No. 15-1672

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA, *et al.*,
Plaintiffs-Appellees,

v.

AMERICAN EXPRESS COMPANY, *et al.*
Defendants-Appellants,

(Full caption commences on inside cover)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NEW YORK

BRIEF FOR AMICI CONSUMER ACTION AND U.S. PUBLIC INTEREST RESEARCH GROUP IN SUPPORT OF PETITION FOR PANEL REHEARING AND REHEARING EN BANC

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UNITED STATES OF AMERICA, STATE OF MARYLAND, STATE OF MISSOURI, STATE OF VERMONT, STATE OF UTAH, STATE OF ARIZONA, STATE OF NEW HAMPSHIRE, STATE OF CONNECTICUT, STATE OF IOWA, STATE OF MICHIGAN, STATE OF OHIO, STATE OF TEXAS, STATE OF ILLINOIS, STATE OF TENNESSEE, STATE OF MONTANA, STATE OF NEBRASKA, STATE OF IDAHO, STATE OF RHODE ISLAND,

Plaintiffs-Appellees,

STATE OF HAWAII,

Plaintiff,

-v.-

AMERICAN EXPRESS COMPANY and AMERICAN EXPRESS TRAVEL RELATED SERVICES COMPANY, INC.,

Defendants-Appellants,

MASTERCARD INTERNATIONAL INCORPORATED and VISA INC.,

Defendants,

CVS HEALTH, INC., MEIJER, INC., PUBLIX SUPER MARKETS, INC., RALEY'S, SUPERVALU, INC., AHOLD U.S.A., INC., ALBERTSONS LLC, THE GREAT ATLANTIC & PACIFIC TEA COMPANY, INC., H.E. BUTT GROCERY CO., HYVEE, INC., THE KROGER CO., SAFEWAY INC., WALGREEN CO., RITE-AID CORP., BI-LO LLC, HOME DEPOT USA, INC., 7-ELEVEN, INC., ACADEMY, LTD., DBA ACADEMY SPORTS + OUTDOORS, ALIMENTATION COUCHE-TARD INC., AMAZON.COM, INC., AMERICAN EAGLE OUTFITTERS, INC., ASHLEY FURNITURE INDUSTRIES INC., BARNES & NOBLE, INC., BARNES & NOBLE COLLEGE BOOKSELLERS, LLC, BEALL'S, INC., BEST BUY CO., INC., BOSCOVS, INC., BROOKSHIRE GROCERY COMPANY, BUC-EE'S LTD, THE BUCKLE, INC., THE CHILDRENS PLACE RETAIL STORES, INC., COBORNS INCORPORATED, CRACKER BARREL OLD COUNTRY STORE, INC., D'AGOSTINO SUPERMARKETS, INC., DAVIDS BRIDAL, INC., DBD, INC., DAVIDS BRIDAL CANADA INC., DILLARD'S, INC., DRURY HOTELS COMPANY, LLC, EXPRESS LLC, FLEET AND FARM OF GREEN BAY,

FLEET WHOLESALE SUPPLY CO. INC., FOOT LOCKER, INC., THE GAP, INC., HMSHOST CORPORATION, IKEA NORTH AMERICA SERVICES, LLC, KWIK TRIP, INC., LOWE'S COMPANIES, INC., MARATHON PETROLEUM COMPANY LP, MARTIN'S SUPER MARKETS, INC., MICHAELS STORES, INC., MILLS E-COMMERCE ENTERPRISES, INC., MILLS FLEET FARM, INC., MILLS MOTOR, INC., MILLS AUTO ENTERPRISES, INC., WILLMAR MOTORS, LLC, MILLS AUTO ENTERPRISES, INC., MILLS AUTO CENTER, INC., BRAINERD LIVELY AUTO, LLC, FLEET AND FARM OF MENOMONIE, INC., FLEET AND FARM OF MANITOWOC, INC., FLEET AND FARM OF PLYMOUTH, INC., FLEET AND FARM SUPPLY CO. OF WEST BEND, INC., FLEET AND FARM OF WAUPACA, INC., FLEET WHOLESALE SUPPLY OF FERGUS FALLS, INC., FLEET AND FARM OF ALEXANDRIA, INC., NATIONAL ASSOCIATION OF CONVENIENCE STORES, NATIONAL GROCERS ASSOCIATION, NATIONAL RESTAURANT ASSOCIATION, OFFICIAL PAYMENTS CORPORATION, PACIFIC SUNWEAR OF CALIFORNIA, INC.,
P.C. RICHARD & SON, INC., PANDA RESTAURANT GROUP, INC., PETSMART, INC., RACETRAC PETROLEUM, INC., RECREATIONAL EQUIPMENT, INC., REPUBLIC SERVICES, INC., RETAIL INDUSTRY LEADERS ASSOCIATION, SEARS HOLDINGS CORPORATION, SPEEDWAY LLC, STEIN MART, INC., SWAROVSKI U.S. HOLDING LIMITED, WAL-MART STORES INC., WHOLE FOODS MARKET GROUP, INC., WHOLE FOODS MARKET CALIFORNIA, INC., MRS. GOOCH'S NATURAL FOOD MARKETS, INC., WHOLE FOOD COMPANY, WHOLE FOODS MARKET PACIFIC NORTHWEST, INC., WFM-WO, INC., WFM NORTHERN NEVADA, INC., WFM HAWAII, INC., WFM SOUTHERN NEVADA, INC., WHOLE FOODS MARKET, ROCKY MOUNTAIN/SOUTHWEST, L.P., THE WILLIAM CARTER COMPANY, YUM! BRANDS, INC., and SOUTHWEST AIRLINES CO.

