

**THE COMPETITION TRIBUNAL**

**IN THE MATTER OF the *Competition Act*, R.S.C. 1985, c. C-34, as amended;**

**IN THE MATTER OF an application by the Commissioner of Competition pursuant to section 76 of the *Competition Act*;**

**IN THE MATTER OF certain agreements or arrangements implemented or enforced by Visa Canada Corporation and MasterCard International Incorporated.**

**B E T W E E N :**

COMPETITION TRIBUNAL TRIBUNAL DE LA CONCURRENCE  <b>FILED / PRODUIT</b>  CT-2010-010 January 31, 2011  Jos LaRose for / pour REGISTRAR / REGISTRAIRE	
OTTAWA, ONT	# 10

**THE COMMISSIONER OF COMPETITION**

Applicant

- and -

**VISA CANADA CORPORATION and  
 MASTERCARD INTERNATIONAL INCORPORATED**

Respondents

**RESPONSE OF VISA CANADA CORPORATION**

**PART I – OVERVIEW**

1. In reliance on section 76 of the *Competition Act*, the Commissioner of Competition seeks an order prohibiting Visa Canada Corporation (“Visa Canada”) from, *inter alia*, continuing to implement rules—fundamental to the operation of the Visa business—that prohibit merchants that elect to accept Visa cards from applying a surcharge to customers who pay with a Visa-branded credit card and require merchants that elect to accept Visa branded credit cards to honour all Visa-branded credit cards presented for payment. These rules (collectively, the “Visa Rules”) are pro-consumer and pro-competitive. Section 76 simply has no application to the Visa Rules. Visa Canada does not sell any product to any person or party for resale. The Visa Rules do not by agreement, threat, promise or other like means influence upward or discourage the reduction of the price at which another person supplies, offers to supply or advertises a product. In any event, the Visa Rules have not had, do not have and are not likely to have, an adverse effect on competition in a market.

2. The Commissioner’s Notice of Application (“the Application”) mischaracterizes the nature and purpose of the Visa Rules and the manner in which competition within the Canadian payments

industry takes place, using self-serving terminology in an attempt to bring the Visa Rules within the purview of section 76. The Application contorts the text and disregards the purpose of section 76. Moreover, by ignoring the two-sided nature of the market in which Visa Canada operates, the Commissioner focuses only on demand for acceptance of Visa cards (ignoring demand for the issuance of Visa cards) and incorrectly argues that the rules restrain competition.

3. The Visa Rules are not “merchant restraints”, as the Commissioner coins them; they are pro-competitive rules that protect Visa cardholders from being subjected to an unexpected surcharge or card decline at the point-of-sale (e.g., a bait and switch). The No Surcharge Rule (“NSR”) prohibits merchants from charging Visa cardholders more, not less, than the advertised price for products when they pay for their purchases using a Visa-branded credit card (“Visa Card”), the opposite of price maintenance. The Honour All Cards Rule (“HACR”) protects cardholders' interests by ensuring that they can use their Visa Card wherever the Visa logo is displayed and promotes competition between and among issuing financial institutions. By protecting the interests of Visa cardholders, the Visa Rules enhance the Visa network for the benefit of all network participants, including merchants, by maximizing output (the volume of transactions), and thus enhancing efficiencies on the network.

4. Although the Commissioner also seeks an order generally prohibiting Visa Canada from impeding or limiting the ability of merchants to engage in any practice that discriminates against or discourages the use of a particular credit card or any other method of payment, Visa Canada has no such rule. Merchants have the ability to decide whether or not they wish to participate in the Visa system by accepting Visa Cards, and many merchants have exercised their option not to participate. Visa Canada denies that steering consumers to other forms of payment will have any effect on the price that acquirers may charge merchants. In any event, the Visa Rules do not impede or constrain the ability of merchants who accept Visa Cards to encourage their customers, by a variety of means including the provision of a discount, to use other forms of payment to complete their purchases, including different types or brands of credit cards, debit, cheques or cash. Merchants can, and do, advertise and charge different prices depending on the method of payment. The Commissioner’s

theory of competitive harm is misguided as a matter of law and economics, and is unfounded on the facts.

## **PART II - CONCISE STATEMENT OF GROUNDS UPON WHICH VISA CANADA OPPOSES THE APPLICATION**

5. Visa Canada opposes the Application on three principal grounds.

6. First, although paragraph 76(1)(a) of the Act requires that the product sold by a person described in subsection 76(3) be resold by another person, Visa Canada does not sell any product identified by the Commissioner to a customer or any other person for resale or otherwise. Rather, the products (services) that Visa Canada sells to its customers, acquiring financial institutions ("Acquirers") and card issuing financial institutions ("Issuers"), are different from the products (services) that Acquirers sell to their customers, retailers or merchants. Paragraph 76(1)(a) is not engaged by the facts as alleged by the Commissioner.

7. Second, in the alternative, the Visa Rules do not, by agreement, threat, promise or any like means, influence upward or discourage the reduction of the price at which another person sells a product in Canada. The Visa Rules impose no constraints or restraints on the price that Acquirers charge merchants for their services, nor do the Visa Rules influence upward or discourage the reduction of the price at which merchants sell products to their customers.

8. Third, in the further alternative, the Visa Rules have not had, do not have, and are not likely to have an adverse effect on competition in any market.

## **PART III - RESPONSE TO GROUNDS AND MATERIAL FACTS SET OUT IN THE APPLICATION**

9. Visa Canada denies each and every allegation in the Commissioner's Statement of Grounds and Material Facts and puts the Commissioner to the strict proof thereof, except as expressly admitted herein.

## **PART IV - STATEMENT OF MATERIAL FACTS UPON WHICH VISA CANADA RELIES**

### **A. Visa Canada**

10. Visa Canada is an unlimited liability company formed by amalgamation under the laws of Nova Scotia pursuant to the *Companies Act*, R.S.N.S. 1989, c.81 as amended, with offices in Toronto, Ontario. It is a subsidiary of Visa Inc., a Delaware corporation with its principal place of business in San Francisco, California.

11. Visa Canada is not a financial institution. Unlike financial institutions, Visa Canada does not issue credit cards, extend credit, or set fees for merchants or consumers. Visa Canada does not charge merchants fees and derives absolutely no revenue from the interchange fees exchanged between Issuers and Acquirers. Rather, Visa Canada's principal source of revenue is fees paid by its financial institution customers—Issuers and Acquirers—with which it contracts for use of the "VISA" brand, authorization, clearing and settlement of transactions over the Visa network and related services which Visa Canada provides to them. As such, Visa Canada's revenue is primarily derived from the volume and dollar value of payment transactions that occur over the Visa network.

