Neutral citation [2011] CAT 41

IN THE COMPETITION
APPEAL TRIBUNAL

Cases No: 1160/1/1/10
1161/1/1/10
1162/1/1/10
1163/1/1/10
1164/1/1/10
1165/1/1/10

Victoria House
Bloomsbury Place
London WC1A 2EB

12 December 2011

Before:

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

Sitting as a Tribunal in England and Wales

B E T W E E N :

(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 SUPERMARKETS 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 U.K. LIMITED
(2) SHELL U.K. OIL PRODUCTS LIMITED
(3) SHELL HOLDINGS (U.K.) LIMITED

Appellants

- v -

OFFICE OF FAIR TRADING

Respondent

Heard at Victoria House on 21, 22, 26, 27, 28, 30 September, 4, 5, 6, 7, 10, 11, 13, 14, 18, 19, 20, 21, 25, 26, 27, 28, 31 October, 1, 2, 3, 11, 17 and 18 November 2011

JUDGMENT

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.

Adam Aldred (of Addleshaw Goddard LLP) appeared on behalf of the Interveners, J. Sainsbury plc and Sainsbury's Supermarkets Limited.

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.

INTRODUCTION

1. We have been asked to rule on whether the hearing of these appeals should now be brought to an end by the Tribunal setting aside the decision which these appellants have challenged. That decision, issued by the OFT on 15 April 2010 ("the Decision"), found that the two main manufacturers of tobacco products in the United Kingdom, Imperial and Gallaher, had each entered into a series of bilateral agreements with 10 different retailers relating to the pricing of tobacco products in those retailers' stores. The Decision found that these agreements had as their object the prevention, restriction or distortion of competition in the United Kingdom and were thus infringements of the prohibition set out in section 2(1) of the Competition Act 1998 ("the Chapter 1 prohibition").

2. For the reasons we set out below our unanimous decision is that these appeals should be allowed and the Decision quashed forthwith, so far as it concerns these appellants.

3. Attached to this judgment is a glossary of terms that are used in this judgment. When we refer in this judgment to 'agreements' or to 'requirements' or 'restraints' which have been 'imposed' on the retailers, we use those terms to encompass arrangements, incentives or expectations of a kind which are capable, according to the case law, of constituting agreements or concerted practices for the purposes of the competition rules. More generally, we should make it clear that this judgment does not address any of the substantive issues raised in these appeals. We have not come to any view as to whether the agreements described in the Decision or the restraints that the OFT now alleges were entered into would, if proven, amount to infringements of the Chapter 1 prohibition.

4. We are handing down this judgment following the adjournment of the main hearing on 3 November 2011. That was Day 26 of a hearing scheduled to last until 21 December 2011. To understand why we are now bringing these appeals to an end without being in a position to decide the many important legal and factual issues they raise, it is necessary to explain in some detail what has happened.

The investigation and the OFT's Decision

5. The investigation which led to the Decision was triggered in March 2003 by an application for leniency made by Sainsbury under the OFT's leniency programme applicable at that time.[1] During the course of the investigation, the OFT sent out over 30 notices requesting documents and information. The statement of objections was issued by the OFT in April 2008 and sent to thirteen parties suspected of engaging in the infringements. Six addressees of the statement of objections entered into early resolution agreements with the OFT in which each of them admitted liability for infringements alleged against them and agreed to pay a fine which, according to the OFT, reflected a significant reduction in the fine that might otherwise have been imposed.

6. Following the parties' responses to the statement of objections, the OFT concluded that the evidence was insufficient to support a finding of infringement in respect of some of the matters that had been alleged. In particular, the statement of objections had alleged that the agreements had both an anti-competitive object and effect. The OFT decided at that stage to proceed with the investigation as an 'object' infringement case only.

7. The Decision was adopted as we have said on 15 April 2010. What follows is necessarily only a summary of a lengthy and complex document. The Decision found that each of the two tobacco manufacturers regarded its brands as being pitted against particular competing brands sold by the other manufacturer. For example, for much of the period covered by the Decision Imperial regarded its Richmond brand of cigarettes as competing primarily against Gallaher's Dorchester brand of cigarettes. Imperial also regarded its Drum brand of roll-your-own tobacco as competing primarily against Gallaher's Amber Leaf tobacco. The OFT found that each manufacturer had entered into an agreement with each of 10 retailers under which the retailer agreed to set its shelf prices in accordance with set parity and differential requirements in relation to the named competing brands of cigarettes and other tobacco products.

[1] As set out in Part 3 of the Director General of Fair Trading's Guidance as to the Appropriate Amount of a Penalty OFT 423 (March 2000): see paragraph 2.92 of the Decision.

8. The Decision found that the terms of the agreements between the manufacturers and the retailers could be derived from a number of sources or factual elements. First, there were the manufacturers' respective internal pricing strategies as to which of their own brands should be linked with which competing brands. Secondly, there were in many instances written trading agreements signed by the manufacturer and the retailer. These incorporated provisions for the payment of bonuses or discounts in return for the retailer abiding by various obligations, including parity and differential requirements, often set out in a schedule to the agreement. The schedule expressed the requirements as being, say, that a particular Imperial brand be sold at a price "not more expensive than", "at least 5 pence less than" or "not more than 3 pence more expensive than" the competing linked Gallaher brand. Thirdly, the OFT found that the infringements were evidenced by the manufacturers paying or withdrawing ad hoc or temporary promotional bonuses designed, the OFT found, to encourage the retailer to bring its shelf prices into line with the desired parity and differential requirements. Fourthly, the OFT cited contacts between the manufacturers and the retailers in which there was detailed discussion of, amongst other things, the shelf prices at which the retailer would sell that manufacturer's brands or, in some cases, the competitor's brands. Fifthly, the OFT pointed to the fact that the manufacturers sent their representatives to the retailers' stores to monitor prices and wrote to the retailer pointing out where prices appeared to be out of line with what had been agreed. The OFT noted that it had not found that each of these five elements was present in each of the 20 bilateral agreements condemned in the Decision but held that it was not necessary for all the elements to be present for a breach of the Chapter 1 prohibition to be found: see paragraph 6.16 of the Decision.

9. The Decision dealt with each of the bilateral relationships separately but used broadly the same wording to describe the infringement in each case. For example, as regards the agreements between Imperial (referred to as 'ITL' in the Decision) and Asda the OFT found:

> "6.389… ITL and Asda were party to an agreement … (the 'Infringing Agreement') whereby ITL coordinated with Asda the setting of Asda's retail prices for tobacco products in order to achieve the parity and differential requirements between competing linked brands that were set by ITL in pursuit of ITL's retail pricing strategy. The Infringing Agreement had the object of restricting

> competition in the manner set out in Section 6.A.1 …and amounted to a breach of the Chapter I Prohibition."

10. The term "Infringing Agreements" was also defined in the glossary of the Decision as:

> "the agreements and/or concerted practices between each Manufacturer and each Retailer whereby the Retailer would apply retail pricing relativities between competing tobacco brands required by the Manufacturer…"

11. The manner in which the OFT found that the Infringing Agreements restricted competition was described in paragraphs 6.213 onwards of the Decision (footnotes omitted):

> "6.213 … If a parity or fixed differential requirement is implemented, an increase or reduction in the retail price of one brand leads to a corresponding increase or reduction in the retail price of the competing linked brand by an equivalent amount.
>
> 6.214 A parity or fixed differential requirement is capable of giving rise to significantly increased certainty for a manufacturer imposing the requirement (in this hypothetical scenario, manufacturer A) that any change in the retail price of its brand, brand X, will be matched by a corresponding change in the retail price of the linked, competing brand, brand Y.
>
> 6.215 In the absence of a parity or differential requirement, manufacturer A can expect that if it raises the wholesale price of its brand X, the retail price of that brand will increase relative to the competing brand Y, assuming that other factors remain constant. As a result, it will expect to suffer a loss of sales volume as consumers switch to the relatively cheaper, competing brand Y of manufacturer B. Conversely, manufacturer A would expect that if it lowers the wholesale price of its brand X, the retail price of that brand will decrease relative to that of competing brand Y, assuming that other factors remain constant, and it will enjoy an increase in sales volume as consumers switch away from the relatively more expensive competing brand.
>
> 6.216 In contrast, if manufacturer A has a requirement that a retailer's price for brand X is linked to the retail price of competing brand Y by virtue of a required parity or fixed differential, that requirement is capable of giving rise to a significant degree of certainty that the retail prices of the two competing, linked brands will move in parallel. The loss in sales volume that manufacturer A would normally expect to suffer by increasing its wholesale price - as a result of an adverse shift in its retail price relative to that of the competing brand - is therefore significantly reduced by virtue of the retail prices for both brands increasing in parallel. As a result, manufacturer A would enjoy the gain in revenue from increasing its wholesale price without suffering the loss in sales volume that would normally result from its brand having a more expensive retail price relative to that of the competing brand Y.
>
> 6.217 Similarly, a manufacturer which does not operate a parity and differential strategy (manufacturer B) would observe, over time, that any change in the retail price of its brand, brand Y, is very likely to be matched by a corresponding change of the same magnitude in the price of the competing, linked brand X and infer the

existence of a relationship between the retail price of its brand Y and the price of the competing brand. In that situation, manufacturer B's incentive to reduce its wholesale price is capable of being significantly reduced by manufacturer A's parity or differential requirement. That is because manufacturer B would suffer the loss in revenue from reducing its wholesale price without enjoying the gain in sales volume that would normally result from its brand having a cheaper retail price relative to that of the competing brand X. Therefore, manufacturer B's incentive to increase its wholesale price is capable of being significantly increased by manufacturer A's parity or differential requirement."

