up and ongoing administrative costs) unless they are confident that sufficient numbers of customers will want to use that card; on the other hand, consumers do not want to carry a specific brand of card unless they are confident that they can use that card at the merchants at which they plan to—or might eventually want to—shop. Op. 340, 342 (SPA176, 178). This "chicken-and-egg" problem has allowed Visa and MasterCard, whose dominant positions ensure that most merchants feel it necessary to accept them, to raise interchange fees repeatedly in recent years. *Id.* The associations and their member banks

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[12]A glossary of witnesses mentioned in this brief, along with their corporate affiliations at the time of their testimony, is attached for the Court's convenience as an addendum.

acknowledge that raising interchange rates increases issuer profits. *See* P-0825 at VU1422163 (E3389); *see also* P-0763 at VU0624084 (E3297); Heasley (VUSA) Dep. 86:9-87:18 (A688-89).

B. The Exclusionary Rules: Visa's Bylaw 2.10(e) And MasterCard's Competitive Programs Policy

1. Visa And MasterCard Adopt Their Exclusionary Rules To Thwart Competition From American Express And Discover

a. Visa USA Adopts Bylaw 2.10(e)

In 1991, Visa USA's Board, comprised of representatives from its member/owners, adopted Bylaw 2.10(e), which provides in relevant part that "[t]he membership of any Member shall automatically terminate in the event it, or its parent, subsidiary or affiliate, issues, directly or indirectly, Discover Cards or American Express Cards, or any other card deemed competitive by the Board of Directors." P-0647 at 0058362 (E2896). The Visa USA Board has never "deemed" MasterCard, Diners Club, or JCB[13] to be "competitive" with Visa,[14] even though (1) MasterCard is the second-largest network and Visa's executives

[13] JCB is a prominent card in Japan. Op. 331 n.3 (SPA167). In 1996, JCB granted to Household Bank—whose president was also Chairman of MasterCard—exclusive rights to issue JCB cards in the United States; ultimately, however, Household never issued any JCB cards. Op. 379 n.19 (SPA215).

[14] Op. 379-80 (SPA215-16) (citing B.Katz (VUSA/VINT) Tr. 3268:18-3269:8 (T2815-16); Pascarella (VUSA) Dep. 53:5-54:15 (A764-65)).

testified to intense competition between it and MasterCard,[15] and (2) "at the time By-law 2.10(e) was passed, the worldwide volume on the Diners Club and Discover networks were about equal." Op. 380 (SPA216). Visa USA enforces Bylaw 2.10(e) to preclude its member banks from issuing cards on the American Express or Discover networks. Tr. 80:15-19 (VUSA opening statement).

b. Visa International Considers An Equivalent To Bylaw 2.10(e)

Foreclosed from doing so in Visa's U.S. Region by Bylaw 2.10(e), American Express entered into "issuing arrangements" with a number of banks abroad. Op. 380 (SPA216) (citing P-0854 (E3403-06)). Visa International was concerned that American Express would use member banks to increase its merchant acceptance and card issuance, thereby becoming a more formidable competitor to Visa.[16] Bennett Katz, general counsel of both Visa USA and Visa

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[15]*See, e.g.*, Pascarella (VUSA) Tr. 5140:7-12 (Pascarella sought to "pound MasterCard into a rat hole") (T4747); Dahir (VUSA) Tr. 4517:20-4521:6 ("all bets were off" in Visa's efforts to win issuer co-branding decisions versus MasterCard) (T4261-65); Schall (VUSA) Tr. 5002:18-5004:18 (describing "fierce" competition with MasterCard for issuer co-branding and mail share decisions) (T4612-14).

[16]*See, e.g.*, P-0053 at 0731178 (suggesting a 2.10(e)-like by-law in response to competitive threats) (E1976); P-0705 at VU0259076 (merchant acceptance remains "central" to American Express strategy because "acceptance drives volume, revenue and income") (capitalization altered) (E3133); Jensen (VINT) Dep. 111:10-17 (A702); Tallman (VUSA/VINT) Dep. 265:6-24, 275:25-276:24 (A815, 819-20); Beindorff (VUSA) Dep. 154:2-25, 251:16-20 (A576-77, 578);

International, confirmed that it was “critical” for Visa International to defend its acceptance advantage against “all competitors.”[17]

In direct response to the perceived threat by American Express, in 1995 Visa International began considering a global bylaw patterned after Visa USA’s Bylaw 2.10(e).[18] Senior executives in Visa International recognized that any “competitive” rule should apply to *all* competitors, not merely American Express and Discover.[19] After the head of the European Commission Directorate for Competition (ECDC) publicly expressed doubts about the legality of the proposed exclusionary rule, the Visa International Board voted not to enact a global 2.10(e)-

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Hagadorn (VUSA) Dep. 248:7-251:4 (A680-82).

[17]B.Katz (VUSA/VINT) Tr. 3273:6-22 (T2820); *see also* P-0631 (E2890-91); P-0541 at VIF0481833 (Visa management concerned that American Express’s partnerships with Visa member banks “threaten to rapidly erode” Visa’s merchant acceptance advantage) (E2727); Jensen (VINT) Dep. 111:11-17 (A731); Beindorff (VUSA) Tr. 4399:9-12 (acceptance parity by American Express would cause 5% market share shift from Visa to American Express) (T4167) (discussing P-0705 at VU0259081 (E3138)); P-0666 at V052724 (Visa International management discussing “potential effect” of American Express partnerships “on member profit”) (capitalization altered) (E3003).

[18]*See* B.Katz (VUSA/VINT) Tr. 3267:16-3268:13 (T2814-15); P-0650 at V010064 (E2910); P-0021 at 0550984 (E1892); P-0542 at VIF0481872 (E2747).

[19]*See* B.Katz (VUSA/VINT) Tr. 3276:10-3277:3 (T2823-24); P-1167 at VISA002312 (Visa International management considering “[p]ros and cons of including JCB, Diners Club and Discover” (but not MasterCard) in a 2.10(e)-equivalent) (E3915).

equivalent.[20] Instead, the Visa International Board delegated authority to the Visa regional boards to decide whether to adopt a 2.10(e)-equivalent, and encouraged those regions to adopt such rules. Op. 380 (SPA216); B.Katz (VUSA/VINT) Tr. 3289:7-3292:17 (T2836-39); P-0661 at V030425-26 (E2986-87).

Following the Visa International Board's delegation to the regional boards, Visa's Latin American-Caribbean Region Board considered a 2.10(e)-equivalent, but ultimately declined to enact it after American Express filed complaints in numerous Latin American countries. Op. 380 (SPA216). Other regional boards also withdrew their proposed exclusionary rules. In the end, "the only region with a prohibition on member bank issuance of American Express and Discover cards was and remains the United States." *Id.*

c. MasterCard Adopts Its CPP

MasterCard's Competitive Programs Policy (CPP) provides in relevant part: "With the exception of participation by members in Visa, which is essentially owned by the same member entities, and several pre-existing programs to the extent individual members participate, most notably Diners Club and JCB, members of MasterCard may not participate either as issuers or acquirers in

[20] *See* B.Katz (VUSA/VINT) Tr. 3288:15-3289:6 (T2835-36); P-0661 at V030425-26 (reflecting consideration of ECDC comments) (E2986-87).

competitive general purpose card programs." P-0284 at MC58737 (E2429). Like Visa's exclusionary rule, MasterCard's CPP applies only to member banks in its United States Region. Op. 381 (SPA217).

"As of early 1996, MasterCard had no rules prohibiting its members from issuing American Express cards," Op. 380 (SPA216), although it was already considering how to react to American Express's increased efforts to form card-issuing arrangements with Visa and MasterCard member banks, both in the United States and abroad. Lockhart (MC) Tr. 1763:15-1764:21 (T1449-50); P-0276 (E2415-16). In May 1996, American Express CEO Harvey Golub delivered a speech "outlining why it would be profitable for banks to partner with American Express and specifically encouraging major MasterCard banks to consider the opportunity in light of the fact that MasterCard had no rule requiring them to give up their MasterCard portfolio if they did so." Op. 380 (SPA216) (citing D-0671 (E390-446)). Several MasterCard members accepted Golub's invitation and held discussions with American Express. Op. 386 (citing examples) (SPA222). By June 1996, MasterCard CEO Eugene Lockhart and U.S. Region president Alan Heuer "knew that four or five MasterCard members were considering issuing

American Express cards."[21] Lockhart testified that he "expected five to ten large MasterCard issuers around the world, including the United States, to issue American Express cards." Op. 381 (SPA217) (citing Lockhart (MC) Tr. 1836:18-24 (T1522); P-0296 at MC85659 (E2499)).

MasterCard was unsure how to respond to American Express's overture to member banks. Lockhart and others in senior management "thought that MasterCard could differentiate itself from Visa and gain share by *not* adopting a rule similar to Visa's 2.10(e). They believed this would encourage banks interested in issuing American Express cards to convert their Visa portfolios to MasterCard."[22] These senior managers eschewed Visa's "very dogmatic and uncompromising" position, Lockhart (MC) Tr. 1771:1-7 (T1457), believing instead that MasterCard should discourage partnership with American Express by responding competitively with better programs within MasterCard. *See* Lockhart Tr. 1771:8-1772:1, 1776:18-1777:7 (endorsing view that "over time you can't legislate markets, it just doesn't work. . . . You rule by creating better value")

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[21]Op. 380-81 (SPA216-17) (citing Lockhart (MC) Tr. 1811:20-1812:16 (T1497-98); Heuer (MC) CID Dep. 112:21-24, 130:19-131:16) ("from the outset I presumed that there would be MasterCard members that would want to, if they had the opportunity, to issue AmEx cards . . .") (A692, 695-96)).

[22]Op. 380 (SPA216) (citing P-0270 (E2408-12); Lockhart (MC) Tr. 1764:8-1765:4 (T1450-51); Hart (MC) Tr. 1459:18-1460:10 (T1173-74)).

(T1457-58, 1462-63); Child (VUSA) Dep. 44:25-45:10, 45:21-46:2 (A622). Lockhart wrote a memorandum outlining various potential competitive responses to American Express.[23] Other MasterCard senior managers, however, including current-CEO Robert Selander, simply wanted to "'make it as hard as possible to have Amex do anything anywhere in the world.'" Op. 380 (SPA216) (quoting Lockhart (MC) Tr. 1774:12-23 (T1460); P-0293 at MC85584 (E2470)).

In June 1996, the MasterCard U.S. and Global boards met in London to consider whether to prohibit member issuance of cards on rival networks. Lockhart told the Executive Committee of MasterCard's Global Board that a "firm prohibition against a competitor can't be legislated. Free market wins at the end of the day." Lockhart (MC) Tr. 1836:12-17 (T1522); P-0296 at MC85658 (E2498). Some board members who opposed the CPP believed that each member should be like a "supermarket being able to sell all branded products." P-0181 at CRW00193 (E2268); Lockhart (MC) Tr. 1827:11-1828:7 (T1513-14). Pete Hart,

[23] *See* P-0277 at MC6382-84 (E2417-21). The competitive responses included "stepping up" efforts to roll out a "Premium offering" to compete with American Express's Platinum card; matching American Express's travel-related features by allying with a national travel agency; and becoming more "aggressive" vis-à-vis American Express in selected interchange rate categories. *See id.*; Lockhart (MC) Tr. 1796:16-1799:19 (T1482-85); P-0274 at MC6300 (MasterCard must "replicate" the "value" benefits that American Express offered member banks) (E2414).

then-CEO of Advanta and previously president of MasterCard, believed that rejection of the CPP would increase competition between the Visa and MasterCard networks because MasterCard would permit its members more issuing options. Hart (Advanta) Tr. 1462:24-1463:15 (T1176-77). On June 28, 1996, MasterCard's U.S. Region Board enacted the CPP "over the objection of six board members, subject to a delegation of the authority to take that action by MasterCard's Global Board at the Global Board's meeting the following day." Op. 381 (SPA217) (citing P-0187 at CRW00539) (E2379)).

The next day, MasterCard's Global Board followed the approach Visa's International Board had taken (three weeks earlier) and "delegated to MasterCard's regional boards the authority to enact rules to prohibit MasterCard's members from issuing American Express cards." Op. 381 (SPA217) (citing P-0188 at CRW00544-45 (E2384-85)). In so doing, the Global board "considered the fact that the European Commission had expressed disfavor with Visa's proposed global by-law." *Id.* (citing Lockhart (MC) Tr. 1824:7-21 (T1510)). No other regional board adopted a rule, bylaw, or policy equivalent to the CPP. MasterCard's CPP applies only to American Express and Discover, not to Visa, Diners Club, or JCB—all of which are controlled by banks that are owner/members of MasterCard.

d. The Purpose Of The Exclusionary Rules

The district court found, based on the contemporaneous evidence, that in adopting its exclusionary rule, each association focused on blunting horizontal competition. Specifically, the court found that defendants adopted the exclusionary rules: (1) to ensure that no member bank would gain the "competitive advantage" of issuing American Express or Discover cards that other members could not issue (a practice labeled by appellants as "cherry picking"),[24] and (2) to weaken American Express and Discover as competitors to the bank-owned networks.[25] Op. 400-01 (SPA236-37).

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[24] *See* Beindorff (VUSA) Dep. 304:2-15 (A582); Allen (VUSA) Dep. 397:25-398:23 (A567); Dahir (VUSA) Dep. 252:23-253:19 (American Express-issuing banks would obtain "unfair advantage" over other members) (A637-38); Lockhart (MC) Tr. 1819:21-1820:5 (T1505-06); Cawley (MBNA) Dep. 72:7-74:12 ("competitive advantage") (A614-16); Zebeck (Metris) Dep. 164:23-165:4 ("tangible benefits" of issuing multiple brands would confer competitive advantage) (A841-42); P-0182 at CRW00459 (would have to be available to all members "on substantially equal terms, so that some of our members are not disadvantaged") (E2361); Fairbank (Capital One) Dep. 113:9-114:7 (A664-65); P-0266 at MBNA0009934 (allowing members to issue American Express "can only strengthen MBNA's competitors") (E2400).

[25] *See* Brooks (VUSA) Dep. 23:17-24:3, 24:12-22 (Visa feared that bank issuance of American Express would strengthen American Express as a competitor) (A605-06); P-0067 at 1123830 ("More Amex Cards Would Weaken Visa Brand to Detriment Of Member Profitability") (E2032); P-0292 at MC85541 ("be ruthless to Amex . . . handle the way Microsoft would, be a strong competitor") (E2437); P-0293 at MC85584 ("Must make it as hard as possible to have Amex do anything, anywhere in the world") (E2470); Lockhart (MC) Tr. 1782:16-1784:7,

2. Anticompetitive Effects Of The Exclusionary Rules

Visa's Bylaw 2.10(e) and MasterCard's CPP have been effective. "The result, as intended, has been that no bank has broken rank; rather than lose access to the Visa and MasterCard networks (as well as their ATM networks, Cirrus and Plus), no bank in the continental United States has agreed to issue American Express" or Discover cards. Op. 400 (SPA236).[26] As the district court found, the effect has been to

> weaken competition and harm consumers by: (1) limiting output of American Express and Discover cards in the United States; (2) restricting the competitive strength of American Express and Discover by restraining their merchant acceptance levels and their ability to develop and distribute new features such as smart cards; (3) effectively foreclosing American Express or Discover from competing to issue off-line debit cards, which soon will be linked to credit card functions on a single smart card, and (4) depriving consumers of the ability to obtain credit cards that combine the unique features of their preferred bank with any of four network brands, each of which has different qualities, characteristics, features, and

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1786:25-1787:25, 1874:19-1876:8 (opportunity to issue American Express products would result in a loss of volume and share from MasterCard to American Express) (T1468-70, 1472-73, 1560-62); P-0424 (predicting market share loss for Visa and MasterCard if members able to offer American Express or Discover cards) (E2581-82); Child (MC) Dep. 33:4-9 (increase in American Express merchant acceptance would harm MasterCard) (A621).

[26] *See* P-0777 at VU064425 (Visa analysis that Citibank's global ATM access "would fall well short" of Visa's if Citibank had to forfeit Cirrus/Plus) (E3356); Kesler (Banco Popular) Tr. 159:17-160:9 (Banco Popular feared losing Cirrus/Plus membership if it issued American Express cards in mainland United States) (T13-14).

> reputations. At the same time, the direct purchasers of network services (the issuers) restrict competition among themselves by ensuring that so long as all of them cannot issue American Express or Discover cards, none of them will gain the competitive advantage of doing so.

Op. 329-30 (SPA165-66). Additionally, the court found that absent the exclusionary rules, total card output would increase and that Visa and MasterCard "would respond to greater network competition from American Express and Discover by increasing their own competitive intensity." Op. 379, 380, 396 (capitalization altered) (SPA215, 216, 232). Finally, the court found that defendants "offered no persuasive procompetitive justification" that might outweigh these "adverse effect[s] on both the issuing and the network market." Op. 406, 379 (SPA242, 215). *See* pp. 72-99 below.

SUMMARY OF ARGUMENT

Visa and MasterCard fundamentally misconceive the nature of this case and this Court's role on appeal. This case is not about a vertical restriction on distribution, nor is it about the joint venture structure of the defendant associations. Rather, it is about horizontal agreements—"of, by and for" the banks that own and control the two dominant providers of general purpose card network services—not to issue cards on competing networks that banks do not control.

The district court conducted a lengthy bench trial and issued a 157-page opinion exhaustively reviewing the evidence. Applying the "rule of reason" according to well-established precedent, the court found that the challenged exclusionary rules restrain competition among providers of general purpose card network services and among the issuing banks. It further found that these restraints significantly harm consumers by reducing the number, variety, and availability of cards and their level of merchant acceptance, and harm merchants by limiting competition to provide acceptance services. The court considered at length appellants' proffered justifications, but found them unsupported by the record. The district court painstakingly supported its findings with detailed citations to the voluminous record, particularly to defendants' contemporaneous documents and the testimony of their current and former board members and executives.

Appellants largely ignore the district court's core findings of fact, basing their arguments instead on a sanitized recharacterization of their actions based on their own proposed—but rejected—findings. But this Court conducts its appellate review based on the district court's findings, which "shall not be set aside unless clearly erroneous." FED. R. CIV. P. 52(a); *see Anderson v. City of Bessemer City*, 470 U.S. 564, 573-74 (1985). Appellants do not make a serious effort to meet that

standard with respect to the controlling findings as to their market power, the horizontal nature and anticompetitive purpose of the agreements, the significant anticompetitive effects, and the lack of record support for the proffered justifications; nor could they in light of the district court's careful review of the evidence.

1. Visa and MasterCard jointly and separately wield market power in the general purpose card network services market. Their market power is demonstrated by the direct evidence of their ability to exclude the non-bank-controlled networks, American Express and Discover, from dealing with bank issuers responsible for 73-85% of general purpose cards issued, and of their power over merchants. Their large combined share in a market with indisputably enormous entry barriers also provides indirect evidence of their market power. Appellants' primary response is to urge the Court to ignore the network services market and focus exclusively on the issuer market, despite the district court's findings that the purpose and effect of the challenged conduct was to limit competition from networks not controlled by banks. Their theory is tantamount to a suggestion that the antitrust laws are not concerned with input markets—a suggestion without basis in law or economics.

2. The challenged exclusionary rules are horizontal "restrictions of, by and for the member banks." Op. 400 (SPA236). The contemporaneous evidence demonstrates that the rules were enacted for two simple reasons: (a) to ensure that no member/issuer gains a "competitive advantage" over other members by offering consumers cards with features available from American Express or Discover, and (b) to weaken the only two networks not owned by the member banks. Op. 400-01 (SPA236-37).

Appellants' efforts to recharacterize their rules as the factual or legal equivalent of vertical, exclusive distribution arrangements entered into by a single entity—presumptively lawful unless they unduly foreclose the market—can be summarily rejected. There is no basis for ignoring the horizontal character of the conduct; as courts have long recognized, agreements among competitors present inherent dangers that single-firm conduct does not. And banks are not mere "distributors" of network services. Banks "co-manufacture" general purpose cards, determining many features of the cards they offer and providing critical services and access to customers that are essential to the ability of networks to compete effectively. Working with networks, issuing banks translate their specialized marketing skills into specialized and targeted products for consumers. In any event, the district court found that the exclusionary rules effectively deny

American Express and Discover access to the issuer relationships and other bank capabilities that the court found critical to effective competition.

3. The exclusionary rules significantly impair competition in the network and issuer markets. As agreements among competing issuers not to deal with networks they do not control, the rules are facially anticompetitive because they "prevent American Express and Discover from offering network services to the consumers of those services." Op. 379 (SPA215). There can be no doubt that American Express and Discover seek to partner with banks, and, but for the exclusionary rules, some banks would agree to partner with them. The challenged rules protect the member/issuers from competition from other member banks choosing to enter into such relationships, and they protect the bank-controlled networks from competition. The law is clear that horizontal competitors may not collectively dictate the contours of competition. *See, e.g.*, *FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447, 459 (1986).

