UNITED STATES COURT OF APPEALS

FOR THE TENTH CIRCUIT

VISA U.S.A. INC.,

Defendant-Appellant

v.

SCFC ILC, INC. d/b/a
MountainWest Financial, Inc.

Plaintiff-Appellee.

Case No. 93-4105

Civil No. 2:91-CV-047B
Honorable Dee V. Benson
Utah, Central Division

OPENING BRIEF OF APPELLANT VISA U.S.A. INC.

On Appeal from the
District Court of the United States
District of Utah, Central Division

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P-1234

ORAL ARGUMENT REQUESTED

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES . . . iii

RELATED APPEAL . . . xiii

I. INTRODUCTION . . . 1

II. STATEMENT OF JURISDICTION . . . 2

III. STATEMENT OF ISSUES PRESENTED FOR REVIEW . . . 2

A. SHERMAN ACT SECTION 1 (15 U.S.C. § 1) . . . 2

B. CLAYTON ACT SECTION 7 (15 U.S.C. § 18) . . . 3

IV. STATEMENT OF FACTS . . . 4

A. ORIGINS OF THE GENERAL PURPOSE CHARGE CARD . . . 4

B. VISA . . . 6

C. INTERSYSTEM COMPETITION . . . 9

D. SEARS' EFFORTS TO JOIN VISA . . . 15

E. TRIAL COURT PROCEEDINGS . . . 16

1. The Antitrust Claims . . . 16

2. The Trial . . . 17

3. Post-Trial Proceedings . . . 19

4. VISA's Motion Under 28 U.S.C. § 1292(b) . . . 20

V. STANDARD OF REVIEW . . . 20

VI. ARGUMENT . . . 21

A. THE DISTRICT COURT ERRONEOUSLY SUSTAINED THE JURY VERDICT ON SEARS' CLAIM UNDER SECTION 1 OF THE SHERMAN ACT . . . 21

1. Introduction . . . 21

TABLE OF CONTENTS

Page

2. The Court Applied an Incorrect Legal Standard 22

a. The Court's Role Under the Rule of Reason 24

b. This Is a "Structure" Not a "Conduct" Case 27

c. Sears Should Have Been Required to Demonstrate That Membership in VISA Is Necessary for It to Compete in the Relevant Market 31

d. Prior Cases Are Consistent with VISA's Position 37

3. Sears Failed as a Matter of Law to Demonstrate That VISA's Exclusion of Sears Unreasonably Restrains Competition 42

a. As a Matter of Law, Sears Failed to Demonstrate That VISA Possesses Market Power in the Relevant Market 42

b. Sears Failed to Demonstrate Any Harm to Competition 49

c. Sears' Alternative "Disincentive" Theory Is Legally Irrelevant and Proves Nothing About the Effect of VISA's Exclusion of Sears . . . 57

d. As a Matter of Law, the Benefits to Intersystem Competition from By-law 2.06 Outweigh Any Restraint on Intrasystem Competition 61

B. THE COURT ERRONEOUSLY CONCLUDED THAT SEARS' ACQUISITION OF A PARTIAL OWNERSHIP INTEREST IN VISA DOES NOT VIOLATE SECTION 7 OF THE CLAYTON ACT 67

1. Analysis of Market Structure Should Have Created a Presumption of Illegality 68

2. The Court's Analysis of Likely Competitive Effects Did Not Adequately Take Account of Sears' Changed Incentives 71

3. The Court Erred by Balancing the Acknowledged Harms to Intersystem Competition Against Potential Benefits to Intrasystem Competition 73

VI. CONCLUSION 74

TABLE OF AUTHORITIES

CASES Page

AA Poultry Farms, Inc. v. Rose Acre Farms, Inc.,
881 F.2d 1396 (7th Cir. 1989),
cert. denied, 494 U.S. 1019 (1990) . . . . *passim*

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152 F. Supp. 387 (S.D.N.Y. 1957),
aff'd, 259 F.2d 524 (2d Cir. 1958) 67

American Floral Servs., Inc. v. Florists' Transworld Delivery Ass'n,
633 F. Supp. 201 (N.D. Ill. 1986) 33, 39

Anago Inc. v. Tecnol Med. Prods., Inc.,
792 F. Supp. 514 (N.D. Tex.),
aff'd, 976 F.2d 248 (5th Cir. 1992) 58, 60

Appalachian Coals, Inc. v. United States,
288 U.S. 344 (1933) 24

Aspen Skiing Co. v. Aspen Highlands Skiing Corp.,
472 U.S. 585 (1985) 12, 13, 28, 31

Assam Drug Co. v. Miller Brewing Co.,
798 F.2d 311 (8th Cir. 1986) 26

Associated Press v. United States,
326 U.S. 1 (1945) 37, 39, 40, 41, 42

Atlantic Richfield Co. v. USA Petroleum Co.,
495 U.S. 328 (1990) 58, 59, 60

Bacchus Indus., Inc. v. Arvin Indus., Inc.,
939 F.2d 887 (10th Cir. 1991) 47, 53

Ball Memorial Hosp., Inc. v. Mutual Hosp. Ins., Inc.,
784 F.2d 1325 (7th Cir. 1986) 44, 47, 51, 54, 56

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978 F.2d 98 (3d Cir. 1992) 44, 47, 52, 54, 60

Barry Wright Corp. v. ITT Grinnell Corp.,
724 F.2d 227 (1st Cir. 1983) 51

Board of Trade of City of Chicago v. United States,
246 U.S. 231 (1918) 25, 50

TABLE OF AUTHORITIES

CASES Page

Broadcast Music, Inc. v. CBS,
441 U.S. 1 (1979) 26, 41

Brook Group Ltd. v. Brown & Williamson Tobacco Corp.,
113 S. Ct. 2578 (1993) . . . . *passim*

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370 U.S. 294 (1962) 72

Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.,
429 U.S. 477 (1977) 56, 58

Cargill, Inc. v. Monfort of Colorado, Inc.,
479 U.S. 104 (1986) 58

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961 F.2d 667 (7th Cir.),
cert. denied, 113 S. Ct. 409 (1992) 29

City of Anaheim v. Southern Cal. Edison Co.,
955 F.2d 1373 (9th Cir. 1992) 39

City of Chanute v. Williams Natural Gas Co.,
955 F.2d 641 (10th Cir.)
cert. denied, 113 S. Ct. 96 (1992) 35

City of Rohnert Park v. Harris,
601 F.2d 1040 (9th Cir. 1979),
cert. denied, 445 U.S. 961 (1980) 58

Continental T.V., Inc. v. GTE Sylvania, Inc.,
433 U.S. 36 (1977) 32

Copperweld Corp. v. Independence Tube Corp.,
467 U.S. 752 (1984) 26, 56

Corsearch, Inc. v. Thomson & Thomson,
792 F. Supp. 305 (S.D.N.Y. 1992) 13

Daubert v. Merrell Dow Pharmaceuticals, Inc.,
113 S. Ct. 2786 (1993) 52, 53

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387 U.S. 485 (1967) 67, 70

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234 U.S. 600 (1914) 26, 40

TABLE OF AUTHORITIES

CASES Page

Eastman Kodak Co. v. Image Technical Servs., Inc., 112 S. Ct. 2072 (1992) 20, 52

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Farrell v. Klein Tools, Inc., 866 F.2d 1294 (10th Cir. 1989) 60

Fashion Originators' Guild v. FTC, 312 U.S. 457 (1941) 26, 40

Florida Fuels, Inc. v. Belcher Oil Co., 717 F. Supp. 1528 (S.D. Fla. 1989) 13

Ford Motor Co. v. United States, 405 U.S. 562 (1972) 73, 74

Fox v. Mazda Corp., 868 F.2d 1190 (10th Cir. 1989) 20

FTC v. Indiana Fed'n of Dentists, 476 U.S. 447 (1986) 45

FTC v. University Health, Inc., 938 F.2d 1206 (11th Cir. 1991) 63, 73

FTC v. Warner Communications Inc., 742 F.2d 1156 (9th Cir. 1984) 71

GAMCO, Inc. v. Providence Fruit & Produce Bldg., Inc., 194 F.2d 484 (1st Cir.), cert. denied, 344 U.S. 817 (1952) 39

Hamilton Watch Co. v. Benrus Watch Co., 114 F. Supp. 307 (D. Conn.), aff'd, 206 F.2d 738 (2d Cir. 1953) 71

Indiana Grocery, Inc. v. Super Valu Stores, Inc., 864 F.2d 1409 (7th Cir. 1989) 47

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CASES | Page

Marrese v. American Acad. of Orthopaedic Surgeons, 706 F.2d 1488 (7th Cir. 1983), rev'd on other grounds, 470 U.S. 373 (1985) 32

Marrese v. American Acad. of Orthopaedic Surgeons, 1991-1 Trade Cas. (CCH) ¶ 69,398 (N.D. Ill. 1991), aff'd, 977 F.2d 585 (7th Cir. 1993) 26

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McKenzie v. Mercy Hosp., 854 F.2d 365 (10th Cir. 1988) 27, 39, 40

McMurray v. Deere & Co., 858 F.2d 1436 (10th Cir. 1988) 60

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Mid-State Fertilizer Co. v. Exchange Nat'l Bank, 877 F.2d 1333 (7th Cir. 1989) 52

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National Soc'y of Prof'l Engineers v. United States, 435 U.S. 679 (1978) 24

TABLE OF AUTHORITIES

CASES Page

NCAA v. Board of Regents of Univ. of Okla.,
468 U.S. 85 (1984) 25, 41

Newman v. Hy-Way Heat Sys., Inc.,
789 F.2d 269 (4th Cir. 1986) 53

Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.,
472 U.S. 284 (1985) 37, 39, 41

Olympia Equip. Leasing Co. v. Western Union Tel. Co.,
797 F.2d 370 (7th Cir. 1986),
cert. denied, 480 U.S. 934 (1987) . . . . *passim*

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672 F.2d 1280 (7th Cir. 1982) 32

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899 F.2d 951 (10th Cir.),
cert. denied, 497 U.S. 1005 (1990) 42, 44, 56

Reazin v. Blue Cross & Blue Shield,
663 F. Supp. 1360 (D. Kan. 1987),
aff'd, 899 F.2d 951 (10th Cir.),
cert. denied, 497 U.S. 1005 (1990) 66

Reserve Supply Corp. v. Owens-Corning Fiberglass Corp.,
971 F.2d 37 (7th Cir. 1992) 48

Richardson by Richardson v. Richardson-Merrell, Inc.,
857 F.2d 823 (D.C. Cir. 1988),
cert. denied, 493 U.S. 882 (1989) 49, 52

Rothery Storage & Van Co. v. Atlas Van Lines, Inc.,
792 F.2d 210 (D.C. Cir. 1986),
cert. denied, 479 U.S. 1033 (1987) 32, 39, 44, 54, 71

RSR Corp. v. FTC,
602 F.2d 1317 (9th Cir. 1979),
cert. denied, 445 U.S. 927 (1980) 74

Rural Telephone Service Co. v. Feist Publications, Inc.,
957 F.2d 765 (10th Cir.),
cert. denied, 113 S. Ct. 490 (1992) 51, 60

TABLE OF AUTHORITIES

CASES Page

SCFC ILC, Inc. v. VISA U.S.A. Inc.,
936 F.2d 1096 (10th Cir. 1991) 16, 19
819 F. Supp. 956 (D. Utah 1993) . . . . *passim*
801 F. Supp. 517 (D. Utah 1992) 16
1993-1 Trade Cas. (CCH) ¶ 70,099 (D. Utah 1992) 19
784 F. Supp. 822 (D. Utah 1992) 17
763 F. Supp. 1094 (D. Utah 1991),
vacated, 936 F.2d 1096 (10th Cir. 1991) 16

Schachar v. American Acad. of Ophthalmology, Inc.,
870 F.2d 397 (7th Cir. 1989) 27, 32, 39, 42, 51

Smith v. FMC Corp.,
754 F.2d 873 (10th Cir. 1985) 60

Spectrum Sports, Inc. v. McQuillan,
113 S. Ct. 884 (1993) 60

Standard Oil Co. v. United States,
221 U.S. 1 (1911) 24, 38

Sun Dun, Inc. v. Coca-Cola Co.,
740 F. Supp. 381 (D. Md. 1990) 32

Sun Ref. & Mktg. Co. v. Statheros Shipping Corp.,
761 F. Supp. 293 (S.D.N.Y.),
aff'd, 948 F.2d 1277 (2d Cir. 1991) 31

Sunkist Growers, Inc. v. Winckler & Smith Citrus Prods. Co.,
370 U.S. 19 (1962) 57

Tarabishi v. McAlester Regional Hosp.,
951 F.2d 1558 (10th Cir. 1991),
cert. denied, 112 S. Ct. 2996 (1992) 27, 40

Thomas v. Hoffman-LaRoche, Inc.,
949 F.2d 806 (5th Cir.),
cert. denied, 112 S. Ct. 2304 (1992) 66

TV Communications Network, Inc. v. TNT, Inc.,
964 F.2d 1022 (10th Cir.)
cert. denied, 113 S. Ct. 601 (1992) 32

United States v. Amax, Inc.,
402 F. Supp. 956 (D. Conn. 1975) 74

TABLE OF AUTHORITIES

CASES | Page

United States v. Associated Press,
52 F. Supp. 362 (S.D.N.Y. 1943),
aff'd, 326 U.S. 1 (1945) 39

United States v. Colgate & Co.,
250 U.S. 300 (1919) 31, 38

United States v. E.I. du Pont de Nemours & Co.,
366 U.S. 316 (1961) 38

United States v. E.I. du Pont de Nemours & Co.,
353 U.S. 586 (1957) 63, 73

United States v. El Paso Natural Gas Co.,
376 U.S. 651 (1964) 72

United States v. Penn-Olin Chem. Co.,
378 U.S. 158 (1964) 35, 67, 72

United States v. Philadelphia Nat'l Bank,
374 U.S. 321 (1963) 74

United States v. Realty Multi-List, Inc.,
629 F.2d 1351 (5th Cir. 1980) 39

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224 U.S. 383 (1912) 38, 39, 40, 41

United States v. Topco Assocs.,
405 U.S. 596 (1972) 24

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438 U.S. 422 (1978) 24

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822 F.2d 656 (7th Cir.),
cert. denied, 484 U.S. 977 (1987) 26

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796 F.2d 1216 (10th Cir. 1986),
cert. denied, 486 U.S. 1005 (1988) 31, 42, 47

White v. Conoco, Inc.,
710 F.2d 1442 (10th Cir. 1983) 21

TABLE OF AUTHORITIES

CASES Page

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STATUTES, RULES

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Sherman Act § 2, 15 U.S.C. § 2 . . . . . 27, 28, 31

28 U.S.C. § 1292 . . . . . 2, 20
§ 1331 2
§ 1337 2

Fed. R. App. P. 28 4

Fed. R. Civ. P. 12 30
50 . . . . . 19, 22, 67
52 21
59 . . . . . 19, 67

10th Cir. R. 30.1.3 1

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Page

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Page

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RELATED APPEAL

SCFC ILC, Inc. v. VISA U.S.A. Inc., 936 F.2d 1096 (10th Cir. 1991) (Holloway, C.J., Ebel, J., Bright, J.).

I. INTRODUCTION

The question presented by this appeal is one of surpassing significance for American antitrust and industrial policy: May an entity which declined the opportunity to participate in a joint venture and elected, instead, to compete successfully against it thereafter demand the right to also become a member of the venture? That is plaintiff's claim in this case and the jury endorsed it. The district court, although declaring at one point that "I would have hung the jury before I would have come back with that verdict" (App. 1592),[1] nonetheless felt constrained to let it stand. As we demonstrate below, that was error.

VISA is a joint venture[2] that took substantial risks and incurred tremendous costs to develop and promote the widespread acceptance of a new product -- the general purpose charge card. Sears is the issuer of the competing Discover card.[3] Discover today boasts over 42 million cardholders and is accepted by virtually every major merchant in the country. Indeed, within five years of Discover's introduction, Sears had become the second largest issuer of general purpose charge cards in the country. Despite this spectacular success as a competitor against VISA, and despite having foregone membership in VISA some eight years ago, Sears now seeks to force entry into the venture so that it can issue VISA cards, too.

There are two principal reasons why that should not be permitted. First, requiring parties to share the fruits of their successful investments in economically risky

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[1] "App." refers to VISA's Appendix, filed separately herewith; page numbers beginning with an "S" are contained in the Addendum to VISA's Appendix filed under seal pursuant to 10th Circuit Rule 30.1.3.

[2] VISA is a non-stock corporation owned by its numerous members who are authorized to use the VISA name and associated trademarks and symbols in offering consumers and merchants a number of payment products, including, most prominently, the VISA credit card.

[3] We continue the trial court's practice of referring to plaintiff, SCFC ILC, Inc., as "Sears." Since the trial, Sears has begun a process of divesting the Dean Witter group of companies, which includes both Discover and SCFC, into a free-standing corporation. That fact has no bearing on any of the issues discussed herein.

innovation necessarily will have an adverse effect upon the incentives of firms to undertake such innovation in the first place. Second, permitting existing intersystem rivals to become part-owners of a major competitor necessarily will reduce competition at the system level, where the market already is highly concentrated.

The result reached below -- compelling a joint venture to accept a system-level competitor as a member -- is literally unprecedented. What is more, there is a curious -- and telling -- mismatch in this case between the supposed competitive problem and the suggested solution to it. If, as Sears contends, the problem is that VISA possesses too much market power, then surely the answer is not to add to that power by letting Sears in. In short, it is not the exclusion, but the potential inclusion of Sears in VISA that raises antitrust concerns because of its effect upon intersystem competition. Indeed, such inclusion would effect an unlawful partial merger between Sears and VISA in violation of Section 7 of the Clayton Act.

II. STATEMENT OF JURISDICTION

The district court's jurisdiction over this case is based on 28 U.S.C. §§ 1331 & 1337. On April 26, 1993 the district court certified its post-trial Opinion and Order[4] for immediate interlocutory appeal pursuant to 28 U.S.C. § 1292(b). App. 302. On May 6, 1993 VISA filed a timely petition for permission to appeal pursuant to Section 1292(b), and on May 28, 1993 the petition was granted by this Court. App. 304.

III. STATEMENT OF ISSUES PRESENTED FOR REVIEW

A. SHERMAN ACT SECTION 1 (15 U.S.C. § 1)

1. As a matter of law, may a joint venture decline to share its property, including its trademarks and proprietary systems, with an existing competitor that is capable of and is competing successfully on its own against the joint venture and its

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[4] The district court's Opinion and Order, reported as SCFC ILC, Inc. v. VISA U.S.A. Inc., 819 F. Supp. 956 (D. Utah 1993), is referred to as "Opn." Page references are to the published version of the opinion.

members; alternatively, was it error for the court to submit plaintiff's Sherman Act Section 1 claim to the jury under instructions that permitted the jury to return a verdict for Sears without finding that Sears is unable to compete successfully in the relevant market absent access to VISA's property?

2. Where plaintiff alleges that VISA By-law 2.06 unreasonably restrains competition in the issuance of general purpose charge cards, does its claim fail as a matter of law where the record will not support a finding that By-law 2.06 gives VISA or its members the power to raise prices or restrict output in the market?

3. As a matter of law, was it error for the trial court to permit the jury to base its verdict in this case on evidence purporting to show that VISA's membership rule excluding successful intersystem competitors, such as Sears and American Express, allegedly might injure competition by creating a "disincentive" for entities <u>other than</u> Sears and American Express to start their own charge card systems?

4. As a matter of law, was it error for the trial court to permit the jury to base its verdict in this case on evidence purporting to show that VISA "discriminated" against and competed "unfairly" with Discover?

B. CLAYTON ACT SECTION 7 (15 U.S.C. § 18)

1. As a matter of law, was it error for the trial court to conclude that permitting Sears to become a VISA member is not likely <u>substantially</u> to lessen intersystem competition in the relevant market, where undisputed facts demonstrate: (a) that system-level competition in the general purpose charge card market is highly concentrated, and (b) that Sears' entry into VISA is likely to lessen system-level competition in connection with the merchant acceptance and systems portion of the general purpose charge card business?

