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.

Wednesday, 2 November 2011

(10.00 am)

THE CHAIRMAN: Mr Howard.

MR HOWARD: Yes.

THE CHAIRMAN: Are you going to say something?

MR HOWARD: I am receptive to whatever the Tribunal wishes to say to me. I am always receptive.

THE CHAIRMAN: We asked for a timetable for the next two days.

MR HOWARD: Where we have just got to, we just asked Mr Lasok, and he has told us that his estimate was, just for his cross-examination, not more than one hour for Ms Williams, not more than four hours for Mr Culham, and not more than three hours for Mr Wragg, and not more than 15 minutes tomorrow morning to answer or to state what the OFT's position is.

THE CHAIRMAN: And as far as re-examination is concerned?

MR HOWARD: Re-examination is difficult to assess, because it is reactive, I don't prepare my re-examination in advance, so it slightly depends on what questions are and are not asked. But in the light of the history of things, we need to assume, I would think, Ms Williams, half an hour for her, and up to an hour for Mr Culham and Mr Wragg.

So that means that we are a little bit tight over

the next two days and we may have to actually shorten things a bit. I would suggest perhaps we just proceed for the moment and see how we get on, but we may have to be a bit more rigid.

Mr Lasok's times are clearly maxima.

THE CHAIRMAN: Yes. Let's start with Ms Williams, but we will then keep you to an hour maximum, and if you can shave a little bit off that, that will be all to the good.

Can we go and ask Ms Williams to come in, please.

MS CYNTHIA ISOBEL WILLIAMS (affirmed)

Examination-in-chief by MR HOWARD

THE CHAIRMAN: Thank you, Ms Williams. Please sit down.

MR HOWARD: Could I ask you to be given, Ms Williams, volume 3 of the core bundle, and just while that's being located could you just for the record confirm your full name and address, please.

A. Cynthia Isobel Williams [redacted].

Q. Thank you very much. Now you are being handed a file, and if you would turn in that file -- I think it's open at tab 43, which should be your witness statement. {C3/43/614} Do you have that? I think it's open already. Is that your witness statement?

A. Oh yes, sorry. Yes.

Q. I just want you to confirm that is your witness statement and that the contents of it are true?

A. Yes, it is.

MR HOWARD: Thank you very much.

Cross-examination by MR LASOK

MR LASOK: Ms Williams, as I understand it, you were employed by Somerfield as tobacco buyer as from, I think, March 2005?

A. That's correct.

Q. I am therefore assuming that you have actually no knowledge about what was going on in Somerfield between 2000 and 2003?

A. Well, I wasn't there at the time, so I do not have direct knowledge.

Q. What knowledge do you have?

A. The knowledge I would have is that when I joined the company, I would have gone, looked through the historical records to assess what their pricing policy was, what the trading agreements were, so I would have, through files at the company, established some knowledge, but I wasn't there at the actual time.

Q. So that your knowledge is that which you gleaned from reading the documents?

A. That's correct.

Q. Okay, thank you. For that reason, I am not going to ask Ms Williams any further questions about Somerfield.

So far as First Quench is concerned -- this is paragraph 3 of your witness statement, at the top of the page {C3/43/615}. In the third line you say that you were the tobacco buyer at First Quench from June 2003?

A. That's correct.

Q. Mr Cheyne, however, said when he was giving evidence -- and for the Tribunal's reference this is the transcript for Day 23 at page 78, line 16, I think, to page 79, line 5 -- that he brought you over to First Quench originally as a consultant in June 2003 to work with him on a particular project concerning, I think, a gantry agreement. He thought that you became the tobacco buyer some time afterwards, but he didn't remember when.

A. The title -- yes, I joined initially as a consultant. David was -- David Cheyne was already there. One of his projects was renegotiating a gantry contract. He also wanted me to get stuck into the day-to-day buying, because the girl who was doing the buying was literally leaving the next day because she was pregnant. And there was somebody else who was buying, I think, spirits at the time and they desperately needed help. So I was actually getting stuck into that.

Plus they had -- there was a new government regulation coming in -- I am trying to remember exactly which one it was -- and they needed somebody to put in

a due diligence procedure and manage that. So it's true, I was a consultant initially, but by September, it was the end of September, First Quench offered me a contract to work for them permanently. So the official title of buyer would have applied from the end of September of that year.
Q. The --
A. But in effect I was doing the job as a buyer from June.
Q. The first document in the file that we have which mentions you is dated 21 July 2003. Maybe the best thing is if I ask you to look at it. Could you possibly have a look at annex 16, please, and turn to tab 51. That's two emails. If you look at the first one in time, it's the one in the middle of the page, which starts just below the first holepunch, and it was sent to you on 21 July {D16/51/113}. The document preceding that is in tab 50, it's dated 20 June 2003, and was addressed to Sarah-Jane Hodson {D16/50/111}. Do you remember who she was?
A. Sarah-Jane Hodson was not the pregnant lady, she was the spirits buyer who had been helping out on tobacco at the time. So she was temporarily handling day-to-day affairs on tobacco.
Q. Perhaps for the sake of completeness, if you go to 49, tab 49, you have a letter dated 25 February 2003

{D16/49/110}. That was sent by Imperial to Fiona -- is that Gittus?
A. It was pronounced "Gittus". She was the lady that was pregnant.
Q. When did she go off?
A. She went off the week -- I think my first day was the Monday in June. She left actually at the end of that week. So I was only there for four or five days when she was there.
Q. Then we have Sarah-Jane Hodson who was sent the letter at tab 50 {D16/50/111}, and she was therefore dealing with the negotiation of the trading agreement, wasn't she?
A. Sorry?
Q. It looks as though she was dealing with the negotiation of the trading agreement, or rather --
A. Sarah-Jane?
Q. Or rather she was involved in the reviewing of the signed trading agreement?
A. I can't confirm that, I wouldn't have direct knowledge. I would imagine she would -- I would think that she wouldn't have been solely responsible for negotiating that agreement. It would have been Fiona Gittus, or indeed the training director. But I would have no direct knowledge. I haven't seen this note before.

Q. But you yourself weren't involved at that stage?
A. No. No, I confirm I wasn't involved. When I arrived, it was -- it had been -- it was a done deal. So I inherited that trading agreement.
Q. It may sound a bit trivial to you, but I am just trying to get a rather more precise idea about when exactly it was that you became involved in the day-to-day management of the trading relationship between --
A. June. It was June.
Q. But when in June?
A. To be honest, I can't remember the exact date. I think it was probably like the second or third week of June. But I wouldn't be able to guarantee that for you.
Q. Now, if we go back to your witness statement, could you look at paragraph 10, please {C3/43/616}. You there say that, in the second line:

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

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

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

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

tiers as follows."

Somebody has written under the 19th another date, the 26th. But it looks as though it was in August 2002 that the move to three price tiers took place. Does that help your recollection?
A. I haven't seen this letter before, so I can't -- it doesn't help me, no. When I joined, I was led to have understood it was earlier in 2003, but I wouldn't know exactly when. It was certainly before I arrived they had moved to three pricing tiers.
Q. We have a slightly different explanation in tab 44(a). It should be the tab after: not 44, the one immediately after it. I am hoping that you have a 44(a).
A. Yes.
Q. Which is a document entitled "Business development plan", and it has a name there, George Byas {D16/44A/88}. Did you ever come across George Byas?
A. No.
Q. If you look at the stamped pagination in the bottom right-hand corner and go to page 23 -- the date of this document, by the way, is February 2003 -- on page 23 {D16/44A/94} you have a heading "Pricing", and in the second paragraph he says that cigarettes are now in three tiers with the exception of two closely aligned tiers in parts of Scotland. Does that ring any bells?

A. No, I mean, I have not seen this note before. The pricing that's mentioned, tier 1, tier 2, tier 3, where they are just defining what premium or reductions above the manufacturer's recommended price, I was aware of.
Scotland is a bit -- I shouldn't say strange, but Glasgow is a very particular area. Life is very competitive there, the mix of brands it sells. When I was dealing with tobacco, was very different. So you would tend to have a different tier just relevant to a few stores to ensure that it met with local needs.
So that was all the exception was.
Q. Right. Could you go to paragraph 24 of your witness statement, please {C3/43/621}. In the first sentence of paragraph 24 you refer to negotiating trading agreements at Alldays, First Quench and Somerfield. The last First Quench trading agreement that we are concerned with in the present proceedings is the one at tab 48 of annex 16 {D16/48/104}. If you look at that, the covering letter is dated 25 February 2003, and the agreement itself you can see from the last page is dated 1 March.
It seems that it must be obvious that you weren't involved in the negotiation of this agreement?
A. No, I was not involved in that. But during my time in First Quench -- and I left in March 2005 -- I would have

been negotiating the next agreement, or at least starting negotiating the next agreement before I left, which is what I was referring to in my witness statement, not this one specifically.
Q. If you go to paragraph 26 of your witness statement, could you just read paragraph 26 and the first sentence of paragraph 27 to yourself, please {C3/43/622}.
(Pause)
A. Yes.
Q. What I was a bit puzzled about is this: in the first sentence of paragraph 27 you say:
"ITL was aware of this."
I wasn't sure what the "this" was. Could you tell us what the "this" refers to, please?
A. What I referred to there was, in the previous paragraph I had said that we had divergent retail pricing strategies, such that I at First Quench was seeking to maximise the profitability without losing volume.
Imperial's strategy, as I saw it, was to achieve competitive pricing with its rivals as a tool to increasing its market share. First Quench: had Imperial, as I say here, just simply lowered their wholesale price, ie not offered an incentive, "if you do this we will pay you that", I would have been unlikely to have passed that money on to the customer.