The district court, however, did not end the analysis there; rather it provided a detailed explanation of specific anticompetitive effects, including:
(1) weakening network competition by effectively forcing American Express and Discover to remain single-issuer networks by denying them access to the "special skills, expertise, and relationships with consumers," Op. 389 (SPA225), that

multiple, diverse bank issuers would provide, and limiting prospects for innovation, including the development of next-generation "smart cards"; (2) weakening merchant acceptance by reducing the number of cards in use on particular networks, thereby adversely affecting not only the acceptance levels for those cards (which directly affects their consumer value), but also limiting network competition to provide acceptance services; (3) limiting the ability of issuing banks to match their unique brands, capabilities, and services with the best network services for particular customers; and (4) reducing the total number of general purpose cards outstanding. The district court rightly concluded that these effects stemmed not only from the direct limits on American Express and Discover, but also from the resulting blunting of Visa's and MasterCard's incentives to engage in vigorous competition.

Appellants assert that their networks offer everything consumers need and that repeal of the exclusionary rules will benefit only American Express, not consumers. But it is for an unfettered market, not the member banks' collective agreement, to determine what consumers want, and what competitors provide. And although, as the district court recognized, American Express and Discover may benefit from the exclusionary rules' repeal, the real winners will be American consumers. In a market with only four competitors and high entry barriers,

competition and consumers benefit when all competitors are given the opportunity to compete.

4. Once the United States proved market power and anticompetitive effects, the burden shifted to defendants to come forward with persuasive evidence of procompetitive benefits that could overcome such anticompetitive effects. Defendants offered *theories* of procompetitive justifications, but the district court soundly rejected those claims on the facts.

Appellants insist that the exclusionary rules are "ancillary restraints" because they promote "loyalty" and "cohesion" among the member banks. The district court acknowledged that restraints promoting loyalty or cohesion among joint venture participants may be procompetitive if they enable the venture to compete more vigorously, but it found that defendants had failed to demonstrate that these rules were enacted for, or accomplished, that purpose. Indeed, the associations' professed concerns about loyalty ring hollow in light of the long history of members' divided loyalties—each association exempts the other (its largest competitor) and certain proprietary networks (controlled by banks) from its exclusionary rule. Appellants offer no sound basis to believe that allowing individual members to choose to issue American Express or Discover would be destructive of the association's ability to compete. And the district court correctly

rejected as “belied by the uncontradicted record evidence,” Op. 402 (SPA238), Visa’s expert’s suggestion that the associations were justified in exempting each other because the associations’ open structures created a “self-enforcing mechanism” that prevented “opportunistic” behavior between the associations, and that would be ineffective in member interactions with American Express and Discover.

Nor did defendants present evidence demonstrating that bank issuance of American Express or Discover cards would “destabilize” the associations or undermine their “cohesion.” The court found “overwhelming” evidence, Op. 403 (SPA239), that the associations currently treat different members disparately—including conferring on select members competitive advantages over sister members—without loss of cohesion. Moreover, American Express’s issuing partnerships with banks in Puerto Rico and abroad—where the exclusionary rules do not apply—has caused no disruption to either association, nor has American Express’s long history of dealings with U.S. banks on matters other than card issuance.

5. The relief ordered is sound. That a proper remedy should order repeal of the offending rules would seem beyond cavil, despite Visa’s claim that the court erred in doing so. Additionally, the district court rightly concluded that the dedication agreements negotiated between the associations and various member

banks while the challenged rules were in effect—which effectively lock a large majority of card issuing volume into the Visa or MasterCard networks—had to be terminable at the option of the issuer if the remedy was to have any meaning. Absent the possibility of rescinding those agreements, American Express and Discover would be left to knocking on doors that were already preemptively closed. Thus, permitting a short transition period during which member banks could terminate their dedication agreements if—but only if—they reached an issuing agreement with American Express or Discover, was not only well within the district court's wide discretion to fashion effective relief, but essential to "effectively pry open to competition a market that has been closed by defendants' illegal restraints." *International Salt Co. v. United States*, 332 U.S. 392, 401 (1947).

6. Finally, the district court properly included Visa International in its final judgment because Visa International has the ultimate authority to insist upon or prevent Visa USA's exclusionary rule. The court's relief would be ineffective if Visa International were free to enact an exclusionary rule that Visa USA is enjoined from enacting. Moreover, when, as here, the district court found that Visa International would have enacted its own exclusionary rule but for the threat of international legal challenges, and that Visa International passed a resolution

assuring Visa USA of its continued—and necessary—support for such a rule, the district court was fully justified in enjoining Visa International.

ARGUMENT

STANDARD OF REVIEW

"Findings of fact, whether based on oral or documentary evidence, shall not be set aside unless clearly erroneous . . . ." FED. R. CIV. P. 52(a). The clear-error standard is rigorous: "If the district court's account of the evidence is plausible in light of the record viewed in its entirety, the court of appeals may not reverse it even though convinced that had it been sitting as the trier of fact, it would have weighed the evidence differently." *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-74 (1985). Indeed, "[w]here there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous." *Id.* at 574. This standard applies to the inferences drawn from findings of fact as well as to the findings themselves. *Cifra v. GE Co.*, 252 F.3d 205, 213 (2d Cir. 2001). Issues of law are, of course, reviewed de novo. *Anobile v. Pelligrino*, 284 F.3d 104, 113 (2d Cir. 2002).

Appellants suggest (VUSA 21-22; MC 21) that the standard of review is less demanding here because many of the district court's findings did not involve credibility determinations. That simply is not the law. The clear error standard

applies to *all* findings of fact, "whether based on oral *or* documentary evidence." FED. R. CIV. P. 52(a) (emphasis added);[27] *Travellers Int'l, A.G. v. TWA, Inc.*, 41 F.3d 1570, 1574 (2d Cir. 1994). Although findings based on credibility determinations "can virtually never be clear error," *Anderson*, 470 U.S. at 575,[28] the rule "does not make exceptions or purport to exclude certain categories of factual findings from the obligation of a court of appeals to accept a district court's findings unless clearly erroneous." *Pullman-Standard v. Swint*, 456 U.S. 273, 287 (1982).

I. VISA AND MASTERCARD, BOTH JOINTLY AND SEPARATELY, HAVE MARKET POWER IN THE NETWORK SERVICES MARKET

In determining that the exclusionary rules' "anticompetitive effects outweigh [their] procompetitive effects," Op. 344 (SPA180), and hence violate Section 1 of the Sherman Act, the district court applied a "full-fledged rule of reason analysis," considering "all of the circumstances of [the] case." Op. 343 (quoting *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36, 49 (1977))

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[27]Indeed, the Supreme Court amended Rule 52(a) in 1985 to make expressly clear that findings based on documentary evidence also are reviewed only for clear error. *See* FED. R. CIV. P. 52(a) advisory committee's note (1985 Amendment).

[28]*See also NLRB v. Dinion Coil Co.*, 201 F.2d 484, 487 (2d Cir. 1952) (credibility determinations are "ordinarily unreviewable").

(SPA179). In this analysis, courts first consider a defendant's market power. *See, e.g.*, *Chicago Prof'l Sports Ltd. P'ship v. NBA*, 95 F.3d 593, 600 (7th Cir. 1996); *Double D Spotting Serv., Inc. v. Supervalu, Inc.*, 136 F.3d 554, 558 (8th Cir. 1998). The district court found that the defendants, jointly and separately, possessed market power in a relevant market consisting of general purpose card network services.

A. The Relevant Markets

The definition of the relevant market is a factual inquiry reversible only for clear error. *International Boxing Club of N.Y., Inc. v. United States*, 358 U.S. 242, 251 (1959); *Todd v. Exxon Corp.*, 275 F.3d 191, 199 (2d Cir. 2001) ("market definition is a deeply fact-intensive inquiry"); *Consolidated Gold Fields PLC v. Minorco, S.A.*, 871 F.2d 252, 261 (2d Cir. 1989).

The district court properly defined markets "composed of products that have reasonable interchangeability for the purposes for which they are produced—price, use, and qualities considered." *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 404 (1956) (cited by Op. 335 (SPA171)). It found two relevant product markets: "the general purpose card network services market and the

general purpose card market."[29] Op. 335 (SPA171). The record fully supports the district court's findings, which were based on the testimony of the economic experts for the government and for the defendants, current and former officers of the associations, and industry participants, as well as on defendants' own documents. Op. 335-39 (SPA171-75).

"General purpose cards" are credit and charge cards "accepted at numerous, unrelated merchants." Op. 331 (SPA167). General purpose cards are issued to U.S. consumers by Visa's and MasterCard's thousands of member banks, and by American Express, Discover, and Citibank (as sole issuer of Diners Club cards), and are accepted by millions of merchants as payment for goods and services.

"General purpose card networks provide the infrastructure and mechanisms through which general purpose card transactions are conducted, including the authorization, settlement, and clearance of transactions. Merchant acceptance of a card brand is also defined and controlled at the system level and the merchant discount rate is established, directly or indirectly, by the networks. These basic or core functions are indispensably done at the network level." Op. 338 (SPA174) (citations omitted). Networks play "a major role in determining the overall quality

[29]Appellants do not challenge the district court's finding that the United States is the relevant geographic market. *See* Op. 339-40 (SPA175-76).

of the brand, encompassing system-level investments in brand advertising, the creation of new products and features and cost-saving increases in the efficiency of the electronic backbone of the networks." Op. 333 (SPA169). Visa and MasterCard provide network services, and American Express and Discover are the only other significant competitors providing network services for general purpose cards. Op. 338 (SPA174).

The relationship between issuing banks and their networks is not that of distributor and manufacturer. Op. 395 (SPA231). "A card issuer, instead, 'actually determines the main characteristics of the card which it puts on the market.'" *Id.* (quoting B.Katz (VUSA/VINT) Tr. 3137:13-3138:4 (T2684-85) (discussing P-0727 at ¶ 28 (E3159-60))). Nor do the networks merely sell services the banks use to produce general purpose cards, because the networks are mainly responsible for creating and promoting the brands and new products. Rather, the banks and networks combine to produce general purpose cards jointly. The exclusionary rules deny American Express and Discover access to the "special skills, expertise and relationships with consumers," Op. 389 (SPA225), banks bring to this enterprise.

1. General Purpose Cards Constitute A Relevant Product Market

In determining the relevant markets, the district court employed the hypothetical monopolist, price-sensitivity test endorsed by this Court and others. The "inquiry is whether a 'hypothetical cartel' would be 'substantially constrain[ed]' from increasing prices by the ability of customers to switch to other producers." *Todd*, 275 F.3d at 202 (quoting *AD/SAT v. Associated Press*, 181 F.3d 216, 228 (2d Cir. 1999) (per curiam)).[30] The district court correctly articulated this legal standard, Op. 335 (SPA171), and expressly adopted the analysis of plaintiff's expert economist utilizing this standard. Op. 335-36 (SPA171-72); *see* M.Katz Dir. ¶¶ 128-31 (T3133-36). Professor Katz's analysis indicated that a hypothetical monopolist over general purpose cards would find a 5% price increase profitable unless that price increase would reduce general purpose card charge volume by more than 16%. Op. 336 (SPA172); M.Katz Dir. ¶¶ 130-31 (T3072-73). Although a price increase for general purpose cards likely would cause some

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[30]*See also Coastal Fuels of P.R., Inc. v. Caribbean Petroleum Corp.*, 79 F.3d 182, 198 (1st Cir. 1996) (the "touchstone of market definition is whether a hypothetical monopolist could raise prices"); *Rebel Oil Co. v. Atlantic Richfield Co.*, 51 F.3d 1421, 1434 (9th Cir. 1995) (adopting hypothetical monopolist test); 2A PHILLIP E. AREEDA ET AL., ANTITRUST LAW ¶¶ 530 at 181, 533 at 200, 536 at 229-31, 537-38 (2d ed. 2002); U.S. Dep't of Justice & FTC, *Horizontal Merger Guidelines* §§ 1.0, 1.11 (1992), *reprinted in* 4 TRADE REG. REP. (CCH) ¶ 13,104.

substitution to other forms of payment, the court found it "highly unlikely that there would be enough cardholder switching away from credit and charge cards to make any such price increase unprofitable for a hypothetical monopolist of general purpose card products." Op. 336 (SPA172).

MasterCard argues that the district court's focus on switching in response to price changes is inappropriate because there is no meaningful price for general purpose cards. MC 67-70. But, for the large portion of consumers carrying a credit balance, the price of using general purpose cards is relatively straightforward: it is the interest they are charged, which the government's expert calculated to average 1.23% of the purchase price of goods.[31] M.Katz Dir. ¶ 120 (T3066).

MasterCard also argues the district court was wrong to focus on switching in response to price changes because innovation, rather than changes in price, has historically caused increased usage of general purpose cards relative to other

[31]For a consumer who pays a negative price for the use of general purpose cards (due to rebates and greater convenience of using cards), it is not difficult to consider financial terms that are 5% worse from the consumer's viewpoint. If, for example, the price was reckoned to be –1% because the consumer got a 1% rebate, the rebate could be reduced to 0.95% to reflect a 5% price increase.

forms of payment. MC 63-65.[32] Consumers have increased their usage of general purpose cards over time in response to changes in factors other than price. It does not follow, however, that other forms of payment that consumers would formerly have used are in the relevant market for general purpose cards. *See United States v. Archer-Daniels-Midland Co.*, 866 F.2d 242, 248 n.1 (8th Cir. 1988) ("evidence of the substantial displacement of sugar by HFCS is irrelevant because this displacement focuses on static, rather than dynamic" factors); *United States v. Rockford Mem'l Corp.*, 717 F. Supp. 1251, 1259-60 (N.D. Ill. 1989) ("substitutability over time" is not relevant for market definition), *aff'd*, 898 F.2d 1278 (7th Cir. 1990). Consumers have increased their usage of personal computers over time in response to both price and non-price factors, but that does not mean that pencils and paper and other substitute technologies are in the relevant market for PCs. *See also* Op. 338 (SPA174) (citing M.Katz Dir. ¶¶ 11, 127 (T3010, 3070-71)).

MasterCard further suggests that "[b]ecause this case is about innovation," this Court should abandon the hypothetical monopolist price-sensitivity test found in its precedents in favor of a test asking whether a hypothetical monopolist would

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[32]MasterCard's recent and ongoing efforts to displace cash and checks focus on its debit card. *See* M.Katz Dir. ¶¶ 124, 139 (T3069, 3077-78); P-0359 (E2539-45).

continue to innovate. MC 20, 68-69. But even MasterCard's own expert employed a price-sensitivity test (*see* Pindyck Dir. ¶ 7.1 (T6125)), and MasterCard offers no case support for its suggestion that the sole test in this case should be whether a hypothetical monopolist would continue to innovate. There was no reason for the court to adopt market definition methods designed for the sort of "innovation market" to which MasterCard refers (MC 68-69), because the government did not allege such a market. Innovation is an issue in this case but, contrary to MasterCard's assertion, many of the anticompetitive effects alleged by the government and found by the court did not relate to innovation. *See* pp. 72-99 below.

Despite its objections to price sensitivity analyses, MasterCard argues that the survey-based price sensitivity analysis performed by its expert (Prof. Pindyck) provides a basis to reject the district court's findings. MC 70-71. The district court found, however—based on the testimony of the government's and Visa's experts—that "it is essentially impossible to make a definitive calculation of consumer price sensitivity or elasticity of demand via survey." Op. 336 (SPA172). Moreover, to the extent one can draw any conclusion from MasterCard's survey, it is that credit and charge cards constitute a relevant market. M.Katz Dir. ¶¶ 116-22 (T3064-68). Professor Pindyck's analysis considered a 2% change in the *overall*

cost of a purchase made using a card, which MasterCard asserts (MC 71) is in the range of actual rebate offers. That means, however, that MasterCard is positing an effective price increase of far more than 100% of the cost to the consumer of using the card.[33] That price increase is vastly higher than any a court ever has used to define a relevant market.[34] Yet even with such a huge price increase, MasterCard represents that only 50% of consumers would switch, which indicates that a hypothetical monopolist would find it profitable to raise prices substantially, M.Katz Dir. ¶ 121 (T3067), and therefore, that general purpose cards constitute the relevant market.

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[33]Instead of paying $1.23 to use a credit card to buy $100 worth of goods, the customer effectively pays $3.23 to use the card (including the opportunity cost of declining the bounty offered for using another form of payment).

[34]MasterCard (MC 71 n.25) criticizes Prof. Katz for not relying on a 1996 American Express-sponsored survey, which asked consumers if they would be willing to give up their credit card if they had an ATM card with the same acceptance as their credit card. Although Prof. Katz had relied on a portion of the survey in his expert report, he later concluded that responses to various portions of the survey contradicted each other, and ultimately declined to rely on it in his testimony for any purpose. M.Katz Tr. 4010:14-4011:10, 4012:12-4013:6 (T3801-02, 3803-04). MasterCard is wrong to suggest that the survey indicated that substantial substitution away from general purpose cards was likely "in the context of a zero price increase." MC 71 n.25 (emphasis omitted). Universal merchant acceptance of an ATM card represents a huge quality improvement to existing ATM cards—currently accepted as means of payment only at PIN-enabled merchants—comparable to a price increase for credit cards of vastly more than 5%.

Appellants contend (VUSA 27 & n.7; MC 60-62) that the district court erred in excluding cash, checks, and debit cards from the relevant market of general purpose cards. The district court, however, properly excluded those items from the market and rejected defendants' proffered "all-payments" market.[35] In light of the court's abundant citations for its multiple findings on market definition, appellants do not come close to meeting their burden of demonstrating clear error.

a. Cash And Checks

To be sure, cash and checks often are functional substitutes for general purpose cards. But functional interchangeability is not enough; the test for market definition is whether users find products to be "reasonably interchangeable." *See*

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[35]Because market definition is a "deeply fact-intensive inquiry," *Todd*, 275 F.3d at 199, the district court was right to disregard *National Bancard Corp. v. Visa U.S.A., Inc.*, 596 F. Supp. 1231 (S.D. Fla. 1984), *aff'd*, 779 F.2d 592 (11th Cir. 1986) (*NaBanco*). *Cf.* VUSA 27 n.7; MC 60-61. That another district court made different findings based on a different trial record compiled by a different plaintiff 17 years ago is immaterial to the record in this case and does not provide a basis to question the court's findings here. *See Columbia Metal Culvert Co. v. Kaiser Aluminum & Chem. Corp.*, 579 F.2d 20, 28 (3d Cir. 1978) ("Meticulous 'color-matching' of precedent to determine how similar a particular product is to others which have or have not constituted markets in other cases is thus not nearly so important as a detailed examination of the record developed in the trial court"). Even if the *NaBanco* decision was correct on its record, it may simply reflect a failure of proof in that case. *Southtrust Corp. v. Plus System, Inc.*, 913 F. Supp. 1517 (N.D. Ala. 1995), provides no meaningful additional authority because it merely cites *NaBanco*, without any further analysis. *Id.* at 1524.

U.S. Anchor Mfg., Inc. v. Rule Indus., Inc., 7 F.3d 986, 995-96 (11th Cir. 1993) (generic anchors not in same product market as Danforth-brand anchors, even though they are "functionally interchangeable" and often "virtually identical"); *Archer-Daniels-Midland*, 866 F.2d at 246 (sugar not in relevant market for high-fructose corn syrup (HFCS) despite being functionally interchangeable in every application in which HFCS was used). Functional interchangeability is only one aspect of reasonable interchangeability. *See Buehler AG v. Ocrim S.p.A*, 836 F. Supp. 1305, 1325 (N.D. Tex. 1993); *United States v. Chas. Pfizer & Co.*, 246 F. Supp. 464, 468 n.3 (E.D.N.Y. 1971).

The district court properly found that consumers, merchants, and defendants themselves do not consider cash and checks to be reasonably interchangeable with general purpose cards. *See* Op. 336-38 (SPA172-74). Consumers cannot use cash to make purchases over the Internet[36] or by phone, and "generally do not want to carry large sums of cash to make large purchases." Op. 336, 341 (SPA172, 177); Schmalensee Tr. 5969:23-5971:4 (T5987-89); Schmidt (VUSA) Dep. 70:12-19 (A790). In addition, holders of general purpose cards without monthly balances

[36]Visa estimated that the volume of Internet transactions using its cards will grow to $104 billion by 2003. Beindorff (VUSA) Dep. 36:5-37:18 (A575-76).

benefit by deferring payment for a short time,[37] and those that carry outstanding balances "benefit from the . . . card's credit function, which allows for the choice to purchase now and pay later." Op. 336 (SPA172). Checks have much lower merchant acceptance than either cash or general purpose cards, which discourages their use. *Id.* Merchants' attitudes derive from and therefore reflect consumers' attitudes. Most merchants believe they would "lose significant sales" if they stopped accepting general purpose cards; thus, even merchants with thin profit margins "feel compelled to accept general purpose cards." Op. 337 (SPA173).[38]

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[37]Consumers who pay their credit card bill in full each month ("pure transactors") pay nothing for their purchases until they actually pay their credit card bill. *See* Op. 336 (SPA172). In effect, these consumers receive a short-term interest-free loan from their issuing bank.

