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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

DISCOVER FINANCIAL SERVICES, DFS SERVICES, LLC, AND DISCOVER BANK,	:	Case No. 04-CV-07844 (BSJ) (DFE)
Plaintiffs,	:	ECF CASE
v.	:	
VISA U.S.A. INC., et al.,	:	
Defendants.	:	

MASTERCARD INCORPORATED'S AND MASTERCARD INTERNATIONAL INCORPORATED'S MEMORANDUM IN OPPOSITION TO DISCOVER'S MOTION FOR PARTIAL SUMMARY JUDGMENT

CONTAINS CONFIDENTIAL AND HIGHLY CONFIDENTIAL INFORMATION
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SUBJECT TO PROTECTIVE ORDER

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CITATION FORM

The evidence cited in MasterCard's memorandum in opposition to Discover's motion for partial summary judgment is set forth in the Declaration of Joseph F. Tringali, dated March 24, 2008, and compiled in the accompanying appendix. The evidence relied on in this memorandum and MasterCard's Response to Discover's Local Rule 56.1 statement will be cited as set forth in the chart below:

[illegible]	Citation Form
Deposition Transcripts	MC Opp. Ex. [exhibit number] (Witness name date Tr.) [page number]
Discover Financial Services et al. v. Visa U.S.A. et al., No. 04-CV-07844 Hearing Transcripts	MC Opp. Ex. [exhibit number] (Hearing [date] Tr.) [page number]
United States v. Visa U.S.A. Inc., No. 98 Civ. 7076 Trial Transcript	MC Opp. Ex. [exhibit number] ([witness name] [date] DOJ Trial Tr.) [page number]
SCFC ILC, Inc. v. Visa U.S.A. Inc., No. 91 Civ. 00475 Trial Transcript	MC Ex. [exhibit number] ([witness name] [date] *MountainWest* Trial Tr.) [page number]
Expert Reports	MC Opp. Ex. [exhibit number] (Expert Name Report) at [page or paragraph number]
Documents	MC Opp. Ex. [exhibit number] at [bates pin cite or page number]
Discover Motion for Partial Summary Judgment	Discover Br. [page number]
MasterCard's Motion for Summary Judgment	MC S.J. Br. [page number]

Unless otherwise stated, italics in quotations are used to add emphasis.

Pursuant to Federal Rule of Civil Procedure 56(c), Defendants MasterCard Incorporated and MasterCard International Incorporated (collectively, "MasterCard") respectfully submit this memorandum in opposition to the motion for partial summary judgment of Plaintiffs Discover Financial Services, DFS Services, LLC and Discover Bank (collectively, "Discover").

PRELIMINARY STATEMENT

Shortly after filing this action seeking billions of dollars from MasterCard, Discover urged this Court to collaterally estop MasterCard and Visa from litigating issues of liability by adopting its findings from its 2001 decision in *United States v. Visa U.S.A. Inc.*, 163 F. Supp. 2d 322 (S.D.N.Y. 2001). According to Discover, this was simply a case about damages. This Court rejected Discover's argument then, recognizing that Discover's private action "isn't the same litigation" as the Department of Justice's ("DOJ") equitable action and that collateral estoppel cannot be decided in a "vacuum." MC Opp. Ex. 1 (Hearing 11/16/04 Tr.) 12-13. The Court should reject Discover's argument again. During the last two years, the parties have engaged in extensive fact and expert discovery, with scores of witnesses being deposed, including nearly sixty Discover witnesses, and over 100 million pages of documents being produced. Discover would urge the Court to ignore that time and effort on the part of all the parties in moving for summary judgment based on collateral estoppel on its First Claim For Relief ("Claim One"), and to estop MasterCard and Visa from litigating eighty-one specific statements from this Court's seven-year-old opinion. Discover's motion should be denied for a myriad of reasons.

First, Discover's present action seeking monetary damages for a private party lacks the requisite identity of issues with the government's enforcement action (the "DOJ

Action"), which sought only equitable relief. As just one example, Discover's theory of injury here is vastly different from the competitive injury at issue in the DOJ Action. There, unlike here, the sole focus was on whether *consumers* were harmed by the alleged impact of MasterCard's Competitive Programs Policy ("CPP") and Visa's By-law 2.10(e) on Discover's and American Express's ability to partner with bank issuers. Discover now, however, advances a *new* theory of injury that depends in substantial part upon the CPP's and By-law 2.10(e)'s effect on Discover's ability to partner with third party *acquirers*—an issue that was neither challenged by the DOJ nor otherwise adjudicated in the DOJ Action, as the Court expressly noted. In addition, significant issues of causation and the impact, *if* any, of the CPP itself (not in conjunction with By-law 2.10(e)) on Discover's business were not litigated previously and are central to MasterCard's liability in this case.

Second, key issues of liability upon which Discover now seeks estoppel—including both injury-in-fact to Discover and the causation of any such injury, both of which are requisite elements of Discover's claims but not of the government's enforcement action—were not necessarily decided in the DOJ Action and therefore estoppel on those issues is unwarranted as a matter of law.

Third, contrary to Discover's assertion that applying collateral estoppel will "streamline" these proceedings (Discover Br. 41), the substantial overlap between damages issues—which indisputably must be litigated here in their entirety—and liability issues virtually assures that any efficiencies would be *de minimis* at best. In addition, there is significant overlap between Discover's many newly-asserted claims—such as monopolization, debit-related, and inter-association conspiracy claims, all of which must be litigated fully—and the issues upon which Discover seeks estoppel. This overlap further guarantees, as this Court has previously

observed, that collateral estoppel will not serve judicial economy. MC Opp. Ex. 2 (Hearing 4/14/05 Tr.) 3 ("I find that applying collateral estoppel would not promote efficiency. . . . [T]here are a number of additional claims and legal theories in this case that were not before me in the DOJ action. Including the plaintiffs' claims relating to monopolies and the debit card market.").

Fourth, applying collateral estoppel here would be fundamentally unfair to MasterCard and Visa. While this Court made its findings in the DOJ Action based on forecasts as to what the world would look like without By-law 2.10(e) and the CPP, discovery in this case has uncovered previously unavailable evidence that counters many of this Court's findings on issues of consumer welfare, product innovation, and procompetitive justifications. Moreover, economic scholarship developed since the DOJ Action reflects that the analysis of market power and market definition advanced by the government and relied upon by this Court runs counter to market realities today. Indeed, Michael Katz, the DOJ's economist upon whose testimony this Court relied in the DOJ Action, has recently testified that there may be no market power in a two-sided platform—such as a payment card network—even if prices are rising on one side of the platform, because that could simply be evidence of competition. MasterCard, accordingly, should be able to present its market power defense in the currently-accepted economic framework. Finally, because issues remain to be litigated that implicate much of the same evidence as those issues for which Discover seeks estoppel, the potential for juror confusion and distortion of the record is high.

Two years of intense discovery, as well as Discover's own expert reports, has filled in the "vacuum" that the Court wanted addressed before making any final decision as to the applicability of collateral estoppel. As a result, it is now abundantly clear that Discover's case is

markedly different from the DOJ Action and that no judicial economies would be served by applying collateral estoppel. Discover should not be permitted to transform the equitable tool of collateral estoppel—the primary purpose of which is to maximize efficiency and judicial economy—into a weapon to bar MasterCard and Visa from presenting evidence that directly contradicts Discover's flawed theories of liability and damages. A doctrine based on equity should not be employed to achieve such an unjust result. Accordingly, this Court should deny Discover's motion in its entirety.

STATEMENT OF FACTS

A. The DOJ Action

In 1998, the DOJ brought an enforcement action for equitable relief alleging that Visa and MasterCard each independently violated Section 1 of the Sherman Act (1) through "governance duality," which allowed members of each network to sit on the board of directors of one network while issuing cards on the other, and (2) by respectively adopting By-law 2.10(e) and the CPP, which allegedly prohibited their respective members from issuing cards on the American Express and Discover networks. *See Visa U.S.A.*, 163 F. Supp. at 327.

The DOJ alleged that Visa and MasterCard jointly and separately had market power in an alleged general purpose card network market, and that they exercised that power to restrain competition in that market, as well as in an alleged market for general purpose credit and charge cards. *See* MC Opp. Ex. 3 at 8-41. The DOJ did not allege, however, that Visa and MasterCard conspired with each other in enacting By-law 2.10(e) and the CPP, which were adopted five years apart—in 1991 and 1996, respectively. Rather, the DOJ alleged that MasterCard and Visa, each separately with its respective "governing banks," restrained

competition through the adoption of By-law 2.10(e) and CPP. *See* MC Opp. Ex. 4 at ¶ 159 ("Each of the defendants, on behalf of and in collaboration with its *governing banks*, has engaged in a continuing combination and conspiracy . . . ."). In addition, the DOJ did not allege that Visa and MasterCard had restrained competition in any purported debit-related markets or that either Visa or MasterCard had violated Section 2 of the Sherman Act.

Following a trial in the summer of 2000, this Court held governance duality of Visa and MasterCard did not cause harm to competition in the credit and charge card industry. *Visa U.S.A.*, 163 F. Supp. 2d at 328. However, the Court held that By-law 2.10(e) and the CPP unlawfully restrained trade. *Id.* at 406-09. The Court found that bank issuance of American Express and Discover cards could benefit consumers by increasing product variety and consumer choice, recognizing that such cards would combine the "unique" features of bank issuers with those offered by the American Express and Discover networks. *Id.* at 329. A vast majority of this Court's opinion pertaining specifically to Discover was predicated on statements made by Discover executives themselves. *Id.* at 386-89, 393-94, 396. Indeed, the sole evidence cited by this Court that banks would have been interested in issuing Discover cards is the testimony of Discover's CEO David Nelms regarding what executives at First USA purportedly said. *Id.* at 386-87. In addition, because Discover had not partnered with any banks to issue Discover cards at the time of the DOJ Action, this Court had to predict what the impact on competition would be from bank issuance of Discover cards. To that end, this Court had to rely on representations from Discover executives regarding the network features Discover would make available to potential bank partners. *Id.* at 395-96 (citing MC Opp. Ex. 5 (Nelms 7/7/00 DOJ Trial Tr.) 3011).

The Court stayed its judgment pending appeal. *United States v. Visa U.S.A. Inc.*, No. 98 CIV 7076 (BSJ), 2002 WL 638537 (S.D.N.Y. Feb. 7, 2002). The Second Circuit affirmed this Court's decision on September 17, 2003, *see United States v. Visa U.S.A. Inc.*, 344 F.3d 229, 244 (2d Cir. 2003), and the Supreme Court denied the defendants' petition for *certiorari* on October 4, 2004. Visa and MasterCard respectively repealed By-law 2.10(e) and the CPP pursuant to this Court's remedy.

B. Discover's Involvement In The DOJ Action

Although Discover was not a party to the DOJ Action, it was active in the litigation, and even moved to intervene in the proceedings because Discover contended that the remedy that the DOJ was seeking in its enforcement action—the end of governance duality and the elimination of By-law 2.10(e) and the CPP—would likely make Discover worse off than it was. MC Opp. Ex. 6 at 8. The testimony of Discover's executives, as well as its court submissions, reveals that Discover was concerned that the elimination of By-law 2.10(e) and the CPP, without more, would hurt, not help, Discover. *See, e.g.*, MC Opp. Ex. 5 (Nelms 7/7/00 DOJ Trial Tr.) 3047, 3073 (Discover's CEO testifying that the elimination of By-law 2.10(e) and the CPP alone could hurt Discover); MC Opp. Ex. 6 at 8, 15-20 (Discover Motion to Intervene; arguing that elimination of By-law 2.10(e) and the CPP, while continuing to allow the enforcement of other rules, would likely harm competition and make Discover worse off); MC Opp. Ex. 7 at 21, 53 (Discover Amicus Brief On Remedy; highlighting negative effects Discover would suffer if only By-law 2.10(e) and the CPP were eliminated, explaining that such a remedy would leave Discover "hampered in its ability to attract third party issuing banks" and "severely compromised in its ability to build transaction volume and merchant acceptance"). Indeed, Discover admitted in its motion to intervene that if the CPP and By-law 2.10(e) were eliminated,

"the low-priced Discover network would continue to be hampered in its ability to grow and, indeed, would become the only card network in the market that could not realistically attract third-party issuers." MC Opp. Ex. 6 at 9. Moreover, during his deposition in the DOJ Action, Phillip Purcell, the CEO of Discover's then-parent company Morgan Stanley, was questioned regarding the DOJ's proposed remedy:

> Q. So the ability of Visa and MasterCard financial institutions to issue Discover Cards, that's the only remedy?
>
> A. That's irrelevant. That alone will not make us economically viable or allow us to get the kind of market share and economics that we need to make the network viable.

MC Opp. Ex. 8 (Purcell 1/14/00 Tr.) 109-10.

