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IN THE COMPETITION
APPEAL TRIBUNAL

Case No. 1160-65/1/1/10

Victoria House,
Bloomsbury Place,
London WC1A 2EB

2 November 2011

Before:

VIVIEN ROSE
(Chairman)
DR ADAM SCOTT OBE TD
DAVID SUMMERS OBE

Sitting as a Tribunal in England and Wales

BETWEEN:

(1) IMPERIAL TOBACCO GROUP PLC
(2) IMPERIAL TOBACCO LIMITED

Appellants

– v –

OFFICE OF FAIR TRADING

Respondent

CO-OPERATIVE GROUP LIMITED

Appellant

– v –

OFFICE OF FAIR TRADING

Respondent

WM MORRISON SUPERMARKET PLC

Appellant

– v –

OFFICE OF FAIR TRADING

Respondent

**(1) SAFEWAY STORES LIMITED
(2) SAFEWAY LIMITED**

Appellants

– v –

OFFICE OF FAIR TRADING

Respondent

**(1) ASDA STORES LIMITED
(2) ASDA GROUP LIMITED
(3) WAL-MART STORES (UK) LIMITED
(4) BROADSTREET GREAT WILSON EUROPE LIMITED**

Appellants

– v –

OFFICE OF FAIR TRADING

Respondent

**(1) SHELL UK LIMITED
(2) SHELL UK OIL PRODUCTS LIMITED
(3) SHELL HOLDINGS (UK) LIMITED**

Appellants

– v –

OFFICE OF FAIR TRADING

Respondent

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HEARING (DAY 25)

Note: Excisions in this transcript marked “[...][C]” relate to passages excluded.

APPEARANCES

Mr Mark Howard QC, Mr Mark Brealey QC and Mr Tony Singla (instructed by Ashurst LLP) appeared on behalf of the Appellants Imperial Tobacco Group Plc and Imperial Tobacco Ltd.

Mr Rhodri Thompson QC and Mr Christopher Brown (instructed by Burges Salmon LLP) appeared on behalf of the Appellant Co-operative Group Ltd.

Mr Pushpinder Saini QC and Mr Tristan Jones (instructed by Hogan Lovells International LLP) appeared on behalf of the Appellants WM Morrison Supermarkets Plc and Safeway Stores Ltd and Safeway Ltd.

Mr James Flynn QC and Mr Robert O'Donoghue (instructed by Norton Rose LLP) appeared on behalf of the Appellants Asda Stores Ltd, Asda Group Ltd, Wal-Mart Stores (UK) Ltd and Broadstreet Great Wilson Europe Ltd.

Ms Dinah Rose QC and Mr Brian Kennelly (instructed by Baker & McKenzie LLP) appeared on behalf of the Appellants Shell U.K. Ltd, Shell U.K. Oil Products Ltd and Shell Holdings (U.K.) Ltd.

Mr Paul Lasok QC, Ms Elisa Holmes, Mr Rob Williams, Ms Anneliese Blackwood and Ms Ligia Osepciu (instructed by the General Counsel, Office of Fair Trading) appeared on behalf of the Respondent.

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1 Wednesday, 2 November 2011
 2 (10.00 am)
 3 **THE CHAIRMAN:** Mr Howard.
 4 **MR HOWARD:** Yes.
 5 **THE CHAIRMAN:** Are you going to say something?
 6 **MR HOWARD:** I am receptive to whatever the Tribunal wishes
 7 to say to me. I am always receptive.
 8 **THE CHAIRMAN:** We asked for a timetable for the next two
 9 days.
 10 **MR HOWARD:** Where we have just got to, we just asked
 11 Mr Lasok, and he has told us that his estimate was, just
 12 for his cross-examination, not more than one hour for
 13 Ms Williams, not more than four hours for Mr Culham, and
 14 not more than three hours for Mr Wragg, and not more
 15 than 15 minutes tomorrow morning to answer or to state
 16 what the OFT's position is.
 17 **THE CHAIRMAN:** And as far as re-examination is concerned?
 18 **MR HOWARD:** Re-examination is difficult to assess, because
 19 it is reactive, I don't prepare my re-examination in
 20 advance, so it slightly depends on what questions are
 21 and are not asked. But in the light of the history of
 22 things, we need to assume, I would think, Ms Williams,
 23 half an hour for her, and up to an hour for Mr Culham
 24 and Mr Wragg.
 25 So that means that we are a little bit tight over

1

1 the next two days and we may have to actually shorten
 2 things a bit. I would suggest perhaps we just proceed
 3 for the moment and see how we get on, but we may have to
 4 be a bit more rigid.
 5 Mr Lasok's times are clearly maxima.
 6 **THE CHAIRMAN:** Yes. Let's start with Ms Williams, but we
 7 will then keep you to an hour maximum, and if you can
 8 shave a little bit off that, that will be all to the
 9 good.
 10 Can we go and ask Ms Williams to come in, please.
 11 MS CYNTHIA ISOBEL WILLIAMS (affirmed)
 12 Examination-in-chief by MR HOWARD
 13 **THE CHAIRMAN:** Thank you, Ms Williams. Please sit down.
 14 **MR HOWARD:** Could I ask you to be given, Ms Williams,
 15 volume 3 of the core bundle, and just while that's being
 16 located could you just for the record confirm your full
 17 name and address, please.
 18 **A.** Cynthia Isobel Williams [redacted].
 19 **Q.** Thank you very much. Now you are being handed a file,
 20 and if you would turn in that file -- I think it's open
 21 at tab 43, which should be your witness statement.
 22 {C3/43/614} Do you have that? I think it's open
 23 already. Is that your witness statement?
 24 **A.** Oh yes, sorry. Yes.
 25 **Q.** I just want you to confirm that is your witness

2

1 statement and that the contents of it are true?
 2 **A.** Yes, it is.
 3 **MR HOWARD:** Thank you very much.
 4 Cross-examination by MR LASOK
 5 **MR LASOK:** Ms Williams, as I understand it, you were
 6 employed by Somerfield as tobacco buyer as from,
 7 I think, March 2005?
 8 **A.** That's correct.
 9 **Q.** I am therefore assuming that you have actually no
 10 knowledge about what was going on in Somerfield
 11 between 2000 and 2003?
 12 **A.** Well, I wasn't there at the time, so I do not have
 13 direct knowledge.
 14 **Q.** What knowledge do you have?
 15 **A.** The knowledge I would have is that when I joined the
 16 company, I would have gone, looked through the
 17 historical records to assess what their pricing policy
 18 was, what the trading agreements were, so I would have,
 19 through files at the company, established some
 20 knowledge, but I wasn't there at the actual time.
 21 **Q.** So that your knowledge is that which you gleaned from
 22 reading the documents?
 23 **A.** That's correct.
 24 **Q.** Okay, thank you. For that reason, I am not going to ask
 25 Ms Williams any further questions about Somerfield.

3

1 So far as First Quench is concerned -- this is
 2 paragraph 3 of your witness statement, at the top of the
 3 page {C3/43/615}. In the third line you say that you
 4 were the tobacco buyer at First Quench from June 2003?
 5 **A.** That's correct.
 6 **Q.** Mr Cheyne, however, said when he was giving evidence --
 7 and for the Tribunal's reference this is the transcript
 8 for Day 23 at page 78, line 16, I think, to page 79,
 9 line 5 -- that he brought you over to First Quench
 10 originally as a consultant in June 2003 to work with him
 11 on a particular project concerning, I think, a gantry
 12 agreement. He thought that you became the tobacco buyer
 13 some time afterwards, but he didn't remember when.
 14 **A.** The title -- yes, I joined initially as a consultant.
 15 David was -- David Cheyne was already there. One of his
 16 projects was renegotiating a gantry contract. He also
 17 wanted me to get stuck into the day-to-day buying,
 18 because the girl who was doing the buying was literally
 19 leaving the next day because she was pregnant. And
 20 there was somebody else who was buying, I think, spirits
 21 at the time and they desperately needed help. So I was
 22 actually getting stuck into that.
 23 Plus they had -- there was a new government
 24 regulation coming in -- I am trying to remember exactly
 25 which one it was -- and they needed somebody to put in

4

1 a due diligence procedure and manage that. So it's
 2 true, I was a consultant initially, but by September, it
 3 was the end of September, First Quench offered me
 4 a contract to work for them permanently. So the
 5 official title of buyer would have applied from the end
 6 of September of that year.

7 **Q.** The --

8 **A.** But in effect I was doing the job as a buyer from June.

9 **Q.** The first document in the file that we have which
 10 mentions you is dated 21 July 2003. Maybe the best
 11 thing is if I ask you to look at it. Could you possibly
 12 have a look at annex 16, please, and turn to tab 51.
 13 That's two emails. If you look at the first one in
 14 time, it's the one in the middle of the page, which
 15 starts just below the first holepunch, and it was sent
 16 to you on 21 July {D16/51/113}. The document preceding
 17 that is in tab 50, it's dated 20 June 2003, and was
 18 addressed to Sarah-Jane Hodson {D16/50/111}. Do you
 19 remember who she was?

20 **A.** Sarah-Jane Hodson was not the pregnant lady, she was the
 21 spirits buyer who had been helping out on tobacco at the
 22 time. So she was temporarily handling day-to-day
 23 affairs on tobacco.

24 **Q.** Perhaps for the sake of completeness, if you go to 49,
 25 tab 49, you have a letter dated 25 February 2003

5

1 {D16/49/110}. That was sent by Imperial to Fiona -- is
 2 that Gittus?

3 **A.** It was pronounced "Gittus". She was the lady that was
 4 pregnant.

5 **Q.** When did she go off?

6 **A.** She went off the week -- I think my first day was the
 7 Monday in June. She left actually at the end of that
 8 week. So I was only there for four or five days when
 9 she was there.

10 **Q.** Then we have Sarah-Jane Hodson who was sent the letter
 11 at tab 50 {D16/50/111}, and she was therefore dealing
 12 with the negotiation of the trading agreement, wasn't
 13 she?

14 **A.** Sorry?

15 **Q.** It looks as though she was dealing with the negotiation
 16 of the trading agreement, or rather --

17 **A.** Sarah-Jane?

18 **Q.** Or rather she was involved in the reviewing of the
 19 signed trading agreement?

20 **A.** I can't confirm that, I wouldn't have direct knowledge.
 21 I would imagine she would -- I would think that she
 22 wouldn't have been solely responsible for negotiating
 23 that agreement. It would have been Fiona Gittus, or
 24 indeed the training director. But I would have no
 25 direct knowledge. I haven't seen this note before.

6

1 **Q.** But you yourself weren't involved at that stage?

2 **A.** No. No, I confirm I wasn't involved. When I arrived,
 3 it was -- it had been -- it was a done deal. So
 4 I inherited that trading agreement.

5 **Q.** It may sound a bit trivial to you, but I am just trying
 6 to get a rather more precise idea about when exactly it
 7 was that you became involved in the day-to-day
 8 management of the trading relationship between --

9 **A.** June. It was June.

10 **Q.** But when in June?

11 **A.** To be honest, I can't remember the exact date. I think
 12 it was probably like the second or third week of June.
 13 But I wouldn't be able to guarantee that for you.

14 **Q.** Now, if we go back to your witness statement, could you
 15 look at paragraph 10, please {C3/43/616}. You there say
 16 that, in the second line:

17 "I understand the pricing tiers were simplified into
 18 three tiers just before I commenced my position at
 19 First Quench."

20 I was a little puzzled about that, because if you go
 21 to tab 31 in annex 16, you should have here a letter
 22 from ITL or Imperial to Mr Plummer, the trading director
 23 at First Quench, dated 30 August 2002.

24 If you look at paragraph 6 at the bottom, he says:

25 "I note that from 19 August you moved to three price

7

1 tiers as follows."

2 Somebody has written under the 19th another date,
 3 the 26th. But it looks as though it was in August 2002
 4 that the move to three price tiers took place. Does
 5 that help your recollection?

6 **A.** I haven't seen this letter before, so I can't -- it
 7 doesn't help me, no. When I joined, I was led to have
 8 understood it was earlier in 2003, but I wouldn't know
 9 exactly when. It was certainly before I arrived they
 10 had moved to three pricing tiers.

11 **Q.** We have a slightly different explanation in tab 44(a).
 12 It should be the tab after: not 44, the one immediately
 13 after it. I am hoping that you have a 44(a).

14 **A.** Yes.

15 **Q.** Which is a document entitled "Business development
 16 plan", and it has a name there, George Byas
 17 {D16/44A/88}. Did you ever come across George Byas?

18 **A.** No.

19 **Q.** If you look at the stamped pagination in the bottom
 20 right-hand corner and go to page 23 -- the date of this
 21 document, by the way, is February 2003 -- on page 23
 22 {D16/44A/94} you have a heading "Pricing", and in the
 23 second paragraph he says that cigarettes are now in
 24 three tiers with the exception of two closely aligned
 25 tiers in parts of Scotland. Does that ring any bells?

8

1 A. No, I mean, I have not seen this note before. The
 2 pricing that's mentioned, tier 1, tier 2, tier 3, where
 3 they are just defining what premium or reductions above
 4 the manufacturer's recommended price, I was aware of.
 5 Scotland is a bit -- I shouldn't say strange, but
 6 Glasgow is a very particular area. Life is very
 7 competitive there, the mix of brands it sells. When
 8 I was dealing with tobacco, was very different. So you
 9 would tend to have a different tier just relevant to
 10 a few stores to ensure that it met with local needs.

11 So that was all the exception was.

12 Q. Right. Could you go to paragraph 24 of your witness
 13 statement, please {C3/43/621}. In the first sentence of
 14 paragraph 24 you refer to negotiating trading agreements
 15 at Alldays, First Quench and Somerfield. The last
 16 First Quench trading agreement that we are concerned
 17 with in the present proceedings is the one at tab 48 of
 18 annex 16 {D16/48/104}. If you look at that, the
 19 covering letter is dated 25 February 2003, and the
 20 agreement itself you can see from the last page is dated
 21 1 March.

22 It seems that it must be obvious that you weren't
 23 involved in the negotiation of this agreement?

24 A. No, I was not involved in that. But during my time in
 25 First Quench -- and I left in March 2005 -- I would have

9

1 been negotiating the next agreement, or at least
 2 starting negotiating the next agreement before I left,
 3 which is what I was referring to in my witness
 4 statement, not this one specifically.

5 Q. If you go to paragraph 26 of your witness statement,
 6 could you just read paragraph 26 and the first sentence
 7 of paragraph 27 to yourself, please {C3/43/622}.

8 (Pause)

9 A. Yes.

10 Q. What I was a bit puzzled about is this: in the first
 11 sentence of paragraph 27 you say:
 12 "ITL was aware of this."

13 I wasn't sure what the "this" was. Could you tell
 14 us what the "this" refers to, please?

15 A. What I referred to there was, in the previous paragraph
 16 I had said that we had divergent retail pricing
 17 strategies, such that I at First Quench was seeking to
 18 maximise the profitability without losing volume.

19 Imperial's strategy, as I saw it, was to achieve
 20 competitive pricing with its rivals as a tool to
 21 increasing its market share. First Quench: had
 22 Imperial, as I say here, just simply lowered their
 23 wholesale price, ie not offered an incentive, "if you do
 24 this we will pay you that", I would have been unlikely
 25 to have passed that money on to the customer.

10

1 THE CHAIRMAN: You were likely or unlikely to pass it on?

2 A. Unlikely.

3 MR LASOK: So you are actually referring to the position as
 4 it was as from when? September 2005?

5 A. I would have referred to the position from when I was
 6 working at First Quench, no, from June 2003.

7 Q. But you then go on to say that what ITL was aware of was
 8 the main reason it offered the bonuses to First Quench,
 9 but wasn't it the case that the arrangements between ITL
 10 and First Quench were set out in the trading agreement,
 11 which is at tab 48, and dates back to March 2003, before
 12 you turned up on the scene?

13 A. What they were offering there were incentives for
 14 First Quench to price below recommended price, so those
 15 sums of monies would be paid if you priced below
 16 recommended price.

17 First Quench's strategy was not to price below
 18 recommended price in all the three pricing tiers.
 19 Therefore, according to that agreement then Imperial
 20 would have paid the money purely against the volume set
 21 against the lower tier, which was about 30 per cent of
 22 the business. So they were offering money to encourage
 23 us to reduce prices below recommended price.

24 First Quench would not have stepped away from its
 25 pricing policy in that case, it would have accepted that

11

1 they would only get those bonuses where we were actually
 2 passing it on to the customer in an ongoing way.

3 Q. Let's go back to tab 47, please. Tab 47 is a document
 4 that dates back to 19 February 2003 {D16/47/103}.
 5 I accept that this was before you turned up on the
 6 scene, but there was one aspect of it that I wondered
 7 whether you could help us with.

8 If you read that email, there are some figures on
 9 the left-hand side starting in the third line, and you
 10 first have a reference to 12.5 gram pack, and then you
 11 have tier 1 and 2, and it says "MRP plus 4p". Do you
 12 happen to know what "MRP" means?

13 A. That would be -- some people probably internally
 14 referred to -- that's manufacturer's recommended price
 15 as on their published price list.

16 Q. Okay, so --

17 A. So that would -- I would interpret that that in tiers 1
 18 and 2, the 12.5 gram pack of handrolling tobacco, the
 19 HRT, they will sell all brands, not just Imperial's,
 20 currently at 4p above the published recommended price.

21 Q. This is an email that was sent by First Quench to
 22 Gallaher, Imperial and Rothmans. I think it's also
 23 copied to BAT. Did you ever have occasion to send
 24 confirmation of First Quench's pricing policy to the
 25 manufacturers?

12

1 A. No. No, I would -- I did not on any occasion write
 2 a joint memo to that extent. Each manufacturer would
 3 know their own retail prices, but I didn't -- I don't
 4 recall ever writing a memo which would have said
 5 everybody's.
 6 Q. If we go back to tab 48, then, and just have a look at
 7 this agreement. So could you go to the second page
 8 {D16/48/105}. This was the trading agreement operating
 9 from 1 March 2003 to 29 February 2004, and therefore you
 10 would have been working in the context of this trading
 11 agreement when you started doing the day-to-day
 12 management of the trading relationship between
 13 First Quench and ITL, as from whenever it was in
 14 June 2003 until this agreement expired and was replaced.
 15 Now, if we go, on that first page, to note 1 at the
 16 bottom, it says {D16/48/104}:
 17 "ITL pricing strategy to be adhered to on all
 18 brands, including 10s."
 19 Wasn't it the case, therefore, that First Quench
 20 agreed to adhere to ITL's pricing strategy on all
 21 brands?
 22 A. It's interesting that this note actually doesn't state
 23 what ITL's pricing strategy is. The interpretation of
 24 that is that if First Quench chose to price below
 25 recommended price, as laid out here, the note, then they

13

1 would receive those bonus levels from Imperial. So that
 2 statement, note 1, appertains to those cigarettes listed
 3 above. So it was an incentive to price below
 4 recommended price.
 5 Q. So that's your interpretation of the agreement?
 6 A. Yes, and that was how it was managed, yes.
 7 Q. That was how it was managed?
 8 A. Mm.
 9 THE CHAIRMAN: Can you just explain that again? I didn't
 10 really quite understand what you were saying. You were
 11 saying that the pricing strategy to be adhered to was
 12 the pricing below MRP strategy?
 13 A. In terms of this agreement, yes.
 14 THE CHAIRMAN: Were you saying that although it says "on all
 15 brands", that actually meant the brands listed under the
 16 heading "Bonus levels", rather than every brand?
 17 A. Yes. It would just be certain brands where Imperial
 18 felt it important to ensure that they had a competitive
 19 platform with their rival manufacturers. So it wasn't
 20 the whole range of cigarettes, cigars, tobaccos, it was
 21 those listed brands.
 22 MR LASOK: Well, now, Mr Culham, do you know him?
 23 A. Yes, I have dealt with Mr Culham.
 24 Q. When did you start dealing with Mr Culham?
 25 A. I would say about 1981. No, sorry, 2001/2002.

14

1 I wouldn't be able to confirm the exact date. I first
 2 dealt with Mr Culham when I was working at Alldays.
 3 Q. You see, Mr Culham, in his witness statement, and at
 4 paragraph 21 {C3/35/409} for the Tribunal's reference he
 5 refers to -- this is in the context of First Quench --
 6 to ITL's pricing strategy and what the phrase "pricing
 7 strategy" means in paragraphs 13 and 21.
 8 Maybe the easiest thing is not for me to just read
 9 it out, but for you to have a look at it. Do you happen
 10 to have tab 35 in the bundle that you have on the left?
 11 A. (Pause) Is it the one headed "National account business
 12 development plan" with a page number --
 13 Q. No, it's not that one.
 14 THE CHAIRMAN: It's in the witness statement bundle.
 15 A. (Pause) Yes.
 16 MR LASOK: If you turn to tab 35; do you have that?
 17 A. Yes.
 18 Q. You should have a witness statement of Mr Culham. If
 19 you go to page 4, that's the document pagination,
 20 internal document. The file page number is 394.
 21 {C3/35/408}. If you go to paragraph 13, and just read
 22 that to yourself.
 23 (Pause)
 24 Then look at paragraphs 21 to 22, which is on the
 25 next page {C3/35/409}.

15

1 (Pause)
 2 A. Yes.
 3 Q. It looks as though he is saying there that the reference
 4 to ITL pricing strategy to be adhered to on all brands,
 5 which is the phrase that he picks up in paragraph 21,
 6 relates to a more general obligation that the retailer
 7 should pass through lower cost prices in the form of
 8 lower absolute and relative shelf prices, irrespective
 9 of the pricings here First Quench was applying.
 10 He says that in paragraph 22 the bonus could be
 11 reduced or withdrawn in the event that the brand pricing
 12 by First Quench wasn't achieving the required
 13 competitive levels.
 14 A. Is this in respect of the ongoing bonuses that they were
 15 offering as an incentive to First Quench, not short-term
 16 tactical promotional discounts?
 17 Q. It looks as though he is referring to the monies that
 18 were being paid out to First Quench under the trading
 19 agreement.
 20 A. Well, the level of detail he talks about in paragraph 21
 21 is not specified in the trading agreement, and that's
 22 what I saw.
 23 Q. Well --
 24 A. There is no mention here of differentials, parities or
 25 whatever, and First Quench would only adhere to its own

16

1 pricing policy. Therefore, it didn't qualify for the
2 money, because it didn't suit First Quench to bring the
3 price down. It would not do it.
4 In actual fact, the policy at that time -- you see,
5 it makes general references to cigarettes 6p above or
6 below recommended price. That would have applied to all
7 brands across the piece. Many of the brands, I guess
8 that Imperial saw as competition from Gallaher, they
9 were at the same recommended price anyway, so the
10 differentials or parities would happen by default.

11 But I would not favour one particular supplier over
12 another. The policy was the policy the policy and they
13 stuck to it. But it is not specified in that trading
14 agreement, which is obviously what I saw first of all.

15 **Q.** You can put Mr Culham away, because I don't think we
16 will be referring back to him again. Somebody may take
17 that file away so that you don't get overloaded.

18 **THE CHAIRMAN:** It also has Ms Williams' witness statement in
19 it, if she is going to need to refer to that again.

20 **MR LASOK:** In that case we might leave it there.

21 At an earlier point in time, if you look at tab 20
22 in annex 16 -- it was before your time, but what you
23 actually have here is something that dates back to
24 October, I think, 2001. You have firstly a handwritten
25 page, but if you turn to the next page {D16/20/41}, you

17

1 have a letter from Imperial to the then category manager
2 at First Quench talking about the new trading agreement.

3 **A.** I am sorry, can I just clarify, I think I might be
4 looking at the wrong document.

5 **Q.** I am sorry. It may be the file on your right. What
6 I was looking at was tab 20.

7 **A.** Yes. Handwritten document.

8 **Q.** Handwritten. Then if you go to the next page, you have
9 a letter from ITL to Mr Williams about the new trading
10 agreement. This is dating back to 2001, so it's before
11 your time. But if you go to the third page {D16/20/42},
12 you should have a page that has the heading "Summary of
13 payments" at the top.

14 **A.** Yes.

15 **Q.** Then if you go to the next heading, it's "B, New Trading
16 Agreement". Do you have that?

17 **A.** Yes.

18 **Q.** So the writer of the letter says:

19 "The objective of a new trading agreement is
20 summarised as follows ...

21 "Pricing. To ensure ITL's strategies are achieved,
22 both in actual levels and differentials measured against
23 Gallaher competing brands."

24 So that was the explanation that was given to
25 First Quench back in 2001. Did you see any document

18

1 like this when you came to First Quench in June?

2 **A.** No. No, I didn't. I can't really comment on that,
3 because I haven't seen this before either.

4 **Q.** Okay. Well, now, let's move to tab 46. This is
5 a letter dated 17 February 2003 to Fiona Gittus, and it
6 deals with the trading agreement, and the writer, who
7 was George Byas, enclosed a final version of the trading
8 agreement. This is the one under which you were
9 operating. But if you go down to the bottom of the
10 first page of the letter {D16/46/101}, just below the
11 first holepunch, we have a bit that says:

12 "With regard to other items discussed ..."

13 And then there is a (e). Do you have that? It's
14 the last line and a bit on the first page.

15 If you prefer to, do read the entire letter.

16 **A.** Can you refer me to where we are again, sorry?

17 **Q.** It should be tab 46, it's the letter dated
18 17 February 2003.

19 **A.** Yes.

20 **Q.** Just below the second holepunch there is a sentence
21 beginning:

22 "With regard to other items discussed ..."

23 Then there is an (a), (b), (c), (d), (e) on that
24 page.

25 **A.** Yes.

19

1 **Q.** If you look at the (e), it says:

2 "You will adjust cigar pricing and achieve parity
3 for ITL and Gallaher brands."

4 Were you aware of this?

5 **A.** No, but that's -- it's difficult for me to comment,
6 because I don't know the context of before and after
7 this discussion. But I am quite clear that
8 First Quench -- and there was some acrimony between
9 them, it wasn't always best relations between ITL and
10 First Quench -- would have operated their own pricing
11 policy. Totally responsible for their own pricing, and
12 would not have received instructions from Imperial
13 Tobacco. Further than that, I can't comment.

14 **Q.** If you look at the next tab, which is 47, we have looked
15 at this one before, I asked you about what MRP meant,
16 this is from Fiona Gittus, and she says, in the last
17 sentence, {D16/47/103}:

18 "Please note that I now only have the cigar pricing
19 to finalise."

20 She goes on to say:

21 "I am to confirm this next week."

22 So it looks as though there was an agreement to
23 confirm the cigar pricing with the manufacturers the
24 following week. How do you explain that?

25 **A.** I would explain that -- again, I don't know the context

20

1 of this particular note -- Fiona at the time, they were
2 formulating a revised pricing policy. At that point,
3 the cigar structure had not been finalised. If and
4 where -- because the manufacturer might be offering
5 bonuses to help support price cuts below at recommended
6 price, they would need to know what those prices are so
7 that those bonuses could be paid.

8 Other than that, I can't comment.

9 **Q.** If you go to tab 49 {D16/49/110}, you have, or you
10 should have, a letter from Mr Byas to Fiona Gittus dated
11 25 February 2003. So again, it was before your time,
12 but could you just read the letter, please.

13 (Pause)

14 The second paragraph of the letter, I think the
15 figures are confidential but we don't need to go into
16 them, indicates that the cigar prices would be at
17 parity, which is consistent with what Mr Byas wrote on
18 17 February 2003. So we don't have, in these documents,
19 any indication that First Quench was saying that Mr Byas
20 had misunderstood the position, and we don't have any
21 indication that First Quench objected to, for example,
22 the letter at 49, which is expressed in rather
23 peremptory terms, because he says at 49 "from this date
24 the price will go to parity".

