IN THE COMPETITION APPEAL TRIBUNAL

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

Victoria House,
Bloomsbury Place,
London WC1A 2EB

6 October 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

Transcribed using LiveNote by Opus 2 International
1 Bell Yard, London, WC2A 2JR
Tel: +44 (0)20 3008 5900
info@opus2international.com

HEARING (DAY 9)

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.

Thursday, 6 October 2011

(10.30 am)

THE CHAIRMAN: Good morning. Before we start with the next witness, there are a couple of points that I wanted to make in relation to the scope of cross-examination, in particular which aspects of witness statements need to be challenged in cross-examination in order for the OFT subsequently to be able to make a submission as to the proper interpretation of a contemporaneous document.

This has come to our attention, particularly having read through the witness statement of Mr Culham, who is giving evidence later. Now, in his witness statement, he deals with correspondence to which he's a party, for example in paragraphs 69 to 77 of his witness statement, and there he explains the background to the letters and what he meant in those documents.

Now, if the OFT wish to submit in due course that his evidence is wrong and in fact he meant something else, then that needs to be put to him. However, in paragraphs 90 onwards, he goes through the documents relied on in the decision and gives his interpretation of them, even though he was not the author or the recipient of them, and in these paragraphs his evidence is phrased in terms of a particular sentence probably being simply a recognition of something. He says, "Well, it would appear that Ms Canavan meant something or other", or he would suggest that she appears to have meant or recognised something.

It doesn't appear to us that Mr Culham is saying that he has spoken to Ms Canavan and she has told him that is what she meant or assumed or thought, that is his interpretation of the document.

Now, in our view, the fact that the OFT may wish in due course to ask the Tribunal to draw a different inference from the document doesn't mean that that document must be put to Mr Culham, still less that other documents need to be put to him to see if that causes him to change his mind about his interpretation of a particular sentence in one of those documents.

Ultimately it's for the Tribunal to decide what the documents mean. This isn't strictly evidence from Mr Culham, and therefore in our view doesn't need to be challenged in cross-examination.

The second point is that we are uncomfortable about witnesses being in the room when other witnesses are being cross-examined, or when Mr Howard is opening in relation to a particular agreement. We are concerned that it should not be an issue as to whether their evidence has consciously or unconsciously been coloured by what they have heard other witnesses say or what they have heard is ITL's case about a particular document or a particular incident.

So we would prefer for the witnesses to be out of the room other than when they are giving evidence, obviously.

A similar point is the use of the term "relative maxima" or RMSs to describe the schedules to the trading agreements. The term RMS, relative maxima schedules, is in fact making an assumption about an important aspect of the case, whether they are maxima or fixed. It's not a term which we recall seeing actually in the trading agreements, and therefore it shouldn't be used in questions to the witnesses to describe those schedules or those trading agreements if there is a dispute in relation to that witness's evidence about whether they really are maxima or whether they are fixed parities and differentials. So we would be grateful if counsel could bear that point in mind when phrasing their questions to witnesses.

Does anyone wish to respond to what I have just said?

MR JONES: Madam, if I may, just in relation to the presence of witnesses in the room, does that simply apply to the particular appeal in question at that moment, because for example Mr Eastwood is here today, he will be giving evidence on behalf of Morrisons next week, and he is here simply to observe how the Tribunal works. Obviously there is no Morrisons commentary or witnesses giving any evidence today.

THE CHAIRMAN: Well, it depends whether he is likely to have documents put to him when he's being cross-examined which are being put to witnesses who are giving their evidence. Now, that's more likely to be a problem in relation to ITL witnesses, because obviously documents are being put to them covering the whole range of the retailers. In relation to a particular retailer witness, that may be less likely to be a problem.

MR JONES: Madam, it may be that a practical solution could be that Mr Lasok may be able to let us know if he thinks there is any moment or any cross-examination which Mr Eastwood shouldn't be present for.

THE CHAIRMAN: Well, I don't really wish to put that burden on Mr Lasok, who probably has enough to think about at the moment. (Pause).

Well, as I say, our sense is that it would be better if the witnesses came and gave their evidence without there being any danger of them having heard about a particular document or what questions are likely to be put to them about a particular document or what interpretation anyone has given in relation to that --

MR JONES: I am grateful.

THE CHAIRMAN: -- document. If that means that Mr Eastwood has had a wasted journey today, then I am afraid that's one of the hazards of litigation.

MR JONES: Yes. I am grateful.

THE CHAIRMAN: Yes, Ms Rose.

MS ROSE: Madam, of course we have already called two witnesses, and our last witness is about to give evidence, without that direction having been given, so obviously we weren't aware that that was the Tribunal's preference, and I just want to lay down a marker that obviously it couldn't be a point that would be taken against Shell --

THE CHAIRMAN: No, no. I absolutely understand that, yes.

MR LASOK: Madam, I take it therefore that the Tribunal doesn't want a witness to see the transcript, because of course if you see the transcript, then it's just as if you were in the courtroom.

THE CHAIRMAN: Well, yes, it would be better if they didn't see the transcript until they have given their evidence.

MR LASOK: Does the Tribunal's ruling apply also to the experts?

THE CHAIRMAN: Can I think about that and get back to you?

MR HOWARD: Actually I think there is a difficulty. Unless the court is sitting in camera, which it isn't, then the transcript is a public record. I don't think one can in fact say that people can't see the transcript any more than a reporter can come in and report things. I think one needs to think about that quite carefully. It's one thing saying one is going to seek to exclude a witness while evidence is being given, that is itself a rather unusual step, I am not saying we shouldn't do that, but restricting people looking at the transcripts, because part of the problem is inevitably there is going to be discussion between instructing solicitors and witnesses, asking them things about the case as it develops.

Unless one is saying, well, we have got to this stage and you are not allowed to talk to the witnesses, I find it very difficult to see how this works in a sensible way.

I quite understand that you don't want people, as it were, actually in court, I am not seeking to argue against that, but I think there are difficulties once one goes beyond that. Certainly the idea that Mr Lasok has just mooted is totally ridiculous. The experts in any case have to know what's been happening in the case, because their evidence has to be adjusted in the light of the factual evidence. It would be completely ludicrous that experts came along and said "I have no idea what the facts are".

I know that's what Professor Shaffer's approach is, but we, of course, will want to ask him about the facts. If he wants to continue to live in his isolated world not looking at the facts, that's up to him, but it's certainly of critical importance that the experts certainly on our side understand what the facts are, they are expressing a view on, otherwise we will just have cross-examination where people say "well, you don't know what the facts are, so what's the use of your opinion?"

THE CHAIRMAN: Yes, well, I see the force of that point in relation to the experts, that it doesn't apply to them in that their evidence will or may need to be tempered by the evidence as it has come out, the factual evidence.

As regards to people reading the transcript, I would hope that a commonsense approach to this can be maintained in the sense if the witnesses should be told that their evidence is likely to carry more weight if it's given -- their recollection as far as they have that recollection -- without them having pored over the transcript to see what everyone else has said about a particular document.

MR HOWARD: Absolutely, that's a question of the weight that you attach to the evidence and the extent to which it is independent and their own evidence, and that's ultimately what you want.

THE CHAIRMAN: Yes.

MR HOWARD: But it is in fact quite difficult to -- I mean --

THE CHAIRMAN: We don't intend to police this in any way.

MR HOWARD: What I am saying is it's quite difficult to have a position -- I can't imagine -- certainly the witnesses mostly on our side, a lot of them are retired people -- that they want to spend their lives reading the transcripts, it's bad enough that we have to. But inevitably, as a case goes on, the solicitors will wish to revert to a witness and ask them for further views in the light and further evidence in the light of things that have arisen. That's what happens in the course of litigation, and you can't say you are not entitled to talk to the witnesses in the course of the witnesses and elicit their further evidence as the case develops.

THE CHAIRMAN: It would be best, in my judgment, if the witnesses are advised that they are certainly not expected to read the transcript, that it would be better if they didn't read the transcript before they give their evidence.

MR HOWARD: Certainly.

THE CHAIRMAN: We can't prevent them from reading the transcript and I fully accept that as the case develops it may be necessary to go back to people after they have given their evidence and say, "Well, you may be asked about this" or whatever.

MR HOWARD: Can I just raise one practical point?

THE CHAIRMAN: Yes.

MR HOWARD: I think I know what the answer is, but I am asked to raise it. Mr Hall is due to give evidence next week in relation to Asda. He is here today simply on the basis of seeing how things work. I don't believe any evidence today has anything to do with Asda, we are going to be on Shell the entire day, plus possibly a Co-op opening, although I am not sure we will get there. Now, I am in your hands as to whether you think it's inappropriate for Mr Hall to be here or not.

THE CHAIRMAN: Well, that's the same position presumably as Mr Eastwood is in.

MR JONES: Madam, it is similar, and I apologise for rising again but I would also just put in one special plea for Mr Eastwood, because he has come from Amsterdam today simply to see how evidence is given. He has not been in court before and it is difficult to see that there would be any document in relation to Shell which could possibly be put to him in relation to Morrisons.

I would, as it were, piggyback on Mr Howard's special pleading in that respect.

(Pause)

THE CHAIRMAN: Well, given that both Mr Eastwood and Mr Hall have made special arrangements to come today, and it is very unlikely that there will be any documents which are being put to these witnesses today which are also going to be relevant to their evidence, we are prepared to let them sit at the back.

MR HOWARD: I should have added that Cynthia Williams is also here, she gives evidence about First Quench. Perhaps we have all put these people in this position, that they were asked to come along, and it's very awkward and embarrassing to say "now go away".

THE CHAIRMAN: Are you going to be asking either Mr Conrad or Mr Culham today any questions about documents relating to those witnesses or documents that are likely to be put to those witnesses?

MR LASOK: No. Mr Conrad will be asked questions from annex 19, Mr Culham, because we are only dealing with that part that deals with Shell, it will be just the annexes that relate to Shell. There is, I suppose, a problem about the ITL witnesses because of the fact that, when you ask them about one agreement, you are actually asking about ITL's approach generally, and the same applies to the problem posed by openings, because for example yesterday's opening on Shell was really generic in nature.

THE CHAIRMAN: Well, why don't we have them in this morning for Mr Conrad's evidence and then review the position when we get to Mr Culham's evidence.

MR HOWARD: That may be the sensible compromise.

THE CHAIRMAN: Yes, thank you. Someone can then go and get whoever it is that needs to come back in.

(Pause)

MR HOWARD: Sorry, I should have said that I don't dispute that Mr Lasok doesn't have to cross-examine witnesses who are -- and I think I made that clear the other day, and although the witness statements and for reasons you will probably understand deal with things which the witness is effectively giving a commentary which can be done by way of submission -- and that applies throughout -- and Mr Lasok in cross-examination shouldn't feel he has to cross-examine witnesses about things unless he wants to establish whether the witness actually saw the document at the time. But if they didn't, I accept it's just commentary.

MR ALEXANDER CONRAD (sworn)

Examination-in-chief by MS ROSE

MS ROSE: If you would like to take a seat, Mr Conrad.

A. Thank you.

Q. I think it's right that you have a bit of a sore throat; is that right?
A. It is.
Q. So everybody knows in advance that you may be a little husky. Can Mr Conrad be given core bundle 11, please. Can you turn to tab 115. You see the document there. Is that your first witness statement? C11/115
A. It is.
Q. Are the contents of that statement true?
A. Yes, they are.
Q. If you would turn to the next tab, is that your second witness statement?
A. Yes, it is.
Q. Are the contents of that statement true?
A. Yes, they are.
MS ROSE: If you would like to wait there, please.
THE CHAIRMAN: If you need to have a break at any point, Mr Conrad, please feel free to say.
A. Thank you, madam.

Cross-examination by MR LASOK

MR LASOK: Now, Mr Conrad, am I right in thinking that you can tell us about what was going on from June 2000 until early September 2001?
A. Yes, that's true.
Q. You don't know when in September 2001 your involvement

with tobacco ceased?
A. My recollection is that I started my -- the role that followed my category manager role on 2 September.
Q. Am I right in thinking that initially -- and we are looking from June 2000, not earlier -- from June 2000 Shell had a single price, a single retail price?
A. In June 2000 there was a price which we published to the retail sites called the Shell retail price.
Q. That was the retail selling price?
A. That was the recommended retail selling price.
Q. Could you turn to your second witness statement, please, and go to paragraph 6.2. Could you read the whole of paragraph 6.2 to yourself, please.
(Pause)
A. Yes.
Q. Now, I read 6.2 of your second witness statement as saying that before the implementation of the RBA, Shell unilaterally set out its own pricing policy for the retail of all products including tobacco; is that correct?
A. That's correct, that's what the statement says.
Q. Is it correct?
A. That is correct.
Q. And that was the shelf price?
A. No, the price that was communicated to the retailers was

the Shell retail price, and essentially this was a recommendation to the Shell retailers that this is the price that we were looking for products to be sold at.

THE CHAIRMAN: Even before the RBAs were implemented?

A. Before the RBA was in place. So this is in the period prior to the RBA being conceived and then eventually rolled out. And the reality in fact was that this price was communicated, and the retailers, who at that stage were Shell employees, would then mark the products on shelf at a price that was close to that price or at that price. But we had no control over actually enforcing that that was the price that they sold the product to the consumer at.

The systems that we had could only communicate one recommended price, and the retailers made a decision as to what price they wished to sell the product at, and sometimes that decision was based on the area of the country they were in, or what they knew their customers would accept as a price.

DR SCOTT: Sorry, you said "we had no control". It raises two questions: one, who is "we", since these are Shell employees, and clearly Shell employed them; and secondly is what you mean is that "we" in the bit of Shell where you were working did not exercise control?

A. That's a fair reflection, yes. So we as the category managers, who were essentially given the role to identify what the Shell retail price for these products should be, and to communicate that to the retail sites, we had no way of exercising control in all of the sites to ensure that every site was selling product at that price. There are 650 sites. It just -- and many hundred products. It was just not possible to be able to say, you know, "That site, every site today is selling at that price".

DR SCOTT: But if a particular case was drawn to your attention, did you have the means of making a correction?

A. We had what I can only describe as really blunt instruments in order to do that. With 600 sites and if, for example, a supplier identified 30 sites that had not positioned the rate of the shelf price as our Shell retail price, we had options to phone those sites to talk to the area sales managers. But if I can just put the context of my moving into the role to give you an understanding of why we didn't spend, invest a lot of time chasing delivery of those prices --

THE CHAIRMAN: Well, I don't think that's the point that we are looking at. What I am still unclear about is whether the price that you were telling them was supposed to be the price that they sold at, albeit that some of them didn't and there wasn't much that you could do about that, or are you saying that your policy was to give local autonomy to the shops to choose their own price even though you recommended a price? Do you see the difference between those two things?