Movants.

CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 16.1 of the Federal Rules of Appellate Procedure, Consumer Action and U.S. Public Interest Research Group, by and through their undersigned counsel, hereby certify that they have no parent corporation and that no publicly held corporation owns 10% or more of their stock.

STATEMENT OF CONSENT TO FILE AMICUS

I, Sharon K. Robertson, am admitted to practice in this Court and have obtained consent from all parties to submit this Amicus Curiae brief in support of Appellees petition for panel rehearing and rehearing *en banc*.

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INTERESTS OF AMICI[1]

Amici curiae, Consumer Action and U.S. Public Interest Research Group, are two leading consumer advocacy groups whose decades of collective experience advocating for consumers make them qualified to assist the Court in understanding the substantial public interest advanced by the challenge to American Express's ("Amex") nondiscrimination provisions ("NDPs"). Amici have broad knowledge about the history of credit cards and are well qualified to assist the Court in understanding how the public interest, and consumer interests in particular, are undermined by the challenged provisions. As discussed below, empirical evidence provides strong support for granting rehearing *en banc* to reverse the Panel's ruling.

ARGUMENT

Rehearing *en banc* is warranted for issues of "exceptional importance." Fed. R. App. P. 35(a)(2). This case presents just such an issue.

The Panel's decision, reversing the district court's well-reasoned decision finding Amex's NDPs anticompetitive and enjoining Amex from enforcing the same, should be reinstated. Absent these NDPs, Plaintiffs have alleged, and *Amici* agree, merchants would be able to use steering "at the point of sale to foster competition on price and terms among sellers of network services" by encouraging

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[1] Pursuant to Fed. R. App. P. 29(c), amici state that no counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief.

the use of less expensive or preferred cards by customers. App. 136. Although the Panel reasoned that NDPs ultimately benefit consumers, the facts are to the contrary. Indeed, NDPs prevent merchants from passing on costs in a sensible manner that could introduce price competition among payment systems. As the District Court found, the results are higher general retail prices and interchange fees, which are extremely detrimental to American consumers. *See United States v. Am. Express Co.*, 88 F. Supp. 3d 143, 216-217 (E.D.N.Y. 2015)

I. NONDISCRIMINATION PROVISIONS FORCE MERCHANTS TO RECOUP SUPRA-COMPETITIVE FEES BY RAISING STICKER PRICES FOR ALL CONSUMERS.

The purpose and practical effect of NDPs is to conceal the underlying true costs of credit by spreading those costs among all consumers. Every time a consumer uses a credit card, the merchant generally pays 1–4%[2] of the transaction value in "merchant fees," most of which go to the issuing bank as "interchange fees."[3] Interchange fees in America are the highest in the world, generating approximately 50 billion dollars per year for credit card issuers, with more than

[2] *See* Elizabeth Warren, *Antitrust Issues in Credit Card Merchant Restraint Rules*, Tobin Project Risk Policy Working Group, 1 (May 6, 2007).

[3] *See* Adam J. Levitin, *Priceless? The Economic Costs of Credit Card Merchant Restraints*, 55 UCLA L. Rev. 1321 (2008).