THE CHAIRMAN: You were likely or unlikely to pass it on?
A. Unlikely.
MR LASOK: So you are actually referring to the position as it was as from when? September 2005?
A. I would have referred to the position from when I was working at First Quench, no, from June 2003.
Q. But you then go on to say that what ITL was aware of was the main reason it offered the bonuses to First Quench, but wasn't it the case that the arrangements between ITL and First Quench were set out in the trading agreement, which is at tab 48, and dates back to March 2003, before you turned up on the scene?
A. What they were offering there were incentives for First Quench to price below recommended price, so those sums of monies would be paid if you priced below recommended price.
First Quench's strategy was not to price below recommended price in all the three pricing tiers. Therefore, according to that agreement then Imperial would have paid the money purely against the volume set against the lower tier, which was about 30 per cent of the business. So they were offering money to encourage us to reduce prices below recommended price.
First Quench would not have stepped away from its pricing policy in that case, it would have accepted that

they would only get those bonuses where we were actually passing it on to the customer in an ongoing way.
Q. Let's go back to tab 47, please. Tab 47 is a document that dates back to 19 February 2003 {D16/47/103}. I accept that this was before you turned up on the scene, but there was one aspect of it that I wondered whether you could help us with.
If you read that email, there are some figures on the left-hand side starting in the third line, and you first have a reference to 12.5 gram pack, and then you have tier 1 and 2, and it says "MRP plus 4p". Do you happen to know what "MRP" means?
A. That would be -- some people probably internally referred to -- that's manufacturer's recommended price as on their published price list.
Q. Okay, so --
A. So that would -- I would interpret that that in tiers 1 and 2, the 12.5 gram pack of handrolling tobacco, the HRT, they will sell all brands, not just Imperial's, currently at 4p above the published recommended price.
Q. This is an email that was sent by First Quench to Gallaher, Imperial and Rothmans. I think it's also copied to BAT. Did you ever have occasion to send confirmation of First Quench's pricing policy to the manufacturers?

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

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

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

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

pricing policy. Therefore, it didn't qualify for the money, because it didn't suit First Quench to bring the price down. It would not do it.

In actual fact, the policy at that time -- you see, it makes general references to cigarettes 6p above or below recommended price. That would have applied to all brands across the piece. Many of the brands, I guess that Imperial saw as competition from Gallaher, they were at the same recommended price anyway, so the differentials or parities would happen by default.

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

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

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

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

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

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

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

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

A. Yes. Handwritten document.

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

A. Yes.

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

A. Yes.

Q. So the writer of the letter says:

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

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

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

like this when you came to First Quench in June?

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

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

"With regard to other items discussed ..."

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

If you prefer to, do read the entire letter.

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

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

A. Yes.

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

"With regard to other items discussed ..."

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

A. Yes.

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

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

Were you aware of this?

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

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

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

She goes on to say:

"I am to confirm this next week."

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

A. I would explain that -- again, I don't know the context of this particular note -- Fiona at the time, they were formulating a revised pricing policy. At that point, the cigar structure had not been finalised. If and where -- because the manufacturer might be offering bonuses to help support price cuts below at recommended price, they would need to know what those prices are so that those bonuses could be paid.

Other than that, I can't comment.

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

(Pause)

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

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

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

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

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

A. Yes.

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

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

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

Q. Let's go back to --

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

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

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

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

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

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

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

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

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

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

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

Q. Well --

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

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

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

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

A. I handled the important pieces of paper like the trading agreement and, for example, a Gallaher furniture agreement. In terms of the day-to-day conversations and ins and outs, I knew there was some rancor between the two, only because their commercial strategies were quite different in terms of pricing. But I wouldn't have seen -- I wouldn't have, within, say, the first three weeks, possibly, seen every piece of paper that related to that relationship. But I would have seen trading agreements.
Q. But the thing is that you didn't see the letter at tab 46?
A. Not that I can recall.
DR SCOTT: Sorry, can you clarify something? You have just said "their commercial strategies were quite different in terms of pricing"; was that between Gallaher and ITL or between the manufacturers and First Quench?
A. Imperial and First Quench. Yes, sorry, I didn't make that clear.
DR SCOTT: Just pausing there for a moment, what did you expect Gallaher and ITL's pricing strategy was about when they used the word "competitive"?

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

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

strategy of First Quench?

A. Well, not -- day-to-day administration I would do. If you are talking about a recommendation to change the pricing policy that I had, I wouldn't have done that until after I was confirmed as the buyer for tobacco.

But on the other hand that was to be expected, because to do the job properly I would need time to evaluate what the situation was, which I used my pricing model to establish competition and so on. So I would not have been making major decisions until after I had been in the hot seat, as it were, for a few months.

Q. So from June 2003, the point in time at which you became involved, who was the person who was making the First Quench decisions regarding the pricing of tobacco products?

A. What I did was to follow the policy that was in place at the time. So if there were price changes to do, they were in line with the price policy. My strategy was not to, at that stage, challenge them until I understood the business a bit more. So I followed policy. I did change prices, for example, but I was following the policy.

Q. Where did this policy come from?

A. The pricing strategy. The tiering system.

Q. So basically -- can I put it in my own words and if I am wrong you will tell me?

A. Yes, please.

Q. There was a sort of -- I'll use the word matrix or pattern or strategy that you inherited?

A. Yes.

Q. And you applied that?

A. Yes.

Q. For a few months?

A. Yes.

Q. Before you were in a position to make your own decisions?

A. Yes, it would have been foolish of me to try and alter anything significantly before I had sufficient knowledge and understanding of the First Quench business.

MR LASOK: No further questions.

Questioned by THE TRIBUNAL

DR SCOTT: You mentioned your pricing model.

A. Yes.

DR SCOTT: Mr Cheyne clearly admired you and you moved with him. I just wondered, you have explained in your statement at paragraph 12 {C3/43/617} that your objective as regards pricing was:

"... to generate ... as high a margin as possible without materially reducing the overall volume of tobacco sold. In pursuing this strategy I was indifferent as to which manufacturers' products I was selling. I was maximising my margin on the basket", and so on.

Then you explain in 14 that you developed this pricing model, which was quite sophisticated, and took into account the amount of bonus support on offer. Then you explain the indicators against budget and margin as percentage of cash margin, the income stream and the turnover.

I just wanted to explore this a bit. What level of detail did the model encompass?

A. Right. It's difficult to explain a spreadsheet to you, but it was basically a spreadsheet or a series of spreadsheets, which I'll explain -- it's two years since I've -- although I developed them, they have obviously left when I left Somerfield.

What I did was to take each subcategory of tobacco product. So, for example, I would take the cigarettes, 10s, I would -- it's quite simple. I listed alphabetically the brands of whatever manufacturer. So my range of cigarette 10s from Gallaher, Imperial, BAT whoever it was, down the left.

Across the top there would be a series of headings. One would be "share of sales": Share of sales relative to the company I was working for at the time. Then there would be -- probably I would say what the recommended price was, the benchmark. Then the price list price that we were paying, because at this stage we were buying through Palmer & Harvey, so I can't remember what it was. Then there would be, if there was a bonus involved, if we were cutting the price below recommended price.

Then there would be each of the tiers, a heading for each of the pricing tiers. Under each of those, I would enter the price. So say I was reviewing what they currently got, so I put in the current price. There would be a formula in there that would calculate cash profit and percentage margin, and that would be done for each tier, pricing tier, for each of the brands listed.

I then used the sales percentage to weight the margins, so you could work out what the overall margin for that tier was, for that group of products, and the overall margin for the company for that group of products.

Then you would -- I would produce a model for 20s, cigarette multipacks, cigars and so on. I knew the share at that stage those products had of the total business. So at the end of the day you could work out a total margin for the business.

So I would use that model (a) in terms of Threshers to understand what they'd currently got. When I got my feet under the table, I was obviously looking at opportunities to -- how could I enhance the margin further, given the stiff targets I was given by the company.

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

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

DR SCOTT: That's very helpful.

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

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

A. Yes.

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

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

A. Yes.

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

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

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

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

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

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

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

A. Yes.

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

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

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

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

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

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

THE CHAIRMAN: Any re-examination, Mr Howard?