12. The OFT noted further that it was possible that parity or fixed differential requirements would restrict *intra*-brand competition because manufacturers would have reduced incentives to seek or pay for retail price reductions on their brands given the knowledge that this would be matched by an equivalent reduction in the price of the competing linked brand (paragraph 6.220). The OFT also found that the restrictive nature of the agreements was "reinforced and increased" where each manufacturer was aware that the other was operating parity or differential requirements (paragraph 6.228).

13. The description of the restrictive nature of the agreements set out above constitutes the OFT's "theory of harm", that is its explanation as to why the agreements it has found to exist have the object of preventing, restricting or distorting competition within the meaning of the Chapter 1 prohibition.

14. The OFT's finding of infringement was set out under the heading "Decision" in paragraph 8.2 which said:

> "8.2 On the basis of the evidence set out above and for the reasons set out above, the OFT finds that the Infringing Agreements comprised in each case an agreement and/or concerted practice between each Manufacturer and each Retailer whereby the Manufacturer coordinated with the Retailer the setting of the Retailer's retail prices for tobacco products, in order to achieve the parity and differential requirements between competing linked brands that were set by the Manufacturer, in pursuit of the Manufacturer's retail pricing strategy. The Infringing Agreements restricted the Retailer's ability to determine its retail prices for competing tobacco products and had the object of preventing, restricting or distorting competition in the supply of tobacco products in the UK, in breach of the Chapter I Prohibition."

15. One of the many factual findings that the appellants contested was the OFT's finding that the parity or differential requirements operated as fixed requirements rather than maxima. For example, where a written trading agreement expressed the desired link in terms that a pack of Richmond cigarettes should be "not more expensive than" a pack of Dorchester cigarettes, the appellants argued that the retailer would comply with the

agreement if Richmond was cheaper than Dorchester. The OFT relied on the way it said the agreements were operated in the market and on the allegation that there were parallel and symmetrical agreements imposed on the same retailers by Imperial and Gallaher as showing that in fact the retailer was bound to price Richmond at the same price as Dorchester, neither more nor less expensive. The OFT found, however, that if the agreements did in fact operate as maxima and not as fixed parities or differentials the theory of harm still applied. The long term implementation of a maximum differential requirement would, the OFT found, reduce the incentives of each manufacturer to engage in inter-brand competition in relation to wholesale prices (paragraphs 6.230 onwards of the Decision).

16. The OFT rejected the parties' submissions as to the application of the Competition Act 1998 (Land and Vertical Agreements Exclusion) Order 2000 (SI 2000/310) which was in force at the time and further held that the agreements did not benefit from the exemption provided for in section 9 of the 1998 Act. The OFT held that most of the infringements should be treated as lasting from 1 March 2001 (the date when the transitional period allowed under the 1998 Act ended)[2] until 15 August 2003 which was the cut off date for the requests for information sent by the OFT to the parties.[3]

17. Substantial fines were imposed on the parties, the largest being a fine of £112.3 million imposed on Imperial. The fines imposed on the retailers who have brought appeals were £14.1 million for Asda (which had entered into an early resolution agreement), £14.2 million for the Co-op, £8.6 million for Morrisons, £10.9 million for Safeway and £3.4 million for Shell.[4]

[2] The 1998 Act came into force on 1 March 2000. Paragraph 9 of Schedule 13 to the Act provided for a one year transitional period during which the Chapter 1 prohibition did not apply to pre-existing agreements.
[3] Since the period covered by the infringements did not extend beyond 1 May 2004, the OFT held that it did not need to consider whether the agreements infringed the EU competition rules as well as the 1998 Act.
[4] We note here that Shell objected to being referred to as a retailer because part of its case relied on its submission that for most of the period covered by the Decision, sales of cigarettes from Shell petrol station forecourt shops were made not by Shell but by independent contractors who ran their own business as far as non-fuel products were concerned. We refer to Shell as one of the retailers in this judgment purely for ease of exposition and without prejudice to those arguments.

The appeals and the evidence served by the parties

18. Six appeals were lodged against the Decision by Imperial and by five of the retailers: the Co-op, Morrisons, Safeway, Asda and Shell. This meant that in all, 15 separate bilateral agreements were challenged before us since Imperial challenged the findings of infringement in relation to its agreements with all 10 retailers condemned in the Decision (and not just those with the retailers who had also appealed) and each of the five retailers who appealed challenged the findings in relation to their alleged agreements with both Imperial and Gallaher.

19. It is convenient at this point to set out the Tribunal's powers in relation to these appeals. The appellants' appeals were brought under section 46 of the 1998 Act. That provides (as amended):

> "46 **Appealable decisions**
>
> (1) Any party to an agreement in respect of which the OFT has made a decision may appeal to the Tribunal against, or with respect to, the decision.
>
> ...
>
> (3) In this section, "decision" means a decision of the OFT—
>
> (a) as to whether the Chapter I prohibition has been infringed, ..."

20. Schedule 8 to the 1998 Act contains further provisions about such appeals. It provides in paragraph 2(1) that an appeal must be made by sending a notice of appeal. That notice must set out the grounds of appeal in sufficient detail to indicate to what extent the appellant contends that the decision against which the appeal is brought was based on an error of fact or was wrong in law.

21. Paragraph 3 of Schedule 8 so far as relevant reads as follows:

> "3. (1) The Tribunal must determine the appeal on the merits by reference to the grounds of appeal set out in the notice of appeal.
>
> (2) The Tribunal may confirm or set aside the decision which is the subject of the appeal, or any part of it and may-
>
> (a) remit the matter to the OFT,
>
> ...

(d) give such directions, or take such other steps, as the OFT could itself have given or taken, or

(e) make any other decision which the OFT could itself have made.

..

(4) If the Tribunal confirms the decision which is the subject of the appeal, it may nevertheless set aside any finding of fact on which the decision was based."

22. The grounds relied on by the appellants in their notices of appeal differ in some respects but none of those differences is relevant for the purposes of this judgment. The relief sought by the appellants (leaving aside penalty and costs) is as follows:

(a) Imperial, Safeway, and Morrisons[5] ask the Tribunal to annul the Decision as it applies to them and to grant any other relief as may be required;

(b) The Co-op asks the Tribunal to set aside the Decision;

(c) Asda asks the Tribunal to annul the Decision in its entirety, alternatively to declare that the practices were excluded from the Chapter 1 prohibition by the Vertical Agreements Exclusion Order or were exempt under section 9 of the 1998 Act, or in the further alternative to remit the matter to the OFT for consideration of exemption under section 9;

(d) Shell asks the Tribunal to quash the Decision, or alternatively to remit the matter to the OFT with directions to reconsider and make a new decision in accordance with the Tribunal's ruling.

23. Each appeal challenged both liability and penalty. The Tribunal decided following a case management conference in October 2010 that issues relating to liability would be determined before hearing issues relating to penalty.

24. Accompanying their notices of appeal, the appellants served a total of 22 witness statements from 20 witnesses dealing with their challenge to the findings of infringement. They also served seven reports from seven different expert economists,

[5] Safeway and Morrisons brought separate appeals but were represented by the same solicitors and counsel.

some of which addressed the OFT's theory of harm and some of which contained analysis of data about prices charged for tobacco products in the market over various periods.

25. The OFT served separate defences on liability to each of the appeals on 17 December 2010. The OFT's "Bundle of Supporting Documents to the Defences" included one witness statement dated 2 September 2005 by Fiona Bayley[6] who had been a tobacco buyer for Sainsbury between October 2000 and May 2002. The OFT's defences maintained the case set out in the Decision as against the appellants. The relief sought at the conclusion of each defence asked the Tribunal to dismiss the appeal against the findings of infringement.

