UK Supreme Court Eases Burden on Antitrust Defendants Pleading a Pass-On Mitigation Defence

06 / 30 / 20

If you have any questions regarding the matters discussed in this memorandum, please contact the following attorneys or call your regular Skadden contact.

Bill Batchelor
Partner / Brussels
32.2.639.0312
bill.batchelor@skadden.com

Bruce Macaulay
Partner / London
44.20.7519.7274
bruce.macaulay@skadden.com

Sym Hunt
Associate / London
44.20.7519.7284
sym.hunt@skadden.com

One Manhattan West
New York, NY 10001
212.735.3000

40 Bank St., Canary Wharf
London, E14 5DS, UK
44.20.7519.7000

Defendants in competition damages actions often argue that claimants mitigated any loss in competition damages claims by passing on any allegedly unlawful price increase to their customers. In *Sainsbury's v. Mastercard* [2020] UKSC 24, the U.K. Supreme Court (UKSC) made it easier for alleged cartelists to prove a mitigation defence in such claims. The UKSC clarified that the extent of mitigation, which may be impossible to determine accurately, need not be proven as a precise amount. Rather than applying standard English damages principles, the court ruled that the claimant's mitigation may be assessed with a "broad axe" — that is, by estimation rather than precise calculation.

The UKSC's eagerly anticipated ruling, which is the latest in the saga of proceedings between retailers and Mastercard/Visa regarding the alleged overcharging of interbank fees, was handed down on 17 June 2020. The core issues of appeal before the UKSC were: (i) whether the English courts are bound by the *Mastercard* ruling of the Court of Justice of the European Union (CJEU) that the multilateral interchange fees (MIFs) restricted competition, contrary to Article 101(1) of the Treaty on the Functioning of the European Union (TFEU); (ii) the standard of proof faced by defendants arguing that an anti-competitive agreement is justified by its economic benefits (per Article 101(3), TFEU); (iii) whether the Article 101(3) exemption required Visa to prove that the benefits provided to the merchants alone (as opposed to benefits enjoyed by cardholders) as a result of the MIFs outweighed the costs arising therefrom; and (iv) the broad axe issue: whether a defendant seeking a reduction of damages payable because of the claimant's mitigation of its loss must prove the exact amount of the mitigated loss. This article focuses on the broad axe issue.

Background

In December 2007, the European Commission (EC) found that Mastercard had violated European Union (EU) competition law by setting default interchange fees (multilateral interchange fees or MIFs) whenever consumers paid using their Mastercard in the European Economic Area. Mastercard's appeals against the EC Decision to the European courts were unsuccessful.[1] In December 2010 and February 2014, Visa committed to the EC that it would reduce its maximum weighted average MIF and require greater transparency within its MIF arrangements. Mastercard and Visa (the Payment Scheme Operators) have since been the subject of a series of damages actions brought by merchants (*i.e.*, retailers) and consumers relating to their MIF schemes.

The MIF arrangements operate broadly as follows. When a card transaction is processed, the merchant pays a fee (the merchant service charge or MSC) to its bank (the acquiring bank). The MSC is affected by (i) the acquiring bank's own fee and operational costs; and (ii) an interchange fee the acquiring bank paid to the bank that issued the card, for processing the transaction. The interchange fee may be set bilaterally or multilaterally (*i.e.*, an MIF). The retailers in *Sainsbury's* argued that the MIFs were anti-competitive and that they accordingly paid inflated MSCs. The retailers' claims were for recovery of that alleged overcharge from the Payment Scheme Operators.

A Broad Axe?

It is well established, generally in the English law of torts and specifically in the context of competition damages actions, that damages must be compensatory; a claimant can only recover the loss that they suffered. Therefore, to the extent that a claimant (C1) mitigated its loss by passing on an overcharge to a supplier or a customer (C2),

[1] See our 8 May 2019 client alert, "*Merricks v Mastercard*: UK Class Actions Back Under the Spotlight".

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C1 has not suffered a loss and C1's damages should be curtailed accordingly. In such circumstances, C2 may sue the infringer of competition law, arguing that C1 passed on the overcharge. The defendant, in each instance, may wish to argue that the claimant's loss was reduced or eliminated by virtue of the overcharge being passed on (in the instance of C1), or not passed on to the claimant (in the instance of C2). As such, in a given claim, either a claimant or a defendant may wish to argue that there was (or was not) pass-on of an overcharge.

In the ruling, one of the issues before the UKSC was, from the defendant's perspective, "the degree of precision that is required in the quantification of mitigation of loss". In other words: Can the defendant rely on a broad axe in establishing the extent to which an overcharge was passed on?

The broad axe principle has been applied for over a century in the context of calculating a claimant's loss: A claimant should not suffer because of the difficulty in calculating its precise loss – reparation can be achieved "by the exercise of a sound imagination and the practice of the broad axe" (per Lord Shaw in *Watson, Laidlaw, & Co. Ltd. v. Pott, Cassels & Williamson*). In *Sainsbury's v. Mastercard*, the Court of Appeal of England and Wales had found that there is "no scope" for applying the broad axe principle where a defendant argues that the claimant's loss has been mitigated by virtue of pass-on. The Court of Appeal considered that the "fact and amount" of any pass-on must be established, with reference to "empirical fact and economic opinion evidence".

