

LAWDRAGON

Cravath's Long Road to Justice For American Express



Photo of Kevin Orsini, Evan Chesler and Peter Barbur provided by Cravath.

The U.S. Department of Justice turned its eye to credit card companies in 2010, suing Visa, Mastercard and American Express to challenge merchant acceptance rules that allegedly violated federal antitrust laws.

“With today’s lawsuit we are sending a clear message: We will not tolerate anticompetitive practices,” said then Attorney General Eric Holder in a press release announcing the suit, which followed an investigation begun in 2007. “We want to put more money in consumers’ pockets, and by eliminating credit card companies’ anticompetitive rules, we will accomplish that.”

Visa and Mastercard, which controlled 70 percent of the market with cheaper cards, settled faster than you can say “charge it.”

AmEx decided to fight, declaring war in an article penned by CEO Kenneth Chenault, which was published in *The Washington Post*.

“The Justice Department is supporting bad policy and disguising it with vague promises of consumer benefit. We think their case is weak and we intend to fight it.”

“It’s never easy to take on a long, costly battle with the government, but what’s at stake are some important issues: consumer choice, free market competition and the ability to deliver superior products and services to our customers. This is a fight worth fighting,” Chenault wrote.

To lead the battle, he chose Cravath, whose brand is pure platinum, while its essence is true grit. Time and again, the firm has joined with clients facing the toughest of odds, assessed their chances and strategized a ground war that defines the truest path to success.

Which makes it even sweeter when that day arrives. For AmEx and Cravath, that day was Sept. 26, 2016 – nearly a decade after Chenault called Evan Chesler, then the firm’s presiding partner, and its longtime lead litigator to say he had a problem.

Chesler began that early autumn day at a meeting of the Executive Committee of New York University’s Board of Trustees. Taking one last look at his email before the Board meeting started, one particular message caught his eye. He walked out into the hallway, and called Cravath partner Kevin Orsini.

“Is this what I think it is?” he asked.

When he received Chesler’s call, Orsini was looking at the cup of coffee he had spilled as he saw the docket entry pop up on his iPhone. He confirmed Chesler’s suspicions while forwarding the news to the head of litigation at AmEx. Orsini rushed back to his office and called his client.

A Winning Appeal

The 2nd U.S. Circuit Court of appeals had handed AmEx and Cravath a massive victory, finding a trial court decision was in error by focusing only on the impact of credit card protocols on merchants, instead of also taking into account the cardholder side of the market.

The Cravath team had been waiting for

this moment for nine months – just the latest battle in the litigation war that had defined much of Orsini’s legal career. Following the tough loss after a trial before federal judge Nicholas Garaufis, Cravath appealed to the 2nd Circuit, which heard arguments Dec. 17, 2015.

In his argument, Chesler had outlined why the court was wrong to focus only on merchant fees – devoid of any consideration of consumer choice in payment methods. The very next day dawned auspicious as the Second Circuit independently lifted the stay on AmEx. It was a good sign when the court suspended the injunction without a motion, says Chesler. “But what we didn’t know was what they ultimately would say and what the bottom-line determination would be. Would it be a remand to further proceedings or would it be a remand with instructions to enter judgment? What would the reasoning of the opinion be?”

Patience proved, once again, a virtue.

As the 2nd Circuit wrote, the district court’s “approach does not advance overall consumer satisfaction. Though merchants may desire lower fees, those fees are necessary to maintaining cardholder satisfaction — and if a particular merchant finds that the cost of Amex fees outweighs the benefit it gains by accepting Amex cards, then the merchant can choose to not accept Amex cards.”

A Long View from the Start

“Taking the long view” was one of many valuable lessons Orsini took from the saga. In 2007, the government sent their first request for documents, Orsini recalls, “at which time I was a bright-eyed associate who had just been assigned to the great Evan Chesler, and one of the first things I was tapped with was working on this case.

“I distinctly remember the very, very early days of this and, as a young associate, taking

the time to go through reams of economic literature on the payment-card industry and two-sided markets.” said Orsini.