A. Yes, I do. I don't recall there being a strict policy that said: the Shell recommended or the Shell retail price was the price that all sites would sell at. The inference was: yes, we would want sites to sell at that price, but if sites took a decision to sell at a different price, we didn't have the resources to rectify that.

THE CHAIRMAN: So it's more the first of my two scenarios than a deliberate delegation of local autonomy to the shops?

A. I think it was something that evolved, and the context being that we had moved from 22 category managers to seven, those 22 category managers had all managed categories at great level of detail and suddenly the seven were left to pick up the work of 13, and an awful lot of skeletons came out of the cupboard, as you can imagine. So the sorts of instances where I was investing my time was not whether a price in a particular site was correct according to our Shell price list, I was more concerned about the £200,000

worth of stock that was stuck in our warehouse that we couldn't shift or we couldn't sell and that the suppliers wouldn't take back. Just from a business perspective, that was where we were going to affect what was happening within our business, and the business was under what we call a red flag in Shell, in that the performance was very poor, and we needed to find changes.
THE CHAIRMAN: Let's not go into too much of that detail.
A. Sure.
THE CHAIRMAN: Yes, Mr Lasok.
MR LASOK: As I understand it, the position was that if a site was directly controlled by Shell and wasn't run by an independent contractor, then Shell actually was running the show, you may have had control problems, but you were running the show; is that not so?
A. I need to understand what you mean by "you". If you are talking about me personally, was I responsible for making actions on site happening, no, I provided guidelines, and we provided a Shell retail price. The expectation was that that product would be retailed at that price, but there was no ability to actually effect any changes to that if a site did not make the choice -- or made a choice to sell at a different price.
Q. It may be better to look at a couple of practical

examples of this. Could you have a look at annex 19, please, and turn to tab 17. D19/17. This should be a letter dated 18 September 2000 to you from ITL. Is it?
A. Yes.
Q. Could you read that letter quietly to yourself, please.
(Pause)
A. Yes.
Q. This is a letter in which, as you can see from the last sentence, which is on the second page, ITL is asking for the implementation of certain price changes promptly, following a meeting that, according to the first sentence of the letter, had taken place on that day, 18 September. If you look at the second holepunch -- not actually at the second holepunch but the text alongside it -- the writer of the letter states that:
"You agreed to issue a trade bulletin to all sites informing them of the lower cost price and the Shell Select selling out price of 3.55 which would be effective from 28 September."
Now, isn't that an indication that, as between you, Shell, and ITL at any rate, the understanding at the time was that Shell would set out the selling price of 3.55, communicate it in the form of a trade bulletin and it would be effective in the Shell Select sites?

A. So I think I understand the question, is that if I recall this letter, yes, I recall this letter, having now seen it again, and the situation being that Imperial had launched this product some time earlier, during the previous year, the product hadn't sold particularly well, and because of the way that price competition was in the market at the time, they chose that they wanted to reduce the retail price, the recommended retail price of that product.

As part of the relationship you have with a supplier, it's about driving the brands that they are investing money behind, and in this case they were investing money, and they wished to lower the price in order to drive sales and attention.

We had agreed that this price was a price that was relevant in terms of their marketing strategy, but there needed to be some discount on the cost price in order for us to still maintain the margin.

So from reading this, that's the situation that it reflects.

THE CHAIRMAN: Yes, but the question you are being asked is: by issuing this trade bulletin showing a Shell Select selling out price of 3.55, were you then expecting that the sites would, as from 28 September, sell that at 3.55? Was that your intention?

A. I don't recall if the trade bulletin went out, but if the trade bulletin went out, it was anticipated that the Shell retail price of 3.55 would be the price that the sites would move to, but knowing that the chances were that a lot of the sites would not move. It was just the reality of the situation at that time. So it was recommended, but I think we both knew from the way that the business was controlled and managed, that some sites would move but there would be quite a few that wouldn't, and from recollection, looking through other documents related to Richmond Kingsize, it was a lot of sites that didn't move.

MR LASOK: Yes. It may help you, I don't know whether it does help your recollection, but if you go to tab 19, D19/19, this is an email exchange that seems to follow on from the letter we have just been looking at. As is usual in these things you have the original message down at the bottom of the page, and it was from Amanda Eager, sent on 26 September 2000. If you just cast your eye over that and turn to the next page, you will see that she was asking you to confirm the new agreed selling price for Richmond Kingsize as 3.55, effective from 28 September.

Your reply is at the top of the first page. You confirmed that Shell Select sites would be retailing the

Richmond brands at 3.56. But again, that is an indication that your belief was that under these arrangements at this time, if Shell set the price, that would be the shelf price?
A. I wouldn't say that my belief was that that would be the shelf price in all sites. As this shows, the request was for 3.55, I have come back and said it was 3.56 and that would be the price that I was going to put it out at, which may not necessarily have pleased Imperial, but that was what we wanted to do. I was never under any illusion that every site would move to that price.
Q. Just to complete the story so that we all know that there are no hidden things connected with this, if you go to tab 22, D19/22, this is an email from Ken Culham to you on 3 November 2000, and he is referring back to the reduction of the price to the Shell depot on 18 September, which was what is dealt with in tab 17, and he refers to the fact that you agreed to alter the selling out price from 28 September in the first instance to £3.56. He then refers to the fact that the move to the correct price, 3.55, from 10 October was confirmed at a meeting on 9 October, and he then sets out data of sites visited, and points out that of the total visited, a certain number were stocking Richmond and of those, a certain number were charging over the

correct price. He ends up by saying:

"Can you please re-issue instructions to sites urgently confirming the correct price is £3.55 and send a copy to me for information."

Is that a fair reflection of the relationship between you and ITL at that time?

A. It certainly doesn't show the whole picture in terms of the relationship between ourselves and ITL. Certainly at this time, so we are in November 2000, there were an awful lot of other things that were going on, and this is one instance of a discussion where Imperial wanted to drive a particular approach in terms of one of their brands. I think it reflects fairly that we weren't capable of implementing instructions in our retail estate. It also reflects that there was a focus from Imperial in terms of driving their prices, but quite frankly from Shell's perspective and certainly from my own personal perspective, there were far bigger fish to fry at this time than worrying about one or two products, and the particular price at 600 sites.

So this would have been a frustration in the relationship, and certainly one of my roles coming into this job was to try and build positive relationships with all of the suppliers, and I think the Imperial relationship was perhaps under a lot of stress because of their position in the market and the fact that Shell had chosen to go with the smallest player in the market for the fixture investment and to work on the development of planograms. There weren't many opportunities from a promotional perspective. So their focus was very much around this. My focus was very much not around this, it was very much about the broader activities in the tobacco category and the other categories that I was responsible for.

Q. You would agree, wouldn't you, that these documents are an example of an agreement between you and ITL as to the shelf price for, here, Richmond in the Shell Select sites?

A. I wouldn't say this was an agreement about the shelf price, this was an agreement or the confirmation of a discussion around the price of two particular products that Imperial were investing in and driving, to communicate Shell recommended price at a certain price, that illustrates our difficulties in actually making anything happen on the sites.

Q. I am slightly puzzled about this. Could you turn to tab 24, and again you have an email string, and the first email starts by the second holepunch. Could you read that one first, and then your reply to Mr Culham.

(Pause)

A. Yes.
Q. So I'll put it to you again: in the documentation that we have just been looking at, we have an illustration of Shell agreeing with ITL the shelf price for an ITL product on the basis that the shelf price would actually appear in the Shell Select sites?
A. Again, I wouldn't agree with what you are saying. This is an email exchange where Ken has been out into a site, he has purchased a product, the price he purchased it at didn't reflect the price on the shelf and the price he purchased at didn't reflect what he understood to be our agreement and what we had agreed.
THE CHAIRMAN: The price didn't reflect the price on the shelf?
DR SCOTT: Yes, there appears to be a shelf price at 3.65 but when he actually purchases it, it's at 3.56. So presumably when it's scanned, it's producing a different price --
A. A different price.
DR SCOTT: -- than the price at which it's marked. The Trading Standards hadn't been round to check.
A. Fortunately not in this case, no. I think again this is a series of conversations and emails that had gone on for several months now, it's 20 November, and so I have apologised to say "look, you know, sorry" and it's all

part of preserving the relationship, but yes, I have given the instruction again that the recommended price is 3.55, knowing full well, and as the evidence shows, that we are not as an organisation capable of delivering these instructions.

DR SCOTT: Mr Conrad, perhaps you can help me with this: am I right in thinking that at this stage there would have been a scan of the barcode?

A. Yes. I believe that all products were scanned, although the system was not locked in such a way that a central download from head office set what the price was. It was possible at local site level to change the prices, and I believe at that time, which was part of our control issue, it was possible to put things through on what was called a dump code, so you could enter a price and still sell a product.

DR SCOTT: Thank you. I think that helps me understand what was going on. So they could either do it manually, in which case presumably it would have been the 3.65, or scanned, which produced a 3.56?

A. Yes. But they would have set up -- this is my understanding of it, they would have set up those prices from their back office system. So product master file was on their back office system, they received a sheet to say "these are the prices" and then they would have

to go and manually check that those were the prices or make the changes. So that was where our control issue came in, there were so many hands in each of the elements of the chain that we had no real control over the price that we communicated to the price that was actually delivered to the customer.
MR SUMMERS: May I just be clear: was each of these shops then a profit centre, or were you determining the profit margin from the centre?
A. I don't recall how the accounting was managed. From a category perspective, we were driven to ensure that if the products were sold at that recommended price, it would deliver a certain margin on each of the products sold. But whether the sites were then a profit centre or whether it was amalgamated up and aggregated up into one, I don't know.
MR SUMMERS: So you would say that in setting whatever prices they were setting, at their own initiative, they were just displaying initiative to maximise or respond to local conditions?
A. Yes.
MR SUMMERS: That would be a charitable interpretation.
A. That would, and I think part of the challenge that we had as an organisation was that people who ran the sites wanted to run the business in a way that was relevant

for their local organisation, and this is where we had this mismatch between what was the design of the organisation and what was actually happening. I believe that was one of the key catalysts to move into the RBA agreement, to say, well, actually, if that's what's wanted and that's where the energy is, then it makes sense for us to change the relationship between Shell and the retailer to say "right, retailer, you are now the entrepreneur. The risk you have is you own the stock, but you set the prices and all you need to do is to comply with our health and safety".

THE CHAIRMAN: But at the moment we are talking about the pre RBA situation. You just said, well, there was this mismatch between what you call the design of the organisation and what was actually happening. So was the design of the organisation that the shops should sell at the price that you and ITL have --

A. I believe that was the way that it was proposed -- supposed to work. Again, I don't actually recall seeing a particular document saying "this is how we should work", but again it was a period of turmoil within the organisation.

THE CHAIRMAN: Yes, thank you.

MR LASOK: Can I try and get clarification, at least in my own mind, about this. At this stage the single price in the price file is intended to be the shelf price; is that so?

A. So the price that was communicated out, the Shell retail price, was intended to be the price at which the product was sold.

Q. It's just that you didn't have the infrastructure that enabled you to ensure that every single site toed the party line, as it were?

A. Absolutely.

Q. That's the reason why, I would suggest to you, that when we get to tab 27 D19/27 -- which is the first trading agreement between Shell and ITL -- we see in the first paragraph this provision:

"In return for Shell UK setting the selling out prices at company owned sites reflecting ITL products no worse than the relative RRP compared to other manufacturers' similar products, an annual payment of [an amount] will be made. A detailed list of these requirements is as attached."

I am afraid to say that the figure is apparently confidential.

In other words, here you have an agreement reflecting the fact that Shell would set out, in the price file, the shelf prices that would be applied at the company owned sites?

A. I think in terms of this business plan investment, this was a document which was titled "Imperial and Shell UK". I don't actually recall being involved in discussions for this particularly, although given the timing I must have been. What I do recall, though, is that this was very much optional, so this wasn't "you must do this and you will get this", this was -- it was our choice as a retailer if we laid these prices out in such a way, and that the incentive for that was this [amount].

Given the knowledge that we had in terms of the way our sites ran, I had no great expectations that we would necessarily achieve that, and I certainly wasn't going to invest an awful lot of time in terms of ensuring that certain things were happening for that amount of money, because the business required other areas to be addressed such as the range and the planogramming.

So for me this was optional, and it was probably more by just coincidence that some prices married up to the parities and differentials and other prices didn't, in terms of the way that the retail prices were communicated to sites, knowing full well that the delivery on site would not be fully implemented anyway. So even though the desire from Imperial in this was for a 95 per cent of company sites to deliver it, the reality was I knew we would never ever get to that place, and actually, quite frankly, the effort to do that certainly wasn't worth that money.

So again, this was part of, I suppose, the management of the relationship. That's what Imperial really wanted. I actually wanted to focus my efforts on other things. I didn't have an awful lot of time to go into heavy negotiations around these things or huge discussions. So it was almost a case of "okay, well, if that's what you want, that's fine, but I am not going to write and say 'we are going to deliver that', it's optional". And for [an amount] I could earn that in a month doing promotions, and I think in one of the documents it shows that you could earn [an amount] in a month doing a promotional activity.

THE CHAIRMAN: Yes. Thank you. You must try and keep your answers a little more concise.

A. Sorry.

MR LASOK: If we put on one side for a moment the implementation problem because you didn't have the infrastructure that enabled you to go round to all the sites and ensure that they were complying with the prices in the price file, we put that on side for a moment. That apart, it is true, isn't it, that while you were dealing with tobacco products, Shell did comply with the ITL differentials?

A. No, I don't agree that that is the case.
Q. Okay. Could you go, we are still in annex 19, could you go to tab 13. D19/13. Tab 13 is a letter to you dated 3 August 2000.
A. Sorry, 13?
Q. 13.
A. Sorry, I have 30.
Q. Your reply is in the next tab. I think some of this stuff is confidential. I think, however, it's just the figures. Could you read to yourself the letter at tab 13, and your reply at tab 14, please.
(Pause)
A. Yes.
Q. Now, I would like to put to you again the question I put to you a moment ago: do you accept that, while you were around dealing with tobacco products, Shell did in fact maintain the ITL differentials?
A. Reading these two documents, I can't say that we actually did maintain the differentials. What I can say from these documents is that at this stage we had our own warehouse and we were purchasing the stock directly from the manufacturers, and at that time in the industry there was the opportunity to buy stock forward, and therefore make additional margin. One of the terms and conditions of that from Imperial was that they wished to

have current differentials against our manufacturers' products maintained.

