

No. 02-6074(L)

Consolidated with Nos. 02-6076, 02-6078

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA,

Plaintiff-Appellee,

v.

VISA U.S.A. INC., VISA INTERNATIONAL CORPORATION,
and MASTERCARD INTERNATIONAL INCORPORATED,

Defendants-Appellants.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK, NO. 98-7076 (BSJ)
HONORABLE BARBARA S. JONES

BRIEF AMICUS CURIAE OF UNDERSIGNED PUBLIC INTEREST GROUPS IN SUPPORT OF AFFIRMANCE

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure, each of the Amici Curiae listed below states that it has no parent corporation and that no publicly-held corporation holds more than 10 percent of its stock. Financial support for certain legal expenses incurred in connection with the filing of this brief was provided by American Express Company. The points advanced in this brief, however, are those of Amici Curiae.

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**BRIEF AMICI CURIAE OF UNDERSIGNED
CONSUMER GROUPS IN SUPPORT OF AFFIRMANCE**

INTEREST OF AMICI CURIAE

This brief is filed on behalf of 26 consumer and public interest organizations representing a range of consumer interests, each of which is described in Exhibit A, attached to this brief. Each organization supports the decision below and respectfully requests that it be affirmed.¹

This case involves one of the most important and ubiquitous consumer products: general purpose credit and charge cards. There were over 500 million general purpose charge and credit cards outstanding in the United States in 2001, involving an estimated \$1.124 trillion in purchases. *See The Nilson Report*, No. 760, March 2002. General purpose charge and credit cards are not just the tools of well-heeled business travelers, but, for most consumers, are necessary for everyday life. Consumers need credit cards to rent cars, reserve hotel rooms, and make purchases on the Internet or over the phone. Merchant acceptance of credit cards makes everyday errands, such as grocery shopping or having a prescription delivered from the drugstore, more convenient.

¹ Pursuant to Fed. R. App. P. 29(a), Amici sought consent of the parties to the filing of this brief. Appellee the United States has consented. Appellants have not provided their consent. Accordingly, pursuant to Rules 29(a) and (b), this Brief is accompanied by an application to this Court for leave to file.

While there are thousands of issuing banks, there are only two dominant networks, Visa and MasterCard. And rivalry between the issuing banks has not led to competitive interest rates for consumers – as consumers with good credit routinely pay more than four times the prime rate. Lawrence M. Ausubel, *Credit Card Defaults, Credit Card Profits, and Bankruptcy*, 71 Am. Bankr. L.J. 249 (1997). Preserving the economic benefits of competition for credit and charge cards is vital to virtually every consumer in this country.

The issue in this case is the illegality of Visa’s By-law 2.10(e) and MasterCard’s Competitive Programs Policy (or CPP) (collectively the “exclusionary rules”). The exclusionary rules have been used by Visa and MasterCard to preclude essentially every bank in the United States from issuing American Express (“Amex”) cards, Discover cards, or any other card “deemed competitive” by Visa and MasterCard. Visa and MasterCard have tried to introduce similar restrictions in other countries around the world, but in each instance the rules were withdrawn (or enjoined) as a result of challenges from local antitrust enforcers. Consequently, it is only in the United States that consumers have been denied the opportunity to secure a bank-issued Amex or Discover card, and it is only in the United States that consumers have been deprived of the benefits that naturally flow from banks competing with each other in an unrestricted marketplace. As explained in the argument below, the exclusionary

rules have restricted choice, innovation, and price competition. That is why consumers are interested in seeing that the District Court's decision overturning the exclusionary rules is upheld.

SUMMARY OF ARGUMENT

A current advertising slogan tells us that "When banks compete, you win." *See* The Lending Tree website (www.c-loans.com/lendingtree.html). The point is correct, and it expresses one of the fundamental principles of antitrust law. Conversely, "When banks agree to limit competition, you lose." The exclusionary rules make certain that consumers lose.

The exclusionary rules are agreements among all bankcard issuers in the United States, through Visa and MasterCard, to limit competition among themselves. Because of the exclusionary rules, banks can issue cards only on the Visa and MasterCard networks. Banks cannot compete against each other by introducing to consumers features, quality, image, and brand attributes available on other networks. There is no dispute on this point.

In this brief, we focus on three of the ways consumers are hurt: the effect of the rules in (1) restricting consumer choice; (2) impeding innovation; and (3) increasing prices. We will explain, from the consumer perspective, the nature and severity of these harms and some of the reasons why the exclusionary rules should be abolished.