### **B. Industry Background**

#### **(i) Credit Cards**

12. Visa Canada is in general agreement with the description of the credit card industry set out in paragraphs 21, 22, 24, 25, 26 and 28 of the Application. However, credit cards compete with all forms of payment including, but not limited to, card-based forms of payment, including credit cards, charge cards, debit cards, prepaid cards, merchant charge accounts and private label cards; paper-based forms of payment, including cash, personal cheques, government cheques, travellers cheques, and money orders; mobile forms of payments, including payments through text messaging, mobile applications, and web browsers; and other electronic forms of payment not typically tied to a payment card or similar device, including online payment services, wire transfers and electronic benefits transfers. Visa Canada estimates that transactions over the Visa network account for only

approximately 18 percent of consumer spending in Canada and less than one percent of business-to-business spending in Canada.

**(ii) Processing of Credit Card Transactions**

13. Visa Canada fundamentally disagrees with the Commissioner's description of the products and services supplied by Visa Canada and the fees associated with those services.

14. Visa Canada operates an electronic payment system network in Canada (the "Visa Network") and provides a range of services to the Issuers and Acquirers with whom it contracts ("Visa Network Services"). In operating its electronic payment system network Visa Canada maintains a set of operating rules to ensure that the payment system is able to perform its core functions efficiently and effectively. These protocols address, among other things, prompt funding for settlement, risk of non-payment, transaction disputes, and fraud identification.

15. Visa Canada provides authorization, clearing and settlement services to Issuers and Acquirers over the Visa Network. "Authorization" involves obtaining confirmation for the Acquirer that the Issuer approves the transaction initiated by the cardholder's presentation of a Visa Card for payment. The transmittal of transaction information from the Acquirer to the Issuer and back to the Acquirer occurs over the Visa Network.

16. "Clearing and settlement" involve the calculation of fees and amount owed for a transaction and calculation of the net position of financial institutions for all transactions processed over the Visa Network over a period of time. The Acquirer transmits the transaction data over the Visa Network, which is routed to the Issuer, and the Issuer transfers the funds over the Visa Network to the Acquirer. Funds are not transferred for each transaction. At the end of the day, the settlement process determines the net position of all financial institution clients. Authorization, clearing and settlement are services provided by Visa Canada to Issuers and Acquirers; they are not services provided by Visa Canada to merchants or by Acquirers to merchants.

17. Acquirers, in competition with one another, provide an array of services to merchants (either directly or through agent processors) (“Merchant Services”) including the sale, lease, deployment and servicing of point-of-sale hardware and software, the submission of transactions for settlement, the preparation of statements or reports, the processing of charge-backs and other exception items, the provision of customer service to merchants, and the assurance to merchants that they will receive payment in respect of the payment card transactions they accept. Acquirers charge merchants a fee for the services they provide (“Merchant Service Fees”).

18. Issuers market and issue Visa Cards to cardholders and manage the relationship with cardholders including the provision of credit, cardholder benefits and monthly statements (“Issuer Services”). In addition to the provision of cardholder benefits, the arrangements between Issuers and cardholders include provisions for bill payment, credit limits, the provision of a grace period, minimum payment amount, the interest rate applicable to unpaid amounts, and cardholder fees (if any). Issuers, in competition with one another, offer cardholders different benefits, service levels, interest rates, fees and other features through the issuance of different types of cards. Issuers bear the risk of the payment of credit card charges incurred by cardholders. Other key functions provided by Issuers include the resolution of charge-backs, and protection and replacement for lost cards.

19. Issuers and Acquirers provide their services to cardholders and merchants, respectively, pursuant to contractual arrangements to which Visa Canada is not a party.

20. Visa Canada does not agree with the description of a typical credit card transaction set out in paragraph 39 of the Application, except to the extent that the diagram demonstrates that Acquirers provide a set of Merchant Services to merchants that are separate and distinct from the Visa Network Services that Visa Canada provides to Issuers and Acquirers.

21. At paragraph 11 of the Application, the Commissioner makes much of the difference between the cost of accepting credit cards for payment as compared with the costs associated with other forms of payment. The existence and magnitude of any cost difference would reflect the

different value that market participants place on these forms of payment in light of the differences in their respective features, some of which the Commissioner identifies (the Commissioner goes so far as to contend that credit cards are in a separate market from other forms of payment). In any event, even assuming such cost differences exist, they raise no issue under section 76 of the Act. Moreover, any such differences do not suggest that credit cards are not part of the same relevant market as other payment methods.

22. As with other tax-deductible costs that merchants incur in the operation of their businesses (e.g., the costs of goods, rent, labour, advertising, etc.), costs for Merchant Services presumably have to be covered in the prices that merchants charge if they hope to make a profit (although as discussed below, that does not mean that Merchant Service Fees increase prices for consumers). In respect of all such expenses, each merchant must decide whether the benefits outweigh the costs and whether the expense will ultimately contribute to the overall success and profitability of the merchant's business. Contrary to the Commissioner's assertion, for example in paragraph 84 of the Application, merchants are free to elect not to accept credit cards generally, or Visa Cards in particular, and many merchants do so. The fact that many (but by no means all) merchants accept credit cards (including Visa Cards) speaks to the fact that, for those merchants, the benefits of doing so outweigh the costs.

23. At paragraph 5 of the Commissioner's Concise Statement of Economic Theory, the Commissioner contends that "the use by a merchant's customer of other methods of payment, such as cash or debit, usually results in lower costs for the merchant." However, other forms of payment (such as cash, cheques, debit or other methods of payment) are not necessarily "lower cost" forms of payment (for the merchant alone, leaving aside the cardholder) as compared to Visa Cards, when the benefits to merchants of accepting Visa Cards (e.g., increased sales, the ability to extend immediate credit for a purchase, guarantee of payment, etc.) are taken into account. In addition, other forms of payment have costs associated with them that credit cards do not, for instance, collection costs involved with cheques, risk of cheque fraud, cost of cash theft and personnel costs

in counting and accounting for cash.