2. As a matter of law, was it error for the trial court to conclude that Sears' proposed acquisition of an ownership interest in VISA does not violate Section 7 of the Clayton Act on the basis of self-serving statements of Sears' intention to maintain the

Discover card as a vigorous intersystem competitor in the event that Sears becomes a VISA owner-member and issues a VISA card?

3. As a matter of law, in determining whether Sears' proposed acquisition of an ownership interest in VISA violates Section 7, was it error for the court to balance the potential harm to intersystem competition resulting from the acquisition against alleged potential benefits to intrasystem competition resulting from Sears' proposed VISA membership?

IV. STATEMENT OF FACTS[5]

A. ORIGINS OF THE GENERAL PURPOSE CHARGE CARD

This case concerns the general purpose charge card – a product of such ubiquity that it is difficult to recall a world in which the question, "Will that be cash, check or charge?" did not exist. Prior to the mid-1950s, however, there was no such thing as a general purpose credit or charge card. Local transactions typically were conducted by cash or check. Some larger merchants offered their regular customers a form of open book ("30 day") or revolving credit account and the oil companies had begun to offer charge cards for the purchase of gasoline and related accessories.[6]

In the early 1950s American Express and Diners Club created the so-called "Travel and Entertainment," or "T&E," card that could be used by business and pleasure travelers to purchase lodging or meals at a variety of establishments. EFT ¶ 1.02[3]; Baxter, Bank Interchange of Transactional Paper: Legal and Economic Perspectives, 26 J.L. & Econ. 541, 573 (1983). At about the same time, a number of banks perceived the need for a more ubiquitous payment service option. Id. ¶ 23.02[1]; Baxter, supra, at 574.

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[5] VISA submits subsection E of this Section (infra pp. 16-20) as its Statement of the Case for purposes of Fed. R. App. P. 28(a)(4).

[6] See D. Baker & R. Brandel, The Law of Electronic Fund Transfer Systems ¶¶ 1.02[3], 23.02[1] (2d ed. 1988) (hereafter "EFT"); National Bancard Corp. (NaBanco) v. VISA U.S.A., Inc., 596 F. Supp. 1231, 1236-37 (S.D. Fla. 1984), aff'd, 779 F.2d 592 (11th Cir.), cert. denied, 479 U.S. 923 (1986).

Their challenge was to create a new product that could both facilitate the purchase of goods and services and respond to consumers' demand for increased buying power. The response was the general purpose charge card: a card that could be used to purchase goods or services not just at a particular, local merchant but at numerous retail stores located across a wide area. The card would not only be accepted at places where the customer was completely unknown, but would permit cardholders to extend the repayment of their purchases through a pre-approved line of credit that they could draw on at any time. Brandel & Leonard, Bank Charge Cards: New Cash or New Credit, 69 Mich. L. Rev. 1033, 1035-37 (1971).

The concept was elegant but extraordinarily complex and, hence, economically risky. To begin with, there was the so-called "chicken-and-egg" problem. For a charge card to have utility to the customer, it needed to be usable at many merchant locations. However, merchants would only agree to accept the new card if enough customers carried and used it to make it worthwhile for store owners to train their sales staffs to accept it and establish the bookkeeping and other procedures required to do so. See, e.g., App. 410-11, 1296.

Second, establishing the new product was both labor and capital intensive. It was necessary to create elaborate systems to evaluate credit risks, approve transactions, process and clear the resulting transaction "paper" and bill and collect from cardholders. In addition, banks had to solicit and educate each prospective merchant about the benefits of the new product. App. 602-06.

The new card was expensive and risky in another sense as well. Permitting consumers to "charge" their purchases required a short-term extension of credit to every cardholder. Since customers were only billed once a month, there was, on average, a two-week extension of credit between the transaction and billing dates. In addition, consumers had a "free" billing cycle within which to pay off their balance in full without incurring any finance charge. The many cardholders who routinely did so effectively

obtained a "free" revolving short-term loan without any offsetting revenue stream to the issuing bank. App. 604-06; see also NaBanco, 779 F.2d at 595.

Moreover, to get merchants to accept the new card at all, the sponsoring bank had to guarantee payment for the transaction, regardless of whether the customer ever repaid his or her bank. Inevitably, some customers did not pay. Equally predictably, some cards were stolen. App. 604-06.

Finally, there were substantial legal limitations that affected the new industry. Banking in the 1950s and 1960s was strictly regulated, at both the federal and state levels. A patchwork system of restrictions on interest rates and other charges plus a ban on interstate banking made it essentially infeasible for any bank to create a viable multistate card system. App. 599; see also EFT ¶ 23.02[1].

For all of these reasons, the early history of the general purpose charge card business was notable mainly for failures and economic risks taken and lost. App. 601-02, 1240-53.

B. VISA

VISA began as a relatively small card program by the Bank of America in Fresno, California. While the program was relatively successful, its true promise lay in the creation of a national charge card system, which necessitated participation of multiple banking entities in other states and the creation of a nationwide automated clearing and authorization system.[7] App. 599-606. Thus, Bank of America began to license its "BankAmericard" system to a limited number of banks. After a period of chaotic operation, the licensees advised Bank of America that they would continue to participate only as co-owners in a reconfigured system featuring a new "neutral" trademark. Bank of America reluctantly consented. Thus was born the joint venture known today as "VISA". App. 600-01, 611-15, 1404.

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[7] For a further description of this early history see NaBanco, 596 F. Supp. at 1238-39; App. 1388.

The original VISA joint venture (then known as National BankAmericard Inc, or "NBI") consisted of approximately 240 banks in separate markets across the country. App. 1390. Each of the owner-members was expected to issue cards bearing the venture's common trademark[8] and to sign merchants to accept cards bearing that mark (but issued by any member) as payment for goods and services. Common rules were established for such essential joint functions as the authorization and interchange of transactions and the processing and daily settlement of accounts among members. App. 420-21. However, each member determined, for itself, the terms on which it would issue cards and enroll merchants to accept them. App. 433-35. As time passed, new systems were created to shorten the processing and settlement time, improve the authorization function and reduce the risk of loss from fraud and bad debts. In fact, in the 1960s and early 1970s, VISA pioneered the creation and improvement of state-of-the-art systems for transaction approval, data processing and settlement. These systems have materially improved the speed and convenience of charge card transactions while reducing their cost. App. 420-21, 601-06, 1408. The frustration of the old paper "warning" bulletin and the seemingly interminable delay in getting telephonic "approval" of transactions has given way to today's electronic environment in which point-of-sale terminals routinely obtain credit approvals and create an electronic processing record in a few seconds. App. 429-31, 602, 615-17.

The basic structure of the organization remains unchanged. The joint venture operates pursuant to a system of rules that govern and facilitate the functions of, and access to, an inherently interdependent financial exchange network. App. 423-34. Many of these rules have changed over time. However, one critical tenet of the system has

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[8] In 1976, "VISA" replaced the former BankAmericard trademark. App. 1392. However, the venture continued to employ the original BankAmericard blue, white and gold "bands" design, which still remains a prominent identifying feature of the VISA system. App. 611-14, 1404.

remained constant: each VISA member determines for itself the terms on which it issues cards and signs merchants to accept them. App. 433-35; Opn. 962.

VISA, itself, does not issue cards or sign merchants, nor does it limit the terms, the geographic areas, or the output of its members in issuing cards or signing merchants. Id. As a result, in literally every area of the country numerous banks compete to solicit new cardholders and merchants on a wide variety of terms. Overall, VISA today has approximately 6,000 issuer-members with the top 10 issuers accounting for approximately 50% of its total volume. Opn. 962, 966 n.8. However, even the smallest bank can offer its customers the full range of VISA services. App. 877-83, 915-29. Moreover, because of the joint venture character of the system, several relatively smaller "regional" banks regularly appear among the very largest VISA issuers. App. 435, 878-82, 1462.

The vigor of intrasystem competition is reflected in the testimony of Robert McKinley, an acknowledged expert on bankcard programs. Mr. McKinley reviewed the great number of card programs that are available to consumers in every market as well as the variety of terms on which they are offered. App. 863-70, 871-83, 1458, 1461.[9] He noted that over 100 VISA members issue cards nationally. App. 1569, 1461, 863-68. In addition, numerous regional and local issuers compete successfully against the national issuers in every area of the country, utilizing a full range of competitive techniques. App. 433-35, 877-84.

Some banks compete for cardholders through heavily advertised programs. Others solicit only their regular banking customers. Some banks charge relatively higher prices in return for greater service or add-ons, such as extended product warranties, or credit towards airline mileage, hotel accommodations, or the purchase of products,

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[9] One of Sears' witnesses testified to the large number of competitive card solicitations -- which he astonishingly characterized as "pollution" -- that he regularly received in the mail. App. 586-87. That testimony was reinforced by the introduction into evidence of numerous card solicitations received in one year by a Utah banker, who was "astounded" by the number of "direct mail solicitations from a lot of issuers." App. 904-13, 1379, 1465, 1472, 1482, 1490.

ranging from small household appliances to a new car. Some banks offer very low interest rates by strictly controlling credit standards, others are more generous in their credit evaluation and must charge higher rates as a consequence; still others offer so-called affinity programs that support charitable, cultural and educational institutions. App. 859-60, 864-79, 1458-59, 1461-64.

VISA membership originally was open only to traditional commercial banks. However, over the years, membership eligibility has been expanded to include savings and loans, thrifts, credit unions and, most recently, even the banking affiliates of industrial corporations such as Ford Motor Company, General Electric, and ITT. App. 1503. In fact, with the exception of its two major intersystem competitors (Sears and American Express), VISA membership is open to any financial institution that is eligible for federal deposit insurance. App. 1400-03.

While the volume of charge card business has expanded consistently, profitability has varied significantly over time. The massive early losses incurred by the system's founders were replaced by profits in the mid-1970s as consumers began to recognize the benefits of the new payment device. Then, when interest rates rose in the late 1970s and early 1980s, banks again lost money as their ability even to cover their direct lending costs was precluded by restrictive state interest rate limits. App. 620-21. In the mid-1980s the industry achieved its greatest profitability as the demand for consumer credit soared, creating a supply-demand disequilibrium, even with the entry of new card issuers and the expansion of many existing card programs. App. 621-23. Within the past few years that profitability has, once again, come under pressure as the economy has become mired in recession and the incidence of fraud and bad-debt losses has increased. App. 996-98.

C. INTERSYSTEM COMPETITION

Our discussion to this point has focused on the development and operation of the VISA system and the "intrasystem" competition among VISA members to issue VISA

cards and sign merchants to accept them. That is an important aspect of the credit card business, but it is only half of the story. Competition between different credit card brands or systems -- intersystem competition -- is equally important. While cards are issued and merchants are signed by individual members of the VISA system in competition with one another, and with the proprietary cards, such as Discover, there are fundamental ways in which competition is between the systems, as such.

Certain important functions are (and must be) carried out at the system level. Thus, VISA, itself, provides the mechanisms through which millions of VISA transactions are approved and settled between members every day. App. 423-32, 1408. It also defines the quality of service at the point of sale and operates a nationwide lost card and customer complaint service. App. 423-32, 1403A-B. As demonstrated at trial, many technological and product developments are attributable to competition between charge card systems. For example, VISA developed BASE I and II, its automated authorization and clearing and settlement networks in response to competition with MasterCard. App. 452-56, 601-04. Other VISA innovations driven by interbrand competition include VISANET and terminal deployment (App. 452-56, 616), and magnetic stripe technology. App. 615-17. Similarly, competition with other card brands has prompted VISA to develop numerous product enhancements (e.g., VISA Gold). App. 428-33.

At least equally important, VISA (and MasterCard) compete at the brand level against their system rivals (principally American Express and Discover), and vice versa. Some of this competition takes the obvious form of direct system-level promotion, such as VISA's well-known sponsorship of the Olympics or its popular "and they don't take American Express" advertising campaign. App. 432-33. Indeed, as for signing merchants, competition between brands is paramount. Even more fundamentally, the vast amounts of money invested by members to promote VISA to consumers and merchants supports the VISA system as well as individual card p ograms. Id. For their part, Discover and American Express do the same.

Unlike the vigorous intrasystem competition among the thousands of VISA (and MasterCard) member banks, intersystem competition in the general purpose charge card business has had a checkered history, at best. To begin, there have never been more than a handful of system competitors. Moreover, there is a nearly complete overlap in ownership of VISA and its early intersystem rival, MasterCharge (now MasterCard), as a result of the so-called Worthen litigation.[10]

Worthen involved a challenge to VISA's "exclusivity" rule, which prohibited VISA member banks from also being members of MasterCharge. VISA asserted that a repeal of that rule would reduce, if not eliminate, competition between the VISA and MasterCharge systems.[11] However, facing a significant treble damage exposure, and with its own financial stability far from established, VISA abandoned its prohibition of duality. Despite predictions that few banks actually would join both systems, there was a rush of such applications, and duality quickly became a way of life in the bankcard business. App. 438-46.[12]

With the emergence of duality, intersystem competition between MasterCharge and VISA diminished substantially. Almost all banks now maintain a single "back room"

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10 Worthen Bank & Trust Co. v. National BankAmericard Inc., 485 F.2d 119 (8th Cir. 1973), cert. denied, 415 U.S. 918 (1974).

11 At approximately the same time VISA sought approval of its exclusivity by-law from the Department of Justice. App. 439-40, 608-10; see also EFT ¶¶ 23.02[2]-[3]; Baxter, supra p. 4, at 587. After considering the matter for a substantial period, the Department advised VISA that it would support a policy requiring exclusivity among issuers (i.e., a rule that banks would not be permitted to issue both VISA and MasterCharge cards) but that it could not grant similar assurances with respect to exclusivity in the signing of merchants. App. 1347, 438-43, 607-10. The Department of Justice also filed a brief in the Eighth Circuit urging the Court of Appeals to reverse the district court's per se holding in the Worthen case. See 485 F.2d at 120 n.2. For a complete history of the Worthen litigation, see EFT ¶¶ 23.02[2]-[3].

12 The Justice Department's decision to allow the development of duality in the bankcard business has been broadly criticized. See, e.g., EFT ¶ 23.02[3]; Constantine, Presentation (Dec. 6, 1990), in Economists' Perspectives on Antitrust Today: Antitrust Issues in Regulated Industries (C. River Assocs. eds., 1991) (App. 1613); Balto, Antitrust and Credit Card Joint Ventures, 47 Consumer Fin. L.Q. Rep. 266, 266-67 (1993) (App. 1606).

operation for their two bankcard programs. There is virtually no competitive advertising or other promotional competition by one system against the other. While the managements of the systems still strive to maintain superiority in new product creation and systems development, their ability to do so is significantly limited by the fact that the owners have a stake in both systems and maintain unified "back room" operations that encourage system compatibility. App. 443-49, 610-11, 633-34.

With the gradual demise of competition between the two national bankcard systems as a result of duality, intersystem competition, itself, became largely non-existent. The only other significant system competitor in the 1970s and early 1980s was American Express, and its competition was largely confined to the so-called T&E market. App. 622-24. Then, in early 1986, Sears, Roebuck & Company entered the market with its Discover card.[13]

In the early 1980s, Sears had conducted an elaborate analysis of the economics of the general purpose charge card industry. App. 313-14. A high-level task force was appointed within the Dean Witter group of companies to consider two alternatives: become a major issuer of VISA or MasterCard or, alternatively, enter the business with a new, wholly-owned proprietary card.[14] App. 366-74. In the course of their work,

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[13] Sears had expanded its financial services operations several years before with its acquisitions of Dean Witter, Coldwell Banker, and several other financial service entities. App. 357-58. In fact, Sears maintained a membership in VISA for several years through Sears Savings Bank, which operated a very small program for its account holders. App. 313-14, 353-54.

[14] At trial, Dean Witter's Chief Executive Officer, Philip Purcell, testified that Dean Witter's strategy was to enter both the proprietary card business and one or both of the joint ventures. App. 313-17, 318-20. Thus, he claimed, the report and recommendation of the card task force actually was concerned only with the "sequence" of entry. Id. That testimony is entirely inconsistent with the testimony of other witnesses and is not supported by the task force report or any other documentary evidence produced by Sears during discovery. App. 361-65, 368-75, 1296-97, 1308, 1211-12, 1549, 1330, 1229-32.

But whatever the "facts," there is no suggestion that VISA was ever informed of Sears' supposed "two stage" plan, let alone that it agreed to facilitate it. App. 375-78. Thus, this case does not present a situation analogous to that in Aspen Skiing Co. v. Aspen Highlands Skiing Corp., 472 U.S. 585 (1985), in which the plaintiff's operations (continued...)

representatives of the task force met with VISA's President, Charles Russell, who encouraged Sears to become a major VISA issuer. App. 320, 1338. Instead, after examining the issue for several months, the task force recommended that Sears enter the business by creating an entirely new, proprietary credit card.

As recounted in the task force's report, membership in VISA or MasterCard offered certain advantages and was less economically risky. App. 536-50, 1325-26. However, those advantages were outweighed by the significant disadvantages of being just one more VISA (or MasterCard) member, with no real control over product configuration and identity or over business and marketing strategies. App. 536-50, 1327-28. Thus, the task force recommended that Sears follow what it termed the "high risk, high reward" strategy of going into active competition with the two bankcard joint ventures through its own, wholly-owned product. App. 542-50, 1327. That strategy was accepted by Sears' management and Discover was launched in early 1986 with a massive promotional campaign. App. 322-24.

The challenge for Sears' new Discover card program was much the same as the one faced by the founders of the bankcard joint ventures twenty-five years earlier: It needed to solve the problem of attracting both merchants and cardholders where the attractiveness to each group depended upon the existence of the other. App. 324, 410, 495-97. Sears recognized that meeting that challenge would be an expensive and time-consuming undertaking and that success would take time, effort and a great deal of money. App. 1296.[15]

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[14](...continued)
were predicated upon a long history of joint marketing activities that the defendant then attempted to disrupt. Id. at 603-04; See Olympia, 797 F.2d at 377-39; Corsearch, Inc. v. Thomson & Thomson, 792 F. Supp. 305, 329 (S.D.N.Y. 1992); Florida Fuels, Inc. v. Belcher Oil Co., 717 F. Supp. 1528, 1536 (S.D. Fla. 1989).

[15] Unlike its predecessors, however, Sears did not face the problems of creating an entirely new product or of inventing the systems necessary to support it. Thanks to the extensive efforts of VISA and MasterCard (and their respective members), general
(continued...)

Sears entered the market with considerable fanfare, offering a no-fee card and a rebate of "up to" 1%." App. 322-24.[16] Sears' new brand came complete with its own authorization and clearing systems that were comparable to those of VISA and American Express. To establish a merchant base, Sears offered discount rates significantly below those being promoted by VISA member banks. App. 410-15, 531. Predictably, VISA reacted aggressively to Sears' new competitive threat. Launching a so-called "anti-Discover" campaign, VISA encouraged its members to compete vigorously against Discover and declined to share any of its proprietary technology with the newcomer. App. 449-53. VISA not only promoted its own product with increased vigor, but advertised comparatively against both Discover and American Express. App. 625-28. In short, it competed.

Discover was equal to the task. It quickly surpassed the company's own internal forecasts on virtually every measure. App. 325-26, 379-80, 386-87, 1586. Within five years of its introduction, Discover had become the second largest issuer of general

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[15](...continued)
purpose charge cards were a well-known and broadly-accepted product in the American economy by 1986. App. 1324-25. Indeed, as noted previously, the industry was then entering a time of substantial growth and profitability. Id.