As part of our ability to get hold of this stock and make that additional money, I've confirmed that we would communicate the prices. I can't say whether that was actually what we did.

Q. Now, I would just like to focus for a minute on numbered paragraph 2 in tab 13. Here ITL says two things. So it's the numbered paragraph 2 which starts off with the words:

"The current differentials ..."

ITL are saying two things. The first is it's talking about current differentials being maintained, and then it asks for additional matters to be observed, and those additional matters are introduced by the phrase "in addition". Have you seen that?

A. Sorry, which line? "In addition the following will be implemented", yeah.

Q. So you have two things in that number 2. If you go to your reply in tab 14, and look at your paragraph numbered 2, you say:

"The Shell selling out prices will continue to reflect the differences in RRPs, ie differentials will be maintained in accordance with the facts of 3 August."

Doesn't this indicate that at that stage you had been applying the ITL differentials against other manufacturers, and at this point you are agreeing to carry on doing so?

A. Well, certainly the wording as it is laid out here suggests that. I can't confirm whether that was actually what happened, and -- yes.

THE CHAIRMAN: When you say "was actually what happened", do you mean that those differentials were in fact subsequently reflected in the pricing?

A. Possibly. I don't know whether that was actually the case.

MR LASOK: Is it the case that you simply don't remember this incident?

A. I remember the MPI and the Budget forward purchases, because that was quite an important aspect in terms of the commercial management of the category, given we are talking about [redacted] worth of stock, and there was -- it was important in order to get that right and also the opportunity to then potentially make some additional margin for a short period of time. I don't recall particularly that the prices were maintained at certain levels or that there were differentials in place. Obviously the documents suggest that that was the case, but I don't recall it.

Q. Basically, as I understand it, you are saying: Well, the document does indicate that there was an agreement to carry on maintaining the ITL differentials, but you can't actually remember what in practice happened?

A. No. I mean, I was new into the job, I was not aware that there were these pieces in play. Certainly I don't recall ten years, nine years later what the finer details of this. I recall the forward purchase of stock, but the finer details I don't recall.

Q. I would like to move on but I think I ought to focus a little bit. If you didn't know what had been going on, wouldn't it have been a bit dangerous to send the email at tab 14, because you wouldn't know what you were agreeing to?

A. I don't think it would be dangerous. I mean, given the circumstances, the forward buy was always made prior to price increases. The way that the category was structured in terms of the pricing would have delivered a certain amount of margin, and we were talking about a period of time that prices would have been kept at those levels whilst the stock was bought in, and then there was the opportunity to add the manufacturer price increases onto the recommended retail prices, but we would still have stock at the old price, so there was an additional margin there.

THE CHAIRMAN: When you were shown the trading agreement earlier, you said, "Well, this is a very small amount of money and so this was entirely optional whether we did this", but here the compliance with the differentials seems to be being linked to a much larger sum of money, so at this stage would it stop being optional, because the amount of money was very small, and become something that you were more committed to?

A. No, not particularly. I mean, again my understanding from coming into this category and this industry only a couple of months before, was that this was standard practice if you had direct supply of tobacco products. So prior to a Budget or prior to a manufacturers' price increase, the opportunity was there to buy forward stock. Knowing that we had that opportunity and there was a margin opportunity, or a margin enhancement opportunity, it was something which our business took the view that, yes, it was worth making that investment.

The reality is you buy that stock forward, it comes into your warehouse, it goes out to the sites, it's sold. I knew that the prices on the retail shelves more than likely would not reflect all the parities and differentials, but from a relationship perspective, Imperial were highly unlikely to come back to me to say "We want our money back because you haven't delivered it in this site". It was the flow of the business. So it was a risk I was prepared to take, knowing that, yes, I have signed up to that but in reality I had no control on it actually being delivered.

DR SCOTT: So what you are saying to us is that you were quite content, in Shell, to undertake agreements which you believed you had neither the intention nor the power to implement --

A. I think at this stage --

DR SCOTT: -- in return for that enhanced margin.

A. Essentially, yes, putting it black and white, in this case.

THE CHAIRMAN: And you entered into that to improve your relationship with ITL?

A. This was very early days in the relationship, so I was very much learning what the relationship was about, and there was very little previous knowledge because the person who ran it before me wasn't around. So in this instance it was a case of: if that's what they want for us to secure this, I can say yes but there is no guarantees that I can deliver it. It's conceivable that a conversation would have been had in terms of that, and a common understanding that at Shell we struggled to deliver --

THE CHAIRMAN: Well, you say it's conceivable; do you remember whether there was --

A. I don't. I don't remember.
THE CHAIRMAN: Let's stick to what you remember.
A. Okay.
MR LASOK: Well, another explanation of this is that the way you read ITL's letter at tab 13 was that they were going to give you something if you simply carried on doing what you had already been doing and therefore you didn't worry about it too much, because they weren't asking you to change your behaviour, they were simply asking you to carry on. Is that consistent with your recollection of what was going on?
A. Well, not especially. As I said, there was very little information handed over. I had started the job a month or two before this. So I am -- I cannot recall actually having seen any written documentation or information that suggested this had happened before. But the information coming from Imperial suggests that there was something in place, but I don't recall there being anything particularly documented and in place.
Q. Can we turn now to tab 18. D19/18 I am particularly interested in the first page of this letter. It's dated 22 September 2000. The first heading deals with outstanding payments. If you go just below the second holepunch you have a heading "Business Agreement". Do you have that?

A. I have.
Q. Then you will see that there is a request to send two invoices. The first one, the figure at the end of the line is confidential, so I won't read it out for once, but this is a request to send an invoice for that amount of money in respect of the retail price differential policy running from 1 July 1999 to 30 June 2000. Do you remember anything about this?
A. No. I didn't recall it, and I think, as I said in my second witness statement, I didn't recall any agreement around parities and differentials.
Q. You didn't write to ITL to query this?
A. I don't recall having done so, no.
Q. You don't recall making any enquiries within the Shell organisation about what this meant?
A. I don't recall this at all, no.
Q. It's all a blank?
THE CHAIRMAN: Well, do you know --
A. Around this particular element in terms of the business agreement, I don't recall having conversations around this business agreement. I was never shown any document that was a business agreement before this period. It was unknown to me when I took up the job.
THE CHAIRMAN: Do you recall whether you did send invoices for those ...

A. I don't, I have read some of the other annexes and I see that later on there is another request for an invoice to be sent for that period and a few more months, but I don't recall whether invoices were actually sent.

DR SCOTT: Mr Conrad, we have just seen documents which talk about "continuing the differentials". I do appreciate that you may have no recollection, but somebody who receives a letter which talks about "continuing", might have a clue that something had been going on.

A. Certainly reading this that would be the inference, but I don't have any recollection, because this was so low priority from the business perspective.

DR SCOTT: Yes.

MR LASOK: Now, if you go to tab 27, D19/27, this is just to remind you that we have got to the trading agreements that covered the calendar year 2001, and I've already drawn your attention to this, we have on the second -- or at least the first page, on the second page we have a page of pricing requirements.

I wanted actually to ask you to look at tab 28. D19/28. Could you read this letter, please, it's a letter dated 19 January 2001 addressed to you.

(Pause)

I would like to look again at this numbered paragraph 2, because this is another letter of a like nature to one that we have seen, and it's again about storing pre-buy stock at no additional cost to Shell.

The condition which is set out in numbered paragraph 2 is:

"The current differentials against other manufacturers' products will be maintained/restored after the Gallaher MPI on 13 February 2001."

Then there is a reference to a slightly different treatment of Richmond. Do you remember this letter?

A. I don't remember the specific letter, but I do recall there was an MPI early in that year, I think this was possibly the last one because our depot closed later this year.

Q. Do you remember whether or not you took up the offer that ITL would store the pre-buy stock at no additional cost?

A. I don't specifically recall it, but I think the verbal "yes" from myself, AC, indicates that we probably did.

Q. I put it to you that this numbered paragraph 2 is an indication that Shell had been maintaining the current differentials against other manufacturers' products, and on the basis that you accept that you agreed to these terms, there was an agreement to maintain or restore them after the Gallaher MPI; is that not so?

A. I think in the same way with the previous one we had discussed from August, I think the same principles would have applied, that there was an opportunity to pre-buy stock, an opportunity for some margin enhancement, the condition -- one of the conditions was around maintaining differentials. The assumption counsel makes is that we did, I don't know whether we actually did, and certainly from the experience we had the chances were at site level those differentials weren't necessarily delivered.

I think also at this stage the RBA has started to be implemented, so we would have had a situation where some sites would have been on the recommended retail price and the maximum price. Of course in those sites we wouldn't have been in a position to govern the on-shelf price.

DR SCOTT: Am I right, Mr Conrad, that in parallel with that -- and this is back on tab 27 and it's the second paragraph under the heading "Prices" -- you had agreed to provide copies of the price lists to ITL and that any errors corrected within two weeks of notification to head office is mentioned there, so that you were now in a position where you were providing back to ITL those price lists, whether they were the single priced ones for the sites that were owned and controlled by Shell,

or those under the RBA; is that right?
A. I am sure that we provided price lists. Generally from my recollection price lists were provided normally after an MPI or a Budget, in order that the manufacturers could inform me if I had made any errors related to the price increases, because the price increases weren't always indicative of the recommended retail price going from one place to another from the manufacturers that was necessarily reflected in the cost prices. So I had the somewhat complex role of managing what those cost prices were and how that then fed through to what the site price was, and then on the target recommended retail price that I was looking, could the site earn the margin that we were looking to earn.
So, I mean, I don't recall this particular clause, but I do recall sending them after the manufacturers' price increases in the Budget for them to confirm that I hadn't missed something.
DR SCOTT: And that would also enable them to confirm whether or not you were abiding by the pre-buy agreement; is that right?
A. I suppose by inference that would provide them the opportunity.
DR SCOTT: Thank you.
MR LASOK: I've just noticed the time.

THE CHAIRMAN: Yes. Well, we would normally take a break, but I know that there is some pressure on Mr Conrad as to whether he can continue this afternoon, so I am wondering what the balance is between having a short break but risking Mr Conrad not finishing in time.

MS ROSE: If the shorthand writers are content ...

THE CHAIRMAN: We will take a short break, then, and we will come back at five past 12.

(11.55 am)

(A short break)

(12.05 pm)

MR LASOK: Now, Mr Conrad, I think we were looking at the trading agreement in tab 27. By this stage, we are now moving into 2001, I put it to you that during the period that you were dealing with tobacco products in 2001 Shell complied with the terms of this agreement and did base its prices on the ITL differentials?

MS ROSE: I am sorry, again that question needs to be put more clearly because we are now in the RBA period, and if he says Shell complied and based its prices, it needs to be clarified whether he is talking about the recommended price or the shelf price.

MR LASOK: The prices in the price files were based upon the ITL agreed parities and differentials, weren't they?

A. No, I can't say that they were based upon the ITL parities and differentials. The prices that were in the Shell price file, either the Shell retail price, the recommended retail price and the maximum price, are based on the prices that we needed to deliver the margin, given the cost of the goods and then the retail sell-out price.

DR SCOTT: Sorry, what you said was you couldn't say, you can't say --

A. I am sorry, I can't say that they were based on parities and differentials.

DR SCOTT: Is that because you don't recollect or that you disagree with what was being said?

A. No, I disagree with what's being said.

DR SCOTT: Staying with the nature of your disagreement, what you have just told us is that these price files were designed to maintain the margin?

A. The price files were designed to communicate to the retailers the recommended retail price --

DR SCOTT: And that recommended retail price was designed to maintain the margin?

A. Was designed to deliver a certain margin at that price.

DR SCOTT: And in delivering a margin, is what matters the absolute price?

A. Well, it's a bit theoretical in the sense that we worked out the margin for each of those products from the recommended retail price, which was obviously a function then of the cost-in price, so the theoretical margin that would be delivered if all the products were sold at that price would be X.

DR SCOTT: But that depends, does it not, on the absolute level of the recommendations?

A. Sorry, I don't understand what you mean by "the absolute level".

DR SCOTT: If you imagine that we have an average price, let's say it's £4, for everything, if you want to increase the margin by 10 per cent, the average has to go from £4 to £4.40.

A. Yes.

DR SCOTT: Within that you can have a great variety of different prices.

A. Yes.

DR SCOTT: So what matters is the average absolute prices in terms of achieving the margin.

A. So the -- in terms of the overall margin delivery, it would be a factor of the sales volume per each item and the price at which that is set. Yes.

DR SCOTT: What that implies is that provided the absolute average is high enough, what happens in terms of parities and differentials doesn't matter so much in terms of achieving that margin; is that right?

A. Yes. I mean, theoretically, if the absolute price is at a certain point, whatever was going on with parities and differentials was irrelevant, from our perspective.
DR SCOTT: Yes. Thank you.
MR LASOK: I think you disagree with the point that I put to you, that after the signing of the first trading agreement with ITL, the one at tab 27, the price files reflected the agreed parities and differentials; you disagree with that?
A. To my knowledge, yes.
Q. How close were you to the --
THE CHAIRMAN: Sorry, I do not understand that answer, to your knowledge, yes. Yes, you disagree with that or yes, the price files reflected the agreed parities and differentials?
A. Sorry, no. Yes, I disagreed that they reflect -- that the prices reflected the parities and differentials.
MR HOWARD: I am sorry to interrupt and I don't mean to be difficult, but I think in order to understand the questions, one actually has to first establish what you are saying are the agreed parities and differentials. In other words, it's totally unclear what the witness is agreeing or disagreeing to.
THE CHAIRMAN: Well, I think -- I thought we had gone through that looking both at the trading agreements and

then at these supplementary agreements, if I can call them that, in August 2000 and January 2001, where it appears, subject to what the witness has said, that one of the conditions for this pre-buying stock was these differentials.

MR HOWARD: My point is, for instance you can see on the face of the trading agreements that the term that's being put forward is "no worse than the relative RRP", and you actually have those differences defined. You have to remember the OFT run a case that it wasn't on that basis of "no worse than" but it's actually something fixed specific.

THE CHAIRMAN: I don't think we have quite got there yet. At the moment we are just exploring whether these apparent agreements had any effect at all on what was put in the price files. If the answer is: no, they had no effect, then it doesn't really matter whether the price files were maxima or fixed.

MR HOWARD: Fair enough.