24. The Commissioner also suggests that it is a cause for concern that the costs for Merchant Services are typically passed on by merchants to all customers, even those who use other forms of payment (for example, in paragraph 4 of the Application). There is no requirement of law, policy or commercial practice that the costs associated with any particular Merchant Service be borne only by a certain subset of customers. For example, merchant costs of providing free parking are “passed on” to all consumers, even those that take public transportation. The costs associated with accepting cash for payment—including security expenses, slower checkout lines (and thus greater labour expense) and loss from theft—are “passed on” to consumers that pay for goods with a credit card. In any event, whether the costs associated with accepting credit cards are borne by some customers and not others raises no issue and is irrelevant to the application of section 76 in this matter.

25. Contrary to the Commissioner's assertion at paragraph 4 of the Application, it is also incorrect to assume that costs for payment card acceptance translate into higher prices for consumers. The services provided by payment networks expand output and facilitate competition among retailers, thereby leading to increased inter-merchant competition which helps lower prices for consumers.

### **(iii) Visa Canada Operates in a Two-Sided Market**

26. The Commissioner's description of the credit card industry ignores a fundamental aspect of the manner in which credit card payment systems operate: they operate in a two-sided market. The existence of the Visa Network depends on a sufficient number of cardholders who use Visa Cards and a sufficient number of merchants who will accept them. Unlike a traditional one-sided market, where the supplier need only concern itself with demand from a single customer group, Visa Canada must meet the demands of both sets of its customers (Issuers and Acquirers) on either side of the market in order to succeed. For the Visa Network to operate effectively, Visa Canada must offer Issuers sufficient incentives to provide Visa Cards to consumers and encourage cardholders to



decide to use them at the point-of-sale, and it must offer Acquirers sufficient incentives to negotiate with and enlist merchants who will accept Visa Cards. Simply stated, merchants will not accept a credit card unless there are enough cardholders who use it and consumers will not use a credit card unless there are enough merchants who accept it.

27. The two-sided nature of the market in which Visa Canada operates is key to understanding the role that interchange plays in the Visa payment system. Visa sets and makes available a set of default interchange rates for use by Acquirers and Issuers within the Visa system. On a typical purchase transaction, interchange flows from Acquirers to Issuers, reflecting the value that Issuers provide. On credit transaction cash advances, interchange flows the other way, from Issuers to Acquirers.

28. As already stated, Visa earns its revenue primarily from Visa Network Service Fees paid by Issuers and Acquirers, based on the number and value of transactions over the Visa Network. Visa Canada does not derive any revenue from interchange fees; it seeks to enhance its revenue by promoting increased system volume. Visa Canada promotes volume growth through a wide range of activities, including by setting default interchange rates that provide incentives for Issuers to issue Visa Cards to cardholders and for Acquirers to encourage their merchants to accept them. Where lower interchange fees would lead to increased merchant acceptance without reducing card issuance and cardholder usage, Visa Canada has every incentive to suggest lower default interchange rates as this would maximize system volume and thus Visa Canada's revenues.

29. Interchange is not a "price" that Visa Canada has any commercial interest in seeking to maximize; rather, interchange is a tool that Visa Canada uses to balance demand on both sides of the two-sided market in which it operates in order to maximize overall system output and the efficiencies resulting therefrom. Visa's interest in setting default interchange rates is to maintain the balance of the system. If interchange rates are set too high, merchants will stop accepting cards. If interchange rates are set too low, Issuers will be undercompensated for the value they deliver to

their cardholders, and the features that attract cardholders will be diminished. This in turn reduces cardholder participation and the value of Visa to merchants.

30. When setting default interchange rates, Visa considers a host of factors and sets rates to help promote overall system growth and growth in specific payment segments, and to reflect the value delivered to retailers and cardholders by payment type. Although under the terms of the Visa Operating Regulations, Issuers and Acquirers are free to negotiate bilateral interchange rates, it is considerably more efficient from a system output and system management perspective for Issuers and Acquirers to adhere to the default interchange rate. Where the Issuer and the Acquirer are part of the same corporate entity (or are otherwise related through ownership interests), the default interchange rate is economically irrelevant to the Issuer and Acquirer. This applies in respect of approximately 15 percent of the volume of transactions for which a Visa Card is used. There is nothing in Visa Canada's contractual relationship with Acquirers that requires them to reflect the default interchange rate in any particular way in the fees that Acquirers negotiate with merchants for Merchant Services.

31. In further recognition of the value of the Visa payment system, a number of merchants have elected to participate in the Visa system by not only accepting Visa Cards, but also jointly issuing with an Issuer a "co-branded" Visa Card. With a typical co-branded card, the merchant shares (along with the Issuer) in the revenue generated by use of the co-branded card. Cardholder benefits associated with co-branded cards may relate to benefits for general usage (e.g., points, miles or cash back) and/or rewards or other benefits associated with doing business with the merchant whose brand appears on the card. Such benefits may be used by merchants as an incentive to shop at their store or to drive repeat sales.

### **C. The Visa Rules**

32. The Visa Rules are part of Visa's Operating Regulations, which are a comprehensive set of rules that govern Visa Canada's relationships on an international and regional basis with its

customers: Issuers and Acquirers. Visa's Operating Regulations establish a consistent operating framework designed to promote the efficient and effective operation of the Visa Network with a view to ensuring that cardholders and merchants experience a common, convenient, safe and reliable payment experience on a global basis. As such, Visa's Operating Regulations require Acquirers to obtain merchants' agreement to abide by the Visa Rules (among others) in their contracts.

33. Both the NSR and the HACR have existed as integral aspects of the Visa payment system since its inception over 40 years ago. The NSR and HACR have existed in Canada since the introduction of the Visa payment system to Canada over 30 years ago.

**(i) The NSR**

34. The NSR states as follows:

Visa Merchants agree to accept Visa cards for payment of goods or services without charging any amount over the advertised price as a condition of Visa card acceptance, unless local law requires that Merchants be permitted to engage in such practice.

35. Among its other benefits, the NSR protects consumers by requiring the price at checkout to be no greater than the advertised price while permitting merchants to advertise and charge different prices depending on the method of payment, or otherwise persuading consumers to use other brands or types of credit cards or other forms of payment. The NSR (and the HACR) also lead cardholders to approach Visa-accepting merchants with their cards in hand, with the knowledge that that merchant represents a viable provider of the goods or services they seek to purchase.