25 **A.** Again, I wasn't there at the time. I haven't --

21

1 I wasn't part of the discussions before or after. I can
2 affirm that First Quench only operated its own pricing
3 policy, and Imperial are probably repeating back to
4 Fiona, or whoever is the buyer at the time, what they
5 understood that to be. And my interpretation -- again,
6 it's only an interpretation -- of the note about Panama
7 cigars was really a reminder that the bonus was ending.
8 Unless you want to carry on funding this activity
9 yourself, you are going to lose margin. So just
10 a friendly reminder to put your price up.

11 It would be up to Fiona where that price would go,
12 because First Quench operated their own policy.
13 Imperial didn't dictate prices to First Quench.

14 **Q.** This is what I am leading up to, because when you say
15 that First Quench pursued its own commercial strategy,
16 do you mean that it pursued an independent commercial
17 strategy with regard to absolute price levels?

18 **A.** Yes.

19 **Q.** But we have seen here that there are documents showing
20 that First Quench pursued that strategy in the context
21 of compliance with what it had agreed with ITL regarding
22 parities and differentials.

23 **A.** I haven't seen any statements on parities and
24 differentials, but I think I mentioned earlier that many
25 of the competing brands were at similar recommended

22

1 prices with similar margins. The pricing policy, which
2 was plus or minus a recommended price, would -- by
3 default you would end up with prices retaining the same
4 differential or being the same price in terms of the
5 policy.

6 **Q.** Let's go back to --

7 **A.** Ultimately First Quench would set its prices at what it
8 wanted.

9 **Q.** Let's go back to tab 46 and the line and a bit at the
10 bottom of the page, the words:

11 "You will adjust cigar pricing and achieve parity
12 for ITL and Gallaher brands." {D16/49/101}

13 Have you any reason to believe that that was not
14 an agreement between First Quench and ITL to price ITL
15 and Gallaher cigar brands at parity?

16 **A.** I have to say I haven't seen anything in writing, and
17 while I was there there was no discussion. I don't
18 believe that there was an agreement, but I don't know,
19 I can't confirm one way or another. But I saw no
20 paperwork about parities or differentials at all.

21 **Q.** Now, if First Quench had agreed to have Gallaher and ITL
22 cigar brands on its shelves at parity, and if it priced
23 them differently, it would be in breach of its
24 agreement, wouldn't it?

25 **A.** Yes, but I haven't seen an agreement.

23

1 **Q.** It looks from Mr Culham's evidence that that would
2 expose it to a reduction or withdrawal of the bonuses
3 under the trading agreement?

4 **A.** Yes, you weren't moneyed if you priced below recommended
5 price.

6 **Q.** Well, it's not the below recommended price that I am
7 focusing on, I am focusing on the bit in the trading
8 agreement at tab 48, where -- if you want to have a look
9 at tab 48 {D16/48/104}.

10 **A.** There is no mention in that trading agreement of
11 parities or differentials. It's not defined.

12 **Q.** Well --

13 **A.** As far as I was concerned. I wouldn't interpret like
14 that at all.

15 **Q.** When you took over, was there a handover at which
16 somebody informed you as to how the trading relationship
17 was actually carried on?

18 **A.** No, the situation to start with, I went in there as
19 a consultant. I had not been in that position before,
20 but it was different. I wasn't initially open with --
21 welcomed, you know, with open arms by either
22 Fiona Gittus or Sarah-Jane Hodson, I had to work my way
23 in and earn respect from them. I had to dig information
24 out of them, to be honest, or else find it myself. It
25 wasn't necessarily forthcoming.

24

1 I think they were suspicious of me, you know, what
 2 was I doing there was I trying to -- was I a threat to
 3 them.
 4 **THE CHAIRMAN:** Because Mr Cheyne had --
 5 **MR LASOK:** When we were talking about Somerfield, I think
 6 you said you had gained knowledge by looking at the
 7 documents?
 8 **A.** Yes.
 9 **Q.** When you came into First Quench, if you had gone through
 10 the documents, particularly the recent ones, wouldn't
 11 you have come across the letter at tab 46 that we have
 12 been looking at? {D16/48/104}
 13 **A.** All I can say in that respect, and no disrespect to
 14 First Quench, there were a few people who had been
 15 handling tobacco, their files were all over the place.
 16 I have to say, the filing system wasn't good, it was
 17 fairly likely that I would not have located every single
 18 piece of paper.
 19 **Q.** Is it, therefore, fair to say that your involvement as
 20 tobacco buyer from what appears to be late June 2003 was
 21 an involvement in which you had not been informed of the
 22 true nature of the trading relationship between
 23 First Quench and ITL?
 24 **A.** No, I don't think it was deliberate in that sense.
 25 **Q.** I am not saying deliberate, I am just trying to say that

1 from June or whenever it was that you were acting as the
 2 tobacco buyer, you did not have a full picture of the
 3 nature of the trading relationship between ITL and
 4 First Quench?
 5 **A.** I handled the important pieces of paper like the trading
 6 agreement and, for example, a Gallaher furniture
 7 agreement. In terms of the day-to-day conversations and
 8 ins and outs, I knew there was some rancor between the
 9 two, only because their commercial strategies were quite
 10 different in terms of pricing. But I wouldn't have
 11 seen -- I wouldn't have, within, say, the first three
 12 weeks, possibly, seen every piece of paper that related
 13 to that relationship. But I would have seen trading
 14 agreements.
 15 **Q.** But the thing is that you didn't see the letter at
 16 tab 46?
 17 **A.** Not that I can recall.
 18 **DR SCOTT:** Sorry, can you clarify something? You have just
 19 said "their commercial strategies were quite different
 20 in terms of pricing"; was that between Gallaher and ITL
 21 or between the manufacturers and First Quench?
 22 **A.** Imperial and First Quench. Yes, sorry, I didn't make
 23 that clear.
 24 **DR SCOTT:** Just pausing there for a moment, what did you
 25 expect Gallaher and ITL's pricing strategy was about

1 when they used the word "competitive"?
 2 **A.** When they used the word "competitive", my interpretation
 3 of their pricing strategy is that they did not -- the
 4 manufacturers, neither of them wanted to be
 5 disadvantaged against the other in terms of the brands
 6 that they felt competed with each other.
 7 **DR SCOTT:** Yes.
 8 **A.** Which usually, as I say, by default had similar
 9 recommended prices in the published price list.
 10 **DR SCOTT:** And so far as you were concerned, therefore, by
 11 sticking to the relativities in the published
 12 recommended retail prices, you weren't disadvantaging
 13 either of them?
 14 **A.** No, but it was by default. Yes, I was only interested
 15 in the margin on the total basket of tobacco sold,
 16 I wasn't about favouring one supplier over the other,
 17 and I certainly wouldn't have been funding myself
 18 promotions to make a brand of Gallaher, you know,
 19 cheaper than that of Imperial, vice versa, and take
 20 a lower margin on one to spite the other. Not at all.
 21 It was the total basket I was interested in. The
 22 differentials and parities happened by accident because
 23 of the published price list. So it was not a strategy
 24 that I was following.
 25 **DR SCOTT:** Thank you.

1 **A.** I think the divergence between the two strategies that
 2 First Quench were -- and this was enhanced during my --
 3 well, I think during the time immediately before
 4 I joined and afterwards, that we were striving to
 5 achieve the maximum margin without losing overall
 6 volume, which meant that we priced as high as we could
 7 without what we used to call insulting the customers so
 8 they would just walk off and you would lose the
 9 customer. And the pricing, so you would look at local
 10 competition and price accordingly. There are actually
 11 bigger issues --
 12 **THE CHAIRMAN:** Wait for Mr Lasok's questions, thank you.
 13 **MR LASOK:** I just wanted to confirm also that if you look at
 14 tab 49 {D16/49/110}, was that a document that you had
 15 seen?
 16 **A.** I can't confirm that I saw it. It doesn't spring to
 17 mind. But I can't remember from however many years ago
 18 every single email that was in the file.
 19 **Q.** I don't wish to go back over, as it were, old ground,
 20 but if you cast your mind back to June 2003, I think you
 21 have told us that you became involved with the tobacco
 22 buying part of the activities of First Quench in
 23 something like the second or the third week of June. At
 24 what stage did you start getting involved in, for
 25 example, decision-making in relation to the buying

1 strategy of First Quench?
 2 **A.** Well, not -- day-to-day administration I would do. If
 3 you are talking about a recommendation to change the
 4 pricing policy that I had, I wouldn't have done that
 5 until after I was confirmed as the buyer for tobacco.
 6 But on the other hand that was to be expected,
 7 because to do the job properly I would need time to
 8 evaluate what the situation was, which I used my pricing
 9 model to establish competition and so on. So I would
 10 not have been making major decisions until after I had
 11 been in the hot seat, as it were, for a few months.
 12 **Q.** So from June 2003, the point in time at which you became
 13 involved, who was the person who was making the
 14 First Quench decisions regarding the pricing of tobacco
 15 products?
 16 **A.** What I did was to follow the policy that was in place at
 17 the time. So if there were price changes to do, they
 18 were in line with the price policy. My strategy was not
 19 to, at that stage, challenge them until I understood the
 20 business a bit more. So I followed policy. I did
 21 change prices, for example, but I was following the
 22 policy.
 23 **Q.** Where did this policy come from?
 24 **A.** The pricing strategy. The tiering system.
 25 **Q.** So basically -- can I put it in my own words and if I am

1 wrong you will tell me?
 2 **A.** Yes, please.
 3 **Q.** There was a sort of -- I'll use the word matrix or
 4 pattern or strategy that you inherited?
 5 **A.** Yes.
 6 **Q.** And you applied that?
 7 **A.** Yes.
 8 **Q.** For a few months?
 9 **A.** Yes.
 10 **Q.** Before you were in a position to make your own
 11 decisions?
 12 **A.** Yes, it would have been foolish of me to try and alter
 13 anything significantly before I had sufficient knowledge
 14 and understanding of the First Quench business.
 15 **MR LASOK:** No further questions.
 16 Questioned by THE TRIBUNAL
 17 **DR SCOTT:** You mentioned your pricing model.
 18 **A.** Yes.
 19 **DR SCOTT:** Mr Cheyne clearly admired you and you moved with
 20 him. I just wondered, you have explained in your
 21 statement at paragraph 12 {C3/43/617} that your
 22 objective as regards pricing was:
 23 "... to generate ... as high a margin as possible
 24 without materially reducing the overall volume of
 25 tobacco sold. In pursuing this strategy I was

1 indifferent as to which manufacturers' products I was
 2 selling. I was maximising my margin on the basket", and
 3 so on.
 4 Then you explain in 14 that you developed this
 5 pricing model, which was quite sophisticated, and took
 6 into account the amount of bonus support on offer. Then
 7 you explain the indicators against budget and margin as
 8 percentage of cash margin, the income stream and the
 9 turnover.
 10 I just wanted to explore this a bit. What level of
 11 detail did the model encompass?
 12 **A.** Right. It's difficult to explain a spreadsheet to you,
 13 but it was basically a spreadsheet or a series of
 14 spreadsheets, which I'll explain -- it's two years since
 15 I've -- although I developed them, they have obviously
 16 left when I left Somerfield.
 17 What I did was to take each subcategory of tobacco
 18 product. So, for example, I would take the cigarettes,
 19 10s, I would -- it's quite simple. I listed
 20 alphabetically the brands of whatever manufacturer. So
 21 my range of cigarette 10s from Gallaher, Imperial, BAT
 22 whoever it was, down the left.
 23 Across the top there would be a series of headings.
 24 One would be "share of sales": Share of sales relative
 25 to the company I was working for at the time. Then

1 there would be -- probably I would say what the
 2 recommended price was, the benchmark. Then the price
 3 list price that we were paying, because at this stage we
 4 were buying through Palmer & Harvey, so I can't remember
 5 what it was. Then there would be, if there was a bonus
 6 involved, if we were cutting the price below recommended
 7 price.
 8 Then there would be each of the tiers, a heading for
 9 each of the pricing tiers. Under each of those, I would
 10 enter the price. So say I was reviewing what they
 11 currently got, so I put in the current price. There
 12 would be a formula in there that would calculate cash
 13 profit and percentage margin, and that would be done for
 14 each tier, pricing tier, for each of the brands listed.
 15 I then used the sales percentage to weight the
 16 margins, so you could work out what the overall margin
 17 for that tier was, for that group of products, and the
 18 overall margin for the company for that group of
 19 products.
 20 Then you would -- I would produce a model for 20s,
 21 cigarette multipacks, cigars and so on. I knew the
 22 share at that stage those products had of the total
 23 business. So at the end of the day you could work out
 24 a total margin for the business.
 25 So I would use that model (a) in terms of Threshers

1 to understand what they'd currently got. When I got my
2 feet under the table, I was obviously looking at
3 opportunities to -- how could I enhance the margin
4 further, given the stiff targets I was given by the
5 company.

6 So you could do what ifs. What if I move more
7 stores to a higher price tier? What happens to my
8 overall margin? What if I try and -- I think I can
9 price all Superkings cigarettes, say, put another penny
10 on a packet. It could be used for questions from the
11 directors, usually. You know, what's the margin going
12 to be after the Budget? You could tap something in and
13 an answer would come out. It was a model, so it wasn't
14 100 per cent accurate. Although as time progressed
15 I found it got more and more accurate.

16 Also I would use it if Imperial, for example, said
17 "We would like to do a short-term promotion on brand X,
18 and we would like to, as a minimum, here is 5p".
19 I could plug that into the model and see what effect it
20 would have on my profitability. So it was really the
21 means I used to control the business.

22 **DR SCOTT:** That's very helpful.

23 You said it would enable you to look at what would
24 happen if there was a short-term promotion by ITL and
25 that it was generating the income stream and the

33

1 turnover. So you could see, presumably, what the impact
2 would be if you implemented an ITL short-term promotion?

3 **A.** Yes.

4 **DR SCOTT:** Presumably, in order to do that, you had to have
5 certain elasticities built into the model which
6 converted a price change in one particular brand and
7 size into an income stream.

8 How did you model the cross-elasticities between --
9 well, let me explain that. Imagine we are going to have
10 an ITL promotion.

11 **A.** Yes.

12 **DR SCOTT:** Richmond 20s are going to go down by 5p. Did
13 your model take account of what would happen as between
14 Richmond and Dorchester in terms of customers switching
15 from --

16 **A.** Yes, because that was the danger that all you would get
17 was cannibalisation of the business. So I would have --
18 from experience I would know roughly what would happen.
19 So -- but it was a model, so I would estimate what would
20 happen and feed that in. So I would play around with
21 the weighting factor, which was the percentages.

22 **DR SCOTT:** So that you could gain an idea of what would
23 happen to the relative shares if Richmond went down as
24 against Dorchester?

25 **A.** Yes, in -- yes. What I predict would happen, yes, for

34

1 a short period of time. The question would be whether,
2 when the promotion ended, depending what else was going
3 on, because there was a very, very competitive market
4 and there were always short-term promotions going on,
5 what would happen afterwards.

6 **DR SCOTT:** Now, ITL have assured us that once their
7 customers switched to Richmond, they loved Richmond so
8 much they would stick with Richmond, but that may not
9 have been your experience.

10 So you did have in the model a way of looking at the
11 cross-elasticities between the two?

12 **A.** Yes.

13 **DR SCOTT:** And they were significant? Worthwhile to do
14 a promotion?

15 **A.** It depended again on the tier. So if Imperial came to
16 me and said "We would like to promote Richmond" or
17 whatever it was, "reduce it by 5p and we will fund it",
18 I mean, I could always price lower but I would never,
19 you know, stick another penny or tuppence on. It would
20 depend how long it went on for, because customers aren't
21 always quick to notice pricing.

22 At that time, advertising was being restricted and
23 by the time I left First Quench you were no longer
24 allowed to put window bills up, for example. There was
25 no advertising in the paper. So it might have taken

35

1 longer to get the message across to the customer. They
2 had to actually go into our shop.

3 It generally had less effect, actually, in the
4 higher price tiers. So I was often -- made a decision
5 not to promote in the top tier because you would
6 literally just give volume away for no reason. Unless
7 it was going to be synergistic for both me and Imperial,
8 there was no point doing it. So I was selective when
9 I did promotions, yes.

10 **DR SCOTT:** That's very helpful, thank you.

11 **THE CHAIRMAN:** Any re-examination, Mr Howard?

12 Re-examination by MR HOWARD

13 **MR HOWARD:** Could I ask you about paragraph 26 of your
14 statement.

15 **A.** Can I just say I have lost my statement.

16 **Q.** It's in core volume 3 at tab 43. At paragraph 26, you
17 say that:

18 "As I say above at paragraph 19, the manufacturers'
19 competitive strategies focused on seeking, particularly
20 in regard to ITL, to increase its market share through
21 ensuring competitive pricing." {C3/43/622}

22 If we go back to the paragraph 19, you explain that
23 during your time at Alldays and First Quench the two
24 manufacturers, ITL and Gallaher, were engaged in intense
25 competition.

36

1 Could you just expand on that and just tell me
 2 something about the extent of the rivalry and the nature
 3 of the intense competition?
 4 **A.** During this period there was fairly rapid and aggressive
 5 inflation in terms of cigarette pricing, mainly through
 6 Budgets, government Budgets. So tax was increasing.
 7 That in itself would encourage customers to start
 8 looking for cheaper cigarette brands.
 9 We were also getting more and more legal
 10 restrictions in terms of advertising. So the
 11 manufacturers -- and this is against a background of
 12 a declining market -- were obviously keen to retain
 13 their share of the market, and indeed in the case of
 14 Imperial, wanted to become number one, so increase their
 15 market share.
 16 And the intense rivalry manifested itself by,
 17 I would say, a proliferation of requests for short-term
 18 promotional activity. There was introduction of
 19 products that carried a much lower recommended price,
 20 called economy or ultra low. Gallaher probably had
 21 a bit of a headstart on that, with Mayfair and
 22 Dorchester. I can't remember exactly when they
 23 introduced those. And Imperial came onto the scene with
 24 Richmond, and at that point, yes, there was intense
 25 rivalry, because it was an expanding part of the

37

1 business.
 2 **Q.** Right.
 3 **A.** On the other hand, because of the tax structure, those
 4 brands of course carried lower percentage margins. So
 5 there was a reluctance to -- for the retailer initially
 6 to push that side of the business, because he was
 7 selling a product at a lower margin instead of a product
 8 at a higher margin. But the market was driving down
 9 that way, so you had to join it to maximise your sales.
 10 **Q.** So if Imperial wanted to enter this or compete in the
 11 low priced, ultra low priced market and wanted therefore
 12 to get its cigarettes, Richmond, at a competitive price
 13 against Dorchester, what did it have to do?
 14 **A.** It would have to -- if it -- it would have to fund that
 15 price cut. It was not something I was prepared to do,
 16 but if it wanted -- are you asking me if he wanted them
 17 to have similar price in the store?
 18 **Q.** Yes.
 19 **A.** Then it would have to fund whatever the current
 20 differential was, ie so that I didn't lose margin. But
 21 I probably wouldn't have gone below, I would have
 22 probably just taken the money, the 5p or whatever it
 23 was, to fund that.
 24 **Q.** Right, and that's because?
 25 **A.** It was because --

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1 **Q.** Why would you --
 2 **A.** It was against my -- my strategy was to go for the
 3 maximum margin I could --
 4 **Q.** Right.
 5 **A.** -- and indeed, to meet the target set by my directors.
 6 **Q.** If we just go back a stage to the First Quench policy
 7 when you arrived. Could you just explain to us what you
 8 understood and what you were implementing as the
 9 First Quench policy?
 10 **A.** First Quench policy was that -- there is a history
 11 attached, because I think the history of First Quench,
 12 they had amalgamated Victoria Wine, which was an ultra
 13 cheap, sell it low, always try and undercut everybody,
 14 football driver policy, with Threshers, who were at the
 15 other end of the scale, who viewed tobacco as
 16 an ancillary product that somebody bought because they
 17 had gone in to buy their bottle of wine, bottle of beer
 18 or whatever it was.
 19 So they had a more premium pricing approach and
 20 Victoria Wine was very cheap. What First Quench was
 21 doing, over a period of time -- you wouldn't do it
 22 overnight -- was to try and pull this together.
 23 Difficult because you have such a span of prices. In
 24 the event, they are all convenience stores, all
 25 operating long, unsocial hours, expensive to run. There

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1 was a general requirement to move prices upwards.
 2 Initially, they had six tiers and I think -- I am
 3 not sure. I mean, I can't confirm this, but I would say
 4 you can't change everything overnight, you do it in
 5 stages, and that would be a stage, before moving to
 6 a higher price structure, but in a simplified system.
 7 **Q.** Right. So in fact the six tiers, if we just look at
 8 tab 44, which you were shown --
 9 **A.** A nightmare to administer.
 10 **Q.** Right. If you look at tab 44 {D16/44/87}, we can see in
 11 January 2003, relating to February, I think, it's
 12 described as six tiers, but some of the tiers I think
 13 are at the same -- well, I am not quite sure how it
 14 operates, actually. Do you have that, tab 44? It's in
 15 bundle 16, amended SO decision 16. I think Mr Lasok was
 16 suggesting to you that the six tiers had gone down to
 17 three the previous August. But if we look at this
 18 document on 28 January --
 19 **A.** Yes.
 20 **Q.** -- do you understand what it's meaning about the number
 21 of different tiers?
 22 **A.** It's not terribly helpfully worded, this email, I think.
 23 **THE CHAIRMAN:** But anyway, as far as you were concerned,
 24 they were simplifying the tier structure?
 25 **A.** Yes, and pursuing a more aggressive, you know, profit

40

1 strategy.

2 **MR HOWARD:** By the time you became involved, anyway, you

3 have told us there were three tiers -- it doesn't matter

4 at what stage they had gone to the three -- and that's

5 what I wanted to be clear about: what was the strategy

6 in relation to those tiers when you joined?

7 **A.** What, the definitive -- what the overall policy for

8 those tiers was?

9 **Q.** Yes.

10 **A.** Roughly, there were a third of the shops in the top

11 premium tier, which would be -- I can't remember the

12 exact figure, say 6p above recommended price, and that

13 would be on, say, cigarettes, and that would be across

14 the range, no matter who the manufacturer was, unless

15 you were doing a short-term promotion.

16 **Q.** Yes. Leave aside short-term promotion --

17 **A.** But the base was 6p. Everything would be sold at

18 a premium.

19 The central tier sold literally at the published

20 recommended price, and the third tier was the

21 price-cutting tier where local competition demanded

22 that, you know, you compete otherwise you would lose

23 sales.

24 **Q.** Right.

25 **A.** At whatever level that was. Again, across the raft of

41

1 brands.

2 **Q.** Now, insofar as you were pricing below RRP in these

3 30 per cent or so of the stores, to what extent was it

4 the policy to go to each of the manufacturers and to

5 secure support from them for that effective price

6 reduction?

7 **A.** Yeah, you would do that, yes. I mean, that was

8 a function of the buyer: to negotiate as much money, as

9 much support as you could from the supplier. It was in

10 your mutual interest to increase the sales, yes.

11 **Q.** I think you mentioned tension between Imperial and

12 First Quench. We have seen elsewhere for Imperial

13 bonusing lots of supermarkets to be below RRP. Can you

14 just explain what the tension is between Imperial's

15 strategy, as you perceived it, and First Quench's

16 policy?

17 **A.** Well, I think actually they understood -- not that they

18 didn't understand to start with, but -- Imperial, as

19 I saw it, wanted to compete with rival manufacturers on

20 brands that they thought were similar, like

21 Benson & Hedges and Embassy, and were keen to increase

22 the -- the target was to increase market share, the

23 sales.

24 To do that, the strategy, especially in the

25 environment of decreasing advertising, they had less

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1 tools in the box to achieve that objective. Pricing was

2 one of the important tools for them. So it would offer

3 incentives to retailers to lower the prices.

4 Whereas First Quench, the strategy was to maximise

5 the margin without overall losing sales. So it wasn't

6 necessarily saying "We need to increase volume overall,

7 we want to increase our bottom line profitability, but

8 we will price cut where it suits us". But in actual

9 fact the tension -- although pricing was important, the

10 tension was actually about how we displayed product,

11 availability, display, and that was the area that

12 ultimately both sides needed to address, which

13 I addressed.

14 **Q.** As I understand it, you were telling us a moment ago

15 when you were answering questions from Dr Scott, that

16 you were purchasing -- when I say "you", sorry,

17 First Quench was purchasing its cigarettes from P&H; did

18 I correctly understand that?

19 **A.** Yes.

20 **Q.** As I understand it, you also told us that you were

21 purchasing at the wholesale list price; is that right?

22 **A.** The exact Q rate? Yes, we paid Palmer & Harvey

23 a Q rate, which was volume related, depending on how

24 much volume, how many drops -- we paid Palmer & Harvey a

25 fee for distribution. So we paid -- the invoice price

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1 was the price list price, and a fee was paid separately

2 to Palmer & Harvey. The fee was not taken into account

3 in my buying margin, it was a distribution cost, that

4 was why it was treated separately.

5 **Q.** Then I think, as I understand it, you explain that, at

6 paragraph 26 {C3/43/622}, if ITL had lowered its

7 wholesale price to us at First Quench, you wouldn't have

8 reflected that in your retail price unless ITL had done

9 something?

10 **A.** Yes.

11 **Q.** Right. Now, if we consider the position before

12 a promotional bonus, can you just explain this to me:

13 insofar as one observes the RRPs, your policy, would

14 your policy in any way distinguish the position of the

15 different manufacturers?

16 Sorry, I haven't made it clear.

17 If the RRPs of Imperial have a brand at £4, Gallaher

18 has a brand at £4, BAT, Rothmans, have a brand at £4,

19 forget whether they are competing brands or whatever,

20 they are just each priced at RRP of £4, did your policy

21 apply any different strategy to those different brands?

22 **A.** No.

23 **Q.** Or did it just add on whatever it is or subtract

24 whatever it is?

25 **A.** It added on or took away a set number of pence from the

44

1 recommended price, irrespective of the manufacturer.
 2 **Q.** So then if we take promotional bonuses, if
 3 a manufacturer wants to reduce the price, say, here
 4 Imperial wants to reduce the price of Richmond, you have
 5 already explained to us that they would have to (a) pay
 6 you a bonus and (b), as I understand it, they have to
 7 make it a term that you are going to feed that through
 8 to the consumer?
 9 **A.** Yes.
 10 **Q.** Going back to the questions that Dr Scott was asking you
 11 about, and let's look at Richmond and Dorchester, did
 12 you understand that Richmond and Dorchester were
 13 competing?
 14 **A.** Yes.
 15 **Q.** Right. So if Richmond comes down, say, by 5p, providing
 16 your margin is maintained on Richmond, does it matter to
 17 you whether you sell Richmond -- your cash margin as
 18 well as your percentage margin is maintained. Does it
 19 make any difference to you whether you sell Richmond at
 20 the 5p reduction or Dorchester at 5p more?
 21 **A.** No. I am not interested -- I am interested in the
 22 overall -- the effect on the overall margin at the
 23 bottom.
 24 **Q.** So I just wanted to understand this point about the
 25 cross-elasticity and danger of cannibalising and so on.