THE CHAIRMAN: If he accepts that there was some influence, then we may get onto the question of: what influence?

MR HOWARD: Okay, well, I've just made the point clear that we don't know actually what it is Mr Lasok is saying the agreed point is.

THE CHAIRMAN: We are not quite at that level of detail yet, I think.

MR LASOK: What was your involvement in the drawing up of the Shell price files?

A. As the category manager, I was the person responsible for identifying what recommended retail price was put forward and establishing from that process the margin that would be delivered.

Q. And you would send these documents round to the manufacturers for them to check them?

A. Yeah, I think as I said before, the only times I recall sending the documents to the manufacturers was after a manufacturers' price increase or the Budget increase, and the reason for sending it was that these complex events in terms of the taxation and duty applied, and it was important that I was reflecting the relevant increases such that it didn't have a detrimental effect on the margin delivery. Ultimately the tobacco companies were the experts in understanding how these were applied.

Q. If you could look at tab 20, please, D19/20, you have here -- again it's two emails, one after the other, but the first one is just by the first holepunch. This is an email from you, it's sent on 25 September 2000, and it's sent to a Carl Pearson of Gallaher, Roger Clarke of Rothmans and Ken Culham of ITL. You send them warning that the current retail prices for the tobacco category and the subject heading indicates that these are the retail prices August/September 2000. Mr Culham then sends the email internally within ITL to have a differential check carried out.

That was what you would expect ITL and the other manufacturers to do at this time, wouldn't you?

A. No, it wasn't. I sent these because of the manufacturers' price increase, and they were aware then what the recommended retail prices were for our product. I was not aware of what Mr Culham was then going to do with it.

Q. Forgive me, but if you weren't aware of what Mr Culham was going to do in, when was it, September 2000, by the time we get to the trading agreement in tab 27, you were obliged to provide price lists and correct any errors within two weeks, weren't you?

A. That's the terminology that's in that trading agreement.

Q. It's right to say, although this happened after your time, that Shell got a payment for compliance during 2001 with this trading agreement?

A. I can't comment on that, I wasn't around at that time.

Q. I think just to substantiate what I've just said, it's tab 43.

THE CHAIRMAN: Well, he has said he can't comment.

MR LASOK: Yes.

Now, you have told us of your involvement with the formation of the price files, and you have also said that the prices did not follow the parity and differential requirements in the trading agreement; is that correct?

A. Let me just clarify. I think, as I stated earlier, yes, I was involved in the development of the price files, they were developed on the basis of what we required to drive margin. In some cases the parities and differentials that were stated may well have been delivered, but in other instances there were products where that was not the case.

Q. Okay. Now, I am going to ask you to do something that some people would regard as courageous and other people would regard as foolhardy and that is to go to tab 27. D19/27. If you go to the second page, you have the price requirements. In my copy I have two separate pages. You have them double-sided printing. What I would like you to do is to lift the lever and open the metal bit so that you can extract the page containing the price requirements. This is the courageous and foolhardy bit, which is removing a piece of paper from a file. You have to remember that it has to go back there, however.

THE CHAIRMAN: Perhaps he could have a sticky note to pop in there.

MR LASOK: I have thought about that, but the problem is when you do this it's actually virtually impossible to do this flicking around like that (indicated). Can I explain why?

THE CHAIRMAN: Yes. Put a sticky note in the file where this needs to be put back. (Handed).

MR LASOK: Right. Now could you go on to tab 32(a), please. This is an extract from Shell's price file, and it's in the bundle at a point after the trading agreement, and in fact it's the closest one in point of time -- it certainly is in this bundle -- to the price requirements that we have.

I fully accept that we can only use the material that we actually have, but I was just going to ask you or rather take you through these price requirements.

So if we have the page with the price requirements, the first one is Embassy No 1, and if we just look at the price requirement, we have 20s packings at least 3p less than the price of Benson & Hedges Kingsize 20s.

If we now turn to the extract from the price file, we can see that Benson & Hedges Kingsize 20s appear fifth and sixth lines down. If we look along to the right-hand side, we have the two prices which at that stage were in the price file, the recommended retail price and the maximum retail price.

Now, Embassy No 1 20s is just over halfway down. If you cast an eye down that page, you will come to Dorchester, which is underlined, and five after Dorchester we have Embassy No 1. If you look across to the right-hand side, you will see the prices, 4.40 and 4.44. Lo and behold they are precisely 3p less than the price of Benson & Hedges Kingsize 20s.

Now, in fact I have gone through this extremely boring exercise myself in relation to the price requirements, and as far as I can see, in each and every case, the price file complies with the price requirements that we have.

The one difference concerns Richmond. If you look at Dorchester, in the middle of this page, and run along to the right, we have 3.66 and 3.86. Do you have that?

A. I have, yes.

Q. If you turn to the next page, seven and eight down, we have Richmond, and we see that the prices are different, it's 3.60, 3.61. Do you have that?

A. Yes.

Q. Now, the price requirement in the contract, which is the seventh one down was that Richmond was to be at least no more than the price of Dorchester. But the explanation for the price of 3.60, 3.61 and the reason why it wasn't at parity appears in tab 31 at page 2, because if you look at page 2 -- I think some of these figures are confidential, but if you cast an eye down that page you will see that ITL had offered to provide support from a pricing of Richmond at 3.60 and 3.61. And that's the reason, it would appear, why Richmond and Dorchester don't correspond to the price requirements that we have.

Now, I could take you through each and every one of these pricing requirements in the contract, and compare them with the price file that we are looking at, but where the price file that we have here does list brands that are mentioned on the price requirements page, you on each and every occasion have the differential exactly as stated in the price requirements document. Exactly.

THE CHAIRMAN: Well, when you say exactly, let's just be clear, are you saying that where in the price requirements it says "no more than 9p above", say, what you are putting to the witness is that he is in fact 9p above and not just no more than 9p above?

MR LASOK: Yes, it is the exact amount. So, for example, we looked at Embassy No 1 and it says "at least 3p less", in fact it is 3p less. If you look at Regal, Regal is on the second page of the price file, and we are looking at Regal Kingsize, which is the sixth line down, and if you have the sixth line and look to the far right, it's 4.38, 4.42. So the question is: is that 5p less than Benson & Hedges? And lo and behold, it is exactly 5p.

MR HOWARD: It's also at least 5p less.

THE CHAIRMAN: Yes, it is also at least 5p.

MR LASOK: I am going to put the question to you again -- well, I'll rephrase it: do you still stand by your answer that you gave to an earlier question of mine, that you did not price in accordance with ITL's parities and differentials?

A. No, that was not the driving force. The driving force was about margin delivery, and I think you will see also that the cost prices are different between these products, and so that would have been the key driver in determining where to position the retail price. Furthermore, these are recommended and maximum retail prices, and so that's what was communicated to the sites, but obviously the sites were at liberty to price on shelf at a price that they chose to.

DR SCOTT: Sorry, Mr Conrad, you puzzle me. Can we go, for example, to Benson & Hedges Kingsize 20s?

A. Yes.

DR SCOTT: The Shell invoice cost is confidential, so I mustn't read it out, but I would like you to look at the number in the red box against "Benson & Hedges

Kingsize 20".
A. Yes.
DR SCOTT: Now, I would like you to go down to Embassy No 1 size 20 and look at the equivalent number in that box.
A. Yes.
DR SCOTT: Now, can you now take me through the way in which the margin is being sustained between those two? I don't have a calculator with me, but can you explain to me how that margin -- you may want a calculator -- works? If your focus was on the margin --
A. Yes.
DR SCOTT: -- how do we get from the one to the other on a margin basis? As I understand it, the invoice cost is for a pack of ten?
A. It would be a pack of ten packs of 20, yes.
DR SCOTT: So what you would say to me, then, is that pricing was near to but not exactly the differential of three times ten?
A. Without calculating, essentially, yes. There was also, from the recommended retail price, you had to strip out what the VAT was, because all of the margins were worked out ex VAT, so that would then also have had an impact. It's not a calculation I can recall. So it would have been the invoice cost which was primarily driving the end recommended retail price.

DR SCOTT: So I think in fact in that case you can explain it either way?
A. Sorry, can you clarify?
DR SCOTT: Yes. If you take the figures in the two boxes which we are not allowed to discuss, the difference between the two figures -- am I allowed to say this?
THE CHAIRMAN: Is 3p --
DR SCOTT: Is 3p.
A. In terms of the cost profit.
DR SCOTT: Roughly, yes. So you can explain it either way, either on the margin basis or on the pricing requirement basis.
A. That in this case the differentials come out at 3p.
MR LASOK: How is it that you managed to, in this price file, hit all the differentials that we can locate if you weren't complying with your contract with ITL?
A. I don't specifically recall that process in terms of saying "these are the differentials, this is what I need to drive". My role was around driving the margin, and in this instance, yes, the differentials have come through. But I did this in the knowledge that at retail site level, that may not be the case in terms of what the customer was paying.
Q. I put it to you that this is simply clear evidence that you were complying with the contract that you had with

ITL in return for which you received payment the following year.

A. I am sorry, is that a question?

Q. It was a question, yes.

A. Sorry, could you repeat it?

Q. Yes. It's clear evidence that you were complying with the terms of the contract that you had with ITL for which you were being paid?

A. I think, I mean, this is evidence in one instance that a number of products have reflected parities where its part of the business investment plan or business plan investment.

So the evidence here suggests that that was the case. I can't say for sure that that was then reflected in other files, and I know for sure that that wasn't necessarily what the price at retail site was.

THE CHAIRMAN: But was it what was in your mind when you set these prices?

A. I can't recall whether specifically that was in my mind at the time because my focus was about the category margin, first and foremost.

MR LASOK: Right. I think the next most important thing is to put the floating page back where it came from, which is tab 27. We have been looking at this price file, and we have these two prices, the recommended retail price

and the maximum retail price. When did the price file change from single price to two prices?
A. I don't recall the exact date, but it would have been some time when the RBA started to be rolled out.
Q. Well, I wondered about that, because if you turn to tab 32 -- I've already drawn your attention to this -- you will see that if you look at Mr Culham's email at the top of the page, which is 9 March 2001, he says in the third line that there are now two prices to show. Maybe I haven't drawn your attention to this one.
A. No.
Q. Is this the first time you have seen it?
A. This is, yes.
Q. Okay. Well, then, you will see that it actually starts off with an email from you which attached a list of the products that had a changed retail price. Then Mr Culham, when he forwards the price list along to Ms Eager, he says that there are now two prices to show, and refers to the Shell retail price and the maximum allowed at the site.
So would it have been around about March 2001 that you moved to a price file with two prices?
A. As I stated before, it was some time early in 2001, I believe, when the RBA was rolled out, and as part of the compliance with the agreement with the contractors,

we would have had to have shown two prices.

Q. It looks from this document and others that the pricing that Shell now had was tiered pricing, you had two levels of pricing, you had what was described as the -- here in Mr Culham's email it's described as the Shell retail price; in the price file that we looked at it was the Shell recommended price. So you have two prices, the Shell recommended price, as it was called, and a maximum price, and the independent contractors were free to choose which of the two to apply. Is that correct?

A. No, that's not correct. It wasn't a price tiering, there was a Shell recommended retail price which the category managers advised as being recommended based on the use of market knowledge, input from suppliers and so forth. And then there was a maximum retail price, which was part of the contract with the retailers, that was in place to prevent what we called insult pricing. So putting a product into the shelves and selling it at a price which would cause offence to our customers.

Q. In this email that we are looking at, Mr Culham shows that he thought that most of the prices would be at -- I should say he says -- I'll quote verbatim what he says, it's the bit before he says "hope all is clear", he says:

"Most should be at the Shell retail price but there will be some at the maximum level."

If we look at the second page of this document, we see that in fact we have a list of prices but we have always two prices: the Shell retail and the Shell maximum retail. When he says "most should be at the Shell retail price" it looks as though he is referring to the sites, "most sites should be at the Shell retail price but there will be some at the maximum level". Was that a correct understanding on his part of what was the situation in March 2001?

A. I can't comment on what Mr Culham thought. Certainly my recollection of the situation and what would have been communicated was that there was a recommended retail price and a Shell maximum retail price, but the contractors, the agents, were at liberty to price where they felt best for their location.

Q. But to your recollection, would it have been correct to say that most sites would be at the Shell retail price but there would be some at the maximum level?

A. I can't recall whether that was the case, I would be speculating.

Q. You see, the independent contractors are moving from a regime in which Shell had determined the retail price, and they are now moving to a regime in which they are told that there are two prices, one is the Shell retail price and the other one is the maximum price, so I would suggest to you that the impression given is that there were two price tiers, there was the price tier indicated by the Shell retail price and the maximum price, and they could choose between the two?

A. No, the interpretation from this small amount of text is that there are two prices. I know that we communicated a recommended retail price and a Shell maximum retail price. The contractors were able to price at whatever point. Some of the contractors -- I think as we heard from Mr Moss yesterday, some of the contractors were new to Shell and independent business people so they wouldn't have been exposed to pricing previously. Some would have been existing employees of Shell who now invested in the business and were independent. They would have seen what the prices were before, but I can't say whether they would have particularly followed the pricing regime or the pricing proposals in the master file that they would have received.

DR SCOTT: And you heard the interchange with Mr Moss about the margins that there were expectations that these new contractors would achieve, the concerns that they had and that Shell had about those margins being adequate, and the floor and ceiling of 70 per cent and

140 per cent, and you have already explained to us that margins loomed large in your own mind before the RBAs came in, and presumably they continued to loom large in your mind when the RBA came in, not least for relationship and contractual reasons?

A. For sure. I mean, we certainly weren't in the business of selling product for no return. Under the RBA, the relationship changed in that we now also had a responsibility to not only Shell but also to the independent retailers, the contractors, such that certain categories of product -- so I think we saw it in one of the files, it had main group 41, so that was cigarettes, and there would have been a category margin, which we would have been striving to deliver on the basis of the sales and the recommended retail price.

The independent contractor would then choose what retail price he wished to deliver to the customers, knowing that in order to deliver that percentage for main group 41, the position was around about the levels that we recommended. But equally, his business, whether it was in central London or the north of Scotland, would have a different mix of sales. So in central London premium product sales, higher priced product sales, which earned a better margin, would probably have a higher volume. So he could then equate whether he wanted to have a lower price to encourage competition or actually, for want of a better word, to milk that margin by having a higher price and driving with the demand he has.

Equally the shop in Scotland might have a different mix, where he knows that the lower cost product drove a lower margin but he had to be competitive because of what was around him.