[38]In setting interchange rates, Visa and MasterCard consider each other's rates, and the merchant discount rates charged by Discover and American Express, but do not consider the costs to merchants of accepting cash or checks (or debit or proprietary cards). Op. 337 (SPA173). And Visa and MasterCard documents calculate shares of a "general purpose card" market, including credit and charge but not debit cards. Op. 338 n.9 (SPA174). "Industry recognition is well established as a factor that courts consider in defining a market . . . because 'we assume that the economic actors usually have accurate perceptions of economic realities.'" *Todd*, 275 F.3d at 205 (quoting *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 218 n.4 (D.C. Cir. 1986)); *see also AD/SAT*, 181 F.3d at 228 (looking at who parties perceived to be their competitors).

b. Debit Cards

There is strong evidence that consumers "do not consider debit cards to be substitutes for general purpose cards." Op. 336-37 & n.6 (SPA172-73). "Although debit cards are similar to credit and charge cards in that they may be used at unrelated merchants, the fact that upon use they promptly access money directly from a cardholder's checking or deposit account strongly differentiates them from credit and charge cards." Op. 331 (SPA167). Debit cards do not defer payment or provide credit. In addition, online debit cards (which require special terminals at the merchant and use of a PIN) do not have the widespread acceptance of general purpose cards. Op. 337 & n.7 (SPA173); *see also* Schmalensee Tr. 5972:7-25 (T5990). And Visa and MasterCard's own research demonstrates that consumers do not view offline debit cards as substitutes for general purpose cards, even though offline debit has widespread merchant acceptance and requires only the purchaser's signature. Consumers use offline debit cards as a substitute for cash and checks, not for credit or charge cards. Op. 337 & n.8 (SPA173).[39]

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[39]*See also* Selander (MC) Tr. 5638:18-5639:7 (debit card "primarily" a substitute for cash and check) (T5310-11); P-0742 at VU0593590 (Visa document noting that growth in debit volume "has been *incremental* to the credit card business, taking *all* of [its] growth from cash and checks") (emphasis added) (E3216); P-0359 (E2539-45).

Visa and MasterCard argue (VUSA 50; MC 36-37) that it was improper for the court to consider the exclusionary rules' effects on American Express's and Discover's debit card programs in light of the fact that debit cards were neither included in the general purpose card market nor found to be a separate relevant market. The district court's findings of anticompetitive effects concerning debit, however, relate to the effect debit card transaction volume has on competition in the general purpose card network services market due to economies of processing both types of cards over the same network[40] and because future cards will provide access to both credit and debit accounts. Op. 392 (SPA228). The district court's appreciation of debit's contribution to effective competition in general purpose card network services does not suggest that debit is reasonably interchangeable with credit and thus in the relevant market for general purpose cards.

In similar circumstances, the court of appeals in *Microsoft* affirmed the district court's finding that Microsoft unlawfully maintained its PC operating systems monopoly by quashing the "middleware threat." *United States v. Microsoft Corp.*, 253 F.3d 34, 53-54 (D.C. Cir.) (en banc) (per curiam), *cert. denied*, 122 S. Ct. 350 (2001). Sustaining the claim of monopoly maintenance

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[40]MasterCard concedes (MC 73 n.27) that offline debit runs over the same electronic network as credit and charge cards.

required neither the delineation of a middleware market nor the inclusion of middleware in the operating systems market. *Id.* at 54, 81-82.

Thus, "because card consumers have very little sensitivity to price increases in the card market and because neither consumers nor the defendants view debit, cash and checks as reasonably interchangeable with credit cards, general purpose cards constitute a product market." Op. 338 (SPA174).

2. General Purpose Card Network Services Constitute A Relevant Product Market

The district court also found that general purpose card network services "constitute a product market because merchant consumers exhibit little price sensitivity and the networks provide core services that cannot reasonably be replaced by other sources." Op. 338 (SPA174). Although no appellant directly attacks this market's existence,[41] Visa asserts the network market is "largely beside the point." VUSA 27. But the network services market is the market in which Visa and MasterCard operate. Visa and MasterCard do not issue credit, charge, or even debit cards themselves, but set interchange rates and provide the network,

[41]MasterCard (MC 61) characterizes the network services market as "derivative" of the general purpose cards market. But a network-services monopolist would have substantial market power—even if competition from other forms of payment meant that a general-purpose-cards monopolist did not—because network services account for a small fraction of issuers' costs. *See* M.Katz Dir. ¶¶ 184, 147-48 (T3103, 3081-83).

backbone, brand support, standardization, and product parameters that permit banks to issue such cards. Networks and issuers are co-manufacturers of general purpose cards, and neither can succeed without the other.[42]

Visa claims that the relevant market is the market for card issuing because that is where the exclusionary rules have their direct effects. VUSA 27-29. To be sure, the restraint is on issuers, but the record fully supports the district court's conclusion that the exclusionary rules had the purpose and effect of blunting network-level competition, to the ultimate detriment of consumers.[43] As Visa has expressly recognized in the past: "Lest there [be] any confusion, the ultimate

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[42]*See, e.g.*, Op. 334 ("Consumers have access to products that combine dozens of features available through the associations with features and services developed by the individual issuers") (SPA170); B.Katz (VUSA) Tr. 3137:9-3138:1 (confirming that issuers determine "the main characteristics" of cards and that issuers are not mere distributors of "spices or ice cream") (T2684-85) (discussing P-0727 at ¶ 28 (E3159-60)); Knox (VUSA) Tr. 4819:9-20 (confirming statements in P-0836 at VU1589532 (E3400) that Visa has "strength to leverage" and can "develop 'one dozen solutions'" to each one that American Express can create because of Visa's multiple issuers, and that Visa members can use those solutions to customize smart cards for the particular customer segments they serve) (T4449-50).

[43]Thus, Visa's reliance (VUSA 27-29) on *MountainWest* for the proposition that the relevant market is the issuer market rather than the network market, is misplaced. The parties there *stipulated* to an issuer market, concerning *intra*system competition. *SCFC ILC, Inc. v. Visa USA, Inc.*, 36 F.3d 958, 966-67 (10th Cir. 1994) ("*MountainWest*"). No one disputes that the issuer market is unconcentrated and that Visa is not an issuer. Thus, it is not surprising that the Tenth Circuit held that Visa did not have market power in that market. *Id.* at 969.

impact of any harm to system-level competition is felt by cardholders and merchants who use or accept general purpose charge cards." P-1187J at VU1588558 (E4138). Moreover, Visa's former general counsel and its primary expert both confirmed that this remains true today. Op. 339 (SPA175) (citing B.Katz (VUSA) Tr. 3190:8-3191:4 (T2737-38); Schmalensee Tr. 5985:21-5987:2 (T6003-05)).[44] Thus, network-level competition is the correct market for analysis in this case.

B. Market Power

The district court found that Visa and MasterCard, "whether considered jointly or separately," have market power in the general purpose card network services market. Op. 341 (SPA177). The court based this finding on two independent analytical methods of determining market power: direct evidence of market power, and inference from market shares. Op. 340-41, 341-42 (SPA176-77, 177-78).[45] Market power is a question of fact, reviewed for clear error.

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[44]In addition, MasterCard's expert testified that "the exit of MasterCard from the systems market would result in significant consumer harm," thereby "confirm[ing] that systems competition affects consumer welfare." Op. 339 (SPA175) (citing Pindyck Tr. 6108:10-23, 6113:1-6116:5, 6120:4-11 (T6245, 6250-53, 6257)).

[45]*See Tops Mkts., Inc. v. Quality Mkts., Inc.*, 142 F.3d 90, 98 (2d Cir. 1998) (market power "may be proven directly by evidence of the control of prices . . . or it may be inferred from one firm's large percentage share of the relevant market"); *Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 937 (7th Cir. 2000).

ASCAP v. Showtime/The Movie Channel, Inc., 912 F.2d 563, 569-70 (2d Cir. 1990); *Consolidated Gold Fields*, 871 F.2d at 261 (deferring to district court's aggregation of "intertwined" entities to determine market power); *Grand Light & Supply Co. v. Honeywell, Inc.*, 771 F.2d 672, 681 (2d Cir. 1985). Thus, appellants must demonstrate that the district court committed clear error with respect to both methods. They have not done so.

Although Visa disputes the relevance of the district court's market definition and the findings of anticompetitive effects, Visa does not challenge the finding that it possesses market power in the market for general purpose card network services. Having failed to address the issue in its opening brief, Visa waives the argument. *See Thomas v. Roach*, 165 F.3d 137, 145-46 (2d Cir. 1999); *United States v. Gabriel*, 125 F.3d 89, 100 n.6 (2d Cir. 1997). Only MasterCard's market power requires discussion.

"Market power may be shown by evidence of 'specific conduct indicating the defendant's power to control prices or exclude competition.'" *K.M.B. Warehouse Distribs., Inc. v. Walker Mfg. Co.*, 61 F.3d 123, 129 (2d Cir. 1995) (quoting *Broadway Delivery Corp. v. UPS*, 651 F.2d 122, 130 (2d Cir. 1981)). "Since the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on

competition, 'proof of actual detrimental effects, such as a reduction of output,' can obviate the need for an inquiry into market power, which is but a 'surrogate for detrimental effects.'" *Indiana Dentists*, 476 U.S. at 460-01 (quoting 7 PHILLIP E. AREEDA, ANTITRUST LAW ¶ 1511, at 429 (1986)); *see also Todd*, 275 F.3d at 206 (proof that "defendant's conduct exerted an actual adverse effect on competition . . . is a strong indicator of market power"); *Capital Imaging Assocs. v. Mohawk Valley Med. Assocs.*, 996 F.2d 537, 546 (2d Cir. 1993); *Toys "R" Us*, 221 F.3d at 937 (market power can be proven through "direct evidence of anticompetitive effects"). Indeed, several courts have relied on direct evidence of market or monopoly power.[46]

1. Direct Evidence

Visa and MasterCard have joint market power, i.e., the power to achieve an anticompetitive effect through the restraint. *See Capital Imaging*, 996 F.2d at 546 ("market power bears a particularly strong relationship to a party's ability to injure

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[46]*See, e.g.*, *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 477 (1992) (it is "clearly reasonable to infer that Kodak has market power to raise prices and drive out competition . . ., since respondents offer direct evidence that Kodak did so"); *Indiana Dentists*, 476 U.S. at 461 ("the finding of actual, sustained adverse effects on competition . . . is legally sufficient to support a finding that the challenged restraint was unreasonable even in the absence of elaborate market analysis"); *Toys "R" Us*, 221 F.3d at 937 (plaintiff had "sufficient proof of actual anticompetitive effects that no more elaborate market analysis was necessary").

competition"); *Oltz v. St. Peter's Community Hosp.*, 861 F.2d 1440, 1448 (9th Cir. 1988) ("market definition and market power are merely tools designed to uncover competitive harm"). The memberships of the two associations collectively have that power because they control the banking assets the district court found critical to competition. *See* Op. 387-96 (SPA223-32); P-0535 at VIF0403236 (banks "have the upper hand in the evolution of their industry") (E2709); *see also Ball Mem'l Hosp., Inc. v. Mutual Hosp. Ins., Inc.*, 784 F.2d 1325, 1335 (7th Cir. 1986) (market power shown by control over productive assets). Network-level competition is harmed, the district court found, in part because the exclusionary rules foreclose American Express and Discover from access to bank partners—to which Visa and MasterCard have ready access. The court further found that the remaining banking assets (i.e., "[s]mall banks not in the Visa and MasterCard system") and non-bank issuers (e.g., retailers, insurers) to which American Express and Discover do have access, are not competitively significant. Op. 394 (SPA230). In other words, Visa and MasterCard exercise market power by excluding American Express and Discover. *See K.M.B. Warehouse*, 61 F.3d at 129 (market power "may be shown by evidence of 'specific conduct indicating the defendant's power to . . . exclude competition'") (citation omitted).

MasterCard mistakenly contends (MC 77) that joint market power is relevant only if there was an agreement between the associations to adopt the exclusionary rules. But the common membership and ownership of the two associations alone means that this power to exclude was exercised by the associations jointly and by each association separately.[47] The exclusionary rules had competitive "bite," *Toys "R" Us*, 221 F.3d at 933, only because (1) both associations enacted them, and (2) the number of banks not subject to those agreements was competitively insignificant.

Indeed, history clearly demonstrates MasterCard's separate market power. In 1996, when Visa Bylaw 2.10(e) was in place but MasterCard had no similar restraint, American Express openly courted MasterCard's members to explore partnerships with it. In fact, MasterCard seriously considered treating American Express's overture as an *opportunity* for MasterCard to shift share from Visa: Banks might be willing to leave Visa entirely for the opportunity to issue both

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[47]The district court's decision with respect to Count I does not alter the analysis. The court held that plaintiff had failed to prove that dual *governance,* by itself, had anticompetitive effects. That says nothing about whether Visa and MasterCard, together or separately, have market power. In fact, the district court found that "even a cursory examination of the relevant characteristics of the network market reveals that whether considered jointly or separately, the defendants have market power," even though it ultimately ruled in favor of defendants on Count I. Op. 341, 328-29 (SPA177, 164-65).

MasterCard and American Express cards. *See* pp. 18-20 above. Had MasterCard allowed this to happen, several large MasterCard members would have partnered with American Express, Op. 381 (SPA217) (citing Lockhart Tr. 1836:12-24 (T1522); P-0296 at MC85659 (E2499)), and this litigation might never have been necessary. Ultimately, however, the majority of banks on MasterCard's Board decided to take a hard line against American Express and Discover by enacting the CPP. Once both Visa and MasterCard's exclusionary rules were in place, the anticompetitive effects followed directly. Thus, MasterCard demonstrated that it has the "ability to injure competition." *Capital Imaging*, 996 F.2d at 546.

Moreover, Visa's and MasterCard's joint and separate market power are evident from their power over merchants. Uncontroverted merchant testimony demonstrated that many merchants "cannot refuse to accept Visa and MasterCard even in the face of significant price increases because the cards are such preferred payment methods that customers would choose not to shop at merchants who do not accept them." Op. 340 (SPA176).[48] Terrence Scully of Target, for example, testified that although Target considered discontinuing acceptance of American

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[48]The district court observed that "Visa and MasterCard . . . charge substantially different prices for those hundreds of thousands of merchants who must take credit cards." Op. 341 (SPA177). The court found that this price discrimination "illustrates" the defendants' market power over merchants. *See* Op. 340-41 (SPA176-77).

Express cards, it would be "foolhardy" to consider not accepting Visa or MasterCard.[49] Scully Dep. 66:14-67:2, 83:3-85:3 (A797-98). Similarly, Publix supermarkets' representative testified that Publix could not drop Visa *or* MasterCard even if interchange fees rose 50%. Woods (Publix) Tr. 399:8-400:3 (T228-29).[50] Thus, the record demonstrates that merchant demand for Visa and MasterCard—collectively and separately—is highly inelastic. That MasterCard can point (MC 72 n.26, 81 n.32) to a particular merchant that accepts American Express but not Visa/MasterCard[51] says only that Visa and MasterCard's market

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[49]Thus, MasterCard's observation (MC 80-81) that many merchants that accept Visa/MasterCard also accept American Express, misses the point. The evidence showed that many merchants feel *compelled* to accept Visa/MasterCard, but do not feel the same way about American Express. *See, e.g.*, McCurdy (Amex) Tr. 1044:14-1045:10 (describing "Boston fee party" wherein restaurants began declining to accept American Express cards to protest its high merchant discount) (T802-03); Chenault (Amex) Tr. 2341:10-2342:10 (same) (T1909-10).

[50]*See also* Rodgers (Saks) Dep. 49:18-50:2, 58:15-59:11, 133:19-25 (would be "ludicrous" for Saks to stop accepting Visa *or* MasterCard) (A781, 782, 783); *id.* at 59:5-11 (could not discontinue accepting MasterCard even if still accepted Visa because "the consumer views them as being the same") (A782); Zyda (Amazon) Tr. 692:10-18 (Amazon could not seriously consider dropping Visa or MasterCard) (T492).

[51]MasterCard twice refers to this one merchant, Costco, as the "largest retailer in the United States" (MC 72 n.26, 81 n.32), but provides no citation for that claim. In fact, according to published reports, Costco is the ninth-largest retailer in the country, with less than one-fifth the sales of the largest retailer, Wal-Mart. *See* http://www.triversity.com/newsandevents/ release_010705.html (2001 rankings by National Retail Federation (NRF)); http://www.costco.com/

power is not absolute.[52] At bottom, the district court resolved a disputed question of fact and its resolution is not clearly erroneous.

The district court supported its finding regarding merchant acceptance by noting that "both Visa and MasterCard have recently raised interchange rates charged to merchants a number of times, without losing a single merchant customer as a result." Op. 340 (SPA176).[53] MasterCard argues here that this fact should carry little weight because its interchange rate is "below cost." MC 79. MasterCard, however, never explained how defendants calculated "cost," how much below "cost" their interchange rates are, or how that "cost" compares to the sum of issuers' various revenue streams (including interest charges, interchange, late fees, annual fees, etc.). One should not expect the competitive interchange fee to cover the entire cost of card issuing because there are other important revenue

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frameset.asp?trg=CustService%2Fcustsvc%2Easp&log= (Costco website). Costco, a membership warehouse club, prefers to deal with single suppliers and sought an exclusive relationship with American Express. Chenault (Amex) Tr. 2438:4-17 (T2006).

[52]"[A]bsolute success in excluding competition," however, is not "an essential element to proving monopoly power," *Woods Exploration & Producing Co. v. Alcoa*, 438 F.2d 1286, 1307 (5th Cir. 1971), let alone market power.

[53]*See also* P-0749 at VU0597265, 271 (between 1997-99, Visa and MasterCard's average interchange rates rose 13%, with some segments increasing by 20-30%) (E3279, 3285).

sources. *See* Fairbank (Capital One) Dep. 49:9-23 (A657-58); Schmidt (VUSA) Dep. 84:9-22 (A791-92). Appellants do not dispute that the average revenue from all sources exceeds the marginal cost of the typical transaction; indeed, MasterCard's own documents confirm that its issuers earn at least a 15% return on equity with some "pure transactors"[54]—those transacting sufficient volume. *See* P-0128 at ARG17640 (E2156); *see also* P-0127 (E2153-55); P-0129 (E2165-87). Because issuers make a profit on some pure transactors—who generate revenues for the issuer only through interchange and possibly small annual fees—it must follow that interchange rates exceed marginal cost. In any event, the question of the associations' power over merchants was hotly contested below, and the district court found that fact in favor of plaintiff. That finding is not clearly erroneous.

2. Market Shares

Independent of the substantial direct evidence of market power, the district court also found Visa and MasterCard's market power could be inferred based on their high market shares in a market with high entry barriers. Op. 341-42 (SPA177-78); *Tops Markets*, 142 F.3d at 100 (market power may "consider[] the defendant's relevant market share in light of other market characteristics, including barriers to entry"); *Coastal Fuels*, 79 F.3d at 196-97 (market power

[54] *See* p. 44 n.37 above.

"may be proved circumstantially by showing that the defendant has a dominant share in a well-defined relevant market and that there are significant barriers to entry in that market . . ."). MasterCard does not—nor could it—contest that the network services market has high entry barriers. There are only four significant providers of network services, no one has entered the market since Discover did so in 1985, and entry would require an investment of over $1 billion. *See* Op. 341-42 (SPA177-78); M.Katz Dir. ¶¶ 164-81 (T3091-3101). Thus, the only remaining question is whether the market share is sufficiently high.

MasterCard assigns error (MC 77) to the district court's consideration of the associations' combined market shares—73% of transaction volume and 85% of cards issued[55] (Op. 341 (SPA177))—but the district court was justified in doing so. *See* p. 53 above. Visa and MasterCard are owned by thousands of common members and exempt each other from their exclusionary rules. *See also* Rodgers (Saks) Dep. 59 (Saks could not discontinue accepting MasterCard even if still accepted Visa because "the consumer views them as being the same") (A782).

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[55]MasterCard does not dispute that a share of 73-85% in a market with high entry barriers is sufficient to infer market power, which it clearly is. *See, e.g.*, *American Tobacco Co. v. United States*, 328 U.S. 781, 797 (1946) (over 66% of the market is a "substantial monopoly").

Even Visa concedes that duality justifies a "distinction between 'them' (AmEx; Discover) and 'us' (MasterCard)." VUSA 70.

MasterCard also contends that, as a matter of law, its share of "only 26%" precludes a finding of market power. MC 20, 75-76. But this Court recently reaffirmed that "a threshold showing of market share is not a prerequisite for bringing a § 1 claim." *Todd*, 275 F.3d at 206 (citing *K.M.B. Warehouse*, 61 F.3d at 129). The cases MasterCard cites (MC 75) stand merely for the proposition that one cannot infer market power *based on* an entity's market share of less than 30%; none of those cases included other indications of market power, such as direct evidence, which the district court found here. *See Toys "R" Us*, 221 F.3d at 937 (market share is irrelevant when market power proved directly). MasterCard cites no case to support its assertion that a share of less than 30% *precludes* a finding of market power, regardless of the circumstances. Nor does MasterCard's alleged decline in market share over time (MC 76-77) "foreclose a finding" of market power. *Oahu Gas Serv., Inc. v. Pacific Res., Inc.*, 838 F.2d 360, 366 (9th Cir. 1988) (citation omitted).