[16] Because of these features, Sears has attempted to portray Discover as a low-priced card. However, as industry-expert Robert McKinley testified -- and as the court, itself, observed in its post-trial Opinion (at 983) -- Discover is scarcely low cost when compared to many other available card programs. It has always charged 19.8% interest (in fact, at the time of trial it was the only one of the top 10 issuers that had not introduced a lower rate to at least some of its customers, App. 884A-90). Its heavily promoted "1%" rebate works out to far less than that for the average Discover customer; and that rebate is more than offset for many consumers by Sears' use of a rare, and expensive, formula (two month average daily balance method) for calculating finance charges. App. 592-97, 890-900,1406, 1460. As for "no-fee," such cards were a staple of the VISA and MasterCard businesses for many years. EFT ¶ 1.02[3], at 1-6. When the products were first launched, consumers were unfamiliar with them and the "chicken-and-egg" problem needed to be solved. In fact, great numbers of cards were mailed out "pre-approved" to consumers, resulting -- predictably -- in huge bad-debt losses. Id. at 1-6 to 1-7. As the cards became more widely accepted, many banks began to charge a small annual fee. Sears planned to follow precisely the same route, though in a much shorter time. Its internal documents show that an annual fee was planned after only two years. App. 567-72. However, introduction of that fee was delayed by competition from VISA and MasterCard issuers, and it may now be commercially infeasible because of other major no-fee cards on the market. Id.

purpose charge cards in the United States, with over 20 million card accounts. App. 533-35, 885-86, 888-90. It had also signed over 1.5 million merchants to accept its card, including virtually every major merchant in the country. App. 379-82, 533-35, 791. With system volume of over $14 billion and net profits of $170 million, Discover was a major contributor to Sears' overall profitability. App. 311, 325-28, 1585-86. In fact, according to documents produced on the eve of trial, the value of Discover as a stand-alone business has been assessed at approximately two billion dollars by Sears' investment bankers. App. 403-04.

D. SEARS' EFFORTS TO JOIN VISA

Shortly after Sears entered the market with Discover, it voluntarily terminated its VISA membership. App. 337, 355-56. Then, in late 1988, Sears again applied for VISA membership through Greenwood Trust, the "issuer" of the Discover card. App. 334. Sears' application was not prompted by any plan to issue VISA cards. App. 334-35, 389, 562. Rather, as revealed by pre-trial discovery, Sears' motive was, in part, to facilitate certain technical operations and, more important, to attempt to inhibit the vigorous intersystem competition by VISA against Sears. According to a memorandum written at the time by a top Discover official, a major purpose for joining VISA was to allow Discover access to confidential VISA information. App. 1346. Equally candidly, Dean Witter's CEO, Philip Purcell, admitted at trial that his reason for promoting Sears' application was the expectation that if Sears became a member of VISA, that would reduce the vigor of VISA's competition against Discover. App. 387-88.

VISA considered Sears' application at a meeting in June 1989. After reviewing a negative recommendation from management, VISA's Directors voted unanimously to reject Sears' application. App. 629-34. In addition, the Board unanimously adopted an amendment to By-law 2.06, which provided as follows:

> [I]f permitted by applicable law, the corporation shall not accept for membership any applicant which is issuing, directly or indirectly, Discover cards

> or American Express cards, or any other cards deemed competitive by the Board of Directors . . . .

App. 1583.

VISA promptly advised Sears of its decision and the adoption of the new by-law. Id. Displeased, Sears' threatened to sue VISA. App. 339-44, 391-403; 1340. However, no action was taken. Instead, the issue appeared to have been dropped. Then, in early January 1991, VISA inadvertently learned that Sears had purchased the assets (including a VISA membership) of a failed Utah thrift from the Resolution Trust Corporation, and was planning to launch a new brand of VISA card (to be known as Prime Option) within the next few weeks.[17] Opn. 964.

Having stumbled upon Sears' undisclosed intentions, VISA declined to approve the printing of Prime Option cards bearing VISA's proprietary trademarks. Id. Sears then sued, claiming that VISA's refusal to permit Sears to become a VISA issuer violated Section 1 of the Sherman Act, 15 U.S.C. § 1. Concurrently, Sears sought and obtained a preliminary injunction requiring VISA to approve Sears' proposed rollout of its new Prime Option program. See 763 F. Supp. 1094 (D. Utah 1991) (Sam, J.). VISA promptly sought and obtained a stay of that order from this Court. See 936 F.2d 1096, 1098 (10th Cir. 1991). In June 1991, this Court reversed and vacated the preliminary injunction order and remanded the case for further proceedings. Id. at 1102.

E. TRIAL COURT PROCEEDINGS

1. The Antitrust Claims

Sears' complaint asserts that VISA By-law 2.06 unreasonably restrains intrasystem competition in the general purpose charge card market by excluding Sears from access to VISA membership, thereby precluding it from using VISA's property

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[17] In VISA's view, Sears' conduct in the acquisition of a purported VISA membership and the proposed launch of Prime Option was fraudulent. VISA has counterclaimed against Sears on that ground. App. 72-74. Trial of that counterclaim was bifurcated and stayed by the court in its pretrial order setting the antitrust liability issues for trial. See 801 F. Supp. 517, 528-29 (D. Utah 1992); see also Opn. 964 n.6.

including, specifically, the VISA name, associated trademarks and other proprietary systems. As a result, Sears is prevented from offering its Prime Option general purpose charge card as a brand of VISA card as opposed to a new proprietary card or an additional brand of Discover card. App. 17, 20-21.

For its part, VISA not only denies any obligation to permit Sears to have access to its property, but further alleges, by way of counterclaim, that allowing Sears to acquire an ownership interest in VISA while owning and issuing the competing Discover card would restrict competition at the highly concentrated intersystem level, thereby violating Section 7 of the Clayton Act, 15 U.S.C. § 18. App. 71-72.

2. The Trial

Pursuant to an agreed-upon pretrial order, the court bifurcated the antitrust liability issues from all other issues in the case, including VISA's non-antitrust counterclaims and Sears' damage claim.[18] The order further contemplated that in light of the importance of the antitrust questions presented, the decision on the liability issues would be subject to immediate appeal -- as a matter of right if VISA prevailed or on a discretionary basis if Sears prevailed. Sears' claims were tried to a jury, while the court served as trier of fact on VISA's equitable counterclaim under Clayton Act Section 7.

The trial lasted 3½ weeks. Sears' principal claims at trial were that VISA's refusal to permit Sears to become a member precluded it from pursuing a preferred "branding" strategy of offering both a Discover card and a VISA card to consumers. App. 306-07, 309. Sears further asserted that its new credit card would be attractive to consumers because of its supposedly low interest rate and other features. Id. Sears did not claim, however, that it was unable to compete successfully in the general purpose charge card market without access to the VISA name and systems or that it was

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[18] For a further, unrelated aspect of the trial court proceedings, see 784 F. Supp. 822 (D. Utah 1992).

prevented from offering Prime Option as a new proprietary card or as an additional brand of Discover card.[19]

VISA asserted, by contrast, that Sears could demonstrate no harm to competition in the general purpose charge card market. With 6,000 competing issuers (and with the top 10 VISA issuers accounting for less than 50% of VISA volume and an even smaller share of the total market) plus no restrictions on price, output or geographic competition, VISA members had no power to restrain or limit price or output in the market. In fact, VISA's by-law does not exclude anyone from the market. Its only effect was to exclude two firms (Sears and American Express) from one brand in the market. And the two affected firms had demonstrated that they did not need access to VISA's property or systems in order to compete by actually doing so successfully on their own.

VISA also offered uncontested evidence that demonstrated a likelihood of harm to intersystem competition if Sears were permitted to issue both Discover and a brand of VISA card. Unlike the highly diffuse market at the issuer level, system-level competition is limited to VISA, MasterCard, Discover, American Express and, arguably, Diners Club. Permitting Sears to become a VISA issuer would increase the opportunities for collusion as well as the possibility for strategic coordination. It would also dramatically affect Sears' competitive incentives in such areas as the setting of merchant discount rates and the creation of new, competitive systems and other technologies.

The jury returned a verdict for Sears.

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19 In fact, Sears had done precisely that with an upscale brand of Discover that it calls "Private Issue." App. 563-64. This card carries the Discover logo (in the same way that all VISA cards bear the VISA name). App. 1356, 1369, 1374. Thus, Private Issue was instantly acceptable at all Discover merchants. App. 503-07, 563-64; 1218-20.

3. Post-Trial Proceedings

Following the jury's verdict, VISA moved for judgment as a matter of law under Rule 50 or, in the alternative, for a new trial under Rule 59. Contemporaneously, the parties briefed VISA's Section 7 counterclaim that had been tried to the court. On April 1, 1993, the court rendered a 107-page opinion that denied VISA's motions and entered judgment against VISA on its counterclaim.[20]

The court's opinion stated that, in its view, VISA's arguments were better taken both as a matter of antitrust policy and on the evidence presented. Opn. 983-84. The court noted that VISA's concern with the need to protect incentives for innovation by joint ventures not only raised "legitimate policy considerations" but was "logical and well reasoned." Opn. 978; see also id. at 981-82. Specifically,

> [t]he court found VISA's policy and economic arguments to be more compelling . . . . [T]he court found persuasive VISA's position regarding the need to protect joint venture innovation, the importance of protecting private property and the economic and competitive consequences of keeping the owner of the Discover Card out of the VISA system.

Opn. 984.

Similarly,

> the court acknowledge[d] that its view of the evidence differs from the jury's findings. . . . In fact, the court would have concluded that the harm to competition from letting Sears into the VISA system is greater than any harm from keeping Sears out. [T]he court believes that Bylaw 2.06 fosters intersystem competition in the relevant market [and that] [s]uch competition is important . . . with only five active intersystem competitors . . . . Simply adding another high-priced card issuer, as Sears has always been . . . may provide short-term intrasystem competitive benefits within the VISA system, but in the long run . . . the damages from such inclusion will outstrip the benefits.

Id. at 983-84.

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[20] Separately, Sears moved yet again for an injunction permitting it to offer its new Prime Option VISA card immediately following the jury's verdict. The court denied the motion on the ground that there was no apparent harm to Sears or to the public interest from refusing the request. 1993-1 Trade Cas. (CCH) ¶ 70,099, at 69,410 (D. Utah Dec. 28, 1992). A similar finding was made by this Court when it vacated the earlier preliminary injunction in Sears' favor. 936 F.2d at 1100-02.

Despite these views, the court held that VISA's policy arguments were beyond its power to implement and that the jury's verdict was not so unreasonable that it should be set aside as a matter of law. Opn. 983.[21]

4. VISA's Motion Under 28 U.S.C. § 1292(b)

As contemplated by the parties' stipulated pre-trial order, VISA promptly moved for certification under 28 U.S.C. § 1292(b). The motion was granted by the district court on April 26, 1993 and by this Court on May 28, 1993.

V. STANDARD OF REVIEW

This appeal principally involves errors of law which are reviewed de novo. Fox v. Mazda Corp., 868 F.2d 1190, 1194 (10th Cir. 1989). That is true of the court's failure to apply a correct legal standard under Section 1 of the Sherman Act (pp. 22-42) as well as its analysis of market power (pp. 42-49), and Sears' "disincentive" theory (pp. 57-60). A de novo standard also applies to the court's failure to correctly instruct the jury that they could not consider Sears' so-called "discrimination" and "anti-Discover campaign" evidence as proof of an adverse effect upon competition (pp. 56-57 (note 72)). Finally, a de novo standard applies to the court's legal errors in analyzing and applying market structure data under Section 7 of the Clayton Act (pp. 68-71) and its use of a "balancing" test in evaluating the harm of Sears' proposed acquisition of an interest in VISA (p. 73).

VISA's challenge to the adequacy of Sears' proof of harm to competition (pp. 49-56, 61-66) presents both legal and factual issues. As the Supreme Court held in Matsushita Electric Industrial Co. v. Zenith Radio Corp., 475 U.S. 574, 594 n.19 (1986), and reiterated recently in Brook Group Ltd. v. Brown & Williamson Tobacco Corp., 113 S. Ct. 2578, 2598 (1993), a jury verdict that is "economically senseless"[22] cannot be

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[21] The court, as finder of fact on VISA's Section 7 claim, similarly favored VISA but held that the asserted harm to competition resulting from Sears' proposed partial acquisition was not great enough to justify an injunction. See pp. 67-68, infra.

[22] Eastman Kodak Co. v. Image Technical Servs., Inc., 112 S. Ct. 2072 (1992).

sustained, even if it is supported by the testimony of a credentialed expert. A jury is deemed to understand not only the facts and the law but "the realities of the market" (Brook Group, 113 S. Ct. at 2598) and a jury verdict that lacks an adequate evidentiary basis regarding such matters as market structure or the existence of supracompetitive profits (pp. 52-54) fails as a matter of law. Id. at 2595, 2598; AA Poultry Farms, Inc. v. Rose Acre Farms, Inc., 881 F.2d 1396, 1403-04 (7th Cir. 1989), cert. denied, 494 U.S. 1019 (1990).[23]

Virtually all of Sears' "evidence" falls into that category. See, e.g., pp. 49-50 (market structure), 56 (consumers' "right to choose"). The only exceptions are VISA's contention that there was insufficient evidence for the jury to find that harm to intrasystem competition outweighs the benefits to intersystem competition (pp. 61-62, 63-66), which is reviewed for clear error, White v. Conoco, Inc., 710 F.2d 1442, 1443 (10th Cir. 1983), and the court's analysis (as trier of fact on VISA's counterclaim) of the likely competitive effects of Sears' proposed partial acquisition of an interest in VISA (pp. 71-73), which is reviewed under an analogous standard. Fed. R. Civ. P. 52(a); Litwin v. United States, 983 F.2d 997, 999 (10th Cir. 1993).

VI. ARGUMENT

A. THE DISTRICT COURT ERRONEOUSLY SUSTAINED THE JURY VERDICT ON SEARS' CLAIM UNDER SECTION 1 OF THE SHERMAN ACT

1. Introduction

At the hearing on Sears' post-trial request for an injunction the court commented on the extraordinary nature of Sears' claim:

> To this moment I don't see how a company the size of Sears Roebuck has to resort to our antitrust laws to obtain the property of a joint venture, or a single company or anyone else, when they have shown their ability, impressively so, to be successful and viable and very profitable in this very arena.

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[23] Permitting the jury to infer anticompetitive effects from the type of intent evidence Sears offered (pp. 50-52, 63) was also a legal error. AA Poultry, 881 F.2d at 1401-02.

App. 1592. Nonetheless, the court felt constrained not to intervene on account of its interpretation of applicable law and its assertedly limited prerogatives in the face of a contrary jury verdict. Opn. 983-84, 1002.

But VISA respectfully submits that the tension between the court's analysis and the jury verdict is not adequately explained by the observation that "reasonable minds may differ." Rather, we submit that the court below erred in two respects: First, the jury should have been instructed that VISA's refusal to admit Sears to membership is permissible as a matter of law, absent proof of "essentiality," that is, proof that it could not compete successfully without access to VISA's property -- a showing that Sears conceded it could not make.[24] Second, on the record presented at trial, there was no basis for the jury to conclude that VISA's exclusion of Sears unreasonably restrains competition in the general purpose charge card market. To the contrary, the exclusion necessarily promotes competition by encouraging the maintenance of intersystem rivalry. Thus, no reasonable trier of fact -- deemed to "know and understand" not only the law and the facts, but the "realities of the market" (Brook Group, 113 S. Ct. at 2598) -- could decide in favor of Sears. That being so, the jury's verdict should have been set aside as a matter of law. Cf. id. at 2592.

2. The Court Applied an Incorrect Legal Standard.

The court erred[25] initially by failing to require Sears to demonstrate an inability to compete successfully on its own. VISA raised that issue in seeking summary judgment and, when that motion was denied, in its proposed jury instructions (App. 153, 1161), in its motion for judgment under Rule 50 when Sears rested (App. 1116-55), and in its post-trial renewal of its Rule 50 request. Opn. at 967 & n.9. As VISA explained

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[24] See Opn. 980: "Sears clearly cannot make . . . a showing [of essentiality]. . . . It does not need membership in VISA in order to compete in the general purpose charge card market."

[25] Standard of review: de novo (see p. 20, supra).

in those various pleadings, the antitrust laws favor the creation of value through innovation and other forms of entrepreneurial risk-taking. Thus, businesses are permitted to retain the fruits of their efforts and are not, as a matter of law, required to share their property with rivals except in very narrow circumstances involving, at a minimum, proof that the excluded parties cannot compete successfully in the market without such compelled sharing. The reason for this principle is both fundamental and evident: if a party knows that its creations are subject to forced sharing if it succeeds, it will have no incentive to devote the time and money or to take the economic risks required to innovate in the first place. Areeda, Essential Facilities: An Epithet in Need of Limiting Principles, 58 Antitrust L.J. 841, 851 (1990) (hereafter "Areeda") (App. 1593). Conversely, if a party can engage in "rivalry by waiting,"[26] that is, sit on the sidelines and thereafter demand to share in the benefits of those efforts that succeed, innovation, similarly, will be deterred.

The court acknowledged that the foregoing is a correct statement of the law as applied to single firms. Opn. 975. It also expressed sympathy for VISA's arguments as a matter of antitrust policy. Opn. 974, 982, 984. However, it held that even if the rationale against forced sharing is identical for single firms and joint ventures[27] the language of the Sherman Act precludes such an argument. Opn. 979 & n.26. As a joint venture, the court held, VISA's by-laws are subject to challenge under the rule of reason and the court's role is limited to presenting the jury with evidence bearing on the competitive effect of the rule. Opn. 979. To do more, held the court, would infringe upon the legislative prerogative to establish competition policy and the jury's role as fact-finder in implementing it. Opn. 981-83. The result of this approach was a verdict that the court, itself, seriously questions.

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[26] Plant, The Economic Theory of Patents for Invention, 1 Economica 30 (1934).

[27] Which it is. See p. 30, infra; App. 832-33, 947-50; see also App. 1496.

But it is not merely the outcome that is flawed; it is the court's approach as well. Contrary to its view, proof of essentiality is as appropriate in this case as in any other "compulsory sharing" case. Since Sears disavowed such a showing, there was, in fact, nothing to go to the jury and judgment should have been entered for VISA as a matter of law.

a. The Court's Role Under the Rule of Reason

The Supreme Court has pointed out on several occasions that if the Sherman Act were read literally, every agreement would be void. See, e.g., National Soc'y of Prof'l Engineers v. United States, 435 U.S. 679, 687 (1978) ("One problem presented by the language of § 1 of the Sherman Act is that it cannot mean what is says. The statute says that 'every' contract that restrains trade is unlawful. But . . . restraint is the very essence of every contract; read literally, § 1 would outlaw the entire body of private contract law."); United States v. Topco Assocs., 405 U.S. 596, 606 (1972). In fact, taken literally, there would not even be a "rule of reason" in the Sherman Act. That standard, instead, was judicially recognized in the Standard Oil case[28] in 1911.

But the Sherman Act not only permits, it demands, judicial interpretation to give meaning to the statute's overly-general terms. The Supreme Court repeatedly has held that, unlike many other statutes, Section 1 of the Sherman Act is an embodiment of common-law principles; therefore, it is not merely the right, but the duty, of courts to give the Act "definition." National Soc'y of Prof'l Engineers, 435 U.S. at 688. "The legislative history [of the Sherman Act] makes it perfectly clear that [Congress] expected the courts to give shape to the statute's broad mandate by drawing on common-law tradition." Id.; see also United States v. United States Gypsum Co., 438 U.S. 422, 438-39 (1978); cf. Appalachian Coals, Inc. v. United States, 288 U.S. 344, 359-60 (1933). In

[28] Standard Oil Co. v. United States, 221 U.S. 1, 60 (1911).

short, the court was wrong to believe itself constrained by the literal language of Section 1.

The court's approach to the rule of reason was similarly flawed. In its view, Sherman Act cases fall into two broad categories: per se and rule of reason. With Sears having abandoned the per se arguments that it advanced early on, the court viewed its function as limited to presiding over a trial in which evidence respecting any aspect (or circumstance relating to) VISA's by-law would be placed before the jury, which then would adjudicate the case under extremely broad standards derived from Justice Brandeis' early formulation of the rule of reason in Chicago Board of Trade.[29]

In one sense, of course, any antitrust claim that does not involve a per se violation by definition comes under the rule of reason. However, that broad division does not adequately enumerate, let alone exhaust, the analytic possibilities in particular cases. Thus, in recent years, as judicial and economic learning has shown that many practices formerly condemned as unlawful per se may, in fact, produce competitive benefits, courts have refined rule-of-reason analysis through various presumptions or filters designed to promote more efficient and predictable decision-making in rule-of-reason cases. As the Supreme Court noted in NCAA v. Board of Regents of Univ. of Okla., 468 U.S. 85, 109 n.39 (1984): "The rule of reason can sometimes be applied in the twinkling of an eye."