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1 At this ultra low price where you have the two cheap
 2 brands, if one brand steals consumers from the other,
 3 providing your margin is maintained, does that make any
 4 difference to you?
 5 **A.** No, if the margins are maintained, no, it doesn't.
 6 **Q.** No. Okay. Now, then --
 7 **A.** Sorry, where it would matter, if it started accelerating
 8 trading down from a higher margin product, because that
 9 was happening as a background in this market at the
 10 time.
 11 **Q.** So your concern, or somebody in your position could have
 12 a concern generally about the ultra low price end of the
 13 market stealing market share from the higher end?
 14 **A.** Yes. It was a force you couldn't stop. It was
 15 happening. It had happened. We didn't like it, but it
 16 happened.
 17 **Q.** Yes, it's just one of those things with cigarettes
 18 becoming more expensive; is that right?
 19 Now, then I would like to ask you about tab 49, it's
 20 in the annex 16 {D16/49/110}. It's a document that
 21 Mr Lasok asked you about on a number of occasions.
 22 Let's just take it in stages. You have got your pricing
 23 policy, which, depending on which tier you are in, it's
 24 either RRP plus or RRP or RRP minus. Then we have
 25 discussed the position where there is a bonus payable on

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1 a particular product.
 2 If we take Panama. If Imperial were paying a bonus
 3 to reduce the price of Panama, then what happens to your
 4 pricing strategy if you have accepted the bonus?
 5 **A.** Can you just clarify, do you mean that that was
 6 a short-term bonus, we want to promote for four weeks or
 7 whatever it is?
 8 **Q.** Yes.
 9 **A.** Then I would pass on that sum of money in addition to
 10 the standard amount that I was offering, merely because
 11 I need to be competitive with retailer A up the road,
 12 whoever it might be, who is going to be doing the same
 13 thing.
 14 **Q.** Yes.
 15 **A.** If I just used it to fund what was already there as
 16 a discount, then, you know, the thing would fail.
 17 **Q.** Again, if we take cigars, what was your understanding of
 18 the strategy as to the pricing of cigars? Was it any
 19 different to cigarettes or roll-your-own?
 20 **A.** Not really, no. They would add or subtract a set pence.
 21 They might have subdivided cigars into large cigars,
 22 small cigars, miniatures, so the rates may have varied.
 23 But basically, you were so many pence above. It didn't
 24 matter who the manufacturer was, that policy applied to
 25 that type of subcategory of cigars.

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1 **Q.** So if Imperial, having bonused Panama for a period to
 2 get it down, then says the bonus, the promotion is going
 3 to end on 10 March --
 4 **A.** Yes.
 5 **Q.** -- then how would that be expected to affect the
 6 pricing of those cigars after 10 March?
 7 **A.** Then they would revert to the previous price so that the
 8 margin was maintained.
 9 **Q.** Yes. Then if we just go back to --
 10 **A.** Unless I saw a competitor who was carrying on, then
 11 I would be knocking on the door.
 12 **Q.** Knocking on the door to say what?
 13 **A.** Normally you would go back to the previous price.
 14 **Q.** Yes. Then if we go back to tab 47 first {D16/47/103},
 15 the First Quench strategy of having three tiers with
 16 products priced at so much above and below RRP, although
 17 I think you say in your time you didn't personally write
 18 a round-robin email to all three manufacturers, but that
 19 strategy, to what extent is it, to an informed person
 20 who goes into First Quench stores, to what extent is one
 21 able to observe it?
 22 **A.** Well, an Imperial representative calling on stores --
 23 and they would call on stores -- they were allowed to
 24 call every six to eight weeks, I think from memory,
 25 would -- could tell from looking at the prices, I mean,

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1 they would be checking availability, displays, all sorts
 2 of other things. They would look at prices and quite
 3 clearly see what was going on. I had no problem in
 4 telling Imperial what Imperial's prices were. I would
 5 not tell Gallaher what Imperial's prices were. They
 6 could find out, they could go in the shops. I'm not
 7 going to tell them voluntarily, and I would not tell any
 8 other manufacturers --

9 **Q.** Perhaps that's actually dealing with something slightly
 10 different.

11 **A.** Sorry.

12 **Q.** The pricing strategy, so the strategy, for instance,
 13 that it's 6p above in premium stores or whatever you
 14 call them, and then at RRP in the regular stores and 6p
 15 below at the more competitive local stores. Whatever
 16 your definition of them is, it doesn't really matter.
 17 Would you tell Imperial that was your policy? Was there
 18 any secret about that?

19 **A.** No, and they would be able to see. It was fairly
 20 straightforward and simple. Yes, I would tell them.

21 **Q.** Because the email that you have here is actually --

22 **A.** I might wait for them to ask, but I would tell them.

23 **Q.** This email is actually just, if you look at it, not
 24 telling people prices of any particular product. What
 25 it's actually confirming is a new pricing strategy on

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1 handrolling tobacco, I suppose that is, HRT --

2 **A.** Yes.

3 **Q.** -- from 24 February, which is then told to everybody.
 4 Would that be anything particularly secret, is what I am
 5 trying to understand. That, in other words, what they
 6 appear to be doing is changing either the tiers or the
 7 differential in some way, in relation to handrolling
 8 tobacco?

9 **A.** Well, I wouldn't have told anybody in advance. They
 10 would see it when it happened. I would -- I might tell
 11 the supplier of their brands that I was changing the
 12 prices, because otherwise you would just get a mass of
 13 calls and queries.

14 **Q.** As I understand it, what you are saying is you might
 15 have sent this email to Imperial separately and to
 16 Gallaher separately and to Rothmans, BAT separately?

17 **A.** Yeah, they might've worded it similarly, but that's no
 18 reason ...

19 **Q.** Right.

20 **A.** You know, and I would expect Imperial to be looking
 21 at -- where I was doing promotions and they were funding
 22 me money, they would naturally be checking to see that
 23 they got their return on the investment. So --

24 **Q.** Yes.

25 **A.** -- there was no reason to hide it.

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1 **Q.** The strategy of exactly what strategy you are going to
 2 apply in the different tiers. So here what we see with
 3 12.5 grams of handrolling tobacco, they have actually
 4 reduced it to two tiers. So tiers 1 and 2 are the same
 5 as tiers 3, 4, 5 and 6, and similarly for 25 grams.

6 That decision as to how the tiers are to interrelate
 7 to each other and what uplift or reduction is going to
 8 be applied to RRP, I mean, whose decision is that?

9 **A.** That would be the buyer doing the fieldwork and all the
 10 rest of it, putting forward -- in my case it would
 11 involve doing all the modelling, putting a proposal
 12 forward and going to normally the trading director of
 13 the company with it and saying "I wish -- this will
 14 benefit the company by X whatever pounds a year and the
 15 margin by X", so I would not have the ultimate authority
 16 just to do it. I would need to get board approval for
 17 that, because certainly in the case of First Quench,
 18 tobacco was 35, 40 per cent of sales, from memory. So
 19 it's very important.

20 **Q.** Right. Then you can see, after dealing with handrolling
 21 tobacco, Fiona Gittus says:

22 "Please note I now only have the cigar pricing to
 23 finalise. I'm to confirm this next week." {D16/47/103}

24 In the context of what we have already seen, that
 25 she is setting a new strategy for handrolling tobacco in

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1 the tiers as to where they are going to be priced at MRP
 2 or above, what do you understand she is talking about
 3 here in terms of the cigar pricing?

4 **A.** How I would read that is that she is doing it in stages.
 5 She has done cigarettes, probably, looking at
 6 an alternative tiering structure, she has tackled
 7 handrolling tobacco, but she is now going to look at
 8 cigars.

9 **Q.** If we then go back to 46, you were asked about
 10 subparagraph (e) at the bottom of the page {D16/46/101}.

11 We can see it's actually another item that's been
 12 discussed between Fiona Gittus and George Byas, and you
 13 were asked about "you will adjust cigar pricing and
 14 achieve parity for ITL and Gallaher brands". I think
 15 you said you don't know the context of what was being
 16 discussed.

17 In terms of cigar pricing, if a different pricing
 18 structure had been applied to cigars, so that, say,
 19 Imperial's had been at plus 6p above RRP and Gallaher's
 20 had been at plus 3p, if that is what had happened, how
 21 would that, as you understood it, have accorded with
 22 First Quench's own pricing policy?

23 **A.** First Quench are obviously free to set their own prices.
 24 If they wanted to do that, they would have done that.
 25 What you did, you had no preference of necessarily one

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1 manufacturer over another. They would literally price
 2 the whole -- might subcategorise the cigars into the
 3 different types, but you would price them all plus or
 4 minus whatever you decided to do.
 5 **Q.** Yes. As far as you understood it, obviously you came in
 6 in June, but from your knowledge of the account and from
 7 reviewing the files and your involvement, did you
 8 understand at any stage, absent promotional bonuses,
 9 that there was any intention to advantage one
 10 manufacturer over another?
 11 **A.** No. Not in terms of pricing, no.
 12 **MR HOWARD:** Thank you very much indeed.
 13 **MR LASOK:** In the light of the examination-in-chief,
 14 I wonder whether I can ask a couple of questions in
 15 cross-examination?
 16 **MR HOWARD:** I would resist that at this stage.
 17 **THE CHAIRMAN:** Well, we do need to keep to the timetable,
 18 Mr Lasok. I think we should call it a day as far as
 19 Ms Williams is concerned, because I am concerned that we
 20 are going to run out of time.
 21 Thank you very much for coming along, Ms Williams,
 22 that's been very helpful, and I can release you from the
 23 witness box now.
 24 **A.** Thank you.
 25 (The witness withdrew)

1 **THE CHAIRMAN:** We will now take a break and come back at 20
 2 to 12, where we will have Mr Culham back.
 3 **MR HOWARD:** That's right.
 4 **THE CHAIRMAN:** Thank you very much.
 5 (11.35 am)
 6 (A short break)
 7 (11.40 am)
 8 MR KENNETH CULHAM (recalled)
 9 **MR HOWARD:** Mr Culham, welcome back, if that's the right
 10 expression. You are still under oath and you are going
 11 to be asked some questions now about First Quench and
 12 the other account that you dealt with.
 13 Cross-examination by MR LASOK
 14 **MR LASOK:** Mr Culham, do you have your witness statement in
 15 front of you?
 16 **A.** I haven't.
 17 **Q.** I wonder whether somebody could pass the witness
 18 statement to him, please. Core 3. You should have it
 19 at tab 35 {C3/35/405}.
 20 **A.** Yes.
 21 **Q.** I am going to ask you some questions first about
 22 First Quench, and then about T&S Stores, and I believe
 23 that you were at one time or another the national
 24 account manager for each of them?
 25 **A.** Yes, for differing periods of time, and with T&S for

1 much longer than First Quench.
 2 **Q.** So if we go to paragraph 8 of your witness statement
 3 {C3/35/407}, you say in the third line that you were
 4 responsible for the First Quench account from 2003 until
 5 2004.
 6 Now, as far as I can see, the first document in the
 7 First Quench annex that mentions your name seems to be
 8 dated, I think, 21 July. If you have annex 16, which
 9 could well be the one that you have there, and turn to
 10 tab 51 --
 11 **A.** I have it, yes.
 12 **Q.** We have here two emails, the first one which starts at
 13 the first holepunch was sent from Mark Mentha to
 14 Cynthia Williams {D16/51/113}. Do you know who
 15 Mark Mentha was?
 16 **A.** Yes, Mark Mentha was employed by Imperial Tobacco and
 17 his role was -- sorry, part of his role -- I'm not sure
 18 if it was his total role -- was looking after our own
 19 label production and contracts of own label products.
 20 **Q.** Then the email at the top of the page is one that he
 21 sends on 21 July to you and to Roger Batty. I don't
 22 think that we have any mention of your name before that
 23 date. If we go to the previous tab, which is tab 50,
 24 this is a letter to Sarah-Jane Hodson dated 20 June 2003
 25 {D16/50/111}. The writer of the letter is George Byas.

1 **A.** That's correct, yes.
 2 **Q.** So George Byas, of course, is the one who is involved,
 3 certainly up until this point in time. Do I take it
 4 that you took over from Mr Byas?
 5 **A.** Yes, on -- after that meeting, which was -- it was some
 6 time in June 2003, which is when George retired.
 7 **Q.** So you would have taken over between 20 June and the end
 8 of June?
 9 **A.** I can't remember the exact date, but some time during
 10 June. It could have been before the 20th because the
 11 letter was written after the meeting, so I don't know
 12 the exact date. Some time in June.
 13 **Q.** At that stage, the trading agreement that was in place
 14 was the one at tab 48. If you look at the second page,
 15 that's where the trading agreement starts {D16/48/105}.
 16 Was this type of trading agreement familiar to you?
 17 **A.** Sorry, can you --
 18 **Q.** Yes. If you look at it, you have the bonus levels,
 19 pricing strategy support, and then you have a note at
 20 the bottom of the page, and there is a paragraph 1,
 21 which says:
 22 "ITL pricing strategy to be adhered to on all brands
 23 including 10s."
 24 Then it goes on to say in note 2 that the support
 25 levels may be reduced or withdrawn in the event of brand

1 pricing not achieving the required competitive levels.
 2 But this was something that, as I understand it, you
 3 inherited it from Mr Byas?
 4 **A.** Yes.
 5 **Q.** It wasn't something that you had negotiated?
 6 **A.** It was in place. I think it was signed in March by
 7 Fiona Gittus at First Quench. So the agreement was in
 8 place when I took over the account. And this was
 9 slightly different to some of the other accounts. When
 10 you say trading agreements, we have -- as you are aware,
 11 we have different trading agreements, and they are
 12 all --
 13 **THE CHAIRMAN:** Slow down, Mr Culham.
 14 **A.** Sorry. Been out of practice for two weeks.
 15 **MR LASOK:** But at all events, this is something that you
 16 inherited. Was there a handover period with Mr Byas?
 17 **A.** There would have been -- there was, sorry, handover
 18 meetings with Mr Byas. We would have met up, gone
 19 through documents that were relevant at the time,
 20 including the trading agreement, and then we would
 21 generally have a meeting, which we did, with the buyer
 22 at First Quench when formally I would take over from
 23 that point.
 24 So I would meet George beforehand to go through the
 25 documents, and obviously documents that were relevant at

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1 the time were then passed to me to manage the account
 2 going forward.
 3 **Q.** Right. Now, if we go back -- you ought to leave that
 4 page open because we will come back to the trading
 5 agreement -- to your witness statement and to
 6 paragraph 13 {C3/35/408}, and if you just read 13 to
 7 yourself, and then look at 21.
 8 (Pause)
 9 Where did you get that understanding of ITL's
 10 pricing strategy from?
 11 **A.** Sorry, understanding of the strategy?
 12 **Q.** Yes. How did you know that the phrase "ITL pricing
 13 strategy" in the trading agreement meant what you say in
 14 paragraphs 13 and 21?
 15 **A.** We were trying to achieve a similar strategy across the
 16 market and in the briefing I would have had with George.
 17 **Q.** Okay. Can you go back in annex 16 to tab 46, please
 18 {D16/46/101}. If you look at this, this is a letter to
 19 the person who was at that stage the First Quench senior
 20 buyer. It's sent by Mr Byas, and is dated
 21 17 February 2003.
 22 He is enclosing a final version of the trading
 23 agreement that we have just looked at. At the bottom of
 24 the page, you have a (e). Do you have that?
 25 **A.** Yes, there is, yes.

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1 **Q.** It says:
 2 "You will adjust cigar pricing and achieve parity
 3 for ITL and Gallaher brands."
 4 So that's part of ITL's pricing strategy at the
 5 time, wasn't it?
 6 **A.** Well, it's -- they were adjusting pricing, whether
 7 Thresher -- sorry, First Quench were changing their
 8 pricing or a discussion took place, I wasn't at the
 9 meeting.
 10 **Q.** I am asking: that is a reflection of ITL's pricing
 11 strategy at the time?
 12 **A.** Well, no, because some of our cigars were a lower RRP
 13 than Gallaher products, so we wouldn't have wanted them
 14 at parity.
 15 **Q.** Well, could you have a look at annex 28, please, and go
 16 to tab 76 {D28/76/180}. Do you have it? It's an email
 17 from Terry Rogers sent on 11 June 2003 to the UK
 18 division NAMs. That would include you, wouldn't it?
 19 **A.** Yes, I would have received a copy.
 20 **Q.** The first line says:
 21 "Classic: match Hamlet shelf price all packings."
 22 Doesn't it?
 23 **A.** It says that, but -- it says match it, but obviously --
 24 **THE CHAIRMAN:** That's not what you are being asked at the
 25 moment. Just wait for the questions, please.

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1 **MR LASOK:** What I was putting to you was that the parity we
 2 see in annex 16, tab 46 is a reflection of ITL's general
 3 policy with regard to cigar pricing. I am going to ask
 4 you that question again: do you agree with that or not?
 5 **A.** No, I don't, because if you're referring to the same
 6 document, 76 in the one you have just taken me to, the
 7 email, it's asking for Panama to be below Hamlet. So if
 8 parity was achieved, our objectives weren't achieved.
 9 **Q.** Wait a minute. In 16/46, right --
 10 **A.** That's this one, yes.
 11 **Q.** -- we have that bit in (e), and this dates back to
 12 February 2003. All right?
 13 **A.** Correct.
 14 **Q.** There is a reference there to parity for cigar products.
 15 Now, I'll try to be as clear as I can. I am not very
 16 good at being clear, but we will have a go. What I am
 17 putting to you is that that (e) represents ITL's pricing
 18 strategy for its cigar brands?
 19 **A.** Well, I would dispute that, because our strategy is in
 20 tab 76, Classic, it says, to match Hamlet, but Panama to
 21 be cheaper than Hamlet.
 22 **Q.** That may have been the case in June, but I am going back
 23 to February. What I am pointing to is the fact that we
 24 can see an indication in, even as late as June 2003,
 25 that there was a policy of matching Classic and Hamlet?

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1 A. We would not want to see Classic higher, so match would
 2 have been acceptable or cheaper. But Panama was always,
 3 in the time I've worked for the company, been a lower
 4 recommended retail price than Hamlet. So the point (e)
 5 wouldn't have achieved our objectives.
 6 Q. (e) is not without any qualification whatsoever, is it?
 7 A. Then I don't know whether George, Fiona, that was her
 8 decision, I don't know, I wasn't at the meeting.
 9 Q. Well, look, if you look at this letter, it's quite
 10 clear, isn't it? You are the NAM, you take over in
 11 June 2003, you inherit a situation. Presumably you have
 12 had a chat with Mr Byas, and surely you were informed
 13 that it had been agreed between First Quench and ITL
 14 that there would be parity for ITL and Gallaher brands
 15 in relation to cigars?
 16 A. This point (e) does say that, but that wasn't Imperial's
 17 strategy at the time. Imperial's strategy at the time
 18 was Panama to be 3p or greater less than Hamlet. So
 19 that doesn't reflect ITL's strategy, point (e).
 20 Q. It may be a variation of the strategy that we see in
 21 June 2003, but it still starts off on the basis of
 22 parity, doesn't it?
 23 A. Not for Panama, no.
 24 Q. This (e) starts off on the basis of parity, doesn't it?
 25 There may have been a change later on, but at this stage

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1 it's parity?
 2 A. What I am trying is if they did achieve parity in their
 3 stores and Panama was the same price as Hamlet, that
 4 would not be in line with Imperial Tobacco's strategy.
 5 That's what I am trying to say.
 6 **THE CHAIRMAN:** Strategy when, though?
 7 A. At any time in the last ten years, 20 or 15 years.
 8 Panama has always, in the time that I have been
 9 an account manager, which goes back to the mid 80s, has
 10 always been cheaper than Hamlet as an RRP.
 11 **DR SCOTT:** Presumably you don't know, you said you didn't
 12 know the context for this?
 13 A. I wasn't there, so ... but if parity was achieved, for
 14 all cigars in Threshers -- sorry, First Quench outlets,
 15 that would have been counter to Imperial Tobacco's
 16 internal strategy. It wasn't what we were trying to
 17 achieve.
 18 **THE CHAIRMAN:** So is what you are saying that there would
 19 have to have been an exception made for that if this
 20 point at (e) was right, but you don't know, because you
 21 weren't there, whether any exception had been made?
 22 A. As I've said, I wasn't there, but if that policy had
 23 been adopted in First Quench stores, that would have
 24 been counter to Imperial Tobacco's strategy. That's
 25 what I am saying.

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1 **MR LASOK:** So it would be wrong for Mr Byas to reach that
 2 agreement with First Quench?
 3 A. As I said, I don't know whether Fiona said "That's our
 4 strategy" or they had a discussion, I don't know,
 5 I wasn't there.
 6 Q. But I am asking you a question: it would be wrong,
 7 according to you, for Mr Byas to agree that pricing
 8 strategy with First Quench?
 9 A. It wouldn't be wrong, because the retailer can set their
 10 own strategy. We would try and persuade them not to do
 11 it, we would like to have Panama cheaper, but we can't
 12 make them reduce the price.
 13 Q. If you go to tab 49 in annex 16 {D16/49/110} --
 14 A. Can I put this one away?
 15 Q. Yes. You have here a letter to the senior buyer at
 16 First Quench from Mr Byas. He recites in this letter
 17 that the pair of them had agreed that the bonus on
 18 Panama would cease from 10 March. And he says:
 19 "From this date, the price will go to parity."
 20 A. Well, that's what it says, which wasn't in line with
 21 Imperial Tobacco's strategy. So George had agreed
 22 something with Thresher -- sorry, with First Quench --
 23 I apologise, I keep getting -- which isn't -- wasn't
 24 within our objectives, but it's what the retailer had
 25 either told him or they had agreed. I don't know.

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1 Q. If you view it from the perspective of the buyer at
 2 First Quench, what the buyer agreed with ITL as being
 3 the pricing strategy would be ITL's pricing strategy in
 4 relation to First Quench, wouldn't it?
 5 A. But as you can see from this it wasn't in the case of
 6 Panama.
 7 Q. How do we know that?
 8 A. Because you have drawn my attention to an email where
 9 it's saying cigars would be at parity. That wasn't in
 10 line with our strategy.
 11 **THE CHAIRMAN:** But was Panama at parity usually with some
 12 cigar other than Hamlet, some Gallaher cigar other than
 13 Hamlet?
 14 A. The recommended retail price for Panama was 3p below
 15 Hamlet, and where we did actually have promotions
 16 running on Panama where there was nothing else the same
 17 price in the market.
 18 **MR LASOK:** Now, if we look at paragraph 22 of your witness
 19 statement --
 20 **THE CHAIRMAN:** Can we put annex 28 away?
 21 **MR LASOK:** We can put annex 28 away.
 22 Can you just read paragraph 22 to yourself
 23 {C3/35/409}.
 24 (Pause)
 25 Now, I read that as saying that if First Quench

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1 didn't achieve the pricing at the competitive levels
 2 required by ITL, ITL would be entitled to reduce or
 3 withdraw the bonus?
 4 **A.** I think -- well, I know you are misinterpreting that.
 5 The change in bonus, if you go back through
 6 correspondence in First Quench, the bonus was paid on
 7 all volume. And as they put more and more prices up to
 8 RRP and above, our level of bonus went down. So when it
 9 says "competitive", it means relative to the RRP.
 10 I think at this point they were receiving a bonus on
 11 30 per cent of the volume. Going back to the start of
 12 the folder, it was on 100 per cent, but as Threshers'
 13 prices moved up absolute terms, the bonus level went
 14 down. So it was then monitored against the stores
 15 selling cheaper to consumers and that's what adjusted
 16 the bonus.
 17 **Q.** Can I press you on this? Go back to the trading
 18 agreement, please, which is tab 48 {D16/48/104}.
 19 **A.** Okay.
 20 **Q.** So we have on that first page, in the section headed "A.
 21 Bonus levels, pricing and strategy support", the two
 22 notes at the bottom of the page, the two numbered notes.
 23 Can I take this in stages. As I read it, A, right,
 24 in this letter, deals with bonus levels; is that
 25 correct?

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1 **A.** Point A does deal with bonuses, yes.
 2 **Q.** Am I also right in thinking that the words "pricing and
 3 strategy support" indicate what these bonus levels
 4 relate to?
 5 **A.** The pricing within the stores, yes.
 6 **Q.** So part of this is strategy?
 7 **A.** Yes, whether it's Imperial's strategy and First Quench's
 8 strategy.
 9 **Q.** When we get to note 1, we have:
 10 "ITL pricing strategy to be adhered to on all brands
 11 including 10s."
 12 Now, am I right in believing that that means that
 13 ITL pricing strategy is to be adhered to on all brands,
 14 including 10s?
 15 **A.** That was our hope, yes.
 16 **Q.** And that is a condition attached to the payment of the
 17 bonus levels?
 18 **A.** But the bonus was only paid on the 30 per cent of volume
 19 that was sold in the discount tier, so there was no
 20 bonus attached to the other 70 per cent of the volume at
 21 all. So there was no conditions on almost --
 22 70 per cent of their volume. There was no payments
 23 attached to that at all.
 24 **Q.** I am not actually talking about that, because what I am
 25 trying to get at is this: as I read it, at the beginning

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1 of A, you have bonus levels, and you specify what
 2 these -- when I say "you", it's ITL -- bonus levels.
 3 So we can see, for example, Embassy No 1 and
 4 Regal Kingsize and promoted premium brands, and then
 5 alongside it there it says "all at", and then there is
 6 an amount per thousand. So that's a bonus level?
 7 **A.** On the 30 per cent of volume sold at a discount to the
 8 RRP, yes.
 9 **Q.** Then I look at note 1, and note 1 says:
 10 "ITL pricing strategy to be adhered to on all
 11 brands, including 10s."
 12 **A.** That's what it says, yes.
 13 **Q.** And that's a commitment made by First Quench?
 14 **A.** It's a commitment that wasn't followed through fully,
 15 but yes, a commitment, yes.
 16 **Q.** Because they signed the trading agreement?
 17 **A.** Yes, they did.
 18 **Q.** Then we get to paragraph 2, where it says:
 19 "These support levels may be reduced or withdrawn in
 20 the event of brand pricing not achieving the required
 21 competitive levels."
 22 Now, am I right in believing that that means that
 23 the support levels may be reduced or withdrawn in the
 24 event of brand pricing not achieving the required
 25 competitive levels?

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1 **A.** No, because the competitive levels which is talked about
 2 in other documents in the file was relative to the RRP.
 3 First Quench did receive those sort of same bonuses on
 4 all their volume, and the bonus percentage paid only
 5 reduced down when they chose to sell above RRP.
 6 So where it's saying "competitive levels", it's
 7 relative to the RRP, ie a discount to the retail price,
 8 not --
 9 **Q.** Okay, so you had actually jumped ahead of me, because
 10 what you are saying is, as I understand it, the first
 11 sentence of note 2 means what it says?
 12 **A.** It says that, but it wasn't delivered, yes.
 13 **Q.** No, no, it means what it says. Okay, are we agreed on
 14 that?
 15 **A.** I assume so, yes.
 16 **Q.** Well, are we or aren't we?
 17 **A.** It says that we would like our pricing strategy to be
 18 achieved in their stores, yes.
 19 **Q.** It says that support levels may be reduced or withdrawn
 20 in the event of brand pricing not achieving the required
 21 competitive levels, and that's what it means?
 22 **A.** No, it doesn't. That's referring --
 23 **THE CHAIRMAN:** Well, can you say what you think "required
 24 competitive levels" relates to?
 25 **MR LASOK:** That's the next question.