Finally, MasterCard questions how it can possess market power with a 26% share when American Express's market share is a "comparable 20%." MC 76. But the direct comparison between MasterCard's and American Express's market

shares is a red herring. The district court did not find that MasterCard possesses market power *because of* its 26% share; it merely rejected MasterCard's argument that such a share precludes a finding of market power based on other evidence. That conclusion was factually and legally sound. The court also found that the size of the merchant acceptance network and consumers' perceptions of it are vital, Op. 387-88 (SPA223-24), and that Visa and MasterCard recognized they had a "significant acceptance advantage over American Express in the United States, which they sought to maintain." Op. 388 (SPA224). MasterCard is accepted at roughly twice as many merchant outlets as American Express domestically, and nearly three times as many internationally.[56] M.Katz Dir. Fig. 4 (T3243); *see also* M.Katz Dir. Fig. 20 (in 1998, MasterCard had 35.8% of card accounts, compared to 5.5% for American Express) (T3260-61).

Moreover, the 6% share difference is not trivial. In justifying its CPP, MasterCard's then-CEO testified that without it, American Express would gain share and "[e]very share point was worth real revenue to us." Lockhart (MC) Tr.

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[56]MasterCard (MC 28) points to the fact that American Express had achieved coverage of 96% as measured in terms of the spending of American Express cardholders. But this considers only the spending of *current* American Express cardholders (Golub Tr. 2715:1-2718:18 (T2279-82); Chenault Tr. 2599:19-2600:21 (T2165-66)), thus ignoring customers American Express was trying to reach, including through its desired partnerships with banks.

1875:21-1876:8 (T1561-62). *See also* D-1856 at VUTE0004647 (1% share of general purpose card volume was $9.32 billion in 1999) (E695). And John Reed, then-CEO of Citibank, concluded that "[t]he reason that American Express does not have the reach necessary to be a broad-scaled card is they don't have enough volume on their card to convince the mom and pop stores to bother to sign up. . . . It isn't that there's anything wrong with the card or the cardholders or anything else, they just don't have enough volume." Reed Dep. 40-41 (A776-77). Reed determined that "an entrant would need to capture a 20 to 25 percent market share to be successful." Op. 342 (SPA178) (citing Reed Dep. 38-41 (A775-77)). American Express's market share is at best at the bottom end of that range,[57] while MasterCard's share places it firmly above the top end.

II. THE DISTRICT COURT PROPERLY ANALYZED THE EXCLUSIONARY RULES AS HORIZONTAL RESTRAINTS RATHER THAN AS VERTICAL DISTRIBUTION RESTRICTIONS

Visa and MasterCard contend that the exclusionary rules should be characterized as exclusive distribution restraints imposed by a single entity on its dealers. VUSA 24-26, 29-34; MC 43-48. The district court rejected their

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[57]Some of the measures of market share place American Express much lower than 20%. *See, e.g.*, Katz Dir. ¶¶ 164-69 & Fig. 20 (as of 1998, American Express had 5.5% of card accounts, 14.7% of the number of purchase transactions, and 7.1% of outstandings) (T3091-95, 3260-61).

characterization, however, and its rejection is a finding of fact, reviewed only for clear error. *Chicago Prof'l Sports Ltd. P'ship v. NBA*, 961 F.2d 667, 672 (7th Cir. 1992) ("Characterization is a creative rather than exact endeavor. Appellate review is accordingly deferential"); *L.A. Mem'l Coliseum Comm'n v. NFL*, 726 F.2d 1381, 1387 (9th Cir. 1984) (the "nature of an entity and its ability to combine or conspire in violation of § 1 is a fact question"). The exclusionary rules are agreements among competing banks to eliminate an important form of competition among themselves and against the networks they control. The joint venture context does not alter the nature of the restraint; hence, the vertical distribution cases, to which Visa and MasterCard direct the Court's attention, have no relevance to this case.

A. The District Court Properly Found That The Exclusionary Restraints Were The Product Of A Horizontal Agreement

A joint venture controlled by competing firms may, of course, take actions as a single entity that do not restrict competition among its members. For example, a joint venture might offer a product in a market in which its owners could not separately compete or it might purchase supplies for its headquarters. But whether particular conduct is concerted action is a question of fact, and there can be little doubt that the exclusionary rules at issue here are horizontal restraints.

As the district court found, Visa's Bylaw 2.10(e) and MasterCard's CPP are "restrictions of, by and for the member banks." Op. 400 (SPA236). The member banks compete as issuers of general purpose credit cards. They do not merely distribute cards, but co-manufacture them, determining many of the "features and services" of the cards they issue, including the nature of any rewards or rebates. Op. 334 (SPA170).

Bylaw 2.10(e) and the CPP were adopted specifically for two reasons. The first purpose was to restrict competition among the member banks as to the kinds of cards they issue, thereby ensuring that no member/issuer gains a "competitive advantage" over other members by offering consumers cards with features available from American Express or Discover. Op. 400-01 (SPA236-37). In enacting a bylaw that "prevents member institutions from competing against each other" on some basis, the "member institutions have created a horizontal restraint—an agreement among competitors on the way in which they will compete with one another." *NCAA v. Board of Regents*, 468 U.S. 85, 99 (1984). *See also Fraser v. Major League Soccer, L.L.C.*, 284 F.3d 47, 57 (1st Cir. 2002) (league acting in horizontal capacity when board acts to control competition among members); *NASL v. NFL*, 670 F.2d 1249, 1252 (2d Cir. 1982) (NFL bylaw banning cross-ownership of other professional sports league team is a horizontal

restraint); *Capital Imaging*, 996 F.2d at 545 (horizontal analysis when HMO board excluded radiology practice group to "insulate" HMO's member radiologists "from increased competition"); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 214 (D.C. Cir. 1986) (horizontal restraint because "all of these legally separate corporations agreed to a policy that restricted competition").

The second reason for the exclusionary rules was to weaken the only two networks not owned by the member banks. Op. 400-01 (SPA236-37). These banks also are involved at the network level, as owners of the Visa and MasterCard associations. Member banks fund competitive initiatives and sit on the boards and committees that make strategic business decisions.[58] And, as owners of the associations, the member banks reap the rewards from the suppression of network-level competition caused by the rules.

B. The Joint Venture Structure Of The Associations Provides No Basis For Treating The Exclusionary Rules As Vertical Restraints

Visa and MasterCard do not seriously dispute that Bylaw 2.10(e) and the CPP restrict competition among issuing banks. Indeed, Visa concedes that "[i]t is unquestionably true, that—absent the joint venture—the antitrust laws would not

[58] *See* Beindorff (VUSA) Dep. 294:9-15 ("The banks control Visa, all they have to do is change the bylaw and they can [issue American Express cards]") (A579); Jensen (VINT) Dep. 22 ("it's the members that ultimately determine what are the rules") (A730).

allow a group of banks to agree that they will not also issue American Express or Discover cards." VUSA Stay Reply 10 (Jan. 29, 2002) (A1873, 1888).[59] Rather, Visa and MasterCard assert that the exclusionary rules are "ancillary" to legitimate joint ventures and that, therefore, the rules should not be treated as horizontal restraints. Visa and MasterCard reason that joint ventures formed by competitors should not be placed at a disadvantage vis-à-vis their unitary rivals, and so the exclusionary rules should be judged by the same standards that would be applied to an agreement between a single manufacturer and its distributors. They contend that the exclusionary rules should be subject to at most a lenient rule of reason inquiry, in which vertical exclusive dealing arrangements may be found to be anti-competitive only if they entirely foreclose a rival's opportunity to distribute cards. VUSA 24-26, 29-34; MC 43-48. This chain of reasoning is fundamentally flawed.

No one disputes that Visa and MasterCard are "legitimate joint ventures," and the district court expressly recognized that "such ventures may employ reasonable restraints to make the joint venture more efficient." Op. 399 (SPA235) (citing *Broadcast Music, Inc. v. CBS, Inc.*, 441 U.S. 1, 23-25 (1979); *Rothery*, 792

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[59] *See also* Op. 401 (noting testimony of a defense expert that it would be economically reasonable to condemn an agreement among competitors not to deal with a supplier) (SPA237).

F.2d at 223-24). This principle, articulated in *Addyston Pipe*[60] and its progeny, reflects recognition that agreements among competitors that might be anticompetitive in another context may be procompetitive if they make a joint venture much more effective in achieving its procompetitive purposes. For example, although an express agreement between two competitors to reduce their output ordinarily would be condemned as per se unlawful, such an agreement may be necessary or appropriate in the context of a sports league so that each team plays the same number of games in a season. *See* 11 HERBERT HOVENKAMP, ANTITRUST LAW ¶ 1908, at 231-32 (1998); *see also Chicago Board of Trade v. United States*, 246 U.S. 231, 239-40 (1918) (output-restricting call rule procompetitive in joint venture context). Such "ancillary" restraints are properly evaluated under the rule of reason in a manner that fully accounts for their procompetitive effects, *BMI*, 441 U.S. at 24-25; *National Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 689 (1978); *Addamax Corp. v. Open Software Found., Inc.*, 152 F.3d 48, 52 (1st Cir. 1998), even if similar conduct unrelated to a joint venture would be unlawful per se. *See BMI*, 441 U.S. at 19-20 (per se rule

[60]*United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 279-82 (6th Cir. 1898), *aff'd as modified*, 175 U.S. 211 (1899).

applies when "practice facially appears to be one that would always or almost always tend to restrict competition and decrease output").

However, the ancillary restraints doctrine does not support Visa and MasterCard's argument that the exclusionary rules in this case should be treated as if they were the product of a vertical agreement between a single entity at the network level and its independent issuers, rather than a horizontal agreement among those issuers. The fundamental problem with their argument is that they failed to establish that the exclusionary rules are ancillary. As we discuss in Part IV below (pp. 101-117), the district court carefully considered the proffered procompetitive rationales for the restraints and rejected them, not because it failed to understand their legal significance, but because it found that the record did not support them. Op. 399-407 (SPA235-43). Appellants' efforts to substitute their own characterizations of the purpose and effect of the exclusionary rules for the district court's fact findings should be soundly rejected. *See Eiberger v. Sony Corp. of Am.*, 622 F.2d 1068, 1078-79 (2d Cir. 1980) (rejecting proffered justification because "factual predicates are lacking").

Moreover, even if Visa and MasterCard had established that the exclusionary rules were ancillary restraints because they were reasonably related to the viability of the joint ventures and thereby promoted competition, it would

not follow that the district court should ignore the horizontal nature of the restraints in evaluating their overall effects on competition under the rule of reason. *See Polk Bros., Inc. v. Forest City Enters., Inc.*, 776 F.2d 185, 189 (7th Cir. 1985) ("[t]he evaluation of ancillary restraints under the Rule of Reason does not imply that ancillary agreements are not real horizontal restraints"). Horizontal agreements, restricting competition among direct competitors, raise competitive concerns that single-firm conduct does not. *See Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 768-69, 774-776 (1984); *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 301 (2d Cir. 1979) ("[t]here is a vast difference, however, between actions legal when taken by a single firm and those permitted for two or more companies acting in concert"). As Chief Judge Boudin of the First Circuit explained, in deciding whether a rule restricting salary competition among a sports league's member teams was the conduct of a single entity or a horizontal agreement:

> From the standpoint of antitrust policy, this prospect of horizontal coordination among the operator/investors through a common entity is a distinct concern. Whatever efficiencies may be thought likely where a single entrepreneur makes decisions for a corporate entity (or set of connected entities), the presumption is relaxed—and may in some contexts be reversed—where separate entrepreneurial interests can collaborate . . . .

Fraser, 284 F.3d at 57.

The district court's analysis afforded Visa and MasterCard the full benefit of their status as joint ventures. The government did not argue that the exclusionary rules constituted per se violations of the antitrust laws, Op. 343-44 (SPA179-80), and the district court applied the rule of reason, which "seeks to 'determine whether the restraints in the agreement are reasonable in light of their actual effects on the market and their procompetitive justifications.'" Op. 343 (SPA179) (quoting *Clorox Co. v. Sterling Winthrop, Inc.*, 117 F.3d 50, 56 (2d Cir. 1997)). The district court's conclusion that the rules unreasonably restrain competition reflects the failure of Visa and MasterCard to prove their claims of procompetitive justification, and not any legal error.

C. Appellants' Reliance On Vertical Distribution Cases Is Misplaced

Appellants urge this Court to treat the exclusionary rules as vertical exclusive distribution restraints. But the antitrust laws "have long drawn a sharp distinction between contractual restrictions that occur up and down a distribution chain—so-called vertical restraints—and restrictions that come about as a result of agreements among competitors, or horizontal restraints." *Toys "R" Us*, 221 F.3d at 930. *Accord Oreck Corp. v. Whirlpool Corp.*, 579 F.2d 126, 131 (2d Cir. 1978) (en banc). Appellants' novel rationale for not drawing this distinction here is entirely unpersuasive.

Although characterization of a restraint as horizontal often proves decisive, because it leads to application of the per se rule, the court below analyzed the exclusionary rules under the rule of reason. And the rule of reason calls for an examination of *all* circumstances surrounding a restraint—whether "horizontal" or "vertical"—to assess the restraint's anticompetitive effects. *See* Op. 343-44 (citing cases) (SPA179-80). Here, that analysis shows that the exclusionary rules unreasonably restrain trade, *see id.* at 379, 382-83 (SPA215, 218-19), notwithstanding appellants' contention that American Express and Discover can use existing distribution channels (e.g., direct mail, telemarketing) to reach every consumer with card offerings and, therefore, are not foreclosed. VUSA 29-34; MC 27-29.

Appellants direct (VUSA 29-34; MC 24) this Court to "exclusive dealing" cases such as *CDC Technologies, Inc. v. IDEXX Laboratories, Inc.*, 186 F.3d 74 (2d Cir. 1999), and *Omega Environmental, Inc. v. Gilbarco, Inc.*, 127 F.3d 1157 (9th Cir. 1997). Those cases, however, are inapposite because the district court found that the exclusionary rules were enacted and maintained by the member banks as horizontal rivals. Op. 379-82, 400-01 (SPA215-18, 236-37). *See United States v. General Motors Corp.*, 384 U.S. 127, 143-48 (1966) (per se condem-

nation of a manufacturer-imposed restraint on its distributors in response to an agreement *among* the distributors); *Oreck*, 579 F.2d at 131.[61]

The law does not support appellants' suggestion that the exclusionary rules should be treated as exclusive dealing despite their clear horizontal character. *See, e.g.*, *Toys "R" Us*, 221 F.3d at 932, 934-36 (rejecting vertical analysis when store orchestrated a "horizontal agreement" among its key suppliers to boycott store's competitors; agreement caused substantial anticompetitive effects); *cf. U.S. Healthcare, Inc. v. Healthsource, Inc.*, 986 F.2d 589, 594-95 (1st Cir. 1993) (utilizing "exclusive dealing" vertical analysis only after finding no evidence of horizontal agreement). The banks are not mere distributors agreeing with a manufacturer to be an exclusive agent for distributing a commodity product; rather, they "are a unique distribution source" based on their individual experience and expertise as well as their access to demand deposit accounts, which is crucial

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[61]Although not an "exclusive dealing" case, appellants' extensive reliance (VUSA 31-34; MC 24-26) on *Clorox Co. v. Sterling Winthrop, Inc.*, 117 F.3d 50, 56 (2d Cir. 1997), is similarly misplaced. That case addressed Clorox's attempt to rescind a trademark agreement to which its predecessor had entered. As the court emphasized, "trademarks are non-exclusionary," trademark agreements are "common, and favored, under the law," and agreements negotiated at arms-length are presumptively "pro-competitive." *Id.* at 57, 55, 60. Clorox simply could not show any anticompetitive effects arising from the agreement. *Id.* at 56-58. Here, by contrast, the exclusionary rules substantially restrained competition and caused significant adverse effects to consumers.

for offering network products with debit functionality. Op. 383 (SPA219); Op. 395 (banks are "not merely distributors of commodity products such as 'spices or ice cream'") (SPA231).

III. THE EXCLUSIONARY RULES CAUSE ANTICOMPETITIVE EFFECTS

A. The Agreements Among Banks Not To Issue Cards On Rival Networks Are Facially Anticompetitive

The exclusionary rules embody agreements among competing bank issuers of general purpose cards to refrain from issuing cards on any network not controlled by them.[62] The issuing banks participating in these agreements account for 85% of all general purpose card issuance, Op. 389 (SPA225), and the small banks not already members of Visa/MasterCard, and therefore not party to the agreements lack their "card-issuing infrastructure" and expertise. Op. 394 (SPA230). On their face, these agreements restrict competition in the issuing and network services markets.

The district court found that the challenged rules "effectively prevent[] Visa and MasterCard member banks from issuing American Express and Discover cards, reducing overall card output and available card features." Op. 379

[62]Both exclusionary rules exempt Diners (owned by Citibank) and JCB (for which Household Bank had obtained exclusive U.S. rights). Op. 379 & n.19, 381 (SPA215, 217).

(SPA215). Individual issuers yield their freedom to decide whether to offer their customers cards with features available on the American Express and Discover networks in exchange for the assurance that they will not face competition from other issuing banks offering those features. As the Supreme Court has emphasized, "[a] refusal to compete with respect to the package of services offered to customers, no less than a refusal to compete with respect to the price term of an agreement, impairs the ability of the market to advance social welfare . . . ." *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 459 (1986). "Absent some countervailing procompetitive virtue . . . such an agreement limiting consumer choice by impeding the 'ordinary give and take of the market place,' cannot be sustained under the Rule of Reason." *Id.* (quoting *Professional Engineers*, 435 U.S. at 692). *See also NCAA*, 468 U.S. at 114 n.54 ("[e]nsuring that individual members of a joint venture are free to increase output has been viewed as central in evaluating the competitive character of joint ventures").

Moreover, "and more importantly for this case, the rules restrain competition in the network market because they prevent American Express and Discover from offering network services to the consumers of those services, the members of the Visa and MasterCard associations." Op. 379 (SPA215). The issuing banks, which control networks with market power, have agreed to deny

rival networks "'relationships the competitors need in the competitive struggle.'" *Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.*, 472 U.S. 284, 294 (1985) (citation omitted). Unless procompetitive justifications are established for such an agreement, "the likelihood of anticompetitive effects is clear." *Id.* The agreements deny American Express and Discover the opportunity to combine their network services and card products with the unique assets and marketing skills possessed by Visa and MasterCard member banks, and thereby reduces the ability and incentives of American Express and Discover to invest in improved network services and card features. As a result, American Express and Discover are significantly less effective competitors in the general purpose card network services market, and the competitive pressure on Visa and MasterCard is reduced. Absent the exclusionary rules, "American Express and Discover would seek to work with a variety of bank issuers . . . ." Op. 382 (SPA218). Indeed, the purpose of the rules was "to restrict competition among competitor networks and banks." Op. 401 (SPA237).[63]

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[63]Although intent alone cannot be used to condemn or save a restraint, *Chicago Board of Trade*, 246 U.S. at 238, "in cases of ambiguity we presume that the defendants, who are in the best position to know their business, are also rational actors. As a result, knowledge of their own expectations can aid a tribunal in determining whether the likely effects of a restraint are competitive or anticompetitive." 11 HOVENKAMP ¶ 1912, at 298. "[E]vidence of the defendants' anticompetitive purpose is relevant in judging its potential anticompetitive effect."

As the district court emphasized, the restraints' effect on competition is the touchstone for legality under the rule of reason. Op. 381-82 (SPA217-18). Vigorous competition does not violate the law merely because it disadvantages less-efficient rivals. But agreements that deny consumers the benefits of vigorous competition do violate the law by denying other firms the opportunity to compete. Thus, when the two dominant incumbents significantly disadvantage their only two significant rivals (actual or potential), a rule of reason analysis involves consideration of the challenged conduct's effects on the opportunities available to competitors. *See, e.g.*, *Full Draw Prods. v. Easton Sports, Inc.*, 182 F.3d 745, 753-54 (10th Cir. 1999). The nexus here is plain. The district court found that by disadvantaging American Express and Discover, the exclusionary rules forestalled competition that could "enhance price competition and benefit consumers" in the issuing market and "increase the available supply and variety of network services," resulting in "more card products for bank issuers and thus more options for consumers." Op. 382 (SPA218).

NASL, 670 F.2d at 1259. *See also K.M.B. Warehouse*, 61 F.3d at 130 ("[i]ntent is relevant . . . to 'help courts interpret the effects' of defendants' actions'") (citation omitted); *General Leaseways, Inc. v National Truck Leasing Ass'n*, 744 F.2d 588, 596 (7th Cir. 1984) (intent may "corroborate an inference of anticompetitive effect based on the objective evidence of what the defendant had done").

Although it could have chosen to rely on the inherently anticompetitive nature of the exclusionary rules, in light of Visa and MasterCard's failure to demonstrate procompetitive justifications for them (see pp. 101-117 below), the court's findings were instead based on its meticulous review of the extensive record.[64] The court set forth in detail the clear evidence of specific anticompetitive effects at both the network and issuer level, to the ultimate detriment of consumers. Op. 381-99 (SPA217-35).