But that observation is apt in both directions. At the "facially pernicious" end of the spectrum, courts perform an important judicial function by allocating the burden of proving justification and by "filtering" those justifications which may not be competitively validated. See, e.g., NCAA, 468 U.S. at 113. At the opposite end of the rule-of-reason spectrum, courts similarly have adopted "filters" or "screens" to dispose of claims in which industry structure or other circumstances demonstrate the absence of

[29] Board of Trade of City of Chicago v. United States, 246 U.S. 231, 238 (1918).

unreasonable harm to competition as a matter of law. See Valley Liquors, Inc. v. Renfield Importers, Inc., 822 F.2d 656 (7th Cir. 1987), cert. denied, 484 U.S. 977 (1987); Assam Drug Co. v. Miller Brewing Co., 798 F.2d 311 (8th Cir. 1986).

This case presents the latter situation. While VISA's by-laws may be subject to rule-of-reason scrutiny, application of that standard to a joint venture's refusal to share its creations with two highly successful competitors presents the same considerations as an analogous refusal by a single entity -- to which the practice is directly akin.[30] Sears' claim rests on the supposed substantial harm to competition effected by that "restraint." But, we submit, that is not a "jury issue" without more. Here, as at the opposite end of the spectrum, it is not only appropriate but necessary for the Court to make a preliminary legal evaluation to determine whether the challenged practice presents a "plausible" threat to competition given society's need to nurture investment and innovation. Matsushita, 475 U.S. at 587-88; see also Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 775 (1984). Put otherwise, VISA submits that in a case involving a simple "refusal-to-share" claim, both economic learning and the law justify a legal rule, or "screen," limiting the circumstances in which a duty to deal will be imposed on a joint venture by the antitrust laws. That "screen" is a requirement that the plaintiff adduce evidence sufficient to show that it has been disabled from competing successfully in the relevant market. Absent such a showing, there is no case to go to the jury.[31]

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[30] The analysis we propose does not apply to every form of competitive aggregation that might, under some definition, be described as a joint venture. It applies, instead, only to those forms of efficiency-creating aggregations (a BMI, NCAA or VISA), in which the whole is "truly greater than the sum of its parts" through the creation of new products through risk and innovation. Broadcast Music, Inc. v. CBS, 441 U.S. 1, 21-22 (1979) ("BMI"). Thus, for example, the analysis does not apply to trade associations or other organizations whose practices have no plausible efficiency justification, such as those condemned in Fashion Originators' Guild or Eastern States Lumber.

[31] See, e.g., Marrese v. American Acad. of Orthopaedic Surgeons, 1991-1 Trade Cas. (CCH) ¶ 69,398, at 65,606 (N.D. Ill. 1991) (plaintiff claimed that denial of membership in an important professional society adversely affected competition by depriving consumers of the benefit of his unique willingness to "undertake high-risk surgery." Summary judgment for defendant was granted, however, because plaintiff could still (continued...)

b. **This Is a "Structure" Not a "Conduct" Case.**

The court's analysis was misdirected from the outset by its failure to observe a critical conceptual distinction: this is a "structure" not a "conduct" case. VISA's members are not alleged to have fixed prices, divided territories or agreed to limit their respective outputs. The only "conduct" alleged is that the association, acting through its Board of Directors, declined to share the venture's creations with Sears by letting it become a VISA member. That is "conduct" for antitrust purposes only in the sense that an agreement by the members of a price-fixing cartel to charge the same prices is "speech."

The distinction is important because the antitrust laws treat "conduct" and "structure" very differently. Agreements among competitors that alter or limit the way in which they compete with one another raise questions under the antitrust laws because they contradict the fundamental assumption of our economic system favoring competition between independent economic entities.

Structure is different. The antitrust laws encourage the creation and exploitation of property rights. Far from requiring competitors to share the fruits of

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[31](...continued)
pursue his profession and, in fact, had done so successfully.), aff'd, 977 F.2d 585 (7th Cir. 1993); Schachar, 870 F.2d at 399 (7th Cir. 1989) ("Unless one group of suppliers diminishes another's ability to peddle its wares . . . there is not even the beginning of an antitrust case, no reason to investigate further to determine whether the restraint is 'reasonable.'"); cf. McKenzie v. Mercy Hosp., 854 F.2d 365, 370-71 (10th Cir. 1988) (essential facilities claim failed, as a matter of law on summary judgment, where evidence showed that hospital's denial of staff privileges did not prevent plaintiff from competing successfully on his own against defendant); Tarabishi v. McAlester Regional Hosp., 951 F.2d 1558, 1568 n.14 (10th Cir. 1991), cert. denied, 112 S. Ct. 2996 (1992).

We further commend to the Court's attention the Seventh Circuit's decision in a frequently-cited Section 2 case, Olympia Equipment Leasing Co. v. Western Union Telegraph Co., 797 F.2d 370 (7th Cir. 1986), in which the court discussed the circumstances under which the antitrust laws may impose a duty to aid competitors. In its opinion, the court drew what we believe is an important distinction between the "negative" duty under the antitrust laws not to restrain competition (as, for example, by agreements that restrict price competition or limit output) as opposed to an "affirmative" duty to aid a competitor's business success. See 797 F.2d at 376. The court's opinion further explained the adverse effect that imposing such a duty would have on incentives to engage in output-enhancing conduct. Id. at 375.

their success with rivals, the antitrust laws value and protect such success because it promotes economic risk-taking and innovation. Structural concerns are raised only when a firm or group of firms acquires and misuses a dominant position so that the ordinary processes of the market cease to work (Sherman Act § 2) or when previously independent firms threaten to bring about a similar result by combining their businesses (Clayton Act § 7). A duty to share one's property with a rival is even rarer. It arises, at best, only when a firm has acquired substantial market power and prospective rivals are unable to enter the market and compete successfully without access to some unique asset controlled by the dominant firm or firms. Olympia Equip. Leasing Co. v. Western Union Tel. Co., 797 F.2d 370, 376 (7th Cir. 1986), ("The monopolistic-refusal-to-deal cases qualify rather than refute the no-duty-to-help competitors cases.") cert. denied, 480 U.S. 934 (1987); see also Aspen, 472 U.S. at 603-04 & n.31.

Joint ventures present a special case under the antitrust laws. In one sense their very existence confounds traditional notions of competition between separate firms. Yet, at the same time, such ventures frequently are pro-competitive, permitting firms to achieve scale economies and leading to important new advances by facilitating the exploitation of competitive synergies or limiting economic risk. Joint ventures also involve less integration than outright mergers and, thus, preserve competition to a greater extent. 4 P. Areeda, Antitrust Law ¶ 947a, at 169 (hereafter "Treatise"). They are increasingly prevalent, particularly in high-technology industries where the combination of both intellectual and financial resources is critical to pursuing important new innovations. See Kattan, Antitrust Analysis of Technology Joint Ventures: Allocative Efficiency and the Rewards of Innovation, 61 Antitrust L.J. 937, 938-40 (1993) (App. 1709).

For such ventures to exist at all (let alone compete successfully) their members must be able to cooperate -- i.e., act like a single firm -- within the limits of the venture. The venturers also must be able to expect to realize and retain the fruits of their

collaboration in the same manner and to the same extent as other types of industrial organizations. While it is, therefore, appropriate to scrutinize agreements that limit competition between the venturers ("conduct"), the same is not true of rules that merely limit participation in the venture after its creation. Joint venture ownership rules involve structural questions. They raise an antitrust issue only if the joint venture threatens to become over-inclusive, i.e., too big, or if (like a single firm) the venture acquires control over some facility or property that makes it infeasible for those who are left out of the venture to compete effectively against it without having access to the joint venture's uniquely advantageous property.

These diverse considerations have led leading antitrust scholars, such as Phillip Areeda of Harvard and Frank Easterbrook (of the University of Chicago and the Seventh Circuit), to caution that a blanket characterization of joint ventures as either "single" firms or multi-firm combinations is a potentially misleading oversimplification -- a point that this case dramatically illustrates. See generally 7 Treatise ¶¶ 1476-78; Chicago Prof'l Sports Ltd. v. NBA, 961 F.2d 667, 672-73 (7th Cir.), cert. denied, 113 S. Ct. 409 (1992). VISA submits that the trial court's failure to heed that caution was critical to its flawed analysis. The court noted that since VISA is a joint venture it, literally, is subject to Section 1 of the Sherman Act. Having so held, it then assumed that every action or rule of the venture should be analyzed in the same manner under Section 1: that is, submitted to a jury under generalized (i.e., unstructured) rule-of-reason instructions.

The problem with that analysis is that it focuses attention on the wrong question. The issue is not whether Section 1 applies at all to joint ventures, but how the particular antitrust issue presented should be analyzed for Section 1 purposes. Excluding Sears from VISA does not limit market competition unless Sears needs VISA to compete in the relevant market. Since it admittedly does not, there was no case to go to the jury.

The point is underscored by the record. Confronted with the observation by VISA's expert, Professor Richard Schmalensee,[32] that there is no sound reason to distinguish between a single firm's refusal to share its property and the same refusal by a joint venture (App. 947-50), the court below dismissed the point as an anomaly resulting from the structure of the Sherman Act. Opn. 978-79. But the proper approach, we submit, was to recognize that VISA's refusal to share its property presents a different issue from an agreement to restrict territories or to eliminate price competition among members of the venture.[33]

The same conclusion is also impelled by the obvious mismatch between the purported problem and Sears' suggested solution to it. As discussed further infra, the central concern of the antitrust laws is the exercise of market power. Hay, Market Power in Antitrust, 60 Antitrust L.J. 807, 807 (1992) (App. 1688). Such power is achieved either by agreements that permit firms to increase their power by eliminating competition between them (conduct) or by having (monopoly) or acquiring (merger) too large a market share. The solution to those concerns, in each instance, is to limit the defendant's power, either by outlawing the conduct or limiting the market share of the offending party or parties. Sears, of course, claims that VISA has such power here by virtue of its members' collective share of the relevant market. See App. 683-85; see also

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32 Prof. Schmalensee is Professor of Economics at MIT, a former member of the President's Council of Economic Advisors and a consultant to the Department of Justice, Antitrust Division. App. 931-34.

33 In the wake of the jury verdict in this case, MasterCard sought a declaration that its refusal to admit Sears was lawful. Sears counterclaimed under Section 1 of the Sherman Act, challenging the refusal. MasterCard then moved to dismiss Sears' counterclaim under Rule 12(b)(6) on the ground, inter alia, that, as a matter of law, it is a single entity, immune from Section 1 of the Sherman Act. On August 26th, the District Court for the Southern District of New York denied MasterCard's pleading motion. MasterCard Int'l, Inc. v. Dean Witter, Discover & Co., 93 Civ. 1478 (S.D.N.Y. 1993).

That order has no force here since, as explained in text, VISA does not assert that Section 1 is inapplicable; rather, VISA argues (consistent with the analyses of Professors Areeda and Easterbrook noted in text) that characterization of a joint venture either as a single entity or plurality of actors is a complex issue properly assessed only in the context of a full factual record, and with particular focus on the kind of conduct at issue.

pp. 44-47, infra. However, its proposed "solution" to the problem is to increase that power by requiring VISA to admit Sears (and perforce American Express as well). But that is a "thirteenth chime" solution: not only absurd itself, but calling into question the twelve that preceded it.[34]

c. **Sears Should Have Been Required to Demonstrate That Membership in VISA Is Necessary for It to Compete in the Relevant Market.**

Proof of essentiality as a precondition to enforced sharing is scarcely novel, under either Section 1 or Section 2 of the Sherman Act. To the contrary, there is abundant law which holds that refusals to deal (what Judge Richard Posner has referred to as a refusal to affirmatively "help [one's] competitors")[35] are permissible, as a matter of law, absent monopolization or essentiality. See, e.g., pp. 32-37, infra; see also Kattan, supra p. 28, at 963 ("the requirement of open access [to joint ventures] is limited to cases that may fall within the 'essential facility' rubric"); Blumenthal, Three Vexing Issues under the Essential Facilities Doctrine: ATM Networks as an Illustration, 58 Antitrust L.J. 855, 860 (1990).

The principle that parties have the right to decide with whom they will deal goes back over 70 years, to the Supreme Court's famous Colgate decision.[36] This principle remains an important element of antitrust policy in both single firm and joint venture cases. See, e.g., Westman Comm'n Co. v. Hobart Int'l, Inc., 796 F.2d 1216, 1225 (10th Cir. 1986), cert. denied, 486 U.S. 1005 (1988). See generally 1 ABA Antitrust Section, Antitrust Law Developments 241-50 (3d ed. 1992). Indeed, the point recently

[34] See, e.g., Sun Ref. & Mktg. Co. v. Statheros Shipping Corp., 761 F. Supp. 293, 304 (S.D.N.Y.), aff'd, 948 F.2d 1277 (2d Cir. 1991).

[35] Olympia, 797 F.2d at 375.

[36] United States v. Colgate & Co., 250 U.S. 300, 307 (1919) (The Sherman Act does not "restrict the long-recognized right of a trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal."). That right, of course, is not absolute. Aspen, 472 U.S. at 601. However, the limits upon the right are not defined by the rule of reason as such, but by monopolization and essentiality principles. See Olympia, 797 F.2d at 376.

was recognized by this Court. See TV Communications Network, Inc. v. TNT, Inc., 964 F.2d 1022, 1027-28 (10th Cir. 1992) ("Section one only prohibits refusals to deal where a manufacturer has monopoly power in the market."), cert. denied, 113 S. Ct. 601 (1992). Consistent with this principle, numerous joint venture refusals to deal and other, similar restrictions have been upheld, as a matter of law, under Section 1 of the Sherman Act.[37] See, e.g., Schachar, 870 F.2d 397; Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 792 F.2d 210 (D.C. Cir. 1986), cert. denied, 479 U.S. 1033 (1987); Marrese v. American Acad. of Orthopaedic Surgeons, 706 F.2d 1488 (7th Cir. 1983), rev'd on other grounds, 470 U.S. 373 (1985); Phil Tolkan Datsun, 672 F.2d 1280; Mid-South Grizzlies v. NFL, 550 F. Supp. 558 (E.D. Pa. 1982), aff'd, 720 F.2d 772 (3d Cir. 1983), cert. denied, 467 U.S. 1215 (1984); cf. Olympia, 797 F.2d 370; see also Dep't of Justice, Antitrust Enforcement Guidelines for Int'l Operations § 3.42 (1988), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,109, at 20,601 ("Int'l Guidelines") (Antitrust Division is concerned with joint venture membership exclusion only if "an excluded firm cannot compete in a related market or markets . . . without having access to the joint venture").

Nor is the rationale for requiring proof of essentiality obscure. It stems in part from the need to protect incentives to innovate or, stated obversely, the need to guard against free riding on the investments, risk-taking and innovations of others.[38] For

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[37] The trial court's opinion at times mistakenly refers to VISA's position as a request for "immunity" or an "exemption" from antitrust scrutiny. Opn. 972. Similarly, Sears has characterized VISA's position as seeking a rule of "per se legality." Neither characterization is correct. As discussed in text, the issue is not whether the rule of reason applies, but how it applies: that is, whether Section 1 reaches a joint venture's refusal to admit a competitor without proof that the excluded party is unable to compete successfully on its own. VISA acknowledges that a duty to deal may be imposed on a joint venture where the plaintiff can make the necessary showing. VISA's refusal is only "per se" lawful in this case because Sears acknowledges its inability to offer the requisite proof.

[38] The economic concept of free-riding has become exceedingly important in antitrust law following the Supreme Court's decision in Continental T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977). In general terms, it refers to circumstances in which a party seeks to benefit from the efforts or expenditures of others. It is important because of its effect upon incentives. See, e.g., Rothery, 792 F.2d at 221, 229; Sun Dun, Inc. v. Coca-
(continued...)

example, Donald Baker, a former head of the Antitrust Division of the Department of Justice, has noted:

> Individual firms or limited joint ventures generally engage in innovation because they expect to improve their position vis-a-vis their competitors. If they are told in advance, as a matter of law, that they are going to have to grant compulsory access to their competitors whenever they achieve a really significant success, then the law has blunted their incentive to invest and innovate.

EFT ¶ 21.05(2), at 21-36. His views are echoed with specific reference to joint ventures by Prof. Robert Pitofsky (formerly an FTC Commissioner):

> Why should joint venturers, particularly those who took significant risks in order to establish the project, offer the advantages of membership to rivals? Incentives for risk-taking and innovative efforts will certainly diminish if advantages of the undertaking must be made available to non-participants. The [compulsory access] rule becomes even more questionable where the rival applicants passed up an opportunity to participate in the joint venture in the first place.

Pitofsky, A Framework for Antitrust Analysis of Joint Ventures, 54 Antitrust L.J. 893, 902 (1985).[39]

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[38](...continued)

Cola Co., 740 F. Supp. 381, 393-94 (D. Md. 1990); American Floral Servs., Inc. v. Florists' Transworld Delivery Ass'n, 633 F. Supp. 201, 220 (N.D. Ill. 1986); see also EFT ¶ 23.07[1] ("The rationale for exclusion [from joint venture payment systems] rests on 'free rider' considerations."); Blumenthal, supra p. 31, at 868.

Sears' trial expert, James Kearl, conceded the legitimacy of free-rider concerns as a general matter. App. 756. However, he testified that because VISA has elected to remain open to others, he could find no "free-riding" problem that would justify VISA's refusal to admit Sears. App. 756-58. But the fact that VISA is open to others does not suggest that there is no free riding problem with Sears (or American Express). Because of so-called "positive network externalities" (App. 667-68), network joint ventures will desire to expand membership up to a point, even though such expansion creates both costs and benefits to pre-existing members. However not all applicants impose the same type or amount of costs. Thus, there are a number of circumstances that distinguish direct competitors, such as Sears (or American Express), from other prospective entrants. These include such things as a concern about confidential information (App. 472-73, 536-37, 993), the possibility of cross-marketing on both the issuing and merchant sides of business (App. 476-78, 632-33), the risk of regulation (App. 454-66, 479-80), the possibility of Sears converting its Discover program to VISA at a later date, the fact that Sears retail stores took Discover but not VISA (App. 478), and the fact that the proposed sharing would operate only in one direction (App. 468-78, 633-34).

[39] Similar observations have been made recently by Joseph Kattan, the current head of the Policy Section of the FTC's Bureau of Competition:

(continued...)

The issue is discussed at length by Prof. Areeda, both in his Essential Facilities article and in his seminal Treatise. Prof. Areeda also stresses the importance of protecting incentives for innovation. Areeda at 851. For that reason, he further observes that once a judgment is made that it is pro-competitive to permit the venture to exist in the first place, it should be allowed to retain the benefits of its collaboration to the same extent as any other entity. 7 Treatise ¶ 1478c. (If it achieves too much power, he says, the solution is to limit its future activities or, in extreme cases, dissolve it. Id. ¶ 1478b.) To do otherwise would disfavor joint ventures over other forms of industrial organization (or other, broader forms of integration, such as mergers.) See also App. 948-50.

A showing of essentiality also is appropriate because if a party is capable of competing successfully on its own, it should be required to do so.[40] While joint ventures frequently are pro-competitive, there is no reason to limit competition by firms that are capable of forming alternative joint ventures or can compete successfully against the venture on their own.[41] While that may often be difficult to determine, it is not in

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[39](...continued)

> From an efficiency standpoint, mandatory access rules are troubling. Limitations on joint venture membership offer a great procompetitive potential . . . . [A] requirement of mandatory access after a venture has succeeded in attaining its goals [also] can inhibit collaborative efforts to innovate in the first place. If free and open access is required, potential venturers may decide to avoid entering a joint venture, and incurring the risk that membership in the venture entails, because they may be required to share the fruits of the joint venture with outsiders if the venture succeeds but will be required to bear the losses alone if the venture fails. This free rider effect creates a serious risk that some efficiency-enhancing projects would be delayed or altogether deterred.

Kattan, supra p. 28, at 963; see also Blumenthal, supra p. 31, at 868.