C. Discover's Private Action

On October 4, 2004, the same day the Supreme Court denied defendants' petition for *certiorari* in the DOJ Action, Discover commenced this private action seeking damages. Discover's Second Amended Complaint, which Discover purports to be premised on the DOJ Action, asserts various claims against MasterCard and Visa. Specifically, Discover's First Claim For Relief asserts that MasterCard and Visa, "on behalf of and in collaboration with their banks," conspired to restrain trade in violation of Section 1 of the Sherman Act in an alleged general purpose card network services market through the enforcement of By-law 2.10(e) and the CPP, and that Discover was injured as a result. MC Opp. Ex. 9 at ¶¶ 93-99. While not apparent from the complaint, Discover claims in its present motion that its First Claim For Relief alleges two separate intra-association conspiracies between MasterCard and its members and Visa and its members. *See* Discover Br. 43. Unlike the DOJ's enforcement action, however, Discover does

not limit its alleged conspiracies to the networks' "governing banks," but rather appears to allege parallel conspiracies between each network and its entire membership.

Discover's Second Claim For Relief alleges a conspiracy between the defendants and their banks to restrain trade in the alleged "relevant markets," in violation of Section 1, resulting in harm to Discover. MC Opp. Ex. 9 at ¶¶ 100-05. The complaint here alleges three relevant markets: (1) a general purpose card network services market; (2) a general purpose credit card market; and (3) a general purpose debit card market, *Id.* at ¶¶ 75-90; and Discover's liability and damages expert Jerry Hausman asserts a fourth relevant market—a general purpose debit card network services market. MC Opp. Ex. 10 (Hausman Report) at ¶¶ 60-64.[1]

Discover's remaining claims assert violations of Section 2 of the Sherman Act. Specifically, the Third and Fourth Claims For Relief allege that Visa monopolized and attempted to monopolize the relevant markets, and the Fifth Claim alleges a conspiracy to monopolize the relevant markets between Visa and MasterCard. MC Opp. Ex. 9 at ¶¶ 106-24.[2] In the DOJ Action, the government did not allege *any* violations of Section 2.

As made clear by Professor Hausman's expert report, a key facet of Discover's alleged injury is its argument that By-law 2.10(e) and the CPP inhibited Discover's ability to increase its merchant acceptance through the use of third party acquirers. *See* MC Opp. Ex. 10 (Hausman Report) at ¶¶ 129-30, 188-91. Although this theory of injury was not litigated during

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[1] Discover does not allege such a market in any of its complaints, even though its Second Amended Complaint was filed less than two months prior to the date on which Discover served Professor Hausman's expert report.

[2] Discover originally asserted monopoly maintenance and attempt to monopolize claims against MasterCard individually. MC Opp. Ex. 11 at ¶¶ 88-100. However, this Court dismissed any such claims against MasterCard on the basis that MasterCard lacked the requisite market share in any alleged relevant market to sustain such claims. MC Opp. Ex. 12 at 3.

the DOJ Action—nor was any discovery taken on this issue during those proceedings—Discover is seeking approximately ***$6 billion*** in damages related to its inability to partner with third party acquirers.[3]

This Court earlier denied without prejudice Discover's request for collateral estoppel on the basis that no judicial efficiency would result in light of, among other things, Discover's newly asserted claims, including its Section 2 allegations and its claims related to debit:

> "The principal virtue of collateral estoppel of course is efficiency and judicial economy. At this stage of the litigation, I find that applying collateral estoppel would not promote efficiency. . . . [T]here are a number of additional claims and legal theories in this case that were not before me in the DOJ action. Including the plaintiffs' claims relating to monopolies and the debit card market."

MC Opp. Ex. 2 (Hearing 4/14/05 Tr.) 3

D. New Developments Since the DOJ Action

After the Court's denial of Discover's initial request for collateral estoppel in 2005, the parties have engaged in extensive discovery. Discover alone has produced more than 30 million pages of documents (in contrast to the tens of thousands it produced in the DOJ Action). MasterCard has produced more than 14 million pages of documents. Approximately sixty Discover witnesses have provided deposition testimony (in contrast to the nine Discover

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[3] Discover is claiming $1.1 billion in damages for cost savings Discover would have purportedly achieved as a result of working with third party acquirers, $2 billion in damages related to incremental spend on Discover's proprietary cards that would have resulted from increased acceptance due in part to the use of third party acquirers, and over $2.8 billion in damages related to Discover's third party credit and debit card issuance programs, where it is assumed that the third party credit and debit issuance would be robust and profitable because merchant acceptance will improve as a result of working with third party acquirers. MC Opp. Ex. 10 (Hausman Report) at ¶258.

executives that testified in the DOJ Action). In addition, nearly 100 third party banks produced voluminous documentary and testimonial evidence (depositions from over 100 bank representatives and more than 1.5 million documents). Much of this new evidence, which was unavailable during the DOJ Action, reveals that in the world without By-law 2.10(e) and the CPP, Discover is unable to compete successfully for issuers due to its inability to offer a compelling value proposition. Moreover, the new evidence reveals that

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The evidence further confirms that the new bank-issued Discover cards are virtually identical to the thousands of credit card products already in the marketplace.

As a result of Discover's lack of value proposition, since October 2004 Discover has partnered with only a handful of banks to issue cards on the Discover network. Of those partnerships,

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In addition, discovery has elicited new testimony from Discover executives—as well as from Discover's liability and damages expert Professor Hausman—that MasterCard's CPP caused Discover *no* incremental harm beyond that being already caused by Visa's By-law 2.10(e). As just one example, Discover's current CEO David Nelms conceded during his 2007 deposition that prior to the enactment of the CPP, banks were effectively "blocked" from issuing cards on the Discover network:

> [I]t's my understanding that—that even before 1996, given the prohibition that Visa had and the prospect that—the fact that all the members were issuing Visa and MasterCard, and that at any time MasterCard could pass such a prohibition . . . that issuers were blocked from issuing cards of any type on our network.

MC Opp. Ex. 13 (Nelms 5/15/07 Tr.) 38. And Professor Hausman made it abundantly clear during his deposition that he agreed:

> Q. And, Dr. Hausman, have you attempted based on your review of the record to quantify in any way what issuance there would have been on Discover if only 210(e) was in effect and not CPP?
> ....
>
> A. In my view, if only 2.10(e) had been in effect, and everything else remained constant, in other words you have duality and all, I think that Discover probably would not have had any significant amount of third party issuance. *In other words, 2.10(e) by itself was sufficient in my view to pretty much stop it.*

MC Opp. Ex. 17 (Hausman 1/26/08 Tr.) 316-17.

* * * *

> [Q.] [D]id you ask [Discover] for any evidence from Discover or otherwise of what, if any, effect 2.10(e) alone had on Discover's business—Discover's ability to do third party issuance?

A. Yes, I did ask that, and my memory of the documents I saw was that *if there had only been 2.10(e) prior to 1996, for instance, that the view was that Discover could not do third party issuing, and the loss of those volumes also affected the merchant acceptance gap as I discussed yesterday.*

Id. at 313. Notably, the impact, if any, of MasterCard's CPP by itself on Discover was never litigated during the DOJ Action.

Moreover, new evidence supports MasterCard's free-riding justification for the adoption of the CPP.

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Finally, since the DOJ Action, there have been significant developments in the economic literature surrounding two-sided markets, such as payment card markets, and how market power should be assessed in such markets. *See, e.g.*, MC Opp. Ex. 19 (James 11/8/07 Tr.) 32-33; MC Opp. Ex. 20. These developments, acknowledged as well by the DOJ's and Discover's expert witnesses, bear directly on this Court's market power analysis in the DOJ Action. Developments in the payments industry since the DOJ Action reveal that this Court's market definition analysis also should be revisited.

E. Discover's Present Motion

Discover's present motion requests that this Court estop MasterCard and Visa from litigating certain issues on the basis of this Court's decision in the DOJ Action and requests that the Court grant partial summary judgment on the liability portions of its First Claim For Relief of its Second Amended Complaint on that basis.

ARGUMENT

Under Rule 56(c) of the Federal Rules of Civil Procedure, summary judgment is proper only when the pleadings and evidence show "there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). A party moving for summary judgment has "the burden of showing the absence of a genuine issue as to any material fact, and for these purposes the material it lodged must be viewed in the light most favorable to the opposing party." *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 157 (1970).

Collateral estoppel is an equitable doctrine that should be applied "only when the alignment of the parties and the legal and factual issues raised warrant it." *Copeland v. Merrill Lynch & Co., Inc.*, 47 F.3d 1415, 1423 (5th Cir. 1995) (internal citations omitted). Application of the collateral estoppel doctrine, "is not a matter of right but rather a matter in which the trial judge has *broad discretion*." *Selectron, Inc. v. Am. Tel. & Tel. Co.*, 587 F. Supp. 856, 860 (D. Or. 1984) (citing *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 331 (1979)). This is because the doctrine is "detailed, difficult, and potentially dangerous." *Jack Faucett Assocs., Inc. v. Am. Tel. & Tel. Co.*, 744 F.2d 118, 124 (D.C. Cir. 1984). Moreover, the use of *offensive* collateral estoppel is particularly dangerous, and is narrowly circumscribed, because it can produce "extraordinarily harsh and unfair results," enshrine errors from previous cases, and "may have a

and fair opportunity for litigation in the prior proceeding; and 4) the issue previously litigated was necessary to support a valid and final judgment on the merits. *See, e.g., Faulkner v. Nat'l Geographic Enters. Inc.*, 409 F.3d 26, 37 (2d Cir. 2005) (setting forth above requirements "[i]n order for a plaintiff to bar a defendant from litigating an issue on collateral estoppel grounds"). As the party seeking to invoke collateral estoppel, Discover bears the burden of demonstrating "with clarity and certainty" each element. *Portlewaite v. McGraw-Hill, Inc.*, 333 F.3d 42, 49 (2d Cir. 2003).

Meeting these four elements, however, does not mandate the grant of collateral estoppel; it is merely a threshold. Because collateral estoppel is an equitable doctrine, courts will not apply it if its application would be unfair to defendants or if it will not achieve the intended trial efficiency. *See, e.g., Bear, Stearns & Co. v. 1109580 Ontario, Inc.*, 409 F.3d 87, 91 (2d Cir. 2005) ("This court has been careful to assure that collateral estoppel is not employed unfairly."); *Remington Rand Corp.*, 68 F.3d at 1486 ("But the discretion [to employ offensive collateral estoppel] has limits; unfair use of a prior determination against a subsequent litigant should not be permitted to stand."); *Tri-Ex Enters., Inc. v. Morgan Guar. Trust Co.*, 596 F. Supp. 1, 7 (S.D.N.Y. 1982) ("If for any reason it would be unfair to a defendant to bind him by a prior finding, the court should not allow the use of offensive collateral estoppel."). Indeed, when it authorized the use of offensive collateral estoppel, the Supreme Court expressly stated that "a trial judge should not allow the use of offensive collateral estoppel" if its application "would be unfair to a defendant." *Parklane Hosiery*, 439 U.S. at 331; *see also Jack Faucett Assocs.*, 744 F.2d at 125 ("Where offensive estoppel is involved, the element of 'fairness' gains special importance.") Thus, even if Discover could satisfy the other prerequisites for invoking collateral

devastating impact on a civil litigant's constitutional right to a jury trial." *Remington Rand Corp. v. Amsterdam-Rotterdam Bank, N.V.*, 68 F.3d 1478, 1486 (2d Cir. 1995); *see also SEC v. Monarch Funding Corp.*, 192 F.3d 295, 303-04 (2d Cir. 1999) (A risk of offensive collateral estoppel is "permanent encapsulation of a wrong result"); *Chartier v. Marlin Mgmt.*, 202 F.3d 89, 94 (2d Cir. 2000) ("[S]ince the doctrine of collateral estoppel poses a danger of placing termination of the litigation ahead of the correct result, it is narrowly applied."); *Johnson v. Watkins*, 101 F.3d 792, 795 (2d Cir. 1996) (same); *see also* 18 Charles Alan Wright et al., Federal Practice and Procedure, § 4416, at 398 (2d ed. 2002) ("The dangers of issue preclusion are as apparent as its virtues. The central danger lies in the simple but devastating fact that the first litigated determination of an issue may be wrong. The risk of error runs far beyond the proposition that most matters in civil litigation are determined according to the preponderance of the evidence.") (citing *Monarch Funding Corp.*, 192 F.3d at 303-04).

As this Court has recognized, "[t]he principal virtue of collateral estoppel of course is efficiency and judicial economy." MC Opp. Ex. 2 (Hearing 4/14/05 Tr.) 3-4; *see also Selectron*, 587 F. Supp. at 860 ("The purpose of the collateral estoppel doctrine is to save judicial and adversarial resources.") (citing *Parklane Hosiery*, 439 U.S. at 326). Where efficiency will not be served, courts have routinely declined to apply collateral estoppel. *See, e.g., Monarch Funding Corp.*, 192 F.3d at 304 ("When the efficiency rationale for collateral estoppel fails . . . courts have understandably declined to apply the doctrine.").

At the district court's discretion, a defendant may be collaterally estopped from relitigating the same issues decided in an earlier proceeding only if the party seeking preclusion shows each of the following prerequisites: 1) the issues in both proceedings are identical; 2) the issue in the prior proceeding was actually litigated and actually decided; 3) there was a full

estoppel, preclusion would be inappropriate if its application "would be unfair" to MasterCard and Visa.

