UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NEW YORK

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IN RE PAYMENT CARD INTERCHANGE FEE and MERCHANT-DISCOUNT ANTITRUST LITIGATION :

This Document Relates to All Class Actions :

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ORAL ARGUMENT REQUESTED

REPLY MEMORANDUM OF LAW IN SUPPORT OF DEFENDANTS' MOTION TO EXCLUDE OPINIONS OF DR. GUSTAVO BAMBERGER

FILED UNDER SEAL

Plaintiffs' arguments in opposition to Defendants' motion to exclude Dr. Bamberger's testimony with respect to the intra-association claims are contrary to substantial case law and antitrust principles, which establish that (1) a but-for world *must* remove the challenged conduct – here, centrally-set default interchange, and (2) courts should not use the antitrust laws to regulate prices; instead, the antitrust laws are directed at competitive *conditions*. Plaintiffs do nothing to rebut the fact that Dr. Bamberger's opinions are wholly at odds with these principles, and accordingly should be excluded from evidence.

ARGUMENT

I. Dr. Bamberger Has Not Removed The "Collective" Establishment Of A Default Interchange Rate From His Primary "But For" World

As to Dr. Bamberger's primary "but for" world, plaintiffs argue that "Dr. Bamberger's analysis does not include any collectively-established default pricing rule . . . ." (Opp. Br. at 3.) Plaintiffs' argument is wrong: Dr. Bamberger's but-for world involves a collectively-set, default interchange payment term just as much as the actual world, only at a different rate – *i.e.*, zero or "par." As plaintiffs admit, their world *requires* network members "to accept, process and settle transactions." (Opp. Br. at 3). If issuers *must* accept merchant transactions forwarded by the acquirer, and *must* do so without the payment of a positive interchange fee, then that is not the absence of a collectively-set default payment term; it is simply a new default payment term set at zero. Indeed, it is precisely because this zero rate is a "default" rate applicable network-wide that Dr. Bamberger concludes for class certification purposes that a zero interchange rate would apply to all (or nearly all) merchants in his but-for world. (*Id.* at 5).

Plaintiffs' characterization of this new default requirement as the mere absence of a pricing rule (p. 13) is entirely semantic, without any substance. A true absence of any pricing rule would be the elimination of any "default" pricing mandate – that is, the parties to the transaction would be required to agree a price before any transaction could be processed. But that is not the world that plaintiffs or Dr. Bamberger propose. In Dr. Bamberger's but-for world, an issuer would not be free to say, "In the absence of some payment, I refuse to accept the transaction from this merchant, and will not pay the acquirer one hundred cents on the dollar." Instead, in Dr. Bamberger's but-for world the issuer would be required to accept the transaction at no charge. Thus, Dr. Bamberger's new default rate would mandate accepting the transaction at par, which is the fundamental difference between this case and the inapposite hypotheticals plaintiffs conjure (Opp. Br. at p. 13). It was in this same context that the court in *Brennan v. Concord EFS, Inc.*, 369 F. Supp. 2d 1127, 1131 (N.D.Cal. 2005), explained that "to say that [default] interchange fees should be abolished" is "the same thing as 'set at zero,'" which is itself a price. Although plaintiffs suggest that *Brennan* is distinguishable because it addressed a *per se* claim rather than a rule of reason claim, there is absolutely no basis to suggest the logic should apply any differently for a rule of reason claim.

Equally fallacious is Plaintiffs' assertion that this zero interchange world would result from "competition," not from any collectively-set pricing rule. According to plaintiffs, Dr. Bamberger's but-for world permits each issuer to "negotiate" bilaterally with merchants over a positive interchange fee, and it is that "competitive" dynamic which would result in a "zero" fee. But as plaintiffs themselves recognize, no merchant would ever choose to pay a positive interchange fee in their but-for world where issuers are *required*, under the default rules, to accept merchant's transactions at no charge.[1] (Opp. Br. at 4; Bamberger Decl. ¶¶ 83-84).

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[1] Plaintiffs misleadingly argue that merchants would not receive services for free in this but-for world, because they would still pay what they refer to as the *acquirer's* component of the merchant discount fee (Opp. Br. at 3-4 n. 2). This ignores the fact that the interchange paid

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Merchants would not volunteer to pay for something when a rule requires that they get it for free. The zero interchange rate is not the result of "competition," but of the new, default rule that requires that issuers process merchants' transactions at a fee of zero. Moreover, it is not disputed that bilateral negotiations are *already allowed* in the real world.[2] Accordingly, it is not the possibility of such bilateral negotiations in the but-for world that changes in Dr. Bamberger's but-for world, or which makes that world any more "competitive" than the real world. The *only* difference between the two worlds is that the default rule reduces the interchange rate to zero in the but-for world; there is no change in the price-setting *processes* whatsoever.