So that was the way that that relationship worked under the RBA.

Now, the category of tobacco was globally within Shell, I think, about 25 per cent of sales, so what I could do in tobacco affected 25 per cent, and what we did with one or two products in the grand scheme of things wouldn't have particularly pushed the 140 per cent or the 70 per cent.

I think as Mr Moss explained, that was a floor and a ceiling to effectively protect against specific external events, so my understanding was that we could drive the category and the focus was to deliver margins in and around that position, the independent contractors made the choice.

Now, whether that would then push them higher or lower, I am not sure whether it would have necessarily affected them that much in terms of that, that was much

more about the road closures or other external events.
MR LASOK: Both before and after the RBA was introduced -- when I say before and after, it was introduced over a period of time, starting in, when, it was October 2000 or something like that, was it?
A. I believe there is a chart that shows when it started.
Q. Yes. It was pretty well completed by August 2001, so you are there at a time when the migration to the RBA is in full swing?
A. Yes, that's correct.
Q. In that period, I put it to you that ITL understood and operated on the basis that Shell was in a position to control or materially influence the shelf prices in the sites of the independent contractors?
A. No, I wouldn't agree with that statement.
Q. All right. At no stage did Shell tell ITL that the position was different?
A. No, that's not correct. I, as my role as category manager and having the relationship with the suppliers, would have been responsible for communicating the changes that we were having, one of which was a critical one around the independence of the contractors. I do recall that both Imperial Tobacco and Gallaher were particularly uncomfortable with this approach because they felt we were now becoming an organisation of 600

independents, which was effectively much more difficult to manage from their perspective. So part of my role was to assure them that, whilst the relationship between our independent contractors and the central head office had changed in terms of particularly around pricing, our focus was very much about delivering the customer offer. That's why we were doing what we were doing, because we needed that entrepreneurial element to help identify and deliver the offer that is relevant for the site in whatever location.

Now, whether Imperial Tobacco understood this or not I can't comment. I mean, I have seen some documents that suggest that they recognised that now the agent was the person who set the price.

Q. Well, now, look, if you move back to tab 27, D19/27 and you look at the third paragraph, it says:

"At least 95 per cent plus of company-owned sites must follow the official Select price policy guidelines."

What were the official Select price policy guidelines?

A. I don't recall a particular document that was a Select price policy guidelines, that's -- I would infer that that would be following the recommended retail price or the Shell maximum retail price, on the understanding that as an independent contractor ultimately they would make the choice of what the price would be on the shelf.

Q. You don't see this as an expectation on ITL's behalf that the 95 per cent plus was achievable?

A. I am sure that ITL had an expectation, an aspiration, that 95 per cent was achievable. At this time I couldn't comment how close we got to that, I am pretty certain that we didn't get to 95 per cent. I think, as I said earlier, I saw this clause, this piece, around prices as optional and that the value of money attached to it was such that I could make that choice.

Q. If you go to tab 29, D19/29, and just look at the first page of this letter, 23 January 2001. (Pause).

A. Yes.

Q. You will see by the second holepunch that they have observed a situation in which a certain percentage of sites were charging above the agreed price. Then they move on, and under the heading "Richmond Kingsize Price Hold" they offer to pay a retro outer allowance on condition that a particular selling out price, which must mean a shelf price, is maintained at most sites. After that, they say:

"This will be to keep your sites more into line with the market."

Doesn't that indicate that their understanding was that you were in a position materially to influence or control the pricing at the sites?

A. I don't believe it does. I think one reflection in terms of the 43 per cent of the sites charging above the agreed price is a clear illustration that we weren't able to do so, to control or influence the price at site. I think the language that is used by Imperial in terms of selling out price, my interpretation of that was recommended retail price, because knowing full well at this stage that we didn't have any control over the price on the shelf.

Q. We don't have any letter from you correcting the position, do we?

A. I don't know, I don't recall whether I did send a letter or didn't. But ...

Q. But if they were wrong, surely you would have pointed it out?

A. I am sure I would have indicated in conversations that -- and I do recall reiterating on a number of occasions, because of the change, that we could only recommend the retail price and set a maximum retail price; beyond that we had no control over the prices at site level.

Q. That was January, so if you had told them at that stage or shortly afterwards, would they have written the letter that we find at tab 31? Just read the whole of that letter. I've pointed out the second page to you, but perhaps you could read the whole of the letter to yourself.

(Pause)

A. Okay.

Q. You see, they are still writing to you now, in March 2001, about specific price points in the sites, and if you look at the second page, right in the middle, we have:

"However, the following support can be offered in return for the prices shown, ie ITL will defer the Budget increase, if the following is achieved in sites by week commencing 19 March."

Then if you run down a bit to the second holepunch, the bit just above it, you have a sentence:

"As you can see, our support level will increase but is subject to the above prices being effective in all sites."

Then they say:

"If you decide not to take up the offer, will you please arrange to alter your selling out prices to the same as Dorchester."

Now, that, does it not, indicates that they understood your position to be that you could control or

materially influence the shelf pricing on the sites?
A. I think what I can say in terms of this letter, this is a dialogue or a review of various things that have happened over a period of time to this particular product. I was very clear that there was a limit to what we could deliver at shelf and within the site, and at this stage with the independent retailers in place and rolling out, there were two things we could offer. One was to communicate what the Shell recommended retail price was and what the Shell maximum price was. What I couldn't guarantee or deliver was what the price on the shelf was.
DR SCOTT: Mr Conrad, the question contained two possibilities, one of which was control, and what you have been saying to us is that you felt unable to control, as a category manager, the pricing at the local level.
A. Yes.
DR SCOTT: The other part of Mr Lasok's question is whether you could materially influence pricing at local level. Now, you may want to ask him what he means by "materially influence" --
A. That was exactly my question, what does he mean by "materially influence"?
MR LASOK: That you could contact the site or that it was

more likely than not that the site would follow the pricing in the price file, and that if there was a divergence from the price file and you contacted the site in question, it was more likely than not that the site would fall into line?

A. I think that there is an assumption here being made that, because of this line "it more likely than not would happen", the reality of the situation is prior to this point we were unable to control even our direct managed sites, now in this situation we had the independent retailers who were free to price at where they wished to be. So whether we could materially influence this was open to question. We were going through a period of learning with this new agreement in place. So this was the aspiration of Ken Culham in ITL but it was by no means what I would have agreed to in terms of agreeing to say that we could deliver certain prices on our sites.

MR LASOK: Now, could you turn to tab --

THE CHAIRMAN: Could I just ask you, on that page, under "Going Forward", it says:

"The new RRP assumed Shell retail price."

So there he does seem to be thinking that the RRP, one can assume that that's the same as what the Shell retail price would be? Or is that not the correct reading of that?

A. I think again this was the period where we were moving from the old price file approach of the Shell retail price to the new recommended retail price plus the Shell maximum retail price. And I think here Mr Culham is making an assumption that the two are connected, but that's not necessarily the case.

MR LASOK: Now, if you turn -- this letter was written --

THE CHAIRMAN: Is that a good moment to break or if you want to go on a little longer --

MR LASOK: I am coming to the end. I have one point on tab 32. However, I have another point concerning Mr Conrad's first witness statement that in principle is a short one but which I fear may take a little bit of explaining because it's connected with about three documents. So it's perfectly possible that that one might take about ten minutes.

THE CHAIRMAN: Well, let's finish your point on document 32, then, before we break.

MR LASOK: The document we are just looking at was 9 March 2001. If you go to 32, D19/32, which we have seen before, the day before that you had emailed Mr Culham with what you described as the Shell retail prices. Mr Culham is there, with your email, being told by you that this is a list of the changed Shell retail prices, and he's also got information from somewhere that, when you look at the two groups of prices, most are going to be under the column "Shell Retail Price", that's to say most sites, and some will be at maximum level, but at this stage you are telling Mr Culham that these are retail prices?

A. I think what you have to bear in mind is that this is a period of change in our business, so a number of factors are changing, and one of them is around the terminology we are using for Shell retail price, recommended retail price and so forth. I think in this instance it's clear that the Budget's happened, we need to understand if we have made the price movements that will cover the tax and duty increases, and I've used terminology which was historically what was being used. The reality of it is that the Shell retail price is now the recommended retail price, because that is what the independent contractors are working to, and then they also have the Shell maximum price. So I think it's just a case that the terminology hasn't moved on with quite the finite detail that would be hoped for, but this was a period of great change.

Q. I am sorry, Mr Conrad, but surely you should have said that the first price was nothing other than a recommended price. Wasn't it wholly misleading to

describe what you were sending to Mr Culham as the Shell retail prices?
A. I don't believe it was wholly misleading --
Q. In which case they were the retail prices?
A. No, I don't believe it was wholly misleading, there was an understanding that we were moving to this new model and that there were two prices: one was the recommended and one was the maximum. In this instance, I didn't make the change, of the terminology "Shell retail price", but that's all I can say about it, I don't recall this particular exchange. But that's what I can ascertain from what I have in front of me and the time we were at.
Q. But you did make the change, because the true position was that you have now moved to two prices, there was the Shell recommended retail price which was the minimum price and there was the Shell maximum price which was the maximum price, and the contractor could choose between the two. That's the correct position?
A. No, that is not the case. The Shell retail price was not a minimum price, it was a recommendation, and the maximum was the ceiling to prevent insult pricing. The retailer was at liberty to choose a price from the maximum down to whatever point they wished to choose.
MR LASOK: I am now stopping the cross-examination on this

document, and there is only just one more issue that remains.

THE CHAIRMAN: Yes, Ms Rose.

MS ROSE: Madam, can I just ask where we are going? I don't know exactly what the constraints are on Mr Conrad. It was my understanding that he had a difficulty this afternoon, I don't know from what time, perhaps the Tribunal would like to ask him.

THE CHAIRMAN: Yes. Mr Conrad, obviously we have not managed to complete your evidence this morning, and it would be best if you were able to stay, if you could make arrangements to stay this afternoon to complete your evidence. Is that going to --

A. I can. I have to make one phone call at lunch to just establish if that's possible, but I will ensure that it is possible.

THE CHAIRMAN: Thank you very much. We will come back at five past 2.

(1.05 pm)

(The short adjournment)

(2.05 pm)

MR LASOK: Mr Conrad, could you get hold of your first witness statement, please, and it will be at tab 115.

A. Yes, I have that.

Q. Could you go to page 139, please. C11/115/139. What

I want to do, I've cross-examined you already on a number of matters dealt with in your witness statement and in particular the last two pages, but what I want to focus on is an incident concerning Hamlet 5 that you refer to in the second half of paragraph 7.23. Now, in 7.23 you talk about the price files and you refer to annex 19, document 32, which I've already taken you to and in the middle of that paragraph you say:

"ITL would then communicate whether Shell had accurately accounted for these changes in its price files."

Do you have that place?

A. The last five lines, is that what you are referring to?

Q. Yes, I am referring to the Hamlet 5 incident here.

A. (Pause). Yes.

Q. You refer to it again in the first sentence of paragraph 7.24.

A. Yes.

Q. You refer to it a third time in paragraph 7.25, in the second half of the paragraph. In the second half you say:

"I was prepared to let them tell me what prices they thought we should have, but if I did not agree I simply did not implement their suggestion (as was the case for Hamlet 5s, see document 9 of annex 19 ...)"

So you have that in your mind, have you?

A. I can see what's on the page, yes.

Q. So thus far you have described this incident in three different ways. In paragraph 7.23 you say that it was an error, that's in the line just after the reference to document 9 of annex 19. You give the cross-reference to the document as an exhibit, AC18. You give the date of the document, and you describe it as follows, it's a document "where ITL highlighted an error."

Then in 7.24 in the second line you simply describe it as an incident of non-implementation of a recommendation. In 7.25 you describe it as an intentional non-implementation, because you say in the bit I drew your attention to that if you didn't agree you simply didn't implement the suggestion.

You are referring here to a document in bundle 19. What you might want to do is to keep those pages of your witness statement open so that you can remember and refer back to what you said, and go to annex 19 and to tab 9. D19/9.

A. Yes, I have that.

Q. What we are talking about is what's referred to on the first page of this letter, under the heading "Budget March 2000". So could you just read the two paragraphs that follow that heading, please.

(Pause)

A. Yes.

Q. I am just trying to get this right in my mind: are you saying that this was an error, that this was an unintentional failure to implement, or an intentional refusal to implement? (Pause).

A. Sorry, could you repeat the question?

Q. Yes. In paragraph 7.23 of your witness statement you say that ITL had highlighted an error. In paragraph 7.24, in the second line, you refer to it as an instance of non-implementation. In 7.25 you state that it was non-implementation because you did not agree. So I am just putting to you the three possibilities that seem to be what you are saying. One is that it was just an error, the second is that it was unintentional failure to implement, and the third is that it was a deliberate refusal to implement. I was just wondering which one it was?

A. Okay. So in this specific incident, I don't recall that moment per se, but certainly reading through this, in paragraph 7.23, the reference to error is really reflecting what has been communicated to me in annex 19/9 from -- I think this is Ken Culham, saying he's highlighted a price error.

Now, at that stage I am not sure whether that's necessarily a price error which is related to the failure to increase the price enough, on cigars, or for some other reason. I do recall that, when Budgets were made by the Chancellor, the transparency on pricing for cigars and rolling tobacco was even less transparent than cigarettes because of the way that the duties were applied on a per gram basis, and there was a different content that applied different duties. So often the prices of those products weren't clear until some days after the actual Budget, whereas with cigarettes it was a little bit more transparent, if not completely.

So I am reading this, in this instance, to say that an error has been highlighted, but that may be because I've miscalculated or some other reason.

In terms of paragraph 7.24, the statement I say is what we were at liberty to do, it was our choice whether to implement suggestions or recommendations or not, as was the case for Hamlet 5s. Well, document 9 of annex 19, in this instance it may be such that we have chosen to keep the price at whatever that price was.

THE CHAIRMAN: Well, in paragraph 7.25 it seems that what you are saying is that you actually recall, at least when you signed that statement, that this was an instance of you simply not implementing their suggestion.

A. And that's --

MS ROSE: Madam, I am sorry, but I do think this is being put on a false basis, because it's the last sentence of 7.23 that's the point, it's what happened after the error was highlighted.

THE CHAIRMAN: Well, that may be a point, but that's not the point that's being put to the witness at the moment. The point that's being put to the witness is that this document seems to be being cited by him in his witness statement as an example of three different kinds of things, and Mr Lasok's trying to clarify which of those things he is saying it's an example of.