Moreover, doubts about application of collateral estoppel should be resolved against its use. *See, e.g., Witkowski v. Welch*, 173 F.3d 192, 206 (3d Cir. 1999) ("[D]oubts about [collateral estoppel's] application should usually be resolved against its use"); *Eureka Fed. Sav. & Loan Ass'n v. Am Cas. Co.*, 873 F.2d 229, 233 (9th Cir. 1989) ("Collateral estoppel is inappropriate if there is any doubt as to whether an issue was actually litigated in a prior proceeding"); *O'Reilly v. County Bd. of Appeals*, 900 F.2d 789, 792 (4th Cir. 1990) (holding that "[a]bsent a clear identity of issues" between prior action and the present suit, collateral estoppel must be denied).

I. DISCOVER'S PRIVATE ACTION LACKS IDENTITY OF KEY ISSUES WITH THE DOJ ACTION AND INCLUDES ISSUES THAT HAVE NOT BEEN LITIGATED

Referring to this Court's statements in the DOJ Action, Discover uses the phrase "this Court already determined" (or some variation thereof) thirty-six times in its motion for summary judgment, implying in every instance that collateral estoppel must apply because the key issues are identical in both actions. The simple fact is that they are not. As this Court has observed, this case "isn't the same litigation" as the Government's equitable action, and collateral estoppel cannot be decided in a "vacuum." MC Opp. Ex. 1 (Hearing 11/16/04 Tr.) 12-13.

The Second Circuit has counseled that "[u]se of collateral estoppel 'must be confined to situations where the matter raised in the second suit is identical in all respects with that decided in the first proceeding and where the controlling facts and applicable legal rules remain unchanged.'" *Faulkner*, 409 F.3d at 37 (quoting *Comm'r v. Sunnen*, 333 U.S. 591, 599-

600 (1948)); *see also O'Reilly*, 900 F.2d at 792 (holding that "[a]bsent a clear identity of issues" between the prior action and the present suit, collateral estoppel must be denied.).

In the present action, Discover urges this Court to find that its Claim One is "identical" to the equitable cause of action asserted by the government in the DOJ Action. Discover Br. 1, 30. Despite Discover's careful attempts to mimic the language of the DOJ's complaint in the underlying litigation, the claims are very different. Moreover, Discover is asserting a myriad of other claims in this action that are closely intertwined with Claim One, and which further demonstrate the lack of identity in the two cases.

A. The Competitive Injury At Issue In The DOJ Action Is Wholly Different From The "Injury" Alleged By Discover In Its Private Action For Damages

Unlike the DOJ, Discover must prove that it has suffered injury-in-fact that was proximately caused by anticompetitive conduct attributable to MasterCard and Visa. *See Blue Tree Hotels Inv., (Canada), Ltd. v. Starwood Hotels & Resorts Worldwide, Inc.*, 369 F.3d 212, 220 (2d Cir. 2004) (to establish antitrust injury, a private litigant must "prove . . . 'injur[y] in its business or property' by reason of the violation . . . [and that] the violation was at least a material cause of the plaintiff's injury'") (quoting *Bohack Corp. v. Iowa Beef Processors, Inc.*, 715 F.2d 703, 710-11 (2d Cir. 1983)); *Argus Inc. v. Eastman Kodak Co.*, 801 F.2d 38, 41 (2d Cir. 1986) (affirming grant of summary judgment for defendant in antitrust suit because "lack of causation in fact is fatal to the merits of any antitrust claim"). Relying on various statements regarding injury to *competition* found in the Court's opinion in the DOJ Action, Discover seeks estoppel on the issue of its alleged injury. Specifically, Discover asserts that this Court's statements regarding the competitive impact of By-law 2.10(e) and the CPP on Discover's and American Express's ability to partner with banks is tantamount to a finding of injury to Discover. Discover

Br. 47-52. Discover's contention misses the mark, however, since the injury to competition found by this Court is vastly different from the injury Discover alleges it suffered as a result of By-Law 2.10(e) and the CPP.[4]

Discover's current theory of injury is based on its claim that the CPP and By-law 2.10(e) caused Discover injury by preventing it from partnering with third party *acquirers* (in addition to third party issuers), which limited its ability to achieve merchant acceptance parity with MasterCard and Visa. MasterCard S.J. Br. 36-37 (citing MC Opp. Ex. 10 (Hausman Report) at ¶¶ 179, 186, 188, 192, 194 & MC Opp. Ex. 22 (Hausman Rebuttal Report) at ¶¶ 230-35, 238-48, 297-301. Indeed, third party acquiring damages are so central to Discover's theory of injury that Discover's liability and damages expert testified that he did not even *consider* a damages model that did *not* include damages tied to third party acquiring. MC Opp. Ex. 17 (Hausman 1/26/08 Tr.) 317-18 (Q. Okay. And I'm correct, then, that you have no damages analysis that provides what damages Discover would have suffered if it did not in the but for world pursue third party acquiring, correct? . . . A. Yes, I have not considered a situation in which third party acquiring does not take place."). Based on this theory of injury, Discover is seeking approximately ***$6 billion*** in damages. Specifically, Discover is seeking $1.1 billion in damages for cost savings Discover would have purportedly achieved as a result of working with third party acquirers, $2 billion in damages related to incremental spend on Discover's proprietary cards that would have resulted from increased acceptance due in part to the use of third party acquirers, and over $2.8 billion in damages related to Discover's third party credit and

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[4] Discover is not entitled to estoppel on any findings that can be construed as findings of injury to Discover for the additional reason that such findings were not necessary to this Court's final judgment. *See* Section II.B *infra*.

debit card issuance programs REDACTED MC Opp. Ex. 10 (Hausman Report) at ¶¶ 184-207, 258. And yet, the effect of By-law 2.10(e) and the CPP on the now-alleged third party acquiring plans of Discover *was not before this Court in the DOJ Action*, and accordingly, *no discovery was taken* on whether Discover suffered any injury due to its purported lack of third party acquiring. Indeed, this Court made it explicitly clear that any prohibitions on third party acquiring were not at issue and were not litigated in the DOJ Action: "*[T]he Government never attempted to prove that Defendants' merchant acquiring rules were anticompetitive*, and . . . there is no evidence in the record to support the repeal of MasterCard's CPP *insofar as it applies to acquirers*." *United States v. Visa U.S.A. Inc.*, 183 F. Supp. 2d 613, 619 (S.D.N.Y. 2001). Nor was any discovery taken on the issue of whether there is a viable link between Discover's ability to work with third party issuers and its ability to enter into partnerships with third party acquirers. MasterCard is entitled to litigate this critical and central component of Discover's alleged injury, which was not litigated in the DOJ Action.

Discover's theory of injury under Claim One also includes allegations of injury to Discover's debit business. Aside from Discover's new claim regarding the direct impact of By-law 2.10(e) on Discover's ability to partner with banks to issue debit cards, Discover maintains that the CPP—which does not apply to debit card programs—nonetheless impacted Discover's ability to implement a debit platform.[3] Specifically, Discover claims that the CPP injured Discover's debit business by impeding Discover's ability to increase its relevance through third

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[3] The CPP does not apply to competing debit card programs. *See* MC Opp. Ex. 23 at DOJ-MC96-0585214; MC Opp. Ex. 24 at MCAD 000221097. Discover does not dispute this point, and indeed, Discover's damages and liability expert concedes it. MC Opp. Ex. 17 (Hausman 1/22/08 Tr.) 736 ("Q. And you don't have—and it's your understanding that CPP did not block Discover from access to DDA accounts for signature debit? A. Yes. . . my memory is that 210(e) had a prohibition, but that CPP did not.").

party issuance. *See* MC Opp. Br. 22 (Hausman Rebuttal Report) at ¶ 291. This type of injury was not before the Court in the DOJ Action and further underscores the difference between the statements regarding injury made by this Court and those advanced by Discover here.

Further, the "finding" with respect to debit cards in the DOJ Action—that the alleged exclusionary rules collectively foreclosed Discover from competing to offer off-line debit cards (*see* Discover Br. 49)—is illustrative of why it would be inappropriate to preclude MasterCard from litigating the issue of injury to Discover. The issue of actual harm to Discover by MasterCard alone was not at issue in the DOJ Action: the Court made no findings and there is no evidence that MasterCard prevented any bank from issuing debit cards on a competing network. Thus, to preclude MasterCard from litigating the issue of injury to Discover is patently unfair where the theory of causation also includes harm to its debit business—an issue neither litigated nor decided in the DOJ Action.

Moreover, the injury found by this Court did not encompass the type of injury that Discover must demonstrate here: that the CPP actually prevented Discover from entering into third party issuing relationships. Specifically, Discover must prove that its value proposition to issuers would have actually enabled it to attract issuance partners—a very different question than that faced by this Court in the DOJ Action. In the DOJ Action, the Court did not need to and did not make any findings as to whether or not Discover actually would have offered something of value to potential third party issuers; rather, the finding of liability and the equitable relief was based on the possibility that Discover *might* be able to offer a valuable deal to issuers. Here, where Discover must prove injury-in-fact, it has to prove that there would have been some deals to establish liability and that Discover would have suffered some monetary harm. In short, the theory of harm to competition on which the DOJ Action rested is not identical to the injury-in-

fact that Discover must prove here. Allowing Discover to side-step its burden to establish injury-in-fact (*i.e.*, that it would have offered sufficient value to some banks to induce them to enter into third party issuance deals) is unfair where new evidence produced in this case reveals that Discover would have been unable to attract a significant number of issuers due to its inferior economic offerings and its unwillingness to provide key network features to its bank partners. *See, e.g.*, MC Opp. Ex. 25 (Oster Discover Report) at 36-39 (Discover's appeal to issuing banks was limited by its inability to offer competitive interchange); MC Opp. Ex. 26 (Hall Discover Report) at 25-26 (Discover would not have been able to enter into third party issuing contracts without offering higher interchange or other benefits); MC Opp. Ex. 27 (Hubbard Report) at ¶¶ 32-35 (Discover Network does not offer third party issuers "unique" features); MC Opp. Ex. 14 (Hochschild 6/4/07 Tr.) 71-73

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B. The Issue Of The CPP's Independent Causal Effect On Any Harm To Discover Was Not Litigated In The DOJ Action

In the absence of a finding of an inter-association conspiracy between MasterCard and Visa, Discover must prove that the CPP *independently* caused Discover injury in order to collect any damages from MasterCard. *See, e.g., Intimate Bookshop, Inc. v. Barnes & Noble, Inc.*, No. 98 Civ. 5564 (WHP), 2003 WL 22251312, at *8 n.5 (S.D.N.Y. Sept. 30, 2003) (granting summary judgment for defendants and criticizing plaintiff's damages model for "not even try[ing] to disaggregate the effect and contribution of each defendant's unlawful conduct to [plaintiff's] alleged injury through any expert witness"); *Universal Amusements Co., Inc. v. Gen. Cinema Corp. of Texas, Inc.*, 635 F. Supp. 1505, 1526 (S.D. Tex. 1985) (finding insufficient

conspiracy evidence against defendants, and that since the lump sum damages model covering all defendants "left the jury no reasonable or principled way to adjust the damage amount if it so found any defendants innocent, the model could not support a jury award").

Here, Discover alleges that but-for By-law 2.10(e) and the CPP, it would have partnered with banks to issue Discover cards as early as 1995. MC Opp. Ex. 10 (Hausman Report) at ¶ 154 ("[I]t is reasonable to conclude that in the but-for world Discover would have already begun marketing its network services to prospective issuers and that third-party issuing on the network would have occurred by 1995"); *see also id.* at ¶ 192. While By-law 2.10(e)—which was enacted in 1991—was in effect at that time, the CPP was not implemented until 1996. Thus, a critical issue of causation in this case that was not present during the DOJ Action is what incremental impact, if any, the CPP had on Discover's ability to partner with banks to issue Discover cards. While this issue was not before the Court in the underlying litigation, numerous Discover executives, as well as Discover's liability and damages expert, have conceded that Discover's ability to partner with banks to issue credit cards was foreclosed by By-law 2.10(e) and that the CPP had no incremental impact on Discover's ability to do third party issuance. *See, e.g.*, MC Opp. Ex. 13 (Nelms 5/15/07 Tr.) 38; MC Opp. Ex. 28 (Purcell 5/23/07 Tr.) 306; MC Opp. Ex. 17 (Hausman 1/26/08 Tr.) 313, 316-17; MC Opp. Ex. 17 (Hausman 1/28/08 Tr.) 740. Thus, the crucial issue of whether MasterCard alone caused Discover any injury remains to be litigated and any preclusion on the issue of causation of injury attributable to MasterCard's conduct is unwarranted.