36. Surcharging would result in harm to both cardholders who face the charge (in the form of unexpected higher prices) and to the Visa Network and its stakeholders (including merchants) by reducing issuance, acceptance, and use of Visa Cards. As outlined above, given the two-sided nature of payment networks, any detrimental effect on the issuing side has a detrimental effect on the acquiring side. As such, the NSR benefits cardholders, which in turn benefits merchants. In addition, the NSR protects the integrity of the Visa brand for the benefit of all stakeholders of the

Visa Network.

**(ii) The HACR**

37. The HACR provides as follows in respect of Visa Cards:

Visa Merchants may not refuse to accept a Visa product that is properly presented for payment, for example, on the basis that the card is foreign-issued, or co-branded with a competitor's mark. Merchants may steer customers to an alternative method of payment, such as providing discounts for cash, but may not do so in a confusing manner that denies consumer choice. Merchants may decline to accept a Visa product that is not covered by their acceptance contract, and may also consider whether present circumstances create undue risk.

38. One of the primary benefits to Visa cardholders is the breadth of merchant acceptance of Visa Cards. Visa Canada markets its product in large part on the promise that cardholders will be able to use their Visa Card (regardless of the type of benefits or the identity of the Issuer, no matter how large or small the Issuer may be) at merchants that display the Visa logo around the world. Cardholder uncertainty about whether their Visa Card will be accepted wherever the Visa logo is displayed diminishes the value of a Visa Card and is therefore a disincentive to carrying and using a Visa Card at all.

39. The HACR requires merchants that accept Visa to accept all Visa Cards regardless of, *inter alia*, the identity of the Issuer, the card type (premium or standard or prepaid or commercial) or the country where the card was issued. Like the NSR, the HACR protects the integrity of the Visa brand for the benefit of all stakeholders of the Visa Network. At the same time, the HACR acknowledges that Visa competes against other forms of payment. Accordingly, it specifically provides that "[m]erchants may steer customers to an alternative method of payment, such as providing discounts for cash." The HACR also enhances competition between and among Issuers by, among other things, supporting product innovation.

40. The Commissioner alleges, among other things, that the HACR precludes merchants from avoiding the Merchant Service Fees associated with premium credit cards, including the Visa Infinite

credit card. The Visa Infinite card is an important competitive tool that allows Visa Canada, Issuers and merchants to compete in a key consumer segment: customers who make high volume and/or high value purchases. Visa Canada developed its Infinite card to compete more effectively, for example, with American Express, which has introduced credit cards with substantial benefits associated with them to target these consumers. To compete in this segment, Visa Canada's current premium credit card, the Infinite card, carries a higher interchange fee to provide Issuers with the incentive and ability to provide more costly benefits in order to compete. Limited acceptance of Visa premium credit cards would diminish the value of such cards by making them less attractive to this type of consumer.

## **PART V - DETAILED STATEMENT OF GROUNDS UPON WHICH VISA CANADA OPPOSES THE APPLICATION**

### **A. Section 76 of the Act Does Not Apply to the Visa Rules**

#### **(i) Visa Canada Does not Sell any Product to any Customer or Other Person for Resale**

41. Visa Canada does not provide the products (services) identified by the Commissioner as Credit Card Network Services to its customers or any other person for resale to merchants or any other party, a required element of paragraph 76(1)(a) of the Act. Contrary to the facts as alleged in section 76 of the Notice of Application, Visa Canada does not supply its services indirectly (or directly) to merchants through Acquirers. Visa Canada supplies Visa Network Services to its financial institution customers (Issuers and Acquirers) and Acquirers provide a different set of services, Merchant Services, to their merchant customers. As such, section 76 has no application to the facts alleged by the Commissioner.

42. Consistent with the above, Acquirers are free to set the prices for the services they provide to merchants. Visa Canada expressly denies that the Visa Rules restrict the price Acquirers charge merchants for these Merchant Services. The Visa Rules prohibit merchants from imposing surcharges on cardholders and refusing to accept certain types of Visa Cards if they otherwise

accept Visa, but do not address, directly or indirectly, the price which Acquirers may charge for Merchant Services.

43. Interchange and Visa Network Services fees are not *products* sold by Acquirers to merchants; they are *costs* incurred by Acquirers. They are akin to all other costs that Acquirers incur in carrying on their businesses and which they presumably have to cover—along with their other costs of doing business—in the prices they charge if they hope to make a profit. The Commissioner states that “Interchange Fees and Network Fees establish a floor for Card Acceptance Fees, as no Acquirer could profitably set Card Acceptance Fees below the combined level of interchange fees and Network Fees.” This is the nature of *all* business costs: such costs *always* set a theoretical floor for the prices of products sold if the supplier hopes to make a profit (although suppliers can, as Acquirers can here, choose to sell their products below cost). Visa Canada expressly denies that the setting of the fees for Visa Network Services and establishing a default interchange rate which Acquirers pay to Issuers (or *vice versa*) constitute resale price maintenance for the purposes of section 76 of Act.

44. For the same reasons, Visa Canada further denies that the Visa Rules constitute resale price maintenance for the purposes of paragraph 76(1)(a) of the Act in respect of the prices that merchants charge to their customers. The costs of Merchant Services are in respect of fees charged to merchants by Acquirers, not by Visa Canada. These are costs that are akin to all other costs that merchants incur and which presumably merchants have to cover in the prices they charge if they hope to make a profit.

**(ii) Visa Canada Has Not Influenced Upward or Discouraged the Reduction of the Price at Which Another Person Sells a Product by Agreement, Threat, Promise or Any Like Means**

45. In the alternative, Visa Canada denies that it has by agreement, threat, promise or any like means influenced upward or discouraged the reduction of the price at which another person

supplies, offers to supply or advertises a product within Canada.

46. The Visa Rules say nothing about what Acquirers may charge merchants for Merchant Services and impose no constraints or restraints on the prices that can be negotiated for those services. The NSR explicitly prohibits merchants from charging cardholders *more, not less* when they purchase products from a merchant using a Visa Card and the HACR (which does not speak to anyone's price at all) protects cardholders from higher "costs" in the form of the diminution of the value of their credit card. Absent the HACR, a cardholder would be significantly disadvantaged in two ways: the prospect that his or her Visa Card would be unexpectedly declined and the possible loss of the benefits associated with using their preferred Visa Card.

