UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

IN RE PAYMENT CARD INTERCHANGE FEE AND MERCHANT DISCOUNT ANTITRUST LITIGATION

This Document Relates to:

All Class Actions

MASTER FILE 05-MD-1720 (JG) (JO)

ORAL ARGUMENT REQUESTED

REPLY MEMORANDUM IN SUPPORT OF MOTION TO DISMISS THE SECOND SUPPLEMENTAL CLASS ACTION COMPLAINT

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PRELIMINARY STATEMENT

As the moving defendants[1] set forth in our opening brief, and as Plaintiffs' opposition confirms, the Second Supplemental Class Action Complaint (the "Supplemental Complaint" or "SSC") alleges the same theory of anticompetitive effects alleged in the First Supplemental Class Action Complaint that the Court dismissed on November 25, 2008 (the "dismissed complaint"). As with MasterCard's IPO in the dismissed complaint, Plaintiffs posit that Visa's IPO is "substantially likely to harm competition by breathing new life into an anticompetitive business model that was placed on life support by the threat of antitrust enforcement." (Opp. Mem. at 20.) And as in the dismissed complaint, Plaintiffs argue that Visa's change of corporate structure -- purportedly undertaken to minimize risks under Section 1 of the Sherman Act -- instead threatens to substantially lessen competition by (1) creating a new "single entity" with the market power to raise interchange rates with impunity; (2) erecting "barriers to entry"; and (3) preserving the banks' "effective control" over Visa. (*Id.* at 23-32.)

With these same arguments before it, the Court previously rejected Plaintiffs' challenge to the MasterCard IPO. *See In re Payment Card Interchange Fee and Merchant Disc. Antitrust Litig.*, No. 05-MD-1720, 2008 WL 5082872, at *10 (E.D.N.Y. Nov. 25, 2008) ("Nov. 25, 2008 Op."). The Court found that Plaintiffs failed to allege plausible facts to suggest that MasterCard's independent board of directors, with fiduciary duties to act in MasterCard's best interests, would adopt the alleged restraints to benefit the banks at MasterCard's expense and that, as result, Plaintiffs did not adequately allege that the MasterCard IPO threatened to lessen competition substantially or caused any actual anticompetitive effects. *Id.*

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[1] Moving defendants are identified in footnote 1 of Defendants' Memorandum of Law in Support of Motion to Dismiss the Second Supplemental Class Action Complaint ("Def. Mem.").

Plaintiffs' opposition scarcely addresses the Court's reasoning. Instead, Plaintiffs seek to minimize the importance of bank control -- the key concept on which the Court relied -- by claiming that their "single entity with market power" and "barriers to entry" arguments are "not dependent upon any finding that the banks continue to control the 'new' networks." (Opp. Mem. at 23-24.) But Plaintiffs cannot dispute that they presented these supposedly "separate" arguments previously in connection with the motion to dismiss the First Supplemental Class Action Complaint.[2] And as the Court indicated in its November 25, 2008 opinion, given Plaintiffs' assertion that interchange rates, both before and after the IPO, are set by Visa's board of directors,[3] Plaintiffs now must "suggest *how* the Banks will nevertheless be able to control [Visa's] board of directors, and thereby *assure* the continued imposition of the allegedly supracompetitive interchange fees." Nov. 25, 2008 Op. at *9, *10 (emphasis added). Plaintiffs fail to do so.

As in the dismissed complaint, Plaintiffs allege no facts to make it *plausible* that the post-IPO Visa would adopt measures to benefit the banks at Visa's expense. Thus, Plaintiffs have not alleged that the Visa IPO is likely to lessen competition substantially, and the Supplemental Complaint should be dismissed.

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[2] *See*, *e.g.*, Reply to April 4, 2008 Objections to Feb. 12, 2008 Report and Recommendation, May 12, 2008 (DE 972), at 7 ("The end result of the IPO and Ownership and Control restrictions is a single entity with market power in the market for General Purpose Card Network Services -- the creation of such entities is precisely the harm that the antitrust merger laws are designed to prevent."); *id.* at 8 ("The Ownership and Control Restrictions decrease the likelihood of entry into the General Purpose Card Network Services market by eliminating the possibility of a low-fee competitior acquiring MasterCard.").