The adverse consumer effect of these rules can also be inferred from the positions taken by consumer advocacy groups themselves. While twenty-six groups have sought leave to file this brief in support of the decision below, no consumer group or advocate to our knowledge has spoken in favor the exclusionary rules that the lower court enjoined.²

ARGUMENT

I. THE EXCLUSIONARY RULES HARM CONSUMERS BY REDUCING CONSUMER CHOICE IN LIMITING BOTH THE AVAILABLE FEATURES OF CHARGE AND CREDIT CARDS AND THE NUMBER OF PLACES CONSUMERS CAN USE THEIR CARDS

The antitrust laws protect consumer choice. The exclusionary rules limit choice. “[A]n agreement limiting consumer choice by impeding the ‘ordinary give and take of the market place’ cannot be sustained under the Rule of Reason.” *FTC v. Indiana Fed’n of Dentists*, 476 U.S. 447, 459 (1986). *See also NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128, 137 (1998); *NCAA v. Board of Regents*, 468 U.S. 85, 102, 107-08 (1984) (“effect of reducing the importance of consumer preference in setting price and output” unlawful); *Eastman Kodak Co. v. Image Tech. Servs.*, 504 U.S. 451, 478 (1992) (“competition is enhanced when a firm is able to offer

² *See also* October 10, 2000 Submission of Consumers Union to Judge Barbara S. Jones (“Consumers Union is concerned that consumers may be harmed by current practices that prohibit financial institutions from offering competing products . . .”).

various marketing options”); *Gonzalez v. St. Margaret’s House*, 880 F.2d 1514, 1517 (2d Cir. 1989) (addressing “the resultant harm to consumer choice”); *Full Draw Productions v. Easton Sports, Inc.*, 182 F.3d 745, 755 (10th Cir. 1999) (“limiting consumer choice” is anticompetitive); *see generally* Robert H. Lande, *Consumer Choice As The Ultimate Goal of Antitrust*, 62 U. Pitt. L. Rev. 501, 508-14 (2001).

A. Because Of The Exclusionary Rules, Consumers Can Not Receive The Benefits of A Bank-Designed Card Combined With The Features Of The Amex Or Discover Networks

1. *The exclusionary rules prevent the creation of cards combining bank features with Amex or Discover network features.*

Because of the exclusionary rules, consumers cannot have an Amex or Discover credit or charge card that is designed by a bank and that combines the features offered by the bank with the features of the Amex or Discover networks. Visa and MasterCard miss the point when they argue that there is no harm because consumers can get cards directly from Amex or Discover. Consumers want the option of getting an Amex card or a Discover card from banks because those cards will offer features and benefits that are different from the cards already offered by Amex and Discover. This differentiation will be designed to provide enhanced value to the banks’ customers. The consumers’ inability to obtain a bank-issued Amex or Discover card is a severe restriction on the choices available.

Consumers value both: (1) the benefits of getting a card from a bank; and (2) the attributes of the Amex and Discover brands. *United States v. Visa USA, Inc.*, 163 F. Supp. 2d 322, 395, *supplemented*, 183 F. Supp. 2d 613 (S.D.N.Y. 2001) (“Because cardholders believe there are differences among credit card brands, many issuers want to be able to deliver them a brand choice.”). The exclusionary rules inhibit the banks in competing against each other by preventing them from combining the features that make Amex and Discover special with the features that make their individual banks special (and the banks’ relationships with their customers special). There is no way for consumers to get both sets of features other than by allowing banks to partner with Amex and Discover. Visa itself admits, as it must, that the exclusionary rules prevent consumers from getting Amex and Discover cards with “‘mix ‘n match’ features of bank issuance.” Visa’s Opening Brief, p. 34.

In addition, as the District Court found, “[t]hrough the use of account information uniquely available to banks . . . , bank issuers more cheaply, easily and effectively find and market credit cards to those consumers,” *id.* at 391, allowing banks to provide those customers with cards on the Discover or Amex networks the consumers might want but would not otherwise obtain.³

³ For example, American Express or Discover may have much more difficulty than a local bank in judging the credit worthiness of consumers with “thin” credit files but substantial wealth. Credit reports often do not report

Consumers have been also denied the choice of a bank creating American Express or Discover cards combining credit and debit functionality. Today, in the United States, there is no card that combines credit card functions with features, such as debit, that depend on direct access to the consumer's checking or savings "demand deposit account" or DDA. Outside the United States, however, where Appellants' exclusionary rules have been banned, consumers have that choice. Examples include a combination credit/online debit card issued in Portugal on the Amex network by BCP and a similar card issued, also on the Amex network, in Singapore by DBS. Tr. 1496-97, 2635-38, 2648-49. Only banks can provide consumers with cards with DDA access. 163 F. Supp. 2d at 393-94. By preventing banks from issuing on the Amex or Discover networks, Visa and MasterCard have effectively blocked the introduction of these combined function cards in the United States. *Id.* at 392-93.

As the District Court found, "bank issuance across all networks would increase product variety and increase consumer choice." 163 F. Supp. 2d at 395. "[T]he combination of banks' knowledge and features with network features and brand preference yields consumer value." *Id.* The Court's findings were well supported by the evidence.

information about a person's wealth. But a local bank that may know that a recent widow has substantial assets and is credit worthy even though she has not established credit history. Tr. 2741-42.

2. *The Amex and Discover networks offer different features.*

As the Court found, consumers are denied today the choice of bankcards utilizing benefits available only on the Discover and Amex networks. For example, “Because American Express and Discover are closed-loop systems that deal directly with merchants, those brands have the infrastructure to collect data and details about spending that many consider superior to defendants’ capabilities.” *Id.* at 395-96. This superior data collection of a closed-loop system means that American Express or Discover cards can provide consumers with statements that contain more detailed transaction information (e.g., the flight information related to an airline charge). Visa/MasterCard bankcards cannot provide the same capability because Visa and MasterCard have no closed-loop system. Allowing banks to issue American Express and Discover cards would allow banks for the first time to provide consumers with this valuable service.