47. Moreover, because interchange is a tool that is used to balance demand on both sides of the two sided market, a reduction in interchange likely will have an impact on other aspects of the payment system, for example, a reduction of the benefits offered to cardholders or the imposition or increase of annual cardholder fees. Even if the Commissioner is, for argument's sake, correct that prohibiting the NSR and HACR would result in lower interchange and result in lower nominal card acceptance fees, that would simply mean that the merchant is paying less for a card that is worth less to cardholders and thus to merchants (i.e. a different product). That is not the same as a lower price, which would mean paying less for the same product. In short, even if the abrogation of the Visa Rules were to result in the reduction of the default interchange rate, the likely result would simply be a wealth transfer from cardholders to merchants, with no net increase in output or competition, and no benefit to consumers, as the Commissioner contends.

48. In the alternative, any putative connection between the Visa Rules and any effect on the fees that Acquirers charge merchants is entirely speculative, premised on the mistaken and unsupported assumption that, but for the Visa Rules, Visa Canada would lower the default interchange rates and/or the Visa Network Service Fees *and* that Acquirers would lower the Merchant Service Fees they charge merchants. With respect to the NSR, based on Visa's business model and experience in

other jurisdictions, one cannot assume that Visa would lower its standard default interchange rates or Visa Network Service Fees in response to the imposition or threat of a surcharge. With respect to the HACR, credit cards require an appropriate level of interchange to support the cardholder benefits associated with them. If, in the absence of the HACR, merchants were to selectively begin refusing to accept certain Visa Cards (e.g., from only a particular Issuer, or of a particular type), cardholder confidence in these products would diminish and a reduction in the default interchange rate on these products would only erode Issuer confidence.

49. Moreover, paragraph 76(1)(a) requires the Tribunal to find that the requisite agreement, threat, promise or other like means “*has influenced upward, or has discouraged the reduction of*” the price referenced in that paragraph. Even if section 76 otherwise applies (which Visa Canada expressly denies), the Commissioner has not, and cannot, establish that the Visa Rules *have had* such an effect.

### **(iii) The Visa Rules Have No Adverse Effect on Competition in a Market**

50. As stated, there is no basis in fact or law for a finding that Visa Canada has engaged in resale price maintenance within the meaning of section 76 of the Act. As such, there is no need to inquire whether the conduct referenced by the Commissioner in the Application has resulted in, is resulting in, or would be likely to result in an adverse effect on competition in a market. In any event, in the further alternative, Visa Canada denies that the Visa Rules have had, have, or are likely to have an adverse effect on competition in a market.

### **(a) The Relevant Market**

51. The Commissioner’s use of the term “Credit Card Network Services,” which she contends is the relevant market, conflates two distinct sets of services provided at two different levels of trade: Visa Network Services provided by Visa Canada to Issuers and Acquirers and Merchant Services provided to merchants by Acquirers.



52. Visa Canada, as the operator of the Visa Network, competes against other payment services and payment options in the Canadian payments industry. Visa Canada denies that Visa credit cards do not compete with other forms of payment, including cash, cheques, debit cards, other card based payment products and various electronic forms of payment, such as Pay Pal. Through competitive innovation, Visa Canada has continued to expand the range of payment transactions for which credit cards are likely to be used. Visa Canada faces fierce and growing competition from existing and emerging competitors and technologies, and seeks to differentiate its product features from those of other payment methods in order to compete.

53. The focus of the Commissioner's allegations under section 76 is an aspect of the provision of Merchant Services (namely, credit card acceptance services), which services Visa Canada does not provide, either directly or indirectly. What the Commissioner describes as "Card Acceptance Fees" are an aspect of what are referred to herein as Merchant Service Fees, being the fees paid to Acquirers by merchants for Merchant Services (terminal rental, data submission, etc). Visa Canada does not provide, either directly or indirectly, Merchant Services. Visa Canada does not set the price for such Merchant Services, nor do the Visa Rules influence upward or discourage the reduction of the price at which any Acquirer supplies, offers to supply or advertises Merchant Services. Visa Canada's conduct does not adversely affect competition between Acquirers for the provision of Merchant Services, or between any provider of payment services such as between Visa and MasterCard.

54. Visa Canada considers that in general terms the relevant geographic market is national in scope, with the proviso that there are several aspects of Visa Canada's business that are cross-border or international in nature.

**(b) Market Power**

55. Visa Canada denies that it has market power in respect of any market that is relevant to the Commissioner's allegations under section 76. Visa operates in a highly competitive environment.

There is robust competition among the payment types and various local and global networks well beyond credit cards. There is an array of existing and emerging competitors, including cash, cheque, pre-authorized debits, Interac, retail-issued credit, PayPal, and other payment networks such as MasterCard and American Express. Moreover, Visa Canada's customers are by and large sophisticated financial institutions that are able to exercise considerable countervailing bargaining power.

**(c) Alleged Competitive Harm Resulting from the Visa Rules**

56. The Commissioner alleges that the Visa Rules adversely affect competition because, but for the Visa Rules, merchants could surcharge or refuse to accept certain types of Visa credit cards, or threaten to do so, which would reduce the volume of transactions on the Visa Network. The Visa Rules promote enhanced volume on the network (output) and, as such, are fundamentally at odds with the exercise of any alleged market power.

57. At paragraph 93 of the Application, the Commissioner alleges various ways in which the Visa Rules adversely effect competition, none of which is sustainable. In summary, the Commissioner contends that the Visa Rules deny merchants the most effective means available to them to steer customers to other forms of payment and further that if merchants were able (with the abolition of the Visa Rules) to effectively steer consumers to other forms of payment this would somehow result in the reduction of Merchant Service Fees. However, at paragraph 83 of the Application, the Commissioner states that competition from other payment methods cannot constrain prices in the market for "Credit Card Network Services". Assuming *arguendo* that the Commissioner is correct in this regard, steering consumers to other forms of payment cannot constrain pricing in the market for "Credit Card Network Services" or Merchant Services, and the Commissioner's theory of competitive harm fails *ab initio*.