Re-examination by MR HOWARD

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

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

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

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

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

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

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

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

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

strategy.
MR HOWARD: By the time you became involved, anyway, you have told us there were three tiers -- it doesn't matter at what stage they had gone to the three -- and that's what I wanted to be clear about: what was the strategy in relation to those tiers when you joined?
A. What, the definitive -- what the overall policy for those tiers was?
Q. Yes.
A. Roughly, there were a third of the shops in the top premium tier, which would be -- I can't remember the exact figure, say 6p above recommended price, and that would be on, say, cigarettes, and that would be across the range, no matter who the manufacturer was, unless you were doing a short-term promotion.
Q. Yes. Leave aside short-term promotion --
A. But the base was 6p. Everything would be sold at a premium.
The central tier sold literally at the published recommended price, and the third tier was the price-cutting tier where local competition demanded that, you know, you compete otherwise you would lose sales.
Q. Right.
A. At whatever level that was. Again, across the raft of

brands.
Q. Now, insofar as you were pricing below RRP in these 30 per cent or so of the stores, to what extent was it the policy to go to each of the manufacturers and to secure support from them for that effective price reduction?
A. Yeah, you would do that, yes. I mean, that was a function of the buyer: to negotiate as much money, as much support as you could from the supplier. It was in your mutual interest to increase the sales, yes.
Q. I think you mentioned tension between Imperial and First Quench. We have seen elsewhere for Imperial bonusing lots of supermarkets to be below RRP. Can you just explain what the tension is between Imperial's strategy, as you perceived it, and First Quench's policy?
A. Well, I think actually they understood -- not that they didn't understand to start with, but -- Imperial, as I saw it, wanted to compete with rival manufacturers on brands that they thought were similar, like Benson & Hedges and Embassy, and were keen to increase the -- the target was to increase market share, the sales.
To do that, the strategy, especially in the environment of decreasing advertising, they had less

tools in the box to achieve that objective. Pricing was one of the important tools for them. So it would offer incentives to retailers to lower the prices.
Whereas First Quench, the strategy was to maximise the margin without overall losing sales. So it wasn't necessarily saying "We need to increase volume overall, we want to increase our bottom line profitability, but we will price cut where it suits us". But in actual fact the tension -- although pricing was important, the tension was actually about how we displayed product, availability, display, and that was the area that ultimately both sides needed to address, which I addressed.
Q. As I understand it, you were telling us a moment ago when you were answering questions from Dr Scott, that you were purchasing -- when I say "you", sorry, First Quench was purchasing its cigarettes from P&H; did I correctly understand that?
A. Yes.
Q. As I understand it, you also told us that you were purchasing at the wholesale list price; is that right?
A. The exact Q rate? Yes, we paid Palmer & Harvey a Q rate, which was volume related, depending on how much volume, how many drops -- we paid Palmer~& Harvey a fee for distribution. So we paid -- the invoice price

was the price list price, and a fee was paid separately to Palmer & Harvey. The fee was not taken into account in my buying margin, it was a distribution cost, that was why it was treated separately.
Q. Then I think, as I understand it, you explain that, at paragraph 26 {C3/43/622}, if ITL had lowered its wholesale price to us at First Quench, you wouldn't have reflected that in your retail price unless ITL had done something?
A. Yes.
Q. Right. Now, if we consider the position before a promotional bonus, can you just explain this to me: insofar as one observes the RRPs, your policy, would your policy in any way distinguish the position of the different manufacturers?
Sorry, I haven't made it clear.
If the RRPs of Imperial have a brand at £4, Gallaher has a brand at £4, BAT, Rothmans, have a brand at £4, forget whether they are competing brands or whatever, they are just each priced at RRP of £4, did your policy apply any different strategy to those different brands?
A. No.
Q. Or did it just add on whatever it is or subtract whatever it is?
A. It added on or took away a set number of pence from the

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

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

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

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

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

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

A. Sorry.

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

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

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

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

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

handrolling tobacco, I suppose that is, HRT --

A. Yes.

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

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

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

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

Q. Right.

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

Q. Yes.

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

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

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

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

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

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

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

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

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

Q. If we then go back to 46, you were asked about subparagraph (e) at the bottom of the page {D16/46/101}. We can see it's actually another item that's been discussed between Fiona Gittus and George Byas, and you were asked about "you will adjust cigar pricing and achieve parity for ITL and Gallaher brands". I think you said you don't know the context of what was being discussed.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

didn't achieve the pricing at the competitive levels required by ITL, ITL would be entitled to reduce or withdraw the bonus?

A. I think -- well, I know you are misinterpreting that.

The change in bonus, if you go back through correspondence in First Quench, the bonus was paid on all volume. And as they put more and more prices up to RRP and above, our level of bonus went down. So when it says "competitive", it means relative to the RRP.

I think at this point they were receiving a bonus on 30 per cent of the volume. Going back to the start of the folder, it was on 100 per cent, but as Threshers' prices moved up absolute terms, the bonus level went down. So it was then monitored against the stores selling cheaper to consumers and that's what adjusted the bonus.

Q. Can I press you on this? Go back to the trading agreement, please, which is tab 48 {D16/48/104}.

A. Okay.

Q. So we have on that first page, in the section headed "A. Bonus levels, pricing and strategy support", the two notes at the bottom of the page, the two numbered notes.

Can I take this in stages. As I read it, A, right, in this letter, deals with bonus levels; is that correct?

A. Point A does deal with bonuses, yes.

Q. Am I also right in thinking that the words "pricing and strategy support" indicate what these bonus levels relate to?

A. The pricing within the stores, yes.

Q. So part of this is strategy?

A. Yes, whether it's Imperial's strategy and First Quench's strategy.

Q. When we get to note 1, we have:

"ITL pricing strategy to be adhered to on all brands including 10s."

Now, am I right in believing that that means that ITL pricing strategy is to be adhered to on all brands, including 10s?

A. That was our hope, yes.

Q. And that is a condition attached to the payment of the bonus levels?

A. But the bonus was only paid on the 30 per cent of volume that was sold in the discount tier, so there was no bonus attached to the other 70 per cent of the volume at all. So there was no conditions on almost -- 70 per cent of their volume. There was no payments attached to that at all.

Q. I am not actually talking about that, because what I am trying to get at is this: as I read it, at the beginning

of A, you have bonus levels, and you specify what these -- when I say "you", it's ITL -- bonus levels.

So we can see, for example, Embassy No 1 and Regal Kingsize and promoted premium brands, and then alongside it there it says "all at", and then there is an amount per thousand. So that's a bonus level?

A. On the 30 per cent of volume sold at a discount to the RRP, yes.

Q. Then I look at note 1, and note 1 says:

"ITL pricing strategy to be adhered to on all brands, including 10s."

A. That's what it says, yes.

Q. And that's a commitment made by First Quench?

A. It's a commitment that wasn't followed through fully, but yes, a commitment, yes.

Q. Because they signed the trading agreement?

A. Yes, they did.

Q. Then we get to paragraph 2, where it says:

"These support levels may be reduced or withdrawn in the event of brand pricing not achieving the required competitive levels."

Now, am I right in believing that that means that the support levels may be reduced or withdrawn in the event of brand pricing not achieving the required competitive levels?

A. No, because the competitive levels which is talked about in other documents in the file was relative to the RRP. First Quench did receive those sort of same bonuses on all their volume, and the bonus percentage paid only reduced down when they chose to sell above RRP.

So where it's saying "competitive levels", it's relative to the RRP, ie a discount to the retail price, not --

Q. Okay, so you had actually jumped ahead of me, because what you are saying is, as I understand it, the first sentence of note 2 means what it says?

A. It says that, but it wasn't delivered, yes.

Q. No, no, it means what it says. Okay, are we agreed on that?

A. I assume so, yes.

Q. Well, are we or aren't we?

A. It says that we would like our pricing strategy to be achieved in their stores, yes.

Q. It says that support levels may be reduced or withdrawn in the event of brand pricing not achieving the required competitive levels, and that's what it means?

A. No, it doesn't. That's referring --

THE CHAIRMAN: Well, can you say what you think "required competitive levels" relates to?

MR LASOK: That's the next question.

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

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

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

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

are purely related to the discount tier, First Quench, relative to the RRP.

They weren't -- it was like they had a lower cost price for the product, but this, the trading agreement, has nothing to do with the cost price of a product.

I may not have answered the question exactly, but it's -- maybe I am making it more complicated than it needs to be, for which I apologise.

MR LASOK: Maybe I ought to retrace my steps slightly, because I was going to approach this in a slightly different way.

MR HOWARD: Could I suggest -- because there is a simple question, I don't think this is really controversial. We seem to be spending a lot of time. Perhaps if you simply ask Mr Culham by reference to the first sentence of paragraph 21: in the event that that happened, which is ITL had a different reduction to RRP to Gallaher, so in other words Gallaher has 8p and Imperial has 6p, what then?

MR LASOK: With all due respect, we haven't got to that point.

What I would like to look at is paragraph 22, the first word, "this" {C3/35/409}. What in your witness statement does the word "this" refer to?

A. Well, the only thing that could be withdrawn was the

trading agreement money, if the absolute price moved above RRP. There was nothing else we could withdraw.

Q. When you said in the last sentence of paragraph 21, "relative shelf prices", right, that doesn't apply in the context of what you are saying in paragraph 22?

A. The only thing that could be withdrawn was the bonus paid on the tier selling below RRP. The lower wholesale price was transferred to their business, whatever they -- they could sell it for, well, any price they chose. And because that was the wholesale price that we supplied all retailers at, we couldn't do anything about that. They would get that benefit anyway.

Q. Why in the last sentence of paragraph 21 did you include the reference to relative shelf prices?

A. Well, it's -- I can't remember. It's over a year ago I wrote the document, so I don't remember exactly why I used those phrase of words, so apologies for that.

Q. Did it reflect your recollection at the time?

A. At the time of writing this document or at the time I was handling the account?

Q. At the time when you wrote your witness statement --

A. Yes.

Q. -- paragraph 21 and paragraph 22, were they accurate?

A. Yes, they are, yes.

Q. Thank you. Right.

Now let's look at paragraph 13 {C3/35/408}. In paragraph 13 you tell us what the phrase "pricing strategy" means. Okay?

A. Can I read it? (Pause). This is where we were offering additional promotional support on mainly tactical bonuses to achieve pricing.

Q. Now, I am interested in the bit about the policy of not increasing the retail prices of ITL's products above identified differentials compared with the prices of identified brands of competing manufacturers. That's the policy, isn't it? That's the strategy?

A. That's our objective, yes.

Q. That's your objective. So if we look at the trading agreement in tab 48, and we look at note 1 {D16/48/104}, and the phrase "ITL pricing strategy to be adhered to on all brands", what we are to understand by that is that First Quench is, as you put it in paragraph 13, not to increase the retail prices of ITL's products above identified differentials compared with the prices of identified brands of competing manufacturers; is that correct?