Visa International itself recognized the importance of unique network features: “[I]f ‘Visa services’ were differentiated from MasterCard services, ‘members will be able to *combine their own marketing strategies with the capabilities of their chosen system* to create more real and more easily perceived differences in the marketplace.” *Id.* (quoting P-1176) (emphasis by the court).

No matter how many bank credit card offers consumers may receive in their mailboxes, the fact is that every one of those offers is for a card issued only on the

Visa or MasterCard networks. Yet, for the consumer, the choice of network matters for critical features, such as network standards for privacy, internet security, correction of invalid charges, emergency card replacement, and more detailed billing statements.

3. ***The restriction on choice is a substantial restriction on competition, harming consumers.***

The products consumers can obtain should be determined by market forces, not Visa/MasterCard's rules. As the Supreme Court put it in *Indiana Fed'n of Dentists*, 476 U.S. at 459, an antitrust defendant "is not entitled to pre-empt the working of the market by deciding for itself that its customers do not need that which they demand." See also *Olympia Equipment Leasing Co. v. Western Union Tel. Co.*, 797 F.2d 370, 378 (7th Cir. 1986) ("the free market and not a judge or jury decides whose products are inferior"). However, Visa and MasterCard have attempted, through the exclusionary rules, to pre-empt the working of the free market, exactly what the antitrust laws are designed to prevent them from doing.

Even if the banks compete against each other in other respects, "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 the agreement" is unlawful. *Indiana Fed'n*, 476 U.S. at 459. Accord, e.g., *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980) (horizontal agreement to refuse to compete on credit terms

unlawful notwithstanding unlimited competition among defendants in all other respects). The exclusionary rules force issuing banks to use the relatively homogenous Visa/MasterCard networks – referred to by Visa and MasterCard at trial as their “common pasture.” *See, e.g.*, Tr. 5307, 5312. The refusal of Visa and MasterCard to permit banks to compete against each other, other than through the “permitted” competition within the Visa and MasterCard “common pasture,” harms consumers – and it violates the Sherman Act.

The reduction in consumer choice caused by the exclusionary rules is a reduction in market output. The District Court separately found, based on substantial evidence, that the effect of the rules has been to decrease output in the form of the total number of cards issued by general purpose card issuers. 163 F. Supp. 2d at 330, 379, 387, 406. But even if the total number of cards were not affected, the exclusionary rules clearly decrease the variety of card products available in the marketplace. That reduction in product variety decreases consumer utility. Consumers value product variety. Variety, just like product quality, is thus one of the many dimensions of output in the legal and economic sense. Robert H. Bork, *The Antitrust Paradox* 187-91, 296-97 (1978); 13 Phillip Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 2104a, at 36 (1999). A significant reduction of output in the form of choice or variety is therefore an unreasonable restraint under the law. *E.g., NCAA*, 468 U.S. at 107-08; *see also Conwood Co. v. United States*

Tobacco Co., 290 F.3d 768, 789 (6th Cir. May 15, 2002) (even though both total market production and plaintiff’s market share increased in relevant period, defendant’s “actions caused higher prices and reduced consumer choice, both of which are harmful to competition.”).

B. Because Of The Exclusionary Rules, Consumers Are Limited In The Number Of Places They Can Use Their Cards

The exclusionary rules have resulted in lower rates of merchant acceptance of American Express and Discover cards, which also impairs consumers’ freedom to use the card of their choice at merchant locations. As the District Court found, the number of cards in the marketplace bearing a particular network brand directly affects the willingness of merchants to accept cards. The relationship between numbers of consumers holding a particular brand of card and the number of merchants willing to accept those cards is well established. 163 F. Supp. 2d at 387-88. The District Court’s findings detail the negative effects the rules have on merchant acceptance of Amex and Discover cards. *Id.* at 388-89. What this all means is that consumers cannot use their Amex and Discover cards in the locations they want. Indeed, consumers may be deterred from even obtaining a card they would otherwise want by the prospect of embarrassment when a card is presented to a merchant for payment and is rejected or, more politely, “not accepted.” If banks were free to design and issue Amex or Discover cards, there would be more

cards with those brands in the marketplace, which would increase the willingness of merchants to accept them, to the benefit of consumers who already own such a card or who might wish to obtain one. The exclusionary rules prevent that from happening.⁴

II. APPELLANTS' RULES HARM CONSUMERS BY RETARDING INNOVATION

In a free market, bank issuance of cards on the Discover or Amex networks could result in the development of innovative features and services that consumers today can only imagine. It is at the network level, not the issuer level, that systems innovations are developed and implemented, including features such as faster processing methods, better security, enhanced privacy protection, or the ability to accept and implement smart chip technology. The effect of the exclusionary rules on system-level innovation is unambiguously negative.