200 million dollars of it from federal agencies alone.[4] The interchange fee rates jumped 23% between 2000 and 2006, but because the volume of credit card transactions also increased dramatically, the absolute cost of interchange fees for merchants increased 139% during the same period.[5] "For many merchants, credit card acceptance has become the fastest growing cost of doing business."[6]

NDPs are the reason that credit cards are increasing in use despite being "more expensive on average for merchants than cash and checks."[7] By preventing merchants from communicating fees to the consumers who choose to use credit cards and returning a small portion of these revenues in the form of rewards to a fraction of consumers, credit card companies have constructed a system whereby consumers actively, and unknowingly, choose the most costly payment system.

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[4] *See, e.g.*, Keith Bradsher, *U.S. Looks to Australia on Credit Card Fees*, N.Y. Times (Nov. 24, 2009), *available at* http://www.nytimes.com/2009/11/25/your-money/credit-and-debit-cards/25card.html?pagewanted=all; Andrew Martin, *Card Fees Pit Retailers Against Banks,* N.Y. Times (July 15, 2009), *available at* http://www.nytimes.com/2009/07/16/ business/16fees.html.

[5] Levitin, *supra* note 3, at 1345.

[6] Levitin, *supra* note 3, at 1345 (citing *Financial Services Issues: A Consumer's Perspective, Hearing Before the Subcomm. on Financial Institutions and Consumer Credit of the H. Comm. on Financial Institutions,* 108th Cong. 115 (2004) (statement of John J. Motley III, Sr. Vice President, Food Marketing Institute)).

[7] David S. Evans & Richard Schmalensee, Interchange Fees in Credit and Debit Card Industries, Proceedings of the 2005 Federal Reserve Bank of Kansas City Conference, *The Economics of Interchange Fees and Their Regulation: An Overview*, 96 (2005), *available at* https://www.kansascityfed.org/publicat/pscp/2005/Evans-Schmalensee.pdf.

Increased fees to merchants fuel greater profits to credit card companies, who use a portion of the fees to provide greater rewards, which fuel greater use and higher profits, in a race to the top—precisely the opposite of competitive pricing. *See Am. Express Co.*, 88 F. Supp. 3d at 215-16.

The restraint on merchants has led to increased retail sticker prices and a massive cross-subsidy among consumers. As Elizabeth Warren has put it: these types of provisions force merchants "to charge *all* consumers higher prices in order to cover the costs of accepting credit card transactions. As a result, non-credit consumers end up subsidizing credit card consumers and, indirectly, subsidizing the entire credit card industry."[8]

The available empirical studies suggest these effects are not negligible. A study of gas station pricing in 1989—when fees were far lower—showed that at stations which maintained unified pricing, cash consumers paid a 1.5% premium over the national averages to subsidize a discount from cost to credit card users of 2%-3.5%.[9] The estimated overall cross-subsidy is staggering: "The average cash-

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[8] Warren, *supra* note 1, at 1.

[9] *See* Adam J. Levitin, *The Antitrust Superbowl: America's Payment System, No-Surcharge Rules, and the Hidden Costs of Credit*, 3 Berkeley Bus. L.J. 265, 274 n.27 (2005) (citing John M. Barron et al., *Discounts for Cash in Retail Gasoline Marketing*, 10 Contemp. Econ. Issues 89, 102 (1992)). In Delaware, all customers paid an extra 1.82¢ per gallon so that credit customers could pay 2.37¢ less per gallon than cost. *Id.* at 302-03. The cash consumer therefore bore between 30%-
(continued…)

paying household transfers $149 . . . annually to card users [each of whom] receives a[n average] subsidy of $1,133 . . . annually from cash users."[10]

Although the Panel credited an increase in merchant fees as benefitting consumers by funding "increased cardholder rewards," the recent explosion in rewards card programs has exacerbated the problem of hidden cross-subsidies. Because NDPs forbid merchants from communicating truthfully about fees, they must increase prices to all consumers to recoup the costs of increasingly profitable networks and their generous, high-end rewards programs. *See Am. Express Co.*, 88 F. Supp. 3d at 216-217. "Rewards cards have risen from less than 25 percent of new card offers in 2001 to nearly 60 percent in 2005" and now are considered to "drive the growth in . . . all credit card usage."[11] The power of rewards to increase credit card usage—though vitally, not to increase overall consumer spending—is closely tied with increases in interchange revenue. In fact, rewards cards and corporate cards can cost merchants twice as much in fees as other credit cards.[12]

Far from being a problem for credit card networks, the across-the-board price increases work in their favor: "Card networks have the incentive to charge

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43% of the marginal cost to the merchant of the costs imposed by credit card transactions. *Id*.