A. That was our objective, yes.

Q. Right. But wait a minute, the question is whether that's what note 1 is about. I'll repeat it. When note 1 says:

"ITL pricing strategy to be adhered to on all brands", right?

Does that mean that First Quench is not to increase the retail price of ITL's products above identified differentials compared with the prices of identified brands of competing manufacturers?

A. That was our objective, yes.

Q. The question is: is that what note 1 means?

A. Well, yes, it would be linked in with that, yes.

Q. Does it mean it or doesn't it?

A. Well, it relates -- note 1 would cover the point you made, yes.

THE CHAIRMAN: Does the term "pricing strategy" as used in note 1 mean the same as you have defined "pricing strategy" to mean in paragraph 13 of your witness statement?

A. I think it's actually -- obviously note 1 is a lot shorter, so if it had been expressed more fully, it would hopefully be -- well, it would say the same in my paragraph 21.

THE CHAIRMAN: Paragraph 13.

A. Sorry, yes, paragraph 13.

MR LASOK: In order to identify what these identified differentials are, we have to go to another source, don't we, because we don't see them identified in the

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

example, £2, and the published Q rate for that product would be X. That's all we would know.

THE CHAIRMAN: The question you are being asked is rather simpler than that. You have maintained that the aim, or one of the aims of the agreement, the differentials agreements, is to ensure that lower ITL prices are passed through to the consumer. Mr Lasok is putting to you: well, that doesn't really work, because the agreement allows for parity between two brands, even if actually the Richmond brand is cheaper.

A. Yes, because our objectives were based on the RRPs, because we didn't know the total cost prices for anyone else. Our agreement, ie the Richmond no more than Dorchester, was based on the published RRP.

MR LASOK: So if we look at it in that light, with ITL's object -- just looking at it objectively speaking, I am not talking about subjective intentions, I am just talking about the nature of this requirement, and the requirement -- I'll remind you -- is a requirement to price Richmond no higher than Dorchester. The ordinary and natural consequence --

A. Sorry, is there a blind?

Q. I have the same problem from time to time. I have got out of it because I am standing up. Could somebody press the magic button?

A. Sorry.

Q. Yes.

A. Thank you.

Q. So we have got the situation in which the requirement is to price Richmond no higher than Dorchester. It doesn't actually give ITL any benefit in terms of passing on a cost price advantage, but what it definitely does is kill off any chance of Gallaher achieving a pass-through if it has got a more competitive net cost price. That's, I think, where we have got to.

Now let's look at what happens when there are changes in prices. We look at it from the perspective of -- I am going to change it slightly -- a requirement or an agreement or a commitment, however you call it, that the retailer should price at parity between Richmond and Dorchester.

So would you agree with me that if that's the scenario, when the shelf price of the Gallaher brand goes up, ITL's objective is to ensure that the price of the ITL brand goes up to follow the rise. Again, to be precise, if the shelf price of Dorchester goes up, the shelf price of Richmond ought to go up.

A. If the retailer changed their strategy, is that what you are saying? What's the question?

Q. No, you have an agreement with the retailer or

a commitment from the retailer that the retailer will price Richmond at parity with Dorchester.

A. Or no more than, yes.

Q. Well, I'm putting it to you as parity. We can deal with the no more than later. So we will take it at parity.

The reason why I am putting that to you is because we have a lot of documents, as you know, in which we see ITL saying things like "we are paying for parity", "please move prices to match". So that's the hypothesis: Richmond is to match Dorchester in shelf prices.

So isn't your -- ITL's -- expectation that if the price of Dorchester goes up, the price of Richmond should go up?

A. What would be the circumstance for Dorchester going up?

Q. All right, let's take it in stages. Let's suppose that the retailer, off its own bat, has looked around the market and it thinks that it's got headroom to increase the price of Dorchester, but it hasn't increased the price of Richmond. It's got the headroom to do so, because both products are in the same market segment, they are all constrained by the same competitive constraints, so what's good for one is good for the other, but the retailer hasn't put up Richmond.

A. That would be taken as a benefit, because our agreements

and the way we operated was no more than. So if they had chosen to put Dorchester up off their own bat, their own strategy, but not Richmond, that would have been taken as an added bonus, a benefit.

Q. You see, the starting point is that the peculiarity of an agreement that doesn't give ITL the benefit when ITL has got a more competitive wholesale price, so if the agreement isn't structured in such a way as to give ITL the benefit of a more competitive wholesale price, why are we supposed to believe that it's structured in such a way as to give ITL some other competitive benefit?

A. Sorry, what's the question? I was explaining if the retailer put Dorchester up but not Richmond, we would take that as a benefit. If Gallaher's had had an MPI, that would have been Dorchester above Richmond, or if there had been a Budget increase generally, they would both go up at the same time.

Q. You see, the point I am putting to you is this: that you have structured a requirement that you have sought to justify on the basis of the pass-through of net cost prices, more competitive net cost prices, and you are launching the argument that this is ITL's strategy, the purpose is to be more competitive vis-a-vis Gallaher. But when we look at this justification, I've put it to you that it just doesn't work. And if it doesn't work, where do we get the idea from that when you move onto shelf prices, ITL's intention is to be cheaper than Dorchester at all? Because if you wanted to be cheaper, you would never have structured these arrangements in this way at all, because your starting point would have been: if we, ITL, have got a lower cost price, we want that to pass through to the customer, and so we would be reducing the -- we would be ensuring in some way that the retailer passes through; you wouldn't have entered into these arrangements involving parities and differentials at all, would you?

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

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

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

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

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

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

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

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

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

A. No, completely the opposite.

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

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

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

A. We were competing in the market with Gallaher to try and encourage consumers to buy our products, and Gallahers were our competitors in the marketplace.

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

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

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

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

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

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

A. Yes.

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

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

Q. But that's not what you get from per using the RRPs, is it?
A. The RRPs, for example, for Richmond and Dorchester were similar, if not the same, most of the time, and that was where our base strategy was. And our objective was to have Richmond no more than Dorchester. If it was cheaper, that was treated as a benefit; if it was dearer, my objective was to try and encourage the retailer or spend tactical bonuses to bring Richmond down so it was no more than Dorchester. But if we were -- if Richmond was cheaper, that was a benefit.
MR LASOK: We can come to tactical bonuses -- I see now it's 1 o'clock -- after lunch.
THE CHAIRMAN: Yes, thank you.
Thank you very much, Mr Culham. We will take a break for lunch now, and come back at 2 o'clock, and over that lunch break you mustn't discuss your evidence with anyone. Perhaps you would like to pop out at the back now, there are some logistical things we need to discuss.
(In the absence of the witness)
Discussion re timetable
THE CHAIRMAN: As far as timing is concerned, we would need to complete Mr Culham's cross-examination this afternoon.

MR LASOK: We will certainly do that, I would have thought by 3.30. I will obviously try and do it more quickly than that.
THE CHAIRMAN: We might then be able to fit in his re-examination this afternoon as well. Let's aim to do that, because tomorrow morning we can not start earlier than 10.30, and if we then have some time, say half an hour, for your response to our questions, that gives us the rest of the day for Mr Wragg.
So if we say you can complete your cross-examination of Mr Culham at, say, 3.45, and then we would have our break then and then re-examination for the rest of this afternoon, Mr Howard?
MR HOWARD: Yes. I think Mr Lasok was saying he would finish at 3.30.
THE CHAIRMAN: Thank you. We will come back at 2 o'clock.
(1.02 pm)
(The short adjournment)
(2.00 pm)
MR LASOK: Mr Culham, before lunch we had actually moved on into some general questions, but for the sake of tidiness I would like to finish off on First Quench.
To that end, I just wonder whether you could look at paragraph 25 of your witness statement, please {C3/35/409}. Here you are referring to the

ITL/First Quench trading agreement that was in force from 1 October 2000, and you say that that trading agreement was fundamentally identical to the one that you were discussing above.
I wonder, in that connection, whether you could turn to tab 20 {D16/20/40}. What you have is a handwritten note, but after that you have got an explanation of the new trading agreement that is to be found in the letter dated 19 October 2001. If you go to the third page of that letter {D16/20/43}, in my copy somebody has written in manuscript some pagination in the bottom right-hand, which is 1, 2, 3 and so forth of 6. If you go to 3 of 6, you have a description of the objective of the new trading agreement, and it says that it's to ensure that ITL's strategies are achieved both in actual levels and differentials measured against Gallaher competing brands. (Pause)
That was reflected in the later trading agreement that we have seen, wasn't it?
A. Well, it says in there also bonus paid on price competitive tiers, which is what I said earlier on.
Q. I am looking --
A. The trading agreement, this wasn't actually formally agreed, I seem to remember. Reading the note from Michael Williams, I don't think that was the final

trading agreement.
Q. The objective of the trading agreement is set out there, and in relation to pricing it includes the bit that says:
"To ensure ITL's strategies are achieved both in actual levels and differentials measured against Gallaher competing brands."?
A. I agree it says that there, yes.
Q. That, so far as you recall, was what was happening at the time when you were running the First Quench account?
A. We were looking to achieve our pricing differentials relative to the RRPs of Gallaher products.
DR SCOTT: Sorry, can I ask a quick question relating to this? This is dated 19 October 2001. In paragraph 25 {C3/35/409}, it says "in force from 1 October 2000".
MR LASOK: That's my mistake. I think paragraph 25 refers to the earlier one, which is in tab 7.
DR SCOTT: Ah, right. Sorry, that's why I was confused. Thank you.
A. Sorry, so which point is this trading agreement ...?
MR LASOK: I made a mistake.
A. Sorry.
Q. What I referred you to in your paragraph 25 doesn't relate to the first trading agreement, which is in tab 7, but it relates to the second trading agreement

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

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

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

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

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

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

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

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

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

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

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

A. Yes.

DR SCOTT: They then announce a price hold.