MS ROSE: That is clearly not what the witness statement says, because if you look at the witness statement, what he says is that in that document the error was highlighted, and that then, although Shell appears to have priced in accordance with ITL's price recommendation of 2.88 for Classic cigars, which is what they were saying in that document, they didn't achieve parity with Hamlet, because the Hamlet cigars were increased to higher. So the document that Mr Lasok ought to be showing the witness is the two price files from the succeeding months which show that, yes, they put the price of Classic up but they didn't put the price of Classic at the same price as Hamlet. That's

the point that's being made in the witness statement.
MR LASOK: I am afraid I disagree with that, and my learned friend has identified that there is indeed a second point, which I was going to come to, because I would like to, at a later stage, take the witness to the last sentence of paragraph 7.23. But at this moment I am focusing on the prior point.
A. Sorry, could you ...
THE CHAIRMAN: Well, in each of those paragraphs, in brackets you refer to this same document.
A. So my recollection of this, in terms of seeing this, was firstly this was an error, so Imperial Tobacco were at liberty to indicate if they felt there was an error, whatever the reason for that might have been. Equally, at all times we were free to implement the prices that we felt were right, whether they met with the suggestions or didn't. And indeed in some instances we were at liberty -- we did not implement those suggestions, and I think in this instance there is -- it's not clearly apparent from this document that -- which way it actually did go, but obviously later on the price files show that we did increase the prices and they weren't aligned with Classic cigars.
MR LASOK: Now can I ask you to look at tab 9, you have it out in front of you.

A. Of annex 19?

Q. Yes, it's the letter of 11 June, and at the bit that I asked you to look at. Mr Culham, I think it is, writes:

"I highlighted a price error in your post Budget prices which you said would be corrected in sites by 1 June."

Now, does that shed any light, does that assist your recollection of what happened, or is it that you can't remember?

A. I don't remember this specific incident. This is one product at a time when we had many products and much change going on. So the level of detail that's being requested to be recalled is just not something that I have, to my recollection.

Q. Well, if you don't remember this incident, why did you say in paragraph 7.25 of your witness statement that this is an example of you not agreeing and simply not implementing a suggestion?

A. My inference in this is that we were at liberty to select the prices, and in this case, as was shown by the evidence of the other price lists, we obviously haven't made the changes as were suggested, from this letter.

Q. If we go back to the letter at tab 9, I'll draw your attention again to the sentence I read out to you, in which an error is highlighted to you and it is recorded that you said it would be corrected. On the face of it, there was agreement between you and ITL that there had been an error and the error was going to be corrected, and more particularly, what is said here in the letter in the next sentence is that the Classics had to be sold at the same price as Hamlets, that's at parity?

A. I don't recall this specific incident, and --

THE CHAIRMAN: So you don't remember whether you did have a discussion with Mr Culham in which you agreed that you would correct this?

A. I don't recall a discussion. The only reference I have is the letter that was sent to me. Now, in that conversation he is saying that I agreed it, I can't recall whether I did or didn't agree it, the price that it should be sold at, according to Mr Culham, was 2.88, the subsequent price files show different prices, so I can only infer from that that whilst in any discussion we had -- we had at the meeting at the end of May, I've then looked at it and made the decision that actually that's not the price that we want to be at.

DR SCOTT: Mr Conrad, if you look at 7.25 in your statement, the last sentence says:

"They could see when I was not complying and know the limits of what I would do following the implementation of the RBA but presumably did not react strongly because they also wished to preserve a good relationship."

We then look at the letter at 19/9, and there is nothing in that letter which suggests that the two of you aren't trying to preserve a good relationship, but in that letter he highlights what he sees as a price error, he highlights a conversation in which you appear to have said you would correct it by 1 June, and then Classic cigars should now be sold at £2.88, the same as Hamlet 5s.

Now, all that suggests that (a) he was reacting, (b) he was seeking to maintain the relationship, but (c) part of that good relationship was that you were assuring him that something was going to be done about what he saw as an error.

Would you agree with that?

A. You could certainly infer that into those two lines. What we don't see is whether there was any other correspondence related to this. All I've seen that there are other price files in June and July that indicate price increases. So whether they were conversations or whether there was other form of communication I don't know.

DR SCOTT: But you would agree he did react to it?

A. In this instance, he has, albeit several months after the event.

MR LASOK: It can't be several months after the event.

A. I'm working on the principle that it was a March Budget so the implementation of those prices would have been at some point in March. We are now in June.

Q. All right. If you go to tab 11, this is an ITL document dated 3 July 2000, D19/11, and if you look down the left-hand side there is a box that says "Pricing Availability Survey", and it says:

"Hamlet 5s and Classic 5s pricing has now been resolved and should now be the same."

So it looks as though by 3 July 2000 ITL had believed that the two products were being priced at parity. I ask you to note that because in your witness statement, at the end of paragraph 7.23, you refer to two price files indicating what you say the position was, and I want to refer to the first of those price files because it's the one that immediately precedes the ITL national accounts brief; right?

Now, that one, which is the one dated 15 June 2000, you will find at tab 10(a) in annex 19. D19/10a

If we look at this, my copy has two horizontal lines drawn in sort of the body of the list of products. Have you also got two horizontal lines?

A. I have, yes.
Q. The lower one has Hamlet 5s?
A. Yes.
Q. If you follow the line across, to the right-hand side, it's 2.95.
A. Yes.
Q. The upper line is Classic Small Cigars 10, and if you follow that one across, it says 2.88?
A. Yes.
Q. Okay? Who drew the upper line?
A. I have no recollection of who would have drawn that.
Q. How do we know that that upper line is accurate?
A. As in -- sorry, let me clarify. In terms of who drew the line underneath "Classic cigars"?
Q. Yes.
A. I have no recollection of who would have done that.
Q. You don't know who did it?
A. No, I don't.
Q. Do you know whether it's right or not?
THE CHAIRMAN: What do you mean by "right"?
MR LASOK: Whether it's the right product, whether it's the right brand.
A. In terms of right product, right brand, are you referring to --
Q. Classic 5s.

A. -- Classic cigars and Hamlet 5s?
Q. Yes. Let's do it this way: could you go to tab 5(a) What you should have in 5(a) is again an ITL document, it's a national accounts brief, it's dated 10 April 2000. On the second page it has a list of prices. Do you have that?
A. Yes, I do.
Q. You have the brand on the left, then you have the pack size, and then you have the Shell SKU code.
A. Yes.
Q. Okay? If you look right down the column, it's the fifth from the bottom, we have Classic 5.
A. We have Classic as the brand and the pack is 5.
Q. And that has an SKU code of 497?
A. Yes.
Q. Right. If you now turn back to 10(a), the first horizontal underlining in the middle of the page is for Classic Small Cigars 10 with a Shell stock code of 61901. But if we move three up, we have Castella Classic 5s which have a stock code of 497, and if you look to the right, it has the Shell retail price of 2.95, which is the same as the Hamlet 5.
A. Yes, I can see that.
Q. The reality is that there is no basis for believing that the Castella Small Cigars 10 are the Classic 5s that are

referred to in the correspondence we have been looking at. Would you accept that?

A. Sorry, could you just clarify, you were saying that the Classic Small Cigars that's underlined could be a different product to the Classic cigars that we were referring to in document 9?

Q. I'm pointing out that the correspondence refers to Classic 5s. If you look at 10 ...

THE CHAIRMAN: It's tab 9.

MR LASOK: 11 refers to:

"The Hamlet 5s and Classic 5s pricing has now been resolved."

THE CHAIRMAN: Just so I am clear, Mr Lasok, is what you are putting to the witness that the error that's referred to at tab 9 as between Classic cigars and Hamlet 5s relates to the Castella Classic 5 as opposed to the Hamlet 5s, rather than the Classic Small Cigars 10 as opposed to the Hamlet 5s.

MR LASOK: That's right. Part of the problem about this is that, if you look at the 10(a), on the face of it, the two horizontal lines are seeking to compare Hamlet 5s with Classic Small Cigars 10. In fact, if you just look at this table, just view it objectively, we have a reference to two Classics, we have the Castella Classic 5 and the Classic Small Cigars 10, but actually we have no basis for believing that the correspondence refers to Classic Small Cigars 10 as opposed to Castella Classic 5s.

THE CHAIRMAN: What did the trading agreement say?

MR LASOK: This was before the trading agreement, and we have limited documentation about this. What we do know is that if you look at, for example, tab 8, there was a problem that had been noted about Hamlet 5s and Classic 5s, and the reference -- it's under the price availability survey, and it says that Shell have been informed and are awaiting action.

The upshot is that we have an explanation in Mr Conrad's witness statement that he accepts is dependent upon an unknown person who has drawn a horizontal line on the price file, but we actually have no independent basis for believing that that horizontal line has been drawn in the right place.

THE CHAIRMAN: Well, what did you understand was the correction that was being pointed out to you that particular cigars should be the same as the Hamlet 5s? Regardless of whether you agreed with that, which was the comparator did you think that Mr Culham was referring to, was it the Classic Small Cigars 10 or the Castella Classic 5, or can you not remember?

A. As I said, I don't specifically remember the discussion around this. Certainly looking at the evidence, and I think my eye was drawn to the line, that was the comparison that I would have made in this instance. Actually if you go to tab 11 and you do the comparison on the Castella 5 Classic then there is a disparity -- there is a difference between the price of that product and the Hamlet 5s. So I think it was more about the fact that the Hamlet 5s were being priced at the price that we wished to set them at, and then in this instance we weren't influenced by what Mr Culham was requesting.

DR SCOTT: On this document, they are in fact priced at parity with the Classic 5s.

MS ROSE: Sir, not if you look at the July file, which is at 11A, you will see that both of the Classics are at different prices from the Hamlet.

MR LASOK: My learned friend is perfectly correct, if you look at 11(a), there is complete disparity between the prices of the three products. What we have in 10A is parity between Classic 5s and Hamlet 5s, and we have a document at 11 that says that the problem about Classic 5s and Hamlet pricing has now been resolved and they should be the same.

THE CHAIRMAN: But your evidence, as I understand it, Mr Conrad, is that so far as your witness statement relies on the document that's at tab 10(a) as indicating that you decided at the time not to comply with what you seem to have said you would do, which is to correct the pricing, that your evidence was based on the fact that when you saw this document at tab 10(a) those lines were drawn and that was the comparison you thought was the relevant one --

A. That was the comparison I thought I was making.

MR LASOK: I have no further questions.

THE CHAIRMAN: Mr Howard.

Cross-examination by MR HOWARD

MR HOWARD: Let's see if I can help. If you turn, while we have this point open, the letter at tab 9 is written on 11 June, and you can see it's about a Budget in March 2000. There had been a Budget in March 2000 where we know from -- I don't need to give you the document, we all have it -- that cigars, Small Classic Cigars had gone up by a certain amount, I think cigars generally had gone up in the Budget by 8p.

If you go back to tab 8, Mr Conrad, this is an internal ITL document, and what you can see, what ITL internally was concerned about was that Hamlet 5s are currently 7p below Classic 5s, Shell had been informed.

Then when we see the letter, what it looks as if -- does this help -- that the price error in your post Budget prices seems to relate to a change in the price following the Budget which they are telling you looks as if you have increased the price of their cigar too much? Is that right?

A. Well, if you say the Budget increase was 8p for cigars at that stage, I don't know how that would have reflected in terms of these particular products.

Q. Well, my point was this is by reference -- this point where the complaint was being made -- to the Budget. It's under the heading of "Budget March 2000".

A. Absolutely, yes, this is related to the Budget, yes.

Q. So the price error prima facie appears to be something that relates to pricing post the Budget; indeed, that's what it says?

A. Yes.

Q. So the discrepancy that they seem to be referring to is as a result of a change in price which may have disadvantaged Classic cigars in that they seem to have been put at too high a price and they are saying that the correct price is 2.88, which is the same as Hamlet?

THE CHAIRMAN: Where is the 2.88?

MR HOWARD: 2.88 is what it says, "Classic cigars should now be sold at 2.88, [tab 9] the same as Hamlet 5s."

A. Yes, I can confirm that my interpretation of the line was that Imperial were saying the Classic cigars should be sold at 2.88.

Q. If we actually look, just to pick up a couple of points, I want to ask some tedious points about these price files.
A. Sure.
Q. If you go to 10(a), what's rather interesting about this, bearing in mind this case is a competition case, if you look at Hamlet 5s, the line there, the Shell invoice cost price, 39.88, what's that? What does that mean, Shell invoice cost price?
A. From recollection, so at this time we would have been in the direct supply, so my understanding of that would be that that would be the cost that we would invoice to the retailers.
Q. What does that reflect, the costs that you have borne in buying them?
A. So the invoice cost price would have included what we called the back door price, the price of the product to the back door of the warehouse, and then if there had been any additional overheads to apply to that product for warehouse costing and then distribution to site.
THE CHAIRMAN: So that's the transfer price that we can --
A. That's the price that -- the invoice that the retailers receive would be charged for one outer of that product.
MR HOWARD: Right. So when you work out what the Chairman's called the transfer price, presumably that's done on

a standardised basis, so it doesn't make any difference whether it's an Imperial product or a Gallaher product, you take the cost that you are incurring and then presumably you add an element which reflects your warehousing, transport and overhead costs?
A. Yeah, I mean, certainly my recollection is that it would have been way too complex to apply different transfer elements, so it would have been a standard internally agreed cost.
Q. You were asked some questions by Mr Lasok as to whether the correct thing to compare with is Castella Classic 5 or Classic Small Cigars. Let's assume for the sake of argument it's Castella Classic 5. As I understand it, the Shell invoice cost, the transfer cost for those is less than for the Hamlet 5s; is that right?
A. Certainly in terms of the information in front of me, yes, that's correct.
Q. Equally, we should be doing the comparison with the Classic Small Cigars. I think to do a comparison you have to double the £19.63 so that you are comparing like with like and there the invoice cost would be £39.26, wouldn't it? That's simple maths, even I can do that.
A. Yes.
Q. So in all cases, in both the cases, whichever it is we should be doing the appropriate comparison with, the

Imperial brands are in fact cheaper than the Gallaher brands; correct?
A. Yes, correct.
Q. Now, we can see a similar exercise if you go to tab 11(a), seeing how a lower priced product seems to have fed through into a lower price.
The Hamlet 5s we see are 41.23 compared to the Castella Classic 5, 39.58, and Classic Small Cigars 19.63. If one doubled that, it would be less than the Hamlet.
So what it looks as if, is you, in setting your retail prices, have taken account of the lower cost price to you; is that right?
A. That would have been part of the evaluation, yes.
Q. Yes. So lower cost prices in these instances result in lower prices to the consumer?
A. That would be the case in the terms of these, yes.
Q. Interestingly on the same point -- no, a slightly different point but we have to look through these schedules. Mr Lasok took you to tab 32(a) and, as I understand him, what he was seeking to do when he took you to tab 32(a), which is a Shell price file in April, I think it says, he was seeking to compare that with the price requirements which are annexed to the contract which are correct as at July 2001. You can see that in

tab 27. Now, you don't need to turn it up.