[40] See Balto, supra note 12, at 272 ("[W]here an excluded party is able to compete effectively without access to the joint venture, mandating its admission may diminish competition in the market in which the venture competes."). Mr. Balto is an attorney with the Policy and Evaluation Office of the Federal Trade Commission.

[41] The mere fact that Sears might prefer to offer Prime Option through VISA, rather than on its own or through Discover, or that it might be somewhat better off economically by doing so, does not establish a right to demand access to the VISA name (continued...)

this case since VISA has drawn its regulation to exclude only those entities that have answered that question themselves by successfully electing to "fight 'em" rather than "join 'em."

In fact, a principal concern with joint venture "membership" rules is the danger that the venture will harm competition by being overinclusive. Unless membership is essential for meaningful competition to take place at all, limiting membership is likely to further competition against the venture by individual firms or through the creation of new, competing ventures. "Open" membership rules, by contrast, create the danger of a ubiquitous venture that eliminates all competition at the venture level.[42]

That concern is an important basis for the Antitrust Division's policy favoring an essentiality standard for joint venture membership:

> [T]he Department in general is concerned about the anticompetitive effects of a joint venture when it is overinclusive. . . . In fact selectivity in the membership of a joint venture often enhances a joint venture's procompetitive potential. Forcing joint ventures to open to all competitors . . . would decrease the incentives to form joint ventures, particularly those that are formed to undertake risky endeavors such as research and development and innovative manufacturing.

Int'l Guidelines, supra p. 32, § 3.42 (emphasis added); see also Pitofsky, supra p. 33, at 898 (reduction in potential competition is "the principal anticompetitive concern" with joint ventures); cf. United States v. Penn-Olin Chem Co., 378 U.S. 158, 174 (1964) (stressing importance of potential competition as "a substantial incentive to competition which cannot be underestimated").

The point is also illustrated by this case. There are thousands of VISA issuers that compete intrasystem to issue cards. However there are only four (or, on Sears'

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[41](...continued)
and systems. City of Chanute v. Williams Natural Gas Co., 955 F.2d 641, 648 (10th Cir.), cert. denied, 113 S. Ct. 96 (1992).

[42] In Mid-South Grizzlies the court rejected, as a matter of law, a claim that the NFL had a duty to grant a franchise to a group of owners from Memphis, Tennessee, on the ground, inter alia, that such an obligation would discourage the creation of new competitive leagues. 550 F. Supp. at 570.

view, five) competing charge card systems. Yet many important types of competition take place (and must take place) at the system level. Requiring VISA (and, presumptively, MasterCard) to accept Sears (and, presumptively, American Express and anyone else) will lead to further diminution in the incentives for intersystem competition. See also pp. 61-66, 71-73, infra.

Nor is this an issue that is appropriately left to the jury. Indeed, the relevant contest is not between competing sets of "facts" at all, but between a broad policy concern for the protection of property rights achieved through innovation and the demand of a party to declare after the fact, "now that you've taken the risk and succeeded, let me share your creations and I will do what you do better [or cheaper]." As Sears' expert acknowledged, that kind of an argument can always be made after the fact and, as thus stated, will often be appealing. App. 828-31. After all, who would not like something better (or cheaper)?

The problem is that the argument focuses on the situation too narrowly and at the wrong point in time. Letting a firm command access to its competitor's property after the fact has an unacceptably adverse impact upon incentives to create and innovate in the first place. That harm to consumer welfare imposes what VISA's expert described as an "invisible tax" on consumers generally, payable not just in their guise as users of credit cards, but as consumers of all products with a consequent stake in preserving incentives for innovation throughout the economy. App. 940-45. That notion inherently cannot be captured by an instruction that asks the jury to look at a rule ex post and to consider its effect solely in a particular "relevant" market. Rather, as Prof. Areeda points out, rules about compulsory sharing must be subject to a legal, or "macro," justification:

> [A]ny essential facilities doctrine must recognize macro level or class justifications. These legitimate business purposes are not personal to any particular defendant, but are propositions of general policy. For example, the justification for refusing to share a research laboratory does not focus on the practical infeasibility of letting another use the laboratory, but on the general concern that the defendant never would have built a laboratory of that size and character in the first place if he had known that he would be required to share

> it. Required sharing discourages building facilities such as this, even though they benefit consumers.

Areeda at 851. See also Areeda, Antitrust Law as Industrial Policy: Should Judges and Juries Make It?, in Antitrust, Innovation, and Competitiveness 28 (T. Jorde & D. Teece eds., 1992).

Finally, there is the problem of uncertainty. Under the decision below, joint venture membership (and other) rules are open to after-the-fact scrutiny under an unstructured rule-of-reason standard with treble damages as the price of predicting incorrectly. See Areeda, Industrial Policy, supra, at 40-41. The vagaries of that process are reflected dramatically by this proceeding. Had the case been tried to the court VISA would have prevailed. Before the jury Sears won.

The lesson that this potential randomness teaches is over-caution (in forming joint ventures at all) and over-inclusiveness (thereafter). The point was recently summarized by David Balto of the FTC in commenting on this case:

> [T]he rules of law concerning mandatory access need to be predictable so that business executives can plan collaborative activity. An unstructured, open-ended rule of reason inquiry, such as the one adopted by the court in [the VISA/Sears] case, gives potential venturers little guidance on how to assess the risks of handling access demands. Faced with this uncertainty, the joint venture may either give in to the access demand, rather than face the costs of uncertain litigation and the threat of treble damages, or forego the venture because such access may be mandated.

Balto, supra note 12, at 272; see also Areeda at 851.

d. Prior Cases Are Consistent with VISA's Position.

The court's response to the foregoing was that, whatever its force as a matter of reason and policy, it is not the law, particularly given the Supreme Court's decision in Associated Press v. United States, 326 U.S. 1 (1945). Opn. 980-81.[43] We respectfully disagree. As noted previously, the principle that firms ordinarily have no duty to deal

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[43] With the possible exception of Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co., 472 U.S. 284 (1985), discussed in text infra, none of the other cases cited by the Court is pertinent to a duty to deal, or share property, claim against a joint venture.

traces its roots back more than seventy years, to the Supreme Court's Colgate decision. 250 U.S. at 307 (1919). At approximately the same time, the Court recognized that this general principle may not apply where a firm or group of firms controls some unique and necessary facility that makes it commercially impracticable for those who are excluded to compete in a downstream market. Control of that "essential facility," thus, effectively precludes competition on the merits in the latter market. To open the "bottleneck" conferred by the natural monopoly, those controlling it may be compelled to grant access to it.

The most famous, and important, decision recognizing this principle is the so-called St. Louis Terminal case,[44] in which a joint venture among a number of railroads that controlled access across the Mississippi River at St. Louis were required to make such access available to non-venturers in order to allow those firms to compete in carrying freight to both sides of the river. 224 U.S. at 411-12. In reaching that result, the Court observed (quoting its Standard Oil opinion from the prior term) that "'one of the fundamental purposes of the [Sherman Act] is to protect, not to destroy, rights of property.'" 224 U.S. at 409 (quoting 221 U.S. at 78); see also United States v. E.I. du Pont de Nemours & Co., 366 U.S. 316, 360-61 (1961). Consistent with that proposition, the St. Louis Terminal Court noted that, "in ordinary circumstances," a combination of independent companies might combine to control facilities for their "exclusive use." Others could thereafter "be admitted" on any terms set by the owners or could be "excluded altogether" without the owners thereby violating the law. 224 U.S. at 405; see also id. at 409. It is only where "inherent conditions" (id. at 409) or some unavoidable obstacle (there, the "physical or topographical condition peculiar to the locality," id. at 405) make fair competition impossible that a duty to deal might be imposed.

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[44] 224 U.S. 383 (1912).

St. Louis Terminal thus laid the foundation of a limited duty to deal where a natural monopoly or some other equivalent circumstance renders the ordinary processes of competition unavailing and, thus, necessitates some form of forced sharing. That holding has since been applied in both single firm and joint venture cases. Its principles were the basis, for example, of the First Circuit's decision in GAMCO[45] involving a joint venture produce terminal as well as the Fifth Circuit's duty-to-deal analysis in United States v. Realty Multi-List, Inc., 629 F.2d 1351, 1371 & n.38, 1386 (5th Cir. 1980). By contrast, plaintiffs who claim a duty to deal without demonstrating an inability to compete in the relevant market, routinely fail as a matter of law. See, e.g., City of Anaheim v. Southern Cal. Edison Co., 955 F.2d 1373, 1380-81 (9th Cir. 1992); Schachar, 870 F.2d at 398-99; McKenzie, 854 F.2d at 370-71; Rothery, 729 F.2d at 222-23.

Associated Press does not require a different result. To begin, it is, at least in part, based upon the essential facilities principles discussed above. AP has been described by leading antitrust scholars as a "natural monopoly"[46] or essential facilities[47] case. The Supreme Court, itself, has so described it. See Northwest, 472 U.S. at 294 (AP involved denial of "access to a supply, facility or market necessary to enable the boycotted firm to compete"). In fact, AP was regarded by the government as an essential facilities case at the time. According to Judge Swan, who was a member of the three-judge panel in the district court in AP, St. Louis Terminal was "the case principally relied upon by the [United States]" as creating a duty by AP to serve all comers. 52 F. Supp. 362, 377 (S.D.N.Y. 1943).

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[45] GAMCO, Inc. v. Providence Fruit & Produce Bldg., Inc., 194 F.2d 484, 487 (1st Cir.), cert. denied, 344 U.S. 817 (1952).

[46] H. Hovenkamp, Economics and Federal Antitrust Law § 10.3, at 283 (1985).

[47] EFT ¶ 21.05; Areeda at 842-44; see also American Floral Servs., 633 F. Supp. at 217-18.

The facts described in the Supreme Court's opinion bear out that view. While there were two other competing news systems (UP and INS) the Court expressly approved the district court's observation that access to AP news was "universally agreed to be of great consequence," particularly among morning newspapers that controlled 96% of "the total circulation." 326 U.S. at 17-18; see also id. at 11 n.7. Failure to have access to AP news "[could] have the most serious effects upon the publication of competitive newspapers." (id. at 17) and it was "practically impossible" for a newspaper to develop a competitive source of news on its own. That is a fair restatement of the modern "essential facility" standard. See Tarabishi, 951 F.2d at 1568 n.14; McKenzie, 854 F.2d at 368-69; MCI Communications Corp. v. AT&T, 708 F.2d 1081, 1132-33 (7th Cir.), cert. denied, 464 U.S. 891 (1983); see also supra note 39.

While Justice Black's plurality opinion also invoked naked boycott cases, such as Fashion Originators' Guild[48] and Eastern States Lumber,[49] AP's by-laws did not contain a general prohibition against new members. Rather, they granted a local "veto power" that could be invoked by existing members against competitors in their respective territories. 326 U.S. at 10. In short, the by-law simply protected powerful local publishers against competition in local markets, rather than furthering any interest of the collective association. In fact, the opinion paid no attention to network-level competition at all.

Both the district court's dismissal of St. Louis Terminal and its reliance on AP are misplaced. St. Louis Terminal does not, as the court suggests, hold that proof of an essential facility "may result in a duty to deal" but does not "require[]" such a "showing . . . before a duty to deal will be imposed." Opn. 981 (emphasis added). That is, in fact, precisely what St. Louis Terminal requires. The Court's opinion is absolutely clear that

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48 Fashion Originators' Guild v. FTC, 312 U.S. 457 (1941).

49 Eastern States Retail Lumber Dealers' Ass'n v. United States, 234 U.S. 600 (1914).

but for essentiality there would have been no violation and no obligation for the joint venture to share its property with others. See 224 U.S. at 405, 409-10; see also p. 38, supra. Equally clearly, the trial court's assertion that the Supreme Court in AP was not concerned with "monopoly power" and that it "used the Rule of Reason to find the restraint unreasonable" (Opn. 976) is wrong on both counts. The Court was concerned with the exercise of economic power, but in local newspaper markets, not by the network. Further, the plurality opinion viewed AP's by-law as unlawful per se (see Northwest, 472 U.S. at 290); it, thus, affirmed summary judgment in the government's favor.

The Supreme Court explained the point in Northwest, where a joint purchasing cooperative excluded a member engaged in wholesale operations. The Ninth Circuit had held the expulsion unlawful per se as a group boycott. The Supreme Court unanimously reversed, holding that exclusions which are ancillary to efficiency-creating activities are not per se illegal. 472 U.S. at 295-98. The Court's opinion contains a lengthy discussion of the legitimate and potentially pro-competitive functions served by such cooperatives. Id. That discussion is entirely at odds with the "naked restraint" approach of Justice Black's opinion in Associated Press. The disparity is even more striking because the joint venture cooperative in Northwest involved far less of a productive integration than the true joint venture before the Court in Associated Press. Even in the case of the limited integration before it, however, Justice Brennan's analysis stressed the venture's potential for efficiencies. Id. at 295. The opinion, in that respect, is congruent with modern joint venture jurisprudence as reflected in such decisions as BMI and NCAA, both of which were extensively cited by the Court.

In sum, the district court's conclusion that the law required it to "stay its hand" in regard to the important antitrust policy issues presented by this case is incorrect. The United States put the point cogently in its brief amicus curiae in Northwest (at 16):

It would make little sense indeed to interpret the antitrust laws as providing for the forced expansion of a procompetitive horizontal arrangement to the point where the arrangement itself violates those laws. Not only does such an approach have little to recommend it as a matter of consistency, it could also lead to a loss of the substantial procompetitive benefits usually associated with purchasing cooperatives and similar joint ventures.[50]

3. Sears Failed as a Matter of Law to Demonstrate That Visa's Exclusion of Sears Unreasonably Restrains Competition.

If Sears is required to demonstrate an inability to compete successfully without access to VISA's property then its case, concededly, fails. See p. 22 n.24, supra; Opn. 980. But even if there is no controlling essentiality "screen," the record at trial was insufficient, as a matter of law, to sustain a finding that VISA's exclusion of Sears unreasonably restrains competition in the general purpose charge card market. Furthermore, any adverse effects of the restraint are outweighed, as a matter of law, by the benefits to intersystem competition resulting from the exclusion.

a. As a Matter of Law, Sears Failed to Demonstrate That VISA Possesses Market Power in the Relevant Market.

Proof of market power[51] is a threshold requirement under the rule of reason. Reazin v. Blue Cross & Blue Shield, 899 F.2d 951, 966, 968 n.24 (10th Cir.), cert. denied, 497 U.S. 1005 (1990); Schachar, 870 F.2d at 398 ("[t]he first question in any rule of reason case is market power"); Westman Comm'n Co. v. Hobart Int'l, Inc., 796 F.2d 1216, 1225 (10th Cir. 1986). In the absence of such power, there is no potential for a practice significantly to affect competition adversely and, therefore, no reason to inquire further. Thus, the issue was properly described by the court below as an acknowledged rule-of-reason "screen." Opn. 970. Proper application of that screen should have ended the inquiry in this case.

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50 Quoted in Balto, supra note 12, at 272; see also id. at n.14: "Where a joint venture provides a product or service necessary to effective competition, depriving a competitor of access to the product or service might well be found to be anticompetitive" (citing, inter alia, Associated Press) (emphasis added).

51 The court's analysis of market power is reviewed de novo (see supra p. 20). For VISA's objections, see App. 1118-32 (directed verdict motion), 700-03, 709-43.

VISA has 6,000 issuers that compete with each other (and with Sears and American Express) to issue cards and sign merchants. The top 10 VISA issuers account for less than 50% of VISA volume (and, of course, still less for the general purpose charge card market as a whole). Opn. 966 n.8. The concentration index, or HHI, for the market is a remarkably low 500.[52] App. 970-73. In addition, because VISA and MasterCard maintain open membership policies (except for direct intersystem competitors), there are virtually no barriers to entry. Even Prime Option, itself, is not excluded from the market since Sears admittedly could issue it as a brand of Discover card with precisely the same interest rate and other features as it has announced. App. 417, 419, 501-03.[53]

That evidence demonstrates a lack of market power. The presence or absence of Sears as an additional VISA issuer would have no material effect upon competition in the issuance of general purpose credit cards. App. 690, 985-86. Put otherwise, the

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52 Anything below 1,000 is considered unconcentrated by the Justice Department and represents, effectively, a "safe harbor" for market structure purposes. See Pitofsky, New Definitions of Relevant Market and the Assault on Antitrust, 90 Colum. L. Rev. 1805, 1821 (1990).

53 The structural evidence in this case is consistent with the conclusions of the relevant economic literature. See App. 978, 1415. Among these studies is a report of the Federal Reserve Board, which is required by law to report on the state of competition in the credit card business (Fed. Reserve Board, The Profitability of Credit Card Operations of Depository Institutions at 14-15 (Aug. 1990) (App. 1667)), recent studies by economists at the Department of Justice (Raskovich & Froeb, Has Competition Failed in the Credit Card Market? (Dep't of Justice EAG 92-7, Jun. 12, 1992) (App. 1796)) and at Brookings Institute, as well as a 1986 study by Lexecon, Inc. which was an expert consultant for Sears in this case and which concluded that the market was "intensely competitive, approaching the textbook example of an 'atomistic' market." App. 1437; see also App. 1819-23, 977-82. None of this evidence should have surprised Sears, since it has repeatedly stated, both internally and publicly, for nearly 10 years that the credit card business is extremely competitive. See App. 1410 ("Competition in the credit card business . . . is extremely intense."), 1341, 1344 ("The credit card environment is highly competitive."), 1524 ("extremely intense" competition).

Sears' expert -- who acknowledged that he has had no experience in the credit card or banking business, has never written on the subjects of his testimony, and does not even list himself as an industrial organizational economist (App. 763-65) -- nonetheless opined that all of those studies and reports were flawed because they failed to take account of VISA By-law 2.06. App. 1819-23. It apparently did not occur to him that all of the other experts who had looked into the matter failed to mention the by-law because it has no competitive significance. See App. 980-85.

structure of the market in this case is fatally inconsistent with Sears' claim. See Brook Group, 113 S. Ct. at 2589 ("where the market is highly diffuse and competitive, or where new entry is easy . . . summary disposition of the case is appropriate"); AA Poultry, 881 F.2d at 1401 ("Market structure offers a way to cut the inquiry off at the pass.").[54]

In Rothery, 792 F.2d at 219-20, the D.C. Circuit affirmed summary judgment in favor of a joint venture that imposed restraints on its members where the venture lacked market power:

> A joint venture made more efficient by ancillary restraints, is a fusion of the productive capacities of the members of the venture. That, in economic terms, is the same thing as a corporate merger. Merger policy has always proceeded by drawing lines about allowable market shares and these lines are based on rough estimates of effects because that is all the nature of the problem allows. If Atlas bought the stock of all its carrier agents, the merger would not even be challenged under the Department of Justice Merger Guidelines because of inferences drawn from Atlas' market share and the structure of the market. We can think of no good reason not to apply the same inferences to Atlas' ancillary restraints.[55]

Id. at 230.

Sears did not dispute VISA's evidence concerning the structure of the market. Instead, its expert argued that notwithstanding those facts VISA possesses market power because its members have the power to make rules for the joint venture. App. 684-85. Therefore, he asserted, it is appropriate to consider the collective share of VISA's members in evaluating market power. Without expressly endorsing Dr. Kearl's thesis, the court below held that it was sufficient to go to the jury and, hence, sufficient to sustain a verdict implicitly adopting it. See Opn. 970.

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54 In AA Poultry the court of appeals affirmed a j.n.o.v. where the episodic evidence concerning defendant's intentions and practices "impressed the jury" but "objective information" about the market was "'not sufficient to find actual competitive injury.'" 881 F.2d at 1398-99. Among the points noted by the court were not only the relevant market share numbers, but the presence of "persistent entry," and the existence of numerous competing suppliers. Id. at 1403; see also Barr Labs., Inc. v. Abbott Labs., 978 F.2d 98, 112-15 (3d Cir. 1992) (summary judgment affirmed where the market structure demonstrated an absence of competitive harm); Reazin, 899 F.2d at 967-69; Ball Memorial Hosp., Inc. v. Mutual Hosp. Ins., Inc., 784 F.2d 1325, 1334-36 (7th Cir. 1986).

55 Cf. App. 824-26 (complete elimination of one of top 10 VISA issuers by merger into another would have no material effect on the market structure).