[10] Scott Schuh et al., Federal Reserve Bank of Boston, *Who Gains and Who Loses from Credit Card Payments? Theory and Calibrations*, 21 (2010).

[11] Levitin, *supra* note 3, at 1344–46.

[12] Levitin, *supra* note 3, at 1323.

high interchange fees to inflate retail prices so that they can create more demand for their services . . . . As the card payments become more efficient and convenient than alternatives, the card networks are able to further raise the interchange fees, inflate the value of transactions and hence extract more profits" without lifting consumer surplus and merchant profits.[13] Neither merchants nor non-credit card users gain any marginal benefit from these high-end rewards cards, but they both end up footing the bill for immense credit card company profits, and the generous rewards they provide to a tiny segment of consumers. NDPs effectively gag merchants and deny consumers vital information, ensuring that cards are never put into serious price competition with each other or with other payment systems.

II. THE PANEL'S DECISION ELEVATES AMEX'S INTERESTS ABOVE THOSE OF MERCHANTS AND CARDHOLDERS.

In analyzing NDPs, the Panel vastly overemphasized the importance of retaining customers by increasing "merchant fees to fund the increased cardholder rewards." This theory can only be employed as a defense of NDPs by elevating the interests of Amex above those of merchants and cardholders. In fact, as explained below, if prohibiting NDPs caused a decrease in credit card usage, it undoubtedly would increase overall consumer welfare.

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[13] Zhu Wang, *Market Structure and Credit Card Pricing: What Drives the Interchange?*, 28 Int'l J. of Indus. Org. 86, 93 (2010), *available at* http://www.frbatlanta.org/news/CONFEREN/08payments/08payments_Wang.pdf.

A. Reducing Interchange Fees Provides Competitive Benefits for Consumers and Merchants.

Prohibiting NDPs will create genuine competition between payment systems, benefiting debit card users and driving down merchant fees for everyone. If NDPs are necessary to maintain Amex's position vis-à-vis other payment systems (and the District Court found they are not), the NDPs are preserving a market failure that substantially harms consumers. *See Am. Express Co.*, 88 F.Supp.3d at 230. In fact, the most likely outcome of allowing merchants to communicate fees and potential avenues for savings is a reduction in fees as credit cards are forced to compete on price. NDPs may be vital to the preservation of supracompetitive profit margins for Amex, but there is no economic theory that can twist this interest into a pro-consumer justification.

B. Overconsumption of Credit Card Debt Causes Uniquely Harmful Social Externalities.

The Panel's supposedly pro-consumer defense of NDPs based on spurring expanded use of credit cards and rewards programs is radically out of step with the facts of credit card debt. Credit card debt in America was $870 billion by May of 2012.[14] "Americans racked up nearly $48 billion in new credit card debt in 2011, 424 percent more than 2010, and 577 percent more than 2009. Although total

[14] The Associated Press, *Consumers Take on More Debt*, N.Y. Times (July 9, 2012), *available at* http://www.nytimes.com/2012/07/10/business/credit-card-debt-climbed-by-8-million-in-may.html?_r=0.

outstanding credit rose only about $4 billion, that number was offset by the magnitude of consumer defaults—*$44.2 billion worth.*" [15] Thus, a reduction in the growth of credit card debt would be a highly desirable side effect.

CONCLUSION

The Court should grant panel rehearing and rehearing *en banc*.

Dated: November 21, 2016

Respectfully submitted,

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[15] Meg Handley, *Consumers Still Buried In Credit Card Debt*, U.S. News and World Report (Mar. 12, 2012), *available at* http://www.usnews.com/news/articles/2012/03/12/consumers-still-buried-in-credit-card-debt (emphasis added).

CERTIFICATE OF COMPLIANCE

This brief complies with the page limitation of Federal Rules of Appellate Procedure 35 and 40 because it is 7 1/2 pages, excluding the parts of the brief exempted by Rule 32(a)(7)(B)(iii).

This brief complies with the typeface requirements of Rule 32(a)(5) of the Federal Rules of Appellate Procedure and the type style requirements of Rule 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Office Word 2007 with 14-point Times New Roman font.

/s/ Sharon K. Robertson
Sharon K. Robertson

CERTIFICATE OF SERVICE

I hereby certify that on November 21, 2016, I electronically filed the foregoing Amicus Brief with the Clerk of the Court of the U.S. Court of Appeals for the Second Circuit by using the Appellate CM/ECF system. All participants are registered CM/ECF users, and will be served by the Appellate CM/ECF system.

/s/ Sharon K. Robertson
Sharon K. Robertson