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December 16, 2010

John R. Read, Esquire
Chief, Litigation III Section
Antitrust Division
United States Department of Justice
450 Fifth Street, N.W.
Suite 4000
Washington, D.C. 20530

Via E-mail and FedEx

RECEIVED

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LITIGATION III, ANTITRUST DIV.
U.S. DEPT. OF JUSTICE

Re: ***United States of America, et al v. American Express Company, et al
Case No. 10-cv-4496 (E.D.N.Y.)***

Dear Mr. Read:

We are Liaison Counsel for the Individual Plaintiffs in direct action (*i.e.*, non-class) antitrust claims against Visa and MasterCard *In re Payment Card Interchange Fee and Merchant Discount Antitrust Litig.*, MDL 1720 (E.D.N.Y.), and we and several other law firms represent supermarkets and drug store chains who have filed direct action antitrust cases against American Express as well. *See, e.g., Walgreen Co. v. American Express Co. et al.*, Case No. 08-cv-2317 (E.D.N.Y.) Pursuant to the Antitrust Procedures and Penalties Act, 15 U.S.C. § 16, we are writing on behalf of those direct action plaintiffs to comment briefly on the Government's proposed Final Judgments with Visa and MasterCard.

We urge the Court to approve the proposed Final Judgments because we believe that they are pro-competitive and in the public interest. The proposed Final Judgments are a positive step in the effort to restore network (and issuing bank) competition on price for merchant acceptance of payment cards at the point of sale ("POS"). Visa's no-discount rule and MasterCard's no-discrimination rule restrain network price competition for merchant acceptance by preventing merchants from using POS discounts or other promotions to incent networks to offer merchants lower interchange rates. The proposed Final Judgments eliminate those anti-competitive rules and further promote competition by, among other things, allowing merchants both to inform cardholders of merchants' payment card acceptance costs and to use POS discounting or other promotions to steer cardholders to pay with lower cost forms of payment.

Despite the pro-competitive benefits of the proposed Final Judgments, they do not go far enough in removing Visa and MasterCard restraints which will continue to impair significantly price competition for merchant POS acceptance of payment cards. Among those network restraints which still need to be removed to restore competition are Visa's and MasterCard's no-

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surcharge rules (more accurately described as no-price rules). Those rules prevent price transparency at the point of sale as merchants cannot include in the ticket price their cost of accepting payment cards.¹ The costs to merchants of supplying goods and services vary across payment means and, as a result, customers who pay with cash or less expensive cards subsidize those who pay with more expensive cards (and who, ironically, are often more affluent). The most transparent and effective way to inform customers of the costs their payment means impose on merchants is to allow merchants to set an explicit "price" for alternative payment choices. A "surcharge" (which is simply a price related to costs and not an extra charge) can accomplish this result. Additionally, surcharging can eliminate the cross-subsidy which is a product of the networks' anti-competitive no-surcharge rules.

Merchants' ability to steer cardholders to pay with a lower cost payment means by surcharging incents the networks to compete on price for merchant acceptance at the POS to avoid the surcharge. A network which wants to avoid having its payment cards surcharged can charge lower acceptance fees which may make it uneconomic for merchants to surcharge the network's cards. It is the networks' desire not to be disfavored at the POS by merchant surcharging – more than discounting or promotions – which will cause networks to compete on price for merchant acceptance. Experience in other countries – notably Australia – where the networks have removed their no-surcharge rules empirically demonstrates that when networks have to compete on price for merchant acceptance to avoid surcharging, networks' interchange rates decline substantially and consumers win.

The functional distinction between discounting and surcharging is of critical importance to the competitive analysis here because of how easy it could be for Visa and MasterCard to circumvent the proposed Final Judgments through the imposition of new or higher merchant fees² that are not subject to market forces. Empirical evidence shows that discounting is not nearly as effective as surcharging in influencing buyer behavior.³ Moreover, there is not a

¹ "Ticket price" refers to the total payment due as stated on the sales receipt. Under the proposed Final Judgments, merchants can communicate their payment card acceptance costs to customers and offer discounts on price to customers who pay with a lower-cost payment means, but merchants still cannot include in the price to customers the merchants' acceptance cost if customers pay with a higher-cost form of payment.

² Our clients do not take issue with the existence of interchange fees. Rather, they take issue with the fact that those fees are not set by the market based on price competition among the networks and their respective issuing banks for merchant acceptance of their payment cards.

³ This does not make the networks' no-discount and no-discrimination rules any less anti-competitive.

sound business basis to discount for a great many merchants because their installed base of customers paying with cash or check or low-cost cards (*i.e.*, non-rewards cards) is so large. In that payments environment, surcharging (or removing the networks' honor-all-cards rules) is the only way for merchants to cover acceptance costs and for this installed base of customers not to subsidize the prices paid by the high-cost payment card customers. Removing the networks' no-surcharge rules is elegant in its simplicity as a competitive solution to Visa's and MasterCard's Merchant Restraints because it gives merchants a market-based means to discipline the price discussion between merchants and the networks about the fees charged merchants for acceptance of the networks' payment cards.

We realize that the proposed Final Judgments reflect an effort by Visa and MasterCard to resolve their contingent antitrust liability to the Government with regard to at least some of their Merchant Restraints. Footnote 3 in the Government's Competitive Impact Statement makes clear that the Government is not challenging the networks' no-surcharge rules or other network restraints "[a]t this time," and has left open the possibility that it could do so in the future. It is this indication that the Government is taking an incremental approach to the network restraints that allows our clients to support and endorse this intermediate step.

While we have reservations about the proposed Final Judgments, we realize that they represent an important incremental step by the Government in its effort to restore price competition for merchant POS acceptance of network payment cards. We therefore support the approval of the proposed Final Judgments by the Court. Our support of the proposed Final Judgments is not intended to suggest or imply that we think the Government has done enough. We do not, which is why our clients intend to continue to press forward with their antitrust claims against Visa and MasterCard (and American Express) to secure the removal of other network restraints which impair network price competition for merchant acceptance of payment cards at the point of sale.

Respectfully yours,



William G. Blechman

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