No. 16-710

IN THE

Supreme Court of the United States

PHOTOS ETC. CORP., ET AL.,

Petitioners,

v.

HOME DEPOT U.S.A., INC., ET AL.,

Respondents.

On Petition for a Writ of Certiorari
to the United States Court of Appeals for the
Second Circuit

MERCHANT TRADE GROUPS RESPONDENTS' BRIEF IN OPPOSITION

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QUESTION PRESENTED

When a class-action settlement creates two different classes, one of past plaintiffs and another of present and future plaintiffs, certifies one under Rule 23(b)(3) and the other under Rule 23(b)(2), provides them with substantially different relief that disproportionately favors the Rule 23(b)(3) class, and uses the mandatory character of the Rule 23(b)(2) class to impose a sweeping, global release of all antitrust claims on class members who receive no meaningful relief under the settlement, does failing to provide those two classes with separate counsel and class representatives violate Federal Rule of Civil Procedure 23(a)(4)?

CORPOARTE DISCLOSURE STATEMENT

The Retail Industry Leaders Association has no parent corporation and there is no publicly held corporation that owns 10% or more of its stock.

The National Retail Federation has no parent corporation and there is no publicly held corporation that owns 10% or more of its stock.

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SUMMARY OF ARGUMENT

Class counsel's claim that the "importance" of this case supports certiorari has it exactly backwards. Pet. 3. To the contrary, the settlement itself achieved nothing important for merchants that accept credit cards, which is why every prominent group that represents merchants has opposed it. Whatever importance this case might have actually counsels *against* any validation of a broad release that allows defendants to purchase, in the Second Circuit's words, "permanent[] immuni[ty]" and to escape judicial scrutiny of their anticompetitive practices in return for giving merchants "actually . . . nothing." Pet. App. 27, 28.

Indeed, while the petitioners speak in broad strokes about the harm that merchants have suffered from the settlement's vacatur, the reality is far different. Although defendants and class counsel laud the settlement, it is broadly unpopular among merchants, and rightly so: The proposed (b)(2) settlement provides no meaningful injunctive relief to the (b)(2) class and has had none of the predicted salutary effects on interchange rates during the four years it has been in place. Merchants are left with the same anti-competitive rules that have long caused rising interchange rates. Consumers continue to suffer as those inflated fees lead to higher prices at checkout. It is hardly surprising, then, that neither any merchant unaffiliated with the settlement nor any consumer group supported the settlement before the Second Circuit or supports it before this Court. All are united in the view that this deal is a bad one, unworthy of resuscitation.

The winners and losers in the settlement are apparent from the parties that alone have argued for

its survival. The chief victors are defendants, who hoped they bought litigation peace and the assurance that their unlawful practices will never be challenged, for the price of the $7 billion settlement. Class counsel also supports the settlement, as it gives them a $545 million attorneys' fee award based entirely on the funds defendants are paying to a *different* group of merchants. But the monetary fund, of course, is meaningless to the millions of merchants that comprise the Rule 23(b)(2) class as the settlement proponents chose to define it. Class counsel purports to speak for merchants, but the merchants themselves, thorough their trade associations, submit this brief to make clear that class counsel does not speak for them.

This disfavor among the merchant community is not surprising, because the mandatory injunctive settlement imposed on the (b)(2) class of merchants would provide virtually no benefit to them while inflicting substantial harm through its broad release, which immunizes defendants' conduct from further merchant challenge. As the Second Circuit found, the "settlement was unreasonable and inadequate." Pet. App. 2. The illusory nature of the (b)(2) relief rebuts petitioners' claim that consummation of the settlement is in the public interest.

At bottom, Petitioners' argument boils down to a claim that the size of the settlement fund for the (b)(3) class members should induce this Court to ignore the fact that the settlement offers nothing of value for the (b)(2) class members—while requiring them to provide a broad release. *See* Pet. 34-36 (lauding the "historic sum" of the damages fund and the "compensation" it provides for class members). That petitioners rest their argument for certiorari on

such grounds aptly demonstrates that they were conflicted in attempting to represent both a (b)(2) and a (b)(3) class of merchants at the settlement table. Pet. App. 16-17.

Class counsel and defendants seek Supreme Court review to re-impose an enormously unpopular and worthless *mandatory* settlement on merchants who want no part of it. The merchant community across the board opposes Supreme Court review. This Court should deny certiorari.