B. By Denying Rivals Access To Multiple And Diverse Bank Issuers, The Exclusionary Rules Suppress Network-Level Competition

Different issuers have different strengths in providing "special skills, expertise and relationships with consumers that collectively strengthen the general purpose card networks." Op. 389 (SPA225). Because banks possess customer relationships, "the most valuable assets available," they "have the upper hand in the evolution of their industry." P-0535 at VIF0403236 (E2709) (quoted by

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[64]The district court declined to decide whether the exclusionary rules could properly be evaluated under a "quick look" analysis, which would permit a court to dispense with elaborate proof of their anticompetitive effects on the ground that "'the great likelihood of anticompetitive effects [from the restraint at issue] can easily be ascertained.'" Op. 344 (brackets inserted by district court) (quoting *California Dental Ass'n v. FTC*, 526 U.S. 757, 770-71 (1999)) (SPA180). The court explained that the parties and the court had already undertaken a "thorough analysis of the alleged restraints and their impact of the relevant markets; it would make little sense for the court to disregard any of the evidence presented." *Id.*

Op. 392 (SPA228)). The collective refusal of the Visa and MasterCard member banks to issue cards on networks not controlled by banks denies those networks access to this expertise and these assets.

Of course, independent issuers such as American Express and Discover can reach consumers without contracting with Visa and MasterCard member banks. They can use the mail or telephone, Op. 395 (SPA231), or buy a bank and have it issue cards, VUSA 50, 54. But these arguments miss the point, which is the significance of access to *multiple* and *diverse* bank issuers—the access that bank members of Visa and MasterCard have agreed collectively to reserve to bank-controlled networks and deny to rival networks. American Express and Discover may be "successful issuers," but "they cannot alone duplicate the strength and breadth of issuance and acceptance achieved by the defendants through issuance by thousands of different entities." Op. 389 (SPA225).

Visa's and MasterCard's CEOs concede that access to multiple, diverse issuers is necessary for a general purpose card network to offer network-level services effectively. *See* Selander (MC) Tr. 5611:6-5613:5 (a network cannot maintain "a viable global franchise [with only] one or two issuers") (T5283-85); *id.* at 5678:6-13 (MasterCard could not survive with just one issuer) (T5350); Pascarella (VUSA) Tr. 5224:17-5225:3 (Citibank "[a]bsolutely" needed other

bank issuers to compete as a network) (T4831-32). As the district court explained, banks can translate their specialized marketing skills into specialized and targeted products. One bank may have particular database marketing skills, another may be a master of cross-selling, or be expert in marketing to Hispanics, while another may reach rural consumers effectively and efficiently, etc.[65] No single issuer possesses all of these attributes (VUSA 43; MC 37), but with many and diverse issuers, the Visa and MasterCard *networks* do, and from that they draw enormous strength. These diverse capabilities are especially important as the effectiveness of direct-mail solicitation has waned. Op. 390 (SPA226). And the possibility of contracting with issuers not affiliated with Visa or MasterCard is not an adequate solution, for such alternative issuers "lack the expertise, experience, personnel, and reach to be effective marketers of cards." Op. 394 (SPA230).

The district court's finding that the collective denial of access to multiple bank issuers had significant anticompetitive effects is supported by detailed examples of the importance of that access. As the court found, "[m]ultiple bank issuance of general purpose cards strengthens general purpose credit and charge

[65]*See* Op. 389-91, 387 (SPA225-27, 223); P-0050 at 0714326 (in reaching rural customers, small banks provide Visa "a marketing and cost advantage over that of competing systems) (E1956); Zebeck (Metris) Dep. 25:15-26:4 (each of MasterCard's 3000 issuers has its own unique point of differentiation from other MasterCard issuers) (A809-10).

card networks in three fundamental areas: increased card issuance, increased merchant acceptance, and increased scale." Op. 387 (SPA223).

1. Increased Card Issuance

Because different banks have different skills in targeting and marketing unique card products to discrete consumer segments, acquiring "additional issuers leads to increased card issuance." Op. 387 (SPA223). The district court found that partnering with banks would increase both American Express's[66] and Discover's card output and total card output, Op. 379 (SPA215). As Visa's expert economist testified, increased output is clearly procompetitive, Schmalensee Tr. 6084:7-15 (T6102), and even share shifting from Visa or MasterCard to products consumers prefer likely enhances consumer welfare. *Id*. at 6083:21-6084:15 (T6101-02).

2. Increased Merchant Acceptance

There is a chicken-and-egg relationship between card issuance and merchant acceptance of those cards. Op. 342 (SPA178). Merchants do not accept

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[66]Op. 387 (SPA223); Hart (Advanta) Tr. 1418:10-25 (Advanta believed it could issue over 3.5 million American Express cards) (T1132); Allen (VUSA) Dep. 313:19-314:17 (acknowledging that in absence of 2.10(e), number of American Express cards would increase) (A565-66); Golub (Amex) Tr. 2734:6-2735:14 (Banco Popular issuance of American Express cards increased number of cards beyond what American Express was already issuing) (T2298-99).

a network's cards unless they are confident that sufficient numbers of customers will want to use that card, and consumers do not want a network's card unless they are confident that merchants will accept it. Thus, "[m]erchant acceptance, and the consumer perception of merchant acceptance, is vital to a network . . . . Card features are irrelevant if consumers cannot use the card. As a result, increased merchant acceptance—and increased perception of merchant acceptance—can lead to an increase in card issuance and transaction volume." Op. 387-88 (SPA223-24).

The associations recognize that American Express is at a competitive disadvantage because its merchant coverage lags behind that of Visa/MasterCard.[67] Indeed, because one purpose of the exclusionary rules was to preserve the associations' merchant advantage, *see* pp. 14-15 & n.17 above, it is hardly surprising that the discrepancy remains. Although American Express's coverage measured by "cardholder spend" (the percentage of total card expenditures for which a current American Express cardholder could use an

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[67] *See, e.g.*, D-2596 at MC0011241 (MasterCard document noting that American Express's lower merchant acceptance "perception (and reality) . . . mak[es] the card much less attractive to the consumer") (E745); P-0067 at 1123834 (Visa document noting American Express's "Real and Perceptual Merchant Acceptance Disadvantage") (E2036); Beindorff (VUSA) Tr. 4387:11-25, 4423:1-24 ("very important" for Visa to maintain its acceptance advantage over American Express) (T4155, 4191).

American Express card) is currently 96%, Op. 388 & n.24 (SPA224), its coverage is much lower if measured in terms of the numbers of merchants that accept American Express, *id.*; M.Katz Dir. Fig. 4 (American Express accepted at only 50% of merchants that accept Visa/MasterCard in U.S.) (T3243), or in terms of consumer perceptions, *see* D-0491 at 22 (1999 perception of American Express acceptance levels still at 1996 levels, showing 95% spend coverage but only 78% perception coverage) (sealed) (CA78). To attract additional cardholders, American Express will have to break into "new industries" and focus on signing smaller locations (D-4119 at AX4006-10 (E1586-90)); after already reducing its merchant discount, further reductions will not significantly improve the situation. Golub (Amex) Tr. 2714:16-2720:8 (T2278-84); Op. 388 (SPA224). Moreover, as the court found, smaller merchants will not accept American Express *even at interchange rates below Visa/MasterCard* until these merchants see more people carrying the card. Op. 388 (SPA224).

Discover also faces a significant merchant acceptance gap. Despite having the lowest merchant discount rate of the four major networks, Discover is accepted at only 90% of the merchants that accept Visa or MasterCard in the United States. Op. 388 (SPA224) (citing Nelms (Discover) Tr. 2981:12-2982:10 (T2539-40)). MasterCard describes this gap as "near merchant parity" (MC 28 n.8), but its own

bank dedication agreements belie this characterization. *See* D-2555R at CMB013617, § 4.2(F) (granting Chase a right to terminate its dedication agreement if MasterCard's global merchant acceptance trails Visa's by more than 7.5%) (E718). Moreover, consumers perceive Discover's acceptance to be even lower. Op. 388 (SPA224). To increase merchant acceptance, it "needs more card issuance and transaction volume, which can only realistically be obtained via third-party issuers, to become a more relevant network." Op. 389 (SPA225) (citing Nelms (Discover) Tr. 2982:11-2984:21 (T2540-42); Heasley (VUSA) Dep. 12:19-21 (increased cardholder base makes it easier to increase merchant acceptance) (A687)).

3. Increased Scale

"Multiple issuers provide networks with the scale, and, in turn, the relevance that they require to be strong competitors. . . . As Charles Russell, former CEO of both Visa U.S.A. and Visa International, explained, scale drives the card network business and lowers network costs, thereby increasing the networks' ability to offer services at lower, competitive prices." Op. 389 (SPA225) (citing Russell (VUSA) Dep. 39:20-40:22 (A786)). Visa's and MasterCard's owners/issuers' collective refusal to deal with American Express and Discover limits those networks' ability to increase their scale.

Appellants contend that American Express and Discover are already "at efficient scale." VUSA 38; MC 16, 31. But growing those networks nevertheless would reduce their costs and strengthen them as competitors, Op. 389 (SPA225), just as Visa and MasterCard are constantly trying to increase scale further so as to lower network costs. *See, e.g.*, Pascarella (VUSA) Dep. 136:16-21 (A771).

4. Access To DDA Accounts

Checking accounts ("demand deposit accounts" or "DDAs") are one of the reasons that access to multiple bank issuers is critical to effective competition in network services. Roughly 90% of U.S. families "have at least one checking account," and "consumers view the DDA as their primary financial relationship." Op. 392 (SPA228). "Visa and MasterCard member banks are the custodians of the vast majority of these accounts." *Id.* The district court found that "[b]ank access to DDA accounts is of competitive significance for two distinct reasons: (1) a network that is able to utilize debit accounts has a link to the next generation of payment devices for which the debit account will be the 'core' payment service; and (2) a network with the ability to provide debit products (particularly off-line debit) gains economies of scale by running additional products over the same network facilities." *Id.*

a. Next-Generation Cards

A bank with DDAs can offer its customers a link to those accounts by issuing them debit cards. Visa and MasterCard "have stressed the importance of the DDA as the primary relationship that a bank has with the consumer," and "view debit cards as the 'portal' to chip-based 'relationship' cards." Op. 392 (SPA228); P-0547 at VIF0598559 ("the road to chip is debit as debit is the core link with the consumer") (E2759); P-0064 at 1073804 ("[t]his migration will be led through debit") (E1999); Lockhart (MC) Tr. 2019:2-2020:6 (MasterCard global strategy since the mid-1990s has presumed that chip-based debit cards would be the "primary access tool" for cardholders) (T1702-03).

"Through a single multi-function chip card, defendants intend that issuers will be able to provide their customers the ability to access credit *and* debit accounts, as well as offering other features such as 'sophisticated loyalty schemes.'" Op. 392 (SPA228) (citing testimony and documents). Visa claims the court found (Op. 347 (SPA183)) that there is no "business case" for smart cards, VUSA 49, but that finding related only to the associations' business decision in the 1980s. And appellants' contention (VUSA 49, 53-54; MC 35-37) that relationship cards do not yet exist simply points to the need for competition. Consumers demand smart and relationship cards, and Visa and MasterCard

continue to include such cards in their plans.[68] Because these next-generation cards depend on DDAs, banks are in the "best position" to offer the products to consumers.[69] "By forbidding their member banks from issuing competitors' general purpose cards, defendants' exclusionary rules thus foreclose the competitive threat that American Express and Discover otherwise might pose to that relationship card strategy." Op. 392-93 (SPA228-29) (citing Beindorff (VUSA) Dep. 307:10-309:4 (A583-84); P-0819 at VU1367107 (American Express's partnerships with banks would represent "a clear threat to Visa's Relationship Card strategy") (E3363); P-0067 at 1123830 (E2032)).

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[68]*See, e.g.*, Williamson (VINT) Tr. 5396:1-21 (Visa International estimate that by 2009, multi-function cards will account for about 80% of global card volume) (T5000); McEwen (VUSA) Dep. 29:2-17, 33:3-34:7 (VUSA's smart card strategy "still today" includes providing consumers a single card that accesses the cardholder's debit *and* credit accounts) (A749, 750-51).

[69]Op. 392 (SPA228) (citing Williamson (VINT) Tr. 5394:18-23 (T4998); Tallman (VUSA/VINT) Dep. 161:7-162:2 (A782); P-0535 at VIF0403236 (banks "have the upper hand in the evolution of their industry") (E2709)); *see also* Op. 391 (banks "issue significant numbers of cards to their retail bank customers") (SPA227) (citing Beindorff (VUSA) Dep. 174:19-175:6 (20% of outstanding Visa cards issued by banks to their DDA customers) (A577)); P-1269 at VU0264998 (banks possess "[c]ompetitive [a]dvantages" in provision of multi-function chip cards) (E4462); P-1265 at VU0592760-61 (Visa report explaining that banks are "valuable partners" in chip card development because they "own the payment cards" and possess "card management expertise" and "relationships through their corporate and commercial banking groups") (E4442-43).

b. Increased Scale

American Express and Discover's preclusion from the market for multi-function cards further restricts their ability to achieve scale economies. Offline debit transactions run over the same network as credit and charge transactions, "the addition of debit volume improves network economies of scale and increases network relevance. In addition, debit functionality makes a network more attractive for consumers and banks desiring a range of products over a single brand or card." Op. 394 (SPA230). Because of the expected growth in relationship chip cards, which can combine credit, debit, and a variety of other products as the issuer and network see fit, the "inability to provide debit functionality on a cost-effective basis further limits the effectiveness of American Express and Discover *as suppliers of credit and charge card network services*." *Id.* (emphasis added) (SPA230) (citing Nelms (Discover) Tr. 2996:12-2997:9 (T2254-55); Rothschild (Amex) Tr. 2613:3-2614:15 (T2179-80)).

c. Denying Rival Networks Access To Issuers Who Control DDAs Restricts Network Competition

Appellants assert that, even if relationship cards represent the future of general purpose cards, the exclusionary rules do not limit their potential. They contend that American Express is not currently precluded from offering multi-

function cards and that its failure to offer them stems from its disinterest. VUSA 54; MC 36. This argument lacks merit. Indeed, appellants ignore the fact that American Express already offers cards through banks outside the United States (where the exclusionary rules do not apply) that combine a credit and debit function. *See* Rothschild (Amex) Tr. 2635:7-2636:24, 2667:2-23 (describing multi-function cards in Czech Republic, Singapore, and Australia) (T2201-02, 2231); Cracchiolo (Amex) Tr. 1495:14-1498:9, 1500:8-23, 1595:1-25 (same) (T1209-12, 1214, 1294).

MasterCard simply distorts the record in asserting that American Express has disclaimed interest in issuing a card combining credit and debit functionality. MC 36 (citing Rothschild (Amex) Tr. 2669:24-2670:5 (T2233-34)). In the testimony upon which MasterCard relies, Rothschild was commenting on the makeshift "debit on charge" product—using the ACH network for debit authorization and settlement—that American Express considered because it could not contract with banks to issue cards. Rothschild (Amex) Tr. 2707:7-2708:14 (T2271-72). This strategy is not viable in part because ACH is an "inferior system." Op. 393 (authorization through ACH has unacceptable processing delays and provides consumers with "only limited transaction information") (SPA229). Accordingly, American Express "wouldn't even be considering a product like

debit on charge" if the exclusionary rules were lifted because they would then be able to form relationships with banks and offer comparable debit products to Visa's and MasterCard's. Rothschild (Amex) Tr. 2669:24-2670:5 (T2233-34). *See also* Nelms (Discover) Tr. 2994:2-2996:11 (Discover determined that offline debit not viable without access to banks' DDA accounts) (T2552-54).

C. The Anticompetitive Effects Of The Rules Are Felt At Several Levels

The district court found that enhanced network-level competition would benefit not just American Express and Discover, but also merchants and—most importantly—consumers.

1. Increased Card Consumer Choice

Issuing banks view Visa and MasterCard as both suppliers of services and as partners. Consumers benefit when multiple networks compete for banks' business because such competition stimulates the networks to offer more competitive products and services. Schmalensee Tr. 6019:7-6020:12 (T6037-38). But for the agreement among member banks not to partner with American Express or Discover, consumers could expect lower prices and better service.

Appellants question whether decreased network prices or improved network services would ultimately benefit consumers (VUSA 48 n.17; MC 38-40), but

there is no basis for special tolerance of conduct restraining competition in upstream or input markets. "In the long run consumers will benefit when upstream as well as downstream markets are made more competitive. The overall impact of noncompetitive upstream prices is that downstream firms will have higher costs, and even in competition they will charge higher prices." PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW ¶ 916, at 93 (Supp. 2002) (discussing upstream mergers); *accord FTC v. H.J. Heinz Co.*, 246 F.3d 708, 719 (D.C. Cir. 2001) ("the antitrust laws assume that a retailer faced with an increase in the cost of one of its inventory items 'will try so far as competition allows to pass that cost on to its customers in the form of a higher price for its product'") (quoting *In re Brand Name Prescription Drugs Antitrust Litig.*, 123 F.3d 599, 605 (7th Cir. 1997)).

Moreover, because "cardholders believe there are differences among credit card brands, many issuers want to be able to deliver them a brand choice . . . to satisfy consumer demand." Op. 395 (SPA231) (citing Boudreau (Chase) Tr. 2071:23-2072:19 (T1726-27); Schmalensee Tr. 6064:4-6 (T6082)). Issuers "recognize that the combination of banks' knowledge and features with network

features and brand preference yields customer value." *Id.*[70] Indeed, in 1993 Visa sought to garner more business from its dual members by differentiating its services from MasterCard's and telling members that banks "will be able to combine their own marketing strategies with the *capabilities of their chosen system* to create both more real and more easily perceived differences in the marketplace." P-1176 at V052280 (emphasis added) (E4111). This is so because banks are "not merely distributors of commodity products such as 'spices or ice cream.' A card issuer, rather, 'actually determines the main characteristics of the card which it puts on the market (in competition with the other issuers)'" Op. 395 (SPA231) (quoting B.Katz (VUSA/VINT) Tr. 3137:9-3138:1 (T2684-85)). Thus, it is true but irrelevant that American Express or Discover can mail a card application to anyone in the United States. *Cf.* VUSA 41; MC 18, 22, 27. American Express and Discover as networks have different strengths and weaknesses than Visa or MasterCard, and banks could mix and match their own

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[70]*See also* Zebeck (Metris) Dep. 146:22-147:11 ("if you can match the right product with the right price to the right individuals, they will perform more profitably for you. . . . [T]hat's why we issue MasterCard and Visa cards . . ., because each brand performs differently and the profit dynamics are different in each brand") (A839-40).

strengths and capabilities with American Express's or Discover's and create new cards for consumers. Op. 395-96 (SPA231-32).[71]

The district court illustrated this fundamental point with a specific example: "Blue from American Express" (Blue). *See* Op. 397-98 (SPA233-34). Blue, introduced in 1999, has both a traditional magnetic stripe and an integrated circuit that could provide multi-applications. "While this limited function is currently 'marginal,' Blue offers a platform and an operating system that allows applications to be developed and downloaded to the chip for widespread use by millions of consumers." Op. 397 (SPA233). The chicken-and-egg problem appears again, however, as "software developers have no incentive to write applications for a piece of hardware that does not have wide distribution." *Id.*; *see also Microsoft*, 253 F.3d at 55 (describing chicken-and-egg problem for operating systems).

"Absent the exclusionary rules, American Express would make the smart card feature available to banks that issue on the American Express network," the district court found, and banks are in fact interested in working with American Express "to issue the card and provide innovative features." Op. 397 (SPA233).

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[71]*See also* McCurdy (Amex) Tr. 762:22-763:15, 764:14-765:14, 767:4-12 (discussing bank interest in "Custom Extras" feature available on American Express network but not the Visa or MasterCard networks) (T557-58, 559-60, 562).

Moreover, multiple bank issuance "would greatly enhance both the *functionality and scale* of the Blue card. . . . Multiple issuers would offer a variety of features designed to appeal to different consumers, maximizing the benefit of a multi-application card." Op. 397-98 (emphasis added) (SPA233-34).[72] "The mass deployment of bank issuing resources would improve the scale economies of smart card issuance. . . . Should the 'Blue' smart cards continue to proliferate, particularly via multiple bank issuers, consumers will benefit because increased functionality will result from increased scale." Op. 398 (SPA234). These scale effects, in turn, potentially would feed network effects on the demand side, further expanding the networks.

Visa argues that there is no need for bank issuance of Blue because bank issuance of Visa's smart cards, which use the same technology, can solve the chicken-and-egg and scale problems equally well. VUSA 53. But it is for the market, and not private agreements among competing issuers, to determine the pace, extent, and qualities of smart card development. *See Indiana Dentists*, 476

[72]Op. 398 (SPA234) (citing P-0836 (Visa believes its vast membership can "develop 'one dozen solutions'" to each one created by American Express, and that its members can use those "solutions" to customize smart cards for the particular customer segments they serve) (E3396, 3400); Knox (VUSA) Tr. 4819:5-20 (T4449); P-0840 at VU1603610-11 (describing Visa's advantage in responding to Blue) (sealed) (CA103-04)).