⁴ MasterCard argues in its brief that merchant acceptance for Discover and Amex is good enough. MasterCard Brief, pp. 16, 28 n.7. The District Court, however, considered each of MasterCard's arguments and rejected them on the basis of substantial evidence. 163 F. Supp. 2d at 388-89 & n.24. Thus, the Court recognized that Amex does not have 95% "merchant coverage" as MasterCard asserts. It has that level of coverage for the dollar volume at locations where *existing* Amex cardholders use their cards. *Id.* at 388 n.24. As the District Court pointed out, the percentage of merchants that actually accepts Amex cards is lower. *Id.* Similarly, although Discover's merchant acceptance has improved, "it still suffers from a perception gap (based on its lower acceptance in the past) [To] close the gap[, . . . Discover] needs more card issuance and transaction volume, which can only realistically be obtained via third-party issuers, to become a more relevant network." *Id.* at 389.

One of the principal ways in which consumers benefit from the pro-competition policy of the antitrust laws is the strong effect that competition has in inducing and encouraging innovation. *See, e.g., Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 281-83 (2d Cir. 1979); *United States v. Microsoft Corp.*, 253 F.3d 34, 49-50 (D.C. Cir.), *cert. denied*, 122 S. Ct. 350 (2001); Department of Justice & FTC, *Antitrust Guidelines for the Licensing of Intellectual Property* § 3.2 (1995). Visa itself admits that network competition – referring to Visa’s limited competition with MasterCard – fosters innovation. Visa’s Opening Brief, pp. 14-15. Once again, Visa and MasterCard seem to be saying that innovation limited to their two networks is all the innovation consumers need or deserve. The point that Visa and MasterCard miss is that the exclusionary rules discourage even more vigorous card innovation by inhibiting the Discover and Amex networks from developing new products and features that can only (or more effectively) be deployed through bank issuers, all to the detriment of consumers.

Innovative products result from the combination of unique bank capabilities and unique network capabilities. An example is the Banco Popular Platinum American Express card, available today in Puerto Rico (where the exclusionary rules do not exist). As the bank’s website (www.bancopopular.com) explains, this card “offers diverse forms of support and service worldwide through Banco Popular and American Express.” By way of example, one feature is “Immediate

attention at Banco Popular branches. You don't have to wait in line at our branches. When you show your card, the bank host will make your transactions for you or will notify an officer that you will be the next to be attended in any transaction.” Cardholders also get a special 800 number for personalized service at the bank. Unique American Express network features, including access to its many travel offices, concierge service, and travel protection enhance the product further. Tr. 749-50. The innovative combination of the bank's features and Amex's features provides consumers in Puerto Rico with a product that does not, and cannot, exist in the 50 states today.

The “relationship card” features analyzed by the District Court provide another particularly important example of innovation deterred. Consumers want to simplify the way they manage their financial transactions. For those consumers, there is an obvious value in having multiple functions embedded in a single card. For example, a single card that enables a consumer to switch between credit and debit functionality – of the sort that exist abroad today (see Point I, *supra*, at p. 8) – allows that consumer to manage financial transactions with a single piece of plastic that enables the consumer to decide, at the point of sale, whether to pay now (by debiting a demand deposit account) or pay later (by accessing a line of credit).

Many believe – including Visa and MasterCard – that multi-function “relationship” cards are the industry's future. 163 F. Supp. 2d at 392. The key

component of any relationship card will be the ability to withdraw or deposit funds into or out of the consumer's demand deposit account – a feature available only to the bank that holds the account and blocked from the Amex and Discover networks today by the exclusionary rules. Because it is the banks that have the access to the consumer's demand deposit accounts, the only way Amex or Discover can provide relationship cards to consumers is by having bank issuers on their networks – precisely what 2.10(e) and the CPP prevent. *Id.* at 392-93. By arrogating all the bank issuers to themselves through their exclusionary rules, Visa and MasterCard have essentially assured a duopoly of relationship cards – the industry's likely future – over the decades to come. *Id.*⁵

Visa and MasterCard have been slow to develop full-service relationship products with banks. By preventing banks from offering Amex and Discover relationship cards to consumers, Visa and MasterCard are able to hobble the competitive pressure they would otherwise have to face from Amex and Discover

⁵ Even today, in the market for offline debit cards – a product dependent on demand deposit account access – Appellants' exclusionary rules have blocked entry of any other network. 163 F. Supp. 2d at 393-94. The debit market is substantial, totaling \$263.74 billion in purchase volume in 2001, 77.83% on Visa (with the rest on MasterCard), and growing at a rate of 26% over 2000. *See The Nilson Report*, No. 760, March 2002. Because of the total exclusion of Amex and Discover from the debit market, Visa and MasterCard have been able to set artificially high interchange rates that inflate merchant discount rates for offline debit card acceptance. *See generally In re Visa Check/MasterMoney Antitrust Litigation*, 192 F.R.D. 68 (E.D.N.Y. 2000), *aff'd*, 280 F.3d 124 (2d Cir. 2001), *cert. denied*, No. 01-1464 (U.S. June 10, 2002).

to develop relationship card products and features that would benefit consumers. Repeal of the exclusionary rules, on the other hand, would mean that consumers would benefit from banks competing for their business by creating innovative relationship cards on any one or all four networks.