[3] Plaintiffs allege that Visa's board of directors retained "ultimate authority" over the alleged restraints both before and after the IPO. (Second Consolidated Amended Class Action Complaint ¶¶ 94, 431; *see also* Opp. Mem. at 17 (Visa's board has "the power to unilaterally determine . . . the interchange fees that will be transferred from merchants to issuers.").)

ARGUMENT

I. The Supplemental Complaint Alleges No Facts to Make It Plausible That the Banks "Control" the Post-IPO Visa

Notwithstanding the reasoning in the Court's November 25, 2008 opinion, Plaintiffs argue that "corporate-law" concepts of control "are inapplicable to an antitrust analysis." (Opp. Mem. at 2.) To Plaintiffs, it is enough that "the banks retain six out of 17 seats on the New Visa board," that Visa's stock affords so-called "control restrictions and veto rights," and that the banks have the "incentive to influence" Visa's decisions regarding the alleged restraints. (*Id.* at 30-31.) Plaintiffs argue that their allegations show that, post-IPO, the banks have *sufficient* control over Visa's decision-making to enable them to continue to impose the alleged restraints, and benefit the banks at Visa's expense. (*Id.* at 27-28.)

Plaintiffs made these arguments before, and the Court's November 25, 2008 opinion rejected them. There, too, Plaintiffs focused on the banks' alleged desire "to engage in anti-competitive conduct," their alleged "history of doing so," and the rules governing ownership of MasterCard shares. (02/12/08 Report and Recommendation (DE 906) ("R.R.") at 27; Pl. Mem. In Opp. to Mot. to Dismiss First Supp. Class Action Compl. (DE 539) at 19-24.) From those allegations, Plaintiffs pleaded that the "banks retain *enough* ownership and control to allow them -- effectively unmediated by outside influence -- to take unfair advantage of the greater freedom to act that MasterCard's new status as a single entity creates." (R.R. at 27-28.)

The Court's November 15, 2008 opinion disagreed, finding that "plaintiffs' allegations, and the reasonable inferences they create, actually demonstrate that the Banks *do not* retain sufficient control to allow them, for example, to continue to impose supracompetitive interchange fees." Nov. 25, 2008 Op. at *10 (emphasis added). The Court inferred from Plaintiffs' allegations that "a uniform interchange fee is not a profit-maximizing measure for

MasterCard itself," and that "an independent corporate director . . . would therefore oppose such fees, while a corporate director controlled by the Banks would support them." *Id.* Taking as true Plaintiffs' allegations that a majority of MasterCard's directors were independent of MasterCard's member banks and selected by common stockholders, the Court concluded that Plaintiffs "cannot plausibly allege that MasterCard will continue to impose supracompetitive interchange fees following its IPO, because its board would not be controlled by the Banks." *Id.*

As Defendants previously explained, the key allegations in the dismissed complaint underlying the Court's decision also appear in the Supplemental Complaint. (Def. Mem. at 7-8, 10-11.) On the critical issue of control, the Supplemental Complaint alleges no *new* or *different* facts -- and Plaintiffs point to none in their opposition -- to explain how the banks will control Visa's independent board of directors *after* the IPO, and thereby cause Visa to act anti-competitively. Plaintiffs' brief recites complaint allegations concerning *impressions* and *intentions* of various individuals about potential restructuring options *before* the IPO. (Opp. Mem. at 11-14.) But as we have argued (Def. Mem. at 14-15), the key issue is what Visa actually did in the IPO. In the post-IPO Visa, the banks have neither majority ownership nor voting control.