The court erred in so holding. This is, to begin, an issue of law, not fact. There was no debate in this case about the relevant evidence (or about the definition of the relevant market, for that matter). The debate, instead, was about whether Dr. Kearl's "collective share" thesis is economically tenable as applied in this case. That is a question of law for the court. Brook Group, 113 S. Ct. at 2598. The point is summarized aptly by Professor George Hay in his recent article, Market Power in Antitrust:

> [D]isputes about the existence of market power frequently are not simply empirical skirmishes, in which one economist's estimate of cross-elasticity is pitted against that of another. Rather, the debate often goes to the very concept of market power, i.e., what is the economist attempting to measure and what factors are properly considered in assessing whether market power exists?

60 Antitrust L.J. at 807.[56]

The principal problem with Dr. Kearl's approach is precisely the point noted by Prof. Hay: It divorces the analysis of market power from any notion of what relevant antitrust question we are trying to answer by making the inquiry, or how the answer relates to the claim advanced by the plaintiff. But market power does not exist "in the air." To the contrary, such power is meaningful only when considered in reference to the specific practice that is challenged in a given case. See 2 Treatise ¶ 518 ("One cannot determine the degree of market power that merits concern . . . without reference to the legal context in which the issue arises."). Market power is, as the Supreme Court noted in Indiana Dentists,[57] simply a surrogate for evaluating actual effects. 476 U.S. at 461. As such, its existence must be assessed with reference to the particular practice in issue.

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[56] VISA does not argue that the existence vel non of market power is a question of law in every case. There often may be legitimate factual disputes about the dimensions of the relevant product and/or geographic market. Here, however, the jury, in effect, was asked to adjudicate questions of economic theory. That is not a factual issue and should not have been presented to the jury.

[57] FTC v. Indiana Fed'n of Dentists, 476 U.S. 447 (1986).

The relevant "power" is that which helps a trier of fact predict the potential competitive effect of that practice.

Sears' claim in this case is that VISA's exclusion precluded Sears from competing as a VISA issuer and offering its new, assertedly low-priced, Prime Option VISA card. Hence the pertinent question is what effect that exclusion might have on competition in the issuance of credit cards to consumers. See AA Poultry, 881 F.2d at 1403 ("[c]oncentration . . . should be measured from customers' perspectives"). The point was addressed at trial by Prof. Schmalensee. He testified that to answer that question properly it is necessary to look at the market in which the alleged restraint occurred (to wit, competition in the issuance of credit cards) and consider the potential effect of the restraint on that competition. App. 985-93, 1080. That effect is measured by evaluating the market with or without Sears, i.e., a market with thousands of issuers in which the only effect of the challenged rule is to exclude Sears and American Express from the VISA brand portion of it. App. 950-58, 973-77, 985-88. That presents no significant antitrust issue as a matter of law. See App. 972-73.[58]

The same point can be demonstrated by reference to the traditional role of market power analysis in both economics and antitrust law. Economists define market power as a firm's (or group of firms') ability to raise prices and restrict output.[59] App. 950-51; Landes & Posner, Market Power in Antitrust Cases, 94 Harv. L. Rev. 937, 937 (1981). Courts express essentially the same concept as the power to raise prices and/or

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[58] The analysis is no different if one focuses on the "top ten" issuers, as Sears repeatedly attempted to do. The HHI is still exceedingly low. App. 973.

[59] Market power does not -- in economics or law -- refer to any quantum of power, or brand differentiation, indicated by a downward sloping demand curve. Hay, supra p. 30, at 813. Rather, "market power" is economists' (and hence, antitrust law) shorthand for the ability of firms to maintain prices significantly above competitive levels over a substantial period of time. See, e.g., 3 Treatise ¶¶ 812-15, at 298-304; Hay, supra p. 30, at 814 ("[m]arket power for antitrust purposes should refer to a situation in which a firm or group of firms is able profitably to maintain prices significantly above the competitive level for a sustained period of time"); see also App. 950-51, 778-79.

exclude competition from the market. Westman, 796 F.2d at 1225 ("Market power is the ability to raise prices above those that would be charged in a competitive market"); Bacchus Indus., Inc. v. Arvin Indus., Inc., 939 F.2d 887, 894 (10th Cir. 1991). Under either articulation, the Sears/Kearl thesis fails to address the pertinent issue: with 6,000 issuers (or 10 issuers accounting for less than 50% the market) who compete with each other on price and other terms, and with no output restrictions, how does By-law 2.06 give VISA any power to restrict output or raise prices? Similarly, there are no barriers to entry into the market in this case. VISA (and Mastercard) are open to any new entrant except for Sears and American Express and those two firms already are in the market successfully on their own. Thus, no firm is excluded from the market (which is the relevant inquiry) and only two firms are excluded from even the VISA brand segment of the market. As this Court has noted, "Without significant barriers to entry, it is unlikely that [a firm] could be able to eliminate competition and control prices for any significant period of time." Bacchus, 939 F.2d. at 894.

Sears' "collective share" thesis simply does not speak to that issue. VISA's ability to pass rules generally says nothing about whether its members have the ability to raise prices or exclude competition from the market. Indiana Grocery, Inc. v. Super Valu Stores, Inc., 864 F.2d 1409, 1414 (7th Cir. 1989) ("[m]arket share indicates market power only when sales reflect control of the productive assets in the business [and thus] ability to curtail total market output"); Barr Labs., 978 F.2d at 112; Ball Memorial, 784 F.2d at 1336.[60]

As an apparent alternative to Sears' "collective share" theory, the court suggested that market power might have been inferred by the jury from evidence that

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[60] Which is not to say that collective share analysis is always irrelevant. If, for example, VISA's members adopted a rule requiring all members to charge subscribers a single fee, it would not only be proper, but necessary, to look at market share collectively since that would be the measure in that case of the amount of competition eliminated from the market by the rule. The point is that one must look at the potential effect of the particular alleged restraint. VISA's analysis does so; Sears' does not.

certain VISA issuers earned "high" profits for several years and that entry of another large VISA issuer might affect price. Opn. 985-86. But the court did so without any reference to a comparable competitive industry that provides a baseline against which the so-called "high" profits could be compared. That approach is flawed as a matter of law.

In fact, "high" profits prove nothing. What was required was competent proof demonstrating the existence of "supra-competitive" profits, that is, profits consistently maintained above the risk-adjusted rate of return across the market. See, e.g., Reserve Supply Corp. v. Owens-Corning Fiberglass Corp., 971 F.2d 37, 52 (7th Cir. 1992) ("high profits" cannot be equated with "supracompetitive" profits absent "evidence, such as studies on comparative costs of production or on market conditions, to indicate that these profits were above those available in a competitive market"). As the Supreme Court pointed out in Brook Group:

> Where . . . output is expanding at the same time prices are increasing, rising prices are equally consistent with growing product demand. Under these conditions a jury may not infer competitive injury from price and output data absent some evidence that tends to prove that output was restricted or prices were above a competitive level.

113 S. Ct. at 2595 (emphasis added); see also Hay, supra p. 30, at 825.

Here, however, Sears' expert expressly disclaimed any view about excess profits at his deposition. When he then attempted to comment about the issue indirectly at trial the court excluded the testimony as improper in light of the earlier disclaimer. App. 709-13, 741-43. Moreover, as Prof. Hay notes, one of the reasons courts look at market structure is "because of the difficulty of measuring market power directly." Hay, supra p. 30, at 825.[61] "Identifying excess profits is no less difficult." Id. And, in any event, "[p]rofits can be the result of luck, skill, or simply the short-run disequilibrium of an industry." Id.; 2 Treatise ¶ 512.

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[61] Sears designated Prof. Hay as a potential trial expert but did not call him.

There was, thus, an entire failure of proof by Sears on this threshold issue. Given the structure of the market, Sears bore a particularly heavy burden of supporting its counter-intuitive position with probative evidence. Brook Group, 113 S. Ct. at 2589. Instead, it offered nothing beyond Dr. Kearl's ipse dixit. That was not enough. In Brook Group, the Supreme Court recently reversed a jury verdict for plaintiff as a matter of law despite the testimony of a highly credentialed expert supporting plaintiff's position. The court noted that "[w]hen an expert opinion is not supported by sufficient facts to validate it in the eyes of the law, or when indisputable record facts contradict or otherwise render the opinion unreasonable, it cannot support a jury's verdict . . . . Expert testimony is useful as a guide to interpreting market facts, but it is not a substitute for them." Id. at 2598; see also Matsushita, 475 U.S. at 594 n.19; Richardson by Richardson v. Richardson-Merrell, Inc., 857 F.2d 823, 829 (D.C. Cir. 1988) (court need not "accept uncritically any sort of opinion espoused by an expert merely because his credentials render him qualified to testify"), cert. denied, 493 U.S. 882 (1989).

b. Sears Failed to Demonstrate Any Harm to Competition.

In addition to its failure to prove market power, Sears failed to demonstrate any cognizable harm to competition in the relevant market.[62] In the early 1980s, when Sears elected to become an important player in the general purpose charge card business, it could have done so by becoming a major VISA issuer. Instead, it chose to introduce its own proprietary card because it concluded that that was its preferred "high-reward" (and "high-risk") strategy. App. 1327, 536-39. Sears' Discover card has been remarkably successful, with an estimated going concern value after only seven years of $2 billion. App. 403-05. Discover is one of the two largest card programs in the country in terms of cards, accounts or volume. App. 887-89. According to its top executives, Discover has been so successful precisely because there are a number of important

[62] For standard of review, see supra pp. 20-21. For VISA's objections, see App. 1132-46, 215, 1157-60, 1176.

advantages to operating a wholly-owned program, rather than being just one member of a joint venture association.[63]

Sears further acknowledges that VISA's 6,000 card-issuing members are free to, and do, compete with one another (and with Discover and American Express) in the issuance of credit cards. VISA does not control the output, prices or territories of its members. Further, with the exception of Sears and American Express, VISA maintains an open membership policy. Thus, absolutely no one has been excluded from the general purpose charge card market. Sears similarly does not dispute that the mandatory access it proposes would be one way – i.e., Sears claims the right to use VISA's name, marks and systems but asserts its prerogative, as a single firm, to keep its creations to itself. App. 418, 500. In short, the only consequence of By-law 2.06 is that it prevents Sears and American Express, which already are in the market successfully in another way (as a result of their own choice), from also using VISA's name, marks and systems to offer another brand of VISA card in competition with the numerous existing VISA issuers.[64]

Those facts, we submit, are dispositive. While By-law 2.06, "restrains" competition in the literal sense described by Justice Brandeis in Chicago Board of Trade, it is not therefore unlawful, nor could a reasonable jury conclude otherwise. Brook Group, 113 S. Ct. at 2595.

Sears' response is that the evidence was a matter for the jury, which was entitled to credit its claims: (a) that VISA's members were interested in protecting their profits; (b) that in spite of overwhelming structural evidence of a competitive market, there appears to be some form of market imperfection; and (c) that Sears intended to

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[63] These advantages are described at some length in internal Sears documents as well as in the testimony of Sears' trial witnesses. E.g., App. 1294, S0001; see also App. 536-61.

[64] We leave aside – but, only for the moment – Sears' "disincentive" argument. See pp. 57-60, infra.

offer a new low-cost brand of VISA card that consumers should have the right to "choose." But none of that evidence was sufficient to sustain a verdict for Sears in this case.

Consider, first, Sears' so-called intent evidence. The court expressly advised the jury that it should consider VISA's intentions in evaluating the legality of its by-law. App. 238. Yet the only "intent" that Sears pointed to was the universal (and lawful) intention of VISA's members to keep whatever business they could for themselves -- i.e., to profit maximize. App. S0091, S0089, S0094. The fact that VISA's members were interested in preserving their profits says nothing about the effect of By-law 2.06. See Ball Memorial, 784 F.2d at 1338; AA Poultry, 881 F.2d at 1402. Professor Areeda notes why such evidence has no bearing on the appropriateness of a refusal to share property with one's rivals:

> The [antitrust] defendant's intention will seldom be helpful, for his denial of access to a competitor is always motivated, at least in part, by the desire to exclude him and keep as much of the market as he can for himself. This lay sense of "exclusionary" must not be confused with its antitrust meaning of "exclusion by improper means."

Treatise ¶ 736.2a (Supp. 1992); see also Brook Group, 113 S. Ct. at 2589 ("[e]ven an act of pure malice by one competitor against another does not, without more, state a claim under the federal antitrust laws"). To the same point, in Rural Telephone Service Co. v. Feist Publications, Inc., 957 F.2d 765, 769 (10th Cir.), cert. denied, 113 S. Ct. 490 (1992), this Court cited with approval the First Circuit's observation that "the desire to crush a competitor standing alone, is insufficient to make out a violation of the antitrust laws . . . . As long as [defendant's] conduct was itself legitimate, the fact that some of its executives hoped to see [plaintiff] disappear is irrelevant."[65]

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[65] Intent evidence has been increasingly discounted by the courts in antitrust cases, even where such intent is literally a part of the offense (as in attempt to monopolize and predatory pricing cases). See, e.g., AA Poultry, 881 F.2d at 1401-02; Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 230-32 (1st Cir. 1983). Without adequate proof of a substantial effect on competition there is no liability under the Sherman Act. Schachar, (continued...)

The balance of Sears' case came almost entirely from its expert, Prof. Kearl. He asserted, first, that despite a seemingly competitive market structure, there nonetheless appeared to be some form of market imperfection. App. 694-97. Second, he claimed that market structure was, in any event, irrelevant because of VISA's "collective rule-making" power. App. 813-15. Finally, he contended that Sears should be allowed into VISA because proprietary cards cannot prevent the "significant" exercise of such market power by VISA's members. App. 684, 687-89.

That testimony fails to sustain the jury's verdict. Dr. Kearl's testimony can have no greater force than the reasonableness of his opinions and the evidentiary foundation upon which they rest. Brook Group, 113 S. Ct. at 2598; Mid-State Fertilizer Co. v. Exchange Nat'l Bank, 877 F.2d 1333, 1339-40 (7th Cir. 1989); Olympia, 797 F.2d at 382.[66]

In fact, plaintiff's thesis is "economically senseless." Eastman Kodak, 112 S. Ct. at 2083 ("[i]f the plaintiff's theory is economically senseless, no reasonable jury could find in its favor"); see also Brook Group, 113 S. Ct. at 2598. The problem with Dr. Kearl's initial argument (that there is a failure of competition in the market, structure notwithstanding) is that it is a pure conclusion -- an a priori premise unsupported by (or actually inconsistent with) the record and based upon no systematic study. See, e.g.,

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[65](...continued)
870 F.2d at 400 ("Animosity, even if rephrased as 'anticompetitive intent' is not illegal without anticompetitive effects."); Barr Labs., 978 F.2d at 106-09 (summary judgment affirmed despite evidence "unequivocally" demonstrating defendant's intent "to force its competitors out of the market and enable it to raise prices" where there was no "market data indicating actual competitive injury").

[66] The court implies that it may have had questions about Prof. Kearl's qualifications but that no objection to them was made. Opn. 985. That being so, the court concluded, all else was for the jury. Opn. 985-86. But that is not the case. The problem is not with Dr. Kearl's right to appear, but with the substance of his opinions and the basis (or lack of basis) for them. Brook Group, 113 S. Ct. at 2598. As the Supreme Court noted last term in Daubert v. Merrell Dow Pharmaceuticals, Inc., 113 S. Ct. 2786, 2795 (1993), the Federal Rules of Evidence require "the trial judge [to] ensure that any and all scientific testimony or evidence admitted is not only relevant, but reliable." See also Richardson, 857 F.2d at 829.

Newman v. Hy-Way Heat Sys., Inc. 789 F.2d 269, 270 (4th Cir. 1986); AA Poultry, 881 F.2d at 1408 (no study by expert); Merit Motors, Inc. v. Chrysler Corp., 569 F.2d 666, 672 (D.C. Cir. 1977).

To begin, Sears did not produce evidence of supracompetitive profits. Instead, Dr. Kearl testified that he had "observed" high profits and "sticky" interest rates that persisted for some time despite substantial entry. App. 694-95. Therefore, Dr. Kearl concluded, there must be a failure of competition in the market. App. 697. But, again, his testimony is premised upon no study of actual market conditions to determine whether his observations about profitability say anything at all about a failure of competition. Cf. Daubert, 113 S. Ct. at 2795 ("the word 'knowledge' [in FRE 702] connotes more than subjective belief or unsupported speculation"). Indeed, he acknowledged on cross-examination that the facts he observed were readily explicable as the response to a surge in demand for credit (or the expansion of its availability) following the so-called Carter credit squeeze in the preceding few years. See App. 800; cf. Hay, supra p. 30, at 825.

The same observations are true of supposedly "sticky" rates -- a phenomenon that has been systematically studied by economists in the Department of Justice whose work rejects the suggestion that it is evidence of a lack of vigorous competition in the credit card market. Raskovich & Froeb, supra note 53; cf. Carlton, The Rigidity of Prices, 76 Am. Econ. Rev. 637 (1986).[67] Prof. Kearl's untested hypothesis is particularly unpersuasive because of his own observation that there has been substantial entry into the market (App. 694-95) -- a circumstance which traditionally dispels any concern over competition. Brook Group, 113 S. Ct. at 2595; Bacchus, 939 F.2d at 894; AA Poultry,

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[67] The anomaly of Dr. Kearl's point is reflected by the fact that, if it were correct, it would prove that Discover -- with its consistent 19.8% APR -- has market power.

881 F.2d at 1403; Ball Memorial, 784 F.2d at 1335; Barr Labs., 978 F.2d at 113-14; see also App. 974-77.[68]

In any event, it is hard to see how Sears' entry would make a difference if others' did not. If Sears' possesses any unique efficiencies of its own, it could exploit them by offering Prime Option itself (or by lowering the price on its Discover card, for that matter). On the other hand, if the only "efficiencies" Sears hoped to exploit came from taking a "free ride" on VISA and its members' prior efforts and investments, the advantage is not only illicit, but demonstrates precisely why VISA voted to exclude Sears. See, e.g., Rothery, 792 F.2d at 221, 229; EFT ¶ 23.07[1].[69]

Dr. Kearl's second point is that VISA possesses market power because its members in the aggregate have the ability to restrain competition through their collective power to pass rules binding upon the joint venture. App. 682. We have dealt with that

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[68] Dr. Kearl's testimony is also unavailing because he took no account of the non-price forms of competition in this industry, such as extended product warranties, bonus attractions (such as airline mileage) and the like. See App. 811-12. Cf. Brook Group, 113 S. Ct. at 2594 (where "price competition is most likely to take place through less observable and less regulable means than list prices, it would be unreasonable to draw conclusions about the existence of . . . supracompetitive pricing from data that reflects only list prices"). Non-price competitive strategies are employed in this industry to avoid the problem of so-called "adverse selection." Lower prices tend to attract those customers more sensitive to cost and hence more likely to default. Non-price competition protects against this adverse selection problem while providing attractive and competitive product offerings. Litan, The Impact of Price Controls on the Credit Card Industry 24-29 (Brookings Institute Monograph, Mar. 1992) (App. 1746).

[69] Dr. Kearl also testified that he has observed "price discrimination" in the market. App. 746-48. That is not surprising since, as he points out in his textbook, "price discrimination is pervasive." J. Kearl, Contemporary Economics 336 (1989). It also is no more than "evidence of some market power." Id. at 337; emphasis in original. Yet Dr. Kearl made no attempt in this case to determine whether the so-called "price discrimination" he observed has any actual significance or, indeed, whether what he observed is properly described as price discrimination at all. Price discrimination is not merely a question of selling the "same" (not "similar" as Kearl testified, App. 746) commodity at different prices, but doing so where the difference is not "explicable by cost differences." App. 1106-07. In fact, as Judge Easterbrook has pointed out, there are many situations in which charging the same price to different customers may represent price discrimination in an economic sense. AA Poultry, 881 F.2d at 1406. Absent evidence that Prof. Kearl made any investigation about price "discrimination" that would permit him to actually identify it as such, let alone determine its extent and significance, the testimony lacks any substantive content. Id. at 1407-08; Merit Motors, 569 F.2d at 672.

argument previously (see pp. 42-47) and note only that whether VISA (or, more precisely, VISA's members) in some technical sense possess "market power" because they have the "ability" or "potential" collectively to restrict competition through rule-making, does not permit Sears to avoid demonstrating that the particular exercise of that power -- to wit, By-law 2.06 -- has a substantial adverse effect on competition. For all of the reasons explained earlier, such a claim is economically untenable.