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Respondents the National Retail Federation ("NRF") and the Retail Industry Leaders Association ("RILA," collectively "Merchant Trade Groups") are trade associations whose members account for more than 100,000 store locations nationwide and trillions of dollars in annual sales.

The Merchant Trade Groups are members of the broadly-defined (b)(2) class, not due to the makeup of their membership rolls, but simply because the Merchant Trade Groups—like almost every business in America—accept Visa and MasterCard credit and debit cards for certain services they provide. In their capacity as members of the (b)(2) class, the Merchant Trade Groups each objected to the (b)(2) settlement and appeared before the Second Circuit to seek its vacatur.

They now submit this opposition brief not only in their individual capacity as (b)(2) class members, but also on behalf of their thousands of members. The diverse group of merchants that encompass their membership often have diverging views on business objectives or legal goals, but on this issue they are united: This settlement is a bad deal—particularly

from the standpoint of future merchants and the vast majority who accept American Express—and was properly rejected by the Second Circuit as the product of inadequate representation. Thus, while the Merchant Trade Groups broadly agree with the points made in the Merchant Respondents' Brief in Opposition, as the recognized, day-to-day representatives of the actual merchant community, they have filed this brief to endorse the Court of Appeals' conclusion.

ARGUMENT

I. THE "INADEQUACY" OF THE INJUNCTIVE SETTLEMENT AND MERCHANTS' SUPPORT OF ITS VACATUR COUNSEL AGAINST CERTIORARI

In urging this Court's review of a highly fact-bound order that causes no Circuit split, petitioners urge adoption of a novel criterion, namely that the "settlement is simply too important to be scuttled without this Court's review." Pet. 36. This is wrong as a matter of Supreme Court certiorari jurisprudence. *Cf.* S. Ct. Rule 10 (listing only a decision on "an important question of federal law," but making no mention of the import of the settlement or case). It is also wrong on the facts.

This injunctive settlement provides no "important" relief to class members and in fact, harms them, rebutting petitioners' claim that the "importance" of the settlement compels Supreme Court review to resurrect it. *Id.* at 36. Far from "depriv[ing]" class members of a worthwhile settlement, as petitioners claim, the Second Circuit's opinion *relieves* members of the Rule 23(b)(2) class from an onerous release and "scuttle[s]" only

meaningless reforms. *Id.* at 34, 36. As Judge Leval found: "This is not a settlement; it is a confiscation." Pet. App. 33.

A. This Injunctive Settlement Is Unworthy of Resurrection: It is Only "Historic" in that It Was a Historic Confiscation

After finding that class members were inadequately represented, warranting a vacatur of the settlement and its release, the Second Circuit could have stopped there. But the Circuit went out of its way to decry the "substance of the deal that was struck" as "confirm[ing]" the inadequacy of representation. *Id.* at 22. The Second Circuit correctly found that the bargain "struck between relief and release on behalf of absent class members is so unreasonable that it evidences inadequate representation." *Id.* at 23. A review of the relief, the release and class members' objections explains why this settlement is so troubling and why resurrection of its terms would be so unwise.

1. The Worthless Relief

The (b)(2) settlement does *not* offer any relief that would facilitate competition among the banks or curb Visa's and MasterCard's market power. The Second Circuit saw this matter clearly, explaining that "class counsel trad[ed] the claims of many merchants for relief they cannot use: they actually received nothing." *Id.* at 27.

That the injunctive relief did "nothing" is largely due to two fatal infirmities of the settlement: (1) The injunctive settlement does not even attempt to reform the most problematic anticompetitive rules, namely, honor-all-cards and default interchange, and

(2) its modification to the "no surcharging" rule is so limited that virtually no merchants would actually be able to surcharge if they wanted to—as borne out by the striking absence of the practice over the past four years.

Petitioners aptly describe the market power of Visa and MasterCard in establishing steadily increasing interchange fees. Pet. 5. Missing from class plaintiffs' discussion—and not by chance—are the two leading drivers of these steadily increasing interchange fees: the honor-all-cards and default interchange rules, though plaintiffs highlighted these rules in their complaint. *Cf.* Pet. 5-6 (no mention of these rules). The Second Circuit explained the import of these two anti-competitive rules. "The 'honor-all-cards' rule requires merchants to accept all Visa or MasterCard credit cards if they accept any of them, regardless of the differences in interchange fees." Pet. App. 5. It effectively "force[s] merchants to accept all Visa and MasterCard credit cards," because "few merchants can afford to accept none of them." *Id.* And "default interchange" is the "supra-competitive rate" for interchange fees set by the defendants as the default; this default rate is "effectively locked in . . . because the issuing banks have little incentive" to "enter[] into a separate agreement," "unless a given merchant is huge enough to have substantial bargaining power." *Id.* at 5-6.