C. Discover Alleges Different Conspiracies In This Action Than Those Alleged In The DOJ Action

In addition to Discover's new claims regarding inter-association conspiracies between MasterCard and Visa that must be litigated in their entirety in this case,[6] Discover seeks collateral estoppel on the basis that this Court found "two parallel intra-association conspiracies" in the DOJ Action. Discover Br. 2, 37. However, this Court was not asked and did not consider whether there were parallel conspiracies between MasterCard and *each* of its members and Visa and *each* of its members. As evidenced in the DOJ's complaint, the DOJ alleged only a combination and conspiracy between MasterCard and its *governing* banks (and a similar conspiracy between Visa and its governing banks). MC Opp. Ex. 4 at ¶¶ 159-60. Discover, however, alleges a combination and conspiracy between "defendants and certain of their banks," which appears, based on Discover's Second Amended Complaint, to include *all* of MasterCard's members: "Defendants, on behalf of and in collaboration with their banks, have engaged in a continuing combination and conspiracy . . . .". MC Opp. Ex. 9 at ¶ 94. The distinction—which Discover conspicuously glosses over in its brief—is critical because MasterCard expects Discover to rely on the overlap in Visa and MasterCard membership to establish its claim of a conspiracy between MasterCard and Visa. Because Discover's conspiracy allegation is broader than and not identical to that alleged by the DOJ, Visa and MasterCard must be afforded the opportunity to litigate the parameters of Discover's alleged "parallel intra-association" conspiracies.

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[6] As the Court expressly noted in the DOJ Action, "[t]he Complaint does not allege a conspiracy between the two associations. *Visa U.S.A.*, 163 F. Supp. 2d at 347.

D. Discover Seeks Estoppel On Liability Issues Bearing Directly On Its Project Explorer Damages Theory, Which Was Also Not Litigated In the DOJ Action

While Discover does not mention the effect of collateral estoppel on its alternative damages theory based on the failed joint venture between Discover and Citibank ("Project Explorer"), a grant of estoppel on Claim One would effectively bar MasterCard from litigating liability issues as to this theory. Under the Project Explorer theory, Discover is seeking approximately ***$2.9 billion*** in damages. However, the DOJ Action did not involve any allegation regarding the effect, if any, of the CPP or By-law 2.10(e) on Project Explorer, or any anti- or pro-competitive effects that the CPP or By-law 2.10(e) might have with respect to it. Accordingly, the Court did not decide any liability issues in the context of Project Explorer, and thus collateral estoppel on Claim One should be denied on that basis as well.

E. The Time Period At Issue In The DOJ Action Is Not Identical To The Period Relevant To Discover's Private Action

Discover's private action lacks the requisite identity of issues with the DOJ Action for the additional reason that Discover is seeking collateral estoppel through October 2004 (when the Court's final judgment became effective), even though the record closed in the DOJ Action four years earlier in 2000. To take facts decided based on evidence from one time period and to use them to preclude litigation of similar facts from a *different* time period would be a plain violation of the "identity" component of the collateral estoppel doctrine. Discover contends that Visa and MasterCard bear the burden of proving that collateral estoppel should not apply. *Id.* at 33-34. Discover's argument is meritless.

Collateral estoppel may be applied only to facts extant in the time period at issue in the prior action. *See, e.g., Pool Water Prods. v. Olin Corp.*, 258 F.3d 1024, 1032 (9th Cir. 2001) (denying motion to apply findings from FTC action to private antitrust suit in part because

"the time period at issue here is different from the period at issue in the FTC proceeding"); *Int'l Shoe Mach. Corp. v. United Shoe Mach. Corp.*, 315 F.2d 449, 456-57 (1st Cir. 1963) ("In the Government case, the development of the evidential complex terminated in June, 1951 and so far as the findings and the decree are concerned, they can speak no later than this date"); *Oberweis Dairy, Inc. v. Assoc. Milk Producers, Inc.*, 553 F. Supp. 962, 966 (N.D.Ill. 1982) (holding that any collateral estoppel effect must be limited to time period of prior action). Because "the ultimate judgment relates only to the period embraced by the evidence adduced at trial," findings contained in that judgment "[can]not reflect a competitive situation subsequent [to the trial], else they would be grounded on speculation, not evidence." *Int'l Shoe Mach. Corp.*, 315 F.2d at 456-57.

In order to apply collateral estoppel to a time period other than that at issue in the prior case, Discover has the burden of proving that the conditions that existed at the time of the DOJ trial continued to exist in the subsequent time period. *See Dracos v. Hellenic Lines, Ltd.*, 762 F.2d 348, 353 (4th Cir. 1985) ("Unless it is shown that the condition found at a first trial is so permanent as to be unlikely to be disturbed, then we think offensive collateral estoppel may not be used with respect to that condition unless it be shown that the facts upon which the condition was based continued to exist."). While some authority suggests that the burden may be placed on the party seeking to defeat estoppel where the difference in time periods is *de minimis*, *see South Boston Allied War Veterans Council v. City of Boston*, 875 F. Supp. 891, 909-10 (D. Mass. 1995) ("Ordinarily, the party asserting collateral estoppel bears the burden of demonstrating that all the requisite elements are present .... Where, as here ... the period between the two cases is *short*, the burden of proving that collateral estoppel does not defeat a

· claim may be placed on the plaintiff"), such circumstances clearly do not apply where, as here, nearly four years transpired in a highly complex and evolving industry.[7]

In addition, Discover argues that collateral estoppel should apply through October 2004 because the stay of the final judgment until then preserved the "status quo." Discover Br. 9-10, 24, 53-54. The argument is nothing more than a play on words and ignores Discover's own position in this case.

First, Discover mischaracterizes the "status quo" that was being preserved. While the CPP and By-law 2.10(e) were left in place during the stay, the "status quo" preserved could not and did not freeze the competitive and economic dynamics of the payments industry. During the years that the stay was in effect, the payments industry continued to evolve and underwent a number of changes, which represent new factors that bear on the question of MasterCard's and Visa's ability to harm competition or competitors during that period. Indeed, with respect to payments industry dynamics, Discover's liability and damages expert Professor Hausman opines *at length* that the performance of Discover's actual world third party issuance programs are not

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7 The authority cited by Discover does not hold otherwise. *See GAF Corp. v. Eastman Kodak Co.*, 519 F. Supp. 1203, 1214 (S.D.N.Y. 1981) (finding that an approximately *six month* period "would not likely cause a jury to find different market definitions or reach different conclusions as to . . . market power," where only market power and market definition—but *not* injury—were at issue); *Harrington Haley LLP v. Nutmeg Ins. Co.*, 39 F. Supp. 2d 403, 407 (S.D.N.Y. 1999) (applying a prior finding that certain legal fees were unreasonable to immediately subsequent time period unless plaintiff could establish "material differences between the factors informing the assessment of reasonableness in the period at issue . . . compared with the *slightly* earlier period at issue before"). *See also Ramallo Bros. Printing, Inc. v. El Dia, Inc.*, 490 F.3d 86, 87-92 (1st Cir. 2007) ("Ramallo II") (applying findings from prior action involving same parties where approximately *eight months* transpired between the June 2005 judgment in the prior action and the event that constituted the cause of action in the second litigation, which occurred in February 2006); *Ramallo Bros. Printing, Inc. v. El Dia, Inc.*, 392 F. Supp. 2d 118, 118 (D.P.R. 2005) ("Ramallo I") (indicating that judgment was entered in the prior case in June 2005).

an accurate proxy for the but-for world because of significant changes that have occurred in the payments industry. MC Opp. Ex. 10 (Hausman Report) at ¶¶ 174, 177. Although it is MasterCard's position that Discover's actual performance *is* the best proxy in the record for the but-for world, Professor Hausman is correct insofar as he opines that industry conditions have not remained constant.[8] Accordingly, collateral estoppel is not appropriate for the time period when the stay was in effect and Discover has not satisfied its burden of proving otherwise.

F. Discover's New Claims Further Demonstrate The Lack Of Identity Between The DOJ Action And Discover's Private Action

In addition to Claim One, Discover is asserting a myriad of other claims that further demonstrate the lack of identity between Discover's private action and the DOJ Action. Specifically, Discover is asserting a variety of claims that were not litigated in the DOJ Action, including Section 2 monopolization, harm in alleged debit-related markets, and an inter-association conspiracy between MasterCard and Visa. MC Opp. Ex. 9 at ¶¶ 106-24, 86-90, 93-105. Moreover, the substantial overlap between the evidence necessary to litigate Discover's new claims and the evidence related to Claim One undercuts any judicial economy that would be served through the application of collateral estoppel on Claim One, *see* Section III.A *infra*, and Discover's motion should be denied on that basis as well.

II. DISCOVER SEEKS ESTOPPEL AS TO ISSUES THAT WERE NOT NECESSARY OR ESSENTIAL TO THE COURT'S JUDGMENT

Discover's motion should be denied for the independent reason that it is seeking collateral estoppel on issues that were not necessary or essential to the Court's judgment in the DOJ Action. As the Second Circuit has held, "[c]ollateral estoppel precludes relitigation of an

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[8] For example, PIN debit has become more prevalent (*see* MasterCard's Response to Discover's Statement of Undisputed Facts at ¶ 40), and Discover's merchant acceptance has improved (*see id.* at ¶ 35).

issue only if the prior determination of that issue was *necessary and essential* to the judgment in the earlier action." *Wickham Contracting Co, Inc. v. Bd. of Educ. of City of N.Y.*, 715 F.2d 21, 28 (2d Cir. 1983) (internal citations omitted); *see also Gelb v. Royal Globe Ins. Co.*, 798 F.2d 38, 44 (2d Cir. 1986) (concluding that "issue previously litigated must have been necessary to support a valid and final judgment on the merits"); *Central Hudson Gas & Elec. Corp. v. Empresa Naviera Santa S.A.*, 56 F.3d 359, 368 (2d Cir. 1995) ("Collateral estoppel or issue preclusion bars relitigation of issues actually litigated and decided in the prior proceeding, as long as that determination was essential to that judgment."). Dicta is not entitled to preclusive effect. *See In re Bean*, 252 F.3d 113, 118 (2nd Cir. 2001) ("pure *dicta* . . . not necessary to decide the issue" cannot have collateral estoppel effect). Similarly, issues "incidental, collateral, or immaterial" to the judgment are not considered necessary. *See Hicks v. Quaker Oats Co.*, 662 F.2d 1158, 1168 (Former 5th Cir. 1981); *see also Pool Water Prods.*, 258 F.3d at 1031 ("Litigants are not precluded from relitigating an issue if its determination was merely incidental to the judgment in the prior action.").

Moreover, in determining whether specific findings are necessary to a prior judgment, the Second Circuit has observed that "[a]ppellate review plays a central role in assuring the accuracy of decisions." *Gelb*, 798 F.2d at 45. "The limitation that a preclusive finding must be necessary to support a judgment is explained at least in part by the difficulty in obtaining appellate review of 'unnecessary' findings." *Id.* Thus, the rule in the Second Circuit is that "[i]f an appeal is taken and the appellate court affirms on one ground and disregards the other, there is no collateral estoppel as to the unreviewed ground." *Id.*; *see also Dow Chem v. U.S. E.P.A.*, 832 F.2d 319, 323 (5th Cir. 1987) ("[F]ederal decisions agree that once an appellate court has affirmed on one ground and passed over another, preclusion does not attach to the

ground omitted from its decision."). Only those findings that are necessary to the judgment actually affirmed by the Second Circuit are entitled to preclusive effect. *See In re Microsoft Corp. Antitrust Litig.*, 355 F.3d 322, 325 (4th Cir. 2004) (directing "district court to give preclusive effect only to factual findings that were necessary" to judgment affirmed by D.C. Circuit); *see also* Wright et al., § 4432, at 63 ("the nature of the ultimate final judgment in a case ordinarily is controlled by the actual appellate disposition"). The fact that a finding is "supportive of" an affirmed judgment is not sufficient to give it preclusive effect in subsequent litigations. *See Microsoft*, 355 F.3d at 325 ("the 'supportive of' standard is not the appropriate standard for applying collateral estoppel").

Despite Discover's overarching claim that granting collateral estoppel will eliminate any issue of material fact concerning "any of the elements of liability for Claim One of Discover's Second Amended Complaint," (Discover Br. 2), injury-in-fact to Discover and the CPP's role in causing this alleged harm were not elements of the DOJ's case. Because a finding of harm to Discover was not necessary to the judgment actually affirmed by the Second Circuit—indeed, the Second Circuit "passed over" the statements Discover contends constituted a finding of harm to Discover—and because the Court never established that the CPP itself caused any injury to Discover, Discover's motion for partial summary judgment as to liability should be denied.

A. A Private Plaintiff's Antitrust Damages Action Has Distinct Elements From A Government Enforcement Action Under The Sherman Act

As an initial matter, a government enforcement action for injunctive relief under Section 1 of the Sherman Act and a private plaintiff's action for alleged violations of the Sherman Act have different elements. The Sherman Act gives the federal government standing

to enforce violations "even when no plaintiff has suffered an injury." *Kruman v. Christie's Int'l*, 284 F.3d 384, 397-98 (2d Cir. 2002). In a government enforcement action, therefore, proof of an antitrust violation by defendants establishes only that injury *may* result. In contrast, Section 4 of the Clayton Act sets forth the substantive requirements a private plaintiff must meet to bring suit for Sherman Act violations: (1) that it suffered injury-in-fact; (2) that the antitrust violation was the proximate cause of its injury; and (3) that the injury was the kind that the "antitrust laws were designed to prevent." *Id.*; *see also In re Microsoft Corp. Antitrust Litig.*, 232 F. Supp. 2d 534, 538-39 (D. Md. 2002) (citing cases), *rev'd on other grounds*, 355 F.3d 322 (4th Cir. 2004). Accordingly, to prevail in the current action, Discover will have to prove that it suffered injury-in-fact and that the CPP and By-law 2.10(e) proximately caused that injury. As discussed below, to the extent the Court considered and reached conclusions as to these elements in the underlying action, the conclusions were not necessary or essential to its findings.