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

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

A. Well, I didn't, because we didn't have an MPI. Therefore, our brand was no more expensive than Dorchester.

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

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

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

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

DR SCOTT: Right.

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

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

A. I believe that's correct, yes.

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

A. We have the same document.

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

with T&S?

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

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

A. Yes, it is.

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

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

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

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

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

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

"The overall requirement is that ITL products are treated no worse than equally in terms of selling prices compared with other manufacturers' similar products." {D29/40/132}

On the next page {D29/40/133}, we have it saying:

"A full requirement is shown on the attached listing."

Then if you go to the attached listing, the pagination in my copy at any rate is the stamped number at the bottom right, but if you go to page 290 {D29/40/136}, you have the price requirements schedule, and for present purposes it's probably sufficient if we look at the fourth item down, which is "Superkings". Do you have that?

A. I have, yes.

Q. So you have a list, "Superkings, Superkings Lights, Superkings Menthols, Superkings Ultra, Raffles, Raffles Lights", then there is a colon and we have the 20s at least no more than the price of Berkeley, and the 100s also at least no more than the price of Berkeley.

Okay?

A. Yes.

Q. Fine. Then if we go back to page 287 just for the sake of completeness {D29/40/133}, and go to the fourth paragraph from the top, we have a paragraph that says:

"T&S head office will correct any errors highlighted by ITL of price tiers."

I interpolate to say that that relates to the price files which had to be supplied by T&S to ITL.

A. If there were errors in them, yes.

Q. Pardon?

A. If there were errors, yes.

Q. Then the contract continues:

"... and allow ITL to react to pricing activity undertaken by other manufacturers, although ITL may not take any action."

So we have called that an opportunity to respond clause. Okay so far?

A. Yes, yeah.

Q. Let's go to tab 46. Tab 46 is dated 11 June 2002, and at this point we are very shortly, I think, after the making of the trading agreement that we have just looked at. I don't think that we have a date for that trading agreement, but certainly the chronology in the bundle tends to suggest that we are now after the trading agreement.

A. Six months later, yes.

Q. The 11 June 2002 letter at tab 46 is a letter from you. Could you have a quick read through, please.

(Pause)

Okay, so what we see here is the same kind of letter that we saw in the First Quench file at annex 16, tab 29. Because what's happened here is that this is now the Gallaher MPI which was to take place on 25 June, and ITL decides not to follow, and so you write to T&S Stores revising the differential requirements and that the purpose of that is to ensure that no ITL brand increases as a result of the Gallaher MPI?

A. I was seeking to keep our prices down and change the differentials. As part of the original trading agreement, it actually said "We can alter it if the relative RRPs change", so that's what I was doing, what the agreement said.

Q. If you look at the next page {D29/40/150}, you have the revised price requirements, and here it's specified as being the price requirements post-Gallaher MPI 25 June 2002.

If we look at the fourth paragraph at the Superkings bit, we can see that that's changed from a "at least no more than" to "20s packings at least 6p less than the price of Berkeley", and the 100s packings at least 30p less than the price of Berkeley?

A. Yes, the differentials had changed because the RRPs had changed.

Q. The next document is tab 47 {D29/47/152}. This is

a letter from you to the buying manager at T&S. I am interested in the bit at the bottom of the first page, moving onto the top of the -- well, moving onto the next page. But I don't mind if you read the entire letter, if that's what you would prefer.

(Pause)

If we just have a look at the bit on the first page headed "Retail prices", you give an explanation of this letter in paragraphs 128 and 130 of your witness statement. Perhaps the better thing to do is to go back to what you say about it. If you go back to your witness statement at 128 {C3/35/432}, and if you could just read paragraph 128 to yourself, please.

(Pause)

Now, in the middle of paragraph 128 you say that you had assumed that Gallaher was running a promotion with the consequence that Superkings and Raffles were more expensive than Berkeley, and you wanted Superkings and Raffles to be at the same price as or cheaper than Berkeley, so you offered a promotional bonus; okay?

A. Yes, we had done, yes.

Q. You see, the thing is we have just seen in the previous tab that that wasn't the case, because you had altered, or at least you had informed T&S of an alteration in the pricing requirements, because in the second page of tab 46 {D29/46/150} we have seen that what had been a -- I'll describe it as a parity, but it was expressed as a "no more than", had been altered to 6p less than or 30p less than, depending on whether it was 20s or 100s packings.

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

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

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

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

Q. Not more than?

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

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

A. Correct.

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

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

A. That's correct, yes, because the RRPs had altered. Therefore, the differential objective had altered, yes.

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

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

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

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

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

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

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

We couldn't advise before the Gallaher MPI what we were going to do because we didn't know what Gallahers were going to do.

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

a result of a Gallaher move?

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

Other retailers in the past have --

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

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

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

A. Correct.

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

A. Correct.

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

the Gallaher price doesn't actually increase?
A. In the multipack they actually put the price down.
MR HOWARD: That was the point. The flat price -- if I can just make it clear, because it will be a lot quicker. That's what Mr Lasok hasn't understood. If you look at the letter it's perfectly clear that what has happened is Gallaher, as well as holding the price, have reduced price, so that the same price applies across a number of tiers. And that's why then these cigarettes get priced also reduced in order to match that activity by Gallaher, and that's why there is a bonus. It's just misconstruing the letter, I am afraid.
MR LASOK: I think that there is a misconception as to what the underlying policy is, but for the Tribunal's note, one document showing the Berkeley price hold is the one at annex 27, tab 29.
But if you look at, for example, annex 28 --
MR HOWARD: Can I say there is not a dispute about this, it's just that two things were happening: one, Gallaher had a price hold; and two, they put down the prices in these tiers.
THE CHAIRMAN: Let's just see what was happening. I think that's what Mr Lasok is going to show us.
MR LASOK: I am going to give an example.
If you have 28, and go to tab 61 {D28/61/125}, this

is dated 3 July 2002, and what you see is it's a letter to Safeway. It wasn't written by you, but if you look at the fourth paragraph, there is a reference to the fact that Superkings, Berkeley and Raffles should be at the same price, at 4.10/4.13.
The point is simply this: that if one thinks back to the trading agreement, the trading agreement specified a price for Superkings and Raffles that was no more than the price of Berkeley. As a result of the Gallaher MPI, which altered the RRPs and which ITL was not following at that stage, ITL found it necessary to send round a letter to a number of the retailers telling them that the strategic pricing requirements had altered from a "no more than" to a differential.
But the problem was that that was not a change in the underlying policy. That was a change designed to prevent the retailers from altering the ITL price as a result of the Gallaher move. The underlying policy remained parity between Superkings and Raffles on the one hand and Berkeley on the other. In fact, the revised strategic price requirements were intended to achieve that parity in shelf prices, but then the complication was that there was a Gallaher price hold.
Then things began to get confused. But the end result here was that they write round -- here to

T&S Stores -- and they seek to get parity again because, in the meantime, things have got out of line as a result of this peculiar combination of the Gallaher MPI, which is followed by a Gallaher price hold for certain brands like Berkeley, which ITL doesn't spot. So it alters the strategic pricing requirements which, in retrospect, it didn't need to do and which it, therefore, has to correct.
So the point about this is not about whether or not, you know, these multipacks are on a particular offer; it's about the underlying policy which remained a policy of parity.
THE CHAIRMAN: So this was not a situation, as we saw, where Richmond was repositioned in the market?
MR LASOK: No, it wasn't.
THE CHAIRMAN: The June 2002 letters were not a repositioning of Superkings to be a cheaper brand than Berkeleys, it was a temporary measure to last one didn't know how long, unless and until ITL had its own MPI to bring the price of Superkings back up?
A. We didn't have an MPI, so therefore the published RRP for Berkeley was 6p above Superkings. I think it was 6p.
THE CHAIRMAN: But if Berkeley didn't go up because of the price hold, you didn't actually want Superkings to be 6p

cheaper in the long-term?
A. No, we weren't seeking that, because our published RRP -- and I don't know what it was at the time -- didn't change. And the fact that Gallaher's did a price hold, tactical bonus, I don't know what --
THE CHAIRMAN: I think we are all agreed, therefore, Mr Lasok.
DR SCOTT: If one looks across at the Gallaher correspondence, there appears to have been a certain amount of confusion going on there, because what 29 says is:
"Is the RRP staying the same or are you bonusing back the difference to us by retro? Can't imagine that you will reprint the prices, so I expect the retro to change."
And back comes the response:
"The RRP is going up as per the price list. We will bonus back the difference. I will go through everything on Thursday."
MR LASOK: There are other Gallaher documents that make it clearer in relation to some of the other retailers, because I think in the case of, from memory, Asda and Morrisons, it's a much simpler email which sets out which brands were the subject of the price hold.
THE CHAIRMAN: Right. So let's carry on.

MR LASOK: Looking at this letter in the second page, though --

A. Sorry, which letter? Because I have several open.

Q. I am terribly sorry. You can put away 28. Sorry, 29 you need to have open.

THE CHAIRMAN: We are looking at tab 47 of annex 29, page 2.

MR LASOK: If we look at this first page again {D29/47/152}, before we got to the bit about Berkeley Superkings, but immediately under the heading "Retail prices" you thanked T&S Stores for the latest price sheets and you say:

"My office is currently checking to ensure the correct differentials are maintained as part of our business plan."