To illustrate the point, this Court need look no further than Visa's own statements in the court below. Visa claimed there was no urgency in repealing 2.10(e) because Visa was in no hurry to deploy any kind of relationship card. Visa's witness, Ms. Knox, testified that Visa was not even "testing or developing such a product" and did not expect Visa to have the product available for at least another seven to ten years. Record 285 (item 128), Declaration of Diane Knox ¶¶ 2, 14-15 (Dec. 17, 2001). But if banks could issue Amex or Discover cards, this feature could be available much sooner. This effect on innovation is exactly why allowing other networks to innovate is so important.

The exclusionary rules are already stalling the deployment of "smart cards," computer chip-based cards capable of multiple functions. Smart cards, like other card products, cannot achieve (or even approach) their potential until they achieve sufficient critical mass. To increase their usefulness, smart cards require software developers to develop applications to be embedded in the chip *and* merchants to have point of sale terminals able to accept the cards and utilize the features provided by the software. 163 F. Supp. 2d at 397-98. In order for consumers to be

able to use smart cards, they must be widely accepted by merchants, which in turn requires merchants to invest in upgrading their card acceptance.

The ability of banks to issue on all networks would lead to more smart cards issued and available in the marketplace. More smart cards would result in more smart card applications and create an incentive for merchants to install terminals capable of reading the new cards and providing the new features. More smart cards on the Amex and Discover networks would increase the urgency of Visa and MasterCard for smart card deployment – a natural effect of competition – and accelerate the process further. The potential consumer benefits are enormous, such as: cards that could add or use loyalty program rewards points immediately at the point of sale; cards that could provide consumers with an ability to track their spending and balances in real time at multiple locations and transfer funds to enable purchases; and cards that could allow consumers to learn of and benefit from specific promotional offers instantaneously at the point of sale.

As Visa and MasterCard appear to concede, the first step in this process is issuing smart cards to consumers. Knox Decl., *supra*, ¶ 11; *see also* Record 226, Declaration of Stephen McCurdy ¶ 18 (Jan. 14, 2002) (quoting Visa executive). Only when sufficient numbers of consumers have smart cards in their wallets will market forces impel the necessary investments by software developers and merchants. *Id.*

The first smart card in the United States was introduced by American Express, not Visa or MasterCard; it was “Blue from American Express.” 163 F. Supp. 2d at 397. That product has been successful, and has led to the introduction of smart cards on the Visa and MasterCard networks in direct response. *Id.*; McCurdy Decl., *supra*, ¶ 19. Yet, as the District Court found, “Blue has been a success for American Express, but its success has nevertheless been constrained by the fact that because of the exclusionary rules, American Express is its sole issuer.” 163 F. Supp. 2d at 397. But for the exclusionary rules, many additional smart cards would be issued by banks on the Amex networks and “consumers [would] benefit because increased functionality [would] result from increased scale.” *Id.* at 397-98. “Moreover, competition with [Visa/MasterCard would] also be enhanced because [Visa/MasterCard] would surely respond with their own accelerated programs for development of competitive smart card products.” *Id.* at 398. “In short,” the court below found, “the evidence is clear that multiple issuer networks provide the best competitive means for consumers to obtain the long-recognized benefits of smart cards.” *Id.*

Technological advances, such as smart cards, benefit consumers. A free market would permit the rapid deployment of the most promising features and advances – allowing them to reach critical mass and achieve economies of scale

such that consumers can enjoy their benefits. The exclusionary rules block this virtuous cycle, and consumers suffer the consequences.

III. APPELLANTS' RULES HARM CONSUMERS BY RAISING THE PRICE BANKS PAY FOR NETWORK SERVICES

Consumers benefit from prices set by a vigorously competitive market. As the District Court's findings demonstrate, the exclusionary rules restrain price competition in the sale of network services because banks have only two networks competing for their business, Visa and MasterCard, not four. More networks competing for the banks' business would result in lower, more competitive, prices for network services. If network prices were lowered, banks would be able to reinvest the difference in new features, or to lower interest rates and fees, to compete more effectively against their bank issuer competitors. Today, however, banks have to pay the higher prices associated with reduced competition, and these increased costs are embedded in their card businesses.

The exclusionary rules directly restrain price competition in the sale of network services to banks. It is undisputed that Visa and MasterCard compete against each other through "specially negotiated individual incentive compensation packages with . . . virtually all of the largest issuers . . . , [the terms of which] are not shared with other members" 163 F. Supp. 2d at 403; *see id.* at 365-71, 382. This competition operates to lower, somewhat, the effective price bank card

issuers pay for card network services. *Id.* at 382. But the exclusionary rules limit this competition only to a duopoly, Visa and MasterCard. Consumers are left to imagine how much lower prices would go without the exclusionary rules which would permit Amex and Discover freely to compete for the banks' business. *See Conwood*, 290 F.3d at 784-85, 788-89, 794-95 (although market growth increased, without defendant's conduct "the market would have grown more"; plaintiff was not required to prove how much).