26. In addition to the witness statement from Ms Bayley, the OFT's Bundle of Supporting Documents to the Defences included two expert economist reports. The report dealing with the OFT's theory of harm was provided by Professor Greg Shaffer of the University of Rochester's William E. Simon Graduate School of Business in New York State, USA. In his report, dated December 2010, Professor Shaffer stated that he had been asked by the OFT to assume the facts as found by the OFT in the Decision and to provide an independent expert report on certain economic issues raised by the appeals. In the summary of his conclusions, Professor Shaffer said (amongst other things):

> "15. My analysis of the facts in the Decision has led me to conclude the following:
>
> Trading arrangements that fix or put a ceiling on the relative retail prices of competing products, thereby affecting a retailer's independent setting of its own relative prices would be expected to have anti-competitive effects:
>
> - even if absolute retail price levels are not stipulated;
> - even if a retailer would have chosen the same parities and/or differentials between competing linked products absent the trading arrangement;
> - because they would be expected to reduce inter-brand competition from the moment they are established;
> - because they would be expected to reduce intra-brand competition from the moment they are established;

[6] Ms Bayley gave evidence to the Tribunal using her married name but we refer to her as Ms Bayley as that is the name that appears in the contemporaneous documents and with which she signed her witness statement.

> - because over time, they would be expected to facilitate coordination in the setting of the Manufacturers' wholesale prices and the Retailers' retail prices;
>
> - because they do not appear to have any pro-competitive justifications.
>
> ...
>
> 17. The Manufacturers' trading arrangements would be expected to reduce inter-brand competition from the moment they are established because each Manufacturer's trading arrangement would (a) reduce the incentive of the rival Manufacturer to compete by lowering its wholesale prices and (b) increase the incentive of the Manufacturer with whom the Retailer has the arrangement to increase its wholesale price. In the former case, incentives to lower wholesale prices would be reduced because the rival would be unable to shift relative retail prices in its favour. In the latter case, incentives to raise wholesale prices would be increased because relative retail prices would not shift to the Manufacturer's detriment. Both effects would increase the incentives of Manufacturers to raise their wholesale prices. Retail prices would thus be expected to rise when these higher prices are passed through to consumers."

27. Pursuant to a direction from the Tribunal, a joint experts' report was lodged on 2 June 2011. This set out the views of Professor Shaffer and those of the appellants' experts whose evidence addressed the OFT's theory of harm.

28. Following replies from the appellants (accompanied by six further witness statements from six of the previous witnesses and seven further expert reports), skeletons were lodged by the parties in preparation for the main hearing. The OFT's skeleton was served on 4 July 2011 ("the OFT's Skeleton"). That Skeleton dealt at length with the OFT's theory of harm and what Professor Shaffer had said about it. The OFT referred to Imperial's skeleton as identifying four anti-competitive consequences of the Infringing Agreement found by the OFT. These were set out in paragraph 40 of the OFT's Skeleton (referring to Imperial as "ITL" and using "P&D" as an abbreviation for "parity and differential"):

> "40. Assuming that ITL has a P&D agreement with a Retailer of the kind identified by the OFT:
>
> a. If the retail price of Gallaher's brand increases, then the retail price of ITL's rival brand must also increase.
>
> b. If the retail price of ITL's brand increases, then the retail price of Gallaher's rival brand must also increase.
>
> c. If the retail price of ITL's brand decreases, then the retail price of Gallaher's rival [brand] must also decrease.

> d. If the retail price of Gallaher's brand decreases, then the retail price of ITL's [rival] brand must also decrease.
>
> 41. The first thing to note is that ITL fails to consider that Retailers may want to change the relativities of prices entirely independent of any Manufacturer price changes. The four permutations therefore do not reflect all constraints which the Infringing Agreements place on the Retailer's prices."

29. Those four restraints were referred to frequently during the course of the main hearing as "the paragraph 40 restraints" and we refer to them as such in this judgment. At the end of each of the sub-paragraphs of paragraph 40 was a footnote identifying documents on which the OFT relied to establish the existence of that restriction at least in respect of some of the retailers. At some points in the hearing it was not clear whether the OFT accepted that an infringement of the kind defined and described in the Decision would display all four of those restraints. Our understanding of the matter is that it was the OFT's case in the Decision, in its pleadings in these appeals and at the start of the main hearing, that the Infringing Agreements contained all those restraints subject to three qualifications. The first qualification was that if the parity or differential requirements were found to be maxima rather than fixed, the OFT accepted that only the restraints in 40(b) and (d) would apply. The second was that so far as 40(d) was concerned, some agreements operated what was referred to as an "opportunity to respond" clause. Under such a clause if, for example, Gallaher triggered a reduction in the retail price of its brand in the retailer's stores, the retailer was not obliged under its agreement with Imperial to lower the price of the linked Imperial brand, unless Imperial took up the opportunity to respond and correspondingly reduced the wholesale price of its brand to that retailer. The third was that the OFT accepted that not all of the 15 agreements which were the subject of the appeals necessarily exhibited all four restraints. The OFT did not, however, at any stage identify any particular agreement which it conceded contained fewer than all four restraints. Apart from those three caveats, the appeals proceeded on the basis that the agreements entered into by Imperial and Gallaher imposed the paragraph 40 restraints on each of the retailers.

The hearing and the growing uncertainty about the OFT's case

30. The main hearing of these appeals before the Tribunal began on 21 September 2011. After five days of opening submissions we heard evidence over 20 days from 19 factual

witnesses. Some of the Imperial witnesses gave evidence on more than one occasion because they dealt with more than one retailer account. In accordance with the Tribunal's usual practice, the witness statements stood as each witness's examination in chief so that the evidence given orally was limited to cross-examination and re-examination. All but one of the witnesses who lodged witness statements relating to liability were called for cross-examination although, of course, the questioning focused on the contentious parts of their evidence. Where the witness was tendered on behalf of one of the retailers, the OFT cross-examined first and then Counsel for Imperial cross-examined before the witness was re-examined by counsel for the relevant retailer appellant. Similarly, the relevant retailer appellant was able, once the OFT had finished its cross-examination, to question the Imperial witnesses whose evidence dealt with Imperial's trading relationship with that retailer.

31. On a number of occasions during the cross-examination of the factual witnesses, Mark Howard QC, Counsel for Imperial, objected that the questions put by the OFT's counsel did not ask the witnesses in a straightforward way whether they agreed or not that any of the paragraph 40 restraints had been imposed or accepted. Mr Howard said that it was not clear why the OFT's case was not being put to the witnesses for their comment. So far as the questions which *were* being put to the witnesses by the OFT, Mr Howard further complained that it was difficult to glean whether the OFT's case had moved away from the paragraph 40 restraints and if so, what was now being alleged to have been the content of the infringement. We understood Mr Howard's objections at this stage to be intended for the most part to alert the Tribunal and the OFT to the possibility that if at the end of the hearing the OFT asked the Tribunal to find as fact the existence of the paragraph 40 restraints, Imperial might contend that such a submission was not open to the OFT because that case had not been adequately put to the appellants' witnesses. What happened with a number of witnesses was that, after the cross-examination by the OFT, Mr Howard would himself put a series of questions to the witness from Imperial or the retailer designed to elicit from him or her whether the agreement between the two companies had contained any of the paragraph 40 restraints. Almost invariably the answers given by the witness to Mr Howard were emphatic that those restraints were not part of the agreement between Imperial and the retailer in question.

32. Criticism by Imperial about the way the OFT's case was being conducted came to a head on Day 16 (19 October) during the cross-examination of Mr Eastwood (a witness tendered by Morrisons). After hearing submissions at the end of that day's proceedings once the witness had withdrawn, the Tribunal agreed that it was not clear how the OFT's cross-examination of the witnesses fitted with the OFT's case in the Decision or with the paragraph 40 restraints or with the factual assumptions underlying Professor Shaffer's report. The Tribunal indicated that if the OFT's case had moved since the OFT's Skeleton was lodged or since Professor Shaffer's report was prepared, everyone needed to be made aware of that. This was important so that the appellants could understand the thrust of the questions being put to the witnesses and ensure that they themselves asked in cross-examination or re-examination any questions that they needed to put, having regard to the OFT's case. Paul Lasok QC, Counsel for the OFT, said in response to the Tribunal that he did not understand the OFT's position to have changed since the Decision and he did not accept that the line of cross-examination had gone off in a direction other than that pointed to or signposted in the Decision. There were further exchanges between the Tribunal and Counsel which did not, in the Tribunal's mind at least, take the matter further forward.

33. On Day 19 (25 October) after the OFT had cross-examined an Asda witness, Mr Howard submitted that the divergence between the Decision and the evidence given by the witnesses might now be so great that it was impossible to see how the case could continue. He also made the point that the hearing was moving towards the days scheduled in the timetable for the cross-examination of the expert witnesses dealing with the OFT's theory of harm. He said that there was "genuine puzzlement" on Imperial's part as to what case the appellants' experts should be addressing.

34. The prelude to the adjournment of the hearing came on the morning of Day 23, Monday 31 October. The OFT's questioning of the witnesses continued to generate uncertainty as to the nature of the restraints now alleged to constitute the infringements. After further submissions, the Tribunal asked the OFT to clarify two matters by close of proceedings on Wednesday 2 November. The first matter was whether the OFT still maintained that each of the 15 agreements which were the subject of these appeals operated in the same way. The second matter was to answer certain questions about how the OFT now asserted that the agreements operated, such as whether the OFT still

maintained that the paragraph 40 restraints operated independently of any changes in the wholesale price set for the brand by the manufacturer for that retailer.