The point that Mr Lasok was making to you is -- I think he was making two points to you. Just so we get them in our minds, his first point was that there was a coincidence between the differentials here and the differentials in the July 2001 document, in that those provide that there should be at least such and such differentials, and he says, well, you are complying with that, therefore he said it shows you must have been seeking to do this. That was one point.

The other is, because in fact he said the differentials reflected the precise amount without any difference, you must have been treating the differentials as fixed.

You do understand those two points?

A. I would be grateful if you could just clarify it again, because it's quite long.

Q. Okay. Perhaps I'll do it this way, rather than go back over that: as I understand your evidence in relation to this schedule, you say if it does correspond to the ITL requirements, for this particular month, you say that's a coincidence because I independently worked out my prices; is that right?

A. Yes, that's correct.

Q. So Dr Scott gave you the example, for instance, we saw, of Benson & Hedges Kingsize compared to Embassy, I think, No 1?

DR SCOTT: Embassy No 1 20, yes.

MR HOWARD: Embassy No 1, and in fact there is a 3p differential in the cost price, and so I think you said it's not particularly surprising, therefore, to find a 3p differential in the recommended retail price; correct?

A. Correct.

Q. What I would like to show you, then, is tab 34(a), which is another one of these price files. Having asked you to turn to it, rather than tediously going through it, can everybody just take it from me I will say what the information is, if I am wrong Mr Lasok in due course will say and therefore it will all have been a waste of time, but assume what I am saying is right.

If one compares -- in the agreement, the schedule provided that Embassy No 1, as compared to Benson & Hedges Kingsize, there should be at least a 3p difference. In fact, in this schedule, there was a 4p difference. I'll just go through a number of them, just so everybody can see. So that was a greater difference, but of course it complied because it had to be at least 3p.

MR LASOK: Can I interject to say of course this is after

the witness had left tobacco. It's not something that I cross-examined on, because he left in September and this is something that relates to the pricing from 1 October. That's Ms Parker's era.
MR HOWARD: Okay. Tell us, by 1 October, this is the file that was prepared on 1 October, would you have been involved in compiling this? Presumably it's compiled prior to that.
A. No, I would not have done.
Q. Okay, then I won't ask you, we will save that for Ms Parker.
Can I ask you: you were asked a lot of questions about what, from correspondence, we can glean that ITL understood about the change to the RBA structure.
In the light of that I would like you to go to tab 30, please. D19/30. This is a note in March 2001 of Imperial's. You wouldn't have seen this but I want you to tell me whether this is an accurate representation of what you were telling Imperial.
You see the paragraph that says "Background":
"Shell now operates about 1,200 sites following the takeover of Gulf at the end of 1997, 700 of which are company owned and all trade as Select. The remaining 500 are dealer sites over whom Shell have no control regarding the shop. Shell directly manage about 300

Select shops. The balance of the Select sites are run by self-employed agents who own the shop stock but are given strong guidance by Shell with regard prices, range, source of supply and display but he or she makes the final decision. The current agent agreement was introduced in the last 12 months and has given operators a high share of the profit generated on the site."

Stopping there for a moment, I think you told us you generally were responsible for briefing the suppliers with whom you dealt; would you have briefed Mr Culham?

A. Yes, I would have briefed Mr Culham.

THE CHAIRMAN: Do you remember briefing Mr Culham?

A. I remember that period of time when the briefing packs for the RBA agreement were made and my responsibility would have been to brief the three -- well, all of the suppliers that I was responsible for. So in that period I would have sat down with Mr Culham and briefed him.

MR SUMMERS: Would you have briefed each of the manufacturers separately?

A. Yes, I would have done.

MR HOWARD: So is what Mr Culham is writing internally there, is that an accurate portrayal of the position as you saw it?

A. Yes. I believe it is accurate.

Q. If you would turn to, we can just pick up, although these are notes from a later time, perhaps you could go to tab 51, I appreciate this is after you have gone, tab 51, D19/51 where we see on the right-hand side "Pricing". The way it's put is:

"Two tiers Shell retail price."

Second:

"The maximum price that can be charged at dealer's decision."

As I understand it, you say it is accurate in the sense that it's up to the dealer to decide whether he charges the Shell retail price or indeed below that, and insofar as there is a maximum price, he can charge anything in the range up to the maximum price?

A. I'm sorry?

DR SCOTT: I think you have sort of leapt on from Shell Select to Shell DOS, and I think here we are discussing the Shell Select. The words "dealer's decision" refer to Shell DOS.

MR HOWARD: I beg your pardon. Okay, then I'll leave that document. I think the other documents are all pretty similar.

So as I understand it, you briefed the suppliers, and what you told them the effect of the RBA was that the independent agents would then be the persons with the power to determine what the price was; is that right?

A. Yes, that's correct, I mean, the briefing document was broader than just around pricing, it was very much around how the business model was changing, the rationale behind it in terms of ensuring we protect the Shell brand, we deliver and offer to the customers that we believed we were targeting, or that we wanted to target, and as part of these arrangements the retailer on the site was now independent and in that process, the agreement was they had the financial responsibility for the stock on the site, but they had the decision in terms of what the prices were that they charged to the customer.

Our role as the central office was to provide what we called the core range, so advice on the core range and where that product was supplied from, so whether it was from our warehouse and then later we sold that, it was from Palmer & Harvey. We would identify what the cost price into the retailer, so the invoice cost to the retailer was, and we would manage it in such a way that each of the categories -- and we called them main groups -- would deliver a certain level of margin, if all of the products were retailed at that recommended retail price. We did not stipulate what the price was that they had to have on the retail shelf.

THE CHAIRMAN: There was a commission also payable, was there, from the retailer -- from the petrol station owner or the shop owner -- to Shell for each pack of cigarettes sold; is that right?

A. From my recollection, and I think the witness statement of David Moss explained this in more detail, but there were issues around managing VAT, and having -- setting up 600 or 650 operations to be VAT registered. So in order to overcome that, because I think there would have had to have been two actual points of sale --

THE CHAIRMAN: No, no, I am not talking about the flash sale thing, I am talking about: was there remuneration that passed from retailer to Shell from their sales, a proportion of their sales?

A. Yeah, there was a royalty then paid from those flash sales to Shell, so it was at that point -- and then the remnants was then paid back to the retailer. That was my understanding.

THE CHAIRMAN: But I thought Mr Moss' evidence was that it was based on the recommended retail price.

A. The margin was based on those recommended retails. So if a product was scanned through at main group margin 40, so cigarettes, the margin for that group, for the sake of argument was, say, 9 per cent. So products scanned through on that main group I believe would have been -- a margin of 9 per cent would have been earnt by the retailer. It's conceivable that if he charged less, then we would still get our 9 per cent and he would get less, but then he is doing that for customer reasons. If he charged more, we would still get our 9 per cent but he would get more.

DR SCOTT: This isn't a question for you, it's a question for counsel: the RBA doesn't actually reveal the royalties by category, and I can't recall whether we do actually have a document which tells us the answer to this, I can't recall seeing one.

MR LASOK: We have never been shown it.

DR SCOTT: Thank you.

MR SUMMERS: I have just one question for you: I can imagine that this presentation that you gave to the manufacturers, for you would have been a pretty big event, this was a major, major change in Shell's approach. How many people would have attended from a manufacturer? How deep down in terms of level did it go?

A. I only ever recall talking to the national account manager who I was dealing with, so in this instance it would have been Mr Culham. There were at later stages of the relationship, may have been reviews of the category and the business, which could have involved or would have involved Mr Culham and his line manager, or someone who was related to merchandising expertise or the legal expertise because of what was happening in terms of the legal environment. But as far as I recall, because this was a roll-out, yes it was a big event but equally there was a lot of attention from the retailers and the dealers at that time I think in some of the trade press that is reflected. So my recollection is that it was: we need to talk to the suppliers in a way that we are not making a big song and dance about this, we want to work together about how we deliver this. So there was no big forum and all the suppliers came together and so forth, it was very much myself and my account manager.

Now, if they then chose to ask for this to be communicated first-hand to other members of their team, then we would have arranged that because it was important that they understood how this was going to work, what the changes were, and that we got them at least to a level of understanding. They may not have been particularly comfortable with it because the message wasn't always what they wanted to hear.

MR SUMMERS: Did you receive a request to go and present to other members of their teams?

A. I don't recall that being the case, but then equally we would have been doing this over a period of time, and it is conceivable that we would have had year end business reviews that then would have had an element of: can you explain more about what's coming, how is it going and what does it look like.

MR SUMMERS: So you would have left the account manager with a presentation document which he would then have waterfalled, as it were, down to other members of the team?

A. I know that there was a sensitivity at that time about having documents available in the wider environment related to this, and because of the difficulties in terms of managing the retailer relationship and the changes that obviously were really impacting them, so as far as I can recall, it was a presentation, but we didn't leave that with them.

Now, later on in the period, so as we moved later into 2001 and there was more roll-out, it's quite possible that we left them -- we gave them some form of document. But I do recall there was a lot of sensitivity about how the message was given and how it could potentially be viewed in the outside word.

MR SUMMERS: And that would have included information about the control or otherwise that you would have over the new agents?

A. Absolutely, and that was, you know, part of the sensitivity.
MR SUMMERS: Thank you.
MR HOWARD: You were asked some questions about correspondence at tab 19 and 22 relating to a Richmond promotion, and it culminates in tab 24, if you would go to that. D19/24. If you go to the second page, you will see what Mr Culham is saying to you is:
"As you know, the correct price should be £3.55 which you agreed to and based on this price, the retro allowance would be paid."
Do you see that?
A. Yes, I do.
Q. So is this right: what had happened here, Imperial had a special promotion or tactical promotion on Richmond Kingsize whereby they were paying you a retro allowance or bonus in order to incentivise you to reduce, insofar as you could, the price of Richmond Kingsize in the Shell outlets?
A. Yes. I mean, that's my understanding, is there was work going on from a marketing perspective regarding this brand, to lower its price position to make it more competitive aware against whom they wanted to compete. Originally, the price would have been higher and our margin would have been based on that price.

THE CHAIRMAN: You don't need to give such a long answer, I think your answer was that, yes, that was my understanding.
MR HOWARD: Yes, but the point is, just to draw that out, you had a higher price and what Imperial have done is to say, "We will pay you this amount which will allow you to reduce the price down to £3.56 and maintain your margin"?
A. Yes, that's correct.
Q. Imperial's complaint in this correspondence was that they had paid to get the price down for the consumer to £3.56 I think, and what they were complaining about was --
THE CHAIRMAN: 55, I think.
MR HOWARD: £3.55, but their complaint was: I have paid money which I want to go through to the lower price to the consumer, and Shell, it's not getting through to the consumer. That was their complaint, wasn't it?
A. Yes, essentially. We weren't delivering what they were paying for.
Q. Their complaint was that the consumer was actually paying a higher price for its product than it expected, it having paid a sum of money to Shell in order to lower that price?
A. Yes.

Q. The trading agreements are at tabs 27 and 40. Firstly, you explained to us that you regarded this as, I think your words were, the first paragraph which says, talks about selling out prices, no worse than the relative RRP. You have told us this morning you regarded this as optional. Do you remember that?
A. Yes, that's correct.
Q. As I understand it, is this a fair summary: your understanding of this part of the agreement is that this was a relatively small payment in the context of what you were doing, but it was operating on Shell as an incentive to them that if they did perform in this way, then they would receive this relatively small sum?
A. Yes.
Q. Now, the incentive sum was, we can see, to set the price -- and I am not distinguishing at the moment between pre and post RBA because it would just be too tedious to do that, I think we all understood your evidence about that so I am not going into that -- but the incentive related to securing that the prices of their products were no worse than the relative RRP. By that, presumably, you understood that they would have no objection if you priced them at a greater differential than had been indicated by the differences between the RRPs?

A. That's my understanding, yes.
Q. Yes. You can turn over the page, where we see that Embassy No 1 was to be at least 3p less than the price of Benson & Hedges. Presumably it would have been obvious to you that Imperial would have been delighted and done a little dance if you had managed to price Embassy No 1 at 10p less than Benson & Hedges?
A. I can't say for what their reaction would be to us pricing below the requested difference, but I am sure they would have been happy from a competitive perspective.
Q. You don't need to speculate as to whether Mr Culham would have done a jig for you, but I think that will do.
DR SCOTT: You were concerned about your margins, won't you?
A. Absolutely, yes.
MR HOWARD: You were concerned about your margins, so you would decide how you were going to price in any event. My point to you was that as far as Imperial were concerned, if you chose to price their products relative to Gallaher, at greater differentials, they would have no objection whatsoever?
A. No, I don't believe they would have had an objection.
Q. No. Now, tell me this: we have this trading agreement here and then we have the later one at tab 40, I don't think any distinctions need to be drawn. As a result of

these trading agreements, when you were dealing with matters, did you regard yourself as in any way inhibited or restricted as to the price that you chose to recommend for Gallaher's products?
A. No, none whatsoever.
Q. We have seen that from time to time, Imperial offer promotional or tactical bonuses. We saw an example of that with Richmond; correct?
A. Yes.
Q. Did you understand that the purpose of Imperial offering promotional or tactical bonuses was to make their promoted product more attractive on price as compared to its competitor?
A. That was my understanding, yes.
Q. Would Imperial's purpose in paying such a bonus, namely to make its product more attractive as to price, be achieved if you also reduced the recommendation in respect of the competing Gallaher or BAT or Philip Morris product?
A. No, it wouldn't have been.
Q. So is this right: if you reduced the recommendation as to price of Imperial's product as a result of an Imperial price cut or promotion, did you understand that Imperial required or expected you to reduce the price of the competing Gallaher product?