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1 **THE CHAIRMAN:** Well, ask that question.
 2 **MR LASOK:** What I'm trying to get at is whether the dispute
 3 between us is over the meaning of the phrase
 4 "competitive levels" or whether it's about something
 5 else.
 6 **THE CHAIRMAN:** Well, what I think it's about, if this is any
 7 help, is that he is saying, as I understand it, that if
 8 they don't comply, then that 30 per cent is likely to go
 9 down if more of their pricing is actually in the higher
 10 price tiers. And you are saying, I think, or are you
 11 putting to him, that it actually relates to
 12 relativities?
 13 **MR LASOK:** That's the next stage. I just want to see where
 14 we agree.
 15 **THE CHAIRMAN:** Well, can we try and jump to a stage beyond
 16 the one at which we seem to have got a bit stuck.
 17 **MR LASOK:** Okay.
 18 Go back to your paragraph 21 of your witness
 19 statement, please {C3/35/409}. In the last sentence,
 20 you say:
 21 "In other words, ITL's pricing strategy was to
 22 encourage the retailer that where ITL had lower cost
 23 prices, such as through lower wholesale prices or
 24 through paying bonuses, these were passed on to the
 25 customer in the form of lower absolute and relative

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1 shelf prices, irrespective of the pricing tier
 2 First Quench was applying."
 3 Then in 22:
 4 "This is also what is being referred to where the
 5 agreement says that the bonus that ITL pays to
 6 First Quench can be reduced or withdrawn in the event of
 7 brand pricing not achieving the required competitive
 8 levels."
 9 So what I'm doing is I am reading this and I am
 10 saying to myself: well, what he is saying is that the
 11 conditions in note 1 and 2 of the trading agreement mean
 12 that if the pricing, the retail pricing in First Quench,
 13 is not in conformity with either the agreed absolute
 14 levels or with the relative shelf pricing, then ITL can
 15 reduce or withdraw the bonuses that we have seen
 16 mentioned on the first page.
 17 **A.** As I've said before, the only time the bonuses were
 18 reduced is where the absolute price moved above RRP. It
 19 wasn't reduced when differentials were not as we would
 20 like. It was only reduced from 100 per cent of the
 21 volume to this point down to 30 as First Quench chose to
 22 move their absolute shelf prices above RRP. It was
 23 never reduced where ITL's strategy on pricing was not
 24 achieved.
 25 **Q.** What was agreed, though? Because, you see, are you now

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1 saying that your paragraph 21 is inaccurate?
 2 **A.** I don't believe so.
 3 **Q.** Well, look at the last sentence of paragraph 21 and read
 4 it in conjunction with paragraph 22.
 5 (Pause)
 6 **THE CHAIRMAN:** What did you mean when you referred to
 7 relative shelf prices as opposed to absolute shelf
 8 prices?
 9 **A.** Well, we have a lower -- the cost price, because it's
 10 talking about the cost price in here, First Quench, and
 11 that was the price they would get on, in their case from
 12 Palmer & Harvey who supplied them. So therefore, if our
 13 cost price was lower than a competitor's product, we
 14 would like to have the consumer benefitting from that
 15 lower shelf price.
 16 However, we couldn't adjust the wholesale cost on
 17 whether they did that or didn't do that. They still got
 18 the lower cost price if they didn't deliver a lower
 19 price.
 20 **DR SCOTT:** Sorry, you have got me utterly confused now. My
 21 recollection -- and maybe I have got it wrong -- was
 22 that ITL's basic pricing strategy was reflected in the
 23 RRP differentials?
 24 **A.** That's correct, yes.
 25 **DR SCOTT:** Now, when we had Cynthia Williams here just now,

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1 she explained --
 2 **THE CHAIRMAN:** Wait a minute.
 3 **DR SCOTT:** Sorry. Okay.
 4 **THE CHAIRMAN:** Perhaps, Mr Lasok, you finish your questions
 5 on this point and then we will see where we have got to.
 6 **MR LASOK:** I was going to move on to the question of cost
 7 prices.
 8 **THE CHAIRMAN:** Well, do we understand now what you meant in
 9 paragraph 21 when you referred to "absolute and relative
 10 prices"? My confusion is that if you are referring to
 11 relative shelf prices being relative as between ITL and
 12 Gallaher, are you then saying that part of the trading
 13 agreement that we see at tab 48 was some kind of
 14 requirement or expectation as far as ITL was concerned
 15 that First Quench was committing itself to adhering to
 16 particular price differentials as between ITL and
 17 Gallaher brands?
 18 **A.** I think where -- the ITL objective in terms of strategy
 19 for our products was based on the RRP difference,
 20 where -- and we talked about cost -- where the -- we
 21 were hoping to achieve a lower shelf price for one of
 22 our products compared to a competitor's product, there
 23 was a lower wholesale cost price for the retailer to buy
 24 the product.
 25 Where the trading agreement monies for First Quench

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1 are purely related to the discount tier, First Quench,
 2 relative to the RRP.
 3 They weren't -- it was like they had a lower cost
 4 price for the product, but this, the trading agreement,
 5 has nothing to do with the cost price of a product.
 6 I may not have answered the question exactly, but
 7 it's -- maybe I am making it more complicated than it
 8 needs to be, for which I apologise.
 9 **MR LASOK:** Maybe I ought to retrace my steps slightly,
 10 because I was going to approach this in a slightly
 11 different way.
 12 **MR HOWARD:** Could I suggest -- because there is a simple
 13 question, I don't think this is really controversial.
 14 We seem to be spending a lot of time. Perhaps if you
 15 simply ask Mr Culham by reference to the first sentence
 16 of paragraph 21: in the event that that happened, which
 17 is ITL had a different reduction to RRP to Gallaher, so
 18 in other words Gallaher has 8p and Imperial has 6p, what
 19 then?
 20 **MR LASOK:** With all due respect, we haven't got to that
 21 point.
 22 What I would like to look at is paragraph 22, the
 23 first word, "this" {C3/35/409}. What in your witness
 24 statement does the word "this" refer to?
 25 **A.** Well, the only thing that could be withdrawn was the

1 trading agreement money, if the absolute price moved
 2 above RRP. There was nothing else we could withdraw.
 3 **Q.** When you said in the last sentence of paragraph 21,
 4 "relative shelf prices", right, that doesn't apply in
 5 the context of what you are saying in paragraph 22?
 6 **A.** The only thing that could be withdrawn was the bonus
 7 paid on the tier selling below RRP. The lower wholesale
 8 price was transferred to their business, whatever
 9 they -- they could sell it for, well, any price they
 10 chose. And because that was the wholesale price that we
 11 supplied all retailers at, we couldn't do anything about
 12 that. They would get that benefit anyway.
 13 **Q.** Why in the last sentence of paragraph 21 did you include
 14 the reference to relative shelf prices?
 15 **A.** Well, it's -- I can't remember. It's over a year ago
 16 I wrote the document, so I don't remember exactly why
 17 I used those phrase of words, so apologies for that.
 18 **Q.** Did it reflect your recollection at the time?
 19 **A.** At the time of writing this document or at the time
 20 I was handling the account?
 21 **Q.** At the time when you wrote your witness statement --
 22 **A.** Yes.
 23 **Q.** -- paragraph 21 and paragraph 22, were they accurate?
 24 **A.** Yes, they are, yes.
 25 **Q.** Thank you. Right.

1 Now let's look at paragraph 13 {C3/35/408}. In
 2 paragraph 13 you tell us what the phrase "pricing
 3 strategy" means. Okay?
 4 **A.** Can I read it? (Pause). This is where we were offering
 5 additional promotional support on mainly tactical
 6 bonuses to achieve pricing.
 7 **Q.** Now, I am interested in the bit about the policy of not
 8 increasing the retail prices of ITL's products above
 9 identified differentials compared with the prices of
 10 identified brands of competing manufacturers. That's
 11 the policy, isn't it? That's the strategy?
 12 **A.** That's our objective, yes.
 13 **Q.** That's your objective. So if we look at the trading
 14 agreement in tab 48, and we look at note 1 {D16/48/104},
 15 and the phrase "ITL pricing strategy to be adhered to on
 16 all brands", what we are to understand by that is that
 17 First Quench is, as you put it in paragraph 13, not to
 18 increase the retail prices of ITL's products above
 19 identified differentials compared with the prices of
 20 identified brands of competing manufacturers; is that
 21 correct?
 22 **A.** That was our objective, yes.
 23 **Q.** Right. But wait a minute, the question is whether
 24 that's what note 1 is about. I'll repeat it. When
 25 note 1 says:

1 "ITL pricing strategy to be adhered to on all
 2 brands", right?
 3 Does that mean that First Quench is not to increase
 4 the retail price of ITL's products above identified
 5 differentials compared with the prices of identified
 6 brands of competing manufacturers?
 7 **A.** That was our objective, yes.
 8 **Q.** The question is: is that what note 1 means?
 9 **A.** Well, yes, it would be linked in with that, yes.
 10 **Q.** Does it mean it or doesn't it?
 11 **A.** Well, it relates -- note 1 would cover the point you
 12 made, yes.
 13 **THE CHAIRMAN:** Does the term "pricing strategy" as used in
 14 note 1 mean the same as you have defined "pricing
 15 strategy" to mean in paragraph 13 of your witness
 16 statement?
 17 **A.** I think it's actually -- obviously note 1 is a lot
 18 shorter, so if it had been expressed more fully, it
 19 would hopefully be -- well, it would say the same in my
 20 paragraph 21.
 21 **THE CHAIRMAN:** Paragraph 13.
 22 **A.** Sorry, yes, paragraph 13.
 23 **MR LASOK:** In order to identify what these identified
 24 differentials are, we have to go to another source,
 25 don't we, because we don't see them identified in the

1 trading agreement?
 2 **A.** I don't believe they were given to First Quench as
 3 a formal document. First Quench themselves based their
 4 pricing strategy on RRP and made their pricing decisions
 5 and their pricing tiers based on the RRP. And as our
 6 strategy was based on RRP, you know, there wasn't
 7 a sheet given to First Quench. There was no
 8 differentials given to them.
 9 **Q.** If we go back to tab 46, and look at the last two lines,
 10 the famous (e), we have a parity referred to
 11 {D16/46/101}. So this is an example of Mr Byas
 12 recording the agreement with First Quench in the context
 13 of the trading agreement that, so far as cigar pricing
 14 is concerned, the object is to achieve parity for ITL
 15 and Gallaher brands?
 16 **A.** Our objective was not to achieve parity. We have --
 17 I mentioned this a while ago. Panama was always -- our
 18 objective was to achieve Panama cheaper. So what George
 19 has put in the letter was either what they agreed, what
 20 First Quench told them they were doing, but it wasn't in
 21 line with ITL's strategy at the time.
 22 **Q.** That, according to you, would therefore explain the
 23 letter at tab 49?
 24 **A.** There again, if First Quench have still got Panama at
 25 parity with Hamlet, that's not in line with Imperial

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1 Tobacco's own strategy.
 2 **Q.** Now, look, let's go back to 46 again.
 3 **MR HOWARD:** Surely there is a point. We can't just go
 4 backwards and forwards on the same document, badgering a
 5 witness.
 6 **THE CHAIRMAN:** Where are we going with this, Mr Lasok? Just
 7 bearing in mind that you need to cover T&S Stores as
 8 well today.
 9 **MR LASOK:** Yes. There is a very simple question.
 10 What you are now saying is that there was
 11 an agreement between ITL and First Quench to diverge
 12 from ITL's pricing strategy at the time?
 13 **A.** What I am saying is that George had written that cigars
 14 were not in line with the strategy. Whether there was
 15 agreement, whether there was a disagreement, I don't
 16 know. It's in black and white, therefore it was
 17 a statement. But whether it was a disagreement or
 18 a dispute, I don't know.
 19 **Q.** You see, what I am looking at now in 46 {D16/46/101} is
 20 a letter in which he encloses a final version of the
 21 trading agreement. He notes various things, he
 22 records --
 23 **MR HOWARD:** As I say, there has got to come a point --
 24 **THE CHAIRMAN:** Just sit down, Mr Howard. I think this
 25 should be, I would hope, the last question on this (e)

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1 point for the time being.
 2 **MR LASOK:** The point is very simple: this is a letter
 3 written in the context of the trading agreement. There
 4 is nothing in it at all that tends to suggest that (e)
 5 is a diversion from what the trading agreement provides,
 6 is there?
 7 **A.** As I've said, the trading agreement, our objective was
 8 to achieve our pricing strategy on products. Point (e)
 9 suggests that our pricing strategy was not achieved.
 10 However, we still paid Thresher -- First Quench the full
 11 trading agreement allowance. There was no ...
 12 **Q.** Right. Now, we have an agreement here to achieve parity
 13 for ITL and Gallaher brands in relation to cigar
 14 pricing. Can you tell us the circumstances in which
 15 a failure by First Quench to observe the parity would be
 16 compatible with the agreement between it and ITL?
 17 **A.** Can I ask you to rephrase the question or repeat it?
 18 Sorry.
 19 **Q.** Yes. On any view we have here an agreement between ITL
 20 and First Quench to price cigars --
 21 **MR HOWARD:** Just to make it clear, because it is quite
 22 important, a question is being put "on any view, there
 23 is an agreement --
 24 **MR LASOK:** Can I just interrupt. There is a problem with
 25 Mr Howard seeking to tip off witnesses.

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1 **MR HOWARD:** No, I'm not seeking to tip off. I'm seeking --
 2 **THE CHAIRMAN:** Both of you sit down.
 3 **MR HOWARD:** -- to make sure questions are put properly and
 4 fairly.
 5 **THE CHAIRMAN:** This must be conducted properly.
 6 Now, Mr Culham's evidence has been that he doesn't
 7 know how it came about that there was this statement in
 8 the letter that appears to him to be inconsistent with
 9 what he understands to have been the ITL strategy on
 10 cigar pricing.
 11 He has not conceded that it was an agreement,
 12 because one of the options he suggests is that, well,
 13 Imperial were just told by First Quench that that was
 14 what First Quench wanted to do.
 15 Now, if you want to ask him a question which follows
 16 on from it appearing to be the case that First Quench
 17 had decided, either in agreement with ITL or otherwise,
 18 that that was what they were going to do, then you can
 19 ask that question, but he has not accepted that there
 20 was an agreement to do that.
 21 **MR LASOK:** Yes. So we are proceeding on the basis -- it's
 22 a hypothesis; I accept that you don't agree with it --
 23 that what we have here is an agreement between ITL and
 24 First Quench to price ITL and Gallaher cigar brands at
 25 parity. Okay? So that's the starting point.

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1 A. That's what you are saying, but I say I disagree
 2 with it.
 3 Q. Yes. But where you have an agreement like that --
 4 A. But it isn't an agreement.
 5 **THE CHAIRMAN:** Just listen to the question, Mr Culham.
 6 **MR LASOK:** Where you have an agreement like that, what are
 7 the circumstances in which a failure by First Quench to
 8 price at parity would be consistent with the agreement?
 9 A. But there wasn't agreement from Imperial to price at
 10 parity, and there would be no -- if First Quench chose
 11 to sell cigars at parity, there is no penalty from us.
 12 Q. I am not asking you about a penalty.
 13 **THE CHAIRMAN:** Perhaps put to him a posited circumstance and
 14 ask whether he would accept it.
 15 **MR LASOK:** No, because there is a reason for doing it in
 16 this way, and I will come to the posited ones in
 17 a minute.
 18 Can you think of any circumstance in which, if ITL
 19 says to First Quench "You should price at parity or
 20 match the price between an ITL and a Gallaher brand",
 21 can you think of any circumstance in which First Quench
 22 could do something different, could not price at parity,
 23 and yet remain in line with the agreement with ITL?
 24 A. First Quench, our objective --
 25 **THE CHAIRMAN:** Just answer the question.

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1 A. Yes, if they sold less than whatever the objective was
 2 we were working to. So if it was -- I use cigarettes,
 3 for example. If Embassy No 1, our objective was to have
 4 3p less than Benson & Hedges, if they went 10p less,
 5 that was good; if they went 4p less, that was good. So
 6 very good.
 7 **MR LASOK:** Wait a minute. If ITL and First Quench agree to
 8 price ITL and Gallaher brands at parity, you say it is
 9 consistent with that agreement for First Quench to price
 10 otherwise than at parity?
 11 A. If our brands were cheaper, yes.
 12 Q. If the brands were cheaper. And what is the fact that
 13 you rely on in order to justify that conclusion?
 14 A. The fact is that I was working for the company for many
 15 years, about 20 years as an account manager, and
 16 wherever retailers chose to sell our products cheaper,
 17 that was a benefit to our business. And as I've said
 18 when I have been here before, occasionally we have
 19 highlighted one or two obvious errors; if a retailer has
 20 made a typographical error or something is not in line
 21 with the strategy they've told us. So there are one or
 22 two exceptions.
 23 But in general, if they sold our brands cheaper than
 24 our objective, that was very positive. In all the time
 25 I've worked for the company, that was the case.

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1 Q. Let's suppose that you see that on the shelf prices in
 2 First Quench stores the price of a Gallaher cigar brand
 3 that is linked to an ITL cigar brand is lower than the
 4 price of the ITL brand. Would you conclude that
 5 First Quench was respecting the agreement to price at
 6 parity?
 7 A. I would just say there wasn't an agreement to price at
 8 parity for us. But if they chose to sell a Gallaher
 9 product less than our competing product, so for example,
 10 Classic and Hamlet, it could be because Gallaher's were
 11 offering a tactical bonus, it could be because we have
 12 had an MPI and Gallaher's hadn't, it could be a retailer
 13 error, or -- I don't know the reason. So there are
 14 occasions when Gallaher products are cheaper on the
 15 shelf than our products.
 16 Q. Well, the question was whether you would regard that as
 17 consistent with an agreement to price the two brands at
 18 parity?
 19 A. We would like to have our brand no more than Hamlet.
 20 Q. Would you regard it as consistent with the agreement to
 21 price at parity?
 22 A. As I've said, there wasn't an agreement to price at
 23 parity, but if they were pricing Hamlet, for example,
 24 cheaper than Panama, one of our products, that wouldn't
 25 be in line with our objective.

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1 Q. So you wouldn't have regarded it as consistent with
 2 an agreement to price at parity?
 3 A. It wouldn't be in line with agreement, but we didn't
 4 have that agreement.
 5 Q. Yes.
 6 Now, if you have a situation in which, when the
 7 Gallaher brand goes down on the shelves and that puts
 8 the parities out of joint, as it were, because we have
 9 now got a differential and not a parity, why do you say
 10 that -- and you accept that in that scenario it's not in
 11 accordance with the agreement, and remember we are
 12 talking about a hypothetical agreement, you don't accept
 13 there was an agreement --
 14 A. Are we still --
 15 **THE CHAIRMAN:** Wait for the question.
 16 **MR LASOK:** Let me be clear. We are talking about
 17 a hypothetical scenario in which ITL and First Quench
 18 have agreed that Gallaher cigar brand or Gallaher
 19 brand X is to be priced at parity with ITL brand Y.
 20 Okay? That's the scenario. You have just told us if
 21 you found on the shelves that Gallaher brand X was below
 22 the price of ITL brand Y, you would not think that
 23 First Quench was complying with this agreement?
 24 A. If such agreement was in place, they were obviously not
 25 honouring their side of the agreement, but there wasn't

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1 such an agreement.
 2 **Q.** Yes. What I am trying to get at is: if that is so, why
 3 would you have concluded that, if the position was the
 4 reverse, the agreement was still being respected?
 5 **A.** Because our brands were treated better, so the consumers
 6 got a lower price. And as I've said in all the time
 7 I was an account manager that was an extra incentive for
 8 consumers to buy our products, and that would be
 9 welcomed.
 10 **Q.** Isn't it more accurate to say that your thought would
 11 be: actually, they are not complying with the agreement,
 12 but I am not going to do anything about it?
 13 **A.** In other agreements, and we are talking about T&S later,
 14 where it says "at least 3p less than" and everything,
 15 there was a lot more detail in that agreement than there
 16 is in this one. So yes, they wouldn't be treating the
 17 products the same. But there was a benefit, and I, as
 18 an account manager, wouldn't raise that with the
 19 retailer.
 20 **Q.** That of course would actually depend upon what ITL's
 21 underlying strategy actually was, because if, for
 22 example, the underlying strategy was parity, then you
 23 might do something about it?
 24 **A.** Our underlying strategy was, in the case of two brands
 25 that had the same RRP, our brand to be no more expensive

1 than, which could be parity or our brand could be
 2 cheaper.
 3 **Q.** I think we have already dealt with that at length, so
 4 I note the fact that we take different views on what
 5 ITL's pricing strategy actually was.
 6 Now, let's move on to a variation of this. In
 7 paragraph 21 of your witness statement, you refer to the
 8 passing through of lower cost prices in the form of
 9 lower absolute and relative shelf prices; right?
 10 **A.** It's referring to lower cost prices. So if our brand
 11 was a pound an outer cheaper than a competitor's
 12 product, we would hope that they would be sold to
 13 consumers cheaper, yes.
 14 **Q.** Am I right in thinking that that's your understanding of
 15 ITL's general position? It's not peculiar to
 16 First Quench; it's your understanding of ITL's general
 17 position?
 18 **A.** If we had lower cost prices, we would hope that would
 19 get passed on to consumers, yes.
 20 **Q.** Now, of course, if you go to paragraph 28,
 21 {C3/35/410} -- you can read the whole paragraph to
 22 yourself if you would like -- but I was interested in
 23 the penultimate sentence, where you say:
 24 "I would also note that no disclosure was made of
 25 the specific cost prices each supplier charged to

1 First Quench."
 2 (Pause)
 3 **A.** I've read the paragraph.
 4 **Q.** I am just interested in the bit where you say:
 5 "No disclosure was made of the specific cost prices
 6 each supplier charged to First Quench".
 7 **A.** Correct.
 8 **Q.** Right. So the upshot is that you couldn't know for sure
 9 that the benefit of lower cost prices was being passed
 10 on to the consumer, could you?
 11 **A.** The cost price -- has anyone else gone into the way the
 12 cost price and the Q rates have been worked out across
 13 the business?
 14 **Q.** We have a lot of information about that, but if you
 15 would like to give your own explanation, I am not going
 16 to stop you.
 17 **A.** We would publish a Q5 rate, for example, and that would
 18 be the basic cost price for the retailer. Other
 19 companies also published their price lists, but where
 20 their overall -- so that would be their cost price. The
 21 trading agreement allowance and all other money
 22 obviously was never in the public domain, so I wouldn't
 23 have known.
 24 **Q.** The problem about the trading agreement that we are
 25 looking at is that it doesn't talk about the passing on

1 of cost prices at all, does it?
 2 **A.** It doesn't mention that, no.
 3 **Q.** No. So the bit in note 1, in tab 48, {D16/48/104} about
 4 ITL pricing strategy to be adhered to on all brands,
 5 that isn't about passing on the benefit of lower cost
 6 prices?
 7 **A.** Well, in effect it is, because our strategy was where
 8 the lower cost prices delivered in the Q -- the
 9 wholesale cost price. That's all that our pricing
 10 strategy was.
 11 Where we had lower Q rate prices, that then
 12 translated into RRP, and that's how the strategy was
 13 built on, based on the lower wholesale start cost
 14 prices.
 15 **Q.** Did somebody tell you that?
 16 **A.** Tell me what, sorry?
 17 **Q.** What you have just said. Is this something that you
 18 found from somewhere, or somebody told you?
 19 **A.** No, our strategy is based on the RRP, but to get to the
 20 RRP you have to have a wholesale start price. So
 21 I would be aware how our pricing -- price list was
 22 produced, yes.
 23 **Q.** Let's take it in stages. Let's assume that you have got
 24 Richmond and Dorchester. Let's also assume for the sake
 25 argument that you have a trading agreement which says

1 that Richmond is to be priced no higher than Dorchester.
 2 Are you with me so far?
 3 **A.** Yes.
 4 **Q.** Okay. We are talking about shelf prices. Okay?
 5 **A.** Yes.
 6 **Q.** Yes. Now, let's suppose that the difference between the
 7 actual cost prices for Richmond and Dorchester are in
 8 Dorchester's favour, so that the retailer would be able
 9 to price Dorchester at, let's say, a penny below
 10 Richmond for a pack of 20s, without suffering
 11 a reduction in its margin by comparison with the margin
 12 that it's getting for Richmond. Let's suppose that is
 13 the case.
 14 **A.** Okay.
 15 **Q.** Okay. Now, how does the requirement that Richmond be
 16 priced no higher than Dorchester enable lower cost
 17 prices to be passed through to the benefit of the
 18 consumer?
 19 **A.** If, using your example, Richmond was priced a penny more
 20 than Richmond -- sorry, Richmond was priced a penny more
 21 than Dorchester, as happened in other brands, we would
 22 obviously try and negotiate with the retailer, and in
 23 some cases we would be offering tactical bonuses to
 24 achieve our objective.
 25 **Q.** Well, I am sorry. We have an agreement --

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1 **THE CHAIRMAN:** No, you've misunderstood the question,
 2 I think.
 3 **MR LASOK:** We have an agreement, right, that Richmond is to
 4 be priced no higher than Dorchester?
 5 **A.** That was our objective, yes.
 6 **Q.** The retailer has signed up to this agreement. Okay? So
 7 the retailer is presented with a situation in which it
 8 could price Dorchester at 1p below Richmond, but it
 9 looks at its trading agreement with ITL and sees that
 10 that would be inconsistent with the agreement. So it
 11 prices Richmond and Dorchester at the same price on the
 12 shelves, even though the difference in net or actual
 13 cost prices would have enabled it to price Dorchester at
 14 one penny below.
 15 Isn't it obvious that in those circumstances the
 16 requirement that we are looking at, which is that
 17 Richmond be priced no higher than Dorchester, wipes out
 18 Gallaher's cost price advantage?
 19 **A.** I don't think it is obvious. Retailers would make their
 20 own choice and price as they wanted to.
 21 **Q.** Well, you have an agreement with the retailer, and your
 22 object is to ensure that Richmond is priced no higher
 23 than Dorchester. Isn't it obvious that the purpose of
 24 your agreement in that scenario is to wipe out
 25 Gallaher's competitive advantage?

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1 **A.** Our -- as I said, it could be as a negotiating tactic --
 2 negotiate with us to get more money from us. I don't
 3 know what the retailer would choose to do.
 4 **Q.** You have signed the retailer up to an agreement; don't
 5 you expect the retailer to comply with the agreement?
 6 **A.** No. The retailer in case of First Quench, there are
 7 many instances where, although the agreement was signed
 8 up to, it was not delivered at shelf level. As we have
 9 just pointed out with the cigars, if all the cigars are
 10 at parity, that was not in line with our agreement. But
 11 we didn't take any money away, we didn't penalise them,
 12 we carried on paying them, because the retailer chose
 13 their own price.
 14 **Q.** So the agreement meant nothing at all?
 15 **A.** I didn't say the agreement meant nothing at all, I said
 16 they didn't take full notice of it.
 17 **Q.** Right. Let's look at the alternative scenario, and this
 18 is where the net cost prices work to the advantage of
 19 ITL so that the retailer could put Richmond 20s on the
 20 shelf at 1p below Dorchester, and the agreement between
 21 ITL and the retailer is that the retailer shall price
 22 Richmond at no more than Dorchester.
 23 Now, can you explain to me how that agreement
 24 secures the pass-through of ITL's wholesale price
 25 advantage?