35. In response to the Tribunal's request, the OFT made submissions at the opening of proceedings on Day 26, Thursday 3 November ("the Day 26 Statement"). That day was supposed to be devoted to cross-examination of the last of the factual witnesses. Mr Lasok said that in the light of the evidence that had emerged in the course of the proceedings, it appeared to the OFT that each and every one of the specific circumstances relied on in the Decision to support the finding of an object infringement "may or may not be established to the appropriate legal standard". He went on to say:

> "… we think, having looked at the evidence in the round as it has come out, that the Decision has, to put it loosely, been cast too narrowly. If you like, it has identified a particular mechanism or method of implementation that gives rise to the anticompetitive harm. But in some of the cases that are before the Tribunal, it looks as though the same end result, that's to say the same anti-competitive harm, results or may result in a different way, which is not captured sufficiently clearly in the Decision. When I say "sufficiently clearly", one can look at the Decision and seek to read it in different ways, but at the end of the day, you know, a decision has a particular legal meaning, the Tribunal decides what the legal meaning of the Decision is, and it is clearly open to the Tribunal to conclude that on the legal meaning of the Decision, it's too narrow to capture some of the permutations that we have seen in the evidence."

36. Mr Lasok then outlined two possible routes by which the Tribunal could arrive at what he called "the correct result". The first was that the OFT could invite the Tribunal to deal with the appeals in exercise of its powers under paragraph 3(2)(d) and (e) of Schedule 8 to the 1998 Act, "expanding the case in the Decision to the alternatives that arise from the evidence". The second route was for the OFT to amend the Decision by removing the Infringing Agreements currently before the Tribunal and, if it considered appropriate, to issue a new statement of objections seeking to capture all the alternatives that the evidence had thrown up. Mr Lasok acknowledged that going down the Schedule 8 route required serious consideration of the practicalities and procedural consequences. He also recognised that if the OFT decided instead to amend the Decision and issue a new statement of objections, these appeals would now be brought to an end. Mr Lasok indicated that the OFT had not yet finalised its view as to which of the two courses the OFT would invite the Tribunal to take.

37. This statement caused consternation among the other parties. Mr Howard on behalf of Imperial submitted with some force that if the OFT was not in a position to say whether it wished to continue contesting the appeals, the appeals should be allowed there and then. After listening to further submissions, the Tribunal acceded to the OFT's request to adjourn the hearing. In our ruling on that point we stated as follows:

> "The OFT has accepted that if it were to decide to ask the Tribunal to allow the proceedings to carry on, it would have to explain in very clear terms: (a) the entirety of the constraints that it now contends were accepted in the 15 bilateral arrangements; (b) how those constraints fit within the description of the infringements set out in the Decision; and (c) whether and how the theory of harm expounded in the Decision applies to an agreement including those, but only those, constraints.
>
> It seems inevitable that the appellants would strongly contest an application by the OFT for the Tribunal to adopt the Schedule 8 course. The Tribunal would have to decide not only whether this was really a practical course but also whether it was fair."

38. The Tribunal therefore directed the OFT to provide a written statement setting out: (a) whether the OFT continued to contest the appeals and (b) if so, the legal and factual basis on which it did so in relation to each of the 15 bilateral agreements. The single remaining factual witness was released and the arrangements for bringing the parties' experts to court to give evidence over the following two weeks were put on indefinite hold. The Tribunal also directed that a case management conference be held on Friday 11 November.

39. A statement was provided by the OFT to the appellants and to the Tribunal on the afternoon of Wednesday 9 November. That statement ("the Refined Case") said that the OFT intended to contest the appeals in relation to each of the 15 Infringing Agreements. It did so on the basis that those agreements were object infringements of the Chapter 1 prohibition. The key paragraphs of the OFT's Refined Case were as follows:

> "2. The OFT considers that the evidence before the Tribunal supports the conclusion that each of the Appellants has committed an infringement of the Chapter I prohibition comprising the agreement or concertation of:
>
> a. specific retail prices in the context of the maintenance of the manufacturer's P&D strategy regarding the retail prices of its own brands relative to the retail prices of linked competing brands;

b. a requirement or expectation that retailers would adhere to the manufacturer's P&D strategy in the absence of manufacturer wholesale price changes or alternative manufacturer instructions.

3. In other words, it was agreed or concerted between the manufacturer and the retailer that, when the manufacturer instructed or requested the retailer to move the latter's shelf price for the manufacturer's brand, pursuant to the manufacturer's P&D strategy, the retailer would move the shelf price to the price instructed and/or requested by the manufacturer. The retailer's ability to determine its retail prices for tobacco products was thereby restricted (Decision/1.4).

4. As stated in the Decision (for example, paragraph 1.8(iv)), the OFT submits that the payment of bonuses and, more generally, the manipulation of wholesale prices by the manufacturer were means of achieving the manufacturer's objective, that of securing shelf prices that reflected the manufacturer's P&D strategy.

5. In the absence of any movement in prices initiated by a manufacturer, the agreement or concertation was that the retailer would not itself move shelf prices for linked competing brands in such a way as to take the price of the manufacturer's brands out of line with the manufacturer's P&D strategy.

6. The articulation of the infringement set out above differs from the description given in the Decision (see, for example, Decision/6.92) in that it is not a consequence of the Infringing Agreements that, following a price change instigated by one manufacturer, the retailer was required to change the retail price of a competing manufacturer's brand in order to maintain or realign the first manufacturer's P&D requirement.

7. Instead, the agreement/concerted practice in each case was that the retailer would follow the manufacturer's pricing instructions/requests in relation to the manufacturer's brands in order to restore the parity or differential.

8. The OFT's case remains that, whichever way a P&D arrangement is implemented, the result is that competition is restricted and consumers are harmed.

9. Under the refined case set out above, the harm arising from each Infringing Agreement in isolation accords with that set out in Decision/6.217, whereby the rival manufacturer would have a reduced incentive to lower its wholesale price and a greater incentive to increase its wholesale price.

10. Where the rival manufacturer also operates a P&D, it will likewise create a reduced incentive for the manufacturer to lower its wholesale prices and a greater incentive to increase wholesale price. Therefore, a consequence of both manufacturers having P&D requirements is that both manufacturers would have an increased incentive to raise their wholesale price and a decreased incentive to reduce their wholesale price."

40. The OFT's submissions as to how the case should proceed were put in the alternative. The OFT's primary case was that the restraints set out in paragraph 2(a) and (b) of the Refined Case ("the Refined Case Restraints") "reflected part but not the whole of the Decision". The appeals could and should proceed on that basis. If the Tribunal disagreed with that submission, the appeals could nonetheless proceed "by reference to the Tribunal's powers under paragraph 3 of Schedule 8 to the 1998 Act". The OFT did

not consider that any additional factual evidence was required in order to decide the case but accepted that the Refined Case would need to be put to the expert economists.

41. At the case management conference on 11 November (Day 27) the appellants strongly contested each element of the Refined Case. A further hearing was held on 17 and 18 November (Days 28 and 29) at which we heard submissions on whether the appeals should be allowed to continue. Prior to that hearing, Imperial produced a full and helpful set of written submissions on the issues arising and Asda, Safeway and Morrisons also made useful supplementary points. As had been agreed, the OFT produced a speaking note on the morning of 17 November.

42. One unusual aspect of the hearing on Days 28 and 29 was that the parties were unsure as to who was making an application to the Tribunal and what the nature of any such application was. The OFT had not withdrawn the Decision or applied to amend its defences. None of the appellants had applied to set aside the OFT's defence to its appeal. A number of possibilities were canvassed at the hearing:

(a) Some of the appellants argued that the hearing should be treated as if the OFT had applied to amend its defence pursuant to rule 11 in conjunction with rule 14(7) of the Tribunal Rules, even though the OFT had made no such application;

(b) Pushpinder Saini QC, Counsel for Safeway and Morrisons argued in the course of his oral submissions that the application should be treated as an application by all the appellants to strike out the defences under rules 10 and 14(7) of the Tribunal Rules (although no such application was referred to in these appellants' written submissions before the hearing);

(c) The OFT appeared to treat the hearing as an application by it to the Tribunal to reset the timetable for the hearing with a view to continuing the appeals on the basis of the Refined Case;

(d) Imperial appeared to regard the hearing as an application to bring the appeals to an end by performing the Tribunal's duty under paragraph 3(1) of Schedule 8 to allow the appeals and quash the Decision.

In the end we have treated this as an application by all the appellants for the Tribunal to exercise its powers under paragraphs 3(1) and (2) of Schedule 8 to determine these appeals by simply allowing the appeals now and setting aside the Decision so far as it relates to the appellants.