58. Visa Canada denies that steering consumers to other forms of payment will have any effect on the price that Acquirers may charge for Merchant Services. Even assuming *arguendo* that it

would, the Visa Rules do not preclude merchants from encouraging customers to use other forms of payment. Visa Canada expressly denies that surcharging is a uniquely effective means of steering consumers to adopt other forms of payment, should a merchant decide to encourage such steering. Canadian merchants have an array of options (apart from surcharging or refusing to accept certain type of credit cards) available to them to persuade consumers to use other forms of payment, including the following:

- deciding not to accept Visa Cards thereby avoiding system participation;
- offering the customer a discount or rebate, including an immediate discount or rebate at the point of sale, if the customer uses a particular brand or type of general purpose credit card or a particular form of payment;
- offering a free or discounted product if the customer uses a particular brand or type of general purpose card or a particular form of payment;
- offering a free or discounted or enhanced service if the customer uses a particular brand or type of general purpose card, or a particular form of payment;
- offering the customer an incentive, encouragement, or benefit for using a particular brand or type of general purpose card or a particular form of payment;
- expressing a preference for the use of a particular brand or type of general purpose card or a particular form of payment;
- promoting a particular brand or type of general purpose card or a particular form or forms of payment through posted information, through the size, prominence, or sequencing of payment choices, or through other communications to a customer;
- communicating to a customer the reasonably estimated or actual costs incurred by the merchant when a customer uses a particular brand or type of general purpose card or a particular form of payment or the relative costs of using different brands or types of general

purpose cards or different forms of payment; or

- offering a store branded (private label) charge card or loyalty programs.

59. A number of merchants use these options to influence their customers' use of payment methods. Other merchants choose not to do so given the benefits associated with payment by Visa or so as not to interfere with consumer choice. Visa Canada denies that surcharging or the refusal to accept certain types of credit cards is uniquely effective in steering consumers to other forms of payment, should a merchant decide that it wants to steer customers to alternative methods of payment. As is more fully explained herein, Visa Canada in any event questions whether such steering is relevant to any issue in this Application.

60. As outlined in paragraph 58, there are a variety of options apart from discounting that are available to merchants to steer consumers to other forms of payment, none of which would be subject, for example, to the considerations referenced in paragraph 66 of the Application. In short, surcharging is harmful to consumers, disruptive of the Visa payment network and potentially a windfall to merchants.

61. The Commissioner further alleges that abrogation of the Visa Rules would bring pressure to bear on Visa Canada to reduce the default interchange rate and/or the Visa Network Service Fees charged to Acquirers, thereby “foster[ing] competition” in the “Credit Card Network Services Market.” As stated, Visa Canada denies that the abrogation of the Visa Rules will affect its default interchange rate or the Visa Network Service Fees, or result in a reduction of the Merchant Service Fees charged by Acquirers. In addition, even if an ability to surcharge or selectively decline certain Visa Cards did lead to a reduction in the default interchange rate, any such pressure brought to bear by merchants on Visa Canada through surcharging or refusing to accept certain types of cards would not enhance or “foster competition” between Visa Canada and any other party. Rather, abrogation of the Visa Rules would merely give merchants the ability to harm or to threaten to harm the Visa Network in an effort to extract concessions for refraining to do so. Neither section 76, nor

the *Competition Act* in general, is intended to result in a market intervention of this kind.

62. Paragraph 93 of the Notice of Application sets out a list of ways in which the Visa Rules purportedly adversely affect competition. Visa Canada expressly denies each of these allegations.

Specifically, Visa Canada states that:

- (a) subparagraph (a) merely restates the allegation of resale price maintenance;
- (b) the allegation in subparagraph (b) is addressed in paragraphs 58 to 60 herein. The Visa Rules neither distort nor harm the “competitive process” or “price-setting mechanism for Card Acceptance Fees” nor do they constrain merchants’ ability to “foster competition” in any market;
- (c) with respect to subparagraph (c), as with any other business costs they incur, merchants presumably are inclined to cover the costs associated with accepting payment by credit card in the prices that they decide to charge to their customers if they hope to make a profit, although that does not mean that prices to consumers are increased;
- (d) the first three sentences of subparagraph (d) simply allege that but for the Visa Rules there would be greater competition “between credit card networks with respect to the prices paid by merchants for Credit Card Network Services”, but fail to say how or in what way this will occur. The meaning of the fourth sentence is unclear; however, to the extent that it suggests that abrogation of the Visa Rules would increase competition between Issuers with respect to the provision of Merchant Services or the level of Merchant Service Fees, no such effects can occur as Issuers do not compete in this regard;
- (e) with respect to subparagraph (e), first, the Respondents compete vigorously with each other and other suppliers of credit cards, and Visa Canada expressly denies that the Visa Rules impair such competition in any way; second, Visa Canada does not offer, set or charge

Merchant Service Fees; all such fees are offered, set and charged by Acquirers;

- (f) with respect to subparagraph (f), as stated, Visa Canada denies that the Visa Rules constrain or prevent merchants from promoting the use of other forms of payment, and in any event, any alleged constraint on output of other payment methods cannot, under the Commissioner's market definition, affect pricing in a distinct market of "Credit Card Network Services"; and
- (g) with respect to subparagraph (g), the Visa Rules neither create nor increase any barriers to entry or expansion for "lower cost credit card networks" as merchants are free to accept any credit cards they choose.

63. With respect to paragraph 94 of the Application, no antitrust authority in any other jurisdiction has ever challenged the HACR and no such authority in any other jurisdiction has ever challenged either the NSR or the HACR as constituting resale price maintenance. Visa Canada denies that the elimination of the NSR in any other jurisdiction has allowed merchants to effectively encourage customers to use "credit cards with lower Card Acceptance Fees and other less expensive" payment methods. In any event, Visa Canada denies that other options were not available to such merchants that would have been at least, if not more, effective in encouraging customers to use such other forms of payment.

64. The US Department of Justice ("US DOJ") recently resolved with Visa Inc. and MasterCard International a lawsuit it brought against Visa Inc., MasterCard International and American Express in respect of their respective operating rules. Following an extensive investigation, the US DOJ limited the relief it sought to the abrogation of Visa USA's and MasterCard International's rules that in some cases prohibited merchants from offering discounts not made available to the network's cardholders (notably, rules that Visa Canada does not have in Canada). The US DOJ concluded that allowing merchants to offer customers discounts or otherwise encouraging them to use other forms of payment was sufficient to address the US DOJ's concerns. The settlement reached by Visa Inc.

and MasterCard International with the US DOJ did not overturn either the NSR or the HACR.