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1 **A.** Well, I can't recollect that instance happening, or
 2 maybe -- I don't know, because I didn't see retailers'
 3 full cost prices. Our objective was to have -- which
 4 was based on the RRP differences, and that's what we
 5 based our strategy on.
 6 **Q.** You see, the problem is that in that scenario where ITL
 7 has the cost price advantage over Gallaher, your
 8 agreement, ITL's agreement with the retailer is
 9 incapable of ensuring that that advantage is passed
 10 through to the customer, because the retailer can comply
 11 with the terms of the agreement by pricing at parity.
 12 There is no obligation on the part of the retailer to
 13 reduce the price of Dorchester at all.
 14 **A.** Sorry, you were talking about Richmond. Richmond or
 15 Dorchester?
 16 **Q.** This is the scenario where the real --
 17 **A.** You were saying that Richmond was cheaper than
 18 Dorchester.
 19 **Q.** I would like to be clear. It's the real cost price for
 20 Richmond --
 21 **A.** When I was --
 22 **Q.** -- is lower than the real cost price for Dorchester?
 23 **A.** We don't know the real absolute cost price of what
 24 a retailer paid for our competitive products. All we
 25 would know is the RRP for a product, which was, for

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1 example, £2, and the published Q rate for that product
 2 would be X. That's all we would know.
 3 **THE CHAIRMAN:** The question you are being asked is rather
 4 simpler than that. You have maintained that the aim, or
 5 one of the aims of the agreement, the differentials
 6 agreements, is to ensure that lower ITL prices are
 7 passed through to the consumer. Mr Lasok is putting to
 8 you: well, that doesn't really work, because the
 9 agreement allows for parity between two brands, even if
 10 actually the Richmond brand is cheaper.
 11 **A.** Yes, because our objectives were based on the RRP's,
 12 because we didn't know the total cost prices for anyone
 13 else. Our agreement, ie the Richmond no more than
 14 Dorchester, was based on the published RRP.
 15 **MR LASOK:** So if we look at it in that light, with ITL's
 16 object -- just looking at it objectively speaking, I am
 17 not talking about subjective intentions, I am just
 18 talking about the nature of this requirement, and the
 19 requirement -- I'll remind you -- is a requirement to
 20 price Richmond no higher than Dorchester. The ordinary
 21 and natural consequence --
 22 **A.** Sorry, is there a blind?
 23 **Q.** I have the same problem from time to time. I have got
 24 out of it because I am standing up. Could somebody
 25 press the magic button?

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1 **A.** Sorry.
 2 **Q.** Yes.
 3 **A.** Thank you.
 4 **Q.** So we have got the situation in which the requirement is
 5 to price Richmond no higher than Dorchester. It doesn't
 6 actually give ITL any benefit in terms of passing on
 7 a cost price advantage, but what it definitely does is
 8 kill off any chance of Gallaher achieving a pass-through
 9 if it has got a more competitive net cost price.
 10 That's, I think, where we have got to.
 11 Now let's look at what happens when there are
 12 changes in prices. We look at it from the perspective
 13 of -- I am going to change it slightly -- a requirement
 14 or an agreement or a commitment, however you call it,
 15 that the retailer should price at parity between
 16 Richmond and Dorchester.
 17 So would you agree with me that if that's the
 18 scenario, when the shelf price of the Gallaher brand
 19 goes up, ITL's objective is to ensure that the price of
 20 the ITL brand goes up to follow the rise. Again, to be
 21 precise, if the shelf price of Dorchester goes up, the
 22 shelf price of Richmond ought to go up.
 23 **A.** If the retailer changed their strategy, is that what you
 24 are saying? What's the question?
 25 **Q.** No, you have an agreement with the retailer or

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1 a commitment from the retailer that the retailer will
 2 price Richmond at parity with Dorchester.
 3 **A.** Or no more than, yes.
 4 **Q.** Well, I'm putting it to you as parity. We can deal with
 5 the no more than later. So we will take it at parity.
 6 The reason why I am putting that to you is because
 7 we have a lot of documents, as you know, in which we see
 8 ITL saying things like "we are paying for parity",
 9 "please move prices to match". So that's the
 10 hypothesis: Richmond is to match Dorchester in shelf
 11 prices.
 12 So isn't your -- ITL's -- expectation that if the
 13 price of Dorchester goes up, the price of Richmond
 14 should go up?
 15 **A.** What would be the circumstance for Dorchester going up?
 16 **Q.** All right, let's take it in stages. Let's suppose that
 17 the retailer, off its own bat, has looked around the
 18 market and it thinks that it's got headroom to increase
 19 the price of Dorchester, but it hasn't increased the
 20 price of Richmond. It's got the headroom to do so,
 21 because both products are in the same market segment,
 22 they are all constrained by the same competitive
 23 constraints, so what's good for one is good for the
 24 other, but the retailer hasn't put up Richmond.
 25 **A.** That would be taken as a benefit, because our agreements

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1 and the way we operated was no more than. So if they
 2 had chosen to put Dorchester up off their own bat, their
 3 own strategy, but not Richmond, that would have been
 4 taken as an added bonus, a benefit.
 5 **Q.** You see, the starting point is that the peculiarity of
 6 an agreement that doesn't give ITL the benefit when ITL
 7 has got a more competitive wholesale price, so if the
 8 agreement isn't structured in such a way as to give ITL
 9 the benefit of a more competitive wholesale price, why
 10 are we supposed to believe that it's structured in such
 11 a way as to give ITL some other competitive benefit?
 12 **A.** Sorry, what's the question? I was explaining if the
 13 retailer put Dorchester up but not Richmond, we would
 14 take that as a benefit. If Gallaher's had had an MPI,
 15 that would have been Dorchester above Richmond, or if
 16 there had been a Budget increase generally, they would
 17 both go up at the same time.
 18 **Q.** You see, the point I am putting to you is this: that you
 19 have structured a requirement that you have sought to
 20 justify on the basis of the pass-through of net cost
 21 prices, more competitive net cost prices, and you are
 22 launching the argument that this is ITL's strategy, the
 23 purpose is to be more competitive vis-a-vis Gallaher.
 24 But when we look at this justification, I've put it to
 25 you that it just doesn't work. And if it doesn't work,

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1 where do we get the idea from that when you move onto
2 shelf prices, ITL's intention is to be cheaper than
3 Dorchester at all? Because if you wanted to be cheaper,
4 you would never have structured these arrangements in
5 this way at all, because your starting point would have
6 been: if we, ITL, have got a lower cost price, we want
7 that to pass through to the customer, and so we would be
8 reducing the -- we would be ensuring in some way that
9 the retailer passes through; you wouldn't have entered
10 into these arrangements involving parities and
11 differentials at all, would you?

12 **MR HOWARD:** I just wonder, is this a fair way to ask
13 a question? This question is running to about 15 lines,
14 I think, on the transcript, and there are multiple
15 questions in there. Surely one has to break something
16 down so the witness can actually follow it. If you are
17 going to argue your case through the witness, you have
18 to break it down fairly.

19 **MR LASOK:** I apologise. I think my learned friend is
20 quite --

21 **THE CHAIRMAN:** I think the question is perhaps this: that if
22 the aim of your agreement with the retailers was to
23 ensure that lower net cost prices were reflected in
24 lower shelf prices, why do you have to add on to that
25 an element about the relativity of that price with

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1 a Gallaher brand? What does that relativity bring to
2 the agreement that you couldn't achieve just by saying
3 to the retailer "Please reflect our cost price in your
4 shelf price"? Is that a different way of putting it?

5 **A.** In effect, without saying it the way you have said it,
6 that's effectively what our pricing differential
7 objectives were.

8 I never, ever knew the net cost price for a product
9 for any retailer from another supplier. So we are only
10 talking about the published gross price that's in the
11 published price list, and that's where the differential
12 was translated from. We could have said "If we give you
13 a product £1.80 an outer cheaper", for example, "we
14 would like you to pass that £1.80 on to consumers".
15 That £1.80 was effectively 2p, so we've said "We'd like
16 you to have it 2p cheaper to consumers".

17 We never knew the net price, only the published
18 gross price. So we never knew what a retailer paid for
19 a competitive product. So all our objectives -- sorry,
20 our pricing strategy was based on the RRP difference in
21 our product compared to a competitor's product, and that
22 was reflected in, in the case of Gallaher's, published
23 wholesale price, not in their net price, we didn't know
24 what it was.

25 **MR LASOK:** Well, I was putting, I think -- Mr Howard is

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1 quite correct to say that it was a bit of a long
2 marathon question. I was trying to look at it from a
3 slightly different angle, which is that when I put to
4 you the question: if the Gallaher shelf price goes up
5 because the retailer has just decided to put it up,
6 wouldn't your expectation, on the basis of an agreement
7 with the retailer that the retailer should price at
8 parity with Dorchester, be that the retailer ought to
9 put the price of Richmond up?

10 **A.** No, completely the opposite.

11 **Q.** And the reason you give me for that is because it's
12 beneficial to ITL to have Richmond below Dorchester?

13 **A.** And to consumers if they are getting a cheaper price,
14 yes.

15 **Q.** But when we look at this cost price scenario, where we
16 see that the requirement simply is incapable of giving
17 Richmond an advantage from a lower cost price, it's
18 really an anti-Gallaher move because it eliminates
19 a Gallaher wholesale cost price advantage?

20 **A.** We were competing in the market with Gallaher to try and
21 encourage consumers to buy our products, and Gallaher's
22 were our competitors in the marketplace.

23 **Q.** But given the fact that you have structured this, even
24 in the case of something that is priced no more than,
25 you have a situation in which there is in fact no

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1 obligation, no requirement, no commitment on the part of
2 the retailer to price Richmond anywhere below
3 Dorchester. They are perfectly entitled, when the
4 Dorchester price rises, to increase Richmond to the same
5 level as Dorchester?

6 **A.** If they wanted to do so, but we don't control their
7 pricing.

8 **Q.** And the difficulty is that, I put to you quite simply,
9 you would like that to happen because actually your
10 strategy is based on the idea that the best place for
11 Richmond is the same price as Dorchester?

12 **A.** No, I would disagree. Our strategy was to have Richmond
13 no more than Dorchester, and we would not encourage --
14 if, in the example used, the retailer chose to put
15 Dorchester up 6p, we would be very pleased with that
16 position as long as we weren't being asked to pay for it
17 retrospectively, which sometimes happened.

18 **Q.** But then you have previously told us that this policy
19 was all oriented around the RRPs?

20 **A.** Yes.

21 **Q.** So the signal that you are sending out is that
22 Richmond's best place and preferred place is alongside
23 Dorchester?

24 **A.** That was our strategy, but better than strategy was
25 always acceptable.

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1 Q. But that's not what you get from per using the RRP's,
2 is it?

3 A. The RRP's, for example, for Richmond and Dorchester were
4 similar, if not the same, most of the time, and that was
5 where our base strategy was. And our objective was to
6 have Richmond no more than Dorchester. If it was
7 cheaper, that was treated as a benefit; if it was
8 dearer, my objective was to try and encourage the
9 retailer or spend tactical bonuses to bring Richmond
10 down so it was no more than Dorchester. But if we
11 were -- if Richmond was cheaper, that was a benefit.

12 MR LASOK: We can come to tactical bonuses -- I see now it's
13 1 o'clock -- after lunch.

14 THE CHAIRMAN: Yes, thank you.

15 Thank you very much, Mr Culham. We will take
16 a break for lunch now, and come back at 2 o'clock, and
17 over that lunch break you mustn't discuss your evidence
18 with anyone. Perhaps you would like to pop out at the
19 back now, there are some logistical things we need to
20 discuss.

21 (In the absence of the witness)
22 Discussion re timetable

23 THE CHAIRMAN: As far as timing is concerned, we would need
24 to complete Mr Culham's cross-examination this
25 afternoon.

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1 MR LASOK: We will certainly do that, I would have thought
2 by 3.30. I will obviously try and do it more quickly
3 than that.

4 THE CHAIRMAN: We might then be able to fit in his
5 re-examination this afternoon as well. Let's aim to do
6 that, because tomorrow morning we can not start earlier
7 than 10.30, and if we then have some time, say half
8 an hour, for your response to our questions, that gives
9 us the rest of the day for Mr Wragg.

10 So if we say you can complete your cross-examination
11 of Mr Culham at, say, 3.45, and then we would have our
12 break then and then re-examination for the rest of this
13 afternoon, Mr Howard?

14 MR HOWARD: Yes. I think Mr Lasok was saying he would
15 finish at 3.30.

16 THE CHAIRMAN: Thank you. We will come back at 2 o'clock.
17 (1.02 pm)

18 (The short adjournment)
19 (2.00 pm)

20 MR LASOK: Mr Culham, before lunch we had actually moved on
21 into some general questions, but for the sake of
22 tidiness I would like to finish off on First Quench.

23 To that end, I just wonder whether you could look at
24 paragraph 25 of your witness statement, please
25 {C3/35/409}. Here you are referring to the

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1 ITL/First Quench trading agreement that was in force
2 from 1 October 2000, and you say that that trading
3 agreement was fundamentally identical to the one that
4 you were discussing above.

5 I wonder, in that connection, whether you could turn
6 to tab 20 {D16/20/40}. What you have is a handwritten
7 note, but after that you have got an explanation of the
8 new trading agreement that is to be found in the letter
9 dated 19 October 2001. If you go to the third page of
10 that letter {D16/20/43}, in my copy somebody has written
11 in manuscript some pagination in the bottom right-hand,
12 which is 1, 2, 3 and so forth of 6. If you go to 3
13 of 6, you have a description of the objective of the new
14 trading agreement, and it says that it's to ensure that
15 ITL's strategies are achieved both in actual levels and
16 differentials measured against Gallaher competing
17 brands. (Pause)

18 That was reflected in the later trading agreement
19 that we have seen, wasn't it?

20 A. Well, it says in there also bonus paid on price
21 competitive tiers, which is what I said earlier on.

22 Q. I am looking --

23 A. The trading agreement, this wasn't actually formally
24 agreed, I seem to remember. Reading the note from
25 Michael Williams, I don't think that was the final

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1 trading agreement.

2 Q. The objective of the trading agreement is set out there,
3 and in relation to pricing it includes the bit that
4 says:

5 "To ensure ITL's strategies are achieved both in
6 actual levels and differentials measured against
7 Gallaher competing brands.?"

8 A. I agree it says that there, yes.

9 Q. That, so far as you recall, was what was happening at
10 the time when you were running the First Quench account?

11 A. We were looking to achieve our pricing differentials
12 relative to the RRP's of Gallaher products.

13 DR SCOTT: Sorry, can I ask a quick question relating to
14 this? This is dated 19 October 2001. In paragraph 25
15 {C3/35/409}, it says "in force from 1 October 2000".

16 MR LASOK: That's my mistake. I think paragraph 25 refers
17 to the earlier one, which is in tab 7.

18 DR SCOTT: Ah, right. Sorry, that's why I was confused.
19 Thank you.

20 A. Sorry, so which point is this trading agreement ...?

21 MR LASOK: I made a mistake.

22 A. Sorry.

23 Q. What I referred you to in your paragraph 25 doesn't
24 relate to the first trading agreement, which is in
25 tab 7, but it relates to the second trading agreement

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1 and I've drawn your attention to the document at tab 20,
 2 and to the point that the pricing objective in the new
 3 trading agreement is set out as there.
 4 **A.** Yes, that was our objective.
 5 **Q.** You have said that to complete the point, however -- and
 6 I should have put it clearly, for which I apologise --
 7 you have said that the first trading agreement running
 8 from 1 October 2000 was fundamentally identical to the
 9 second trading agreement. So what I am putting to you
 10 is that this pricing objective or pricing strategy set
 11 out in the letter at tab 20 is a common theme running
 12 from the first trading agreement to the later one?
 13 **A.** Our objective was the same from the start -- from the
 14 first trading agreement through to the final one.
 15 Obviously, as you have seen, the words have changed as
 16 the trading agreements have developed over the years,
 17 but yes.
 18 **Q.** Now, previously, before lunch, we were talking about
 19 what happens when there is a movement upward in
 20 a Gallaher price.
 21 Another case that we can look at is the situation
 22 where ITL is moving its price up in the market. So the
 23 hypothesis I am putting to you is this: you have ITL
 24 wishing to move the price of Richmond up, and it's got
 25 an agreement with the retailer, and the agreement with

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1 the retailer is that Richmond and Dorchester are to be
 2 kept at parity, or it could be that the price of
 3 Richmond is to be no more than the price of Dorchester.
 4 But the point I am putting to you is based on what
 5 we were discussing before lunch, and that is that ITL's
 6 pricing strategy isn't really about low pricing of ITL
 7 products, it's about maintaining a relativity between
 8 an ITL brand and a Gallaher brand.
 9 So shall we just pause there. Do you accept that
 10 ITL's pricing strategy was concerned with maintaining
 11 a relativity or a pricing relationship between ITL
 12 brands and Gallaher brands?
 13 **A.** We benchmarked our products against Gallaher products,
 14 and our pricing objectives, strategy, were based on the
 15 relative RRP's of those products.
 16 **Q.** From time to time ITL would change the relationship. It
 17 would say to the retailer "We have decided that the
 18 parity or differential that we have previously had is
 19 different"?
 20 **A.** There are circumstances in all the documents where
 21 relative RRP's have changed for tactical bonus reasons
 22 and different objectives have been sought.
 23 **Q.** To give an example, I know that it's not something that
 24 you were involved in, in the First Quench case, but it
 25 was something that you were involved in in relation to

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1 T&S Stores and also others. If you go to tab 29, and
 2 just read tab 29 to yourself {D16/29/59}.
 3 (Pause)
 4 So this is an example of Gallaher, Rothmans and
 5 Philip Morris have announced an MPI. ITL decides not to
 6 follow suit, but what it does is to write to -- here
 7 it's First Quench, reminding First Quench -- and this is
 8 the third paragraph -- that a very important aspect of
 9 ITL's pricing strategy is the differential pricing. And
 10 what ITL then does is to indicate that the normal
 11 differentials have now changed.
 12 So this is an instance in which we have a Gallaher
 13 price move upwards, and in order to prevent there from
 14 being a move upwards by the retailer in the ITL brand
 15 price, ITL revises the pricing differentials?
 16 **A.** They were revised because the RRP's have changed, and as
 17 you mentioned with T&S, in their agreement they said we
 18 can revise the differentials if the relative RRP's
 19 change.
 20 **Q.** Yes. What that meant was that ITL could do it the other
 21 way as well, because in the case of an ITL price
 22 increase it might say to the retailer "We are altering
 23 the differentials", or it might not; isn't that correct?
 24 **A.** As I say, if I use the -- you brought up T&S, and if we
 25 use that example, it said we could change the

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1 differentials subject to changing RRP's, yes.
 2 **Q.** If it didn't alter the differentials, but it simply
 3 increased its own prices, the expectation would be that
 4 the retailer would move the linked Gallaher brand's
 5 price in accordance with the pricing differential
 6 strategy that had been agreed between it and ITL?
 7 **A.** I think the only reason the retailer would do that is to
 8 make more profit themselves, and we would certainly not
 9 expect them to do that.
 10 There are instances over the years where retailers
 11 have chosen to change prices, but we very much had not
 12 encouraged that, had fought against it. So no,
 13 I disagree.
 14 **Q.** Could you look at tab 30, please {D16/30/60}. The
 15 figures are confidential, but we don't need to worry too
 16 much about those. Just read the letter to yourself.
 17 (Pause)
 18 Did you ever write letters like this?
 19 **A.** I can't say what letters -- I have written hundreds of
 20 letters over the years, so I may have done, I may not
 21 have done. I can't answer that question.
 22 **Q.** Okay, but what we see here is ITL organising a move
 23 upwards in prices --
 24 **A.** We were having a manufacturers' price increase.
 25 **Q.** But more importantly, you have in paragraph 9

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1 alterations to the differentials. At the last three
2 lines of the letter we have ITL saying that it wishes to
3 move the market up on Richmond brands, but goes on to
4 encourage First Quench to follow on Dorchester, and then
5 gives a guideline across the trade of prices for both
6 Richmond and Dorchester. And it's anticipating that
7 shelf prices would end up as stated in that letter.

8 So its expectation was -- and I put it, I think, as
9 clearly as I can -- that unless Gallaher issued
10 a countermanding instruction to the retailers, the
11 result of the Richmond price rise across the trade would
12 be the rise in Dorchester by the retailers. I'll just
13 stop there.

14 **A.** I think it goes back to the previous letter you have
15 drawn my attention to where Gallaher's had had an MPI,
16 they had chosen to put Dorchester up at that MPI, and
17 then because Imperial didn't have an MPI, Gallaher
18 appeared to have done a tactical promotion on
19 Dorchester.

20 So our, or George's -- I can't speak for George
21 because he is not here, but my expectation would be if
22 Gallaher's were doing tactical promotions on Dorchester
23 post their MPI, we would -- maybe Gallaher's would stop
24 the tactical promotions, maybe they wouldn't, but that's
25 all it's to do with, I think.

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1 **Q.** It wasn't a tactical promotion. What had happened was
2 there had been a Gallaher price hold. In other words,
3 at the time of the MPI in June, its prices for certain
4 brands, such as Richmond and Dorchester, hadn't gone up.
5 There hadn't been a change?

6 **A.** If Gallaher's brand was Dorchester and they had an MPI
7 but they hadn't put Dorchester up, ie a tactical
8 promotion or price hold, it's the same effect. They had
9 announced the MPI, but didn't implement it.

10 **DR SCOTT:** So if we can understand what happens, Gallaher
11 announce the MPI, so the RRP differential shifts.

12 **A.** Yes.

13 **DR SCOTT:** They then announce a price hold.

14 **A.** Which obviously they wouldn't announce to us, they would
15 announce to the retailers.

16 **DR SCOTT:** So presumably at that point, rather than allow
17 a disadvantage to occur, you would want an opportunity
18 to respond to the price hold, would you?

19 **A.** Well, I didn't, because we didn't have an MPI.

20 Therefore, our brand was no more expensive than
21 Dorchester.

22 **DR SCOTT:** Yes, but what you explained to us was that
23 because their RRP had changed, the differentials in your
24 strategic pricing requirement would change as
25 a consequence of the MPI.

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1 **A.** Yes, but they had done a tactical promotion for Gallaher
2 products and we had left our selling price, whatever it
3 was, at the same level. We hadn't then reduced the
4 price when Gallaher's had an MPI. We left our price the
5 same.

6 **DR SCOTT:** But you would not expect the retailer then, the
7 differential having changed, to take the price of
8 Richmond down to restore that differential?

9 **A.** I don't think many retailers would have done. They
10 would have ignored our wish.

11 **DR SCOTT:** Right.

12 **MR LASOK:** Well, now, I think you can put away the
13 First Quench file, and now could you look at annex 29,
14 please, and we will move to T&S.

15 I think that, from your witness statement, you were
16 the national account manager for T&S from around 1997 to
17 1998 to 2002/2003?

18 **A.** I believe that's correct, yes.

19 **Q.** Okay. So if you go to tab 40 {D29/40/131}, this should
20 be the T&S Stores/Imperial Tobacco business agreement
21 effective from 1 January 2002?

22 **A.** We have the same document.

23 **Q.** Am I right in thinking that -- well, it isn't signed by
24 you, it's signed by Doug Flello from T&S. Do I take it
25 that you were the person who negotiated this agreement

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1 with T&S?

2 **A.** Yes, it was -- I produced it, yes.

3 **Q.** It was during your period as NAM for T&S?

4 **A.** Yes, it is.

5 **Q.** So in this, if we look at this agreement, the second
6 paragraph on the first page says:

7 "In return for the continued full distribution of
8 ITL distributed products plus prompt co-operation
9 regarding new product launches and pricing activities
10 during the year, ITL will offer the following
11 support ..."

12 Then there are various things under the heading
13 "2002 planned investment". I believe that the amounts
14 are confidential, but we don't need to worry too much
15 about that. The first column under the heading "2002
16 planned investment" has in the third item "pricing
17 policy". Do you have that?

18 **A.** I have, but mine is redacted so I don't know what the
19 figures are.

20 **Q.** If you go to the next page, we have a bit at the bottom
21 of the page called "Pricing policy", and it starts off
22 by referring to the fact that ITL was going to
23 contribute monthly promotional bonuses to assist with
24 the cut prices charged in selected T&S branches.

25 Then if you go to the last two lines we have this:

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1 "The overall requirement is that ITL products are
 2 treated no worse than equally in terms of selling prices
 3 compared with other manufacturers' similar products."
 4 {D29/40/132}
 5 On the next page {D29/40/133}, we have it saying:
 6 "A full requirement is shown on the attached
 7 listing."
 8 Then if you go to the attached listing, the
 9 pagination in my copy at any rate is the stamped number
 10 at the bottom right, but if you go to page 290
 11 {D29/40/136}, you have the price requirements schedule,
 12 and for present purposes it's probably sufficient if we
 13 look at the fourth item down, which is "Superkings". Do
 14 you have that?
 15 A. I have, yes.
 16 Q. So you have a list, "Superkings, Superkings Lights,
 17 Superkings Menthols, Superkings Ultra, Raffles, Raffles
 18 Lights", then there is a colon and we have the 20s at
 19 least no more than the price of Berkeley, and the 100s
 20 also at least no more than the price of Berkeley.
 21 Okay?
 22 A. Yes.
 23 Q. Fine. Then if we go back to page 287 just for the sake
 24 of completeness {D29/40/133}, and go to the fourth
 25 paragraph from the top, we have a paragraph that says:

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1 "T&S head office will correct any errors highlighted
 2 by ITL of price tiers."
 3 I interpolate to say that that relates to the price
 4 files which had to be supplied by T&S to ITL.
 5 A. If there were errors in them, yes.
 6 Q. Pardon?
 7 A. If there were errors, yes.
 8 Q. Then the contract continues:
 9 "... and allow ITL to react to pricing activity
 10 undertaken by other manufacturers, although ITL may not
 11 take any action."
 12 So we have called that an opportunity to respond
 13 clause. Okay so far?
 14 A. Yes, yeah.
 15 Q. Let's go to tab 46. Tab 46 is dated 11 June 2002, and
 16 at this point we are very shortly, I think, after the
 17 making of the trading agreement that we have just looked
 18 at. I don't think that we have a date for that trading
 19 agreement, but certainly the chronology in the bundle
 20 tends to suggest that we are now after the trading
 21 agreement.
 22 A. Six months later, yes.
 23 Q. The 11 June 2002 letter at tab 46 is a letter from you.
 24 Could you have a quick read through, please.
 25 (Pause)

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1 Okay, so what we see here is the same kind of letter
 2 that we saw in the First Quench file at annex 16,
 3 tab 29. Because what's happened here is that this is
 4 now the Gallaher MPI which was to take place on 25 June,
 5 and ITL decides not to follow, and so you write to
 6 T&S Stores revising the differential requirements and
 7 that the purpose of that is to ensure that no ITL brand
 8 increases as a result of the Gallaher MPI?
 9 A. I was seeking to keep our prices down and change the
 10 differentials. As part of the original trading
 11 agreement, it actually said "We can alter it if the
 12 relative RRP's change", so that's what I was doing, what
 13 the agreement said.
 14 Q. If you look at the next page {D29/40/150}, you have the
 15 revised price requirements, and here it's specified as
 16 being the price requirements post-Gallaher MPI
 17 25 June 2002.
 18 If we look at the fourth paragraph at the Superkings
 19 bit, we can see that that's changed from a "at least no
 20 more than" to "20s packings at least 6p less than the
 21 price of Berkeley", and the 100s packings at least 30p
 22 less than the price of Berkeley?
 23 A. Yes, the differentials had changed because the RRP's had
 24 changed.
 25 Q. The next document is tab 47 {D29/47/152}. This is

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1 a letter from you to the buying manager at T&S. I am
 2 interested in the bit at the bottom of the first page,
 3 moving onto the top of the -- well, moving onto the next
 4 page. But I don't mind if you read the entire letter,
 5 if that's what you would prefer.
 6 (Pause)
 7 If we just have a look at the bit on the first page
 8 headed "Retail prices", you give an explanation of this
 9 letter in paragraphs 128 and 130 of your witness
 10 statement. Perhaps the better thing to do is to go back
 11 to what you say about it. If you go back to your
 12 witness statement at 128 {C3/35/432}, and if you could
 13 just read paragraph 128 to yourself, please.
 14 (Pause)
 15 Now, in the middle of paragraph 128 you say that you
 16 had assumed that Gallaher was running a promotion with
 17 the consequence that Superkings and Raffles were more
 18 expensive than Berkeley, and you wanted Superkings and
 19 Raffles to be at the same price as or cheaper than
 20 Berkeley, so you offered a promotional bonus; okay?
 21 A. Yes, we had done, yes.
 22 Q. You see, the thing is we have just seen in the previous
 23 tab that that wasn't the case, because you had altered,
 24 or at least you had informed T&S of an alteration in the
 25 pricing requirements, because in the second page of

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1 tab 46 {D29/46/150} we have seen that what had been a --
 2 I'll describe it as a parity, but it was expressed as
 3 a "no more than", had been altered to 6p less than or
 4 30p less than, depending on whether it was 20s or 100s
 5 packings.