II. An Agreement To Establish Lower Default Interchange Fees Is Not A "Less Restrictive Alternative"

Plaintiffs do not dispute that Dr. Bamberger has not eliminated the alleged "collective" adoption of default interchange fees in his alternative "but for" world, in which default interchange fees would have been "collectively" set at (on average) 28% of current default interchange fees. (Opp. Br. at 2).

Instead, plaintiffs contend that even if some "collective" establishment of interchange fees is found to be necessary, the "less restrictive alternative" doctrine allows a fact-finder to determine that defendants should have set default interchange rates at a level no higher "than necessary to achieve the pro-competitive benefit of a viable network." (*Id.* at 5-6.) This

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to *issuers* would be zero, such that merchants would not be required to pay anything for the services and value issuers provide, such as the payment guarantee.

2 *See* Plffs. Mem. in Support of Class Cert. at 13 (quoting Visa rule allowing bilateral negotiations); MasterCard Worldwide, *MasterCard Worldwide Fact Sheet: Interchange and the Payments Industry* at 2 (May 2007), *available at* http://www.mastercard.com/us/company/en/docs/Interchange%20backgrounder.pdf.

assertion finds no support whatsoever in case law, and stands fundamental antitrust law principles on their head.

The "least restrictive alternative" doctrine has not been applied to price levels, and the cases relied on by plaintiffs do not suggest otherwise. (Opp. at p. 8). That doctrine addresses the question whether alternative *conduct* (*e.g.*, an alternative price-setting mechanism) – not alternative price *levels* – would achieve the same pro-competitive outcome in a less restrictive manner.[3] Put simply, a lower price is not itself "less restrictive" under the antitrust laws when the underlying conduct remains the same.

Plaintiffs' argument that interchange should have been reduced by 72%, or the lowest amount that would leave defendants "viable," would circumvent the well-established precedent holding that the antitrust laws are not designed to be a price regulatory mechanism. *See* Defendants' initial brief at pp. 12 – 13 & n. 9. Plaintiffs attempt to take issue with that proposition, arguing that the cases relied on by defendants involved claims under Section 2 of the Sherman Act, and not Section 1. (Opp. Br. at 14 – 15). But these fundamental principles have been applied to Section 1 claims as well. *See United States v. Trenton Potteries Co.*, 273 U.S. 392, 397-98 (1927) (lawfulness of price setting agreement must be judged "in the light of its effect on competition"; in absence of express legislation, courts should not attempt to determine reasonableness of price level); *Chicago Prof'l Sports Ltd. P'ship v. Nat'l Basketball Ass'n*, 95 F.3d 593, 597 (7th Cir. 1996) (court not authorized to alter amount of association-set fee). And, more fundamentally, there is no suggestion in any of these cases that the broad principles they

[3] There is a reason for this. The "least restrictive alternative" analysis has to do with what is least restrictive from the perspective of promoting competition or minimizing competitive restraints. A price is not itself a competitive restraint (except, potentially, in the extraordinary instances of predatory pricing or economic tying).

articulate apply only to Section 2 cases, and the logic of the cases – *i.e.*, that the antitrust laws are concerned with competitive conduct, not establishment of "proper" prices, which courts are ill-suited to determine – apply equally to Section 1 claims.

Plaintiffs also assert that the avoidance of price regulation is a concept applicable only for purposes of injunctive relief, not with respect to retroactive damages claims. (Plffs. Opp. Br. at 10). But this unsupported assertion fundamentally confuses the issue here. Of course, if liability is established a "but-for" inquiry into price is permissible for purposes of assessing *damages*. But this is not a normative inquiry into what price "ought" to have been; it is a factual inquiry into what price *would* have been in the absence of some offending conduct. What plaintiffs propose here is quite different: They propose to premise *liability itself* on the "wrong" price level having been selected, to the extent it exceeds the minimum necessary for their self-invented "viability" standard to be met. That is nothing more than a form of price regulation, and whether it is retrospective or prospective in its application makes no difference. The principles that bar a court from engaging in the exercise of determining what prices "ought" to be – as opposed to letting the market determine this fundamental outcome – are exactly the same. *See* Df. Mem. at 12 – 13.

III. There is No Presumption of Impact

Plaintiffs also assert that they are not required to submit any expert testimony in support of a but-for world, because there is purportedly a "presumption" that price fixing agreements impact all class members. *See* Opp. Br. at 11 – 12. Their argument, however, has no relevance to *this* motion, which deals with whether Dr. Bamberger's but-for worlds are admissible; at most their argument relates to the motion for class certification (which is already fully briefed).