65. The Canadian government has also looked extensively at the Visa Rules. In April 2010, the Government of Canada, through the Department of Finance, a governmental body with extensive industry-specific expertise, issued the *Code of Conduct for the Credit and Debit Card Industry in Canada* ("the Code of Conduct") referenced in the Application, to which Visa Canada is a signatory. Like the conclusion reached by the US DOJ referenced in paragraph 64 herein, the Department of Finance concluded that it was unnecessary to address either the NSR or HACR in the Code of Conduct. While it is the case that the Code of Conduct does not require credit card networks to permit merchants to offer discounts based on the type of credit card used, as opposed to the brand of card, the Visa Rules have no such limitation. Merchants using Visa credit cards are free to discount on the basis of either type or brand of credit card used.

#### **PART VI - CONCISE STATEMENT OF ECONOMIC THEORY**

66. Visa's Concise Statement of Economic Theory is set out in Schedule "A" to this Response.

#### **PART VII - RELIEF SOUGHT**

67. Visa Canada expressly denies that there is any basis in fact or law for any of the remedial relief sought by the Commissioner in paragraph 95 of the Application, both with respect to the Visa Rules, singly or in combination, and with respect to "any other agreements, arrangements, policies, rules or regulations or any other like means," the latter of which cannot be subject to any such remedy as the Commissioner has not identified the conduct or established that it is engaged by section 76 of the Act. However, even if the Tribunal concludes that the Visa Rules—or any other unspecified "agreements" or "like means"—constitute price maintenance that adversely affects competition, which Visa Canada expressly denies, the Tribunal should exercise its discretion not to make any order under section 76 of the Act, whether sought by the Commissioner or otherwise.

68. Visa Canada requests an order dismissing the Application with costs payable to Visa

Canada in an amount to be determined by the Tribunal after hearing submissions from the parties.

## **PART VIII - LANGUAGE AND VENUE**

69. Visa Canada agrees with the Commissioner's request that this application be heard in English and in the City of Ottawa.

Dated at Toronto, this 31st day of January, 2011.

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## **Appendix “A”**

### **Concise Statement of Economic Theory**

#### The Visa Canada Business

1. Visa Canada operates in competition with other credit card network operators as well as many other forms of payment including charge cards, prepaid cards, private label cards, debit cards, cash, cheques, and other electronic and non-electronic payment methods.
2. Visa Canada's principal source of revenue is fees paid by its financial institution customers—Issuers and Acquirers—for network services including the authorization, clearing and settlement of transactions over the Visa Network. Visa Canada's revenues are derived primarily from the volume and dollar value of payment transactions that occur over the Visa Network, not from interchange fees. Accordingly, Visa Canada's principal business objective in setting interchange fees is to maximize the volume of transactions that flow across the Visa Network, achieving the efficiencies associated therewith.
3. Visa Canada does not compete with Issuers or Acquirers. In particular, Visa Canada does not compete with Acquirers for the provision of Merchant Services to merchants, for example, the sale, lease, deployment and servicing of point-of-sale hardware and software, the submission of transactions for settlement, the preparation of statements or reports, the processing of charge-backs and other exception items, the provision of customer service to merchants, and assurance to merchants that they will receive payment in respect of the credit card transactions they accept.

#### The Economic Significance of Operating in a Two-Sided Market

4. Visa Canada operates in a two-sided market, which is fundamentally different, from an economic perspective, than a one-sided market. A payment system such as Visa can increase its output only if it attracts demand on *both* sides of the market: the issuing side and the acquiring side. In a two-sided market, the price is the sum of the effective prices paid by purchasers on both sides

of the market. A payment system competes by attracting loyal cardholders through offering valuable benefits, and by delivering incremental sales to merchants who accept the payment card. In general terms, merchants will find it more valuable to accept payment by a credit card brand if more cardholders use that brand, and consumers will find it more valuable to use a credit card if more merchants accept that brand of credit card. Accordingly, Visa Canada seeks to ensure that Issuers have sufficient incentives to enlist and service cardholders and Acquirers have sufficient incentives to enlist and service merchants.

5. Appropriately balancing the two-sides of payment card networks is key to increasing the overall output through the Visa Network, thereby enhancing its efficiency.

6. Interchange is not a price. It is an economic tool used to balance demand on both sides of the market with a view to maximizing output on the payment network. In general terms,

- Interchange fees create incentives for Issuers to offer valuable cardholder benefits and other features (e.g., funding of an interest free period, statements, etc.), which allow the payment system to build a base of loyal cardholders and thereby deliver incremental sales to merchants;
- Interchange fees cannot be raised too high, or else acceptance will suffer. Similarly, interchange fees for a particular payment network cannot be too low, or else the network will not be able to attract sufficient issuance and cardholder usage;
- In contrast to prices in one-sided markets, in which a higher price generally leads to lower output but higher revenue per unit, an increase in interchange fees does not necessarily imply a reduction in output. A higher interchange fee makes the payment card more attractive to the issuing side of the market, thereby increasing the number of cardholders and/or cardholders' incentives to use a Visa-branded card. This adds value to the Visa Network, thereby benefiting both cardholders and merchants;

- An increase in interchange fees is not indicative of market power, but rather a result of increased demand for issuance. Lower interchange fees do not necessarily imply greater or more effective competition;
- The ability to set differential interchange rates across merchants and transaction types does not indicate that Visa Canada has market power. Rather, it reflects a desire to maximize output on the Visa Network by, for instance, seeking to increase acceptance in certain merchant categories that are not well penetrated or as well penetrated as others (e.g., gasoline stations, bill payment and recurring payments).

7. From an economic perspective, with respect to merchants, payment acceptance (the various methods by which a customer may pay for a purchase of a good or a service) is an important means through which merchants compete with each other in order to attract customers, that is, by offering a better (more rewarding and more efficient) transactional experience to consumers. In this respect, payment card acceptance is similar to merchants competing with each other by providing, for example, free parking, attractive premises, longer store hours, or better in-store service. As with payment acceptance, merchants offer these types of services in order to increase their sales. In addition, payment networks such as Visa facilitate non-face to face transactions such as Internet transactions and phone transactions (which would not be possible through certain other payment mechanisms such as cash or cheques) and reduce costs associated with other types of payment (e.g., collection of cash, risk of NSF cheques, etc.). For some merchants, these are significant business features that form the basis of their business model.