6 So it wasn't the case, on the basis of the strategic
 7 pricing requirements, that Superkings and Raffles were
 8 to be no more expensive than Berkeley?

9 **A.** Well, the letter you referred to, tab 46, was written
 10 prior to the Gallaher MPI being implemented, and I can
 11 only assume that, looking back at this now, Gallaher
 12 would have not implemented their MPI on those products.

13 **Q.** Yes. What happened was that the original policy set out
 14 in the trading agreement was parity in shelf prices --
 15 I fully accept that in your terminology "parity" means
 16 no more than and could be less --

17 **A.** Parity doesn't mean that, it means not more than.

18 **Q.** Not more than?

19 **A.** I don't use the word parity in my correspondence,
 20 I don't think.

21 **Q.** But the original policy was set out in the trading
 22 agreement and it was this "no more than"?

23 **A.** Correct.

24 **Q.** The next stage is that in order to prevent people moving
 25 the ITL price up as a result of the Gallaher MPI, the

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1 strategic pricing requirements are altered, and we see
 2 the alteration in tab 46?

3 **A.** That's correct, yes, because the RRP's had altered.
 4 Therefore, the differential objective had altered, yes.

5 **Q.** But then you got caught out because Gallaher had put
 6 a price hold on, so you had to countermand the notice
 7 that you gave in tab 46 which had altered the old
 8 pricing differentials in order to get back to the result
 9 that you had started off with. So that is why, in
 10 tab 47, at the bottom, you are noting that the Berkeley
 11 Superkings multipack were at 19.99, and you wanted the
 12 changes to be made in the Superkings 100s and Raffles
 13 100s multipacks, because you wanted at that stage
 14 parity. And actually what you say in this letter is:

15 "Will you change the following brands in the
 16 Supercigs tiers 1 to 4 to 19.99 with immediate effect."
 17 {D29/47/152}

18 And you don't say "19.99 or better", you don't say
 19 "19.99 or less", do you?

20 **A.** Not in this letter, no, I don't.

21 **Q.** Let's ensure that we are all agreed about this, because
 22 this is a situation where you have been using changes in
 23 the strategic pricing requirements in order to achieve
 24 a particular result in shelf prices, ITL's shelf prices,
 25 as a result of a Gallaher change. You haven't got that

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1 result because your revised strategic pricing
 2 requirements didn't reflect the Gallaher price hold, so
 3 you then had to issue another instruction to the
 4 retailers, in this case T&S, in order to ensure that
 5 they priced at the correct parity or differential, which
 6 here is expressed in your letter as a straight parity?

7 **A.** Well, I think because when the letter I wrote -- the
 8 letter that I wrote on 11 June, we were aware Gallaher's
 9 were having a price increase, and this has happened
 10 after their price increase and we have found out that
 11 Gallaher's in fact didn't increase Berkeley, or did
 12 a tactical promotion on Berkeley or did a price hold on
 13 Berkeley -- I don't know what Gallaher's did, and it's
 14 only after their MPI can then we look at what we should
 15 do as a strategy.

16 We couldn't advise before the Gallaher MPI what we
 17 were going to do because we didn't know what Gallaher's
 18 were going to do.

19 **Q.** But the point that I am making -- and I do apologise
 20 that it has not been made clearly -- is that you are in
 21 a situation in which you are having to notify T&S --
 22 and, indeed, it's not only T&S who is receiving this
 23 type of correspondence -- you have to notify them in
 24 order to prevent them from changing the ITL price
 25 pursuant to the strategic pricing requirements as

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1 a result of a Gallaher move?

2 **A.** It's completely the opposite. As I said earlier, there
 3 are instances over my years as an account manager where
 4 a retailer would, for their ease and their
 5 profitability, choose to change all prices on the same
 6 day. We were not having an MPI and we wanted to make
 7 sure our consumers got better value for longer because
 8 we weren't having an MPI.

9 Other retailers in the past have --

10 **THE CHAIRMAN:** Why did you have to give them -- perhaps you
 11 are coming to this, Mr Lasok. The following paragraph
 12 refers to having to give a retro allowance of 6p.

13 **MR HOWARD:** I think the answer is that Mr Lasok has
 14 misunderstood the letter.

15 **THE CHAIRMAN:** Well, perhaps if you can say again what
 16 your ... You are saying that in June, the 11 June letter
 17 indicates that, Mr Culham, you thought there was going
 18 to be a Gallaher MPI, which was not going to be followed
 19 immediately by an ITL MPI?

20 **A.** Correct.

21 **THE CHAIRMAN:** So you tell them the differentials are going
 22 to increase because you don't want your brand's price to
 23 go up?

24 **A.** Correct.

25 **THE CHAIRMAN:** Then it turns out -- is this right -- that --

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1 the Gallaher price doesn't actually increase?
 2 **A.** In the multipack they actually put the price down.
 3 **MR HOWARD:** That was the point. The flat price -- if I can
 4 just make it clear, because it will be a lot quicker.
 5 That's what Mr Lasok hasn't understood. If you look at
 6 the letter it's perfectly clear that what has happened
 7 is Gallaher, as well as holding the price, have reduced
 8 price, so that the same price applies across a number of
 9 tiers. And that's why then these cigarettes get priced
 10 also reduced in order to match that activity by
 11 Gallaher, and that's why there is a bonus. It's just
 12 misconstruing the letter, I am afraid.

13 **MR LASOK:** I think that there is a misconception as to what
 14 the underlying policy is, but for the Tribunal's note,
 15 one document showing the Berkeley price hold is the one
 16 at annex 27, tab 29.

17 But if you look at, for example, annex 28 --

18 **MR HOWARD:** Can I say there is not a dispute about this,
 19 it's just that two things were happening: one, Gallaher
 20 had a price hold; and two, they put down the prices in
 21 these tiers.

22 **THE CHAIRMAN:** Let's just see what was happening. I think
 23 that's what Mr Lasok is going to show us.

24 **MR LASOK:** I am going to give an example.
 25 If you have 28, and go to tab 61 {D28/61/125}, this

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1 is dated 3 July 2002, and what you see is it's a letter
 2 to Safeway. It wasn't written by you, but if you look
 3 at the fourth paragraph, there is a reference to the
 4 fact that Superkings, Berkeley and Raffles should be at
 5 the same price, at 4.10/4.13.

6 The point is simply this: that if one thinks back to
 7 the trading agreement, the trading agreement specified
 8 a price for Superkings and Raffles that was no more than
 9 the price of Berkeley. As a result of the Gallaher MPI,
 10 which altered the RRP's and which ITL was not following
 11 at that stage, ITL found it necessary to send round
 12 a letter to a number of the retailers telling them that
 13 the strategic pricing requirements had altered from
 14 a "no more than" to a differential.

15 But the problem was that that was not a change in
 16 the underlying policy. That was a change designed to
 17 prevent the retailers from altering the ITL price as
 18 a result of the Gallaher move. The underlying policy
 19 remained parity between Superkings and Raffles on the
 20 one hand and Berkeley on the other. In fact, the
 21 revised strategic price requirements were intended to
 22 achieve that parity in shelf prices, but then the
 23 complication was that there was a Gallaher price hold.

24 Then things began to get confused. But the end
 25 result here was that they write round -- here to

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1 T&S Stores -- and they seek to get parity again because,
 2 in the meantime, things have got out of line as a result
 3 of this peculiar combination of the Gallaher MPI, which
 4 is followed by a Gallaher price hold for certain brands
 5 like Berkeley, which ITL doesn't spot. So it alters the
 6 strategic pricing requirements which, in retrospect, it
 7 didn't need to do and which it, therefore, has to
 8 correct.

9 So the point about this is not about whether or not,
 10 you know, these multipacks are on a particular offer;
 11 it's about the underlying policy which remained a policy
 12 of parity.

13 **THE CHAIRMAN:** So this was not a situation, as we saw, where
 14 Richmond was repositioned in the market?

15 **MR LASOK:** No, it wasn't.

16 **THE CHAIRMAN:** The June 2002 letters were not
 17 a repositioning of Superkings to be a cheaper brand than
 18 Berkeleys, it was a temporary measure to last one didn't
 19 know how long, unless and until ITL had its own MPI to
 20 bring the price of Superkings back up?

21 **A.** We didn't have an MPI, so therefore the published RRP
 22 for Berkeley was 6p above Superkings. I think it
 23 was 6p.

24 **THE CHAIRMAN:** But if Berkeley didn't go up because of the
 25 price hold, you didn't actually want Superkings to be 6p

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1 cheaper in the long-term?

2 **A.** No, we weren't seeking that, because our published
 3 RRP -- and I don't know what it was at the time --
 4 didn't change. And the fact that Gallaher's did a price
 5 hold, tactical bonus, I don't know what --

6 **THE CHAIRMAN:** I think we are all agreed, therefore,
 7 Mr Lasok.

8 **DR SCOTT:** If one looks across at the Gallaher
 9 correspondence, there appears to have been a certain
 10 amount of confusion going on there, because what 29 says
 11 is:

12 "Is the RRP staying the same or are you bonusing
 13 back the difference to us by retro? Can't imagine that
 14 you will reprint the prices, so I expect the retro to
 15 change."

16 And back comes the response:

17 "The RRP is going up as per the price list. We will
 18 bonus back the difference. I will go through everything
 19 on Thursday."

20 **MR LASOK:** There are other Gallaher documents that make it
 21 clearer in relation to some of the other retailers,
 22 because I think in the case of, from memory, Asda and
 23 Morrisons, it's a much simpler email which sets out
 24 which brands were the subject of the price hold.

25 **THE CHAIRMAN:** Right. So let's carry on.

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1 **MR LASOK:** Looking at this letter in the second page,
 2 though --
 3 **A.** Sorry, which letter? Because I have several open.
 4 **Q.** I am terribly sorry. You can put away 28. Sorry, 29
 5 you need to have open.
 6 **THE CHAIRMAN:** We are looking at tab 47 of annex 29, page 2.
 7 **MR LASOK:** If we look at this first page again {D29/47/152},
 8 before we got to the bit about Berkeley Superkings, but
 9 immediately under the heading "Retail prices" you
 10 thanked T&S Stores for the latest price sheets and you
 11 say:
 12 "My office is currently checking to ensure the
 13 correct differentials are maintained as part of our
 14 business plan."
 15 So am I right in thinking that you were checking to
 16 ensure that the ITL prices and the Gallaher prices
 17 respected the differentials?
 18 **A.** Yes, or better than, yes.
 19 **Q.** And --
 20 **A.** And because T&S had 27 tiers it was quite a cumbersome
 21 exercise.
 22 **Q.** Yes. Then on the next page {D29/47/153} the first two
 23 lines are concerned with a change in the price of the
 24 five SKUs. Those will be the ones referred to at the
 25 bottom of the previous page, I think? (Pause)

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1 Am I right in thinking that the reference to
 2 "changing the above five SKUs to 19.99" refers to the
 3 five SKUs listed at the bottom of the first page?
 4 **A.** I certainly believe so, yes. It's to reduce the price
 5 of those, yes.
 6 **Q.** Then when we get to the second page, the next paragraph
 7 but one you say:
 8 "On a quick look I also noticed the following prices
 9 should be amended to bring Raffles into line."
 10 {D29/47/153}
 11 You refer to a meeting in May. Then you set out the
 12 prices, and so you have the One Stop tier of shops.
 13 Those were the most expensive, were they?
 14 **A.** Yes, generally.
 15 **Q.** Then you have the CTNs and the Supercigs, and the
 16 Supercigs were the cheapest, weren't they?
 17 **A.** That's correct, yes.
 18 **Q.** Then you say:
 19 "Where no price is shown, the correct differentials
 20 are already in place against Berkeley Superkings."
 21 So this is an instance of you asking them to amend
 22 the Raffles prices to bring them into line with the
 23 differentials against Berkeley?
 24 **A.** To bring them down so they are no more than Berkeley,
 25 yes.

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1 **Q.** From that point, if we go to tab 51, we get to a letter
 2 from you dated 6 August 2002 {D29/51/165}. Oh, no, it's
 3 not a letter from you, it's a letter from Nick Law. Who
 4 was Nick Law?
 5 **A.** He was an executive -- like a junior account manager in
 6 the department, and I was actually on holiday, I think,
 7 at this time.
 8 **Q.** Is this the kind of thing that he would have written on
 9 instruction from somebody?
 10 **A.** With regard to the price increase, we would have all
 11 been told there was a price increase, yes.
 12 **Q.** In fact it's a letter very, very similar to the one we
 13 saw in relation to First Quench at annex 16, tab 30.
 14 The Tribunal has seen other letters of this nature
 15 before, so this is quite common as a letter written by
 16 ITL at this time.
 17 Now, could you just read this letter, please. I am
 18 not asking you to read it out loud.
 19 (Pause)
 20 So if you just run through this letter {D29/51/165},
 21 the second heading on the first page is "Differential
 22 update", and when he talks about the ITL price increase
 23 on 2 September, he is talking about the announcement
 24 that there would be an MPI taking effect on 2 September,
 25 isn't he?

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1 **A.** There would be one taking effect on the 2nd, yes.
 2 **Q.** So he then says that he has enclosed revised
 3 differential requirements, which he describes as being:
 4 "... as part of the business plan payments."
 5 We don't have a copy of those differential
 6 requirements, but would they be the same as the ones
 7 that we saw, for example, attached to tab 46? The same
 8 nature, I should say.
 9 **A.** Yes.
 10 **Q.** That too is a letter to you, it's headed "Price increase
 11 differentials update" {D29/46/149}, and then we have on
 12 the second page a price requirements sheet.
 13 **A.** That's the one with the post-Gallaher MPI.
 14 **Q.** When we get to the letter at tab 51, which is also about
 15 a differential update, and also refers to the revised
 16 differential requirements, would there have been a sheet
 17 like the one --
 18 **A.** Similar, but obviously the figures would be different
 19 because we were having an MPI, and some of the
 20 differentials had changed.
 21 **Q.** Then he sets out a number of points that he would like
 22 to draw T&S' attention to. At the bottom of the first
 23 page there is a reference to Embassy and Regal, and this
 24 was an increase in Embassy and Regal which he says will
 25 entail -- the differential between these brands and

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1 Benson & Hedges Silk Cuts will have been reduced, and he
 2 refers the reader to the pricing requirements for the
 3 new differential positions. So that was part of the
 4 instruction to T&S as to how they were to price in
 5 accordance with the differentials?
 6 **A.** Well, it wasn't the instruction to price, it was what
 7 our -- because they set their own pricing across their
 8 27 tiers, it was to highlight what our required -- or
 9 our objective was, because I think Benson & Hedges went
 10 up 6p.
 11 So prior to the MPI our differential was for Embassy
 12 No 1 to be at least 3p less than Benson & Hedges, but at
 13 our Imperial MPI, I think -- well, it says here Embassy
 14 went up 7p, so we then altered the differential
 15 objective to be at least 2p less than Benson & Hedges.
 16 As we have said, we changed it in line with the RRP
 17 change.
 18 **Q.** If you go to the next page {D29/51/166}, there is a bit
 19 just above the first holepunch headed "Roll your own
 20 tobacco", and in the paragraph under the subheading
 21 "Golden Virginia", he says:
 22 "Please ensure that pricing differentials between
 23 Golden Virginia and Old Holborn are achieved."
 24 So that was what ITL wanted T&S to do, wasn't it?
 25 **A.** It was a reflection of the difference in the RRP,

1 because Old Holborn had gone up, and I don't know the
 2 absolute figures. For example, if it had gone up 4p,
 3 prior to the Gallaher MPI, our differential objective
 4 would have been Golden Virginia no more than
 5 Old Holborn. So if Golden Virginia didn't go up, our
 6 objective was to have Golden Virginia 4p less than
 7 Old Holborn.
 8 **Q.** Then if you look at the top of the next page
 9 {D29/51/167}, he refers to the fact that the selling
 10 price -- by which he means shelf prices, doesn't he?
 11 **A.** Well, I think it's -- the way I read that is we wouldn't
 12 be doing any price holds at our MPI, so the selling
 13 price. So we wouldn't be deferring increase, that's
 14 what I read it as, but I didn't write the letter so I
 15 don't know actually what he said.
 16 **Q.** No, but the term "selling prices" is commonly used in
 17 the correspondence to refer to shelf prices, isn't it?
 18 **A.** It has been used, yes.
 19 **Q.** So he is envisaging at any rate that the selling prices
 20 are to be adjusted in line with the amounts detailed in
 21 the price list effective 2 September, and he says:
 22 "My expectations are that Gallaher will follow suit
 23 with the price positions on those brands that were
 24 frozen post their MPI to achieve strategic pricing
 25 against ITL brands."

1 Did you work from home? I think some people did
 2 work from home.
 3 **A.** For most of the time I was the account manager, I did
 4 work from home, yes.
 5 **Q.** How often did you meet Mr Law?
 6 **A.** Well, I can't remember, because at some point Nick
 7 directly reported to me and on the other points he
 8 didn't, so I can't answer that question. When he was
 9 working directly for me, I would see him probably once a
 10 month, but when he wasn't working for me -- he was
 11 working for someone else -- I might see him three or
 12 four times a year.
 13 **Q.** I think it's been suggested by another witness that
 14 there were monthly meetings of the NAMS?
 15 **A.** Yes, but not always national account executives, and
 16 Nick was a national account executive; it was a more
 17 junior level.
 18 **Q.** I was interested in this business about Mr Law's
 19 apparent knowledge about Gallaher's strategic pricing as
 20 against ITL brands. Was that common knowledge at the
 21 level of the NAMS?
 22 **A.** Well, we didn't know what Gallaher's strategic
 23 objectives were. All he is using there was effectively
 24 they had frozen some prices post their MPI and he has
 25 used the phrase "strategic -- they have obviously set

1 some tactical bonuses or deferred the price increase, so
 2 his expectation is when our brands go up, Gallaher's
 3 would probably stop, but we don't know for definite.
 4 **Q.** Isn't he actually saying that he envisages that Gallaher
 5 is going to change its prices to achieve strategic
 6 prices against ITL brands?
 7 **A.** Well, it actually says that they have frozen post their
 8 MPI to achieve strategic pricing, so they froze their
 9 MPI to achieve it.
 10 **Q.** So he is talking about the freezing of the prices which
 11 was designed to achieve strategic pricing against ITL
 12 brands?
 13 **A.** I am saying -- I didn't write the letter, as I said
 14 earlier. In fact, Nick's wrote the letter. I was on
 15 holiday at the time. I am saying what I read it as, he
 16 is saying "were frozen post their MPI to achieve
 17 strategy pricing". So Gallaher's had an MPI, took
 18 a decision not to go up, so that was their strategic
 19 decision.
 20 **Q.** Was there any discussion in your monthly meetings about
 21 Gallaher's pricing strategy?
 22 **A.** We would only see that Gallaher's had chosen not to
 23 implement their MPIs, and so we would discuss, but there
 24 wasn't -- obviously Gallaher's had taken their decision
 25 and we just saw the results.

1 Q. And you didn't discuss amongst yourselves in any detail
 2 Gallaher's strategic pricing strategy against ITL?
 3 A. Well, this is their strategic pricing by holding their
 4 brands at an MPI. This is what this is referring to.
 5 Q. It's a strategy against ITL brands, isn't it?
 6 A. It's freezing some of their brands post their MPI.
 7 Q. Why would they have frozen some brands and not others?
 8 A. I don't know. I don't work for Gallaher.
 9 Q. All right, I'll put the question another way: If it's
 10 being said here by Mr Law that the price positions on
 11 certain brands, Gallaher brands, had been frozen by
 12 Gallaher to achieve strategic pricing against ITL
 13 brands, that implies that Mr Law had an idea (a) that
 14 that was what Gallaher was doing, and (b) he had an idea
 15 about Gallaher's pricing strategy?
 16 A. All he is saying is they took a decision to freeze their
 17 prices at their MPI, and obviously our expectation was:
 18 when we have an MPI, they may well stop their own price
 19 hold or tactical bonuses.
 20 Q. Let's take a step backwards so far as T&S is concerned.
 21 Broadly speaking, the T&S position is that, back in sort
 22 of 1996/1997, there was a trading agreement with
 23 parities and differentials expressed in fixed terms?
 24 A. There was one prior to my handling the account, yes.
 25 I think it's tab 1 in the --

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1 Q. Tab 1, with a payment for compliance?
 2 A. I haven't got the payment, but if you say so, yes.
 3 Q. At that period, ITL operated the trading agreements as
 4 movements to fixed price points, and it did it to
 5 maintain differentials?
 6 A. At that point the wording used in the trading agreements
 7 was different.
 8 Q. We can see, if we go to tab 8 in annex 29 {D29/8/29},
 9 I think part of this is, I think, boxed as confidential,
 10 but underneath what I think is boxed there is a bit that
 11 isn't confidential, and it says:
 12 "In return for the above allocation of stock,
 13 arrangements and ITL storing the pre-buy stock at no
 14 extra charge to T&S the following points are agreed ..."
 15 Then if you go to point 4, it's:
 16 "All the correct differentials as per business plan
 17 will be implemented."
 18 So this is an example of what we have called
 19 a pre-buy arrangement, which is conditional upon
 20 observance of the parities and differentials in the
 21 business plan?
 22 A. The relative price requirements. And I don't know what
 23 it was in June 99, I don't know which agreements were
 24 under -- because I think the first one that I drafted,
 25 it's in the file at tab 11.

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1 Q. Yes. This is an email that you have sent?
 2 A. Yes.
 3 Q. Then we get to a series of trading agreements, which are
 4 effective from 1 October 1999. The first one of those
 5 is at tab 11 {D29/8/34}. Have you looked at this one
 6 recently?
 7 A. Within the last week, yes.
 8 Q. Am I right in thinking that broadly speaking the trading
 9 agreements that were effective from this date were more
 10 or less in the same terms, because so far as we are
 11 concerned you had a requirement that ITL brands were to
 12 be treated no worse than equally by comparison with
 13 other manufacturers' similar products?
 14 We can get that from this trading agreement on the
 15 third page. It's the stamped page 29 {D29/8/36}.
 16 A. What I would say, though, is I don't know whether the
 17 same document was in place the year before or not,
 18 because I don't know -- I haven't got a copy.
 19 Q. I'm not sure that we have either.
 20 A. So it may have been this was the second or third or
 21 first, I don't know.
 22 Q. Then we have the requirements shown in -- the full
 23 requirements were shown in an attached listing, which is
 24 at page 32 {D29/8/39}. And we have an example of these
 25 pricing requirements that we have seen before.

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1 There was an opportunity to respond clause, we see
 2 that on page 29 {D29/8/36}, and we have seen that in the
 3 other agreement that we have been looking at.
 4 A. Yes.
 5 Q. It's the fifth paragraph on page 29, and it follows
 6 a paragraph dealing with the submission of the price
 7 sheets to ITL. Okay?
 8 A. Yes.
 9 Q. The idea was that ITL would get the price sheets from
 10 T&S, it would highlight any errors, and it was T&S that
 11 would correct the errors?
 12 A. If they chose to do so, yes.
 13 Q. Well, you say if they chose to do so, but I am rather
 14 puzzled about that, because this actually says:
 15 "T&S head office will correct any errors."
 16 A. Yes. Our expectation is we would ask them to, but we
 17 couldn't physically make them, and most of the time they
 18 would do, but they wouldn't all the time.
 19 Q. So you couldn't physically guide their pen, but the deal
 20 was that they would make the changes?
 21 A. The expectation was they would lower our prices where
 22 necessary, yes.
 23 Q. Pretty hard expectation, though, wasn't it, because it
 24 was in a contract?
 25 A. It was in the contract and discussions would take place

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1 to try and achieve that as part of our objectives.
 2 **Q.** Then you have the opportunity to respond clause, and ITL
 3 reserved its position on that because it might or might
 4 not take any action to respond to a competing
 5 manufacturer's promotional activity; that's correct?
 6 **A.** That's correct.
 7 **Q.** We still have instances of pre-buy arrangements that are
 8 conditional on observance of the differentials, because
 9 I think that if we go to tab 12, we have an example of
 10 that {D29/12/41}. (Pause)
 11 So you agree?
 12 **A.** Yes, it's there, yes.
 13 **Q.** So it's: pre-buy is subject to maintenance of the
 14 correct differentials as per the business plan?
 15 **A.** Yes.
 16 **Q.** We see examples of the differentials being applied in
 17 terms of fixed amounts. So, for example, if we go to
 18 tab 14 {D29/14/43}. (Pause)
 19 At the moment I am just looking at Richmond and
 20 Mayfair, because I think that L&B and Sovereign are ITL
 21 brands, aren't they?
 22 **A.** L&B is an Imperial brand, and Sovereign is a Gallaher
 23 brand.
 24 **Q.** Oh, I was wrong about that then. But at any rate, if,
 25 for example, we look at the second paragraph, or at

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1 least the paragraph by the first holepunch, you say that
 2 the correct price should be 3.39, the same as Mayfair.
 3 But then you suggest that a move to a different tiered
 4 price of 3.44 would still be acceptable. But that would
 5 be a move upwards of the Richmond brand, wouldn't it?
 6 You wouldn't want that?
 7 **A.** No, that should have been moved down, because they are
 8 currently 3.59, so I am trying to bring it down 20p, but
 9 accepting a reduction of 15 or 14p. So I am trying to
 10 get the price down.
 11 **Q.** Okay. Let's go to 19, tab 19 {D29/19A/63}. Perhaps the
 12 best thing is for you to read -- I am interested only in
 13 the first page -- down to the heading "Advertising and
 14 Units".
 15 (Pause)
 16 So, as I understand this, we are talking here about
 17 Day & Nite stores and the retail prices in those stores.
 18 In the second paragraph under the heading "Retail
 19 prices", you talk about bonus support, which is going to
 20 start from 3 July. And you say that there are currently
 21 no special short-term tactical bonuses on Day & Nite
 22 sales volumes, and no invoice bonuses except for the
 23 Rizla products. Then you say that you have noticed
 24 differential errors from the branch visits, and you ask
 25 T&S to arrange to correct those differential errors the

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1 following week.
 2 If we look at the differential errors, we are
 3 looking at ITL and Gallaher brands, aren't we?
 4 **A.** Yes, they are, yes.
 5 **Q.** Yeah. As I read it, what you want to do is to achieve
 6 changes in the prices of the brands in order to restore
 7 the differentials that were provided for in the trading
 8 agreement, and the trading agreement we are looking at
 9 is the one at tab 11, which has the strategic pricing
 10 requirements at the page stamped 32 {D29/11/39}.
 11 I don't know whether you want to look at that page in
 12 order to refresh your memory.
 13 (Pause)
 14 So, for example, if we look in your letter at tab 19
 15 {D29/19A/63} to the first item, which is band 3, B&H
 16 Kingsize 100s, compared with Regal Kingsize 100s, you
 17 want a change so that there is a 25p difference between
 18 the two.
 19 If we look at tab 11, we can see that in the price
 20 requirements sheet at page 32 {D29/11/39} the second
 21 item is Regal Kingsize, and for the 100s there had to be
 22 at least 25p less than the price of Benson & Hedges
 23 100s. Am I right?
 24 **A.** Yes.
 25 **Q.** You got Sovereign 100s, you refer to two possible