In all events, plaintiffs' argument is based on a fundamental mischaracterization of case law. The primary authority on which they rely – *In re Master Key Antitrust Litig.*, 528 F.2d 5 (2d Cir. 1975) – does not hold that impact is "presumed" in price-fixing cases. Instead, it states that "[i]f the [plaintiffs] *establish at the trial for liability* that the defendants engaged in an unlawful national conspiracy *which had the effect of stabilizing prices above competitive levels*, . . . *we would think that the jury could reasonably conclude* that appellants' conduct caused injury to each appellee." *Id.* at 12 n.11 (emphasis added). This is in line with other cases relied on by plaintiffs, where a threshold showing of impact on class members must be made before injury can be established on a classwide basis. *See* Df. Mem. in Opp'n to Class Cert. at 44 - 45. Here, plaintiffs have not demonstrated – at trial or otherwise – that the alleged conspiracy "had the effect of stabilizing prices above competitive levels" for all class members. To the contrary, as demonstrated in defendants' opening brief and sur-reply in opposition to class certification, plaintiffs have not met their burden of demonstrating any such thing, and in fact it is more likely that the impact on class members would vary, requiring denial of class certification. Plaintiffs' reliance on other cases that purportedly support a "presumption" of impact is similarly misguided, as outlined in defendants' opposition to class certification. *Id.*

Moreover, plaintiffs' interpretation of the 34 year-old dicta from a footnote in *In re Master Key* is contrary to the Second Circuit's much more recent holding in *Miles*, which – far from allowing plaintiffs to rely on presumptions – holds that plaintiffs bear the burden of actually establishing that each requirement of Rule 23 has been met. *See Miles v. Merrill Lynch & Co., Inc.* (*In re Initial Public Offering Securities Litigation*), 471 F.3d 24, 40-41 (2d Cir. 2006). Plaintiffs must demonstrate that injury can be proven with common, classwide evidence, which Dr. Bamberger's legally-impermissible opinions cannot do.

Conclusion

For all of the foregoing reasons, as well as the reasons set forth in defendants' moving briefs, the opinions of Dr. Gustavo Bamberger relating to proof of damages and injury-in-fact with respect to the so-called "intra-network" conspiracy claims should be excluded.

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Respectfully submitted,

ARNOLD & PORTER LLP

By: /s/ Robert C. Mason
Robert C. Mason
399 Park Avenue
New York, NY 10022-4690
Tel: (212) 715-1000
Fax: (212) 715-1399
robert.mason@aporter.com

Robert J. Vizas
275 Battery Street, Suite 2700
San Francisco, CA 94111
Tel: (415) 356-3000
Fax: (415) 356-3099

Mark R. Merley
Matthew A. Eisenstein
555 12th Street, N.W.
Washington, DC 20004
Tel: (202) 942-5000
Fax: (202) 942-5999
Attorneys for Defendants Visa Inc., Visa U.S.A. Inc., and Visa International Service Association

PAUL, WEISS, RIFKIND, WHARTON & GARRISON LLP

By: /s/ Kenneth A. Gallo
Kenneth A. Gallo
Joseph J. Simons
2001 K Street, N.W.
Washington, DC 20006-1047
Tel: (202) 223-7300
Fax: (202) 223-7420
KGallo@paulweiss.com
JSimons@paulweiss.com
Bruce Birenboim
Andrew C. Finch
Gary R. Carney
1285 Avenue of the Americas
New York, NY 10019-6064
Tel: (212) 373-3000
Fax: (212) 757-3990
BBirenboim@paulweiss.com
AFinch@paulweiss.com
GCarney@paulweiss.com

HUNTON & WILLIAMS LLP
Keila D. Ravelo
Wesley R. Powell
200 Park Avenue
New York, NY 10166-0005
Tel: (212) 309-1000
Fax: (212) 309-1100

Attorneys for Defendants MasterCard Incorporated and MasterCard International Incorporated

MORRISON & FOERSTER LLP

By: /s/ Mark P. Ladner
Mark P. Ladner
Michael B. Miller
1290 Avenue of the Americas
New York, NY 10104-0050
Tel: (212) 468-8000
Fax: (212) 468-7900
mladner@mofo.com
Attorneys for Defendants Bank of America, NA., BA Merchant Services LLC (f/k/a Defendant National Processing, Inc.), Bank of America Corporation, and MBNA America Bank, N.A.

O'MELVENY & MYERS LLP

By: /s/ Andrew J. Frackman
Andrew J. Frackman
Edward D. Hassi
Peter C. Herrick
Times Square Tower
7 Times Square
New York, NY 10036
Tel: (212) 326-2000
Fax: (212) 326-2061
afrackman@omm.com
Attorneys for Defendants Capital One Bank (USA), N.A., Capital One, N.A., Capital One Bank, Capital One F.S.B., and Capital One Financial Corp.