Crucially, the settlement does not even purport to reform the honor-all-cards or default interchange rules. Obtaining an injunction against enforcement of these rules would be the s*ine qua non* of the injunctive relief merchants would seek at trial, as in previous antitrust actions against Visa and

MasterCard. *Cf. Wal-Mart Stores, Inc. v. Visa U.S.A., Inc.*, 396 F.3d 96, 101 (2d Cir. 2005) (revoking by settlement rule tying merchant acceptance of debit cards to credit cards); *United States v. Visa U.S.A., Inc.*, 344 F.3d 229, 234 (2d Cir. 2003) (rescinding prohibition on issuance of AmEx and Discover cards). Yet the settlement provides merchants with no relief whatsoever from these rules. (And, as detailed below, the settlement would release merchants' right to seek to reform these rules through a separate litigation).

The changes to the one set of rules that were modified by the settlement—the rules banning surcharging—were so limited that the relief was meaningless to virtually every merchant. This is not speculation. It was known at the time of settlement and has been further demonstrated in the four-plus years since the settlement went into effect.

The settlement's limited "permission to surcharge" is useless to three groups of merchants that collectively encompass the overwhelming majority of merchants. *First*, the settlement was drafted in such a way as to make the relief meaningless to merchants who also accept American Express. Specifically, the settlement contains a "most-favored-nation" clause that "permits surcharging for Visa or MasterCard only if the merchant also surcharges for use of cards issued by competitors such as American Express." Because "American Express effectively prohibits surcharging," "merchants that accept American Express cannot avail themselves of the surcharging relief." Pet. App. 8. Nearly 70% of merchants accept American Express—representing 90% of card volume—and not one of these merchants can

surcharge Visa or MasterCard products and continue to accept American Express. *Second*, the surcharging modifications are valueless to the merchants in the ten states that *prohibit* surcharging—roughly 40% of merchants. They cannot surcharge regardless of the settlement terms. *Third,* "merchants that begin business after July 20, 2021 gain no benefit at all," although they are bound by the release. The effect of state laws, the American Express rules, and the 2021 expiration date of relief was no secret; as the Second Circuit found, "class counsel knew at the time the Settlement Agreement was entered into that this relief was virtually worthless to vast numbers of class members." *Id.* at 27.

Before this Court, however, class counsel attempts to resurrect the claim that the theoretical ability to surcharge—unusable by nearly every merchant—will allow merchants to "steer consumers toward lower-cost forms of payment," which will somehow "place downward pressure on interchange fees going forward." Pet. 2. When this claim was originally made it rested on a baseless foundation. But now, four years into the settlement, it is clear that the hoped-for "downward pressure on interchange fees" from the surcharging modification has not materialized.

The settlement's injunctive relief took effect upon preliminary approval in November 2012—well over four years ago. And the injunctive relief has remained in place ever since. While defendants had the right to terminate the settlement upon the Second Circuit's vacatur, for reasons about which we can only speculate, defendants have not bothered to revert to the pre-settlement rules. *See In re Payment Card Interchange*, 05-md-1720, dkt. 6745 (Nov. 28,

2016). As a result, the injunctive relief has been in effect for the last four-plus years and we are now nearly halfway through the period of relief, which ends in 2021. So before claiming that this settlement is “historic”—indeed, so “historic” that it warrants Supreme Court review—it is worth considering the on-the-ground effects of this so-called surcharging relief.

The results are glaring: In the four-plus years since the settlement went into effect, there has been little to no surcharging or steering of consumers and no reduction in interchange fees.[1] There is little evidence that merchants have actually *used* this supposedly “groundbreaking” relief, much less that it has effected a “sea change” in the industry. “Virtually worthless to vast numbers of class members,” indeed. *Id.* at 27.