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1 changes. It's either altering Sovereign 100s to £18, or
 2 changing L&B 100s to £18.40.
 3 Now, if we look at the Sovereign 100s at 17.90 and
 4 look at the alternative L&B change to 18.40, that's
 5 a 50p difference. If we go back to the price
 6 requirements sheet in tab 11, and look at Lambert &
 7 Butler, it's the sixth group down, more or less in the
 8 middle of the page, you have Lambert & Butler Kingsize,
 9 Lights and Menthol and Ultra. The line below that is
 10 the 20s packing and the line below that is the 100s, and
 11 that says "No more than 50 above the price of
 12 Sovereign". So you were looking for a 50p differential.
 13 **DR SCOTT:** Sorry. Oh, I see. So what's happening here is
 14 there is an alternative being suggested.
 15 **MR LASOK:** Yes.
 16 **DR SCOTT:** So either they have to move Sovereign or they
 17 have to move L&B.
 18 **MR LASOK:** Yes, it's one or the other. You either move the
 19 ITL brand or you move the Gallaher brand, it doesn't
 20 matter, as long as the differential is restored.
 21 The third item in tab 19 is the Classic Twin, which
 22 you say was 5.44, and you ask for it to be changed to
 23 5.54, equal to Hamlet 10s.
 24 If we go back to the price sheet, the price
 25 requirements sheet in tab 11, we see just below the

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1 second holepunch "Classic, all packings, at least no
2 more than the price of the same Hamlet packing".
3 The last item is bands 1 and 3: Drum, 12.5, and you
4 wanted that changed, or at least you wanted that the
5 same as Amber Leaf. Again, if we go back to the price
6 requirements sheet in tab 11, Drum is mentioned by the
7 second holepunch, and for Drum all packings had to be at
8 least no more than the price of the same Amber Leaf
9 packing.
10 So this is a situation, isn't it, in which what has
11 happened is that T&S has not complied with its agreement
12 with you, with ITL, because its pricing has not
13 corresponded to the pricing requirements in the
14 contract, and you are drawing this to the attention of
15 T&S and asking them to make the appropriate changes,
16 whether that means a change in the price of a Gallaher
17 brand or a change in the price of an ITL brand, and
18 whether prices are going up or down?
19 **A.** The whole background to this was T&S took over
20 Day & Nite stores, which were based somewhere in the
21 northwest. When they took over the business, the
22 Day & Nite pricing policy was not in line with what T&S'
23 policy was. So T&S were moving towards integrating the
24 Day & Nite stores into T&S' own pricing policy.
25 All I am highlighting here is where stores --

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1 ie this is data from store visits, not from a price
2 file, aren't in line with what T&S head office thought
3 or wished it to be.
4 **Q.** I put it to you that that explanation is implausible,
5 because it's quite clear that you are asking them to
6 price in line with the terms of the agreement?
7 **A.** Well, I've actually asked them to -- I had noticed these
8 differential errors, so they are out of line with our
9 requirements, but they are also not in line with what
10 T&S were doing in their own stores.
11 **THE CHAIRMAN:** How do you know what they wanted to do?
12 **A.** Because the first part, this first paragraph, T&S had
13 informed me where their outline pricing was going to be,
14 and this didn't seem to be in line with what their
15 pricing policy was meant to be.
16 **DR SCOTT:** The suggested price list mentioned, is that
17 a price file that was being prepared by ITL or a price
18 file that they had prepared?
19 **A.** The background to it was Day & Nite had several --
20 I don't remember how many stores --
21 **THE CHAIRMAN:** Never mind about the background to their
22 pricing decisions.
23 **A.** The T&S buyer and myself sat down to see where they were
24 going to -- sorry. They wanted investment from Imperial
25 going forward in terms of cut price contributions and

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1 ongoing business plan. So therefore, the T&S buyer had
2 decided to put Day & Nite stores into T&S tiers, and
3 this is highlighting where it hasn't actually happened.
4 And obviously I don't know which tier they were in.
5 **MR LASOK:** Well, Mr Culham, you deal with this document in
6 paragraph 123 of your witness statement {C3/35/431}.
7 Maybe you should have a look at that. Do you have 123?
8 **A.** Yes, I have. (Pause)
9 **Q.** As I read that paragraph, you say in the second sentence
10 that your letter was pointing out certain instances
11 where the prices were out of line with the
12 differentials?
13 **A.** Yes. In the same letter, it's asking for the price
14 list, because we have had a discussion over what T&S
15 pricing was, but I hadn't actually got a copy of what
16 the T&S price file was. So in the letter of tab 19,
17 I am actually asking him to let us know what his price
18 file -- what the correct prices were.
19 **Q.** The oddity is that you talk in that second sentence of
20 certain instances where the prices of ITL's products
21 were out of line, but the very first brand that we see
22 is B&H.
23 **A.** I am just quoting that as a benchmark. The thing that's
24 out of line is the Regal Kingsize.
25 **Q.** Then you say in paragraph 123:

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1 "These were presumably errors, and therefore I asked
2 T&S to correct them."
3 So am I right in thinking that at the time when you
4 wrote your witness statement you didn't know whether
5 they were errors or not?
6 **A.** They were errors by store managers that aren't in line
7 with T&S head office policy, because this is --
8 **THE CHAIRMAN:** And that policy, as far as you were
9 concerned, was to comply with the differentials?
10 **A.** Yes. So this -- these four or five prices being quoted
11 here are what we found going into stores, and it was
12 different to what the T&S buyer had told us should be
13 seen in the stores. So that's why I am highlighting it.
14 And yes, it wasn't in line with our objective --
15 **THE CHAIRMAN:** And they had agreed with your objective, as
16 far as you were aware?
17 **A.** Yes.
18 **THE CHAIRMAN:** Maybe this is a semantic difference rather
19 than an actual difference.
20 **MR LASOK:** But it's something that sometimes one has to
21 pursue in order to get an answer.
22 Then you say:
23 "Of course it was up to T&S whether to make my
24 suggested amendments."
25 But your language isn't in that form, because what

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1 you actually say is:
 2 "Could you please arrange to correct them next
 3 week."
 4 That doesn't tend to suggest you thought it was just
 5 up to them?
 6 **A.** Well, it's a "could" and it's a "please". I think
 7 that's asking someone to do something.
 8 **Q.** It's asking somebody to do something that they were
 9 required by their trading agreement to do, isn't it?
 10 **A.** But as I stress, these are prices from stores, this
 11 wasn't T&S head office policy.
 12 **THE CHAIRMAN:** Well, we can see the letter. I think we have
 13 seen it enough times now to be able to draw our own
 14 conclusions as to what it means.
 15 **MR LASOK:** Now if we go to your paragraph 129, and I think
 16 we have looked at price sheets, but in the last sentence
 17 of 129 {C3/35/433} you say that you would generally not
 18 notify T&S of instances where ITL's products were
 19 cheaper in relative terms to competing products, but do
 20 we have an example of this here?
 21 **A.** And I have said, whilst sitting in the witness box,
 22 generally I wouldn't do it, but there are odd instances.
 23 T&S had across their business, I think, 3,000 different
 24 price points for all the different products. So yes, I
 25 have highlighted one there, yes.

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1 **Q.** But actually, you see, the reason you give here is that
 2 it's a differential error. Isn't it actually the case
 3 that you would notify T&S of divergences from the agreed
 4 parities and differentials, you would do that whether
 5 the ITL retail price was above or below the required
 6 level?
 7 **A.** Generally not. Where our price was more expensive than
 8 our objective, I would always try to highlight that.
 9 And as I've said before, there are one or two occasions
 10 or a few occasions where I've highlighted the other way
 11 round. So I accept that, but it's very, very rare.
 12 **Q.** These trading agreements were signed agreements, and ITL
 13 expected to get what it paid for, didn't it?
 14 **A.** ITL invested money in developing the business with
 15 various accounts, yes.
 16 **Q.** Wouldn't it have been improper to make payments under
 17 the contract unless you could justify the payments to
 18 your superiors and the auditors?
 19 **A.** Every single trading agreement you have to take a view
 20 on balance: is it right to pay. And most -- if we have
 21 tried to withhold money for every little instance where
 22 things didn't happen, I don't think we would get on with
 23 any customers at all.
 24 **Q.** You would have to make a business case, wouldn't you?
 25 If you had made a payment when T&S wasn't complying with

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1 the contract, you would have to go to your superiors or
 2 somebody and justify the payment?
 3 **A.** As I think I said when I was here, when payments were
 4 due, I authorised them to be paid, and then they were
 5 accounted for within our national account budget.
 6 **Q.** You couldn't just make payments to T&S Stores, could
 7 you?
 8 **A.** Sorry, I didn't write the cheque, no.
 9 **Q.** I do apologise. What I meant was in order to justify
 10 the payment, you had to be able to say to your superiors
 11 or to the auditors "Well, the contract says this, we
 12 owed them the money", or "They may not have been
 13 compliant with all the terms of the contract, but there
 14 was a justifiable commercial reason to make the
 15 payment"; it was one or the other, surely, wasn't it?
 16 **A.** I didn't have that conversation. If I felt our overall
 17 business relationship with an account, in the case of
 18 T&S, was moving in the right direction, if they didn't
 19 deliver on point 1, 2 and 3, but other things developed,
 20 I would authorise the payment and no one questioned it.
 21 **Q.** But that would be a commercial decision that you had
 22 made in the overall interest of the ongoing trading
 23 relationship?
 24 **A.** I would have taken it in the interest of Imperial
 25 Tobacco and the ongoing relationship with that customer,

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1 yes. I wouldn't penalise them for minor errors or ...
 2 **Q.** Okay. Could you turn to paragraph 141, please, and just
 3 read that to yourself, please {C3/35/435}.
 4 (Pause)
 5 You are talking about a document that is in annex 29
 6 at tab 23.
 7 (Pause)
 8 Okay? If we look at the letter at tab 23
 9 {D29/23/73}, you start off, you have the heading
 10 "Lambert & Butler and John Player Special families", and
 11 the first thing you do is, after referring to the move
 12 of Mayfair and Royals to what you describe as "normal
 13 prices", you ask T&S to implement certain price changes
 14 to L&B and JPS 20s and multipacks. Okay?
 15 **A.** Yes.
 16 **Q.** If we get to the next page {D29/23/74}, we get in the
 17 middle of the page to a heading "The Richmond family"
 18 and then you say, in relation to Richmond 20s, that:
 19 "Following the move of Dorchester planned for
 20 22 October, will you also change Richmond Kingsize 20s
 21 and Richmond Lights 20s as follows from 22 October.
 22 These prices assume Richmond will be priced no higher
 23 than Dorchester in any tier. If this is likely, please
 24 reduce the Richmond price accordingly."
 25 Now, we can see from tab 22 {D29/22/71} that these

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1 changes are moves upwards, I think, because tab 22 has
 2 a list on the first page of tab 22 starting by the
 3 second holepunch, we have a list of the agreed selling
 4 out prices divided between nine tiers and also
 5 horizontally between Supercigs, C-Stores and CTNs. And
 6 if we do a straight comparison, we can see that tab 23,
 7 page 2 {D29/23/74} is talking about movements upwards.

8 This is quite simply a straightforward instruction
 9 to T&S to price at parity, because what you want them to
 10 do is to move Richmond up on the same day as Dorchester
 11 to a price that is no higher and no lower than
 12 Dorchester?

13 **A.** It does say "no higher", but I don't think it says "no
 14 lower".

15 **Q.** You do say "if this is likely", that's to say "please
 16 reduce the Richmond price accordingly".

17 **A.** So if Richmond is higher, I would ask him to reduce it,
 18 yes.

19 **Q.** Yes, to parity with Dorchester?

20 **A.** But only if it's higher. If these prices were lower
 21 than Dorchester, I'm not -- the effect of this, we
 22 appear to have withdrawn some of our tactical funding to
 23 the equivalent of 3p a packet. So, therefore, I am
 24 advising them of that price. I don't know what price
 25 move Dorchester had, but I am just saying this is our

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1 move, and if Dorchester is going to be cheaper, can you
 2 reduce Richmond.

3 **Q.** Well, these are moves upwards.

4 **A.** Yes, that's what I said. I said that.

5 **Q.** But they are moves upwards to achieve a parity with
 6 Dorchester. They are following the Dorchester move on
 7 the same day, you don't want to go higher than
 8 Dorchester and you don't want to go lower.

9 **A.** We don't want to go higher than them, sorry.

10 **Q.** And you don't want to go lower either?

11 **A.** We'd be happy to go lower, but I don't know what the
 12 Dorchester move was.

13 **Q.** Right. Let's move to --

14 **THE CHAIRMAN:** Are we coming to an end, because we need to
 15 have a break for the --

16 **MR LASOK:** Yes, we are.

17 Could you move to tab 38 {D29/38/126}, please. We
 18 were previously, in the last letter, looking at what was
 19 in fact a prospective price move. Now, we are here
 20 looking at another one. Could you read tab 38? You
 21 comment on it at paragraphs 137 and 138 of your witness
 22 statement {C3/35/435}. So probably the best thing for
 23 you to do is to read tab 38 and then read your witness
 24 statement.

25 (Pause)

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1 In the second line of the email to you from
 2 Mr Ffello, you are told that Dorchester are going to be
 3 increasing on 4 November by 10p subject to Richmond
 4 increasing. That's what he says?

5 **A.** Yes.

6 **Q.** His email is being sent on 12 October 2001. When we
 7 look at paragraphs 137 and 138 of your witness
 8 statement, you start talking about Mayfair. Then in 138
 9 {C3/35/435}, in the third line you say:

10 "The email was from T&S, not from me. I do not know
 11 why T&S informed us that the promotion was also
 12 happening in other retailers, but we would probably have
 13 been aware of this anyway from our MTRs price checks in
 14 stores, and in view of the fact that the information
 15 concerned was publicly available."

16 Are you actually referring to the second line of the
 17 email?

18 **A.** No, I think it's referring to the Mayfair.

19 **Q.** If we look at the second line, you are being given
 20 advance notice of what Gallaher are proposing to do on
 21 4 November, and you are being given advance notice not
 22 only of the date and the Gallaher brand but also the
 23 amount of the price change. You also are being told
 24 that this is -- that's to say what Gallaher is intending
 25 to do -- subject to Richmond increasing. At the end of

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1 paragraph 137 of your witness statement, you say about
 2 this email:

3 "I replied to say that on this occasion we did not
 4 want to respond with our own promotion."

5 Did your reply also deal with the second line of the
 6 email?

7 **A.** Sorry, in what ...? I think there is a letter a bit
 8 further on. Tab 39.

9 **Q.** Okay.

10 **A.** Obviously when the email was sent I was on holiday, and
 11 then ten days later I've written a letter back to T&S.

12 **Q.** So what happens is that -- because I didn't know how you
 13 replied and I had rather assumed that you had replied by
 14 email or by telephone call.

15 **A.** As it says, I was on holiday.

16 **Q.** But the reply comes, is it in the 22 October 2001
 17 letter?

18 **A.** Yes.

19 **Q.** This is where the prices go up?

20 **A.** Well, we decide not to react to the Richmond -- sorry,
 21 the Mayfair promotion, and we have made a decision on
 22 Richmond to have a 10p increase on Kingsize and 11p on
 23 Superkings.

24 **Q.** If you go to the penultimate paragraph on the first page
 25 {D29/39/127}, you say:

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1 "These new prices will be implemented on 4 November,
2 assuming Dorchester Kingsize/Superkings is not on sale
3 at a lower price in any store/tier."
4 So you are co-ordinating a rise with Gallaher?
5 **A.** No, we have taken the decision on our pricing and we
6 hope that we won't be more expensive than Dorchester.
7 **Q.** Right. Now, so far as I can see you didn't reply to
8 Mr Fello, "I'm terribly sorry, you shouldn't be sending
9 me emails that warn me of what a competitor is going to
10 do"?
11 **A.** I don't believe I did send that email, no.
12 **Q.** Were there any other instances of this kind of
13 communication?
14 **A.** Rarely, but occasionally, you know, very rarely.
15 **Q.** It just happened from time to time?
16 **A.** Very, very rarely.
17 **Q.** How rarely?
18 **A.** Most ... I couldn't put a number. It's very unusual.
19 **Q.** Right.
20 **A.** Most of the information we find out about the pricing
21 was when we see it on a retailer's shelf.
22 **Q.** Well, I don't know, because if we go back to tab 23,
23 that's a letter dated 6 October, and you are talking
24 about, certainly on the second page, a future move in
25 price {D29/23/74}?

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1 **A.** Yes.
2 **Q.** In the middle of the page, to be absolutely precise, you
3 are talking about a move of Dorchester planned for
4 22 October. How did you discover that?
5 **A.** I would have been told by T&S.
6 **Q.** So T&S was passing information of this nature to you,
7 and that, combined with the checking of the price sheets
8 for compatibility with the differentials, enabled you
9 and Gallaher to keep the pricing in accordance with your
10 respective strategic pricing policies?
11 **A.** No, as I said, rarely we had the information, and I am
12 assuming this came from T&S rather than the Gallaher
13 price increase, I've said T&S. I don't assume -- there
14 wasn't an MPI at this time, I assume? Occasionally, we
15 would get -- I said rarely we would get -- the
16 information passed to us, yes.
17 **Q.** It boils down to this, doesn't it: what we have seen are
18 a sequence of documents in which ITL's pricing strategy
19 is oriented around maintaining relativities between ITL
20 brands and Gallaher brands, and as prices change, you
21 take steps to ensure that T&S keeps in line with the
22 agreed relativities; is that not the case?
23 **A.** We do from time to time offer tactical bonuses, we
24 withdraw tactical bonuses and we make our own decision
25 on pricing.

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1 **Q.** We are seeing a bit more than that, though, aren't we?
2 If we look at this document and 38 {D29/38/126}, we are
3 seeing movements that are not tied to tactical bonuses
4 and things like. Any changes in tactical bonuses and
5 the like is a consequence of the operation of the parity
6 and differential strategy, isn't it?
7 **A.** Well, both of these documents involved a change to our
8 tactical bonuses, so it was a tactical promotion either
9 increased or decreased.
10 **Q.** And in the case of movements downwards in price by
11 Gallaher, for example, you had the opportunity to
12 respond clause, didn't you?
13 **A.** There was, and sometimes we would respond and sometimes
14 we wouldn't.
15 **Q.** And that worked the other way around when there was
16 an ITL reduction in price?
17 **A.** I can't comment whether Gallaher's asked for that or did
18 it, I can't comment.
19 **Q.** And when Gallaher's price went up, you anticipated that
20 the ITL price would go up as a result of your own parity
21 and differential requirements?
22 **A.** No, that's not the case.
23 **Q.** But I put it to you that you did, and that was the
24 reason why we have this extremely peculiar exchange of
25 communications in about July 2002.

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1 **A.** No, was that when Gallaher's had the earlier MPI?
2 **Q.** That's when Gallaher has the earlier MPI, then you alter
3 the strategic pricing requirements.
4 **A.** We changed our pricing objectives because we hadn't had
5 an MPI and we wanted to lower cost price -- the lower
6 cost prices to still be reflected in better value on the
7 shelf.
8 **Q.** Are you tripping out something that you have learnt by
9 heart?
10 **A.** No.
11 **Q.** If an ITL price increase took place, the Gallaher
12 reaction, or rather the reaction in terms of any change
13 in Gallaher's shelf prices would depend on what
14 communication you were sending to the retailer, because
15 if you were telling the retailer "This is a widening of
16 the differentials", the expectation would be that the
17 retailer would do nothing with the Gallaher price,
18 unless Gallaher had told the retailer to do something?
19 **A.** When we had a price change we didn't tell the retailer
20 what to do with Gallaher products. It would be up to
21 Gallahers to decide.
22 **Q.** Yes, but if you didn't do that, that is to say if you
23 didn't tell the retailer that you were widening the
24 differentials, the expectation would be that the
25 retailer would do something to the Gallaher price, and

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1 it would follow suit to maintain the contractual --
2 **A.** No --
3 **Q.** -- obligation to price in accordance with the pricing
4 requirements?
5 **A.** I can't comment on behalf of Gallaher, but we certainly,
6 if we had a price increase we would not expect Gallaher
7 products to go up.
8 **Q.** So in fact what you would actually do would be to take
9 care to ensure that that wouldn't happen?
10 **THE CHAIRMAN:** I think we have been round this turf --
11 **MR LASOK:** I have no further questions.
12 **THE CHAIRMAN:** -- Mr Lasok.
13 We will take a break now for ten minutes and then we
14 will have re-examination, and I would ask you,
15 Mr Howard, to ensure that your questions in
16 re-examination do arise out of the cross-examination so
17 far as we have heard it during the course of today.
18 **MR HOWARD:** Yes. I ought to say I think my re-examination
19 is not going to be complete this evening, and I think
20 I just want to say that (a) it's quarter to 4, and we
21 are going to have ten-minute break, and there is quite
22 a lot of points I want to cover.
23 **DR SCOTT:** And I have just a couple of questions.
24 **THE CHAIRMAN:** Well, we will take a break now and consider
25 further when we get there.

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1 (3.45 pm)
2 (A short break)
3 (3.55 pm)
4 **THE CHAIRMAN:** Mr Howard, can we make clear please, that so
5 far as re-examination is concerned, where the answers
6 that Mr Culham gave in response to questions on
7 a particular document were consistent with his
8 description or explanation of that document in his
9 witness statement, we don't see the need or point in
10 going back to that to get him to say the same thing for
11 a third time.
12 **MR HOWARD:** No. I hope in my re-examinations I haven't been
13 doing that. If I have, I apologise. I certainly have
14 never intended to simply get the witness to repeat what
15 he said in his witness statement, and to repeat the
16 answer given. So that's certainly never my intention in
17 re-examination.
18 It's usually to elicit further evidence in relation
19 to matters which either haven't been dealt with and have
20 arisen in cross-examination or to clarify an issue
21 that's arisen in cross-examination.
22 **THE CHAIRMAN:** Because we would, if possible, like to be
23 able to release Mr Culham this afternoon.
24 **MR HOWARD:** I appreciate that. I do think it's unlikely we
25 will be able to achieve that. There are two accounts

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1 here. I will certainly endeavour to do it.
2 **THE CHAIRMAN:** Dr Scott has a couple of questions.
3 **MR HOWARD:** Of course.
4 Questioned by THE TRIBUNAL
5 **DR SCOTT:** The first is very straightforward. One of the
6 documents we looked at today referred -- I don't think
7 you need to look at it, but for the record it's tab 51
8 {D29/51/165} -- both to roll-your-own, RYO, and
9 make-your-own, MYO, and it's simply this: I think we
10 understand RYO, roll-your-own; what is "make-your-own"?
11 **A.** It was, we actually -- the tobacco is very similar, but
12 we actually sold the tube, so a pre-formed tube. So
13 people bought a machine, put the pre-formed tube in the
14 machine and stuffed the tobacco into it, whereas
15 a roll-your-own, you buy the paper and roll it itself.
16 **DR SCOTT:** That's very helpful. Not being a smoker,
17 I didn't understand that. Thank you very much.
18 The other point is this: was there much of a change
19 in First Quench's behaviour when Cynthia Williams
20 arrived?
21 **A.** In what context?
22 **DR SCOTT:** In terms of pricing.
23 **A.** I think she looked at the pricing model. I don't know
24 what her objectives were in terms of margin or
25 expectation for the business, but she looked at the

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1 range stocked in their business, how it was displayed,
2 and I assume the pricing. But I don't know what --
3 I can't remember how exactly what decisions took place.
4 But they were still tiered, they were still expensive
5 tiers, RRP, RRP tiers and cheaper tiers, and probably
6 about a third of the stores in each tier.
7 **DR SCOTT:** I'll explain why I asked the question. Back at
8 page 67, line 5 of today, and 68, line 2, you suggested
9 in relation to 16, tab 48 {D16/48/104} -- again, when we
10 were talking about pricing strategy -- that it wasn't
11 followed through fully and that it wasn't delivered on.
12 The reason I ask that question is that when
13 Cynthia Williams was with us, she explained that things
14 were pretty straightforward in relation to the RRP and
15 that they were either X pence up, or they were the same,
16 or they were Y pence down.
17 **A.** Yes.
18 **DR SCOTT:** And that therefore, by default, they were
19 affecting the parities and differentials set out in the
20 RRP's.
21 She thought that was all pretty straightforward,
22 really, that they did it by default. So I was just
23 trying to understand the difference between her
24 perception of what was going on and your perception of
25 what was going on.

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1 A. If everything happened correctly it would be spot on and
2 it would happen, but it never seemed to happen that way.
3 And that's why we called them errors rather than you
4 have done something deliberately wrong. It was, you
5 know, sometimes it was a retailer had deliberately taken
6 a decision on pricing, but in most cases, like using T&S
7 as an example, they had over 3,000 prices in their
8 system just for tobacco, and errors do occur.

9 The same at Thresher. If what Cynthia said about
10 starting with the RRP as the base, in theory, as our
11 differentials were nothing different to the RRP
12 difference, if that happened, then yes, it would happen.
13 But it never happened everywhere all the time.

14 **DR SCOTT:** So in essence, if all went well the P&Ds would be
15 in place?

16 A. If the retailer's strategy was straight to use the RRP
17 to then make their decision, if the retailer's strategy
18 was to say "I want to make X percentage margin" then
19 obviously that wouldn't happen.

20 **DR SCOTT:** No, I mean, her evidence was that they were
21 seeking to price in relation to the RRP.

22 A. In which case it should happen, but there again, having
23 been an account manager for many years, that's the
24 theory, but it doesn't happen in practice.

25 **DR SCOTT:** So it was still worth having an agreement to try

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1 to turn the theory into practice?

2 A. Yes.

3 **DR SCOTT:** Thank you very much, that's helpful.

4 Re-examination by MR HOWARD

5 **MR HOWARD:** I will try to limit this.

6 Mr Culham, what I want to do is to ask you some
7 questions about how the contracts here worked. But
8 I think probably the easiest way to do this is to go to
9 some examples and then see how this fits in with the way
10 the contract worked and some of the suggestions being
11 made to you.

12 Could you look at annex 29, and let's start with
13 T&S. I am just going to pick out some examples, because
14 we haven't got time to go through all the
15 correspondence. If you go to tab 16, first we see this
16 letter was dealing with Lambert & Butler {D29/16/48}.
17 Can we just focus on that for a moment. So we see that
18 Lambert & Butler is being reduced to 3.59 in August
19 tiers, and you pay a bonus for that?

20 A. That's correct, yes.

21 Q. Then what we see in respect of Richmond, in the second
22 paragraph under "Richmond", the price of 20s in all
23 Supercigs is to move to a maximum of 3.39, equal to
24 Mayfair and Royals. And then in CTNs and C-Stores, the
25 maximum price would be 3.34, with extra bonuses.

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1 So it looks as if in respect of Richmond, is this
2 right, that you are reducing the price as a result of
3 what Mayfair and Royals have done?

4 A. That's correct, we were offering tactical bonuses.

5 Q. The tactical bonus in respect of Lambert & Butler and
6 JPS, is that a counteraction to what Gallaher has done,
7 or is that you taking the lead yourselves to get a price
8 advantage?