As the District Court found, Visa and MasterCard – facing no competition from Discover or Amex – were able to terminate their prior, more intensely competitive, "mail share" and "co-branding" programs, in which "issuers were playing the associations against one another and demanding ever-increasing amounts," 163 F. Supp. 2d at 367-68, and to replace them with the current "partnership" programs, pursuant to which banks have agreed to commit all future volume exclusively to either Visa or to MasterCard for lengthy periods of time. *Id.* at 368-69; *see also* Record 285 (item 89), Defendants' Joint Proposed Findings of Fact, pp. V-18 to V-19 (because of "concer[n that] issuers were playing the associations against one another and demanding ever-increasing amounts . . . ,

[b]oth associations ultimately took steps to move . . . to longer term arrangements”).⁶

The exclusionary rules prevent the more vigorous price competition that would be generated by two *additional* networks competing for the banks’ business. As Visa itself told the District Court, repealing 2.10(e) and the CPP will create “competition for issuers [that] almost assuredly will result in higher payments to [bank] issuers – as reflected in the so-called ‘mail share’ wars between Visa and MasterCard several years ago.” Record 285 (item 127), Visa Mem. in Support of Stay Pending Appeal, p. 11 (Dec. 17, 2001); *see id.* at 22 (same). “Higher payments to [bank] issuers” by networks means banks are paying less for network services – lowering banks’ costs and creating an environment where banks can decrease charges to consumers.

Because of the exclusionary rules, the increased prices to banks for network services are not subject to the discipline of market forces based on competition from other networks. Moreover, the cost of card network services is increased, not just to bankcard issuers, but to Amex and Discover as well. The American Express

⁶ The “mail share” programs were programs under which Visa and MasterCard, respectively, provided individual funding incentives to selected banks to induce the bank to provide direct mail solicitations to consumers for one brand or the other. The “co-branding” programs were similar incentive programs pursuant to which Visa and MasterCard, respectively, offered funds to particular banks to help win co-brand deals (for example, NBA team sponsorships) for Visa or MasterCard. 163 F. Supp. 2d at 366-68.

and Discover networks are precluded from spreading their network costs across multiple bank issuers and are unable to achieve the greater economies of scale that multiple issuers would provide. 163 F. Supp. 2d at 382, 398. This increase in the costs of Visa/MasterCard’s competitors, coupled with the exclusionary impact of 2.10(e) and the CPP, renders Amex and Discover unable to constrain Visa/MasterCard’s network services pricing; this facilitates Visa and MasterCard’s exercise of market power, and causes prices to increase to all issuers – a classic case of raising rivals’ costs to achieve power over price. Thomas G. Krattenmaker & Steven C. Salop, *Anticompetitive Exclusion: Raising Rivals’ Costs to Achieve Power Over Price*, 96 Yale L.J. 209 (1986). The upshot is that the exclusionary rules raise the price of card network services across the entire market. *See Premier Elec. Constr. Co. v. NECA*, 814 F.2d 358, 368 (7th Cir. 1987) (“The Association raised its rivals’ costs, and thereby raised the market price to its own advantage.”).

The artificially high price of network services to all issuers necessarily harms consumers *irrespective of the degree of competition at the issuer level*. Basic economics says that, when all suppliers’ costs are raised, prices to customers must rise too. This is true no matter how great (or weak) the competition may be at the issuer level. Network services represent a necessary input for every card issuer, an unavoidable cost each issuer must bear. A market price increase on this essential input raises the costs of the industry as a whole and ultimately *must* be

borne by all consumers who carry general purpose charge and credit cards. Whether this price increase takes the form of higher revolving interest rates, annual fees, late fees, or decreased services does not matter. *E.g.*, *Indiana Fed'n*, 476 U.S. at 459; *Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643 (1980) (effect on credit terms as harmful as effect on prices generally).

This increase in the price of network services is unlawful even absent specific proof that the price increase has been passed along to consumers. A reduction in price competition for an intermediate good, input, or service purchased by wholesalers or middlemen – here, network services purchased by banks – is every much as harmful as a direct increase in prices at the consumer level. *See FTC v. H.J. Heinz Co.*, 246 F.3d 708, 719 (D.C. Cir. 2001) (“no court has ever held that a reduction in competition for wholesale purchasers is not relevant unless the plaintiff can prove impact at the consumer level”). As the *Heinz* court explained, “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.’” *Id.* (quoting *In re Brand Name Prescription Drugs Antitrust Litig.*, 123 F.3d 599, 605 (7th Cir. 1997)).

**IV. APPELLANTS' RULES HARM CONSUMERS BY
RETARDING NETWORK BRAND
COMPETITION TO RESTRICT HIDDEN
PRICING BY ISSUING BANKS**

The average credit card interest charged by banks nationally has been estimated to be as much as five percentage points higher than the competitive rate. *See* Lawrence M. Ausubel, *The Failure of Competition in the Credit Card Market*, 81 *Am. Econ. Rev.* 50, 73 (1991); Lawrence M. Ausubel, *Credit Card Defaults, Credit Card Profits, and Bankruptcy*, 71 *Am. Bankr. L.J.* 249 (1997). Additionally, the current marketplace conditions do not sufficiently constrain some banks from engaging in the hidden pricing of credit. *See, e.g.*, Robert K. Heady, *The Credit Card Beefs Go On*, Ft. Lauderdale Sun-Sentinel, Sept. 3, 2001, p. 19.