ISSUE 1: ARE THE REFINED CASE RESTRAINTS PART OF THE DECISION?

43. The first question we need to decide is whether the Refined Case Restraints are part of, or within, the Decision such that if the existence of those restraints is established on the evidence and if, further, all other issues are determined in the OFT's favour, the Tribunal could dispose of the appeals by confirming part of the Decision, pursuant to paragraph 3(2) of Schedule 8.

44. The starting point is section 46 of the 1998 Act which provides that the "appealable decision" which may be brought to the Tribunal is a decision of the OFT as to whether the Chapter 1 prohibition has been infringed. There is no definition in the 1998 Act of what constitutes the "decision" for this purpose but it is a question that has been considered by the Tribunal in a variety of contexts. In *MasterCard UK Members Forum Ltd v Office of Fair Trading* [2006] CAT 10 the Tribunal noted (at paragraph 25) that:

> "… it is particularly important to be able to identify clearly what findings are made in the Decision by the OFT, upon what basis those findings are made, and whether those findings are maintained. Moreover, from the point of view of the parties it is important that, when appealing, they are in a position to identify precisely the findings that are in issue, and the basis for those findings. It is also important for the Tribunal to be able to identify clearly the findings in issue, bearing in mind that the Tribunal's jurisdiction under section 46 of the Act arises in respect of the Decision and not otherwise."

45. In *Argos Ltd v Office of Fair Trading* [2003] CAT 16 the Tribunal stated at paragraph 65:

> "(1) The appeal before the Tribunal is directed against "the decision that the Chapter I or Chapter II prohibition has been infringed", which necessarily implies that the appeal is directed against the facts and matters set out in the decision and not against other facts and matters not set out in the decision (section 46(1) and paragraph 2(1) of Schedule 8 to the 1998 Act).
>
> …
>
> (3) The Tribunal must determine the appeal on the merits, but by reference to the grounds of appeal set out in the notice of appeal. Since the notice of appeal must refer to and so far as necessary put in issue the facts as set out in the decision, it follows that the Tribunal is concerned with the facts in the decision, as contested in the notice of appeal, and not with the correctness of other facts sought to be adduced as evidence of the infringement after the notice of appeal has been lodged and which, by definition, the notice of appeal has not dealt with."

46. In our judgement it is not enough simply to be able to point to disparate passages in the Decision where it is said that the OFT found that the Refined Case Restraints were accepted by the retailers and that they arguably restricted competition. Conversely it is not enough that one might construe paragraph 8.2 of the Decision, read in isolation, as wide enough to cover the Refined Case Restraints. There has to be a link or bridge in the reasoning set out in the Decision between the findings of fact and the conclusion as to infringement. In order for those restraints to be within or part of the Decision for present purposes, we must, therefore, be satisfied that the Decision includes findings that the Refined Case Restraints constituted object infringements of the Chapter 1 prohibition.

47. One can readily think of examples where the scope of an infringement decision is cut back in the course of an appeal so that ultimately only a part of that decision can be upheld. For example, it might emerge during a hearing that the OFT could prove to the required standard that a cartel agreement lasted for only two of the four years originally found in the decision or that it operated in only six geographic areas rather than seven. In such instances, while the evidence heard during the appeal may have shown the cartel to be of more limited duration or scope, it would nevertheless be clear that the decision had found that smaller cartel to be an infringement of the Chapter 1 prohibition so that the decision could ultimately be upheld to that extent. The question for us is

whether the Refined Case Restraints are part and parcel of the infringement found in the Decision in the same way.

48. Imperial argue that we should find that the Refined Case Restraints were not part of the Decision for this purpose on two bases. The first was that the OFT conceded as much in the Day 26 Statement and it should be held to that concession. The second was that a proper construction of the Decision shows that the Refined Case Restraints were not part of what was condemned as a breach of the Chapter 1 prohibition.

49. As to the effect of what Mr Lasok said in the Day 26 Statement, we listened carefully against the background of the way the proceedings had unfolded up to that point. We understood the OFT's position to be as follows:

(a) the OFT was now limiting its case to reliance on the restraint described in paragraph 40(a) – that is a restraint imposed by, say, Imperial on the retailer to the effect that when the price of Gallaher's brand went up, the price of Imperial's linked competing brand was to be raised by the retailer to suit;

(b) so far as downward movements in price were concerned (that is the restraints in paragraph 40(c) and (d)), the OFT now accepted that these generally operated through an "opportunity to respond" mechanism (see paragraph 29 above) and, further, that if a retail price movement was the result of a manipulation of the wholesale price, that might reflect a restraint that was not included in paragraph 40 of the OFT's Skeleton;

(c) so far as concerns the retailer's obligation in a situation where Imperial raised its prices (that is the restraint in paragraph 40(b)), the OFT accepted that the evidence did not support the finding that the retailer was expected to move the price of Gallaher's linked brand upwards;

(d) if the Tribunal were to find in relation to any one of the Infringing Agreements that none of the paragraph 40 constraints was present, that would not mean that there was no object infringement on the evidence before the Tribunal, but it would be a departure from the Decision as currently formulated.

50. The Day 26 Statement was, we assumed, made on instruction in response to the request made three days earlier by the Tribunal seeking clarification of the OFT's case on precisely those issues. The Tribunal and the parties were entitled to treat it as the OFT's considered view. We are satisfied that the OFT did concede that if the case it wished to put forward at that stage went outside the paragraph 40 restraints, that would require the Decision to be set aside. In that event, the only question for the Tribunal would be whether to keep the appeals going in order to exercise its powers under paragraph 3(2)(e) to make a new decision.

51. It was therefore striking that the Refined Case, served a few days later, alleged two restraints which were clearly not the same as any of the paragraph 40 restraints and yet the OFT still maintained that the Refined Case "reflected a part but not the whole of the infringement found in the Decision". The Refined Case made no reference to the concession that had been made on Day 26, either to ask the Tribunal's permission to withdraw that concession or to explain how the Refined Case fitted with the Day 26 Statement or with the paragraph 40 restraints.

52. We see considerable force in Imperial's submission that the OFT should not be permitted now to argue that the Refined Case Restraints are within the Decision. However, it would be unsatisfactory for all the parties for these appeals to be brought to an end purely on the basis of the Day 26 Statement. We do not propose therefore to end our consideration there since, regardless of the OFT's concession on Day 26, it is clear in our judgement that the Refined Case Restraints are not part of the Infringing Agreements as defined in the Decision.

53. We have already cited the passages from the Decision in which the main findings were set out. In its written submissions for the hearing on Days 28 and 29, Imperial listed 26 quotations from the Decision – from (a) to (z) – in which the OFT referred to the retailers being constrained in their pricing of "competing brands" or "linked brands". The OFT's defence to the Imperial appeal referred to paragraph 6.216 of the Decision (quoted earlier) as being the "central part of the OFT's explanation of the anti-

competitive nature of the Infringing Agreements". Similarly, the OFT's Skeleton had referred to the "crucial aspect" of the Infringing Agreements in this case being that "they involve the linking of horizontal competitors' retail prices through a vertical agreement". The OFT had therefore argued that the Infringing Agreements had the same economic effect as a horizontal price fixing agreement since "if one Manufacturer knows its rival Manufacturer's retail price will always be the same relative to its own retail price, then it can never win (lose) customers from (to) its rival."

54. The OFT has consistently stressed that the Decision should be assessed on its own precise terms and that arguments about similar but different restraints are irrelevant. For example, the OFT's Skeleton said:

> "One notable tack taken by at least some of the Appellants as the pleadings and written arguments have developed has been for them to contemplate different kinds of agreements or concerted practices to those found by the OFT to exist, and to claim that such supposed agreements or concerted practices would not be by their nature anti-competitive. This is self-evidently an irrelevant distraction and appears to be little more than an attempt to obscure the fundamentally anti-competitive nature of the Infringing Agreements."

55. In our judgement it is not open to the OFT now to argue that a restraint which is significantly different from any of the restraints set out in paragraph 40 is a restraint that was found to be part of each Infringing Agreement and subject to the theory of harm as set out in the Decision.

56. So far as the paragraph 2(a) restraint is concerned, the OFT's case is now that the price instruction given to the retailer by the manufacturer required the retailer only to move *that* manufacturer's price. These price instructions were given "in the context of" the maintenance of the manufacturer's parity and differential strategy. In formulating this restraint, the OFT accepts now that there was no requirement on the retailer to move the price of the *competing* brand. Nonetheless, the OFT wishes to argue, the choice of price by the manufacturer reflected its own strategy as to which competing brands its products should be priced against. By complying with the manufacturer's instruction, it is therefore alleged that the retailer enabled the manufacturer to implement its parity and differential strategy.