9 A. I can't recollect exactly. My expectation is
10 probably -- was in reaction to Mayfair, to a Gallaher
11 activity.

12 Q. Okay. Insofar as, therefore, there has been Gallaher
13 activity whereby Gallaher have done something to reduce
14 here T&S to rules the price of their brands, firstly
15 were T&S entitled to reduce the retail selling price of
16 Mayfair and Royals where Gallaher reduced their
17 wholesale price?

18 A. Yes. Yes.

19 Q. Where they did this, where they reduced the price of the
20 Gallaher brands as a result of Gallaher taking action to
21 reduce their wholesale cost price, whether by bonusing
22 or otherwise, did you ever object to their having
23 a lower price or a price that didn't accord with your
24 differentials?

25 A. No, never in over 20 years as an account manager, never.

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1 Q. And you were dealing with four accounts, I think, that
2 we have looked at here?

3 A. Four that we have looked at over this case, but I've
4 dealt with 25 different accounts over the years.

5 Q. Have you ever, in relation to any of those accounts,
6 suggested to a retailer that it wasn't entitled to price
7 a Gallaher or a BAT product more advantageously or
8 disadvantageously, from your point of view, if the cost
9 price to them of that product was lower than yours?

10 A. No, never. Never, ever in over 20 years.

11 Q. What would you have expected their reaction to have been
12 if you had sought to raise that?

13 A. (a) I don't think they would have taken any notice, but
14 (b) I would never have suggested it in the first place.

15 Q. If we could go forward to tab 27. Just before we look
16 at that, having looked at that example in relation to
17 T&S, so where Gallaher reduces its wholesale price so
18 that its net wholesale price is lower than yours, and
19 the retailer you told us you regarded as entitled to
20 price it in that way, was he obliged to do anything as
21 far as you were concerned with the retail price of your
22 product?

23 A. No, because if Gallaher were, by one mean or another,
24 investing extra money into that account, all we would
25 like to have is the opportunity to respond, and some

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1 retailers would take up our response and some wouldn't.
 2 **Q.** We will come back to First Quench in a moment, but in
 3 T&S we know there is an opportunity to respond clause,
 4 it's called "explicitly stated". In First Quench we
 5 don't see an explicit statement of that clause. As far
 6 as you were concerned, was there a difference between
 7 the two situations?
 8 **A.** In general, if we saw a promotion run on, let's say,
 9 Mayfair, for example, and we saw it in store, it had
 10 happened in First Quench as an example, we would go back
 11 to First Quench and say "We would like to respond with
 12 this". But there was no obligation on them to take it.
 13 **Q.** Yes. Now, in a situation where you see -- you told us
 14 you know what the list price is of your product and you
 15 know what the list price is of Gallaher's products;
 16 that's right, isn't it?
 17 **A.** Yes, we would know the RRP's and the Q rate prices, but
 18 not the absolute net prices.
 19 **Q.** Yes. The net prices, the bulk discounts I think are on
 20 the price list. So you know that, don't you?
 21 **A.** Yes.
 22 **Q.** What you don't know is what particular bonus, as
 23 I understand it, or incentive, whatever it is, that's
 24 being paid, or a discount, however it's described, you
 25 don't know what --

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1 **A.** No. All we would know is the published Q rate price for
 2 Gallaher products and the published RRP, but nothing to
 3 do with the investments or anything like that.
 4 **Q.** Paragraph 21 I think of your statement, you told us that
 5 as far as you were concerned the objective was to ensure
 6 that your, as you perceived it, lower prices were fed
 7 through to the consumer {C3/35409}. Where the retailer
 8 prices the Gallaher -- let's take Dorchester and
 9 Richmond. If you see Dorchester on his shelf at a lower
 10 price, or let's say you see Dorchester across the market
 11 at lower prices than Richmond, what conclusion would you
 12 then draw as to the stance that Gallaher had taken
 13 vis-a-vis the net wholesale price?
 14 **A.** They would have put more investment into the account to
 15 achieve that lower shelf price, ie paid a bonus,
 16 a tactical bonus or whatever.
 17 As I say, I don't know how they arrange their
 18 payments, but one assumes a tactical bonus.
 19 **Q.** Right. If you would go to document 27 {D29/27/88},
 20 under Richmond we can see that you say:
 21 "This is to confirm that all Richmond 20s should be
 22 held at current prices until further notice. Richmond
 23 Kingsize and Superkings must not be increased on
 24 12 February when you implement the Gallaher MPI, and the
 25 retro support shown in my letter dated 10 January will

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1 continue."
 2 What were you trying to achieve here about
 3 holding -- I think you have had an MPI, so what were you
 4 trying to achieve here?
 5 **A.** What we were basically saying is to try and keep --
 6 well, to encourage the retailer not to put Richmond up,
 7 and whatever Gallaher decided to do with Dorchester, we
 8 wanted to carry on paying the bonuses on Richmond.
 9 **Q.** What I want you to then consider: if one has a situation
 10 generally where Gallaher, let's say they withdraw
 11 a bonus in a situation where you had bonused Richmond to
 12 come down to match them, if they withdraw their bonus
 13 and you don't withdraw yours, you don't say anything,
 14 you just have a bonus that's in place, what do you
 15 expect the retailer to do to the price of your Richmond
 16 brand?
 17 **A.** We would expect them to keep the price of Richmond at
 18 the lower price and pass on the bonus that we are paying
 19 them.
 20 **Q.** Right. Where Gallaher has an MPI, as you are referring
 21 to here, do you have any requirement as to where
 22 Gallaher has an MPI what they should do to your brand?
 23 **A.** Not at all, no. If Gallahers had an MPI, that's their
 24 choice and nothing to do with our brands.
 25 **Q.** Could we perhaps just switch to First Quench for

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1 a moment, annex 16, please. If you go to tab 5, some of
 2 these documents are before your time, but I just want to
 3 see how the First Quench was operating {D16/5/8}. One
 4 sees at paragraph 2 that:
 5 "When Dorchester is increased by 5p per 20, expected
 6 soon, please leave Richmond price unaltered, thereby
 7 matching the Dorchester price".
 8 Right? So it appears that at that stage Dorchester
 9 was 5p cheaper than Richmond?
 10 **A.** That's correct, yes.
 11 **Q.** So in relation to First Quench, in a situation where
 12 Gallaher had managed to reduce the price of Dorchester,
 13 whether by bonusing or otherwise to get it 5p below
 14 Richmond, what, as you understand it, was First Quench
 15 required to do vis-a-vis Richmond if you didn't
 16 yourselves bonus Richmond down?
 17 **A.** I think the background to this, this was at the time
 18 when we changed the retail price of Richmond and were
 19 seeking to bring the price down of Richmond across the
 20 market.
 21 **Q.** Right.
 22 **A.** First Quench chose not to bring Richmond down to the
 23 price that we would like to have achieved, as low as we
 24 wanted, and decided to keep Dorchester 5p cheaper than
 25 Richmond.

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1 Q. Right. Was that as a result of a Gallaher price cut, or
 2 you don't know?
 3 A. I don't know the reason why, but there is a letter
 4 further in the folder where the buyer is not wishing to
 5 accept our lower price on Richmond.
 6 Q. Right. That sort of point, where they decide they don't
 7 want to accept the lower price on Richmond, were they
 8 free to do that?
 9 A. Yes.
 10 Q. Was that something you experienced yourself on these
 11 accounts?
 12 A. There are occasions -- there is a couple of occasions
 13 with T&S not accepting tactical bonuses on products in
 14 these folders. I wouldn't say it was common, but yes,
 15 it did happen from time to time.
 16 Q. Right. Would you go to document 11. One sees on the
 17 second page {D16/11/29} that on 29 January onwards the
 18 Richmond price was to be held -- sorry, this is in the
 19 context of an MPI -- at £3.34, no increase of 5p at MPI,
 20 [REDACTED] per thousand bonus.
 21 Now, where in relation to this account,
 22 First Quench, one held the Richmond price, if Gallaher
 23 had their own MPI and put up their price, what then was
 24 to happen to your price?
 25 A. We were maintaining this price until further notice.

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1 Q. Okay. You were asked some questions by Mr Lasok
 2 concerning the situation where -- what we have been
 3 looking at the moment are situations where Gallaher has
 4 a lower wholesale price and a lower shelf price.
 5 Mr Lasok asked you some questions to the effect that:
 6 suppose actually Imperial has a lower wholesale price,
 7 and how the agreement is to operate. I think what
 8 Mr Lasok was suggesting to you was that the retailer,
 9 where you have a lower wholesale price, has to --
 10 a lower wholesale price than Gallaher -- price your
 11 product at the same level as Gallaher, and therefore
 12 cannot pass through to the consumer --
 13 MR LASOK: No, that's not actually what I said.
 14 MR HOWARD: That is what you said, but anyway, let me go
 15 back.
 16 What Mr Lasok, as I understood it, was suggesting
 17 was that where Imperial has a lower wholesale price, his
 18 suggestion was: if one has a fixed relationship, the
 19 retailer will not pass through the lower retail price,
 20 the lower wholesale price of Imperial through to the
 21 consumer, because he can charge both the Imperial
 22 product and the Gallaher product at the higher price and
 23 still be maintaining the differential.
 24 Now, what I wanted to ask you is, firstly, you dealt
 25 with these four accounts. Insofar as you had

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1 a differential policy, you have told us that as far as
 2 you were concerned in these accounts it was always
 3 a "not more than" policy, ie not more expensive than.
 4 How would the retailers who you dealt with have
 5 understood the position, as far as you were aware?
 6 A. In the case of -- using Richmond and Dorchester, we
 7 wouldn't want Richmond to be higher, but they were free
 8 to set it lower. And there is examples with T&S where
 9 they have chosen to sell Lambert & Butler cheaper on
 10 their own promotions.
 11 Q. What was the reason for -- for instance, if we take
 12 Richmond and Dorchester -- the strategy, as far as you
 13 understood it?
 14 A. Consumers viewed those products as equally acceptable.
 15 Therefore, if both products were on the shelf, consumers
 16 might switch between those two. So, therefore, if our
 17 brand was either cheaper or the same price, we would
 18 have the opportunity to get more consumers buy our
 19 product. If our product was dearer, then consumers
 20 might choose the Gallaher product, because the products
 21 were very similar.
 22 Q. You have already told me that where Gallaher's net
 23 wholesale price was lower than yours, as far as you were
 24 concerned the retailer could represent that in a lower
 25 shelf price and you would have to compete.

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1 Now, conversely, if your net wholesale price to the
 2 retailer was lower than Gallaher's, to what extent was
 3 the retailer entitled to reflect your lower wholesale
 4 price in his shelf price?
 5 A. We would have hoped that they would have sold it for
 6 a cheaper price to consumers.
 7 Q. Sorry, say that again?
 8 A. We would hope they would have sold it at a cheaper price
 9 to consumers.
 10 Q. Right.
 11 THE CHAIRMAN: But they could still fulfil the terms of the
 12 agreement by charging the same price?
 13 A. Yes.
 14 DR SCOTT: Just now when we were looking at tab 11, I think
 15 we got into a confusion about who was doing what,
 16 because 29 January 2001 was actually an ITL MPI, not
 17 a Gallaher one, and what it says is:
 18 "29 January onwards until further notice, Richmond
 19 price held at 3.34", which is, as far as I can see
 20 an absolute number, "no increase of 5p at MPI", that was
 21 what had been announced in the ITL MPI, and the Gallaher
 22 MPI doesn't follow until February. So it looks as
 23 though this is actually ITL doing a hold down.
 24 MR HOWARD: Exactly. Let's just clarify the position.
 25 What is the reason for doing a hold? Why do you

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1 want to do a hold? What's the purpose?
 2 **A.** To keep our shelf price lower and not more than
 3 Dorchester in this case. So we didn't want the
 4 retailers to put our prices up, our shelves, because we
 5 might lose more consumers. Therefore, we would offer
 6 a tactical bonus in this case to encourage them not to
 7 put the prices up.
 8 **Q.** You see, why do that? Why have a price hold if,
 9 whenever you put up your prices, the retailer has to put
 10 up the Gallaher price? Why would you need to do that?
 11 **A.** If that was what happened, we wouldn't need to do it.
 12 **Q.** Yes. Was it? Was that your expectation, that whenever
 13 you put up your price, the retailer had to put up the
 14 price of the Gallaher product?
 15 **A.** Never, no.
 16 **THE CHAIRMAN:** But was what was happening here that in your
 17 MPI you were publishing an intention, all being well, to
 18 put Richmond up and then you held it so that it didn't
 19 go up at the time, and then you wait and see how
 20 Gallaher react? And would it be likely that if they
 21 react by putting up, or announcing that they are going
 22 to put up Dorchester by the same amount, you might then
 23 release the price hold and put up Richmond? Whereas if
 24 Gallaher don't announce a Dorchester increase, you might
 25 have to hold the Richmond price for longer?

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1 **A.** That's possible. And obviously this is a month --
 2 almost a month after -- so we actually had a price
 3 increase. Doing it this way actually cost the company
 4 more money, because we have to pay the ad valorem tax,
 5 so ...
 6 **MR SUMMERS:** May I just ask: when you did your annual
 7 budget, did you budget for price increases in certain
 8 months of the year?
 9 **A.** I didn't, no.
 10 **MR SUMMERS:** You never budgeted for the impact of a price
 11 increase --
 12 **A.** No.
 13 **MR SUMMERS:** -- in assessing what revenue you were likely
 14 to --
 15 **A.** No.
 16 **MR SUMMERS:** Thank you.
 17 **MR HOWARD:** Could you just go back to tab 7 in the
 18 First Quench file. I just want to actually understand
 19 how First Quench operated, because I think you were
 20 asked various questions about the agreements throughout
 21 the period. Let's look at the first one. If you go to
 22 paragraph 3 on the second page {D16/7/12}, you say that:
 23 "The bonus levels shown above will only be paid if
 24 existing levels of pricing and percentage of branches
 25 within each Pricing Tier are maintained."

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1 Then:
 2 "A proportional reduction if there is movement of
 3 prices in any tier relative to RRP to a more expensive
 4 tier.
 5 "The transfer of branches to a more expensive tier."
 6 Then the writer set out the six tiers, and we can
 7 see that they are basically the most expensive tier is
 8 at RRP and then going down, as you go through the tiers,
 9 with slightly different pricing on different brands.
 10 Now, if First Quench priced in accordance with
 11 what's set out here, would they be complying with what
 12 ITL was expecting?
 13 **A.** Well, that -- these were the prices that they had told
 14 us, and if all brands in those tiers -- well, we don't
 15 know what the Gallaher brands' minuses were, because
 16 it's different across our brand portfolio, so I can't
 17 comment, but one would hope they would be, because if
 18 they are starting from the RRP and then taking
 19 a discount from that, in all probability it would be in
 20 line with the difference in the RRP's across the range.
 21 **Q.** Right. If you go forward to tab 20, on the next page --
 22 not the manuscript page, the second page in -- we have
 23 the letter of 19 October. You see what's in the bottom
 24 right-hand corner, if you go to page 3 of 6, and you see
 25 the pricing says:

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1 "To ensure ITL's strategies are achieved both in
 2 actual levels and differentials measured against
 3 Gallaher competing brands, pay bonus only in price
 4 competitive tiers."
 5 I think Mr Lasok didn't ask you what that meant,
 6 "pay bonus only in price competitive tiers"?
 7 **A.** It was only on the tiers that were selling our brands
 8 below the RRP, and that's why over the years we moved
 9 from paying 100 per cent of the bonus to only
 10 30 per cent of stores received the bonus.
 11 **Q.** In fact we see the bonus in this one, if you go back to
 12 page 1 of 6, the bonus under paragraph 1 was [redacted],
 13 and so we see from the text below that the payment there
 14 was being paid on all volumes, even though 55 per cent
 15 at this stage were sold at RRP and above.
 16 So when we read then on page 3 of 6 "pay bonus only
 17 in price competitive tiers", just explain that to me
 18 again, how that fits together?
 19 **A.** The previous agreement, which is the one that's on
 20 page 1 of 6, the bonus was paid on all volume, but
 21 because First Quench had chosen to put their prices up
 22 across the board, the "price competitive" statement is
 23 we were only going to pay the bonus in those stores that
 24 sold below RRP.
 25 **Q.** Right. So when we then come forward to tab 44(a), and

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1 you go to what is page 20 of this document, the business
 2 development plan, the bit that somebody has put in
 3 a box:
 4 "Price support bonus money is now paid on only
 5 30 per cent of volume. This is as a result of only this
 6 percentage now being sold below RRP."
 7 I think also if you go to page 23 under "Pricing",
 8 we get the references to three tiers. Then, after the
 9 tiers:
 10 "These percentages vary somewhat between brands.
 11 They should be monitored given the fact the trading
 12 agreement pays on 30 per cent of volume sold at below
 13 RRP."
 14 So by this stage, what is it that Imperial is going
 15 to pay a bonus on?
 16 **A.** Only on the volume that is sold in stores when our
 17 selling price is below RRP, which was about a third of
 18 their volume.
 19 **Q.** Right. In relation to the differentials, so where they
 20 are selling below RRP, how were they to treat -- in the
 21 RRP discount, how were they to treat you and Gallaher as
 22 far as you were concerned?
 23 **A.** We were seeking them to not treat us worse than the
 24 compet -- I don't know what Gallaher's were seeking, so
 25 if in the case of Benson & Hedges and Embassy No 1, we

1 would hope they would have Embassy No 1 3p below
 2 Benson & Hedges.
 3 **Q.** If we go to tab 48, which is the final trading
 4 agreement, you have already explained to us that they
 5 had these tiers and only 30 per cent of volumes are
 6 being sold in the low tier, which is below RRP. In
 7 relation to the higher tiers, were they being paid
 8 anything in order to achieve your strategy?
 9 **A.** No, not a penny.
 10 **Q.** In the higher tiers, if they -- for instance, let's say
 11 in the tiers where they are pricing above RRP, the
 12 premium tier, if they priced Embassy at the same price
 13 as Benson & Hedges, rather than at a 3p differential or
 14 minimum 3p differential, would you, as far as you were
 15 concerned, have any complaint about that? Was it
 16 anything to do with the agreement?
 17 **A.** There was nothing in the contract. I might try and ask
 18 them to reduce Embassy, but there was no -- because the
 19 bonus or the investment we made was based on the cut
 20 price tiers only.
 21 **Q.** Right. You were asked some questions about a letter
 22 that Mr Byas wrote. Just before we get to that, could
 23 I ask you to be given annex -- no, let's perhaps, in
 24 view of the time, move on.
 25 Actually, could you take annex 13, please. If you

1 go to tab 7, this is a pricing sheet.
 2 **A.** Sorry, did you say tab 7?
 3 **Q.** 7(a), I am sorry.
 4 **A.** I have nothing in there.
 5 **Q.** Oh, have you not?
 6 **THE CHAIRMAN:** We have two volumes of annex 13.
 7 **MR HOWARD:** Let's put it away, it doesn't really matter, he
 8 can deal with it without seeing the document.
 9 **A.** It would be the big A, is it?
 10 **Q.** It doesn't matter, let's go to tab 46. Sorry, I am
 11 trying to do it quickly and I am jumping around. I am
 12 saying put away the other one and go to the First Quench
 13 annex 16. I apologise. I will be able to finish,
 14 I think.
 15 Tab 46, the letter that we have looked at several
 16 times today. You have told us that, in respect of
 17 cigars, certain cigars, that it was never Imperial's
 18 strategy to have them priced at the same level as
 19 Gallaher cigars?
 20 **A.** Panama, in my recollection, was always cheaper than
 21 Hamlet, in an RRP, yes.
 22 **Q.** The document I was going to show you is just
 23 a differential sheet at this time which shows precisely
 24 that.
 25 Assuming that was the strategy, did the pricing

1 strategy differ according to whether one was dealing
 2 with First Quench or somebody else in the market as to
 3 the relative price positioning?
 4 **A.** We would try and achieve the same objectives across the
 5 retail market.
 6 **Q.** Would Mr Byas have authority to agree a different
 7 pricing strategy?
 8 **A.** No.
 9 **Q.** If we look at tab 46, what was being suggested to you
 10 about tab 46 is that -- and I think the same point was
 11 being made in relation to tab 49 -- the reference here
 12 to "parity" must mean that all cigars were to be priced
 13 at the same level. I think you told us that that simply
 14 doesn't represent ITL's strategy, so you had some
 15 difficulty understanding that?
 16 **A.** It doesn't represent the strategy at all.
 17 **Q.** I want to see whether an alternative construction of the
 18 sentence would then fit in with ITL's strategy, as you
 19 understood it. You are obviously not the author of the
 20 letter, Mr Byas is, but if what was being referred to
 21 here by "parity", "achieve parity for ITL and Gallaher
 22 brands", what he was trying to convey was at the same
 23 RRP differentials in the different tiers, would that
 24 accord with ITL's strategy?
 25 **A.** I don't think so, because the brands, the three tiers

1 that First Quench were operating on was a different
 2 issue over Panama being the same price as Hamlet. So
 3 if ... I don't know, obviously I wasn't -- I didn't
 4 write this letter, but parity for cigars, if it was the
 5 same across all the tiers, that wouldn't be in line with
 6 our strategy. If it was different parities in different
 7 tiers, it still wouldn't be in line with our strategy.
 8 So in no way would this fit in with what we were -- my
 9 objective was or our objective was as a business.
 10 **Q.** My question was: if what he was trying to convey was
 11 that you should treat them equally in the sense of
 12 applying the same -- either price them at RRP or RRP
 13 plus or RRP minus, in other words keep them in the same
 14 relativity to the RRP's?
 15 **A.** If he had said that and that's what First Quench were
 16 doing, that would have achieved our objective, yes.
 17 **Q.** Now, then on the final point on that correspondence,
 18 tab 49 we see is an example of there being a Panama
 19 bonus, so what appears to have happened is that the
 20 price of Panama has been reduced by Imperial by a bonus.
 21 Where that happened, in other words where Imperial seems
 22 to have gone first, taking steps to reduce the price of
 23 Panama, what would be the purpose of that?
 24 **A.** Why we were offering a bonus?
 25 **Q.** Mm.

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1 **A.** To achieve a lower shelf price for Panama.
 2 **Q.** Lower shelf price, right. Where you have done that,
 3 what would you expect them to do to the competing
 4 brands?
 5 **A.** Nothing at all to the competing brand. Only we would
 6 offer the tactical bonus to achieve a lower shelf price
 7 for our products, but it wouldn't have any impact on any
 8 other product.
 9 **Q.** Could we then close for good First Quench, and just go
 10 back to the T&S account in annex 29. {D29/46/149} If
 11 you go to tab 46, this is the 11 June, summer 2002
 12 episode. What's happened is Gallaher announces its
 13 price increase, we see that, and so Gallaher's prices
 14 are due to go up.
 15 Now, if we take it in stages: firstly, if you hadn't
 16 written this letter to Mr Lyons on 11 June, and you
 17 hadn't had an MPI but Gallaher had, firstly do you have
 18 any requirement as to what he should do to your brands
 19 under your contract?
 20 **A.** Sorry, if Gallaher's have had an MPI?
 21 **Q.** Yes. It's this situation: if you hadn't written this
 22 letter, what did you require Mr Lyons to do with your
 23 brands?
 24 **A.** Do nothing, keep the prices down.
 25 **Q.** Right. What was the purpose of the letter in the light

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1 of that?
 2 **A.** It was a reminder effectively that our prices were not
 3 going up and highlighting the effect that would have on
 4 the differentials.
 5 **Q.** Right.
 6 Can I then ask you about tab 47, {D29/47/152}
 7 Mr Lasok was suggesting to you that this was, I think,
 8 countermanding the widening of the differentials.
 9 I just want to actually understand what happened. If
 10 you look under "Retail prices", you will see you wrote:
 11 "I have noticed you have a flat price on Berkeley
 12 Superkings multipack at 19.99."
 13 Then you ask him to change the following brands in
 14 the Supercigs tiers 1 to 4. Similarly, if you go over
 15 the page, you note that you have also introduced a flat
 16 price on Berkeley multipacks in all the CTN stores.
 17 Explain to me what this reference is to the flat
 18 price and its relevance in relation to tiers 1 to 4;
 19 what's going on here, as you understand it?
 20 **A.** Both -- in Supercigs they would have had nine tiers, and
 21 in tiers 5 to 9 they wouldn't have been at 19.99.
 22 I don't know what price they would have been at, but
 23 normally, under T&S' normal policy, Berkeley would have
 24 been higher than 19.99 in tiers 1 to 4, so we have
 25 noticed that our brand has become more expensive, and

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1 are therefore offering a tactical bonus to bring our
 2 brand down.
 3 **Q.** So I think it was being suggested to you this letter was
 4 just about the response to the Gallaher price hold. But
 5 what have Gallaher actually done, as far as you
 6 understood it at this time, in order to get Berkeley
 7 Superkings and the other Berkeleys at this price across
 8 a number of the tiers?
 9 **A.** Well, they would have (a) paid a bonus to counteract the
 10 effect of their MPI, and secondly added an extra bonus
 11 to bring this flat pricing in, because otherwise
 12 Berkeley would have been higher.
 13 **Q.** So what are you doing and how do you have to pay for it?
 14 **A.** By fully funding the reduction from their, T&S', natural
 15 price in tiers 1 to 4 down to 19.99.
 16 **Q.** Did you at any stage say to Mr Lyons "Well, you are
 17 simply not entitled to do this, you can't reduce the
 18 price of Berkeley, we can't have that"?
 19 **A.** No, not to Mr Lyons or anyone else was it ever said.
 20 **MR HOWARD:** I think we are probably only to go over more
 21 similar correspondence, and I think you have the
 22 picture, so I'll stop there.
 23 **THE CHAIRMAN:** Thank you very much, Mr Howard.
 24 Thank you very much, Mr Culham. This is positively
 25 your last appearance, Frank Sinatra like, before

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1 the Tribunal. So thank you again for attending and for
 2 your evidence. I realise it's been a long day, but
 3 thank you, that's been very helpful, and I can now
 4 release you from the witness box.
 5 **A.** Thank you.
 6 (The witness withdrew)
 7 **THE CHAIRMAN:** Tomorrow morning we will start at 10.30 with
 8 you briefly, Mr Lasok, and then Mr Wragg.
 9 I don't know whether you will have a chance to
 10 discuss with Mr Howard or anyone else what you plan to
 11 say tomorrow. Clearly it will take up less time if you
 12 have been able to discuss it amongst yourselves, but
 13 that may be impractical.
 14 **MR LASOK:** Yes.
 15 **THE CHAIRMAN:** Good. We will meet again, then, at 10.30.
 16 **MR HOWARD:** Sorry, could I be impertinent just to raise one
 17 timetabling question?
 18 **THE CHAIRMAN:** Yes.
 19 **MR HOWARD:** Sorry to do that, but I am concerned about this
 20 question of experts, and I asked Mr Lasok, and he says
 21 his estimate -- or whoever is doing it on their side --
 22 is still five days. The reason I'm simply raising the
 23 is question is whether or not there is any possibility
 24 of the Tribunal being available on one of those
 25 non-sitting days in the next two weeks, or whether we

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1 should be scheduling the day in the following week, or
 2 whether you say: no, it's all got to be done in four
 3 days and four days.
 4 **THE CHAIRMAN:** I thought yesterday we asked to see
 5 a breakdown of what the timetabling was for those weeks
 6 in relation to the eight days, as a useful first step to
 7 considering this.
 8 **MR HOWARD:** You did.
 9 **THE CHAIRMAN:** But we will also overnight look at the two
 10 non-sitting days in those weeks and see if there is any
 11 possibility even of sitting an extra half day. We will
 12 check that out. Thank you.
 13 (4.45 pm)
 14 (The court adjourned until 10.30 am on
 15 Thursday, 3 November 2011)
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