These real-world effects—or, rather, non-effects—of the settlement are consistent with admissions from MasterCard’s and Visa’s CEOs that the settlement’s surcharging relief will have limited practical effect on their businesses. Visa’s CEO stated: “[W]e do not look at surcharging *per se* as it relates to this litigation as something that will . . . significantly affect us at all. I mean, that’s our feeling about it.” Ct. App. JA2342. Similarly,

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[1] *Compare* Nilson Report Issue 1022 (July 2013), available at http://www.businesswire.com/news/home/20130801006868/en/Merchant-Processing-Fees-U.S.-Nilson-Report *with* Nilson Report Issue 1065 (June 2015).) http://www.businesswire.com/news/home/20150624005977/en/Nilson-Report-U.S.-Merchant-Card-Fees-2014 (based on most recent data, card processing fees virtually unchanged between 2012 and 2014).

MasterCard's CEO stated that, based on his "experience of [allowing limited] surcharging in other markets[,] . . . frankly it didn't really lead to a great deal of actual surcharg[ing]," except for "online airline bookings and the like." Ct. App. JA2390, 2393. These CEOs know their business. It is therefore no surprise that, even after the Second Circuit vacated the settlement and the attendant release, the defendants were willing to continue to offer essentially meaningless surcharging relief.

2. The Unprecedented Scope of the Release

As the Second Circuit explained, the settlement's broad release "permanently immunizes the defendants from any claims that any plaintiff may have now, or will have in the future, that arise out of, e.g., the honor-all-cards and default interchange rules." Pet. App. 28. That permanent immunity means that "defendants never have to worry about future antitrust litigation based on their honor-all-cards rules and their default interchange rules." *Id.* at 29. In fact, the release covered every rule in the defendants' vast rulebooks, even "substantially similar" future rules and conduct. *Id.* at 9. Defendants purchased that immunity with a $7.25 billion payment to the (b)(3) class in exchange for a sweeping mandatory release from the (b)(2) class and no meaningful modification of Defendants' practices to conform to the law. It is no surprise that Visa and MasterCard sought this broad release, but we should celebrate, not bemoan, its disappearance.

The scope of the release is staggering. The release is not limited to future injunctive claims: Members of the mandatory Rule 23(b)(2) class must also release claims for damages. It is not limited in temporal

scope: While the injunctive relief expires in 2021, "this release has no end date." *Id.* at 9. Nor can any class member exclude itself from the release: It is imposed on all members of the mandatory Rule 23(b)(2) class. Even merchants that do not come into existence until *after* 2021 cannot exclude themselves. The scope of the mandatory class is unprecedented, capturing literally millions of current and future merchants—likely the largest class of merchants ever bound in a single judgment.

The mandatory nature of this release is particularly disturbing: Even the most sophisticated merchant is deprived of the right to decide for itself whether the modification of the surcharging ban is sufficient to justify granting this release. The result is that even those merchants who excluded themselves from the Rule 23(b)(3) settlement and are currently litigating opt-out lawsuits cannot seek damages for ongoing antitrust violations.

3. The Breadth of Opposition from the Trapped Class

That this settlement offers so little and that its vacatur does not warrant Supreme Court review is further demonstrated by the extent of the opposition. By volume, more than 25% percent of merchants opted-out of the (b)(3) class and some 20% filed formal objections to the (b)(2) injunctive relief. Of the 19 original class representatives, 10 objected to the settlement, including all six trade association class representatives whose primary interest in the case was injunctive relief for their thousands of members. Dozens of trade associations—including NRF and RILA—collectively representing the interests of tens of thousands of merchants opposed the settlement. No merchant—not one—uninvolved in the settlement

negotiations voiced support for it. This reaction stands in stark contrast to the apathetic response to virtually all class action settlements, particularly *injunctive* class settlements.

It is striking that in a case that class counsel characterizes as offering a "historic" and "groundbreaking" settlement, Pet. 35, not a single person—no merchant, no consumer—has appeared as an amicus to support the value of the supposedly "historic" relief that the settlement gives to merchants or to explain away Visa and MasterCard's attempt to release all future liability. Instead, the Merchant Trade Groups, on behalf of merchants representing 100,000 store locations nationwide, actively oppose the settlement. And interim co-lead counsel for a putative class of plaintiffs seeking class certification pursuant to Rule 23(b)(2) (appointed by the district court in this case on November 30, 2016) also has not sought this court's intervention. Every indication shows that the merchants that this "historic" settlement is supposed to benefit appear to believe they are better off with vacatur.