57. The OFT submits that the object of such an agreement in economic terms is the same as the anti-competitive object of the Infringing Agreements described in the Decision. The appellants strongly contest this. Whether the outcome on the market of such an agreement would be the same, this is in our judgement a very different case from the reasoning set out in the Decision and the OFT's Skeleton. The nature of the infringement which was condemned in the Decision and to which the OFT's theory of harm related was the requirement that the retailer alter the prices not only of that manufacturer's brand but also of the linked competing brand. The key element of that reasoning has now gone. Any harm arising from the linkage of the prices of competing brands is now said to arise not from restraints *imposed on the retailer* by the manufacturer but from a combination of a more limited restraint and *unilateral action* taken by the manufacturers in this transparent, duopolistic market.

58. It is true that the OFT refers in the Decision to contacts between the manufacturer and the retailer in which the manufacturer appears to instruct the retailer to move the shelf price of a named brand to a particular price point. However, the OFT was not relying on those contacts to establish that the instruction was an infringement of itself. Rather the contacts were relied on in support of one of the findings in the Decision, namely that the parity and differential requirements were fixed and not maxima (see paragraph 15 above). Further, even if there are passages in the Decision which set out findings that this restraint was accepted, the necessary link between those findings and the infringement described in paragraph 8.2 is not there. Mr Lasok accepted on Day 28 of the hearing that the paragraphs in the Decision in which he asserts that the Refined Case Restraints were described were not "elevated into an alternative case" by the OFT. The bridge between the Refined Case and findings of infringement in the Decision was therefore neither clearly articulated nor properly reasoned in the Decision.

59. So far as the restraint in paragraph 2(b) of the Refined Case is concerned, this was in our judgement not part of the finding of infringement in the Decision. On Day 29, it was rightly conceded by the OFT that a restriction on retailer-led changes to retail prices in the absence of a change in wholesale prices was not part of the paragraph 40 restraints. The restraints condemned in the Decision were regarded as object infringements because of the effect they had on the *manufacturers'* incentives to decrease or increase prices at the wholesale level, see for example paragraphs 6.213 to

6.219 and 6.222 of the Decision. A restraint which is limited to preventing price moves instigated *by the retailer* (rather than following on from a change in the wholesale price) is not one of the paragraph 40 restraints. An analysis of the anti-competitive nature of such a restraint cannot be underpinned by the theory of harm which is set out in the Decision and described by Professor Shaffer in his report. Paragraph 41 of the OFT's Skeleton acknowledged as much (see paragraph 28 above). To put it another way, there was no finding in the Decision that an agreement which (i) left the retailer free to move its prices out of line with the specified parity and differential requirements in response to changes in wholesale prices but (ii) constrained it from departing from those requirements on its own initiative would be an object infringement of the Chapter 1 prohibition.

60. Finally, in addition to analysing the wording of the Decision and the OFT's case, set out in the defences and the OFT's Skeleton, we have had the benefit of listening to 25 days of submissions and evidence about the Infringing Agreements. That has given us a sense of what the appellants thought were the findings at which their considerable fire power should be directed. It is clear to us that the appellants did not come to the Tribunal thinking that they had to meet a case which included the Refined Case Restraints.

61. We are therefore satisfied that the Decision does not include findings by the OFT that the Refined Case Restraints are infringements of the Chapter 1 prohibition. Given that the OFT has abandoned its defence of the Decision beyond arguing that these two restraints are part of it, that must mean that the Decision must be set aside as against these appellants.

ISSUE 2: SHOULD THE APPEALS STILL PROCEED?

62. The OFT submits that that is not the end of the matter. It argues that if the Refined Case Restraints are not part of the Decision, the Tribunal can and should allow the hearing of the appeals to continue. This is because if the existence of those restraints is established on the evidence and if, further, all other issues are determined in the OFT's favour, the Tribunal could on setting aside the Decision exercise its powers under

paragraph 3(2) of Schedule 8 to the 1998 Act in respect of those restraints. The possibility of exercising those powers entitles the Tribunal, the OFT argues, to continue with these appeals on the modified basis. Mr Lasok said that this course would enable the OFT "to bank the progress that had already been made before the Tribunal in these proceedings and move on from there". The alternative, which would involve the OFT issuing a new statement of objections would, he said, be much more cumbersome, involve more time and costs and be more onerous for the OFT and for the appellants. Mr Lasok stated that the OFT was not seeking the remittal of the matter, a course that was also opposed by the appellants.

63. The appellants argue that once we have decided that the Decision must be set aside, the Tribunal has no jurisdiction to continue hearing the appeals. Even if they are wrong on that point, they argue that the Tribunal should exercise its discretion to allow the appeals forthwith and set aside the Decision with no further grant of relief (otherwise than as to consequential matters such as costs).

Does the Tribunal have jurisdiction to continue?

64. The OFT's submissions in favour of the Tribunal's continued jurisdiction depend, in our judgement, on a construction of our powers which is not supported either by the wording of the statutory provisions or by earlier jurisprudence. According to paragraph 3 of Schedule 8 to the 1998 Act[7] our primary duty is to determine the appeals on the merits by reference to the grounds of appeal set out in the notice of appeal. Rule 8 of the Tribunal Rules specifies the content of the notice of appeal, requiring it to spell out the ways in which it is alleged that the decision challenged is wrong. The evidence that must be served with the appeal is directed at supporting the appellant's attack on the decision. The defence served by the competition authority responds to those allegations and that evidence. The parties' decisions about what factual and expert evidence is needed and the Tribunal's case management decisions in preparation for the final hearing are informed by and directed towards the case pleaded in the notice of appeal.

65. This is not to say that cases never change after the appeal is first lodged. Arguments may be adapted or abandoned during the course of the proceedings. Any such proposed

[7] The text of paragraph 3 of Schedule 8 is set out in paragraph 21 of this judgment.

changes should be brought to the attention of the Tribunal and, where necessary, set out clearly in amendments to the pleadings made with the Tribunal's consent. The Tribunal's case law shows that the test applied under rule 11 of the Tribunal Rules for allowing amendments is a stringent one. We have in mind what the Tribunal has said in earlier cases where the evidence emerging during the course of a long hearing has diverged from the material analysed in the relevant decision. In *Napp Pharmaceutical Holdings Ltd v Director General of Fair Trading* [2002] CAT 1 the Tribunal said (at paragraph 134):

> "... it is virtually inevitable that, at the judicial stage, certain aspects of the Decision are explored in more detail than during the administrative procedure and are, in consequence, further elaborated upon by the Director. As already indicated, these are not purely judicial review proceedings. Before this Tribunal, it is the merits of the Decision which are in issue. It may also be appropriate for this Tribunal to receive further evidence and hear witnesses. Under the [1998] Act, Parliament appears to have intended that this Tribunal should be equipped to take its own decision, where appropriate, in substitution for that of the Director."

66. This approach was also applied by the Tribunal in *JJB Sports plc v Office of Fair Trading* [2004] CAT 17 (at paragraph 284), where the Tribunal said that provided each party has a proper opportunity to answer the allegations made and that the issues remain within the broad framework of the original decision, the Tribunal should determine the appeal on the basis of all the material placed before it during the appeal.

67. Nothing that we say here is intended to cast doubt on the potential for flexibility described in those cases. We do not, however, regard those statements as authority for the proposition that wherever evidence emerges during the trial that indicates that an infringement of the competition rules has been committed, the Tribunal is entitled to make a finding to that effect, even if that infringement has not formed part of the decision and is not therefore addressed in the pleadings served in the appeal.

68. The powers in paragraph 3(2)(e) may well affect the scope of the issues before the Tribunal because the content of the notice of appeal, in particular the relief sought, may anticipate the possible exercise of those powers. For example, where an appellant challenges a non-infringement decision, the notice of appeal may ask the Tribunal not only to set aside the decision but to go on and make its own findings of infringement. If the Tribunal determines the appeal in the appellant's favour and sets aside the decision, it may exercise the powers in paragraph 3(2)(e) and make a finding of

infringement. That does not take the Tribunal beyond the task set out in paragraph 3(1) because it would still be determining the appeal by reference to the grounds of the appeal.

69. The OFT submitted that the judgments of the Tribunal in *Albion Water Ltd v Water Services Regulation Authority* [2006] CAT 36 and of the Court of Appeal in the appeal from the Tribunal's judgment (*Dŵr Cymru Cyfyngedig v Albion Water Ltd* [2008] EWCA Civ 536) decide that the Tribunal's powers extend to making decisions under paragraph 3(2)(e) where the evidence disclosed in the course of an appeal indicates that an infringement has been committed.