For example, there is a large class of “unintentional borrowers” who are subject to these credit charges because at least once or twice a year they fail to pay their bill within the grace period allowed by the card. Ausubel, 81 *Am. Econ. Rev.* at 70. And banks make a substantial proportion of the credit card profits from these backend charges. *Id.* at 58; Paul S. Calem & Loretta J. Mester, *Consumer Behavior & the Stickiness of Credit-Card Interest Rates*, 85 *Am. Econ. Rev.* 1327 (1995).

While there are thousands of banks issuing on the MasterCard and Visa networks, these banks often do not compete on offering better terms because these unintentional borrowers “mak[e] credit card choices without taking account of the

very high probability that they will pay interest on their outstanding balances.”
Ausubel, 81 Am. Econ. Rev. at 50.

Brand competition among the networks is one mechanism to restrain the hidden pricing of issuing banks. Just as the Mobil gasoline brand constrains its service stations to provide clean bathrooms (and appeals to customers on this basis), credit card networks could constrain their member banks from charging outrageously supra-competitive credit terms (and appeal to consumers on this basis). Gasoline stations may find it in their interests to commit to clean bathrooms, and individual banks may similarly find it advantageous to issue cards on a network that prohibits interest-rate gouging. A network brand that commits to clean credit practices would increase ultimate consumer demand for cards issued on that network. And individual banks accepting the networks limitation could gain access to this heightened demand, safe in the knowledge that their rivals issuing cards on this network will be similarly restrained.

But to date the appellant networks have failed to constrain issuing banks on these dimensions that are so crucial to consumer welfare. Eliminating the exclusionary rules is likely to foster network brand competition along just these lines. Generically, competition among a larger number of network brands increases the incentives of individual brands to differentiate themselves by offering

superior value. (Think of Saturn's policy of restricting its dealerships ability to negotiate unconscionable vehicle prices.)

Were open competition among networks to be permitted, it could be expected that at least one network would take the initiative to induce its issuers to provide a greater level of transparency in the fees, charges, and interest rates consumers are assessed, and that other networks might then follow. The existing regime, where network competition is limited to Visa and MasterCard only, has yielded no such result.

CONCLUSION

The District Court's decision was sound. The collective agreement of banks to restrict competition, as embodied in the exclusionary rules and policies of Visa and MasterCard, decreases choice, reduces innovation, and increases price – all to the manifest detriment of consumers. Amici respectfully urge that the decision be AFFIRMED.

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Respectfully submitted,

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EXHIBIT A: LISTING OF AMICI CURIAE

Gray Panthers

The Gray Panthers is a national organization of intergenerational activists dedicated to progressive social change. Among the issues of interest to the Gray Panthers are corporate accountability and market competitiveness. The Gray Panthers have at times appeared as amicus curiae in various courts on these issues.

The American Antitrust Institute, Inc.

The American Antitrust Institute is an independent research, education, and advocacy organization that believes that the national economy is best served by the vigorous enforcement of the antitrust laws.

American Association of Business Persons with Disabilities

The American Association of Business Persons with Disabilities is an advocate for individuals and small business owners with disabilities. The Association monitors and comments on many diverse issues that impact the lives and livelihood of individuals and small business owners with disabilities.

The Consumer Alliance

The Consumer Alliance is a broad-based, national coalition of consumer, senior, minority, rural, employee, low-income, labor, farm and small business organizations that provides a unified voice on issues affecting consumers. TCA educates the media, consumer advocates, policymakers, and the general public about regulatory and legislative initiatives that affect families and individuals and advocates for their interests.

Consumers First, Inc.

Consumers First, Inc. is a consumer education and advocacy organization representing the interest of diverse consumers, including homeowners, renters, consumer activists, community leaders, senior citizens, disability groups, small business owners and rural communities. This broad-based grass-roots association is active in providing information and participating in the governmental process.

Self-Help for the Elderly

Self-Help for the Elderly is a community based organization established to improve the quality of life for seniors in San Francisco, San Mateo and Santa Clara

counties in California by providing a comprehensive range of multilingual and multicultural services to empower seniors. Serving approximately 25,000 seniors a year, Self-Help for the Elderly advocates for better consumer protection and consumer services for seniors.

Consumer Alliance of the Southeast

The Consumer Alliance of the Southeast (CASE) is a regional coalition of consumer groups, community leaders, and small business owners with members in 12 states that speaks out on service issues vital to the home and small business.

California Small Business Association

The California Small Business Association is a grassroots, volunteer-driven, non-profit organization whose mission is to provide small businesses with a meaningful voice in state and federal government. The Association, representing over 187,000 small businesses, works to foster governmental legislation and regulations that will create an environment for the members to grow their businesses while serving the needs of all Californians.

The Consumer Research Institute

The Consumer Research Institute is a non-profit institution established to teach and disseminate educational material to the public, including but not limited to, material related to consumer protection, through publication, lectures or otherwise.

The Democratic Process Center, Inc.

The Democratic Process Center, Inc. is a 501c3 educational and public interest organization, engaged in research, workshops, seminars, etc. on educational and public policy issues. The Democratic Process Center trains teachers and educational employees in the philosophy of the democratic process as it relates to education and public policy.