U.S. at 462 (defendant "not entitled to pre-empt the working of the market by deciding for itself that its consumers do not need that which they demand"); *Professional Engineers*, 435 U.S. at 695 ("all elements of a bargain . . . are favorably affected by the free opportunity to select among alternative offers"). There are opportunities for all four networks to work with banks to increase the smart card choices for consumers, thereby greatly enhancing the competitive vitality of the program. *See* Op. 398 (SPA234). American Express likely would develop different applications than Visa or MasterCard; banks working with American Express could well issue smart cards with different features than banks working with Visa. Consumers would benefit from the ability to choose among alternatives. "In short, the evidence is clear that multiple issuer networks provide the best competitive means for consumers to obtain the long-recognized benefits of smart cards." Op. 398 (SPA234).

2. Increased Competition For Rates Charged Merchants

The district court found that merchants also would benefit from increased network-level competition. Op. 396 (SPA232). Merchants have an interest in having interchange pricing set competitively, and "enhanced competition from American Express and Discover would likely cause defendants to be more responsive to the interests of merchants." *Id*.

Appellants speculate about what will happen to interchange rates—and the attendant consequences—if their members issue American Express cards. VUSA 46-48; MC 39. But network providers consider a variety of factors when setting interchange rates, as do merchants in deciding which cards to accept.[73] Visa's expert acknowledged the difficulty in analyzing the effects on consumer welfare of changes in interchange rates. Schmalensee Tr. 5982:17-5983:15 (T6000-01). The court reasonably concluded that "merchants—and ultimately consumers—have an interest in the vigor of competition to ensure that interchange pricing points are established competitively." Op. 396 (SPA232). American Express has lowered its discount rate to open up new merchant categories in the past, Golub (Amex) Tr. 2719:11-2720:22 (T2283-84), and it may elect to do so in the future. In any event, there is no reason to permit a private agreement among issuers to deny merchants and others the prospect of vigorous competition among providers of network services. *See Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 4-5 (1958) (Sherman Act "rests on the premise that the unrestrained interaction of competitive

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[73]Appellants assume (VUSA 43, 47-48; MC 39) American Express can attract issuers only by offering high interchange rates. In fact, the district court found that American Express and Discover offer other features and services that issuers find attractive, including the wealth of data that flows from those networks' closed-loop systems. Op. 395-96 (SPA231-32).

forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress”).

D. Enhanced Network-Level Competition Would Spur The Associations

A more-competitive network market not only would bring better products and services from American Express and Discover, but, as the district court found, “would also cause Visa and MasterCard to respond to the greater network competition by offering new and better products and services of their own, thereby benefitting consumers.” Op. 396 (SPA232). In fact, the record repeatedly demonstrates that even the possibility of competition by American Express or Discover has spurred competitive responses from Visa and MasterCard.

American Express’s initial overture to banks in 1996 caused MasterCard to “‘speed up’” its development of a premium card product, and “to consider partnering with a travel agency to compete with American Express.” Op. 396 (SPA232) (citing Lockhart (MC) Tr. 1998:21-1999:7 (T1681-82); P-0277 at MC6383 (E2420)). Similarly, a Visa International Competitive Assessment cautions that Visa must “proactively strengthen” its product offerings with member banks in response to actual and potential American Express partnerships with member banks, and that “Visa needs to monitor the situation and counter with

competitive products that meet banks needs." Op. 396-97 (SPA232-33) (quoting P-0575 at VIF6008245 (E2761)).

Similarly, American Express's arrangements with foreign banks (unaffected by the exclusionary rules) caused Visa and MasterCard to "react[] competitively." Op. 398-99 (SPA234-35). For example, after declining to adopt a 2.10(e)-equivalent, the Visa European Region Board "directed that Visa compete aggressively by making sure that members could offer a 'full range of competing products.'" Op. 399 (SPA235) (quoting P-0667 (E3005-64)); *see also* P-1192 (describing responsive competitive initiatives) (E4217-25); P-0668 (discussion of competitive initiatives) (E3065-91). Visa management "responded with a number of significant initiatives offered to member banks specifically to reduce their incentive to partner with American Express. . . . These included, among others, permission for multi-national corporate cards, increasing network support for the Visa premium product, and improving service to merchants." Op. 399 (SPA235) (citing P-0238 (E2391-96)).[74] The district court found that MasterCard also

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[74] *See also* P-0546 at VIF0596089 (stressing need for premium Visa product in Europe to respond to American Express) (E2748); Somerville (VINT) Dep. 79:20-82:20 (citing need to improve commercial card infrastructure to compete with American Express) (A804-06).

"responded to American Express on the international level." Op. 399 (SPA235) (citing P-0467 (E2594-2700)).[75]

Visa has also responded competitively when rival networks sought to increase merchant acceptance. For example, Visa was so concerned about the potential volume loss at Wal-Mart when that merchant began accepting the Discover card that Visa offered promotional support to Wal-Mart for the first time. Op. 396 (SPA232).

As the district court found, competition forces all four network competitors—not just the two heretofore excluded—to produce better products at lower prices. Visa and MasterCard sought to reduce that competitive pressure through the exclusionary rules; their repeal will enhance competition.

E. The Exclusionary Rules Limit The Prospects For Effective Competition From American Express And Discover

The exclusionary rules limit American Express and Discover to competing for the banks' business on an all-or-nothing basis, requiring a bank to renounce the possibility of offering its customers cards on the two dominant Visa and

[75] *See also* P-0494 at MCJ6000463 (MasterCard announcement of World MasterCard, a high-end product to be "targeted to markets where American Express is strong or making inroads" and would be introduced in select markets and expanded to other areas only "*if there is a strong need for a response to American Express franchising activities*" (emphasis added)) (E2705).

MasterCard networks (as well as their associated debit and ATM networks) as the price of doing business with American Express or Discover. *See* M.Katz Dir. ¶¶ 269-74, 299 (due to exclusionary rules, American Express and Discover face much higher costs than do the associations to obtain banks' business) (T3152-56, 3173-74). Appellants do not deny that these rules have prevented American Express from entering into agreements with banks. Nor could they. *See* Op. 383-86 (American Express would have entered into issuing agreements with certain banks but for the exclusionary rules) (SPA219-22).

Visa and MasterCard both assert (VUSA 20 n.6; MC 21 n.6), however, that banks would be uninterested in issuing Discover cards because Discover's interchange rate is too low, and that Discover would actually be hurt by the court's remedy. But the district court found that the exclusionary rules—not Discover's interchange—deterred First USA from entering into an issuing arrangement with Discover. Op. 386-87 (SPA222-23). And if appellants truly believed "that the ban would not significantly foreclose [Discover] . . . they would hardly have gone to the trouble of adopting it." *NASL v. NFL*, 670 F.2d 1249, 1260-61 (2d Cir. 1982).

In any event, appellants' insistence that Discover would be harmed by the remedy ignores Discover's view that it "fully supports" Sections III(A), (B), and

(C) of the Final Judgment, including repeal of the exclusionary rules.[76] *See* Discover's *Amicus* Comments On Proposed Final Judgment 2 (Oct. 17, 2001) (A1717). Although Discover sought additional language in the decree concerning anti-discrimination provisions, the district court found that the Final Judgment already provided the protection Discover sought. Remedy Op. 615 (SPA262). Discover's strategy is to be the low-cost competitor, offering banks other features, services, and qualities that would lead to beneficial relationships, notwithstanding its low interchange rate. Nelms (Discover) Tr. 3010:4-3011:16 (T2568-69); Op. 395-96 (SPA231-32). The market, and not an agreement among competing issuers, should determine whether that strategy succeeds.

F. *MountainWest* Is Fully Consistent With The District Court's Decision

Visa and MasterCard argue (VUSA 55-58; MC 25, 45) that the Tenth Circuit's decision in *MountainWest*, 36 F.3d 958 (10th Cir. 1994), somehow

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[76]Appellants misleadingly rely on Nelms's testimony that Discover would be harmed by the exclusionary rules' repeal because they ignore Nelms's assumption that Visa and MasterCard prohibited banks from having an equity interest in Discover. *See* Nelms (Discover) Tr. 3073:1-18 (T2631). Visa did not clarify until it commented on the proposed final judgment that no such prohibition exists. Moreover, MasterCard misstates the point as involving whether Discover could obtain equity in issuing banks, rather than banks obtaining equity in Discover. *See* MC 22 n.6.

controls this case.[77] That decision, however, addressed Visa Bylaw 2.06, which prevented Discover from becoming a member *of Visa*. The district court in this case correctly summarized *MountainWest* as holding that "[t]he value of an additional one of thousands of Visa-branded issuers to intrasystem competition did not outweigh the effects of having weakened network or brand level competition through Discover joining the Visa network." Op. 339 n.10 (SPA175).

Even if the fact findings in *MountainWest* were relevant here, there would be no logical inconsistency between them and the district court's findings as to competitive effect. Bylaw 2.06 affected *intrasystem* competition, and the Tenth Circuit held "there was no evidence the bylaw harms consumers." 36 F.3d at 971. Discover sought to issue a particular type of card as yet another issuer of Visa, but there was "no evidence . . . [Discover] needed Visa USA to develop the new card," *id.* at 972, or that one more Visa issuer would significantly enhance competition. The *MountainWest* court also determined that Visa's justification for the bylaw—

[77]Visa goes so far as to invoke, without citation, the doctrine of stare decisis. VUSA 58. That argument is meritless. The doctrine of stare decisis "is not applicable to determinations of fact," *In re Tug Helen B. Moran, Inc.*, 607 F.2d 1029, 1031 (2d Cir. 1979), which is the basis of market definition and findings of anticompetitive effects. Moreover, stare decisis "is a doctrine that binds courts to follow their own earlier decisions or the decisions of a superior tribunal." *National Org. of Veterans' Advocates v. Sec'y of Veterans Affairs*, 260 F.3d 1365, 1373 (Fed. Cir. 2001). Thus, even if *MountainWest* turned on a question of law, it would not bind this Court.

preventing free-riding on Visa's investment in its brand—was legitimate and outweighed any harm that flowed from a limitation on intrasystem competition. *Id.* at 970, 972. This case focuses on *intersystem* competition; it involves an agreement to prevent issuers from issuing cards on rival networks, not Visa's control over its own brand. And the district court rejected—on the facts—defendants' justifications for their restraints. Op. 399-406 (SPA235-42). We have no quarrel with the result in *MountainWest*, but it does not inform the analysis here.

IV. VISA AND MASTERCARD FAILED TO MEET THEIR BURDEN OF ESTABLISHING PROCOMPETITIVE JUSTIFICATIONS

Once the government established that the challenged rules had substantial anticompetitive effects, the burden shifted to Visa and MasterCard to come forward with evidence demonstrating procompetitive justifications. Op. 345 (SPA181); *Capital Imaging Assocs. v. Mohawk Valley Med. Assocs.*, 996 F.2d 537, 543 (2d Cir. 1993); 11 HOVENKAMP ¶ 1914, at 313-14. This they failed to do. Op. 406 (SPA242). Visa and MasterCard's proffered justifications were that the exclusionary rules are ancillary to the joint ventures because they foster "loyalty" and "cohesion" among the members. The district court expressly acknowledged that joint ventures "may employ reasonable restraints to make the joint venture more efficient." Op. 399 (SPA235). It carefully considered Visa and

MasterCard's claims that Bylaw 2.10(e) and the CPP are such ancillary restraints, Op. 399-406 (SPA235-42), concluding that "defendants have offered no persuasive procompetitive justification," Op. 406 (SPA242). That conclusion is entirely consistent with the record evidence, which belied defendants' claimed justifications.

Whether a restraint is ancillary is a question of fact. *Lektro-Vend Corp. v. Vendo Co.*, 660 F.2d 255, 266 (7th Cir. 1981) (applying clearly erroneous standard to ancillarity determination). To demonstrate ancillarity, appellants were required to offer more than merely plausible *theories* of how the exclusionary rules could be reasonably necessary to the procompetitive benefits of the joint ventures—they were also required to prove that their theories were validated by the facts in this case. *See NASL*, 670 F.2d at 1261; *Graphic Prods. Distribs., Inc. v. Itek Corp.*, 717 F.2d 1560, 1576 (11th Cir. 1983) ("the record must support a finding that the restraint in fact is necessary to enhance competition and does indeed have a pro-competitive effect"); *Eiberger v. Sony Corp. of Am.*, 622 F.2d 1068, 1078-79 (2d Cir. 1980) (rejecting proffered justification because "factual predicates are lacking").

A restraint is not automatically deemed ancillary simply because it is "related" (VUSA 23) to a joint venture. Such a lax standard "could protect cartels

from the heightened scrutiny attending naked restraints through the simple device of attaching the cartel agreement to some other, independently lawful transaction." 11 HOVENKAMP ¶ 1908, at 229. Rather, to be ancillary, a restraint must be *reasonably* designed to further the procompetitive aspects of the joint venture. *See, e.g.*, *NBA v. Williams*, 45 F.3d 684, 690 (2d Cir. 1995) (rule of reason "permits 'ancillary restraints' necessary to a legitimate transaction"); *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 302 (2d Cir. 1979) (look at the "reasonableness" of the restraint's "relationship to the purposes of the venture"); 11 HOVENKAMP ¶ 1904, at 203 (an ancillary restraint is an "essential or at least important part of some arrangement that has potentially redeeming virtues"); *id.* ¶ 1912, at 287 ("An ancillary restraint is one that is reasonably related to a joint venture or transaction that, at least on initial examination, promises to increase output, reduce costs, improve product quality, or otherwise benefit consumers").[78]

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[78]*See also Sullivan v. NFL*, 34 F.3d 1091, 1102 (1st Cir. 1994) (ancillary restraint is "one that is required to make the joint activity more efficient"); *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210, 224 (D.C. Cir. 1986) (not ancillary if "it is so broad that part of the restraint suppresses competition without creating efficiency"); *General Leaseways*, 744 F.2d at 595 (need an "organic connection between the restraint and the cooperative needs of the enterprise"); *Addyston*, 85 F. at 290-91 (must be "commensurate"); Robert Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division*, 74 YALE L.J. 775, 797-98 (1965) (under *Addyston*, ancillary restraints are those "subordinate and collateral to another legitimate transaction and necessary to make that transaction effective"); 11 HOVENKAMP ¶ 1908, at 227 ("to say that a restraint

Accordingly, courts have often struck down agreements (including bylaws) even though related to legitimate, procompetitive joint ventures.[79]

Visa argues that the "fragility" of the Visa and MasterCard associations makes them vulnerable to "opportunistic behavior" by "members seeking primarily to further their own individual interests." VUSA 58-62. Consequently, Visa argues, Bylaw 2.10(e) is an ancillary restraint because it "prevents opportunistic behavior that is destructive of the venture's cohesion." *Id.* at 69. MasterCard similarly argues that the CCP was a legitimate response to American Express's "announced desire . . . to 'cherry pick' select MasterCard issuers," which would "destabilize the association and reduce the incentives of other members to invest in the MasterCard brand" by allowing "'defecting' members nonetheless to avail themselves of the benefits" of the MasterCard network. MC 53. These arguments

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is truly ancillary is to conclude that a significant argument for positive output effects can be made and supported; thus further inquiry into net competitive effects is appropriate"); *id.* at 239 (restraint must be "'commensurate' with the enterprise or transaction to which it relates").

[79]*See, e.g.*, *NCAA*, 468 U.S. 85 (1984) (NCAA rule restricting schools' ability to televise football games); *Indiana Dentists*, 476 U.S. 447 (1986) (dentist trade association rule regarding providing x-rays to insurers); *Professional Engineers*, 435 U.S. 679 (1978) (professional association's bylaw regarding bidding practices); *NASL*, 670 F.2d 1249 (2d Cir. 1982) (NFL's cross-ownership rule); *Sullivan*, 34 F.3d 1091 (1st Cir. 1994) (NFL bylaw regarding public offering of team stock); *Law v. NCAA*, 134 F.3d 1010 (10th Cir. 1998) (NCAA rule regarding coaches' salaries).

are sound *as theories* but, as the district court found, the record evidence demonstrates that such theories are not factually supported.[80] As the district court concluded: "Describing American Express' motives with the pejorative term 'cherry picking' does not change the anticompetitive purpose of the rules: to restrict competition among competitor networks and banks." Op. 401 (SPA237).[81]

A. The Exclusionary Rules Do Not Maintain Members' "Loyalty"

Restraints designed to encourage members to devote their efforts to promoting a joint venture's product may be ancillary. Indeed, the government's expert economist so testified. M.Katz Tr. 3769:20-3770:15 (T3568-69). *See also Addyston*, 85 F. at 280. But in this case, the district court agreed with the analysis of the government's expert, M.Katz Dir. ¶¶ 327-50 (T3188-202), and rejected this

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[80]In the district court, Visa and MasterCard additionally argued that the exclusionary rules were ancillary because they prevent free-riding by American Express on association assets. The court soundly rejected this justification based on its findings of fact. *See* Op. 400, 404-05 (SPA236, 240-41). Appellants do not raise that free-riding justification in their opening briefs here, and hence have waived the argument. *See* p. 50 above.

[81]MasterCard argues that its procompetitive justification should be evaluated as of the time the CPP was adopted. MC 59 (citing *Polk Bros.*, 776 F.2d at 189). Even if so, the district court did not find that MasterCard enacted the CPP "for the legitimate purpose of furthering brand loyalty," MC 54 (citing Op. 374 (SPA210)). Rather, the court found that the "contemporaneous evidence shows that defendants' motives are to restrict competition at the network and issuer levels to enhance member bank profitability." Op. 401 (SPA237); *see also* p. 21 above.

proffered justification as unsupported by the record. *See* Op. 402-05 (SPA238-41).

The instant case is akin to the one this Court faced in *NASL*.[82] There, an NFL bylaw prohibited members from owning other professional sports teams. The NFL justified its rule as "assur[ing]" the NFL joint venture the "undivided loyalty" of its member clubs. 670 F.2d at 1261. While acknowledging the legitimacy of the proffered justification as a theoretical matter, this Court rejected it on the facts: "We do not question the importance of obtaining the loyalty of partners in promoting a common business venture, even if this may have some anticompetitive effect. But in the undisputed circumstances here the enormous financial success of the NFL league despite long-existing cross-ownership by some members of NASL teams demonstrates that there is no market necessity or threat of disloyalty by cross-owners which would justify the ban." *Id.*

As the district court found, the associations' concerns about loyalty ring hollow in light of their long history of successful operation despite the divided loyalties of their members, which the associations specifically sanction. The most

[82]In discussing ancillarity and joint ventures, Visa relies (VUSA 22, 25, 62) on a dissent from denial of certiorari in *NFL v. NASL*, 459 U.S. 1074 (1982) (Rehnquist, J., dissenting), rather than on this Court's unanimous decision in that case. MasterCard ignores *NASL* altogether.

obvious and material illustration is that both associations—the two dominant networks—exempt each other from their exclusionary rules.[83] This means thousands of issuers aggregating 73% of the market as measured by transaction volume (85% measured by cards issued), Op. 341 (SPA177), have their loyalties divided between Visa and MasterCard. Appellants tout their recent history of dedication programs, *see* Op. 368-70, 403 (SPA204-06, 239), but neither association insists on exclusivity even under such agreements (though member banks still are not free to offer American Express or Discover on the uncommitted portion) or even requires issuers to enter into such agreements.[84]

Moreover, both associations exempt certain proprietary networks from their exclusionary rules. Citicorp, the largest issuer of association cards,[85] is free to own and be the sole U.S. issuer on the Diners Club network, Op. 379 n.19, 371

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[83]*See also* pp. 13-14, 20 above.

[84]Indeed, two large issuers with representatives on MasterCard's U.S. Region board have not signed dedication agreements with either association. MC 84-85; Op. 371 (SPA207). In addition, at the time the Complaint was filed, Providian had a representative on MasterCard's board despite having a card portfolio skewed 90% to Visa. Op. 375 (Providian on MasterCard board) (SPA211); D-3350 at MCJ4369364 (90% skew) (E1177).

[85]Citicorp was the largest single issuer of Visa cards but, after signing a dedication agreement with MasterCard in 1999, committed to convert 85% of its Visa card portfolio to MasterCard by March 2002. P-0165R at CC024533, CC024535 (E2193, 2195).

(SPA215, 207), even though "at the time By-law 2.10(e) was passed, the worldwide volume on the Diners Club and Discover networks were about equal." Op. 380 (SPA216). Similarly, both exclusionary rules exempt issuance of JCB cards, despite the fact that one association member, Household, obtained exclusive rights to issue JCB cards in the United States.[86]

The associations (VUSA 68-72; MC 56-58) argue that divided loyalties have a different effect when American Express or Discover is involved.[87] But, as the district court found, "there is no evidence as to why it would be any more opportunistic for American Express to offer a deal to a large issuing bank than it is for MasterCard to offer a special deal to a Visa bank." Op. 403 (SPA239).

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[86]MasterCard contends that Diners and JCB are "not considered competitively significant." MC 58 n.19. But the CPP expressly assumes just the opposite: Visa, Diners, and JCB are exempted *despite* being "competitive general purpose card programs." *See* pp. 16-17 above. Moreover, MasterCard's contention merely restates the conclusion, because the MasterCard board subjectively determines what rival networks are "competitively significant" and, hence, whether the CPP applies.