B. A Finding of Injury to Discover Was Not Necessary To The Prior Judgment

As the Second Circuit acknowledged in its decision in the DOJ Action, the "proper inquiry" in a Section 1 action is not whether competitors have been harmed, but "whether there has been an actual adverse effect on competition as a whole in the relevant market." *Visa U.S.A.*, 344 F.3d at 242 (citing *KMB Warehouse Distribs. v. Walker Mfg. Co.*, 61 F.3d 123, 127 (2d Cir. 1995)). Any finding with respect to individual competitors, even in a market with a limited number of competitors, is therefore not necessary to the previous judgment.

The district court's decision in *In re Microsoft Corp. Antitrust Litigation*, 232 F. Supp. 2d 534, is instructive. There, in private antitrust proceedings brought following a successful government enforcement action, the plaintiffs sought partial summary judgment on

the issue of liability on a collateral estoppel theory. *Id.* at 538-39. Although the court granted estoppel as to certain findings made in the government action,[9] it held that the government had not proven in its case "all of the elements that the private plaintiffs must prove in their action for damages," namely that the private plaintiffs had (1) suffered injury in fact; (2) caused by the alleged antitrust violation; and (3) that the injury constituted "antitrust injury." *Id.* at 538 (citing *Associated Gen. Contractors of Calif. v. Calif. State Council of Carpenters*, 459 U.S. 519, 539-40 (1983); *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489 (1977); *Microbix Biosystems, Inc. v. Biowhittaker, Inc.*, 172 F. Supp. 2d 680, 696 (D. Md. 2001)). Notably, while the decision recognized that "[i]t seems self-evident" that Microsoft's unlawful monopoly maintenance had some effect on its competitor Netscape, the court held that "both the government's and the court's focus was on the harm to the structure of the market, that is to competition, not to particular competitors" and that, therefore, "it cannot be fairly said that the facts found in the government case are sufficient to establish Microsoft's liability to Netscape." *Id.* at 538-39. The result should be no different where, as here, the DOJ Action's focus was on harm to competition.[10]

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[9] This grant of collateral estoppel was ultimately reversed on appeal. *See In re Microsoft Corp. Antitrust Litig.*, 355 F.3d at 325, 329.

[10] *In re Ivan Boesky Secs. Litig.*, 848 F. Supp. 1119 (S.D.N.Y. 1994), relied upon by Discover to show that it need not litigate certain elements of its claim is readily distinguishable. *See* Discover Br. 51-52. In *In re Boesky*, the private plaintiff had to establish two elements—reliance and loss causation—in addition to the three required elements established by the SEC in proving its § 10(b) claim. *Id.* at 1124. However, there, under the controlling legal standard, the plaintiff's reliance on defendant's violation was established by a rebuttable presumption, and the defendant presented no evidence to rebut the presumption. *Id.* at 1125. Unlike here, injury and causation in *In re Boesky* were straight-forward. In contrast, this case involves (1) no rebuttal presumptions, (2) complicated and new theories of injury to Discover, including allegations regarding Discover's ability to partner with third party acquirers, and (3)

Moreover, the standard for relief articulated by this Court also made clear that injury to Discover (and to American Express) was not "necessary" to establish liability in the DOJ Action: "The core of Section 1 inquiry is whether the challenged restraint is 'unreasonable,' *i.e.*, whether its anticompetitive effects outweigh its procompetitive effects .... Identifying 'anticompetitive effects' under the rule of reason involves analysis of whether the *competitive process itself has been harmed.*" *Visa U.S.A.*, 163 F. Supp. 2d at 344. Not once did this Court or the Second Circuit mention injury to Discover or American Express as a necessary element for a finding of a Section 1 violation. Indeed, in denying Discover's motion to intervene in the DOJ Action, this Court expressly recognized harm to Discover as a competitor was not at issue: *"To the extent that Discover seeks intervention to protect its private interests, Discover's interests as a competitor are not the subject of this case ...,"* MC Opp. Ex. 30 at 2.

Nonetheless, Discover argues that it should be entitled to estoppel on the issues of injury-in-fact and causation because this Court's statements regarding injury to competition are tantamount to findings of injury to Discover. Discover is wrong. The specific statements related to harm to Discover and American Express are "supportive of," but not necessary to, the judgment. *See In re Microsoft*, 355 F.3d at 325 (holding that "supportive of" standard is not appropriate standard for collateral estoppel). As such, any finding of harm particular to Discover, as opposed to competition, should not be given preclusive effect here. *See id.* (directing district court to give preclusive effect only to factual findings necessary to its judgment).

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complex issues of causation, including whether the CPP independently caused Discover any injury.

Indeed, in addition to the *Microsoft* decision, other courts have refused to apply estoppel, even as to findings made by a prior court, where those findings were determined to be legally unnecessary. The Second Circuit's decision in *Wickham Contracting*, 715 F.2d 21, is instructive. There, in the earlier proceeding, an unfair labor practices administrative hearing, the lower court found that a union defendant had excluded all competitors, even though the plaintiff needed to show only that one competitor was excluded to prevail. *Id.* at 27-28. In the subsequent antitrust proceeding, despite the court's finding concerning the complete exclusion of competitors, the court held that, because "a narrower holding would have sufficed," the finding regarding complete exclusion was "neither necessary nor essential to the unfair labor practices claim." *Id.* at 28. The court reasoned that the defendant had no reason to litigate the "precise issue" of whether particular competitors had been harmed. *Id.* Similarly, here, the court previously needed only to find general harm to competition, not specific injury to Discover—much less the identical injury Discover is claiming in this case. *See* Section I *supra*. MasterCard had no reason to litigate the precise issue of whether or not Discover, as opposed to competition, had actually been injured by the CPP, including issues surrounding causation from the CPP alone. Indeed, as in *Wickham Contracting*, a narrower holding than Discover advocates in its summary judgment papers would have sufficed to find the CPP violated Section 1. Therefore, a finding of harm to Discover was not necessary to this Court's earlier holding.

Furthermore, this Court, in finding harm to competition, made virtually no findings of any potential harm solely to Discover; instead, the Court typically discussed Discover and American Express collectively.[11] *See, e.g.*, *Visa U.S.A.*, 163 F. Supp. 2d at 341 (Visa and

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[11] Discover claims that the Defendants "conceded" that the central question to the DOJ's case was whether Discover and American Express were foreclosed, and therefore cannot

MasterCard's rules deny "American Express and Discover the opportunity to issue cards through bank issuers"); *id.* at 379 ("American Express and Discover cannot access the issuing competencies and segmented marketing expertise of the banks"). The lone exception is this Court's finding that First USA "would have liked" to issue cards over the Discover network but-for By-law 2.10(e) and the CPP. *Id.* at 386-87. However, the only evidence cited by this Court in support of that finding is one-sided testimony from Discover's CEO David Nelms. *See id.* As outlined above, this finding was not necessary to the judgment actually affirmed by the Second Circuit—and indeed, the Second Circuit's decision does not reference this finding nor include any other references to any impact of By-law 2.10(e) or the CPP solely on Discover.

Moreover, the record evidence establishes that no deal was consummated between REDACTED and Discover for reasons unrelated to By-law 2.10(e) and the CPP. In fact, Mr. Nelms himself admitted that the negotiation

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deny that injury to Discover was a central issue in the DOJ Action. *See* Discover Br. 49. Discover's contention is meritless. In the DOJ action, defendants argued that if Discover and American Express were able to reach consumers directly, *consumers* could not have been harmed. *Visa U.S.A.*, 163 F. Supp. 2d at 382-83. This Court rejected this argument. *Id.*

REDACTED While this Court's finding may have been supportive of this Court's ultimate conclusion of harm to competition, it would be fundamentally unfair to preclude MasterCard entirely from disputing Discover's alleged harm by granting collateral estoppel based on the limited and one-sided evidence available to the Court in the DOJ Action—especially where the finding was not necessary to this Court's final judgment. *See, e.g., Remington Rand*, 68 F.3d at 1486 (warning of "extraordinarily harsh and unfair results" that can result from applying of offensive non-mutual collateral estoppel).

As in *Microsoft* and *Wickham Contracting*, and despite Discover's claims that a finding of harm to competition and a finding of harm to Discover are "inextricably linked," *see* (Discover Br. 48), the focus of both the DOJ and the Court was on harm to *competition*, not on the issue of injury to Discover or on the cause of any such injury to it. Because Discover has not shown that any statements regarding any such harm or the cause of such harm are necessary or essential to this Court's judgment, collateral estoppel is not warranted on those issues and Discover's motion for summary judgment should be denied.

III. COLLATERAL ESTOPPEL WILL NOT SERVE JUDICIAL ECONOMY AND WOULD BE UNFAIR

Discover's motion should also be denied because granting collateral estoppel will not serve judicial economy and would be fundamentally unfair. Preclusion should be denied when the efficiency rationale fails or fairness is in doubt. *See, e.g., Parklane Hosiery*, 439 U.S. at 329-31; *Monarch Funding Corp.*, 192 F.3d at 304; Restatement (Second) of Judgments § 29 (1982). The Second Circuit has recognized that "courts have understandably declined to apply the doctrine" when the "principal virtue" of promoting judicial economy fails. *Monarch Funding*, 192 F.3d at 304. This is because "[w]hatever values may be gained by nonmutual

preclusion are substantially diminished when the need to try related issues requires consideration of much the same evidence as bears on the issue tendered for preclusion." Wright et al., § 4465, at 738. Accordingly, courts have denied "nonmutual preclusion on issues that are closely related to the issues to be tried." *Phonetele, Inc. v. Am. Tel. & Tel. Co.*, CV-74-3566 (MML), 1984 WL 2943, at *2-5 (C.D. Cal. Jan. 19, 1984).

A. Collateral Estoppel On Claim One Will Not Serve Judicial Economy

As this Court has acknowledged, "*The principal virtue of collateral estoppel of course is efficiency and judicial economy.*" MC Opp. Ex. 2 (Hearing 4/14/05 Tr.) 3-4. Indeed, where, as here, preclusion would not promote judicial efficiency, courts often decline to apply it. *See, e.g., Schwab v. Philip Morris USA, Inc.*, 449 F. Supp. 2d 992, 1079 (E.D.N.Y. 2006) (declining to apply collateral estoppel in part because plaintiffs would still have had to present much, if not all, of the same evidence heard in the prior case); *Acevedo-Garcia v. Monroig*, 351 F.3d 547, 577 (1st Cir. 2003) ("Where even one issue of liability must be made available to defendants in the second trial, granting preclusive effect to the other issues may not result in efficiency gains because litigation of the 'live' issue may require introduction of some of the same evidence pertinent to the estopped issues."); *Setter v. A.H. Robins Co.*, 748 F.2d 1328, 1331 (8th Cir. 1984) ("[I]f collateral estoppel were invoked here, little court time would be saved, because . . . the same facts, or most of them, that would have been relevant on [the precluded issue] would still have to come in and be considered by the court or jury on [the remaining issues].").

While Discover contends that collateral estoppel on Claim One will "streamline" these proceedings, Discover's additional claims, which were not at issue in the DOJ Action, and the substantial overlap between liability and damages issues effectively guarantee that no judicial

economy will be served by granting Discover's motion. Moreover, any minimal efficiency gains will be offset by the potential for juror confusion due to inconsistent findings.

(1) There Is Substantial Overlap Between Liability And Damages Issues

Collateral estoppel will not result in judicial economy because there is substantial overlap between the issues that must be litigated for damages—as well as the causation element of liability—and the issues for which Discover seeks estoppel. This overlap defeats any prospect of judicial economy through preclusion. *See, e.g., Schwab*, 449 F. Supp. 2d at 1079 (denying collateral estoppel where "plaintiff's proof of reliance and damages would almost certainly . . . require presentation of all evidence available to them of defendants' alleged scheme"); Wright et al., §4465.3, at 782 ("The need to relitigate individual issues that overlap the common issues may provide a special reason to deny preclusion—little if any trial time will be spared . . . .").[12] Discover will have to introduce much of the same underlying evidence in order to establish the remaining issues of causation and damages. For instance, Discover's damages model depends upon the factual assumption that Discover would have partnered with numerous banks to issue credit and debit cards but-for CPP and 2.10(e). MC Opp. Ex. 10 (Hausman Report) at ¶¶150, 218. In order to *quantify* its damages, Discover will need to present evidence regarding potential

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[12] Courts frequently address the issue of overlap between damages and liability issues in the context of requests for bifurcated proceedings. Notably, courts regularly deny such requests due to the confusion and uncertainty that may arise where there is such overlap. *See, e.g., Martin v. Heideman*, 106 F.3d 1308, 1312 (6th Cir. 1997) (holding trial court abused discretion in bifurcating trial between damages and liability where "extent of plaintiff's damages was relevant to the question of liability"); *United Air Lines, Inc. v. Wiener*, 286 F.2d 302, 306 (9th Cir. 1961) (denying request for bifurcated proceedings where "question of damages is so interwoven with that of liability" that the adjudication of one without the other would cause "confusion and uncertainty"); *Thorndike v. DaimlerChrysler Corp.*, 220 F.R.D. 6, 8 (D. Me. 2004) (denying bifurcation where "theories of liability and damages are substantially inter-related and there will necessarily be an overlap between the evidence," and "whatever efficiencies may be gained . . . are offset by potential confusion of the issues").

bank deals, which will overlap extensively with the evidence necessary to demonstrate harm to competition and injury to Discover. In addition, MasterCard will need to put on evidence to counter Discover's damages assumptions.[13]

Similarly, to prove liability under Claim One, Discover would have to establish that banks would have been interested in issuing Discover cards and were foreclosed from doing so by the CPP. To prove damages, Discover must go further and make assumptions regarding the anticipated volume of bank issuance and anticipated spend on bank-issued cards that would have occurred but-for the CPP. Discover cannot realistically do so without making certain assumptions as to how many or which banks would have been interested, why they would have been interested, and how many cards those banks would have issued. For the damages model to be admissible, Discover has to introduce evidence that supports these assumptions. To rebut these assumptions, MasterCard will rely on much of the same evidence that it would rely on to defend against the foreclosure and injury arguments relating to liability—that is, evidence tending to show that the "differentiation" and "value proposition" Discover expert Professor Hausman claims would have attracted banks is grossly overstated. *Compare, e.g.*, MC Opp. Ex. 10 (Hausman Report) at ¶¶ 159-164, *with* MC Opp. Ex. 32 at DFS 030086497)

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[13] A collection of certain of Discover's factual assumptions bearing on its damages model is attached hereto as Appendix A.