So am I right in thinking that you were checking to ensure that the ITL prices and the Gallaher prices respected the differentials?

A. Yes, or better than, yes.

Q. And --

A. And because T&S had 27 tiers it was quite a cumbersome exercise.

Q. Yes. Then on the next page {D29/47/153} the first two lines are concerned with a change in the price of the five SKUs. Those will be the ones referred to at the bottom of the previous page, I think? (Pause)

Am I right in thinking that the reference to "changing the above five SKUs to 19.99" refers to the five SKUs listed at the bottom of the first page?

A. I certainly believe so, yes. It's to reduce the price of those, yes.

Q. Then when we get to the second page, the next paragraph but one you say:

"On a quick look I also noticed the following prices should be amended to bring Raffles into line." {D29/47/153}

You refer to a meeting in May. Then you set out the prices, and so you have the One Stop tier of shops. Those were the most expensive, were they?

A. Yes, generally.

Q. Then you have the CTNs and the Supercigs, and the Supercigs were the cheapest, weren't they?

A. That's correct, yes.

Q. Then you say:

"Where no price is shown, the correct differentials are already in place against Berkeley Superkings."

So this is an instance of you asking them to amend the Raffles prices to bring them into line with the differentials against Berkeley?

A. To bring them down so they are no more than Berkeley, yes.

Q. From that point, if we go to tab 51, we get to a letter from you dated 6 August 2002 {D29/51/165}. Oh, no, it's not a letter from you, it's a letter from Nick Law. Who was Nick Law?

A. He was an executive -- like a junior account manager in the department, and I was actually on holiday, I think, at this time.

Q. Is this the kind of thing that he would have written on instruction from somebody?

A. With regard to the price increase, we would have all been told there was a price increase, yes.

Q. In fact it's a letter very, very similar to the one we saw in relation to First Quench at annex 16, tab 30. The Tribunal has seen other letters of this nature before, so this is quite common as a letter written by ITL at this time.

Now, could you just read this letter, please. I am not asking you to read it out loud.

(Pause)

So if you just run through this letter {D29/51/165}, the second heading on the first page is "Differential update", and when he talks about the ITL price increase on 2 September, he is talking about the announcement that there would be an MPI taking effect on 2 September, isn't he?

A. There would be one taking effect on the 2nd, yes.

Q. So he then says that he has enclosed revised differential requirements, which he describes as being:

" ... as part of the business plan payments."

We don't have a copy of those differential requirements, but would they be the same as the ones that we saw, for example, attached to tab 46? The same nature, I should say.

A. Yes.

Q. That too is a letter to you, it's headed "Price increase differentials update" {D29/46/149}, and then we have on the second page a price requirements sheet.

A. That's the one with the post-Gallaher MPI.

Q. When we get to the letter at tab 51, which is also about a differential update, and also refers to the revised differential requirements, would there have been a sheet like the one --

A. Similar, but obviously the figures would be different because we were having an MPI, and some of the differentials had changed.

Q. Then he sets out a number of points that he would like to draw T&S' attention to. At the bottom of the first page there is a reference to Embassy and Regal, and this was an increase in Embassy and Regal which he says will entail -- the differential between these brands and

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

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

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

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

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

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

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

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

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

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

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

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

second holepunch "Classic, all packings, at least no more than the price of the same Hamlet packing".

The last item is bands 1 and 3: Drum, 12.5, and you wanted that changed, or at least you wanted that the same as Amber Leaf. Again, if we go back to the price requirements sheet in tab 11, Drum is mentioned by the second holepunch, and for Drum all packings had to be at least no more than the price of the same Amber Leaf packing.

So this is a situation, isn't it, in which what has happened is that T&S has not complied with its agreement with you, with ITL, because its pricing has not corresponded to the pricing requirements in the contract, and you are drawing this to the attention of T&S and asking them to make the appropriate changes, whether that means a change in the price of a Gallaher brand or a change in the price of an ITL brand, and whether prices are going up or down?

A. The whole background to this was T&S took over Day & Nite stores, which were based somewhere in the northwest. When they took over the business, the Day & Nite pricing policy was not in line with what T&S' policy was. So T&S were moving towards integrating the Day & Nite stores into T&S' own pricing policy.

All I am highlighting here is where stores --

ie this is data from store visits, not from a price file, aren't in line with what T&S head office thought or wished it to be.

Q. I put it to you that that explanation is implausible, because it's quite clear that you are asking them to price in line with the terms of the agreement?

A. Well, I've actually asked them to -- I had noticed these differential errors, so they are out of line with our requirements, but they are also not in line with what T&S were doing in their own stores.

THE CHAIRMAN: How do you know what they wanted to do?

A. Because the first part, this first paragraph, T&S had informed me where their outline pricing was going to be, and this didn't seem to be in line with what their pricing policy was meant to be.

DR SCOTT: The suggested price list mentioned, is that a price file that was being prepared by ITL or a price file that they had prepared?

A. The background to it was Day & Nite had several -- I don't remember how many stores --

THE CHAIRMAN: Never mind about the background to their pricing decisions.

A. The T&S buyer and myself sat down to see where they were going to -- sorry. They wanted investment from Imperial going forward in terms of cut price contributions and

ongoing business plan. So therefore, the T&S buyer had decided to put Day & Nite stores into T&S tiers, and this is highlighting where it hasn't actually happened. And obviously I don't know which tier they were in.

MR LASOK: Well, Mr Culham, you deal with this document in paragraph 123 of your witness statement {C3/35/431}. Maybe you should have a look at that. Do you have 123?

A. Yes, I have. (Pause)

Q. As I read that paragraph, you say in the second sentence that your letter was pointing out certain instances where the prices were out of line with the differentials?

A. Yes. In the same letter, it's asking for the price list, because we have had a discussion over what T&S pricing was, but I hadn't actually got a copy of what the T&S price file was. So in the letter of tab 19, I am actually asking him to let us know what his price file -- what the correct prices were.

Q. The oddity is that you talk in that second sentence of certain instances where the prices of ITL's products were out of line, but the very first brand that we see is B&H.

A. I am just quoting that as a benchmark. The thing that's out of line is the Regal Kingsize.

Q. Then you say in paragraph 123:

"These were presumably errors, and therefore I asked T&S to correct them."

So am I right in thinking that at the time when you wrote your witness statement you didn't know whether they were errors or not?

A. They were errors by store managers that aren't in line with T&S head office policy, because this is --

THE CHAIRMAN: And that policy, as far as you were concerned, was to comply with the differentials?

A. Yes. So this -- these four or five prices being quoted here are what we found going into stores, and it was different to what the T&S buyer had told us should be seen in the stores. So that's why I am highlighting it. And yes, it wasn't in line with our objective --

THE CHAIRMAN: And they had agreed with your objective, as far as you were aware?

A. Yes.

THE CHAIRMAN: Maybe this is a semantic difference rather than an actual difference.

MR LASOK: But it's something that sometimes one has to pursue in order to get an answer.

Then you say:

"Of course it was up to T&S whether to make my suggested amendments."

But your language isn't in that form, because what

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

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

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

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

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

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

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

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

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

Q. Yes, to parity with Dorchester?

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

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

Q. Well, these are moves upwards.

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

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

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

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

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

Q. Right. Let's move to --

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

MR LASOK: Yes, we are.

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

(Pause)

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

A. Yes.

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

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

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

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

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

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

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

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

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

Q. Okay.

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

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

A. As it says, I was on holiday.

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

A. Yes.

Q. This is where the prices go up?

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

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

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

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

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

A. No, was that when Gallaher's had the earlier MPI?
Q. That's when Gallaher has the earlier MPI, then you alter the strategic pricing requirements.
A. We changed our pricing objectives because we hadn't had an MPI and we wanted to lower cost price -- the lower cost prices to still be reflected in better value on the shelf.
Q. Are you tripping out something that you have learnt by heart?
A. No.
Q. If an ITL price increase took place, the Gallaher reaction, or rather the reaction in terms of any change in Gallaher's shelf prices would depend on what communication you were sending to the retailer, because if you were telling the retailer "This is a widening of the differentials", the expectation would be that the retailer would do nothing with the Gallaher price, unless Gallaher had told the retailer to do something?
A. When we had a price change we didn't tell the retailer what to do with Gallaher products. It would be up to Gallahers to decide.
Q. Yes, but if you didn't do that, that is to say if you didn't tell the retailer that you were widening the differentials, the expectation would be that the retailer would do something to the Gallaher price, and

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

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

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

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

A. If everything happened correctly it would be spot on and it would happen, but it never seemed to happen that way. And that's why we called them errors rather than you have done something deliberately wrong. It was, you know, sometimes it was a retailer had deliberately taken a decision on pricing, but in most cases, like using T&S as an example, they had over 3,000 prices in their system just for tobacco, and errors do occur.
The same at Thresher. If what Cynthia said about starting with the RRP as the base, in theory, as our differentials were nothing different to the RRP difference, if that happened, then yes, it would happen. But it never happened everywhere all the time.
DR SCOTT: So in essence, if all went well the P&Ds would be in place?
A. If the retailer's strategy was straight to use the RRP to then make their decision, if the retailer's strategy was to say "I want to make X percentage margin" then obviously that wouldn't happen.
DR SCOTT: No, I mean, her evidence was that they were seeking to price in relation to the RRP.
A. In which case it should happen, but there again, having been an account manager for many years, that's the theory, but it doesn't happen in practice.
DR SCOTT: So it was still worth having an agreement to try

to turn the theory into practice?
A. Yes.
DR SCOTT: Thank you very much, that's helpful.
Re-examination by MR HOWARD
MR HOWARD: I will try to limit this.
Mr Culham, what I want to do is to ask you some questions about how the contracts here worked. But I think probably the easiest way to do this is to go to some examples and then see how this fits in with the way the contract worked and some of the suggestions being made to you.
Could you look at annex 29, and let's start with T&S. I am just going to pick out some examples, because we haven't got time to go through all the correspondence. If you go to tab 16, first we see this letter was dealing with Lambert & Butler {D29/16/48}. Can we just focus on that for a moment. So we see that Lambert & Butler is being reduced to 3.59 in August tiers, and you pay a bonus for that?
A. That's correct, yes.
Q. Then what we see in respect of Richmond, in the second paragraph under "Richmond", the price of 20s in all Supercigs is to move to a maximum of 3.39, equal to Mayfair and Royals. And then in CTNs and C-Stores, the maximum price would be 3.34, with extra bonuses.