The Ruling

In relation to the substantive grounds of appeal, the UKSC found against the Payment Scheme Operators. The CJEU's *Mastercard* decision was binding, such that it could not be contested that the MIFs restricted competition. Cogent empirical evidence is required in order to evaluate the argued efficiencies and benefits of a restrictive agreement. The benefits cardholders enjoyed could not be taken into account in assessing whether impact of the MIFs on merchants was justified for the purposes of Article 101(3).

In relation to the issue of quantification of the claimed overcharge pass-on, the UKSC found that quantification can be estimated, rather than needing to be proven precisely. The UKSC held that English law does not require a greater degree of precision in quantification from a defendant than it does from a claimant.

The UKSC found that:

- Competition damages actions are claims for breach of statutory duty, for which damages must be compensatory (*i.e.*, be calculated as the sum of money that will put the wronged party in the same position they would have been had the wrong never occurred). A claimant must not be overcompensated or undercompensated, meaning that the damages award must take account of any pass-on.
- A party subject to an overcharge may respond in four principal ways: (i) do nothing and suffer a reduction of profits; (ii) reduce discretionary (*e.g.*, marketing) expenditure; (iii) reduce its costs by renegotiating with suppliers; and/or (iv) increase the prices it charges its customers. Options (i) and (ii) do not involve any obvious pass-on; options (iii) and (iv) result in pass-on because other parties (suppliers, and customers, respectively) bear some of the brunt of the overcharge. If the court were to conclude that a claimant had deployed options (iii) or (iv), then its recoverable loss would be less than the total overcharge.
- It is open to defendants to plead and prove that the claimant's loss has been mitigated. Once the defendants have raised the issue of mitigation, there is a "heavy evidential burden" on the claimant to "provide evidence as to how they have dealt with the recovery of their costs in their business". This is a question of fact.
- The EC's Guidelines for national courts on how to estimate the share of overcharge that was passed on to the indirect purchaser (2019 Guidelines) recognise that pass-on may be "invoked by an infringer as a shield against a claim for damages and by an indirect purchaser as a sword to support the argument that it has suffered harm" (according to the UKSC). As set out above: C1 may use pass-on as a shield against a defendant; C2 may use pass-on as a sword against the same defendant for the same infringement. The UKSC saw "no reason in principle" why the standard of precision of quantification should differ depending on whether it is a defendant or a claimant who is pleading that there was pass-on.
- Article 12.5 of Directive 2014/104/EU (the Damages Directive) provides that national courts must be empowered to estimate the share of any pass-on. The 2019 Guidelines provide that national courts "cannot reject submissions on passing-on merely because a party is unable to precisely quantify the passing-on effects" and should "strive for an approximation of the amount or share of passing-on which is plausible"; and cite Lord Shaw's "broad axe" metaphor with approval. There is, therefore, ample guidance at the EU level that the extent of a pass-on may be estimated regardless of which party is raising the argument.

Takeaway

The UKSC's finding on the broad axe issue may be unsurprising. The use of a broad axe in damages calculations is a long-standing principle and is supported by the Damages Directive and

the 2019 Guidance. The ruling should reassure defendants in competition damages actions that the court will take a pragmatic approach to assessing pass-on. This appears sensible, given that, as the UKSC noted, claimants in competition damages actions are often "sophisticated" and would consider an overcharge "along with a multiplicity of other costs when developing their annual budgets". As such, the quantification of pass-on may "only be a matter of estimation".

The ruling helpfully recognises that a defendant will be in a highly disadvantageous position when trying to prove pass-on. The evidence will all be in the hands of the claimant, and tracking the surcharged price through the claimant's organisation to its customers (or perhaps to suppliers) may be highly complex forensic task. Precision will almost never be achievable. The UKSC recognised that "[m]ost of the relevant information [...] will be exclusively in the hands of the merchant itself". Therefore, it is important for the defendant to ensure that mitigation (by virtue of pass-on) has been raised, so as to place the "heavy evidential burden" on the claimant and require the disclosure of relevant evidence.

The UKSC also reconciles "the need to avoid double recovery through claims in respect of the same overcharge by a direct purchaser and by subsequent purchasers in a chain". A defendant should not be exposed to paying both direct and indirect purchasers for the same harm if an overexacting quantification standard forecloses its mitigation defence to direct purchasers while indirect purchasers need only claim passed-on overcharges to a lower standard of broad axe quantification. Mastercard is currently the subject of a proposed class action brought by consumers in respect of the MIFs that were allegedly passed on by the retailers. (See Skadden's coverage of the Court of Appeal's judgment in *Merricks*; the UKSC heard the appeal against this judgment in May 2020.)

The 2019 Guidelines encouraged proactive measures to ensure consistency between damages actions related to the same competition law infringement. The UKSC's ruling in *Sainsbury's* may further this goal by ensuring that defendants are on an equal footing with claimants when arguing pass-on. It remains to be seen how the UKSC will take account of indirect purchaser harm quantification at the group certification stage in *Merricks*.