As another example, Professor Hausman posits that Discover is entitled to damages because By-law 2.10(e) and the CPP limited Discover's relevance to consumers, which in turn limited its merchant acceptance. *See* MC Opp. Ex. 10 (Hausman Report) at ¶¶ 183-87, 200-07. Discover's damages model therefore assumes that bank issuance of Discover cards in the but-for world would have caused more merchants to accept its cards. *Id.* In addition, Professor Hausman also asserts that Discover invested "substantial" amounts of money in attempting to achieve greater merchant acceptance, and that it is entitled to damages reflecting the savings it would have enjoyed in its but-for world. *See id.* at ¶¶ 194-99. To evaluate how much injury Discover may have suffered, the jury will have to consider how attractive Discover-branded bank cards would have been to merchants (which entails evaluating evidence about which consumers would have likely have been attracted to such cards) in the but-for world and how much spend these cards would have generated. Once again, the evidence bearing on these questions overlaps significantly with evidence related to whether Discover suffered any injury at all—a liability issue.

The same is true for the other statements for which Discover seeks estoppel. Discover's liability and damages expert assumes that there would have been substantial consumer demand for bank-issued Discover products and that such demand would have made such third party issuance partnerships profitable for Discover. MC Opp. Ex. 10 (Hausman Report) at ¶¶ 90, 106-07, 115-16, 148. However, a key driver of consumer demand is a product's ability to differentiate itself from existing products in the market. This Court, in ruling on liability in the DOJ Action, previously predicted that demand for bank-issued American Express and Discover cards would be fueled by a combination of Discover's and American Express's network attributes with the "unique" features and expertise of banks. *Visa U.S.A.*, 163

F. Supp. 2d at 329, 382. For damages purposes, MasterCard is entitled to prove whether or not such combinations would have taken place in the but-for world and the likely magnitude of any resulting consumer demand.

(2) There Is Substantial Overlap Between Claim One And Discover's New Claims, Including Section 2, Debit, and Inter-Association Claims

Because Discover has moved for summary judgment based on collateral estoppel on only one of its claims, four claims would remain to be litigated. This Court has already acknowledged that Discover's new claims substantially diminishes—if not eliminates—any judicial economy to be gained through collateral estoppel: "[T]here are a number of additional claims and legal theories in this case that were not before me in the DOJ action. ***Including the plaintiffs' claims relating to monopolies and the debit card market. The collateral estoppel doctrine, in my opinion, would do nothing to promote judicial economy vis-à-vis those claims.***" MC Opp. Ex. 2 (Hearing 4/14/05 Tr.) 3-4. Discover cannot argue to the contrary. Indeed, the evidence underlying Claim One overlaps extensively with the evidence required to prove Discover's newly-asserted claims—including its Section 2 monopolization, inter-association conspiracy, and debit claims—which will need to be litigated in their entirety. By pursuing numerous other claims that were not litigated in the DOJ Action, Discover will have to present substantial evidence on related questions of monopoly power, market definition, and anticompetitive conduct, erasing any purported efficiency gains.[14]

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[14] In a footnote, Discover argues that it does not need to prove market definition or Visa's and MasterCard's market power in the general purpose card network services market in order to prevail on its Section 1 claim because proof of "actual detrimental effects" was established in the DOJ Action. Discover Br. 45 n.23. Discover's argument is pointless. If Discover means to imply that market power and market definition were not necessary to the Court's Judgment regarding effects on competition—and that it does not intend to put on evidence regarding market definition and power—then collateral estoppel on

Discover is asserting an inter-association conspiracy claim against Visa and MasterCard under Section 1. MC Opp. Ex. 9 at ¶¶ 100-05. In addition, Discover is asserting Section 2 monopolization and attempted monopolization claims against Visa individually and Section 2 inter-association conspiracy to monopolize and attempt to monopolize claims against Visa and MasterCard collectively. *Id.* at ¶¶ 106-24.

First, the inter-association conspiracy charge is a new claim and the critical link to holding MasterCard and Visa jointly and severally liable. MC Opp. Ex. 9 at ¶¶ 106-24, 100-05. Without a showing of conspiracy, MasterCard is not liable for any damage caused by Visa. Discover chose to sue MasterCard together with Visa; Discover chose not to proffer a damages model that allocates damages between those caused by Visa and those caused by MasterCard; and, Discover chose to move for partial summary judgment, based on collateral estoppel, but without any finding of causation supporting joint and several liability by MasterCard and Visa. Even if collateral estoppel is granted such that each of Visa and MasterCard are held individually liable and the inter-association conspiracy charge is dismissed (as it should be), Discover has no damages theory as to MasterCard or Visa. Discover's damages claims must fail because it has no evidence to support what portion of its alleged damages was caused by MasterCard. If the evidence of inter-association conspiracy will be presented to the jury, there is little efficiency in

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market power is inappropriate on lack of necessity grounds. (*see* Section II *supra*). Alternatively, if Discover intends to present evidence of market definition and market power, collateral estoppel is inappropriate because of lack of judicial economy and changed circumstances (*see* Section III.B *infra*).

precluding MasterCard from litigating liability because all the evidence surrounding the circumstances under which MasterCard enacted CPP will need to be introduced.[15]

Second, because the DOJ Action did not involve Section 2 allegations or any allegations of a conspiracy to monopolize between MasterCard and Visa, Discover is not entitled to any findings of preclusion on these claims, and will have to litigate each element of these claims. *See* Wright et al., §4417, at 421 ("[C]lear distinctions of applicable law generate different issues, free from preclusion.") Specifically, Discover will need to present evidence that Visa has (and that Visa and MasterCard collectively are seeking to achieve) "monopoly power" in the alleged markets. *See Verizon Commc'ns v. Trinko, LLP*, 540 U.S. 398, 407 (2004) (stating that monopolization requires proof that the defendant possesses monopoly power). For Section 2 monopolization purposes, "monopoly power" and "market power" are often used interchangeably. *See, e.g., Toys Mkts., Inc. v. Quality Mkts., Inc.*, 142 F.3d 90, 97-98 (2d Cir. 1998) ("Monopoly power [is] also referred to as market power."). However, monopoly power is something different from market power under Section 1 of the Sherman Act and "requires, of course, something greater than market power under §1." *Eastman Kodak Co. v. Image Tech. Servs., Inc.*, 504 U.S. 451, 481 (1992).

Since evidence of monopoly power overlaps with, but is distinct from, the issue of market power under Section 1, Discover will by necessity have to present much of the same evidence used to prove market power under Section 1. This Court's findings of market power are not tantamount to a finding of monopoly power under Section 2. Discover's counsel

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[15] For example, the parties' briefing in connection with MasterCard's Rule 56 motion for summary judgment on the inter-association conspiracy claim demonstrates the scope of at least the critical evidence that needs to be introduced in connection with the inter-association conspiracy.

conceded as much during the parties' hearing on motions to dismiss, noting that there are "very significant differences" between a Section 1 and Section 2 case. MC Opp. Ex. 2 (Hearing 4/14/05 Tr.) 32 ("You've made very extensive findings on the structure of this market. . . . These are part of an overall section two course of conduct, *and there are very significant differences in a section two case. We ought to have the right to present that case to a jury.*").

The same is true for Discover's debit-related claims. To prevail on its claims of harm in its newly alleged debit card and network services markets, Discover will have to litigate the existence of such markets and of harm to competition in those markets. *See, e.g., Heerwagen v. Clear Channel Comme'ns*, 435 F.3d 219, 229 (2d Cir. 2006) ("[A] plaintiff claiming monopolization is obligated to establish the relevant market because the power to control prices or exclude competition only makes sense with reference to a particular market."). Since this evidence will overlap substantially with that necessary to prove a general purpose credit and charge card market and general purpose credit and charge card network services markets and harm to competition in those markets, granting collateral estoppel on Claim One will not create significant efficiencies.

Discover argues in a footnote that the presence of its new claims should not impact this Court's assessment of whether granting Discover's motion will serve judicial economy. Discover Br. 42 n.21. It contends that it would be in a position to voluntarily dismiss its "duplicative" Section 2 claims against Visa in the alleged credit network services market because such claims do not lead to additional damages beyond those associated with Claim One. Discover is wrong. Discover cannot dismiss—and tellingly does not offer to dismiss—its inter-association conspiracy claim under Section 1 because it has no damages theory for either

MasterCard or Visa individually. Nor is Discover offering to dismiss its debit claims which raise completely new and overlapping issues with its Claim One under Section 1 of the Sherman Act.

Further, aside from the fact that Discover has not withdrawn its duplicative claims, Discover's argument is misleading because it fails to mention that the very same Section 2 claims and inter-association conspiracy charges need to be litigated with respect to the alleged *debit* market under Sections 1 and 2. Thus, Discover still would have to litigate each element of the Section 2 claims, requiring it to present the overlapping evidence discussed above, as well as to prove concerted action between Visa and MasterCard. This belies Discover's attempt to claim that collateral estoppel will yield real efficiencies.[16]

In any event, because Discover is not entitled to collateral estoppel for the periods 2000 to 2004 (or beyond) (*see* Section I.E *supra*), liability issues will need to be litigated *in their entirety* for that period. Thus, a grant of collateral estoppel will create little, if any, judicial economy in this case.

B. Collateral Estoppel Would Be Unfair

Any efficiency gains that could potentially be achieved through the application of collateral estoppel are far outweighed by the potential for unfairness that would result. *First*, precluding MasterCard would prevent the jury from considering for purposes of liability newly available evidence that bears directly on the Court's previous findings, including findings regarding consumer harm and procompetitive justification. *Second*, estoppel would prevent the jury from considering new scholarship regarding market power in the context of two-sided

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16 Discover also claims that it has "done its utmost to narrow the issues in dispute in this litigation." Discover Br. 42. To the contrary, Discover has attempted to expand the issues in dispute by claiming damages associated with third party acquiring—conduct that was not challenged in either the DOJ Action or in any of the three complaints Discover has filed in this case. *See* MC S.J. Br. 35-37.

platforms and new evidence bearing directly on market definition. *Third*, in light of the overlap between liability and damages issues, as discussed above, collateral estoppel could substantially distort the record or result in juror confusion. *Fourth*, application of collateral estoppel would be unfair because Discover seeks to establish "facts" contradicted by its own executives under oath. For these additional reasons, Discover's motion should be denied. *Parklane Hosiery*, 439 U.S. at 329 (offensive use of collateral estoppel should not be granted where "it may be unfair to a defendant").

(1) Collateral Estoppel Should Be Denied In Light of Critical New Evidence Available Since the DOJ Action

Granting Discover's request for estoppel, if successful, would result in fundamental injustice to defendants because it would bind the parties to statements this Court made almost seven years ago, even though many of those statements were necessarily predictive in nature and have since been proven inaccurate by new evidence. The injustice would be particularly acute here, where Discover is seeking billions of dollars in damages and where over 100 million pages of documents and the depositions of approximately sixty Discover witnesses provide *new real world* evidence that undercuts many of this Court's forecasts.