So it looks as if in respect of Richmond, is this right, that you are reducing the price as a result of what Mayfair and Royals have done?
A. That's correct, we were offering tactical bonuses.
Q. The tactical bonus in respect of Lambert & Butler and JPS, is that a counteraction to what Gallaher has done, or is that you taking the lead yourselves to get a price advantage?
A. I can't recollect exactly. My expectation is probably -- was in reaction to Mayfair, to a Gallaher activity.
Q. Okay. Insofar as, therefore, there has been Gallaher activity whereby Gallaher have done something to reduce here T&S to rules the price of their brands, firstly were T&S entitled to reduce the retail selling price of Mayfair and Royals where Gallaher reduced their wholesale price?
A. Yes. Yes.
Q. Where they did this, where they reduced the price of the Gallaher brands as a result of Gallaher taking action to reduce their wholesale cost price, whether by bonusing or otherwise, did you ever object to their having a lower price or a price that didn't accord with your differentials?
A. No, never in over 20 years as an account manager, never.

Q. And you were dealing with four accounts, I think, that we have looked at here?
A. Four that we have looked at over this case, but I've dealt with 25 different accounts over the years.
Q. Have you ever, in relation to any of those accounts, suggested to a retailer that it wasn't entitled to price a Gallaher or a BAT product more advantageously or disadvantageously, from your point of view, if the cost price to them of that product was lower than yours?
A. No, never. Never, ever in over 20 years.
Q. What would you have expected their reaction to have been if you had sought to raise that?
A. (a) I don't think they would have taken any notice, but (b) I would never have suggested it in the first place.
Q. If we could go forward to tab 27. Just before we look at that, having looked at that example in relation to T&S, so where Gallaher reduces its wholesale price so that its net wholesale price is lower than yours, and the retailer you told us you regarded as entitled to price it in that way, was he obliged to do anything as far as you were concerned with the retail price of your product?
A. No, because if Gallaher were, by one mean or another, investing extra money into that account, all we would like to have is the opportunity to respond, and some

retailers would take up our response and some wouldn't.

Q. We will come back to First Quench in a moment, but in T&S we know there is an opportunity to respond clause, it's called "explicitly stated". In First Quench we don't see an explicit statement of that clause. As far as you were concerned, was there a difference between the two situations?

A. In general, if we saw a promotion run on, let's say, Mayfair, for example, and we saw it in store, it had happened in First Quench as an example, we would go back to First Quench and say "We would like to respond with this". But there was no obligation on them to take it.

Q. Yes. Now, in a situation where you see -- you told us you know what the list price is of your product and you know what the list price is of Gallaher's products; that's right, isn't it?

A. Yes, we would know the RRPs and the Q rate prices, but not the absolute net prices.

Q. Yes. The net prices, the bulk discounts I think are on the price list. So you know that, don't you?

A. Yes.

Q. What you don't know is what particular bonus, as I understand it, or incentive, whatever it is, that's being paid, or a discount, however it's described, you don't know what --

A. No. All we would know is the published Q rate price for Gallaher products and the published RRP, but nothing to do with the investments or anything like that.

Q. Paragraph 21 I think of your statement, you told us that as far as you were concerned the objective was to ensure that your, as you perceived it, lower prices were fed through to the consumer {C3/35409}. Where the retailer prices the Gallaher -- let's take Dorchester and Richmond. If you see Dorchester on his shelf at a lower price, or let's say you see Dorchester across the market at lower prices than Richmond, what conclusion would you then draw as to the stance that Gallaher had taken vis-a-vis the net wholesale price?

A. They would have put more investment into the account to achieve that lower shelf price, ie paid a bonus, a tactical bonus or whatever.

As I say, I don't know how they arrange their payments, but one assumes a tactical bonus.

Q. Right. If you would go to document 27 {D29/27/88}, under Richmond we can see that you say:

"This is to confirm that all Richmond 20s should be held at current prices until further notice. Richmond Kingsize and Superkings must not be increased on 12 February when you implement the Gallaher MPI, and the retro support shown in my letter dated 10 January will

continue."

What were you trying to achieve here about holding -- I think you have had an MPI, so what were you trying to achieve here?

A. What we were basically saying is to try and keep -- well, to encourage the retailer not to put Richmond up, and whatever Gallaher decided to do with Dorchester, we wanted to carry on paying the bonuses on Richmond.

Q. What I want you to then consider: if one has a situation generally where Gallaher, let's say they withdraw a bonus in a situation where you had bonused Richmond to come down to match them, if they withdraw their bonus and you don't withdraw yours, you don't say anything, you just have a bonus that's in place, what do you expect the retailer to do to the price of your Richmond brand?

A. We would expect them to keep the price of Richmond at the lower price and pass on the bonus that we are paying them.

Q. Right. Where Gallaher has an MPI, as you are referring to here, do you have any requirement as to where Gallaher has an MPI what they should do to your brand?

A. Not at all, no. If Gallahers had an MPI, that's their choice and nothing to do with our brands.

Q. Could we perhaps just switch to First Quench for

a moment, annex 16, please. If you go to tab 5, some of these documents are before your time, but I just want to see how the First Quench was operating {D16/5/8}. One sees at paragraph 2 that:

"When Dorchester is increased by 5p per 20, expected soon, please leave Richmond price unaltered, thereby matching the Dorchester price".

Right? So it appears that at that stage Dorchester was 5p cheaper than Richmond?

A. That's correct, yes.

Q. So in relation to First Quench, in a situation where Gallaher had managed to reduce the price of Dorchester, whether by bonusing or otherwise to get it 5p below Richmond, what, as you understand it, was First Quench required to do vis-a-vis Richmond if you didn't yourselves bonus Richmond down?

A. I think the background to this, this was at the time when we changed the retail price of Richmond and were seeking to bring the price down of Richmond across the market.

Q. Right.

A. First Quench chose not to bring Richmond down to the price that we would like to have achieved, as low as we wanted, and decided to keep Dorchester 5p cheaper than Richmond.

Q. Right. Was that as a result of a Gallaher price cut, or you don't know?
A. I don't know the reason why, but there is a letter further in the folder where the buyer is not wishing to accept our lower price on Richmond.
Q. Right. That sort of point, where they decide they don't want to accept the lower price on Richmond, were they free to do that?
A. Yes.
Q. Was that something you experienced yourself on these accounts?
A. There are occasions -- there is a couple of occasions with T&S not accepting tactical bonuses on products in these folders. I wouldn't say it was common, but yes, it did happen from time to time.
Q. Right. Would you go to document 11. One sees on the second page {D16/11/29} that on 29 January onwards the Richmond price was to be held -- sorry, this is in the context of an MPI -- at £3.34, no increase of 5p at MPI, [redacted] per thousand bonus.

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Now, where in relation to this account, First Quench, one held the Richmond price, if Gallaher had their own MPI and put up their price, what then was to happen to your price?
A. We were maintaining this price until further notice.

Q. Okay. You were asked some questions by Mr Lasok concerning the situation where -- what we have been looking at the moment are situations where Gallaher has a lower wholesale price and a lower shelf price.
Mr Lasok asked you some questions to the effect that: suppose actually Imperial has a lower wholesale price, and how the agreement is to operate. I think what Mr Lasok was suggesting to you was that the retailer, where you have a lower wholesale price, has to -- a lower wholesale price than Gallaher -- price your product at the same level as Gallaher, and therefore cannot pass through to the consumer --
MR LASOK: No, that's not actually what I said.
MR HOWARD: That is what you said, but anyway, let me go back.
What Mr Lasok, as I understood it, was suggesting was that where Imperial has a lower wholesale price, his suggestion was: if one has a fixed relationship, the retailer will not pass through the lower retail price, the lower wholesale price of Imperial through to the consumer, because he can charge both the Imperial product and the Gallaher product at the higher price and still be maintaining the differential.
Now, what I wanted to ask you is, firstly, you dealt with these four accounts. Insofar as you had a differential policy, you have told us that as far as you were concerned in these accounts it was always a "not more than" policy, ie not more expensive than. How would the retailers who you dealt with have understood the position, as far as you were aware?

A. In the case of -- using Richmond and Dorchester, we wouldn't want Richmond to be higher, but they were free to set it lower. And there is examples with T&S where they have chosen to sell Lambert & Butler cheaper on their own promotions.
Q. What was the reason for -- for instance, if we take Richmond and Dorchester -- the strategy, as far as you understood it?
A. Consumers viewed those products as equally acceptable. Therefore, if both products were on the shelf, consumers might switch between those two. So, therefore, if our brand was either cheaper or the same price, we would have the opportunity to get more consumers buy our product. If our product was dearer, then consumers might choose the Gallaher product, because the products were very similar.
Q. You have already told me that where Gallaher's net wholesale price was lower than yours, as far as you were concerned the retailer could represent that in a lower shelf price and you would have to compete.