Chesler vividly remembers the call from AmEx, for whom the firm had done a few antitrust matters before, but the relationship was still young. “Frankly, this probably says more about my flaws than anything else, but I’m always optimistic, even when I shouldn’t be.

“I thought the government would go through the process and would ultimately be persuaded that there was nothing there – that this was not something they should devote any more time to. Obviously, that was wrong,” Chesler says. “That said, I respect the government and I respect their view of things. I believe that they believed this was a problem they had to address.”

When the lawsuit was filed, Chesler reached out to Cravath partner Peter Barbur, with whom he had done many trials in the past and who had recently returned from The Sedona Conference, where the credit card litigation was the talk of the town. And once again, Chesler called Orsini, who had recently completed his associate training rotation.

“About two days after I was elected a partner, Evan came to me and said, ‘You want to work on this case?’ I stopped celebrating for a moment and said, ‘Absolutely.’”

The AmEx victory provides a casebook study in Cravath’s long-run strategy. “The first thing we did was spend a tremendous amount of time understanding the client’s business, understanding what made them tick, understanding their history,” said Orsini. “We learned about the experiences that AmEx had suffered at the hands of its more dominant competitors and their challenges.”

That laid the groundwork for a partnership between client and firm – “a partnership in figuring out what was the best way to resolve this from the client’s perspective,” said Orsini.

“Every great trial lawyer wants to try lots of great cases,” he said. “But that’s not always in the client’s best interest, so what we focused on here was understanding whether there was another approach that we could take or whether this was something that we should fight to the end.”

To Chesler, Chenault’s determination to take a stand for the company he had spent most of his career building was defining. “One of the great things here was the fact that [Kenneth Chenault] lived the history that Kevin was reading.

“In the course of all the work we did to understand the history and the business, one of the things that came out fairly early on was Ken Chenault’s having personally called the company to arms 20 years before, when it faced the real and present danger of extinction at the hands of its dominant competitors. Those competitors were waging a war to undermine the AmEx business model, to attack AmEx at the point of sale, to conduct a steering exercise that would lure customers away from the AmEx brand through the Visa and Mastercard brands.”

So essential to the story of AmEx was Chenault’s experience, that it became a pillar of the trial strategy.

“To [Chenault’s] credit and to the credit of his management team, AmEx had the courage and commitment to say, ‘This is an assault on our entire business model and we have to stand for something. We have to stand for principle here. We’re going to fight this and we’re going to defend ourselves.’ We were very, very fortunate to be standing there when they made that judgment and to have the opportunity to work with them in telling their story,” said Chesler.

To win, Cravath and AmEx also needed to persuade the appellate court that the Justice Department was wrong by half – which is to say that it was in error by only looking at the

merchant side of the market. And that the only true way to measure competition in the credit card market was to look at the whole – the merchant side as well as the consumer side, and how the interaction of the two in the form of processing fees impacted consumers.

“It was so clear to us from the outset that this was a market that really revolved around the coming together of three pieces: a consumer with her card; a merchant from whom she wishes to buy something; and the connective tissue of a credit infrastructure that unites the two of them to accomplish a transaction,” explained Chesler.

While disappointed with the district court judge’s decision after a seven-week trial, Cravath looked at the case anew to prepare the appeal. “The judge acknowledged our view of the two-sided market,” said Barbur, “he just said he wasn’t going to go there.”

“If you do complex litigation as we do, you’re constantly looking at the case anew,” says Chesler. “You’re constantly evaluating and re-evaluating, you’re constantly looking at the case through the other side’s eyes to make sure that you’re not myopic, that you’re not falling in love with the case instead of looking at it critically.”

The harsh review “reaffirmed our view that we had the right side of this argument, but we didn’t blindly follow it. We stepped back, held everything up to the light and looked at it with a critical eye all over again. That’s our job.”

When December 17, 2015 rolled around, the Cravath team teased out their arguments about the so-called “Non-Discrimination Provisions.”

“Non-Discrimination Provisions go by that name for a reason,” says Chesler. “If you think about how odd it would be to, for example, go into a car dealership to buy a Honda, and have the dealer say to you, ‘You know what? Do me a favor and go next door to our sister agency and buy a Chevy Cruiser because we’ll make

an extra \$50 commission. You don’t really want the Honda anyway.’”