The Supreme Court, concerned with the fair application of collateral estoppel, has found that "changes in facts essential to a judgment will render collateral estoppel inapplicable in a subsequent action raising the same issues." *Montana v. United States*, 440 U.S. 147, 159 (1979); *see also* Restatement (Second) of Judgments § 29, cmt. j ("Important among [circumstances where collateral estoppel would be inappropriate] is the disclosure that . . . new evidence has become available that could likely lead to a different result."); *Jack Faucett Assocs.*, 744 F.2d at 119 (no collateral estoppel "where important, material evidence can be

introduced in the current trial that was unavailable in previous trial"); *Baby Dolls Topless Saloons, Inc. v. City of Dallas*, 295 F.3d 471, 478-479 (5th Cir. 2002) (upholding district court's denial of collateral estoppel where in first proceeding district court held statute unconstitutional, finding no evidence regarding deleterious effects of prohibited conduct; city later adopted a virtually identical ordinance against same conduct; nevertheless, in second proceeding district court *did not* apply collateral estoppel because city had gathered and presented evidence of conduct's negative effects). Indeed, the Second Circuit has held that where a prior judgment's factual underpinnings have been eroded, a court should not estop a party from re-litigating those issues. *See, e.g., Ezagui v. Dow Chem. Corp.*, 598 F.2d 727, 731 (2d Cir. 1979) (upholding district court's denial of plaintiff's application for collateral estoppel "on the ground that new scientific evidence cast doubt on" plaintiff's causation theory); *see also United States v. Alcan Aluminum Corp.*, 990 F.2d 711, 719 (2d Cir. 1993) ("[A] court should decline to give effect to a prior judgment if there have been changes either in the applicable law or the factual predicates essential to that prior judgment.").

This Court's holding that By-law 2.10(e) and the CPP violated Section 1 of the Sherman Act resulted from an analysis based largely—and necessarily—on predictions by Discover, American Express, the DOJ, bank witnesses, Visa, and MasterCard as to what the payments industry would look like in the absence of By-law 2.10(e) and the CPP, and similar predictions about how banks and consumers would react in this but-for world. Relying to a great extent on these predictions, the Court concluded that By-Law 2.10(e) and the CPP harmed competition. *Visa U.S.A.*, 163 F. Supp. 2d at 379. In addition, the Court concluded that the harm to competition was not outweighed by any procompetitive justification. *Id.* at 406. In the seven

years that have passed since the DOJ Action, new evidence of actual marketplace developments has emerged that has a direct bearing on this Court's liability findings.

As just one example, this Court concluded that consumers were harmed by By-law 2.10(e) and the CPP in part because (1) consumers were denied access to innovative new products combining the features of the American Express and Discover networks with those of bank issuers and because (2) By-law 2.10(e) and the CPP resulted in reduced output of Discover cards. *Id.* at 379, 382. However, new real world evidence of Discover's value proposition to issuers reveals two truths:

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Thus, even in the absence of the CPP and By-law 2.10(e), there is strong evidence that there would not have been increased output of Discover cards as a result of third party issuance programs, and consumers would not have benefited from any combination of Discover's "unique" network features on a third party issued Discover card.[17]

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[17] In fact, when questioned about whether consumers will benefit from the third party issuance of Discover cards, Discover's own liability and damages expert conceded that "It's too early to tell" and that "[i]t could go either way, though." MC Opp. Ex. 17 (Hausman 1/26/05 Tr.) at 429.

Although projections regarding consumer harm may have been sufficient for the purposes of the DOJ Action, in this private action for billions of dollars in *damages*, MasterCard and Visa should be allowed to present the new real world evidence developed in the course of this litigation pertaining to the issue of consumer harm.

As another example, evidence that was not before the Court in the DOJ Action supports MasterCard's procompetitive justification for the adoption and enforcement of the CPP. Specifically, the evidence reveals that MasterCard's fears about bank issuers free-riding on MasterCard's assets were well-founded.

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These programs, which offer nothing new or innovative, threaten to reduce the incentives of MasterCard and Visa to invest in their merchant acquiring network.

While the degree of prediction and forecasting present in the prior action was unavoidable where real-world evidence was nonexistent or unavailable, to preclude MasterCard

from fully litigating and presenting this newly-available evidence to the jury would be patently unfair.

(2) Collateral Estoppel Should Be Denied On Issues Of Market Power And Market Definition In Light Of Changes In Economic Literature and New Evidence

Discover seeks to estop MasterCard from litigating issues related to market power and market definition. In finding market power in the DOJ Action, the Court and the Second Circuit relied heavily on the notion that "both Visa and MasterCard have recently raised interchange rates charged to merchants a number of times, without losing a single merchant customer as a result." *Visa U.S.A.*, 163 F. Supp. 2d at 340; *Visa U.S.A.*, 344 F.3d 239-40. However, economic scholarship regarding two-sided platforms (such as payment card networks) that has developed since the DOJ Action undermines this analysis. While the concept of two-sided platforms had been introduced in the economic literature prior to the DOJ Action, the vast majority of literature on two-sided platforms was produced after 2001. *See, e.g.*, MC Opp. Ex. 27 (Hubbard Report) at ¶ 22 (discussing literature); *see also* MC Opp. Ex. 35; MC Opp. Ex. 20; MC Opp. Ex. 36. According to the new scholarship, in a competitive two-sided market, rising prices on one side of the market are consistent with a competitive market in which those higher prices expand output by lowering prices and stimulating demand on the other side of the market. *See* MC Opp. Ex. 27 (Hubbard Report) at ¶¶ 18-36.

Based on the evolving scholarship on how to analyze two-sided platforms, both the DOJ's expert Professor Katz and Discover's expert Professor Hausman recently testified in other proceedings that increasing interchange rates was not indicative of an exercise of market power by a large PIN debit network. *See* MC Opp. Ex. 37 at 107 (Professor Katz: "[U]ltimately [the] interchange fee is driven by competition to attract the issuers, to attract merchants, and,

again . . . one of our points [is] that the increases in interchange fees that we have been seeing is a result not of the exercise of market power, but it is the result of competition. . . ."); *id* at 142 (Professor Hausman: explaining that basing a finding of market power on increasing interchange is "confusing competition for getting banks with what looks like what a monopolist might otherwise be."); *id.* at 152 (Professor Hausman: "The problem is that what is actually competition which is trying to get issuers by raising the interchange. If you only look at the other side of the market, looks like you are exciting market power . . . .").

Nonetheless, Discover continues to argue that increases in interchange rates constitute evidence of market power. *See, e.g.*, MC Opp. Ex. 10 (Hausman Report) at ¶ 80. The jury should have the benefit of considering this new analytical framework in assessing the issue of market power at trial, and Discover's motion should be denied with respect to market power on that basis. *See, e.g., Continental Airlines, Inc. v. Am. Airlines, Inc.*, 824 F. Supp. 689, 712-13 (S.D. Tex. 1993) (collateral estoppel as to relevant market finding inappropriate where, at time of first decision, conceptual framework for understanding competition at hub and individual airport level was not well known); *Clark v. SmithKline Beecham*, No. 7:06-cv-30 (HL), 2006 WL 3329141, at *3 (M.D. Ga. Nov. 16, 2006) (noting that a grant of collateral estoppel would "freeze science in place from a[n] [earlier] verdict without taking into account subsequent advances").

In addition, collateral estoppel should not be applied to issues of market definition in light of developments in the payments industry since the DOJ Action. In the DOJ Action, this Court determined that debit cards should not be included in the general purpose credit and charge card market it found, on the basis that "[c]onsumers . . . do not consider debit cards to be substitutes for general purpose cards." *Visa U.S.A.*, 163 F. Supp. 2d at 336-37. However,

during the seven years since the DOJ Action, consumers' use of debit cards has continued to evolve and there is now substantial new evidence that consumers view debit and credit cards as reasonably interchangeable. *See, e.g.*, MC Opp. Ex. 38 at DFSHC 002451907-08, 918 (2002 Discover Debit Card Business Plan noting that "more consumers are beginning to pay with their offline debit cards for purchases that were traditionally conducted with credit cards;" and projecting debit payments will continue to grow 10-20% annually); MC Opp. Ex. 39 at VUSA 113717010 (Wall Street research report showing that total debit volume from 2003-2005 increased from $589 billion to $842 billion, with year-over-year growth in 2004 and 2005 at 24% and 15%, respectively). Indeed, even Discover's CEO now concedes that credit and debit are "not necessarily" in separate categories:

> [S]ignature debit that run on the exact same networks and have the same acceptance, has a lot of similarities to a credit card . . . in all other aspects, material aspects, it's the same. . . . I think on the issuing side, again a customer can choose to use their debit card versus a credit card sometimes.

MC Opp. Ex. 13 (Nelms 5/15/07 Tr.) 52-54

In light of this new evidence, collateral estoppel on the issue of market definition is unwarranted, and the jury should be allowed to consider this evidence. *Coburn v. Smithkline Beecham Corp.*, 174 F. Supp. 2d 1235, 1240 (D. Utah 2001) ("[I]t would be unjust to freeze in time the answers to these questions when the resolution of these questions . . . will be decided upon the basis of. . . knowledge as it exists at the time of trial.").

(3) Estoppel Would Cause Juror Confusion And Substantially Distort The Resolution Of Closely Related Issues

Discover's request for offensive collateral estoppel should also be denied because estoppel would inevitably cause juror confusion and substantially distort the record in Discover's favor. As emphasized by the Second Circuit, offensive collateral estoppel must be applied carefully in recognition that it "may have a devastating impact on a civil litigant's constitutional right to a jury trial." *See Monarch Funding Corp.*, 192 F.3d at 304. The Second Circuit's concern applies with special force where, as here, there are closely-related issues remaining for resolution, because the risks of having the "precluded" issues from an earlier trial distort the jury's resolution of the "open" ones.

For instance, in a leading case, a district court rejected a request to give preclusive effect to findings from a prior bench trial, fearing the risk of plaintiffs "unduly swaying or confusing the jury" through the skillful use of the earlier findings. *See Whelan v. Abell*, 953 F.2d 663, 669 (D.C. Cir. 1992). In affirming the lower court, the D.C. Circuit acknowledged the heightened risks of unfairness when bench findings are offered in a subsequent jury trial:

> A ruling for the Whelans on issue preclusion might have given them a head start larger than warranted in the jury's deliberations. The [district] judge, in other words, indicated concern not simply about the difference in factfinders; rather, his practical judgment turned on the prospect of skewing or distorting the jury's judgment in the particular setting before him. We cannot say that it was unsound for the district judge . . . to exercise his discretion in favor of allowing both sides to submit their full case to the jury's judgment.

Id.; *see also Phonetele*, 1984 WL 2943, at *5 (offensive collateral estoppel rejected in Sherman Act litigation because "the application of issue preclusion to the questions . . . would make a fair resolution of the remaining questions unacceptably difficult"); Wright et. al., § 4465, at 738-39 (noting that "preclusion on one issue while closely related issues must be tried may substantially

distort decision of the issues that remain open" and which "must be tried in any event"); *id.* § 4465.2, at 757 (stating that courts should "consider the nature of jury trial in determining whether to permit nonmutual preclusion"). Here, even if the Court granted collateral estoppel, Discover will still need to prove and defend its damages as to all of its claims. Because issues related to damages substantially overlap with issues on which Discover seeks preclusion, the potential for confusing or unduly swaying the jury or otherwise distorting the record is unacceptably high. This problem could also cause distortion of the jurors' views of the evidence relating to the new claims, including inter-association conspiracy, debit, and Section 2 claims.

Moreover, significant juror confusion could result from applying collateral estoppel to the issue of market definition. If this Court grants preclusion on the existence of a general purpose credit and charge card market and related network services market, in deciding the separate debit card and related network services markets, the jurors' consideration of the evidence will be clouded by the collateral estoppel with respect to the credit-related markets.

(4) Collateral Estoppel Is Unfair Because Discover Is Seeking To Establish Facts Contradicted By Its Own Executives During The DOJ Action

Granting collateral estoppel on the issue of injury to Discover—aside from being unwarranted on lack of identity of issues and necessity grounds—would be unfair because Discover is now advocating a theory of injury that is contradicted by statements it made before this Court during the DOJ Action regarding the impact of the CPP and By-law 2.10(e).

Specifically, during the DOJ Action—before this Court at trial, in depositions, and in court submissions—Discover maintained that the elimination of the CPP and By-law 2.10(e) *alone* would leave Discover "hampered in its ability attract third party issuing banks" and "severely compromised in its ability to build transaction volume and merchant acceptance." *See,*

e.g., MC Opp. Ex. 7 at 21, 53. Indeed, Discover argued repeatedly that the greatest harm it suffered resulted from rules that prevented Discover from acting as an acquirer for Visa and MasterCard and from acquiring Visa and MasterCard portfolios and running them on the MasterCard or Visa networks, *see, e.g.*, MC Opp. Ex. 31 (Nelms 1/5/00 Tr.) 80-81; *see also* MasterCard S.J. Br. 19-22 (and materials cited therein), and that any remedy that failed to address these additional rules and policies but eliminated the CPP and By-law 2.10(e) was likely to make Discover competitively *worse off*.

If collateral estoppel were granted, defendants would be severely prejudiced because they would be precluded from presenting this stark contradiction to the jury.