[87]Visa also argues that the exemption for MasterCard is an historical anomaly that it would have preferred to avoid. VUSA 68-70. MasterCard, however, does not share Visa's perspective. *See* Op. 346-47 (SPA182-83). And Visa has chosen to tolerate the "anomaly" over the years (its member/owners have the power to change it)—and to allow other exceptions from Bylaw 2.10(e). Visa suggests (VUSA 72) that the associations appropriately treat each other differently from American Express and Discover because they, and not American Express and Discover, are not-for-profit associations. But Diners Club and JCB are proprietary networks, yet both Bylaw 2.10(e) and the CPP exempt them.

Indeed, Visa hypothesizes (VUSA 74-76) that American Express might destabilize the Visa association by luring away its largest issuer of corporate cards, yet MasterCard's corporate card program survived when Visa "enticed Wells Fargo to sign a Partnership Agreement even though Wells was one of MasterCard's top three corporate card issuers." Op. 404 (SPA240) (citing Selander (MC) Tr. 5617:12-5618:6 (T5289-90)).

Visa and MasterCard's primary rationale for treating each other differently from American Express/Discover is that the associations are both "open" joint ventures, whereas American Express and Discover will choose which banks issue their cards. Under the theory articulated by Visa's expert, Prof. Gilson, "a 'self-enforcing mechanism' limits opportunistic behavior between the associations, but not between the associations and their closed, for-profit competitors." Op. 402 (SPA238); *see also* VUSA 70-71; MC 56-58. The district court openly questioned Prof. Gilson's credibility and qualifications, but "[m]ost importantly," found that his testimony was "belied by the uncontradicted record evidence." Op. 402 (SPA238).

Professor Gilson's "self-enforcing mechanism" depends on the ability of issuers to shift resources between the associations to "share collectively in any single issuer's attempted opportunistic behavior," which they cannot do if an

American Express-issuing bank acts "opportunistically" because, by hypothesis, most member banks would not have issuing agreements with American Express. *See id.* The district court recognized, however, that the associations' move toward dedication agreements limits the extent to which contractually committed issuers can shift from one association to the other, and thereby undermines the supposed self-enforcing mechanism. *Id.* MasterCard argues that the dedication agreements represent an alternative to the self-enforcing mechanism (MC 58-60), but, in fact, the two work at cross-purposes. To the extent most large issuers have dedicated themselves to one association, "they demonstrate that association members are willing to voluntarily sign agreements which deny them the ability to counteract the opportunistic behavior that the rules ostensibly combat." Op. 402 (SPA238).

In short, the exclusionary rules do not say "You're with us or you're against us" (VUSA 22), but rather "You're with us . . . or our largest competitor . . . or a network controlled by an important member . . . or you're against us." Visa and MasterCard may indeed prefer that member banks exhibit "loyalty" by not choosing rival network services and not competing to offer cards that consumers might find more attractive. But the record does not support their claim that permitting members to issue cards on rival networks would substantially undermine the joint ventures' ability to compete.

B. Defendants Did Not Demonstrate That Member Issuance Of American Express Or Discover Cards Will Undermine The Associations' "Cohesion"

Visa and MasterCard contend that the exclusionary rules are reasonably necessary to maintain the associations' "cohesion" and prevent American Express or Discover from "destabilizing" the associations. Such arguments are not new. In *NASL*, this Court recognized that damage to or losses by even one league member could "adversely affect the stability, success and operations of other members." 670 F.2d at 1253. Nevertheless, this Court held that the NFL's justification for its bylaw failed on the facts. *Accord FMC v. Aktiebolaget Svenska Amerika Linen*, 390 U.S. 238, 250-51 (1968) (rejecting similar justification for shippers' conference prohibiting its authorized travel agents from also selling tickets on non-conference ships, because factfinder "found no indication . . . that elimination of the rule would in fact jeopardize the stability of the conference"). That same focus on the lack of evidentiary support for defendants' claims led the district court to reject defendants' "cohesion" justification on this record.

Appellants argue that American Express's overture to the member banks was intended to subvert the associations and that bank issuance of American Express or Discover cards would undermine the cohesiveness of their "fragile" associations. The contemporaneous evidence, however, does not support the

associations' current claim that they acted out of fear of destabilization; rather, the record reflects that the associations enacted the exclusionary rules merely to eliminate or weaken the competitive threat that American Express posed and to prevent some banks from gaining a "competitive advantage" over other banks in the association. Op. 400-01 (SPA236-37); *see* pp. 13-21 above.

Moreover, the district court found abundant historical and contemporaneous evidence of the associations' disparate treatment of their own members without loss of cohesion. For example, there is no "dissension or disruption within Visa" arising from the continued presence of large, non-dedicated members, such as MBNA, despite the fact that most major issuer/members are now dedicated to one association. Op. 403 (SPA239) (citing Pascarella (VUSA) Tr. 5236:15-24 (T4843); Heasley (VUSA) Tr. 5331:1-8 (T4935)). Nor has Citibank's continued membership in Visa caused divisiveness or loss of cohesion despite the fact that it is the largest issuer of association general purpose cards (Op. 379 n.19 (SPA215)), has committed to dedicating itself to MasterCard, and continues to control Diners Club. Op. 403 (SPA239) (citing Pascarella (VUSA) Tr. 5232:11-17 (T4839); Heasley (VUSA) Tr. 5332:6-21 (T4936); Schmalensee Tr. 6049:2-6050:16, 6065:17-6066:10 (T6067-68, 6083-84)).

Most importantly, the district court found "overwhelming" evidence that the associations' special deals that conferred competitive advantages on select members "did not cause disruption" within the associations. Op. 403 (SPA239) (citing Schmalensee Tr. 6070:3-17 (T6088)). Over the years and continuing today, the associations have paid hundreds of millions of dollars in incentive payments and provided product development assistance to select members. In the early 1990s, these payments were made to induce select large member banks to favor one association in that member's mail solicitations to consumers, Op. 367-68 (SPA203-04), even though such payments "did not offer new value to cardholders or to the association." Op. 368 (SPA204). In addition, as part of some of those dedication agreements, Visa and MasterCard work closely with individual members to develop new products that will give those members a competitive advantage over sister members.[88] As a whole, the associations have dedication agreements "with virtually all of the largest issuers, controlling more than half of all card issuance, . . . and their terms are not shared with other members of the cooperative." Op. 403 (SPA239); Knox (VUSA) Tr. 4833:18-23 (sealed) (CA23); Heasley (VUSA) Tr. 5324:5-21 (board members not privy to amount of payments

[88]*See, e.g.*, Knox (VUSA) Tr. 4825:7-4834:15 (sealed) (CA15-24); Saunders (Fleet) Tr. 2249:10-2257:5, 2255:11-2256:6, 2256:25-2257:5, 2259:15-2260:1, 2261:12-15 (sealed) (CA6-14, T1879-82).

to individual members) (T4928); Dahir (VUSA) Tr. 4611:17-4612:1 (T4352-53) (same).

The associations also permit Household and Citicorp to issue cards that no other member can, thereby conferring a competitive advantage on these select members. Visa also has maintained two classes of members since 1992, with "charter" members retaining governance rights, and newer, "non-charter" members having no such rights and paying higher fees. Op. 402-03 (SPA238-39) (citing P-1164 at VISA2401 (E3870); P-1175 at V040364 (E4044); Heasley (VUSA) Tr. 5342:7-16 (T4946)). MasterCard has a two-tiered membership as well. *See id.* (citing Selander (MC) Tr. 5717:1-22 (T5385)). Thus, the associations provide cash, discounts, special products, and other differential treatment to select members, yet justify their exclusionary rules by the supposed need to prevent American Express from engaging in the same conduct. The district court surely was justified in concluding that this "inconsistency cannot withstand scrutiny." Op. 404 (SPA240).

Nor is there any reason to believe that bank issuance of American Express or Discover cards will introduce disloyalty or loss of cohesion any more than does the current practice of dual issuance. Member banks have a "long history" of dealings with American Express in the United States (including issuance of lines

of credit to American Express cardholders and selling American Express travelers checks), without loss of cohesion among members. *See* Op. 403 n.27 (citing evidence) (SPA239). The story is even more forceful outside the associations' self-defined U.S. Regions. Banco Popular's issuance of American Express cards in Puerto Rico[89] "has caused no disruptive effect."[90] And many member banks issue American Express cards abroad,[91] yet representatives from Visa USA,

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[89]Although Puerto Rico is a United States territory, both Visa International and MasterCard include Puerto Rico in non-U.S. regions. *See* Op. at 375 (SPA211); D-4659 at 70 (E1806) (Puerto Rico in each association's respective Latin America-Caribbean Region). Thus, Bylaw 2.10(e) and the CPP do not apply to member banks in Puerto Rico.

[90]Op. 404 (SPA240) (citing Schmalensee Tr. 6082:3-11 (T6100); Gilson Tr. 5901:8-20 (T5611); Kesler (Banco Popular) Tr. 173:8-11, 190:19-191:2 (T27, 44-45)).

[91]Visa and MasterCard criticize the district court's use of foreign evidence. VUSA 64-66; MC 40-41. Although Visa moved to exclude foreign evidence at trial, the district court never expressly ruled on the motion. The district court, however, did cite foreign evidence in its opinion to demonstrate that defendants reacted competitively to American Express's initiatives, and as further evidence dispelling defendants' proffered procompetitive justifications. The district court's use of the foreign evidence, and its entry of a final judgment inconsistent with defendants' motion to exclude, constitutes a denial of Visa's motion. *See Mosier v. Federal Reserve Bank of N.Y.*, 132 F.2d 710, 712 (2d Cir. 1942).

A district court's evidentiary rulings are reviewed for abuse of discretion and are not reversed unless "manifestly erroneous." *General Elec. Co. v. Joiner*, 522 U.S. 136, 141-42 (1997). The standard of review is at its most deferential in bench trials because judges are skilled at assessing the reliability of evidence. *Microsoft*, 253 F.3d at 100-01. Further, appellants must show that they have been

MasterCard, and Visa International all testified that such issuance had caused no "disruption" or loss of "cohesion."[92] Moreover, "both Visa and MasterCard knowingly continue to have banks that issue American Express serve on their Regional, and even International, Boards."[93] Appellants have not shown how mere bank issuance of American Express or Discover cards in the United States could diminish cohesion within the associations, if such presence on the *boards* by American Express-issuing members does not.

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substantially prejudiced by reliance on inadmissible evidence. "[I]n bench trials, the admission of incompetent or irrelevant evidence is not a ground for reversal when there is sufficient competent evidence to support the judgment and it does not appear that the court was induced by . . . [inadmissible] evidence to make essential findings that it otherwise would not have made." *Greater Kan. City Laborers Pension Fund v. Superior Gen. Contractors, Inc.*, 104 F.3d 1050, 1057 (8th Cir. 1997) (internal quotation omitted); *see also United States v. Matlock*, 415 U.S. 164, 176 (1974). The district court's references to evidence of Visa's and MasterCard's procompetitive responses to bank issuance of American Express cards, Op. 396-97, 399 (SPA232-33, 235), as well as the lack of any adverse effects of such behavior on cohesion, Op. 404 (SPA240), were entirely logical and reasonable uses of that evidence and certainly well within its broad discretion in this bench trial. *See Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 604 n.30 (1985) (comparing defendant's practice in Colorado to its practice in Canada and Europe).

[92]*See* Selander (MC) Tr. 5625:3-18 (T5297); Heasley (VUSA/VINT) Tr. 5334:1-17 (T4938); Williamson (VINT) Tr. 5380:4-23 (T4984).

[93]*Id.* (citing Kesler (Banco Popular) Tr. 173:8-11 (T27); Partridge (VINT) Dep. 34:21-35:8, 38:15-20 (A763); Cullen (VINT) Dep. 71:2-23, 75:21-77:5 (Visa International executive did not hesitate to name American Express issuer to Visa executive committee in Turkey) (A632-33)).

In sum, it was not enough for Visa and MasterCard to assert that the exclusionary rules encouraged "loyalty," or even to advance plausible theories as to why loyalty provisions might contribute to the "cohesion" of the joint ventures. Rather, it was their burden to come forward with evidence demonstrating that these particular rules were reasonably necessary to maintain loyalty and cohesion and thereby preserve the joint ventures' ability to compete effectively. The district court found that the evidence did not support their claimed procompetitive justifications and, given the substantial anticompetitive effects of the exclusionary rules, found those rules to violate Section 1 of the Sherman Act. The record strongly supports those findings, which should be affirmed.

V. THE DISTRICT COURT DID NOT ABUSE ITS DISCRETION IN FASHIONING RELIEF

"The District Court is clothed with 'large discretion' to fit the decree to the special needs of the individual case." *Ford Motor Co. v. United States*, 405 U.S. 562, 573 (1972); *accord International Salt Co. v. United States*, 332 U.S. 392, 400-01 (1947); *George Basch Co. v. Blue Coral, Inc.*, 968 F.2d 1532, 1542 (2d Cir. 1992) ("the contours of an injunction are shaped by the sound discretion of the trial judge"). The "determination of the scope of the decree . . . is peculiarly the responsibility of the trial court," *United States v. United States Gypsum Co.*,

340 U.S. 76, 89 (1950), and so long as "the findings of violations are sustained," appellate courts "will not direct a recasting of the decree except on showing of abuse of discretion." *United States v. Crescent Amusement Co.*, 323 U.S. 173, 185 (1944). "[O]nce the Government has successfully borne the considerable burden of establishing a violation of law, all doubts as to the remedy are to be resolved in its favor." *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316, 334 (1961).

A trial court "has the duty to compel action" that will "cure the ill effects of the illegal conduct, and assure the public freedom from its continuance." *Gypsum*, 340 U.S. at 88; *accord National Soc'y of Prof'l Eng'rs v. United States*, 435 U.S. 679, 697 (1978); *du Pont*, 366 U.S. at 326; *International Salt*, 332 U.S. at 401. The district court found that Visa's and MasterCard's exclusionary rules "decreased network-level competition," resulting in "fewer and less varied credit card products to the consumer." Op. 379 (SPA215). To "cure the ill effects" of these unlawful exclusionary rules, the district court properly fashioned relief with two basic components: repeal of the exclusionary rules themselves and a transition period during which members are permitted to terminate "dedication agreements" entered into by Visa and MasterCard with many of their member banks, which otherwise would lock a large majority of card issuing volume into

the Visa or MasterCard networks.[94] The court's remedy was lawful and appropriate, and MasterCard's argument that the court did not engage in sufficient process before ordering its remedy is without merit.

A. The Decree Properly Forbids Continuation Of The Unlawful Conduct

Given the district court's findings that the exclusionary rules violate the antitrust laws, Op. 379, 406 (SPA215, 242), a necessary component of relief is mandating their repeal. *Crescent Amusement*, 323 U.S. at 188 (court's "duty" is "'to frame its decree so as to suppress the unlawful practices'") (quoting *Ethyl Gasoline Corp. v. United States*, 309 U.S. 436, 461 (1940)); *id.* ("Civil suits under the Sherman Act would indeed be idle gestures if the injunction did not run against the continuance or resumption of the unlawful practice"). Visa argues, however, that various modifications of the exclusionary rules would be more appropriate.

First, Visa suggests that what "is needed here, . . . is greater brand separation, not less," so the "correct response" is not "that By-law 2.10(e) should be repealed," but rather that it should be "extended" to cover all competing

[94]At the time of trial, 439 Visa USA members, representing over 60% of its transaction volume, and several of MasterCard's largest issuers, had signed dedication agreements. Op. 368-69 (SPA204-05)

networks, VUSA 72-73, 77, presumably including MasterCard. But the *factual* premise for this suggestion—that issuance of multiple cards "reduce[s] incentives to compete at the network level"—was rejected by the district court. Op. 330 (SPA166).[95] Moreover, the court's remedy does not prohibit Visa or other networks from seeking an exclusive agreement with any issuing bank, nor does it prohibit any issuing bank from entering into such an exclusive arrangement; it simply requires defendants to compete with American Express and Discover rather than foreclose that competition by edict.

Second, Visa suggests only a limited repeal of the exclusionary rules, directed only to those specific products in which the court found American

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[95]The district court's decision on Count I, rejecting the challenge to defendants' dual governance, is consistent with this finding and the remedy ordered under Count II. The court's decision on Count I was based not only on its view that plaintiff had failed "to establish causation between dual governance and any significant blunting of brand promotion or network and product innovations," Op. 328 (SPA164), particularly in light of the "record of vigorous competition between MasterCard and Visa," Op. 363 (SPA199), but also on its observation that "dual governance is virtually at an end" in any event, Op. 329 (SPA165). The court did not find that the ability of association members (as distinct from governors) to issue multiple brands of cards should itself be condemned under the rule of reason. Rather, the district court concluded that dual issuance had been "procompetitive" and that increasing the number of network competitors would further enhance competition. Op. 330 (SPA166). The elimination of the exclusionary rules as part of the injunction entered by the court, FJ §§ III.A, III.B (SPA268), is certainly consistent with that finding. Moreover, the court's remedy permits each association to continue taking steps to promote the dedication of its governing members. Op. 330 (SPA166).

Express and Discover to be disadvantaged. VUSA 77. But the court should not attempt to regulate what products appellants' members may offer in conjunction with rival networks. Network competition should instead be allowed to proceed unfettered by restraints.

Finally, Visa suggests that its members be permitted to work with only those networks "that are (or agree to become) open to other issuers generally." VUSA 78. But, given that the district court found no basis for concern about the "opportunism" appellants believe to be associated with networks not open to all issuers, there is no basis for its suggested modification. Network competitors should be free to partner with those banks with the precise package of complementary assets they seek.

B. The Decree Properly Permits Issuers To Terminate Existing Dedication Agreements

The decree affords Visa and MasterCard member banks a limited opportunity to terminate existing dedication agreements. The court included this provision because "such agreements between issuers and Visa and MasterCard now predominate the market," so "American Express and Discover have been effectively foreclosed from a large portion of the card issuing market." Op. 408-09 (SPA244-45). The court found that merely abolishing the exclusionary rules

would not restore competition. *Id.* And the court narrowly tailored the remedy by (1) limiting the rescission provision to a two-year period, (2) allowing rescission only if a bank enters into an issuing agreement with Discover or American Express, and (3) permitting Visa or MasterCard to apply for the equitable return of any funds paid to the issuer but not yet earned under the agreement, in the event of such termination. As the court found, this remedy "is the *least* burdensome way of achieving the appropriate result under the antitrust laws." Stay Order at 3 (A1891) (emphasis in original).

MasterCard argues that the dedication agreements were neither challenged nor found to be "violations of the antitrust laws." MC 85. It is well established, however, that conduct remedies may go beyond enjoining the specific conduct proven to violate the antitrust laws. *Gypsum*, 340 U.S. at 88-89. Courts may enjoin lawful and otherwise permissible practices when necessary to correct the anticompetitive effects of unlawful conduct. *United States v. Glaxo Group Ltd.*, 410 U.S. 52, 60-63 (1973); *Professional Engineers*, 435 U.S. at 698; *United States v. Loew's, Inc.,* 371 U.S. 38, 50-51 (1962).[96] The decree should "effectively pry

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[96]Indeed, the Supreme Court has often stepped in to impose additional relief in antitrust cases where the district court's remedy did not go far enough to cure the effects of illegal conduct. *E.g.*, *Glaxo*, 410 U.S. at 64; *du Pont*, 366 U.S. at 325-35; *Gypsum*, 340 U.S. at 88-89.

open to competition a market that has been closed by defendants' illegal restraints. If this decree accomplishes less than that, the Government has won a lawsuit and lost a cause." *International Salt*, 332 U.S. at 401.

MasterCard argues that the district court was wrong to conclude that the rescission provision was necessary, because: (1) a few large issuers had not signed dedication agreements when the trial record closed; (2) the agreements are of "limited duration"; and (3) some of the agreements allow the member-issuer to issue a limited number of cards on other networks. MC 85-87. The district court, however, carefully considered and rejected the purely factual arguments MasterCard raises. The court found that as a result of the dedication agreements, "American Express and Discover have been effectively foreclosed from a large portion of the card issuing market, and will continue to be so foreclosed for the duration of those agreements." Op. 409 (SPA245). Before permitting rescission of the agreements, the court gave due consideration to their duration[97] and to the

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[97]*See, e.g.*, Op. 369 (SPA205) ("Chase's agreement with MasterCard has a five-year term"). Although Visa's standard dedication agreement contains a voidability clause, a member seeking to void its dedication agreement would be forced to return the cumulative discount it had received from Visa over the preceding two years. Dahir (VUSA) Tr. 4539:14-4540:13 (T4280-81); Heasley (VUSA) Tr. 5326:10-18 (T4930). Such a significant penalty for voiding the agreements is likely to deter its exercise.

fact that Visa and MasterCard had not yet "locked up" all of their issuing banks.[98] MasterCard emphasizes that some of its dedication agreements permit member banks to issue as much as 20% of their card portfolio on other general purpose card networks. MC 86-87. This, too, was considered by the district court.[99] MasterCard demonstrates no abuse of discretion, and having been found to have violated the antitrust laws, is not entitled to set limits on the portion of each bank's portfolio for which rivals may compete.