70. We do not read those judgments as authority for that construction of Schedule 8 and we do not regard the position in *Albion Water* as analogous to the current position. In that case the notice of appeal lodged by Albion Water had clearly sought relief which included a finding of infringement and, inherent in that, a finding of dominance: see paragraph 17 of the Tribunal's judgment, [2006] CAT 36. The possibility of the Tribunal exercising the power in paragraph 3(2)(e) was therefore part and parcel of the appeal from the outset and other parties were able to respond in their pleadings and evidence on that basis. The Court of Appeal rejected the submissions of Dŵr Cymru that to allow the Tribunal to make a decision on the basis of information that had not been available to the competition authority when the original decision was adopted would amount to the Tribunal usurping the role of the first tier competition authority and going beyond its appellate function. The Court held that paragraph 3(2)(e) "does not look at the historical position but confers jurisdiction on the Tribunal to make a decision of a kind that the competition authority, if still seized of the matter, could have made on the basis of the material now available" (at paragraph 127).

71. None of the notices of appeal we are considering asks the Tribunal to make a decision under paragraph 3(2)(e) and the relief sought by the OFT in the defences is limited to dismissing the appeals. The Court of Appeal's judgment in *Albion Water* does not address the issue that currently faces us and nothing in this judgment is intended to be inconsistent with the Court of Appeal's description of the scope of the Tribunal's powers under paragraph 3(2)(e).

72. We also agree with Mr Howard's submission that the *Albion Water* case did not contradict the Tribunal's comments in earlier cases as to the dangers of allowing the OFT to alter its case on appeal. In *Aberdeen Journals Ltd v Director General of Fair Trading* [2002] CAT 4, for example, the Tribunal said:

> "... such an approach could give rise to a tendency to transform this tribunal from an essentially appellate tribunal to a court of trial where matters of fact, or the meaning to be attributed to particular documents, are canvassed for the first time at the level of the tribunal when they could and should have been raised in the administrative procedure and dealt with in the decision. We do not think that such a development would be conducive to appropriate rigour in administrative decision making, or to a healthy and fair system of appeals under the [1998] Act."

73. The Court of Appeal in *Office of Communications v Floe Telecom Ltd* [2006] EWCA Civ 768 also stated that paragraph 3(1) makes clear that the appeal is on the merits and also "limits the appeal to the points taken in the notice of appeal" (at paragraph 24).

74. Our attention was also drawn to the judgment of the Tribunal in *MasterCard UK Members Forum Ltd v Office of Fair Trading* [2006] CAT 14 and the earlier reasoned order made by the Tribunal in that case: [2006] CAT 10. Those judgments do not appear to us to be addressing the point that arises here. In that case the OFT was not seeking to change the restraints that it alleged were infringements. Rather, as the Tribunal put it, the OFT's defence revealed that "in important respects the route by which the OFT reached the conclusion ... that the domestic interchange arrangements in the MasterCard scheme infringed [the Chapter 1 prohibition], … was different from the route by which the OFT had reached that conclusion in the Decision". The Tribunal in *MasterCard* was faced with a situation where the OFT wished to withdraw the Decision but the appellants wished the appeals to continue since they were seeking a declaration that the agreements in issue were not anti-competitive. The Tribunal's uncertainty as to its continued jurisdiction in those circumstances is not relevant to the question that we have to decide.

75. In our judgement, the powers under paragraph 3(2) do not extend the scope of our jurisdiction under paragraph 3(1) and do not enable us to engage in an investigation, independent of the issues raised in the appeal, as to whether other infringements have been committed. In the light of our analysis of the Decision, of the Refined Case and of the relevant statutory provisions, the OFT's current position amounts in effect to a

recognition that none of the findings of infringement in relation to these appellants is adequately supported by the evidence before the Tribunal. In those circumstances, we do not have jurisdiction to continue the hearing of these appeals.

How would we exercise our discretion if we had such a discretion?

76. In case we are wrong about the scope of our jurisdiction, we have considered whether we would exercise a discretion to allow the OFT to change course at this stage in the proceedings. In our judgement, the arguments against such an exercise of any discretion are overwhelming. We cannot see how continuing the hearing could result in circumstances in which it would be fair or appropriate for us to exercise our powers under paragraph 3(2) in the manner proposed by the OFT.

77. In formulating the test which should apply we have been hampered by the uncertainty about what application we are in fact considering (see paragraph 42 above). If the OFT had applied to amend its defences, we would apply the criteria in rule 11 of the Tribunal Rules, adapted appropriately to apply to a defence rather than a notice of appeal: see rule 14(7). That would require us to consider whether (a) the proposed new defence is based on matters of law or fact which have come to light since the defence was first served; (b) whether it had not been practicable to include these matters in the original pleading; or (c) whether the circumstances are exceptional.

78. We have also had regard to the criteria set out in the Tribunal's judgment in *Burgess v Office of Fair Trading* [2005] CAT 25, where the Tribunal considered the circumstances in which the Tribunal might exercise its power under paragraph 3(2)(e). The Tribunal said at paragraph 132:

> "In our judgment … the Tribunal should, if necessary, take its own decision rather than remit if (i) it has or can obtain all the necessary material (ii) the requirements of procedural fairness are respected and (iii) the course the Tribunal proposes to take is desirable from the point of view of the need for expedition and saving costs. Such an approach in our view is compatible with the overriding objective of deciding cases justly."

79. Those were the criteria that the Tribunal applied in the *Albion Water* judgment discussed earlier. The application of each of those criteria points firmly against allowing these appeals to proceed.

80. We have considered whether the OFT's Refined Case is based on matters of fact that have come to light since the defence was served and which it was not practicable to include in the original pleading. The OFT's view appears to be that we have arrived at our current position as the result of the witness evidence having unfolded in an unexpected way. Mr Lasok said in his submissions on Day 28 (17 November) that it was only "after the evidence had turned out as it did that there was a change to the OFT's case, and that followed on from the cross-examination of the witnesses". Until that time, he said, the OFT's understanding was based largely on contemporaneous documents and accounts provided by the parties and their witnesses during the administrative procedure. He said:

> "That approach, based on placing the greater weight on the contemporary documentary evidence, was … entirely reasonable. But it was also… entirely reasonable for the OFT to pay attention to the evidence of the witnesses as it came out in cross-examination for the purposes of evaluating its credibility, its consistency with other evidence and then to reach a conclusion as to [where] that had led the case. That is the reason why we are now where we are."

81. We do not accept that characterisation of what has happened here. For each bilateral agreement, the Tribunal and the parties were provided at the outset of the appeals with a witness statement from at least one Imperial executive who had managed that retailer account for part, if not the whole, of the infringement period and, similarly, a statement from the tobacco buyer employed by that retailer. All those witnesses made their statements specifically for the purposes of the appeal and were able to comment directly on the evidence and reasoning relied on in the Decision. This was first hand evidence from the people who negotiated and operated the arrangements as to the content and meaning of the written trading agreements and of the various emails and letters on which the OFT relied. Their evidence in the witness box confirmed what they had said in their witness statements.

82. The appellants complained at several points before and during the main hearing that the OFT had not put forward any signed witness statements in support of its case other than that of Ms Bayley. Given that her statement was served in the OFT's bundle of documents supporting all the defences, it was not clear whether it was relied on by the OFT only in respect of the agreement between Imperial and Sainsbury or more widely in respect of agreements to which Imperial was a party or more generally still in relation to the other appellants. We note here that the OFT acknowledged in paragraph

6.16 of the Decision that the evidence it cited was relied on only as against the parties to which the documents directly related.

83. Ms Bayley's statement was signed on 2 September 2005, before the statement of objections was served and well before the issues had crystallised in the Decision and these appeals. The statement did not squarely address all the matters that were germane to the appeals. Moreover, Imperial submitted in its Notice of Appeal that the statement did not support the OFT's case in some important respects. For example, Ms Bayley stated (paragraph 55 of her statement) that if the price of Imperial's brands went up because of a wholesale price increase she would not put up the price of the Gallaher brand if Gallaher had not announced a price increase. She also said that the Imperial account manager would ask her to move the prices up and down on his own brands but her recollection was that "he never told me to do anything with a competitor brand".

84. When Ms Bayley was cross-examined by Mr Howard on Day 21 of the hearing she appeared to us to be a confident and impressive witness. Mr Howard put to her questions the effect of which was to ask whether she had regarded herself as bound by the restraints in paragraph 40 of the OFT's Skeleton. She said firmly that she had not. There was nothing in her oral evidence which was inconsistent with what she had said in her witness statement.

85. It is true that from the Tribunal's point of view – and perhaps from the appellants' – the significance of the gaps in Ms Bayley's 2005 statement only really became apparent when those gaps were filled by her answers to Mr Howard's questions in the witness box. If the OFT had tested the evidence more stringently, for example if Ms Bayley had updated her witness statement for the purpose of the appeals, it might have become clear sooner that her evidence as to how the agreement between Sainsbury and Imperial worked did not appear to be consistent with the OFT's findings in the Decision. The OFT might have been able at that point to consider the implications of her evidence for the strength of its case.

86. As things turned out, at the point when the main hearing was adjourned there had been 19 witnesses who had come to the Tribunal to state on oath that the contemporary documents did not bear the meaning attributed to them by the OFT and that none of the

paragraph 40 restraints formed part of the agreement between the manufacturer and the retailer. Conversely, there was no witness who said that the OFT was right in drawing the inferences it did from the contemporary documents. There was no sworn evidence before us in either written or oral form in which any witness said that he or she had entered into or operated an agreement of the kind condemned by the Decision.