Prof. Kearl's final point is that, for a variety of purported reasons, a proprietary card cannot be a fully effective competitor against a VISA card. Therefore, he argues, the market needs to have another VISA card. App. 687-90. But the argument simply avoids the issue.[70] The reason why there is no competitive need for another VISA card is not because proprietary cards are a complete substitute (which is the question Dr. Kearl chose to pose for himself), but because the 6,000 VISA and MasterCard issuers already in the market demonstrate that there is no competitive harm to begin with. Yet before Sears is permitted to demand access to VISA's property to solve a problem with competition it needs to show that there is such a problem. By attempting to focus attention on the wrong question ("Do proprietary cards adequately substitute for VISA or Mastercard?"), his testimony invites us to ignore the real and dispositive issue ("With 6,000 VISA and MasterCard issuers, almost entirely open entry, and no restrictions on output or price competition, what difference does it make?"). See AA Poultry, 881 F.2d at 1408.

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[70] It is, also, a sub silentio effort to redefine the relevant market that Sears itself had alleged.

Finally, Sears' evidence concerning its supposedly low-cost card and consumers' right to "choose" is not only factually unpersuasive[71] but beside the point as a matter of law. No principle of antitrust law with which we are familiar makes a willingness to charge a lower price warrant for access to someone else's property -- be it a single firm, a joint venture or otherwise. Similarly, the desire of consumers to have Toyota or Honda manufacture "Chevrolets" creates no obligation for General Motors to oblige. Indeed, the point underscores the extraordinary nature of what Sears claims in this case. The paradigm of competition in our society is to build a better mousetrap, not take someone else's.[72]

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[71] As aptly recognized by the trial court, free lunches are as infrequent in the credit card business as they are elsewhere. Opn. 984. Sears' incentives are no different than VISA's: in the words of a Prime Option "planning" document, to "maximize profitability." App. S0002. To that end, it is perfectly reasonable to expect Sears to offer low introductory prices in order to establish its new product by taking market share away from existing firms. However, over the long run, its incentives will be to price its card in the way that achieves the greatest advantage for Sears, not for consumers. See Opn. 983-84. The court also properly disregarded Sears' self-serving testimony about Prime Option as a low-cost card. Opn. at 983. In fact, as noted above (supra note 16), the court observed that Sears has never offered a particularly low-cost product. Id.

[72] The jury's verdict should be set aside for a further reason. We have discussed in text why Sears' evidence was insufficient to establish a violation of the Sherman Act. However, Sears' case to a large extent was not directed to that issue at all. Rather, a substantial portion of Sears' evidence at trial was directed at showing that VISA engaged in aggressive competition against Discover and that it "discriminated" against Discover by permitting "duality" and by allowing one of its members, Citicorp, to issue the Diners Club card. See, e.g., App. 349-50, 352. For VISA's objections, see App. 83, 458-63, 512-30, 210-12, 1165-70. As Sears tried its case to the jury, VISA's open membership policy and its 6,000 members was not fatal evidence of competition and lack of market power but, instead, was proof of "discrimination" by VISA against Sears -- a discrimination that Sears described as the "heart" of its case. App. 510, 517, 565. Similarly, the fact that VISA competed aggressively against Sears' new Discover card was repeatedly adverted to as a form of "unfairness." See, e.g., App. 387-91.

But such evidence is not proof of an antitrust violation. The antitrust laws are not civil rights or unfair competition statutes. Brook Group, 113 S. Ct. at 2589 (antitrust laws "do not create a federal law of unfair competition"); Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 488 (1977) (the antitrust laws were enacted for "the protection of competition, not competitors"); Reazin, 899 F.2d at 960. Nor do they impose an obligation to treat one's competitors generously. To the contrary, the Sherman Act encourages vigorous, aggressive competition. Copperweld, 467 U.S. at 767; Ball Memorial, 784 F.2d at 1338-39. VISA therefore requested an instruction advising the jurors that VISA's "anti-Discover campaign" and its differential treatment of Sears, were not evidence of an antitrust offense and could not be taken into account as such in the jury's deliberations. App. 458-63, 512-30, 1121-22, 210-212. The court declined the (continued...)

c. Sears' Alternative "Disincentive" Theory Is Legally Irrelevant and Proves Nothing About the Effect of VISA's Exclusion of Sears.

The event that led to this lawsuit was VISA's refusal to admit Sears to membership, thereby preventing it from offering consumers its new, assertedly low-cost, brand of VISA card. However, at trial, Sears' economist offered a new and additional theory: that VISA's by-law is anti-competitive not only because it precludes Sears' from offering a new brand of VISA card, but because it discourages other firms from starting new proprietary credit card programs to compete against VISA (and, presumably, against Discover and American Express as well). App. 682.

VISA objected to this "disincentive" theory on the ground that since Sears already was offering a proprietary card, it was not affected by the supposed disincentive. App. 1132-46, 215, 1157-60, 1176. That being so, Sears had no basis to assert the entirely separate interests of other parties who (theoretically) might have been dissuaded from starting a new card brand. The Court agreed that Sears had suffered no harm from the supposed "disincentive" but, nonetheless, held that Sears could present its theory to the jury on the ground that once a party has standing to challenge a rule or practice on one ground it may rely upon any evidence concerning its effect, even if the particular theory bears no relation to the way in which the plaintiff assertedly was harmed by the challenged practice.[73] Opn. 988-89. Thus, not only did Sears present its disincentive

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[72](...continued)
proffered instructions and, instead, instructed the jury only that "[t]he antitrust laws do not necessarily require businesses to deal with similar firms in a similar manner." App. 238 (emphasis added). Far more important, the court advised the jury that it could consider the evidence as bearing on VISA's "intent" and further instructed them that it had admitted the evidence "in order to help you decide what effect the passage and enforcement [of VISA's by-law] had on competition in the relevant market." Id. (emphasis added). The jurors were told to give the evidence whatever weight they "believe[d] it deserves" on that issue. This was error and, by itself, requires reversal for a new trial. Sunkist Growers, Inc. v. Winckler & Smith Citrus Prods. Co., 370 U.S. 19, 30 (1962) (if "upon any one issue error was committed, either in the admission of evidence, or in the charge of the court, the verdict cannot be upheld").

[73] Standard of review: de novo (see supra p.20).

claim to the jury, but the court's post-trial decision repeatedly cites the disincentive argument as a basis for sustaining the jury's verdict. See, e.g., Opn. 986, 988-89.

VISA submits that permitting the jury to base its verdict on Sears' disincentive evidence was error and requires a new trial without more. That is true for several reasons:

(1) The court erred in holding that because Sears allegedly was harmed by being prevented from offering a VISA card, it was entitled to present evidence that VISA's by-law unreasonably restrained trade by dissuading others from creating new proprietary card systems. A party seeking relief under the antitrust laws -- whether damages[74] or an injunction[75] -- must show that it has suffered harm of the type the antitrust laws were intended to prevent" by reason of the challenged practice. Local Beauty Supply, Inc. v. Lamaur, Inc., 787 F.2d 1197, 1204 (7th Cir. 1986); City of Rohnert Park v. Harris, 601 F.2d 1040, 1044 (9th Cir. 1979), cert. denied, 445 U.S. 961 (1980). The fact that some other party assertedly may have been harmed by the supposed "disincentive" effect of VISA's by-law does not mean that Sears has been. In fact, it concededly has not. Opn. 989.

An antitrust plaintiff may not assert someone else's injury to support a verdict in its favor under an entirely separate theory. Atlantic Richfield Co. v. USA Petroleum Co., 495 U.S. 328, 337-38 (1990) ("ARCO"); Anago Inc. v. Tecnol Med. Prods., Inc., 792 F. Supp. 514, 519 (N.D. Tex.), aff'd, 976 F.2d 248 (5th Cir. 1992). The fact that some other party might complain about a particular aspect (or effect) of a challenged practice does not mean that an unaffected party may do so. Yet that is precisely what Sears attempted to do here. See ARCO, 495 U.S. at 342 (plaintiff may assert a claim only

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[74] Brunswick, 429 U.S. 477.

[75] Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104 (1986).

where "the harm claimed . . . corresponds to the rationale for finding a violation of the antitrust laws in the first place").

In fact, Sears' disincentive argument is not only different but inconsistent with its demand for VISA membership. The disincentive argument rests on the supposed need for system-level competition, whereas Sears' own claim for membership relates only to intrasystem competition. What is more, forcing VISA to admit Sears is likely to reduce existing intersystem competition. See pp. 61-66, infra. As an existing competitor Sears would benefit, not suffer, from any disincentive to the formation of new systems. Cf. ARCO, 495 U.S. at 336-37; Matsushita, 475 U.S. at 585 n.8.

(2) The foregoing point can be demonstrated in an additional way. Sears asserts that it was attempting to present evidence of two separate effects of one practice. But that is incorrect. Its evidence, instead, involved the separate effects of two different practices. Sears challenges VISA's refusal to admit two existing interbrand competitors into the VISA system, thereby limiting -- at least to that modest extent -- intrabrand competition within VISA. That is what assertedly harmed Sears and, further, is what assertedly harmed consumers by depriving them of the putative benefits of Sears' proposed new Prime Option VISA card. In addition, VISA's rules provide that anyone that elects to offer a card deemed competitive with VISA will be precluded from also offering a VISA card -- thereby, says Sears, creating a disincentive against the creation of new intersystem competition. But not only are the effects different, the rules themselves are separate. Whether it is permissible for VISA to attempt to "disincent" additional potential system competition, says nothing about the appropriateness of VISA's effort to maintain existing competition from Sears and American Express, which is the only question presented by this case.[76]

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[76] Moreover, as Prof. Schmalensee aptly noted, the disincentive rule will not discourage anyone (such as Sears, or American Express) that believes it can do better on its own. App. 996-1001. In short, not only is no one excluded from the market, but every firm can enter in whatever mode it considers best for itself.

(3) There also is no evidence to support Sears' "disincentive" theory. It was presented by Sears' expert as a mere theoretical possibility. Nor did Sears or its expert even make an effort to validate its novel thesis. App. 795-96. See AA Poultry, 881 F.2d at 1407-08 (expert's testimony rejected where no study done). Something more is required to sustain a verdict than that kind of speculation, by an expert or anyone else. See Rural Telephone, 957 F.2d at 769 (plaintiff "unable to identify anyone" who was dissuaded from dealing with plaintiff); Barr Labs., 978 F.2d at 114 (summary judgment affirmed where no evidence that any competitor was forced out by defendant's conduct); Zenith Radio Corp. v. Matsushita Elec. Indus. Co., 505 F. Supp. 1313, 1356-62 (E.D. Pa. 1980), (expert used assumptions rather than evidence of costs); Brook Group, 113 S. Ct. at 2598.

(4) If the court finds Sears' other evidence legally insufficient, as we submit it should, outright reversal is required as a matter of law, since Sears cannot base liability on a claim it has no right even to assert. ARCO, 495 U.S. at 337-38; Anago, 792 F. Supp. at 519. However, even assuming Sears' other evidence were sufficient, a new trial still would be required because of the court's error in permitting the jury to consider Sears' disincentive thesis in evaluating the competitive effects of VISA's by-law. Since the jury returned the equivalent of a general verdict on the purported effect of By-law 2.06 it is impossible to disaggregate the jury's deliberations and determine what weight was given to Sears' various contentions. That being so, remand for a new trial is the very minimum that is required. Farrell v. Klein Tools, Inc., 866 F.2d 1294, 1298-99 (10th Cir. 1989) ("when one of two or more issues submitted to the jury was submitted erroneously, a general verdict cannot stand"); McMurray v. Deere & Co., 858 F.2d 1436, 1444 (10th Cir. 1988); Smith v. FMC Corp., 754 F.2d 873, 877 (10th Cir. 1985); see also Spectrum Sports, Inc. v. McQuillan, 113 S. Ct. 884, 892 (1993).

d. As a Matter of Law, the Benefits to Intersystem Competition from By-law 2.06 Outweigh Any Restraint on Intrasystem Competition.[77]

As noted in our earlier description of the credit card business (at pp. 8-12), competition takes place at two levels. On the one hand, there is competition between the numerous banks that compete with each other, and with Discover and American Express, to issue cards to consumers. At that level, the industry is structurally unconcentrated -- in the words of Sears' economic consultants, virtually "atomistic." App. 1437; see pp. 42-47, supra.

There is also competition at the system level. Thus, for example, VISA (or MasterCard), Discover and American Express compete on technologies, system functions, advertising, and product innovation.[78] See note 80, infra. The competitive structure at the system level is quite different from that at the issuer level. There are, at most, four or five competing card systems: VISA, MasterCard, Discover, American Express and, in

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[77] Standard of review: see pp. 20-21, supra.

[78] There is also competition to sign merchants -- competition inexplicably ignored by the district court in its post-trial order. That competition is analogous to card issuance in the sense that VISA (or MasterCard) members compete against each other (as well as against the proprietary cards), offering whatever merchant discount rates they choose. However, that competition also takes place at the intersystem level because the largest single merchant-side cost item for association members is the so-called "interchange fee," an internal, cost-based transfer fee which is established by the VISA (or MasterCard) system and is paid by the merchant-signing bank to the card-issuing bank to equalize the costs and risks involved in charge card transactions. See generally NaBanco, 596 F. Supp. 1231.

Competition for merchant business is extremely important since the credit card business necessarily involves both card usage and card acceptance. That competition centers around merchant discount rates. As attested by Sears' Phillip Purcell, "there is certainly competitive tension in the merchant discount field." App. 415-16. In fact, as one would expect, when Sears entered the market with Discover in 1986, it solicited merchants by offering discount rates below those generally prevailing for VISA and MasterCard. App. 413-15, 531. That competition continues and has an impact on the level of VISA interchange fees, just as VISA members' typically lower merchant discount rates constrain the higher rates charged by American Express. App. 1214. For example, in 1990, K-Mart threatened to encourage customers to use Discover, rather than VISA, because of an increase in VISA's interchange fee. App. 1378, 639-44. Similarly, a number of restaurants in Boston recently threatened to discontinue accepting American Express cards because of its high merchant discount rates. App. 415-16; see also Balto, supra note 12, at 271 ("[W]ith the admission of American Express and Dean Witter into VISA, competition for merchants through attractive merchant discounts may diminish.").

Sears' view, Diners Club. The HHI at the system level is a highly concentrated 3231. See Opn. 993 & n.43.[79]

As the court below concluded, intersystem competition is important and permitting Sears to become a VISA member while also issuing its Discover card is likely to harm such competition. Opn. 996-97. Given the comparative market structures at the two levels, the harm to competition at the system level necessarily outweighs any asserted benefit from allowing Sears to issue Prime Option as another brand of VISA card, rather than, e.g., as an additional brand of Discover.[80]

Sears did not dispute the importance of intersystem competition nor did it dispute VISA's evidence concerning it. Instead, it offered three other responses: First, it attempted to dismiss the evidence as a pretext. VISA and its members, argued Sears, are concerned with their own interests, not the health of intersystem competition. Second, Sears' witnesses testified that there is no need for concern about intersystem competition because Discover intends to compete as vigorously after it offers Prime Option as it has before. App. 408, 490, 508-09, 532, 590-91. The final answer was from Sears' expert, Dr. Kearl, who professed not to understand what the fuss was all about. We consider each in turn.

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79 Anything over 1800 is considered highly concentrated by the DOJ. At or above that level, virtually any increase in concentration is presumptively unlawful and will be challenged. Dep't of Justice & FTC Horizontal Merger Guidelines § 1.51(c), reprinted in 4 Trade Reg. Rep. (CCH) ¶ 13,104, at 20,573-6 (1992) ("Merger Guidelines"). In a market with few competitors, the exercise of market power is far more likely, as is the risk of collusion. See pp. 67-74, infra.

80 The evidence concerning such competition fully supported the court's conclusions. See, e.g., App. 415, 428-33, 481-83. For example, there was considerable evidence about competition in "terminals" (the devices that enable stores to get prompt transaction approval and also capture data for use in the clearing and collection process). App. 330-34, 383-85, 615-20. Similarly, evidence of the systems' widespread and aggressive advertising campaigns (samples of which were introduced and played for the jury), demonstrated the intensity of competition between VISA and its major proprietary competitors. App. 1502. There also was uncontradicted testimony that Discover's entry into the market led to a lowering of VISA's interchange fees (as well as corresponding testimony about the impact of VISA members' merchant discount rates on the generally higher discounts charged by American Express). App. 410-16, 639-44.

Sears initially attempted to deflect attention away from the evidence by arguing that VISA is not concerned about preserving Discover as an intersystem competitor. E.g., App. 308. But VISA does not assert that its motive for excluding Sears was some public-spirited interest in preserving intersystem competition.[81] Rather, VISA excluded Sears to avoid free-riding, an unlevel playing field, and the added costs that Sears would impose on VISA members by taking advantage of a brand and operating systems that it not only had done nothing to create but had chosen to compete against. App. 468-78, 631-35, 922-26, 1259-63, 1269-85, 1290-93. The idea that firms do not ordinarily rush to benefit their major competitors scarcely qualifies as novel -- or illicit.

But whatever VISA's private interests, the matter to be decided in this case is the effect of VISA's actions on competition. VISA was entitled to present evidence pertinent to the "public interest" in intersystem competition just as Sears was not only permitted, but required, to demonstrate "injury to competition," i.e., harm to consumers, not just injury to itself (although concern for the "public" was no more Sears' reason for seeking access to VISA's property than for VISA's refusal).

Sears' second response -- that Discover will continue to compete vigorously -- is no more persuasive. Since Prime Option does not actually exist, any discussion about its competitive effects, pro or con, necessarily falls within the realm of prediction, if not speculation. Therefore, one must, as Prof. Kearl urged (in a different context), consider "incentives" and invoke the predictive force of industrial organization theory. Tested in that crucible, the self-serving testimony of Dean Witter and Prime Option executives can scarcely be credited. United States v. E.I. du Pont de Nemours & Co., 353 U.S. 586, 607 (1957); FTC v. University Health, Inc., 938 F.2d 1206, 1223 (11th Cir. 1991); Mississippi River Corp. v. FTC, 454 F.2d 1083, 1089 (8th Cir. 1972). That is true not only as a

81 The closest to that argument VISA came is the testimony of its former General Counsel, Bennett Katz, who testified that he was concerned that if VISA admitted its interbrand competitors it might become subject to government regulation as a utility. The court credited that concern as legitimate. Opn. 984.

matter of "incentive" theory, but as a matter of evidence. One of Sears' principal witnesses was B.J. Martin, presently the head of Prime Option and formerly a high-ranking officer with Discover. Mr. Martin emphatically insisted that Sears' VISA and Discover programs would be entirely separate and that there would be no harm to competition if Sears became a VISA member. App. 577-85. However, in contrast to his assurances from the witness stand, Mr. Martin wrote a memo in 1988 in which he urged Sears to apply for membership in VISA so that Discover could "know everything" that was going on at VISA. App. 1346.

The testimony of Dean Witter's CEO, Philip Purcell, is even more telling. Mr. Purcell was the executive who approved Sears' 1988 application. After acknowledging that Sears did not even have a plan to issue VISA cards at that time (App. 387-89), he testified that his reason for seeking VISA membership was to limit the intense intersystem competition being waged by VISA against Discover:

> Q. And is your testimony here that by becoming a member of VISA you would have the opportunity to perhaps limit their exercise of these kinds of marketplace activities against Discover?
>
> A. What I believe I said was that by becoming a member of VISA it is much harder to discriminate against us with some of these kinds of activities and that would be preferable.