The Center for Public Interest Law

The Center for Public Interest Law is an academic and statewide law firm, representing the interests of consumers within the state of California and training law students in the skills of public interest law practice. CPIL publishes the California Regulatory Reporter. CPIL represents consumer interests in regulatory and competition related matters.

Consumer Fraud Watch

Consumer Fraud Watch was organized to promote greater awareness of financial and insurance frauds and related criminal activities to educate the public on techniques for recognizing frauds and avoiding becoming a victim.

Americans for Competitive Telecommunications

Americans for Competitive Telecommunications is a broad-based grassroots coalition, which seeks to provide consumers with information and useful tools about federal law opening telephone markets to competition. A.C.T. helps consumers evaluate the level of competitive access available to them and monitors and supports various forms of competition that promote consumer access to maximum choice among innovative products and services.

Wireless Consumers Alliance, Inc

Wireless Consumers Alliance, Inc. is a non-profit corporation dedicated to ensuring that providers of wireless telecommunications services are meeting the needs of the more than 100 million users of wireless communications throughout the U.S. Wireless Consumers Alliance is very interested in the potential consumer benefits available through the use of smart chip cards to increase the utility of wireless communications and believes that increased competition will promote innovation in this area.

Electric Consumers' Alliance

Electric Consumers' Alliance represents and advocates the energy-related interests of approximately 300 consumer organizations throughout the U.S. Among the issues which Electric Consumers' Alliance actively pursues are consumer protection and the importance of competition to ensure consumer choice and product and service innovation.

Congress of California Seniors

The Congress of California Seniors is a coalition of community senior groups, church groups, labor retiree groups, and such other national groups as the Gray Panthers, Older Women's League. The coalition's principle function is to represent interests of seniors and others to protect and inform them about consumer issues.

Consumer Action

Consumer Action is non-profit, membership-based organization that serves consumers nationwide by advancing consumer rights, referring consumers to complaint handling agencies through our free hotline, publishing educational materials in many different languages, advocating for consumers in the media and before lawmakers, and comparing prices on credit cards, bank accounts, and long distance services.

Arizona Consumers Council

The Arizona Consumers Council is a statewide educational and advocacy organization that represents the interests of consumers throughout the state of Arizona before regulatory commissions, the legislature and the courts. It conducts research on issues of concern to consumers. It is a member of the Consumer Federation of America, Washington, DC.

Utility Consumers' Action Network

UCAN, the Utility Consumers' Action Network is a non-profit corporation with 40-50,000 members. UCAN's mission is to protect consumers from utility abuse, poor service, and excessive rate hikes, using every legal means available. The Privacy Rights Clearinghouse, one of UCAN's programs, is very active in efforts to reduce identity theft and improve Internet privacy, both of which can be addressed through development of smart chip cards.

California Small Business Roundtable

California Small Business Roundtable is an organization that makes public policy recommendations on behalf of California businesses. The roundtable is comprised of 40 of the key small business leaders in the state. They set public policy goals and objectives for government officials and organizations that improve the state's economic climate.

Consumer Coalition of California

Consumer Coalition of California (CCC) is active in protecting the rights of individual and small businesses consumers who are directly affected by the actions of major corporations and administrative law agencies. CCC has intervened before numerous California regulatory bodies and has testified before State and Federal agencies.

Jefferson County Committee for Economic Opportunity (JCCEO)

JCCEO is the community action agency of Jefferson County in Alabama, representing the interests of low-income consumers and provide a wide range of programs and services. JCCEO represents low-income consumer interests in regulatory and other related matters.

The California Alliance for Consumer Protection

The California Alliance for Consumer Protection (CACCP) was founded by Consumer Advocate Michael Ross to support the following concept: “Marketplace Competition is the best form of consumer protection”.

Florida Action Coalition Team

The Florida Action Coalition Team (FACT) is a non-partisan grassroots organization with thousands of advocates throughout the state active in taxpayer, consumer healthcare and environmental issues. FACT involves itself in the important political issues affecting Florida’s citizens.

Consumers for Affordable and Reliable Services

Consumers for Affordable and Reliable Services is a grass roots organization concerned with the well being of citizens of Alabama.

Children's Advocacy Institute

The Children's Advocacy Institute (CAI) is a part of the University of San Diego School of Law and a sister organization to the Center for Public Interest Law. It is an academic center and advocacy group representing the interests of children before agencies, the legislature, and courts, and training child advocates. CAI has an interest in assuring a competitive environment for credit, of particular importance to youth who often must or do rely on credit card based credit.

CERTIFICATE OF COMPLIANCE

Pursuant to Local Civil Rule 32(a)(7)(B), I hereby certify that by computerized count on Microsoft Word, there are no more than ____ words in this brief, excluding the attached Exhibit A. I further certify that the brief uses a proportionately-spaced font of 14-point type.

Dated: July 3, 2002

Ian Ayres

CERTIFICATE OF SERVICE

I hereby certify that, on this ____ day of July, 2002, I caused two copies each of this Brief Amicus Curiae of Undersigned Public Interest Groups in Support of Affirmance on the following counsel by first-class mail, postage prepaid:

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