IV. COLLATERAL ESTOPPEL IS NOT WARRANTED ON THE EIGHTY-ONE INDIVIDUAL STATEMENTS IN ATTACHMENT A TO DISCOVER'S MOTION

In addition to seeking estoppel on liability issues related to Claim One, Discover seeks estoppel on eighty-one individual statements from the DOJ Action, which are listed in Attachment A to Discover's motion. For each of these statements, Discover bears the burden of proving with "clarity and certainty" each of the necessary elements before collateral estoppel may be applied. *See Postlewaite v. McGraw-Hill*, 333 F.3d 42, 49 (2d Cir. 2003). Discover has not even attempted to do so here. Rather, Discover asserts *in a single sentence* that the collateral estoppel elements have been met for all of these statements because each statement was "exhaustively litigated" and necessary to the judgment because the statements "support" the Court's conclusions. However, as discussed in Section II.B, statements that are merely "supportive" of a judgment may not be necessary to it, and thus, even Discover's proposed standard (which it does not even apply) is infirm. *See Microsoft*, 355 F.3d at 325 ("the 'supportive of' standard is not the appropriate standard for applying collateral estoppel").

Discover has failed to sustain its burden and its motion should be denied as to all eighty-one statements on that basis.

Even if Discover had attempted to articulate whether any of the statements in Attachment A satisfy the proper requirements, which it has not, collateral estoppel would still be unwarranted for the reasons stated throughout this memorandum. By way of example:

- Many of Discover's proffered assertions—including those it claims show harm to Discover—were not addressed by the Second Circuit and therefore were not "necessary" to the final judgment. *See, e.g.*, Discover Br., Att. A at ¶¶ 38, 40, 41, 43, 45, 46-50, 54-59, 70, 71 & 74-81; *see also* Section II *supra*.

- MasterCard and Visa should not be precluded from litigating statements Discover claims demonstrate harm to competition. New real world evidence demonstrates that consumers will not benefit from third party issued Discover cards. *See, e.g.*, Discover Br., Att. A at ¶¶ 21, 23-29 & 31-34; *see also* Section III.B.1 *supra*.

- MasterCard and Visa should not be precluded from litigating the individual statements Discover claims relate to market power and market definition, in light of the new scholarship and new evidence. *See, e.g.*, Discover Br., Att. A at 2-20; *see also* Section III.B.2 *supra*.

- In light of real world evidence of actual free-riding, MasterCard and Visa should not be precluded from litigating the statements regarding the CPP's procompetitive justification. *See, e.g.*, Discover Br., Att. A at 70 & 71; *see also* Section III.B.1 *supra*.

Accordingly, the Court should deny Discover's request that it collaterally estop MasterCard and Visa from litigating the eighty-one statements contained in Attachment A to its motion.[18]

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[18] MasterCard reserves the right to rebut any attempt by Discover to establish that any of the particular findings in Attachment A satisfy the collateral estoppel requirements.

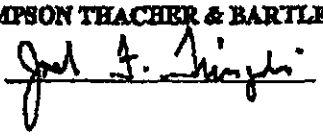
CONCLUSION

For the foregoing reasons, MasterCard respectfully requests that the Court deny Discover's motion for partial summary judgment.

Dated: New York, New York
March 24, 2008

Respectfully submitted,

SIMPSON THACHER & BARTLETT LLP

By: 

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APPENDIX A

ILLUSTRATIVE FACTUAL ASSUMPTIONS MADE BY DISCOVER'S EXPERT PROFESSOR HAUSMAN IN HIS OPINIONS RELATED TO DAMAGES

- In addition to the direct effect of additional issuing (and transaction volume) increasing output over the Discover network, those volumes would have resulted in greater merchant acceptance of Discover. Those volumes would have enabled the use of third-party acquirers, which would have accelerated Discover's ability to close the merchant acceptance gap in the United States. Greater merchant acceptance of Discover, in turn, would have led to greater issuing and usage in a self-reinforcing cycle. (MC Ex. Opp. 10 (Hausman Report) at ¶ 116)

- Some banks wanted to compete and differentiate themselves by issuing a Discover branded credit card. This new product variety would have intensified competition in the issuing market. (*Id.* at ¶ 117).

- Entry by Discover with an innovative offering in the mid-1990s could have spurred such competition between debit issuers. (*Id.* at ¶ 119).

- As discussed throughout this report, in the absence of the exclusionary rules, Discover would have entered into third-party issuing deals with Visa and MasterCard member banks. In the credit and charge card network services market, Discover would have attracted third-party credit card issuers with its differentiated network offering (which I discuss in detail below). (*Id.* at ¶ 125).

- As discussed throughout this report, in the debit market, Discover would have entered into issuing agreements driven, in part, by its innovative signature debit network offering. Discover would have offered expertise and brand awareness in the area of cash rewards. Discover Network also would have offered cash at the point-of-sale functionality, and superior fraud control. All of these functions would have been attractive to banks seeking ways to protect the greater interchange revenue associated with signature debit. (*Id.* at ¶ 126).

- In my opinion, absent the exclusionary rules, Discover would have closed the merchant acceptance gap between it and Visa and MasterCard in the United States by the late 1990s. (*Id.* at ¶ 129).

- The enhanced network acceptance, in turn, would have improved Discover's competitiveness as an issuer. With greater merchant acceptance, there would have been more spending and larger balances per account on Discover Cards. This loss of increased volume and revolving balances due to having a weaker network because of lesser merchant acceptance harmed Discover. (*Id.* at ¶ 130).

- My framework quantifies Discover's damages by examining the business opportunities and strategies that Discover would likely have pursued and implemented in a world without the exclusionary rules. (*Id.* at ¶ 149).

- In the first alternative [damages model], Discover enters into deals with credit card issuers in the but-for world. Discover would have earned margins on these third-party issuing deals, and I estimate the lost profits from a network perspective. The volumes from these deals, in turn, would have enabled Discover to close the domestic merchant acceptance gap. Reducing the acceptance gap also results in damages to Discover's network and issuing businesses as holders of the Discover Card would have used their cards more and carried greater revolving balances if Discover had been more widely accepted. (*Id.* at ¶ 150).

- In the second alternative [damages model], Discover enters into a joint venture deal with Citibank, a prospective deal discussed between the parties in the actual world. While other credit card third-party issuing on the network would likely have occurred under this but-for alternative, I focus on estimating the additional profits Discover would have enjoyed had the exclusionary rules not existed and the parties been able to enter into a joint venture agreement in the but-for world. (*Id.* at ¶ 151).

- Given this state of readiness, it is reasonable to conclude that in the but-for world Discover would have already begun marketing its network services to prospective issuers and that third-party issuing on the network would have occurred by 1995. (*Id.* at ¶ 154).

- Shortly after the exclusionary rules were eliminated in October 2004, Discover (1) acquired a PIN debit network, and (2) developed and launched a signature debit network offering. Discover did so even though the prospects of succeeding in the debit network services market were much less favorable in 2005-06 than they would have been in 1994-95 when the debit markets were highly fluid and relatively undeveloped. I therefore assume that Discover would have also developed and begun to execute a debit strategy in 1994-95. (*Id.* at ¶ 155).

- Discover would have shown greater flexibility in working with issuers in terms of branding and merchant pricing. Flexibility on branding also would have been attractive to issuers because some, REDACTED were looking for network branding that would not compete with their efforts to differentiate via their own branding. This exclusive merchant acceptance would have differentiated the network, as issuing on Discover would have meant incremental volumes for the issuer through access to these exclusive accounts. The closed loop—which gives Discover the ability to capture unique information from merchants and create card programs that are limited to select merchants—is another differentiator that Discover could have used to attract third-party issuers. (*Id.* at ¶ 160).

- Discover, therefore, likely would have offered banks a very attractive, differentiated signature debit network platform. (*Id.* at ¶ 169).

- Discover's relative lack of international acceptance would not have been a serious impediment to such a debit network strategy. (*Id.* at ¶ 170).

- Fourth, the differentiating value proposition for Discover (e.g., rewards, value, cash over, merchant exclusives, flexibility, etc.) would have had more value in the 1990s before the associations and banks began more fully emulating Discover's innovations in these areas. (*Id.* at ¶ 174).

- My general principal in calculating network margins from third-party issuing is to assume that Discover would have offered a financial package to issuers (interchange and incentives net of fees and assessments) that would have been competitive with offers from Visa and MasterCard. (*Id.* at ¶ 178).

- While Discover's merchant discount rates would have been below those of Visa's or MasterCard's in the but-for world, Discover would have offered competitive economics to issuers and earned a margin on network volumes. (*Id.* at ¶ 180).

- Second, greater issuing volumes would have permitted Discover to use third-party acquirers to accelerate its ability to gain domestic parity. Third-party acquirers could more cost effectively acquire small merchants for Discover because the marginal costs of adding Discover acceptance to existing accounts for the third-party acquirer was less than the costs to Discover of acquiring such accounts on its own. As a result, third-party acquirers could have offered Discover a distinct cost advantage. (*Id.* at ¶ 186).

- Moreover, the use of third-party acquirers would have substantially enhanced Discover's ability to reach the millions of small merchants that are difficult for a network to reach with its own sales force. (*Id.* at ¶ 186).

- In the but-for world, with third-party acquiring, Discover would have been able to choose the more economically efficient strategy of relying on third-party acquirers. (*Id.* at ¶ 194).

- In addition, improved merchant acceptance would lead to greater activation of inactive Discover Card accounts. (*Id.* at ¶ 203).

- I also have evaluated whether third-party issuing on Discover's credit card network would have had a cannibalization effect on Discover's issuing business. In my opinion, such cannibalization would not have had a significant effect on Discover's issuing business for several reasons. (*Id.* at ¶ 208).

- Given greater acceptance, some of those cardholders would have begun to use the Discover Card as their primary card, leading to greater spend. (*Id.* at ¶ 253).

- During the relevant time frame, Discover had discussions with various entities in the payments industry about a wide range of deals each of which would have transformed

Discover's business. These discussions included discussions with REDACTED REDACTED . In the but-for world, it is reasonable to believe that one of these deals might have occurred, and that it would have resulted in a network that would have been attractive to third-party issuers. REDACTED

- In a but-for world without the exclusionary rules, I assume that the Project Explorer negotiations would have involved the parties pursuing the Cross Sell option given its higher economic value. To model the damages from this particular option, I make use of the modeling and valuations that Discover and Citibank prepared at the time. Both parties prepared estimates of the value to each party of implementing Project Explorer, and of the total value they expected to be created by the project. Much of the modeling was focused on the Big Bang option, but the modeling can be modified to analyze the Cross Sell option. (*Id.* at ¶ 266).

- If Discover had a strong differentiating appeal in 2006, it must also have had one in 1995. (MC Opp. Ex. 22 (Hausman Rebuttal Report) at ¶ 122).

- Discover's [m]erchant [d]iscount [r]ate [w]ould [h]ave [b]een [h]igher in the [b]ut-[f]or [w]orld. (*Id.* at VIII, C(i))

- By contrast, in the but-for world (as with the post-2004 actual world) several things would have changed: (1) Discover would have more actual and prospective volume on its network; (2) Discover would be able to rely upon third-party acquirers to obtain the merchants Discover could not economically directly acquire; (3) Discover would have adopted a more open payment network model where it would have sought to earn sufficient merchant discount fee income to compensate third-party issuers. (*Id.* at ¶ 213).

- Many banks, however, would have been interested in issuing on the Discover network in the but-for world. Some issuers would have opted not to enter into dedication agreements, in much the same way that REDACTED has elected to maintain complete flexibility to issue over any of the various networks in the actual world. Other issuers would have likely insisted that the dedication agreement be structured to give them freedom to segment their credit card issuing and issue cards on the Discover and American Express networks. I would expect the very banks that would have been most interested in issuing on the Discover network would be those banks that would have insisted on this flexibility. (*Id.* at ¶ 253).

- Discover's historical lack of merchant acceptance parity made it subject to adverse selection. It has tended to have a higher charge-off rate than it otherwise would have because it has tended to attract cardholders of higher average credit risk. (*Id.* at ¶ 307).

- As Discover's merchant acceptance nears parity, its issuing product will improve and it will be less susceptible to adverse selection, improving the charge-off rate. (*Id.* at ¶ 308).

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

DISCOVER FINANCIAL SERVICES, DFS SERVICES, LLC, AND DISCOVER BANK,	Case No. 04-CV-07844 (BSJ) (DFE)
Plaintiffs,	ECF CASE
v.	
VISA U.S.A. INC., et al.,	
Defendants.	

CERTIFICATE OF SERVICE

I am a resident of the State of New York, over the age of eighteen years. My business address is Simpson Thacher & Bartlett LLP, 425 Lexington Avenue, New York, NY 10017. On March 24, 2008, I served the following document(s): DECLARATION OF JOSEPH F. TRINGALI IN SUPPORT OF MASTERCARD INCORPORATED'S AND MASTERCARD INTERNATIONAL INCORPORATED'S OPPOSITION TO DISCOVER'S MOTION FOR PARTIAL SUMMARY JUDGMENT; MASTERCARD INCORPORATED'S AND MASTERCARD INTERNATIONAL INCORPORATED'S MEMORANDUM IN OPPOSITION TO DISCOVER'S MOTION FOR PARTIAL SUMMARY JUDGMENT; AND MASTERCARD INCORPORATED'S AND MASTERCARD INTERNATIONAL INCORPORATED'S LOCAL RULE 56.1(b) STATEMENT IN RESPONSE TO DISCOVER'S LOCAL RULE 56.1(a) STATEMENT.

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

Executed on March 24, 2008, New York, NY.

Brittany Ori

Litigation Paralegal