#### The Visa Rules Contribute to the Economic Efficiency of the Visa Network

8. The Visa Rules enhance output on the Visa Network and therefore are at odds with the exercise of any alleged market power; rather, the Visa Rules contribute to the Visa Network's economic efficiency and effectiveness. The Visa Rules are premised on consumer protection and the enhancement of the cardholder experience at the point of sale. Both the NSR and the HACR

protect the expectation interests of Visa cardholders and, as such, promote card issuance and usage at the point-of-sale. Stated differently, in the absence of the Visa Rules cardholders will have diminished incentives to use Visa credit cards, leading to reduced issuance. If cardholders have diminished incentives to use Visa Cards and issuance is reduced, merchants will have diminished incentives to accept them.

9. Merchants that impose a surcharge or that reject a particular type of Visa credit card when presented would effectively subject cardholders to a “bait and switch,” whereby cardholders expecting to pay a certain advertised or listed price with their payment card would learn at the point of sale that they would have to pay more or would not be allowed to use their particular Visa Card. This would decrease the value of the payment system to cardholders and undermine the Visa product/brand as a whole, as it would create uncertainty regarding retail prices that cardholders would expect to pay when they purchase goods or services from a merchant using a Visa-branded credit card. This in turn would reduce output on the Visa Network and undermine the efficiencies associated with output maximization.

10. Merchants that surcharge or do not accept all Visa credit cards would also create a “free-rider” problem that would further damage the Visa payment system, placing a greater burden on those merchants that do not surcharge and accept all Visa-branded credit cards. Free-riding occurs because these merchants would obtain the benefits of accepting Visa Cards, for example, incremental sales, while avoiding the cost of supporting the payment system, i.e., violating the implicit economic arrangement they agreed to in accepting Visa Cards.

#### Resale Price Maintenance and Antitrust Economics

11. The Application fails to demonstrate that the Visa Rules constitute resale price maintenance from an antitrust economics perspective, let alone that such resale price maintenance has had, has, or is likely to have an adverse effect on competition in any market. In the latter respect, the NSR and HACR do not inhibit, but rather enhance, competition because they protect the benefits that

cardholders and merchants derive from the payment card network, thereby expanding output. By protecting these benefits, Issuers are able to offer cardholders competing products with different features (including rewards) while giving all cardholders certain basic benefits (such as fraud protection, charge-back, etc.). The NSR and HACR do not prevent payment card networks from competing for cardholders, including by competing for payment card issuance or by entering into arrangements with merchants to promote a particular payment card network to cardholders.

12. The NSR and HACR also do not prevent payment card networks from competing, including by competing for acceptance of payment cards, as is evident from the fact that merchants often accept both Visa and MasterCard credit cards, as well as Interac, and may also accept other credit cards such as American Express or other forms of electronic payment such as through PayPal.

13. At paragraph 7 of the Commissioner's Concise Statement of Economic Theory, the Commissioner alleges that the Visa Rules prevent or limit competition with respect to "Card Acceptance Fees" because "the Merchant Restraints impede or constrain the ability of Merchants to effectively encourage customers to use credit cards that result in lower costs to Merchants, or other lower-cost methods of payment." This statement is flawed in a number of respects, notably the following:

- It is not clear what is meant by "competition with respect to Card Acceptance Fees." In the Application, the Commissioner defines Credit Card Network Services as the relevant market and proceeds to conflate the separate and distinct services provided by Visa Canada and Acquirers in this one definition, failing to distinguish between demand for a product for resale and derived demand;
- The Visa Rules do not address the prices that Acquirers charge merchants for the services provided them;
- Merchants do have significant tools at their disposal (e.g., discounting) to encourage

customers to use alternative forms of payment;

- The Commissioner again wrongly compares the use of credit cards to other forms of payment by focusing solely on the costs to merchants and disregarding the benefits to consumers and merchants associated with credit card acceptance.

14. Paragraph 7 of the Commissioner's Concise Statement of Economic Theory further alleges that the Visa Rules constrain the ability of merchants to refuse to accept or surcharge higher cost credit cards, thus impeding competition within each of the Visa and MasterCard networks. Given the Commissioner's definition of the relevant market—Credit Card Network Services—it is not clear what is meant by competition *within* each of the Visa and MasterCard networks. If the Commissioner means competition between Issuers for card issuance, or competition between Acquirers for merchant acceptance, these are not markets in which Visa Canada participates.

15. In economic terms, the Commissioner's principal theory of the mechanism by which the Visa Rules have an adverse effect on competition is nonsensical. The Commissioner posits that the Visa Rules prevent merchants from encouraging cardholders to use other forms of payment and that, if merchants could steer cardholders to other forms of payment, this would constrain prices that Acquirers charge merchants for “Credit Card Network Services.” However, it is the Commissioner's position that other forms of payment cannot constrain supra-competitive prices in the market alleged to be relevant. If other forms of payment cannot constrain pricing for “Credit Card Network Services,” then steering consumers to use other forms of payment cannot have the effect the Commissioner contends.

16. Contrary to the Commissioner's allegations (e.g., at paragraph 10 of the Concise Statement of Economic Theory), the existence of the NSR or the HACR is not anti-competitive just because it may result in different customers being charged the same price for a product irrespective of whether they use a payment card or not. A competitive market does not necessitate the price to each customer being reflective of the cost to that particular customer. In any event, focusing on the costs

to the merchant as being indicative of competitiveness (or lack of competition) ignores the role of payment networks and the two-sided market, which is fundamental to understanding payment network economics.

17. Ultimately, abrogation of the Visa Rules would not "foster competition" between Visa Canada and any other party, as the Application contends; rather, it would provide merchants with a tool to reduce output on the Visa network (and impose harm on the Visa payment system) in an effort to tilt the balance in favour of merchants. Antitrust economics generally, or that related to resale price maintenance specifically, does not suggest that market intervention of this nature is warranted or desirable.



**CT-2010-010**

**AND IN THE MATTER OF** the *Companies Act*, R.S.C., 1985, c. C-34, as amended;  
**AND IN THE MATTER OF** an application by the Commissioner of Competition pursuant to section 79 of the *Competition Act*;  
**AND IN THE MATTER OF** certain agreements or arrangements implemented or enforced by Visa Canada Corporation and MasterCard International Incorporated.

**B E T W E E N:**

**THE COMMISSIONER OF COMPETITION**  
Applicant

- and - **VISA CANADA CORPORATION et al**  
Respondents

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**THE COMPETITION TRIBUNAL**

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**RESPONSE OF VISA CANADA CORPORATION**

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