SHEARMAN & STERLING LLP

By: /s/ James P. Tallon
James P. Tallon
Wayne D. Collins
Lisl J. Dunlop
599 Lexington Avenue
New York, NY 10022-6069
Tel: (212) 848-4000
Fax: (212) 848-7179
jtallon@shearman.com
Attorneys for Defendants Barclays Financial Corp., Barclays bank Delaware and Barclays Bank plc

SKADDEN, ARPS, SLATE, MEAGHER & FLOM, LLP

By: /s/ Peter E. Greene
Peter E. Greene
Cyrus Amir-Mokri
Peter S. Julian
Linda W. Cenedella
Four Times Square
New York, NY 10036
Tel: (212) 735-3000
Fax: (212) 735-2000
peter.greene@skadden.com
Attorneys for Defendants JPMorgan Chase & Co., Chase Bank USA, N.A., Chase Paymentech Solutions, LLC and JPMorgan Chase Bank, N.A. as acquirer of certain assets and liabilities of Washington Mutual Bank

SIDLEY AUSTIN LLP

By: /s/ Benjamin R. Nagin
Benjamin R. Nagin
787 Seventh Ave
New York, NY 10019
Tel: (212) 839-5300
Fax: (212) 839-5599
bnagin@sidley.com

David F. Graham
Eric H. Grush
One South Dearborn Street
Chicago, IL 60603
Tel: (312) 853-7000
Fax: (312) 853-7036
Attorneys for Defendants Citigroup Inc., Citicorp, and Citibank, N.A.

WILMER CUTLER PICKERING HALE AND DORR LLP

By: /s/ Christopher R. Lipsett
Christopher R. Lipsett
David S. Lesser
399 Park Avenue
New York, NY 10022
Tel: (212) 230-8800
Fax: (212) 230-8888
chris.lipsett@wilmerhale.com

A. Douglas Melamed
Ali M. Stoeppelwerth
Perry A. Lange
1875 Pennsylvania Ave., N.W.
Washington, DC 20006
Tel: (202) 663-6000
Fax: (202) 663-6363
Attorneys for HSBC Finance Corporation and HSBC North America Holdings, Inc.

KEATING MUETHING & KLEKAMP, PLL

By: /s/ Patrick F. Fischer
Patrick F. Fischer
Richard L. Creighton, Jr.
Drew M. Hicks
One East Fourth Street, Suite 1400
Cincinnati, OH 45202
Tel: (513) 579-6400
Fax: (513) 579-6457
pfischer@kmklaw.com
rcreighton@kmklaw.com
dhicks@kmklaw.com
Attorneys for Fifth Third Bancorp

JONES DAY

By: /s/ John M. Majoras
John M. Majoras
Joseph W. Clark
51 Louisiana Avenue, N.W.
Washington, DC 20001
Tel: (202) 879-3939
Fax: (202) 626-1700
jmmajoras@jonesday.com
jwclark@jonesday.com
Attorneys for Defendants National City Corporation, National City Bank of Kentucky

PULLMAN & COMLEY, LLC

By: /s/ Jonathan B. Orleans
Jonathan B. Orleans
850 Main Street
P.O. Box 7006
Bridgeport, CT 06601-7006
Tel: 203-330-2000
Fax: 203-576-8888
jborleans@pullcom.com
Attorney for Defendant Texas Independent Bancshares, Inc.

PATTERSON BELKNAP WEBB & TYLER LLP

By: /s/ Robert P. LoBue
Robert P. LoBue
Norman W. Kee
1133 Avenue of the Americas
New York, NY 10036
Tel.: 212-336-2596
Fax: 212-336-2222
rplobue@pbwt.com
Attorneys for Defendant Wells Fargo & Company, Wachovia Bank, NA., and Wachovia Corporation

ALSTON & BIRD LLP

By: /s/ Teresa T. Bonder
Teresa T. Bonder
Valerie C. Williams
1201 W. Peachtree Street, N.W.
Atlanta, GA 30309
Tel: (404) 881-7000
Fax: (404) 881-7777
teresa.bonder@alston.com

Naeemah Clark
90 Park Avenue
New York, NY 10016
Tel.: (212) 210-9400
Fax.: (212) 210-9444
Attorneys for Defendants Wachovia Bank, NA., Wachovia Corporation, and Suntrust Banks, Inc.

WASHINGTON MUTUAL[4]

[4] The defendants understand that, on September 26, 2008, defendant Washington Mutual, Inc. filed a voluntary petition under Chapter 11 of Title 11 of the United States Code in the United States Bankruptcy Court for the District of Delaware and, therefore, that the automatic bankruptcy stay, 11 U.S.C. § 362, applies to plaintiffs' claims against Washington Mutual, Inc. The matter is currently pending in that court as Bankruptcy Case No. 08-12229-MFW.