App. 388.[82]

These observations capture precisely why Sears should be kept out of VISA. If Discover were to become a VISA member, it would be far easier for Sears to coordinate its interbrand competitive strategies. For example, it is reasonable to expect Discover to compete less vigorously on merchant discounts. Until now, Discover has been an aggressive competitor on the merchant side of the business in order to increase its

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[82] Mr. Purcell acknowledged the same point in his deposition: "[I]t would be better to be in VISA where we would be, perhaps, better treated, better accepted and, at a minimum, would be aware of any anti-Discover moves made by VISA." (Purcell Dep., 3/27/92, at 174); see also id. at 175: "The urgent need was to put the company in a position where the market power of VISA and the use of that market power could perhaps be limited." (Emphasis added).

merchant base while simultaneously cutting into the margins of its competitors. App. 531; see also App. 414-16, 642-44. Discover's economic interests would be better served, however, if it could successfully raise its merchant discount rates. That benefit would double if Sears were also a VISA member since it expects to earn huge amounts of money from VISA interchange fees.[83] Lessening competitive pressure on VISA's interchange rates by raising Discover's merchant discounts, thus, would be of immense benefit to Sears.[84]

Obviously, it is not possible to predict precisely what other strategies Discover might elect to pursue. However, depending upon the relative success of its two programs, one can envision substantial resources being diverted from Discover to Prime Option. App. 484-90, 493, 588-89. At the extreme, it could become advantageous for Sears to convert its Discover program entirely (however much its current intentions may honestly be to the contrary). See 5 Treatise ¶ 1203c, at 319-20. Similarly, the plans of those who currently lead Dean Witter's credit card operations will not necessarily be the same as those who follow them. Two things remain clear, however: Economic actors will seek to act in a self-interested, profit-maximizing way, and the opportunity (and the incentives) for such actions to materially harm intersystem competition are far greater than any possible benefits from admitting Sears to VISA.[85]

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[83] According to Prime Option's financial model, it anticipates receiving VISA interchange fees of $651 million over 7 years. That represents 95% of its total anticipated after-tax profits from Prime Option. Huber Dep. at 156-60 and Dep. Exh. 5 at S1971022.

[84] See Balto, supra note 12, at 271 ("If Dean Witter becomes a VISA member and card issuer . . . it may have a significant incentive to keep merchant discounts up in order to protect the VISA interchange fees that will be available to it. Indeed . . . it could seek to induce increases in VISA's interchange fee by increasing Discover's merchant discount rate.").

[85] History in a related area bears out this concern. As recounted by David Balto of the FTC, the forced admission of BayBanks (then the largest proprietary ATM operation in the United States) to Yankee 24, a joint venture ATM network, led to an increase in consumer fees. See Balto, supra note 12, at 267-68. Similar events occurred in Texas. Id.; see also Baker, Financial Networks Avoid Antitrust Ills, The Nat'l L. J., Jun. 21,

(continued...)

Finally, Prof. Kearl's testimony on this point is simply mysterious. His overall conclusion was that he could find "no benefits" to excluding Sears from VISA. App. 754-56. Further, when queried about intersystem competition, he seemed to all but deny its existence: "Discover does not compete with VISA. It competes only with the VISA issuers." App. 845. That assertion, by itself, should disqualify Prof. Kearl's testimony from serious consideration. In any event, the facts reviewed above cannot be so easily discarded nor can his conclusory opinions sustain a verdict not supported by the record. Zenith Radio Corp., 505 F. Supp. at 1356-62; Reazin v. Blue Cross & Blue Shield, 663 F. Supp. 1360, 1480 (D. Kan. 1987), aff'd, 899 F.2d 951 (10th Cir.), cert. denied, 497 U.S. 1005 (1990); Merit Motors, 569 F.2d at 672; see also Thomas v. Hoffman-LaRoche, Inc., 949 F.2d 806, 816 (5th Cir.) (discussing Matsushita), cert. denied, 112 S. Ct. 2304 (1992).

What is more, as Prof. Schmalensee pointed out, the logic of Prof. Kearl's testimony compels the conclusion that By-law 2.06 is pro-, not anti-, competitive. See App. 999-1001. In advancing the theory that VISA possesses market power through its collective rule-making capacity, Prof. Kearl opined that the market shares of MasterCard and VISA members should be aggregated because of the ownership overlap between the two associations. App. 684. As we have explained previously, there is a logical fallacy in that assumption, at least as applied to By-law 2.06. See pp. 42-47, supra. However, at the system level, not only is aggregation appropriate (see pp. 68-71, infra), but the logic of Prof. Kearl's testimony is that admitting Sears to VISA will increase its market power and the antitrust concerns that go with it. In fact, if American Express promptly follows Sears into VISA, the relevant market share under Prof. Kearl's thesis would be 100%. Yet, as Prof. Schmalensee noted, the remedy for being too fat is not to eat more ice cream, and the remedy for too much market power is not to create more. App. 1003.

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[85](...continued)
1993, at 25. By contrast, in Canada, where duality between VISA and MasterCard has not been permitted, the "networks remain . . . very competitive." Id. at 26.

B. THE COURT ERRONEOUSLY CONCLUDED THAT SEARS' ACQUISITION OF A PARTIAL OWNERSHIP INTEREST IN VISA DOES NOT VIOLATE SECTION 7 OF THE CLAYTON ACT

VISA counterclaimed under Section 7 of the Clayton Act, 15 U.S.C. § 18, on the ground that the effect of Sears' proposed interest in VISA "may be substantially to lessen competition" in the general purpose charge card business.[86] In particular, VISA contends that the highly concentrated nature of system-level competition, the changed incentives resulting from Sears' acquisition and the "potential likelihood of collusion" make such an adverse effect highly likely. VISA therefore requested an injunction against the acquisition. App. 80.

Since the requested relief was entirely equitable, VISA's counterclaim was tried to the court while the jury heard Sears' Section 1 claim. The court rendered its decision on the claim as part of its opinion addressing VISA's post-trial motions under Rules 50 and 59. Opn. 990-98. In brief, the court found that "intersystem competition will be decreased by Sears' entry into the VISA system" and that, "to a certain degree" at least, the acquisition "will likely cause Sears to change its marketing strategy, thereby decreasing competition between VISA and Discover." Opn. 996. The court further "agree[d] with VISA" that the merger presented a "concern regarding confidential information, and will likely cause a decrease in intersystem competition." Id. By contrast, the court was "not convinced that [any short-run] increase in intrasystem competition will continue over the long run." Id. To the contrary, the court found that

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[86] As the court concluded (Opn. 992), there is no question that Section 7 applies here. By its terms, it covers partial acquisitions. 15 U.S.C. § 18 ("the whole or any part . . ."); see also American Crystal Sugar Co. v. Cuban-Am. Sugar Co., 152 F. Supp. 387, 395 (S.D.N.Y. 1957), aff'd, 259 F.2d 524 (2d Cir. 1958). The statute also applies whether or not the acquisition, itself, creates control, since "[a] company need not acquire control of another company in order to violate the Clayton Act." Denver & R.G.W.R.R. v. United States, 387 U.S. 485, 501 (1967); see also 5 Treatise ¶ 1203b, at 317. Equally clearly, Section 7's standards apply to the creation and operation of a joint venture. Penn-Olin, 378 U.S. at 170-71.

Sears would "have an incentive to maintain higher-than-average interest rates." Id. at 996-97.

Notwithstanding all of those views, the court rejected VISA's claim because VISA's market structure evidence was not persuasive since intrasystem competition is "vigorous" (id. at 994) and "Sears' joining VISA does not constitute a true merger." Id. at 997. Further, the court held that the harm to intersystem competition is not that "significant" because "Sears intends the Discover Card to remain strong." Id. Thus, while "the probable harms to competition . . . outweigh the benefits," they do not do so "substantially" enough to violate Section 7. Id.[87]

VISA respectfully disagrees with the court's analysis in three respects:

First, the court incorrectly analyzed the market for Section 7 purposes.

Second, the court failed to give appropriate consideration, under Section 7's incipiency standard, to changes in Sears' post-acquisition incentives.

Third, the court erred as a matter of law by balancing the potential harm to intersystem competition against potential benefits to intrasystem competition.[88]

1. Analysis of Market Structure Should Have Created a Presumption of Illegality.

Since merger analysis, by definition, is prospective, it has always depended to a larger-than-usual extent upon market structure. That is true, as well, because the relevant competitive concerns are primarily a function of market concentration. While structural data are not conclusive, they create a presumption about likely future

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[87] Sears argued that VISA lacks standing to challenge the proposed acquisition under Section 7. The court rejected that claim. Opn. 991-92. The court also rejected Sears' contention that in light of the jury's finding that VISA's by-law unreasonably restrains competition under Section 1 of the Sherman Act, the court was prohibited by the doctrine of issue preclusion from ruling in VISA's favor on its counterclaim. Id. at 998 n.52.

[88] The first and third issues are are reviewed de novo (see pp. 20-21, supra). The second is reviewed for clear error. Id.

consequences which must be rebutted by evidence indicating why the predictions that flow from structure are inapplicable in the particular case.[89]

VISA presented evidence showing that competition at the system level -- which the court agreed is "important" (Opn. 983) – is highly concentrated with, at most, five competitors and an extremely high HHI of 3231.[90] If Discover actually merged into VISA the result would be an increase of 500 points, to 3,732. Opn. 993 & n.44. Such an increase is considered presumptively anti-competitive under DOJ Guidelines. Merger Guidelines, supra note 79, § 1.51(c).

The court rejected this analysis for two reasons. First, the court said that it was not "appropriate to view the . . . market on a system-wide basis." Opn. 994. Rather, it noted that VISA had presented "persuasive evidence" of "vigorous" intrasystem competition in light of the fact that "members are free to set their own prices and output" and that "both systems generally remain open to new members." Thus: "Based on this evidence, the court agrees with VISA's expert Professor Schmalensee that each individual issuer of VISA and MasterCard cards should be included in the HHI analysis, resulting in a system HHI of below 500." Id. Second, even if the market were viewed system-wide, VISA's analysis was inapposite because there is no "true merger between Discover and VISA." Id.

The court's conclusions regarding intrasystem competition are completely correct. As we have explained previously, the reason that VISA's "persuasive" analysis applies to Sears' claim is because Sears is complaining about its exclusion as a VISA issuer. See pp. 45-47, supra. That is where the alleged effect operates and that is, accordingly, the appropriate place to look at the market. By contrast, VISA's

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[89] The court's discussion of market structure uses the term "prima facie" case. Opn. 994. We assume that that was intended as a reference to the standard "presumption" effect flowing from market share and other related data.

[90] For example, a market consisting of only four firms in which the top two firms, respectively, controlled 40% and 25% of total sales would have a lower HHI.

counterclaim focuses on <u>system</u> structure because the relevant concern for Section 7 purposes is diminution in those forms of competition that necessarily occur at the system level. There is, thus, no inconsistency at all in VISA's separate views of the market and the court's chiding suggestion to the contrary (<u>Opn</u>. 993) is both incorrect and unfair.[91] In fact, the court got the matter backward. It permitted the jury to rely on system-level percentages to show power at the issuer level (with regard to Sears' Section 1 claim) while using issuer-level percentages to eliminate concern at the system level under Section 7.

The court's second observation begins with an accurate premise but ignores other critical facts. Thus, it is true that VISA and Discover are not planning to merge. Sears is only seeking the right to become one of VISA's issuers while still operating Discover (about which more in a moment) -- in short, a partial integration. While that distinction is relevant, it does not bear the dispositive weight attributed to it by the court.

Partial acquisitions are subject to Clayton Act scrutiny because they present many of the same threats to competition in a concentrated market as a complete merger. H. Hovenkamp, <u>supra</u> note 46, § 11.9, at 317; <u>see</u> <u>also</u> <u>Denver & R.G.W.R.R.</u>, 387 U.S. at 501; 5 <u>Treatise</u> ¶ 1203d, at 320-22. These concerns relate both to the likelihood of future collusion and to the altered competitive incentives that would exist in the newly configured market. One of the principal concerns with partial mergers is the potential

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91 Competition at the system level is the correct focus for the additional reason that market power at the system level is not capable of being dissipated by competition at the member level. A couple of examples may illustrate why. Assume that the effect of Sears' action was to eliminate or reduce system-level competition, whether through express collusion, the sharing of confidential information or a reduction in competitive incentives. No amount of member level competition would eliminate those adverse competitive effects. Similarly, any effect on merchant discount (or, in the case of VISA, interchange fee) rates occurs at the system level and is largely impervious to being competed away through member-level price competition.

The point was further illustrated by the testimony of VISA's former General Counsel, Bennett Katz. He noted that if there were a thousand automobile dealers but only one automobile manufacturer, one would expect to have a great deal of price and other competition at the dealer level but there would be few incentives for product improvement by the manufacturer. <u>See</u> <u>App</u>. 453-55.

for diminished competition when competitors work together. While such coordination is tolerated when it is ancillary to an efficiency-creating joint venture, elimination of competition between competitors (here, VISA and Discover) enjoys no such approbation. Among the ways in which such competition may be threatened is through the presence of a competitor on a rival's board (see, e.g., F&M Schaefer Corp. v. C. Schmidt & Sons, Inc., 597 F.2d 814, 818 (2d Cir. 1979); Hamilton Watch Co. v. Benrus Watch Co., 114 F. Supp. 307, 314 (D. Conn.), aff'd, 206 F.2d 738 (2d Cir. 1953)), or through the exchange of confidential information. 5 Treatise ¶ 1203c, at 319. Both of those concerns exist here. See App. 435-37, 636-38; see, e.g., App. 1590 (showing that each of the Top 10 VISA/MasterCard issuers enjoys Board representation); see also App. 1346 (B.J. Martin's Oct. 25, 1988 Memo urging Greenwood Trust to apply for VISA membership so that Discover could be "in a position of knowing everything that takes place at VISA").

Structure bears as directly upon the incipient likelihood of these events coming to pass in this case as it does in the case of a "true" merger. What is more, the extent of the potential effect is captured precisely by the HHI increase resulting from the partial merger since the effect of any coordination of competitive strategies will be felt throughout the partially merged firms. Thus, the court's suggestion that because Discover will remain in the market "the HHI would remain unchanged" (Opn. 994) misses the mark.

2. The Court's Analysis of Likely Competitive Effects Did Not Adequately Take Account of Sears' Changed Incentives.

The court's analysis of the likely competitive effects of a partial integration between Sears and VISA also was misdirected. The court purported to credit VISA's position but found its concerns insufficiently "substantial". Opn. 997.

To begin, the standard of evaluation under the Clayton Act is stricter than under Section 1 of the Sherman Act. See Rothery, 792 F.2d at 220; FTC v. Warner Communications Inc., 742 F.2d 1156, 1160 (9th Cir. 1984). That is true, specifically,

because Section 7 is intended to arrest "incipient threats to competition." Penn-Olin, 378 U.S. at 170-71; United States v. El Paso Natural Gas Co., 376 U.S. 651, 658-59 (1964). Indeed, the goal of the law is to prevent situations in which future competition may be adversely affected, regardless of any existing harm. Penn-Olin, 376 U.S. at 171; Brown Shoe Co. v. United States, 370 U.S. 294, 323 (1962).

In implementing this standard, it is critical to consider the predictive force of economic incentives. While the court notes that Sears will be "likely . . . to change [its] marketing strategy" (Opn. 996), its opinion ignores the more important ways in which Sears' competitive incentives would be altered if it were both a VISA member and issued Discover. See 5 Treatise ¶ 1203c, at 320 (in the case of a partial acquisition "the acquiring firm's market decisions might now be affected not only by their impact on its operations but also by their impact on its investment . . . in its competitor"). Indeed, in extreme circumstances "competition at the borderline of profitability may be abandoned" entirely. Id. Thus, for example, Prof. Areeda notes that partial acquisitions "may form the basis of willing cooperation between two companies" by, among other things, making "tacit understandings more attractive to the parties." Id. at 319-20. He adds that partial cross-ownership creates the potential for psychological disincentives to vigorous competition (id.) as well as obvious economic incentives to "direct . . . competitive energies away from the acquiring firm." Id. at 320.

These concerns arise here in a number of different ways and for a number of different reasons. Much of the relevant evidence has been reviewed previously in our discussion of intersystem competition under Section 1. See pp. 61-66, supra. Two points, however, bear mention. First, the incentives for collusion in innovation will be increased materially if Sears becomes a VISA member. In fact, collusion aside, the incentives for Sears to lessen the vigor of its competition would be significant. (In that regard, recall Mr. Purcell's testimony that the reason for seeking VISA membership in 1988 was to mitigate the vigor of VISA's competition against Discover.)

The incentive for Sears to raise its merchant discount rates is even more important because it would now be receiving VISA interchange fees as well. See supra pp. 64-65. Sears not only would want to avoid any adverse impact on that revenue stream but could benefit itself further by raising Discover's discount rates.

Sears responded by protesting the purity of its intentions, and the court credited those protestations. Opn. 996. That, too, was error. du Pont, 353 U.S. at 607 (honest intentions of high-level executives cannot defeat showing of likely anticompetitive effects); University Health, 938 F.2d at 1223 ("self-serving" assertions do not overcome a presumption of illegality); Mississippi River Corp., 454 F.2d at 1089 ("Honest intentions, business purposes and economic benefits are not a defense to violations of antimerger law."). The law presumes (Matsushita) that economic actors will behave in a rational, profit-maximizing manner. They are presumed to act -- now and in the future -- in whatever fashion will maximize their welfare. Thus, it is perfectly reasonable for Sears to assert that it will not abandon its substantial investment in Discover -- and VISA does not suggest otherwise.[92] But it also must be assumed that Sears will seek to maximize the overall return from its card operations and will allocate resources (human and otherwise) and adopt competitive strategies rationally directed to that end. For the reasons explained above, pursuit of such strategies is likely to harm system-level competition.

3. The Court Erred by Balancing the Acknowledged Harms to Intersystem Competition Against Potential Benefits to Intrasystem Competition.

In evaluating VISA's Section 7 claims the court balanced the likely harm to system competition against the potential benefits to intrasystem competition. Opn. 997. However, such balancing is not permitted under Section 7. Ford Motor Co. v. United

[92] Contrary to the court's suggestion (Opn. 995), VISA's argument does not assume that Discover will cease to exist -- although that could happen at some future time, depending on competitive developments that cannot now be foreseen. Rather, VISA's assumption is that Discover will continue to compete, but will have incentives to do so differently.

States, 405 U.S. 562, 570 (1972); United States v. Amax, Inc., 402 F. Supp. 956, 967 n.40 (D. Conn. 1975).

In one of the Supreme Court's most important merger decisions, Philadelphia National Bank,[93] the district court balanced potential harms and benefits to competition in different markets. Having done so, it concluded that the merger did not violate Section 7. On direct appeal the Supreme Court reversed and struck down the merger as a matter of law. In so doing, the Court held that Section 7 of the Clayton Act does not permit a court to use alleged benefits in one market to offset harms to competition elsewhere. Id. at 370-71. That holding remains the law. Ford, 405 U.S. at 570-71; RSR Corp. v. FTC, 602 F.2d 1317, 1325 (9th Cir. 1979), cert. denied, 445 U.S. 927 (1980); Mississippi River Corp., 454 F.2d at 1089. Thus, here, it was inappropriate for the district court to offset harm to competition at the system level by any supposed benefits at the issuer level.

VII. CONCLUSION

For the foregoing reasons, the decision of the district court should be reversed. Sears' claim under Section 1 of the Sherman Act should be dismissed and an injunction should be entered under Section 7 of the Clayton Act enjoining Sears' proposed acquisition of any interest in VISA.

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93 United States v. Philadelphia Nat'l Bank, 374 U.S. 321 (1963).

Because this case raises significant issues of antitrust law and policy that substantially affect competition in the general purpose charge card market and the creation of productive joint ventures, ORAL ARGUMENT IS REQUESTED.

Dated: August 31, 1993

Respectfully submitted,

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PROOF OF SERVICE

I, Gretchen A. Wilson, declare as follows:

I am employed in the City and County of San Francisco; I am over the age of eighteen years and not a party to this action. My business address is 333 Bush Street, San Francisco, CA 94104.

On August 31, 1993, I caused a true copy of OPENING BRIEF OF APPELLANT VISA U.S.A. INC. to be transmitted by facsimile electronic equipment and delivered by Federal Express to the following:

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I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Executed at San Francisco, California this 31st day of August, 1993.

Gretchen A. Wilson