C. The District Court Was Not Required To Hold A Separate Hearing On the Decree

MasterCard suggests the Final Judgment should be vacated, at least in part, because MasterCard was not afforded an evidentiary hearing concerning relief. MC 85. A district court, however, has broad authority to determine its

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[98]*See* Op. 369 (noting that the two large issuers MasterCard mentions (MC 86) had not signed agreements at the time of trial) (SPA205); *see also* Op. 330 (dedication agreements have locked up "most" of the general purpose card market) (SPA166).

[99]Op. 368, 370-71 (SPA204, 206-07). *See also* Op. 370 (SPA206) (the general purpose card issuing members of Visa USA Board had committed 90% of their portfolios to Visa, and MasterCard U.S. Region Board members that had entered agreements with MasterCard had committed an average of 87% of their portfolio to it).

procedures,[100] and a decision not to hold a separate evidentiary hearing concerning remedy is reviewed for abuse of discretion, *Davoll v. Webb*, 194 F.3d 1116, 1139-40 (10th Cir. 1999). There plainly was no such abuse here.

MasterCard's brief does not identify any remedy-related disputed facts requiring a hearing, nor did its remedy filings below. Nor did any defendant ever request an evidentiary hearing concerning the remedy, before or after they reviewed the proposed decree. They should not be heard to raise the argument for the first time on appeal. *Maska U.S., Inc. v. Kansa Gen. Ins. Co.*, 198 F.3d 74, 79-80 (2d Cir. 1999).

Moreover, the defendants had ample opportunity to offer evidence related to relief. The government filed its Proposed Final Judgment and its supporting Memorandum during the trial, on August 11, 2000. Two expert witnesses for Visa USA and MasterCard's only expert witness subsequently testified concerning the proposed remedy. Gilson Tr. 5857:21-5870:5, 5929:22-5941:10 (T5567-80, 5639-51); Schmalensee Tr. 5952:20-5955:11, 6097:24-6100:16 (T5970-73, 6115-18); Pindyck Tr. 6104:23-6121:23 (T6241-58). Thereafter, defendants collectively

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[100]*See United States v. Bayless*, 201 F.3d 116, 131 (2d Cir. 2000); *Microsoft*, 253 F.3d at 100.

filed over eighty pages concerning the proposed remedy.[101] In its initial opinion, the district court instructed the parties to submit "comments and objections regarding the Proposed Final Judgment." Op. 411 (SPA247). In response, defendants submitted nearly seventy pages of comments concerning the proposed decree.[102] There was no abuse of discretion in failing additionally to order an unsought evidentiary hearing. *See American Can Co. v. Mansukhani*, 814 F.2d 421, 425 (7th Cir. 1987) (defendants not entitled to remedies hearing because they failed "to explain to the district court what new proof they would present").[103]

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[101]VUSA Remedy Memo (Aug. 18, 2000) (A843-77); MC Remedy Memo (Sept. 11, 2000) (A878-91); VINT Remedy Memo (Sept. 22, 2000) (A904-19); VUSA Response (Oct. 4, 2000) (A1668-1706).

[102]MC Comments (Oct. 17, 2001) (A1698-1706); VUSA Comments (Oct. 17, 2001) (A1682-97); VINT Comments (Oct. 17, 2001) (A1707-14); MC Reply Comments (Oct. 22, 2001) (A1723-27); VUSA Reply Comments (Oct. 23, 2001) (A1728-34); VUSA Response To Amex (Oct. 29, 2001) (A1741-57); VINT letter (Oct. 29, 2001) (A1758-59); MC Additional Reply Comments (Oct, 29, 2001) (A1735-40); VUSA letter (Nov. 1, 2001) (A1760-66).

[103]The cases on which MasterCard relies are inapposite. In *United States v. Ward Baking Co.*, 376 U.S. 327 (1964), the defendant's requested relief was granted prior to any trial in the case, and without any opportunity for the Government to present any evidence. In *Microsoft*, the defendant had requested a remedies hearing and submitted two separate offers of proof that identified 23 witnesses that, if permitted to testify, would have challenged many of the plaintiff's factual representations. 253 F.3d at 101-02.

VI. THE DISTRICT COURT DID NOT ABUSE ITS DISCRETION IN INCLUDING VISA INTERNATIONAL IN THE INJUNCTION

Visa International's brief is principally devoted to disclaiming its liability under Section 1 of the Sherman Act. It largely ignores the district court's rulings that Visa International was properly joined as a defendant and properly included in the decree—whether or not it is liable for violating the Sherman Act—because the court could not otherwise fashion effective relief. Op. 406-07 (SPA242-43); Remedy Op. 617 (SPA264). Those rulings are determinative for purposes of the remedy the government obtained in this case and should be affirmed.

A trial court's determination under Rule 19 of the Federal Rules of Civil Procedure with respect to the joinder of persons needed for a just adjudication is reviewed for abuse of discretion. *Viacom Int'l, Inc. v. Kearney*, 212 F.3d 721, 725 (2d Cir. 2000); *Johnson v. Smithsonian Inst.*, 189 F.3d 180, 188 (2d Cir. 1999). District courts are vested with large discretion in molding effective and appropriate relief in antitrust cases, and the district court's choice of remedy is reviewed for abuse of discretion. *See* pp. 117-119 above.

A. Parties Necessary To Effective Relief Are Properly Joined As Defendants And Included In Antitrust Decrees

The district court in a civil government antitrust case has broad discretion to approve joinder of a party who may not have violated the antitrust laws, and to enjoin certain conduct of that party if necessary to afford effective relief. Visa International ignores the controlling authority requiring its joinder in this case.

Rule 19(a) expressly provides for joinder of a non-party if "in the person's absence complete relief cannot be accorded among those already parties." In fact, "Rule 19(a) *requires* the Court to join any person who is necessary to effect 'complete relief,' where such joinder is feasible." *Jota v. Texaco Inc.*, 157 F.3d 153, 162 (2d Cir. 1998) (emphasis added); *accord Johnson*, 189 F.3d at 188 (court "must" order joinder if "any" Rule 19 criterion is met).[104]

Complete relief in a government antitrust case means relief that is "'effective to redress the violations.'" *Ford*, 405 U.S. at 573 (citations omitted). *See also du Pont*, 366 U.S. at 326 ("courts are . . . required [] to decree relief

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[104] *See also Essex Engineering Co. v. Credit Vending, Inc.*, 732 F. Supp. 311, 316 (D. Conn. 1990) (joinder of defendant's wife necessary to secure judgment against defendant's community property); *Hatten v. Worden*, 38 F.R.D. 496, 499 (E.D. Pa. 1965) (whether or not members administering employer's profit-sharing fund are ultimately found liable, they must remain parties so they can be ordered to direct trustee to pay over money to plaintiff); CHARLES ALAN WRIGHT ET AL., 7 FEDERAL PRACTICE AND PROCEDURE § 1604, at 46 & n.22 (3d ed. 2001).

effective to redress the violations, whatever the adverse effect of such a decree on private interests"). As we have noted, see pp. 122-123 above, it is well established that appropriate conduct remedies go beyond enjoining the specific conduct proven to violate the antitrust laws. And an antitrust court not only can, but "should" include non-liable third parties in any remedy orders when necessary to effectuate a decree. *United States v. Southern Pac. Co.*, 259 U.S. 214, 241 (1922); *Crescent Amusement*, 323 U.S. at 190-91; *see also United States v. Coca-Cola Bottling Co.*, 575 F.2d 222, 226, 229, 230 (9th Cir. 1978).

B. The District Court Did Not Abuse Its Discretion In Concluding That Complete Relief Could Be Effected Only By Including Visa International

1. The district court determined that Visa International is a necessary defendant under Rule 19, whether or not it is liable under the Sherman Act, "because it has the authority to adopt exclusionary by-laws in the United States." Op. 406 (SPA242). Thus, the district court denied Visa International's motion to dismiss it as a defendant because "Visa International has the power to impose its own version of By-law 2.10(e) unless legally prevented from doing so." *Id*. at 407 (SPA243). The court subjected Visa International to a single provision of the decree, enjoining it and the other defendants from "enacting, maintaining or enforcing any by-law, rule, policy or practice" equivalent to Bylaw 2.10(e), to

ensure "effective relief by preventing Visa International from adopting at an international level a by-law that Visa USA would be prohibited from adopting itself." Remedy Op. 617 & n.2 (SPA264); *see also id.* at 617 n.3 (decree prohibits Visa International "from circumventing the effect of this decision by using its authority to enact practices that this court has found to be anticompetitive") (SPA264).

Visa International asserts that the injunction is "improper and unnecessary" because it has only "limited, conditional power over Visa USA and its bylaws." VINT 45. But the express terms of Visa International's bylaws justify the district court's concern. Section 15.02(a) of those bylaws gives Visa International "exclusive[]" authority over "interregional matters." P-1168 (E3973). Although the regulation of "intraregional matters" resides initially with Visa USA, even that authority is "subject to Visa International policies," which may be adopted by a majority of Visa International's total membership. *Id.* §15.02(b). The bylaws place no limits on the types of policies that Visa International's membership might adopt. In addition, "intraregional matters which may have a significant effect on the worldwide Visa program" can be "preempted or regulated" by Visa International. *Id.* §15.02(c). Again, the bylaws do not limit the Board's power to determine which intraregional matters have such an effect. Section 15.05 further

provides that the Board can consider "conflicts and/or controversies" between the policies of regional boards (such as Visa USA) and the regulations, bylaws, or policies of the International Board—including whether regional policies "are inconsistent with the rules, regulations, and/or policies, or otherwise not in the best interests of the corporation." E3974.

In disputing the district court's conclusion that it has power to preempt Visa USA's Bylaw 2.10(e), Visa International complains that the district court did not make findings as to the meaning of particular bylaw terms, as applied to issues related to 2.10(e). VINT 31-33. But Visa International's bylaws do not provide for judicial review of the Board's interpretations of its own authority. The bylaws give the Board "final" authority to determine whether a matter is "purely interregional, purely intraregional, or intraregional having a significant effect on the worldwide Visa program, and to be preempted or regulated by [Visa International]." P-1168 § 15.02(d) (E3973); *see also* § 15.05 (Board decisions are "binding") (E3974); B.Katz Tr. 3293:16-3296:20 (Visa International's "federal system" vests legislative and judicial power in a single entity) (T2840-43).[105]

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[105]Visa International claims (VINT 30-31) that this Court should review its bylaws "de novo," citing cases that apply such review to "a pure textual construction." *Bellefonte Reinsurance Co. v. Aetna Cas. & Sur. Co.*, 903 F.2d 910, 912 (2d Cir. 1990). Visa International is attempting to avoid the "pure text" of its bylaws, however, by suggesting limits that the bylaws do not contain, and

Moreover, Visa International's own conduct gave the district court further reason for concern that Visa International might exercise its authority to circumvent the decree by adopting a rule equivalent to Visa USA's Bylaw 2.10(e). As the court noted, Visa International had "provided affirmative encouragement for By-law 2.10(e) and would have passed its own international version of that rule absent intervention from foreign competition authorities." Op. 407 (SPA243). Visa International then adopted a resolution delegating authority to Visa USA, among others, in order "to ensure that the United States Region knew the International Board supported a continuation of By-law 2.10(e)." *Id.* That resolution expressly reaffirmed the Board's opposition to "dual issuance of VISA and competitive cards, including American Express cards" and specifically promised that "Visa will continue to examine other alternatives to eliminate or diminish the adverse anti-competitive effects . . . which would result from Visa Members issuing and/or acquiring competitive products, including American Express products . . . ." P-0661 at V030425-26 (E2986-87). In these circumstances, the district court was amply justified in its concern that Visa

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relying on interpretations offered by its CEO for purposes of trial that are subject to credibility determinations. *See* VINT 31-32.

International could circumvent a decree applicable only to Visa USA by replacing Bylaw 2.10(e) with an equivalent provision.

2. Visa International's remaining objections to the decree are insubstantial. Visa International claims that it is "powerless to engage in the conduct proscribed by the court's injunction" because the injunction contains the factually incorrect premise that Visa International has "issuers" that issue cards in the United States. VINT 44, 45.[106] Visa International never challenged the remedy on this basis in the district court, however, and thus should be foreclosed from raising this issue for the first time on appeal. *Maska*, 198 F.3d at 79-80. Application of this "well-established general rule," *id.*, is particularly appropriate here where the district court could easily have made the minor correction required to reflect the court's obvious intent. In any event, a request for correction can be made to the district court, which retains continuing jurisdiction over the decree. FJ § V(C) (SPA270).

Visa International also argues that the possibility of contempt proceedings were it "to somehow frustrate the court's overall relief" is an adequate substitute for applying the decree to it. VINT 45. That alternative would defeat an

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[106]Section III(C) enjoins all defendants, including Visa International, from "enacting, maintaining, or enforcing any by-law, rule, policy or practice that prohibits *its issuers* from issuing general purpose or debit cards in the United States on any other general purpose card network." Remedy Op. 617 n.2 (emphasis added) (SPA264).

important Rule 19 purpose: to avoid repeated and unnecessary litigation. WRIGHT ET AL. § 1602, at 21 & n.10; § 1604, at 47. Moreover, contempt remedies can reach only non-parties who "abet the defendant, or [are] legally identified with him." *Alemite Mfg. Corp. v. Staff*, 42 F.2d 832, 833 (2d Cir. 1930) (L. Hand, J.).[107] Visa International maintains that it and Visa USA "are now and always have been separate and distinct entities," VINT 17, and it denies that its conduct to date could be considered to aid or abet Visa USA's actions, *id.* at 43. The district court properly tailored the relief in this case to avoid the necessity of further litigation to prevent Visa International from circumventing the decree.

3. The district court weighed the need to include Visa International in the decree's prohibitions against the burden imposed, concluding that the provisions to which Visa International would be subject are "'minor and ancillary.'" Remedy Op. 617 (SPA264) (citing *EEOC v. Local 638*, 81 F.3d 1162, 1180 (2d Cir. 1996) (citing *General Building Contractors Ass'n v. Pennsylvania*, 458 U.S. 375

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[107] *See also Sheet Metal Contractors Ass'n v. Sheet Metal Workers' Int'l Ass'n*, 157 F.3d 78, 82-83 (2d Cir. 1998) (rejecting contempt because "although the International participates in the governance of Local 25 and its constitution is binding on the local, the International has not acted *in concert with or participated with* Local 25—the party to the EEOC litigation—to violate the [order and judgment]") (emphasis added).

(1982))).[108] The court carefully considered Visa International's objections on a section-by-section basis, and modified the proposed decree to limit its applicability to Visa International where appropriate. Remedy Op. 617 (SPA264). The final decree "requires no affirmative conduct on the part of Visa International, but rather merely prohibits it from circumventing the effect of this decision by using its authority to enact practices that this court has found to be anticompetitive," *id.* at 617 n.3 (SPA264), and that Visa International now disclaims any intent to undertake. In these circumstances, the district court acted well within its discretion.

C. The District Court Reasonably Found That Visa International Is Liable

Visa International devotes the bulk of its brief to attacking the district court's determination that Visa International "was in part responsible for the illegal rule and therefore is liable." Remedy Op. 617 (SPA264). These arguments, even if accepted, would provide no basis for modifying the decree or dismissing Visa International from the litigation. As the district court held, Visa

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[108]The injunction against Visa International imposes no financial burdens, and it is not otherwise burdensome in any significant respect. *Cf. General Building Contractors*, 458 U.S. at 399; *Local 638*, 81 F.3d at 1180.

International was appropriately joined as a defendant and included in the remedy, "regardless of whether [it] is found to be liable." *Id.*

Contrary to Visa International's contention (VINT 33-36), it was held liable for its own conduct, not for Visa USA's conduct under a theory of strict liability. The district court's determination that Visa International was liable as a participant in the challenged agreement among Visa USA and its issuers was based on its finding that Visa International "not only had the power to preempt Visa USA's exclusionary rule, but also provided affirmative encouragement for the illegal bylaw." Remedy Op. 617 (SPA264); *see also* Op. 407 (SPA243).[109] The Visa

[109]Visa International asserts that the district court's fact finding of affirmative encouragement is "erroneous" (VINT 38) because the delegation occurred after Visa USA adopted 2.10(e), because other Regions did not react to the resolution by enacting similar rules, and because the government did not offer testimony that Visa USA was in fact influenced. VINT 37-38. Liability under section 1 of the Sherman Act, however, does not require participation in the initial formulation of an agreement, *United States v. Rea*, 958 F.2d 1206, 1214 (2d Cir. 1992); *Goldman v. McMahan, Brafman, Morgan & Co.*, 706 F. Supp. 256, 263 n.7 (S.D.N.Y. 1989), and the failure of other Regions to adopt similar rules, based at least in part on the announced opposition of their competition authorities (Op. 407 (SPA243)), does not undercut the district court's finding that Visa International was affirmatively encouraging maintenance of Bylaw 2.10(e). Nor was the government obligated to prove that Visa International's efforts to encourage continuation of the bylaw were effective. *Summit Health, Ltd. v. Pinhas*, 500 U.S. 322, 330 (1991) ("because the essence of any violation of § 1 is the illegal agreement itself—rather than the overt acts performed in furtherance of it . . . proper analysis focuses, not upon actual consequences, but rather upon the potential harm that would ensue if the conspiracy were successful); *United States v. SKW Metals & Alloys, Inc.*, 195 F.3d 83, 90 (2d Cir. 1999) (defendants properly

International Board's resolution delegating authority "to ensure that the United States Region knew the International Board supported a continuation of By-law 2.10(e)," Op. 407 (SPA243), and promising to "continue to examine other alternatives," P-0661 at VO30425-26 (E2986-87), provided Visa USA and its issuers not only encouragement, but assurance that Visa International would not act to preempt their exclusionary practice, despite the expressed opposition of other regions and competition authorities. In these circumstances, the district court reasonably found that Visa International knowingly joined the conspiracy, and that finding is not clearly erroneous. *See United States v. Torres*, 901 F.2d 205, 244 (2d Cir. 1990) ("If a defendant, with an understanding of the unlawful character of the conspiracy, intentionally engages, advises, or assists, for the purpose of furthering the illegal undertaking, he thereby becomes a knowing and wilful participant, a conspirator"); RESTATEMENT (SECOND) OF TORTS § 876(b) (liable for "tortious conduct of another" if one "knows that the other's conduct constitutes a breach of duty and gives substantial assistance or encouragement to the other so to conduct himself").

Visa International's reliance on *Copperweld Corp v. Independence Tube Corp.*, 467 U.S. 752 (1984) (VINT 25-29) for the proposition that, as a matter of

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convicted of Section 1 conspiracy even if conspiracy not successful).

law, it cannot be held liable for conspiring with Visa USA if it has the power to exercise control over Visa USA's adoption and adherence to an anticompetitive rule, is beside the point because the challenged conspiracy also involved Visa issuers. *Id.* at 764 & n.9; *see also Pinhas v. Summit Health, Ltd.*, 894 F.2d 1024, 1032-33 (9th Cir. 1990), *aff'd on other grounds*, 500 U.S. 322 (1991). Corporations, their senior officers, and subordinates over whom they exercise significant control are often joined as defendants in suits under Section 1 of the Sherman Act when they conspire with outside competitors. *See, e.g.*, *United States v. United States Gypsum Co.*, 550 F.2d 115, 117 (3d Cir. 1977) (corporation, its chairman, and its VP for sales), *aff'd*, 438 U.S. 422 (1978); *United States v. Waldbaum, Inc.*, 612 F. Supp. 1307, 1309-10 (D. Conn. 1985) (corporation, its CEO, its executive VP, and its VP of Marketing and Sales), *aff'd sub nom. United States v. Korfant*, 771 F.2d 660 (2d Cir. 1985).[110]

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[110]In any event, it is far from clear that Visa International and Visa USA could claim the protection of the *Copperweld* doctrine even if they were the sole participants in the challenged conspiracy. As Visa International concedes, "[t]he two are now and always have been separate and distinct entities." VINT 17. Although the district court properly determined that effective relief could not be devised without including Visa International, that fact is not necessarily sufficient to demonstrate that their economic interests are so intertwined that they should be treated as a single economic entity. *See, e.g.*, *Capital Imaging Assoc., P.C. v. Mohawk Valley Med. Assoc., Inc.*, 996 F.2d 537, 544-45 (2d Cir. 1993) (HMO and its physicians' association are capable of conspiring); *Fishman v. Estate of Wirtz*, 807 F.2d 520, 541-42 n.19 (7th Cir. 1986) (despite some overlap in ownership and

CONCLUSION

The judgment of the district court should be affirmed.

Respectfully submitted.

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control, corporations lacked the unity of interest necessary under *Copperweld).*

CERTIFICATION CONCERNING LENGTH LIMITATIONS

Pursuant to Federal Rule of Appellate Procedure 32(a)(7), as modified by this Court's Order of June 25, 2002, allowing plaintiff-appellee United States 32,000 words for its brief, I hereby certify that this brief contains 31,780 words, exclusive of the addendum, as counted by the word processing system used to prepare this brief, and uses a proportionally spaced font of 14-point.

Dated: August 30, 2002

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ADDENDUM

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I certify that on August 30, 2002, two true and correct copies of the Brief Of The United States (Final Version) were served by Federal Express, overnight delivery, on:

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