In the face of this unprecedented level of class member objection to this valueless settlement, it is worth noting who is asking this Court to take on this case: class counsel, who wishes to secure their $545 million fee award, and defendants, because the settlement gives them *carte blanche* to continue to mandate acceptance and fix interchange rates without fear of future suits from the merchants who are the targets of their conduct. The value of such immunity is, to quote a MasterCard slogan, "priceless."

B. The Class's Interests Are Better Served By Allowing This Case to Proceed

Any outcome that results from vacating this settlement is better than approving a settlement that grants defendants "permanent[] immuni[ty]" while merchants "actually receive[] nothing." Pet. App. 27, 28. Petitioners' brief warns darkly of the "risk to merchants of losing the benefit of this groundbreaking settlement" if the Second Circuit is not reversed. Pet. 3. These risks are fabricated. Any result is far better than binding unwilling merchants to a harmful settlement.

1. The Parties May Settle on Terms that Are More Fair

Vacating this settlement and correcting the structural flaws that led to it in the first place may allow the parties to go back to the drawing board to reach a settlement with terms that are more fair—aided in that effort by counsel actually focused on the value of prospective relief *as such*, and not just the value of a prospective *release* to grow the pot of money awarded to the (b)(3) class.

The first time at the bargaining table, this case was settled on the back of the merchants' injunctive claims. As the Second Circuit explained, class counsel was conflicted during the negotiations in representing both merchants in the (b)(3) class who "would want to maximize cash compensation for past harm," and those in the (b)(2) class who "would want to maximize restraints on network rules to prevent harm in the future." Pet. App. 16. Without counsel tasked solely with representing merchants whose interests were in "prevent[ing] harm in the future,"

the (b)(2) class members were required to accept a "confiscat[ory]" settlement. *Id.* at 16, 33.

Once the Second Circuit's vacatur is final, defendants will have an incentive to return to the bargaining table because, as Judge Leval notes in his concurring opinion, "the fact that the Defendants were willing to pay $7.25 billion, apparently the largest antitrust cash settlement in history, suggests that the claims were not entirely devoid of merit." *Id.* at 33. And, since merchants pay $40 billion each year in interchange fees, the potential damages at trial far outstrip the current settlement's value. Ct. App. JA1906 ¶ 12.

Indeed, defendants have repeatedly demonstrated that they believe this settlement is a great deal for them: That they have joined in class counsel's request for certiorari demonstrates that they recognize that if they went back to the bargaining table with unconflicted counsel for the merchant classes, defendants would have to offer more. *Cf.* Def. Br. 9 They are right. Adequate new counsel must demand better; unconflicted counsel would not cede to defendants' meaningless settlement offer. Indeed, adequate counsel may determine that no mandatory (b)(2) class is even appropriate here. *See* Pet. App. 32-35 (Leval, J., concurring). Moreover, even though the high rate of opt-outs (more than 25% percent by volume) entitled defendants to abandon the settlement, they have chosen not to. Similarly suggestive is defendants' decision to continue to provide the injunctive "relief" even after the Second Circuit vacated the settlement, without any certainty of a release in return. Notably, defendants' brief never claims they would refuse to settle on other terms.

2. No Settlement at All Is Better than Resurrecting This Flawed Settlement

Even if the parties cannot reach a new settlement that provides *both* damage relief to the Rule 23(b)(3) class members and meaningful injunctive relief to a Rule 23(b)(2) class, the (b)(2) class members would be better served by vacatur. Faced with the choice between a "confiscat[ory]" release that "permanently immunizes" defendants' anti-competitive conduct and no settlement at all—thereby preserving merchants' future right to pursue these claims— merchants prefer the latter, further demonstrating why certiorari should not be granted.

CONCLUSION

For the reasons stated above and in Merchant Respondents' Brief in Opposition, the petition for a writ of certiorari should be denied.

Dated: February 21, 2017
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CERTIFICATE OF COMPLIANCE

Pursuant to Supreme Court Rule 33.1(h), I hereby certify that the foregoing Merchant Trade Groups Respondents' brief in opposition contains 3,587 words, excluding the parts of the document exempted by Supreme Court Rule 33.1(d).

I declare under penalty of perjury that the foregoing is true and correct.

Executed on February 21, 2017.

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