Plaintiffs point to *United States v. E.I. du Pont de Nemours & Co.*, 366 U.S. 316 (1961), on which the Report and Recommendation also relied (R.R. at 28), but that case is not inconsistent with the Court's November 15, 2008 analysis. There, du Pont purchased stock in General Motors so that du Pont could "entrench itself as the primary supplier of General Motors' requirements for automotive finishes and fabrics." *du Pont*, 353 U.S. 586, 606 (1957). The Court found that this stock purchase "led to the insulation of most of the General Motors' market from free competition," in violation of Section 7. *Id.* at 589. In a subsequent opinion, the Court

rejected a proposed remedy under which du Pont would retain ownership of General Motors stock, but distribute the stock's voting rights to du Pont's shareholders. 366 U.S. 316, 331-32. The Court held that, although du Pont "the corporation" no longer had voting rights, anticompetitive effects could still occur because a group with similar interests as du Pont -- its shareholders -- held the voting rights. *Id.*

Here, however, Plaintiffs do not allege that Visa's IPO divested the banks' voting rights to bank shareholders or anyone else with interests aligned with the banks. To the contrary, there is no dispute that only members of the public (not banks) may vote for Visa's board of directors, and a majority of directors "must be independent directors in accordance with New York Stock Exchange and SEC rules."[4] Consistent with the Court's prior ruling, these independent directors "would theoretically oppose any efforts to enrich the Banks at [Visa's] expense." Nov. 25, 2008 Op. at *10.[5]

II. The Court Has Already Rejected Plaintiffs' Argument That a Fifteen Percent Ownership Limitation Constitutes a Barrier to Entry

Plaintiffs assert that the 15% ownership limitation on Visa's common stock serves to "protect[ ] the most effective means of entry into the payment card market," because "it may well be easier for a competitor to enter the market by acquiring Visa or MasterCard than by building its own network from the ground up." (Opp. Br. at 26.) However, Plaintiffs' assertions

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[4] *See* Decl. of Michael R. Hartman in Support of Mot. to Dismiss, Ex. A (Visa Inc., Amend. No. 4 to Form S-1 Registration Statement (Form S-1/A) (Feb. 25, 2008)), at 177.

[5] For this same reason, Plaintiffs' reliance on *United States v. Dairy Farmers of America*, 426 F.3d 850 (6th Cir. 2005), is misplaced. There, a milk marketing organization acquired a milk processing plant, resulting in a monopoly on the market for school milk in certain locations. *Id.* at 851. The acquiring marketing organization attempted to cure potential antitrust problems by conveying its voting rights in the plant to the organization's business partner. The Court ruled that this divestiture did not resolve concerns about the lessening of competition, because the organization and its business partner had "closely aligned interests to maximize profits via anticompetitive behavior." *Id.* at 862. In this case, the interests of the banks and Visa's independent directors are not "closely aligned" in the same way. Nov. 25, 2008 Op. at *10.

are misplaced, given that Visa is controlled by independent directors with fiduciary duties to act in Visa's best interests, and not the interests of the banks. As the Court previously found, given an "independent MasterCard, . . . by plaintiffs' own allegations, a takeover by some trust-busting white knight (which plaintiffs allege is impossible due to the 15% limit on ownership of [MasterCard's] class A shares) *is not required* to prevent the imposition or continuation of MasterCard's allegedly anticompetitive practices." Nov. 25, 2008 Op. at *10 (emphasis added). The Court should reach the same conclusion here.

In addition, the 15% cap on ownership by a single shareholder does not threaten competition unless it prevents the entry by a firm that would increase the number of competitors and reduce market concentration. Even if the 15% rule served as a barrier preventing a company from buying Visa, it has no anticompetitive effect. Mere "replacement of one [party] with another [is] an action having little evident effect on competition." *Sullivan v. NFL*, 34 F.3d 1091, 1099 (1st Cir. 1994); *see also Levin v. Nat'l Basketball Assoc.*, 385 F. Supp. 149 (S.D.N.Y. 1974) (barring defendant from buying into league of 17 teams by purchasing an existing team, which remained in existence after the rejected purchase, was not anticompetitive).[6]