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

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

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

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

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

you go to what is page 20 of this document, the business development plan, the bit that somebody has put in a box:

"Price support bonus money is now paid on only 30 per cent of volume. This is as a result of only this percentage now being sold below RRP."

I think also if you go to page 23 under "Pricing", we get the references to three tiers. Then, after the tiers:

"These percentages vary somewhat between brands. They should be monitored given the fact the trading agreement pays on 30 per cent of volume sold at below RRP."

So by this stage, what is it that Imperial is going to pay a bonus on?

A. Only on the volume that is sold in stores when our selling price is below RRP, which was about a third of their volume.

Q. Right. In relation to the differentials, so where they are selling below RRP, how were they to treat -- in the RRP discount, how were they to treat you and Gallaher as far as you were concerned?

A. We were seeking them to not treat us worse than the compet -- I don't know what Gallaher's were seeking, so if in the case of Benson & Hedges and Embassy No 1, we

would hope they would have Embassy No 1 3p below Benson & Hedges.

Q. If we go to tab 48, which is the final trading agreement, you have already explained to us that they had these tiers and only 30 per cent of volumes are being sold in the low tier, which is below RRP. In relation to the higher tiers, were they being paid anything in order to achieve your strategy?

A. No, not a penny.

Q. In the higher tiers, if they -- for instance, let's say in the tiers where they are pricing above RRP, the premium tier, if they priced Embassy at the same price as Benson & Hedges, rather than at a 3p differential or minimum 3p differential, would you, as far as you were concerned, have any complaint about that? Was it anything to do with the agreement?

A. There was nothing in the contract. I might try and ask them to reduce Embassy, but there was no -- because the bonus or the investment we made was based on the cut price tiers only.

Q. Right. You were asked some questions about a letter that Mr Byas wrote. Just before we get to that, could I ask you to be given annex -- no, let's perhaps, in view of the time, move on.

Actually, could you take annex 13, please. If you

go to tab 7, this is a pricing sheet.

A. Sorry, did you say tab 7?

Q. 7(a), I am sorry.

A. I have nothing in there.

Q. Oh, have you not?

THE CHAIRMAN: We have two volumes of annex 13.

MR HOWARD: Let's put it away, it doesn't really matter, he can deal with it without seeing the document.

A. It would be the big A, is it?

Q. It doesn't matter, let's go to tab 46. Sorry, I am trying to do it quickly and I am jumping around. I am saying put away the other one and go to the First Quench annex 16. I apologise. I will be able to finish, I think.

Tab 46, the letter that we have looked at several times today. You have told us that, in respect of cigars, certain cigars, that it was never Imperial's strategy to have them priced at the same level as Gallaher cigars?

A. Panama, in my recollection, was always cheaper than Hamlet, in an RRP, yes.

Q. The document I was going to show you is just a differential sheet at this time which shows precisely that.

Assuming that was the strategy, did the pricing

strategy differ according to whether one was dealing with First Quench or somebody else in the market as to the relative price positioning?

A. We would try and achieve the same objectives across the retail market.

Q. Would Mr Byas have authority to agree a different pricing strategy?

A. No.

Q. If we look at tab 46, what was being suggested to you about tab 46 is that -- and I think the same point was being made in relation to tab 49 -- the reference here to "parity" must mean that all cigars were to be priced at the same level. I think you told us that that simply doesn't represent ITL's strategy, so you had some difficulty understanding that?

A. It doesn't represent the strategy at all.

Q. I want to see whether an alternative construction of the sentence would then fit in with ITL's strategy, as you understood it. You are obviously not the author of the letter, Mr Byas is, but if what was being referred to here by "parity", "achieve parity for ITL and Gallaher brands", what he was trying to convey was at the same RRP differentials in the different tiers, would that accord with ITL's strategy?

A. I don't think so, because the brands, the three tiers that First Quench were operating on was a different issue over Panama being the same price as Hamlet. So if ... I don't know, obviously I wasn't -- I didn't write this letter, but parity for cigars, if it was the same across all the tiers, that wouldn't be in line with our strategy. If it was different parities in different tiers, it still wouldn't be in line with our strategy. So in no way would this fit in with what we were -- my objective was or our objective was as a business.

Q. My question was: if what he was trying to convey was that you should treat them equally in the sense of applying the same -- either price them at RRP or RRP plus or RRP minus, in other words keep them in the same relativity to the RRPs?

A. If he had said that and that's what First Quench were doing, that would have achieved our objective, yes.

Q. Now, then on the final point on that correspondence, tab 49 we see is an example of there being a Panama bonus, so what appears to have happened is that the price of Panama has been reduced by Imperial by a bonus. Where that happened, in other words where Imperial seems to have gone first, taking steps to reduce the price of Panama, what would be the purpose of that?

A. Why we were offering a bonus?

Q. Mm.

A. To achieve a lower shelf price for Panama.

Q. Lower shelf price, right. Where you have done that, what would you expect them to do to the competing brands?

A. Nothing at all to the competing brand. Only we would offer the tactical bonus to achieve a lower shelf price for our products, but it wouldn't have any impact on any other product.

Q. Could we then close for good First Quench, and just go back to the T&S account in annex 29. {D29/46/149} If you go to tab 46, this is the 11 June, summer 2002 episode. What's happened is Gallaher announces its price increase, we see that, and so Gallaher's prices are due to go up.

Now, if we take it in stages: firstly, if you hadn't written this letter to Mr Lyons on 11 June, and you hadn't had an MPI but Gallaher had, firstly do you have any requirement as to what he should do to your brands under your contract?

A. Sorry, if Gallaher's have had an MPI?

Q. Yes. It's this situation: if you hadn't written this letter, what did you require Mr Lyons to do with your brands?

A. Do nothing, keep the prices down.

Q. Right. What was the purpose of the letter in the light of that?

A. It was a reminder effectively that our prices were not going up and highlighting the effect that would have on the differentials.

Q. Right.

Can I then ask you about tab 47, {D29/47/152} Mr Lasok was suggesting to you that this was, I think, countermanding the widening of the differentials. I just want to actually understand what happened. If you look under "Retail prices", you will see you wrote:

"I have noticed you have a flat price on Berkeley Superkings multipack at 19.99."

Then you ask him to change the following brands in the Supercigs tiers 1 to 4. Similarly, if you go over the page, you note that you have also introduced a flat price on Berkeley multipacks in all the CTN stores.

Explain to me what this reference is to the flat price and its relevance in relation to tiers 1 to 4; what's going on here, as you understand it?

A. Both -- in Supercigs they would have had nine tiers, and in tiers 5 to 9 they wouldn't have been at 19.99. I don't know what price they would have been at, but normally, under T&S' normal policy, Berkeley would have been higher than 19.99 in tiers 1 to 4, so we have noticed that our brand has become more expensive, and

are therefore offering a tactical bonus to bring our brand down.

Q. So I think it was being suggested to you this letter was just about the response to the Gallaher price hold. But what have Gallaher actually done, as far as you understood it at this time, in order to get Berkeley Superkings and the other Berkeleys at this price across a number of the tiers?

A. Well, they would have (a) paid a bonus to counteract the effect of their MPI, and secondly added an extra bonus to bring this flat pricing in, because otherwise Berkeley would have been higher.

Q. So what are you doing and how do you have to pay for it?

A. By fully funding the reduction from their, T&S', natural price in tiers 1 to 4 down to 19.99.

Q. Did you at any stage say to Mr Lyons "Well, you are simply not entitled to do this, you can't reduce the price of Berkeley, we can't have that"?

A. No, not to Mr Lyons or anyone else was it ever said.

MR HOWARD: I think we are probably only to go over more similar correspondence, and I think you have the picture, so I'll stop there.

THE CHAIRMAN: Thank you very much, Mr Howard.

Thank you very much, Mr Culham. This is positively your last appearance, Frank Sinatra like, before the Tribunal. So thank you again for attending and for your evidence. I realise it's been a long day, but thank you, that's been very helpful, and I can now release you from the witness box.

A. Thank you.

(The witness withdrew)

THE CHAIRMAN: Tomorrow morning we will start at 10.30 with you briefly, Mr Lasok, and then Mr Wragg.

I don't know whether you will have a chance to discuss with Mr Howard or anyone else what you plan to say tomorrow. Clearly it will take up less time if you have been able to discuss it amongst yourselves, but that may be impractical.

MR LASOK: Yes.

THE CHAIRMAN: Good. We will meet again, then, at 10.30.

MR HOWARD: Sorry, could I be impertinent just to raise one timetabling question?

THE CHAIRMAN: Yes.

MR HOWARD: Sorry to do that, but I am concerned about this question of experts, and I asked Mr Lasok, and he says his estimate -- or whoever is doing it on their side -- is still five days. The reason I'm simply raising the is question is whether or not there is any possibility of the Tribunal being available on one of those non-sitting days in the next two weeks, or whether we

should be scheduling the day in the following week, or whether you say: no, it's all got to be done in four days and four days.

THE CHAIRMAN: I thought yesterday we asked to see a breakdown of what the timetabling was for those weeks in relation to the eight days, as a useful first step to considering this.

MR HOWARD: You did.

THE CHAIRMAN: But we will also overnight look at the two non-sitting days in those weeks and see if there is any possibility even of sitting an extra half day. We will check that out. Thank you.

(4.45 pm)

(The court adjourned until 10.30 am on Thursday, 3 November 2011)

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