87. We recognise that the OFT has to adopt a sceptical attitude to the evidence of company executives who deny the existence of anti-competitive agreements in the teeth of unambiguous documentation showing the contrary. The Tribunal has emphasised the importance of contemporaneous documents and the difficulties which competition authorities often face in obtaining clear evidence of infringing activity. The OFT's Skeleton referred to the well-known passage from the judgment of the Court of Justice in Cases C-204/00P, etc, *Aalborg Portland A/S v Commission* [2004] ECR I-123, at paragraph 57 where the Court said:

> "In most cases, the existence of an anti-competitive practice or agreement must be inferred from a number of coincidences and indicia which, taken together, may, in the absence of another plausible explanation, constitute evidence of an infringement of the competition rules."

88. However, in our judgement there were other factors which were important here. The comment of the Court of Justice in *Aalborg* was made in the context of agreements which the parties operate in a clandestine fashion because they know they are acting illegally. The agreements condemned in the Decision were not operated covertly. The appellants' case has always been that there was nothing unlawful about these agreements. This was not a case therefore where evidential difficulties arose because the participants deliberately failed to record or retain information about what they were doing.

89. Secondly, in relation to 10 of the 15 bilateral agreements which were the subject of these appeals, one party (Gallaher or one of the five retailers who have not appealed) had either benefited from the OFT's leniency programme or entered into an early resolution agreement with the OFT. Non-confidential copies of the early resolution agreements were annexed to the Decision. They require the undertaking to "maintain continuous and complete co-operation" throughout the investigation and until the conclusion of any action by the OFT, including any proceedings before the Tribunal.

Such co-operation expressly includes, in relation to any Tribunal proceedings, using reasonable endeavours to facilitate and secure the complete and truthful co-operation of its current and former employees in attending those proceedings, speaking to any relevant witness statements and being cross-examined on such witness statements. Despite this we were not provided with any evidence from these parties confirming that they had entered into agreements of the kind defined as Infringing Agreements or that they had imposed or been subject to the paragraph 40 restraints.

90. In our judgement, therefore, there is nothing in what happened during the course of the hearing that could properly be described as coming to light since the defences were first served or as something which it was not practicable for the OFT to know at that stage or as amounting to exceptional circumstances.

91. We have also considered, in the light of what the Tribunal said in *Burgess*, whether we have before us, or can we obtain, all the necessary material we would require in order to arrive at the decision the OFT asks us to make. The OFT is unrealistic in submitting that no further factual evidence would be needed beyond the evidence we have already seen and heard. Certainly we would expect the appellants to argue that the evidence they lodged with their appeals and the questions that they asked the witnesses would, at the least, have had a different focus if the case they thought they were challenging was the Refined Case rather than the case set out in the Decision and the OFT's defences.

92. The OFT conceded that the experts would need to address whether and how the theory of harm set out in the Decision could apply to the Refined Case Restraints. The OFT stated that "it would not be difficult to put the Refined Case to the expert witnesses". We regard this as a triumph of hope over experience, given the number of experts involved in these appeals and the absence of much common ground between them so far.

93. We have also asked ourselves whether procedural fairness could be assured; a point stressed by the Tribunal in both the *Burgess* and *Albion Water* judgments. We agree with the submissions of Safeway and Morrisons that these appeals cannot simply now carry on from where we left off as if nothing had happened. Mr Saini drew our attention to *Swain-Mason v Mills & Reeve* [2011] 1 WLR 2735, where the Court of

Appeal recently emphasised that a party seeking a late amendment to its case bears a "heavy onus" in persuading the court to allow this. There is a strong public interest in ensuring that parties should not have litigation hanging over them for a long period. Lloyd LJ (with whom the other members of the Court agreed) said (at paragraph 73):

> "A point which also seems to me to be highly pertinent is that, if a very late amendment is to be made, it is a matter of obligation on the party amending to put forward an amended text which itself satisfies to the full the requirements of proper pleading. It should not be acceptable for the party to say that deficiencies in the pleading can be made good from the evidence to be adduced in due course, or by way of further information if requested, or as volunteered without any request. The opponent must know from the moment that the amendment is made what is the amended case that he has to meet, with as much clarity and detail as he is entitled to under the rules."

94. That judgment, of course, concerned private party litigation conducted under the Civil Procedure Rules rather than proceedings before the Tribunal. We consider that the point applies by analogy in these appeals. The documents so far produced by the OFT do not set out the Refined Case in a manner which enables the appellants to understand fully the allegations they have to meet. The case management of the appeals from this point forward, seeking further clarification of the OFT's case and then working out how the appellants should respond would not be straightforward. We share the appellants' concern at the prospect of proceedings before the Tribunal turning into a costly, open-ended investigative process at a time when the appellants believed that a procedure that had begun in 2003 was drawing to an end.

CONCLUSION

95. For the reasons set out above, and in the light of the fact that the OFT no longer contests these appeals on the basis set out in its defences, we are unanimous in holding that:

(a) the restraints that the OFT now wishes to prove are not part of, or within the Infringing Agreements condemned in the Decision;

(b) the Tribunal does not, therefore, have jurisdiction to continue to hear these appeals for the purpose of exercising its powers under paragraph 3(2) of Schedule 8 to the 1998 Act on setting aside the Decision;

(c) if the Tribunal did have such jurisdiction, we would exercise our discretion against continuing these appeals.

96. The appeals must therefore be allowed and the Decision quashed in relation to these appellants. We invite the parties to provide us now with an appropriate draft order. We will consider other issues, in particular costs, at a later date if necessary.

Vivien Rose	Adam Scott	David Summers

Charles Dhanowa
Registrar

Date: 12 December 2011

ANNEX TO JUDGMENT OF 12 DECEMBER 2011

GLOSSARY OF TERMS

The parties to the appeals	
The appeals	The appeals before the Tribunal in Cases 1160-1165/1/1/10
The appellants	The appellants in Cases 1160-1165/1/1/10
Imperial	The First and Second Appellants in Case 1160/1/1/10, Imperial Tobacco Group plc and Imperial Tobacco Limited
The Co-op	The Appellant in Case 1161/1/1/10, Cooperative Group Limited
Morrisons	The Appellant in Case 1162/1/1/10, Wm Morrison Supermarkets plc
Safeway	The First and Second Appellants in Case 1163/1/1/10, Safeway Stores Limited and Safeway Limited
Asda	The First, Second, Third and Fourth Appellants in Case 1164/1/1/10, Asda Stores Limited, Asda Group Limited, Wal-Mart Stores (UK) Limited, and Broadstreet Great Wilson Europe Limited
Shell	The First, Second and Third Appellants in Case 1165/1/1/10, Shell U.K. Limited, Shell U.K. Oil Products Limited and Shell Holdings (U.K.) Limited
OFT	The Respondent in all six appeals, the Office of Fair Trading
Other parties to the investigation	
Sainsbury	Sainsbury’s Supermarkets Limited and J Sainsbury plc
Gallaher	Gallaher Group Limited and Gallaher Limited
Decision	The decision in Case CE/2596/03, dated 15 April 2010, taken by the OFT
Legislative provisions	
The Chapter 1 prohibition	The prohibition contained in section 2(1) of the 1998 Act
1998 Act	The Competition Act 1998 (as amended)
Paragraph 3(2)	Paragraph 3(2) of Schedule 8 to the 1998 Act
Paragraph 3(2)(e)	Paragraph 3(2)(e) of Schedule 8 to the 1998 Act which provides that the Tribunal may make any other decision which the OFT could itself have made
The Tribunal Rules	The Competition Appeal Tribunal Rules 2003 (SI 2003/1372)

Other terms	
Paragraph 40 restraints	The restraints set out in paragraph 40(a)-(d) of the OFT's Skeleton argument dated 4 July 2011
The defences	The defences on liability, filed and served by the OFT on 17 December 2010, in response to each of the appeals in Cases 1160-1165/1/1/10
Early resolution agreement	An agreement between a party under investigation and the OFT, under which the party admitted liability in respect of the matters set out in that agreement and also agreed, among other matters, to cooperate with the OFT, in return for a reduction in the penalty that might otherwise have been imposed
Infringing Agreements	The agreements and/or concerted practices found to be infringements between each manufacturer of tobacco producers and each retailer where the retailer would apply retail pricing relativities between competing tobacco brands required by the manufacturer (per the Glossary in the Decision)
The Day 26 Statement	The oral submissions made by leading Counsel for the OFT at the beginning of Day 26 of the main hearing, 3 November 2011
The Refined Case	The written statement provided by the OFT to the appellants and the Tribunal on 9 November 2011
The Refined Case Restraints	The alleged restraints set out in paragraph 2(a) and (b) of the Refined Case