“Think of the management team back at Honda and whether they would think it was a great idea to continue to sell cars through that first dealer who was directing consumers to buy the car of a competitor. It seemed to us common sense that that’s not what antitrust laws were designed to prohibit. But it’s obviously a subject about which people could have a debate or the government would not have proceeded with the case.”

An Impactful Decision

Needless to say, when the 2nd Circuit released its unanimous decision the effects were as immediate as they may be long-lasting. Since the Justice Department and State Attorneys General commenced their investigations a decade ago, credit card litigation has become a booming industry.

“To us, the Second Circuit has clearly signaled its agreement with our view throughout this case, which centered on the fact that, to understand competition and the marketplace, you have to look at both sides. We think this decision will be important as we deal with remaining litigation for AmEx,” says Orsini.

Chesler says the concept of two-sided markets is far from a new phenomenon. “It has been around for quite awhile and there are live two-sided markets in our economy. This is one of them. Because the 2nd Circuit is an important, prominent court, I’m sure other courts will look at this decision and be guided by it. But this is not a revolutionary principle.

“Early on in the learning process it was evident to us that, without a consumer and a merchant, there was no transaction in the first place. Merchants don’t buy their own products and consumers need stores from which to buy their product. It seemed clear to us that it takes two to complete a transaction.”

The model is core to many businesses – such as newspapers, which publishers sell to subscribers while selling space to advertisers. There are different forms of two-sided markets, and this one involves transactions where there’s a simultaneity to things. The transaction takes place the moment the consumer and the merchant come together with the network as the interconnecting fabric.

What does the win mean for American Express? Among other things, American Express had flagged the litigation as having the possibility of a material adverse effect on its business – not quite a signal of a terminal condition, but a caution, at the very least.

“Ken Chenault said this case was mission critical,” says Chesler. “It was a courageous choice to stake out that position at the outset and to have the fortitude to stick with it. We’re all very grateful that the business model has been vindicated.”

Lessons Learned

All ground wars require a period of reflection, and for the Cravath team the AmEx victory provided at least three compelling points of view.

To Orsini, “looking down the road, this victory helps solidify what I’ve been trained to do as a Cravath litigator. The importance of approaching a case from the beginning by looking at the fundamental, basic questions of: ‘What is the best outcome here for the client and how does the client’s business relate to this lawsuit?’ This victory underscored the significance of that approach.”

And, however long the litigation takes, “never fall in love with your case and never fall in love with a particular argument. We were constantly trying to approach this case from different angles to put ourselves in the

strongest position possible once we got to the argument.

“The success was obviously very satisfying, but it also reinforced for me the right way to litigate for your client,” said Orsini.

Barbur looks back on working with Chesler since 1991. “Many, many cases and trials together later, this was for me a really great capstone to 25-plus years of collaboration with an amazing partner and a great person to learn from.”

And for the legendary Chesler? “This victory says to me a number of things. First, the Cravath system, the entire firm is founded on the concept of teams. We are all acutely aware that no one person excels alone. It just isn’t possible, and there are a lot of people engaged in the mythology of one-man bands and remarkable accomplishments done in isolation. That is mythology in my four decades of experience,” he said.

He pointed in particular to the efforts of Orsini, Barbur, and a large team of associates whose work was “exemplary and absolutely invaluable” to the outcome. He also noted the contribution of recently retired partner Stuart Gold; Chesler and Gold worked on their first trials together, and for Gold, his last.

“Cravath is a firm founded on the concept that collective effort will always exceed in quality what any one individual can do on his or her own. This is a great testament to that principle.

“Second, I am reminded that Tom Barr, who taught me how to try cases, used to say all the time, ‘Don’t do it for the applause.’ Success is gratifying, of course. But at the end of the day, we don’t do it for the applause,” said Chesler. “We do it because that’s our life’s work. That’s what we do. Seeing that your hard work is recognized and the client has benefited from it is as good as it gets.”

CRAVATH, SWAINE & MOORE LLP