Moreover, Plaintiffs allege no facts to support their assertion that a single purchaser of more than 15% of the voting control of Visa would operate Visa any differently -- or more competitively -- than it is now operated as a public company, whether that hypothetical purchaser would be a merchant (who would have no incentive to set lower interchange fees for transactions at its merchant competitors) or someone else. Plaintiffs cannot satisfy their burden

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[6] *Bon-Ton Stores, Inc. v. May Dep't Stores Co*, 881 F. Supp. 860 (W.D.N.Y. 1994), cited by Plaintiffs, is not to the contrary. There, the court enjoined defendant from purchasing the assets of an existing competitor who was going out of business because "the market concentration of [defendant] would increase dramatically after the acquisition." *Id.* at 875.

of establishing a "reasonable probability" of anticompetitive effects based on speculative allegations. *See United States v. Marine Bancorporation*, 418 U.S. 602, 623 (1974) ("ephemeral possibilities" will not satisfy Section 7).

III. Plaintiffs Have Offered No Allegations to Support the Conclusion That the Creation of a "Single Entity" Threatens Substantially to Lessen Competition

Plaintiffs describe their "single entity" theory as follows: "The Restructurings harmed competition because but for the Restructurings, the Networks' supracompetitive interchange fees would be subject to elimination through enforcement of antitrust laws prohibiting collusive activity." (Opp. Mem. at 25.) This argument *assumes* that a post-IPO independent Visa would impose supracompetitive interchange rates, even if not in Visa's best interests. Under the Court's November 25, 2008 decision, that logic fails.

Plaintiffs' "single entity" argument fails for other reasons as well. Plaintiffs concede that the Clayton Act "is more concerned with market structure than with conduct," and that the "central focus of Section 7 is preventing the creation of firms with market power." (*Id.* at 22, 24.) As a result, Section 7 "provides for scrutiny of a transaction to evaluate if the acquisition will tend to increase concentration of market power and/or inhibit competition." *Geneva Pharms. Tech. Corp. v. Barr Labs. Inc.*, 386 F.3d 485, 511 (2d Cir. 2004). Thus, where an "acquisition itself [has] no effect on the degree of concentration or competition in the [relevant] market," a plaintiff cannot allege potential antitrust harm from the acquisition. *Id.*[7]

Here, Plaintiffs have not alleged (because they cannot) that the Visa IPO has increased concentration in, or Visa's market share of, any alleged relevant market. Although Plaintiffs

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[7] As discussed in MasterCard's reply memorandum, Plaintiffs miscite the Second Circuit's *Geneva Pharmaceuticals* decision and the Supreme Court's decisions in *Addyston Pipe & Steel Co. v. United States*, 175 U.S. 211 (1899), and *Northern Securities Company v. United States*, 193 U.S. 197 (1904). *See* Reply Memorandum in Support of Motion to Dismiss the First Amended Supplemental Class Action Complaint ("MC Reply Mem.") at 3-4 & n.6.

assert that the Visa IPO created a single entity "with market power and the attendant ability to continue increasing interchange fees" (Opp. Mem. at 17), only the identity of Visa's owners has changed as result of the IPO. Plaintiffs do not allege that the composition and concentration of any relevant market has changed at all.

Finally, as discussed in detail in MasterCard's reply memorandum, Plaintiffs cannot plausibly argue that the antitrust laws prevent Visa from changing its purportedly impermissible pre-IPO structure, including through transactions like the IPO. In effect, Plaintiffs seem to be suggesting that Visa's structure was unlawful pre-IPO, and that Visa also cannot change that structure unless it is prevented from setting interchange rates at all (or is required to set some judicially regulated rates). There is no basis in antitrust law for Plaintiffs' theory. *See* MC Reply Mem. at 4-5. (Visa hereby incorporates by reference the reasoning set forth in MasterCard's Reply Memorandum in Support of Motion to Dismiss the First Amended Supplemental Class Action Complaint, insofar as it addresses parallel allegations in the Supplemental Complaint challenging the Visa IPO.)

CONCLUSION

For the foregoing reasons, the Second Supplemental Class Action Complaint should be dismissed with prejudice.

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