A. No, I didn't have that expectation.
Q. Would it be fair -- well, that's fine.
Now, let's look at the other side of the coin. We know in this market that prices go up as a result of both Budget increases and manufacturer price increases; right?
A. Yes.
Q. They can also go up because a manufacturer has been running a promotion which he withdraws?
A. Yes.
Q. Bearing all of that in mind -- leave aside Budgets, because the Budget affects everybody across the board; correct?
A. Yes, correct.
Q. Now, a manufacturers' price increase, if one manufacturer, here Imperial, decides to announce a price increase, that is presumably a matter for it?
A. Yes, it was Imperial who would have informed us that they were increasing their prices.
Q. Now, as we have also seen from looking at tab 10(a) for instance, what we see is generally in Shell that higher cost prices, higher wholesale prices from a manufacturer, will result in higher selling prices, because you have to add on your margin?
A. Yes, that's correct.

Q. So if Imperial increases its wholesale price to you, either as a result of an MPI or terminating a special promotion whereby they are paying bonuses, that would obviously affect your margin on the relevant Imperial product; correct?
A. Yes, that's correct.
Q. So if Imperial chooses to increase its wholesale price, it is likely that, following that, or indeed probably inevitable, you would increase the Shell recommended price in respect of the Imperial products that were affected by the price increase?
A. Yes, unless there was a decision that we were going to reduce our margin, but the margins were very tight anyway, so I don't ever recall that being the case.
THE CHAIRMAN: What do you mean your margin?
A. Sorry, the Shell -- the available margin for Shell and its retailers.
THE CHAIRMAN: Yes, because if ITL puts up its price, then you can decide to put up your invoice cost at which you sell to the retailers.
A. (Witness nods).
THE CHAIRMAN: But -- and they have to pay that to you for those goods, whatever they decide to do in relation to their pricing.
A. Yes.

THE CHAIRMAN: So by putting up the invoice cost price, you have covered yourself, as it were, as far as the increase in what you have to pay ITL is.

A. Yes.

THE CHAIRMAN: Yes.

MR HOWARD: So what happens, just to follow through the Chairman's point, Imperial increases its wholesale price. You will in turn, where we have the RBA structure in place, increase your transfer price; correct, to reflect that?

A. The price to sell into the retailer, yes.

Q. And at the same time when you do that, you will increase the recommended price in order to allow the independent agent to still get the margin that you believe is appropriate, and you also may increase the maximum price; correct?

A. Yes, because the relationship between the category manager who is representing Shell and the independent retailer was based around helping them to earn that margin. So if an invoice price went up and we didn't increase the recommended retail price or -- and maximum price, then they were put in a position where they would have to sell at a lower margin.

THE CHAIRMAN: So was it the case that they always all went up in step by the same amount in pence?

A. Generally they would do, yes.

DR SCOTT: So, I mean, as we understand it, in the case of a Budget, everything happened at once, but in the case of other manufacturer price increases, they quite often didn't happen at the same time, so the situation was slightly more complicated in that, say it was an Imperial price increase, Imperial might want to wait and see what Gallaher were going to do and vice versa. So how did you handle that degree of uncertainty in terms of your price files?

A. You handled each price increase as it came, so if -- normally they would say that the price was effective on a certain date, you made the necessary calculations, what the new invoice cost to the retailer would be, what the recommended retail price to earn the category margin would be, and from that point or a date near that, you would recommend that -- well, you would say that "this is the new invoice cost price and the recommended retail price for that product is now this", that reflects that --

THE CHAIRMAN: Was that done just by adding through the pence amount so that if ITL's price went up by 3p, you would add 3p onto the invoice cost transfer price and 3p onto the recommended price and 3p onto the maximum price? Or was it more complicated than that?

A. In its simplistic form, yes, but of course the VAT had an impact in terms of where the resale price point came. So sometimes you would look at a product and if it was approaching a particularly sensitive price point, for example you were at say 3.96 and it's now going to go over £4, you might well say, "Well actually, our recommendation is to keep this at £3.99".

So there is a bit of margin shaving there, potentially. Equally you might try to balance that out by saying, okay, the product is already at £4.08, actually we could probably take this to £4.15 in order to make that balance.

So there was a little bit of that, but it was a complex process in terms of the amount of information coming through, so you tended to be fairly simplistic about it wherever you possibly could be.

DR SCOTT: And as we understand it, at these stages, you would also be in negotiations about pre-buying, because the additional margin you could make on pre-bought stock was, as we understand it, very significant compared to the amount of bonus you would get under the trading agreement?

A. Yeah, I can't recall the exact benefits that we had, but certainly up until the point where we had our own supply chain, that was an option during these periods of price increases.

DR SCOTT: And as we understand it, from the tabs to which we have been taken, those pre-buying agreements involved references to differentials being maintained; is that ...

A. That was one of the conditions that was attached to that, yes.

DR SCOTT: So that in rewriting your price file, bearing in mind the pre-buying and the pre-buying agreement, you would need to remember the agreements you had made; is that right?

A. There was certainly an element of that, but at a Budget time all the prices across the manufacturers would have gone up the same, so more often -- and given that the whole product range was being affected, and I think we are talking 100, 150 product lines that overnight would have to change, so it was pretty much a straight line: you are at that price, these two products are at that price, we are moving them up to that price and it's 5p on a packet of cigarettes, now it's 5p plus.

So it was pretty much a straight line. When it came to the manufacturers' price increases, they may not have happened at the same time, so it was really a case of, well, actually my priority here is the protection of the margin that Shell and its retailers can earn from this category. Then it was about the offer to the customer in terms of, if we remedy price, where does that fit in the price points. Then a distant third was very much, okay, so what do we say in the parities and differentials, because the prices aren't necessarily going up at the same time. That was something that you would manage after the event, if it had to be managed at all.

MR HOWARD: I want to break things down a little bit and firstly let's just pick up the general point which I had asked you, which I think led into a number of questions.

So if Imperial puts up its price, that results -- it's more complicated than just 3p feeding all the way through because of the tax implications and no doubt the margin calculations that have to be done. But in general terms, if Imperial puts up its wholesale price, then that is likely to lead to an increase in your recommended price to the agents; correct?

A. Yes, and to the maximum retail --

Q. And to the maximum. Of course, if they want to continue to earn their margins, then it's likely that they will in fact increase their selling price because otherwise they will have a loss in their margin?

A. Yes.

Q. Now, the decision that Shell makes to put up

Imperial's -- the price at which you sell to the agents and the price that you recommend to the agents, that's a Shell independent decision; correct?

A. Yes.

Q. Then the price at which the agents choose to sell the Imperial product in that event is an independent decision?

A. Yes.

Q. Now, I want to move on to another point but I want to come back to this point about pre-buying. The pre-buying -- perhaps we should turn back to the tabs -- that was something which of course occurred, I think you were saying, at a particular time when, prior to the RBA structure, I think, isn't that right?

A. It occurred through the period until our direct supply chain was sold and we no longer had a direct supply chain. From recollection that was some time in the middle of 2001.

Q. Right. Now, tab 13, there were two examples that Dr Scott was referring to, there is tab 13, I think, and tab 28. D19/13. If we just go to tab 13 first, so we can be clear what was happening, is this right: ITL are announcing an MPI. They have announced it, it's going to take effect on 21 August; correct?

A. Correct.

Q. We in fact know, for everybody's note, that Gallaher had an MPI on 8 August, which must have also been announced at some earlier date, because these things get announced some way in advance, don't they?
A. If you say so, yes.
Q. Is that not right from your experience; they inform you in the same way as Imperial was informing some three weeks in advance, that's generally what happens?
A. Yes, that would be what happened.
Q. So what Imperial is offering you is the opportunity to buy essentially some stock at the price that prevailed prior to the manufacturers' price increase; is that right?
A. That's correct, yes.
Q. And they are going to store it for you?
A. No, we would store it in our --
Q. Well, it says, "they will supply and store"?
A. Okay, sorry, yes, they did store and then we called it off, yes.
Q. That's the advantage of this arrangement, that you have stock at the previous price, and then Imperial are imposing conditions relating to the sale of that stock; correct?
A. Yes, that's correct.
Q. So it's not something that relates more generally, it's

to the sale of the specific stock that you are buying at a discounted price, effectively?
A. Yes.
Q. The terms are that essentially --
THE CHAIRMAN: Could you perhaps ask him this in a non-leading way?
MR HOWARD: Okay. I was trying to take it quickly.
Firstly, to just break it down, what is it you are getting? What is Shell getting?
A. So we have been informed of what the price increases will be, we had been given the opportunity to buy an amount of stock that would relate to a rate of sale that we had, so the amount of that, I don't recall what that meant in terms of the number of days or weeks of stock, but it would have been a sufficient amount that, once we came to the point of putting the prices up, on 21 August, the theory was that we should still have some of that pre-buy stock available so that it would be at an enhanced margin position for a limited period of time afterwards.
Q. Right. Then if we look at the conditions that are being set out, the first condition that ITL prices when changed will not do so before 21 August, is that something that's relating to ITL and when it's going to impose the MPI, or is it something that's relating to

what Shell is doing?

A. No -- my reading of that and my recollection is that they are providing advance warning of a manufacturers' price increase which they don't want to see in the market until 21 August.

Q. All right. Then:

"The current differentials against other manufacturers' products will be maintained, in addition the following will be implemented to reflect the change in relative RRPs."

We can see then:

"Richmond to be at least 5p below Mayfair, L&B and JPS families to be no more than 9p above Sovereign and no more than 16 above Mayfair."

There is no agreement that anybody has seen at this stage of a similar type to tab 27. Now, just help us about this: was there in fact an agreement which was similar to what we have at tab 27 that covered this period?

A. I am not aware that there was one.

Q. Right. Notwithstanding there wasn't any written document, was there any understanding to a similar effect, namely that Shell would be setting prices no worse than relative RRPs?

A. I am aware that there was anything agreed between

Imperial and Shell around the setting of prices at this stage.

THE CHAIRMAN: It must have been a bit mystifying then to have seen this letter? Perhaps you are getting to that.

DR SCOTT: If you read the first sentence of paragraph 2, that's the cause of the mystification.

A. Sure. No, I understand that, but I don't recall having taken over the category only a month or two months before --

DR SCOTT: With no handover, as we understand it.

A. With no handover then, I don't recall having seen anything and I may well have asked Ken the question around what does this mean, and he may well have informed me that it's about keeping the prices as they currently are in terms of the difference between different products.

MR HOWARD: Okay. Then tab 28, D19/28, which I think is the other example we have, that's a similar arrangement, is it?

A. Yes, in this instance it seems like this is a similar arrangement to the one in August.

Q. Yes. The second paragraph refers to the differentials being maintained and restored after the Gallaher MPI. Do you see that?

A. I do see that, yeah.

Q. Now, that takes me back to the point I was going to ask you about before: remember I was asking you about the effect of an Imperial price increase, and basically we went through that and you explained to us that if Imperial have a price increase that will result in the higher transfer price being fed through to the outlets and a higher recommended and maximum retail price?

A. Yes, that's correct.

Q. Right. Now, so if Imperial -- we just stop there for a moment -- puts up its price as a result of an MPI or terminating a promotion, presumably it runs the risk that the price of its products ultimately will go up?

A. Yes.

Q. Right. Now, tell us what the position is in relation to this: if you recommended -- there was an Imperial MPI and you as a result increased the transfer price for the Imperial products and you recommended an increase in the recommended price of the Imperial product, but there was no Gallaher or BAT or Philip Morris MPI, what, if anything, did you regard yourself as required to do concerning Gallaher's or Philip Morris' or BAT's products?

A. Nothing. I mean, this was an Imperial price increase, so the Imperial product would be increased. The other manufacturers' products would be maintained at the prices that they currently were.

DR SCOTT: Did that actually occur between Imperial and Gallaher during your tenure, which wasn't very long?

A. Certainly in terms of this item in number 28, there is a two week period between an Imperial increase and a Gallaher increase, so there would have been a period there where two products were -- or two sets of suppliers' products were at different prices.

DR SCOTT: So for that two weeks, how did you understand paragraph 2, which says "maintained/restored after the Gallaher MPI", what it suggests is you are being given a choice that you can either go through a two week period where things are different, or you can maintain the differentials right the way through, but by the time both MPIs are in place, you will be back to the differentials as they were. Is my understanding of that correct?

A. Yes, assuming that obviously Gallaher price increase was at the same level that the Imperial price increase was.

DR SCOTT: Now, am I right in thinking that during this period the price changes were in fact parallel so far as their RRPs were concerned?

A. I honestly can't comment whether they were. Gallaher may have taken a view in this particular instance to keep the cost price down a certain amount or to be more aggressive with their retail prices to generate more revenue. I don't know whether that was the case.

DR SCOTT: The question that's in my mind, assuming in fact there were parallel changes, goes back to what you were talking about earlier on about the difficult price points that might occur, so you talked about there being a 3.96 price, which wouldn't be too bad if it went to 3.99, but if it was going to go to 4.02, it might be worth popping a bit more on.

Now, if all --

A. Or suppressing that.

DR SCOTT: Or suppressing it. So you would be looking at that in relation to, say, the ITL price changes, in parallel, though a fortnight apart here, you have the Gallaher price changes, and presumably you would be looking in the same way at the Gallaher product prices?

A. Yes.

DR SCOTT: And in some cases you would be in a situation where the logic of the way in which you have explained your reasoning about the sensitivity of certain price points might result in the differentials drifting apart.

A. Possibly, yeah.

DR SCOTT: Where that was likely to happen, how would you approach 2? So if, for example, you had a situation in which there was a 3p differential and one was going from

3.99 to 4.02 and the other was going from 3.96 to 3.99, how would you handle that?

A. Ultimately I would have gone back to firstly about the delivery of the margin and where does that leave us, and it also depends to some extent on the volume driven by that product. So if it's a very high volume product, every penny makes a different sort of difference to a low volume product.

So that was also taken into account. So if I could generate more margin and there was a disparity in terms of maintaining the differential, then that's what I would do.

If I was then challenged on it, I would explain what my position was, but first and foremost it was about our margin, Shell and the retailers' delivery.

DR SCOTT: Thank you.

MR HOWARD: Is this a fair summary of the position: if Imperial increases its price, absent Gallaher -- sorry, let's take it in stages. It's a question for Imperial, as we already agreed, whether it wants to increase its prices; correct?

A. Sorry, the question is if Imperial wants to increase --

Q. Yes, it's a matter for Imperial's judgment whether it wants to --

A. Yes, absolutely.

Q. And equally it's a matter for Gallaher's judgment when and if it wants to increase its prices?

A. Yes.

Q. As Dr Scott I think was observing, very often in the market both Imperial and Gallaher introduced price increases at around the same time?

A. Yes.

Q. But neither of them obviously had any obligation as far as you were concerned to do that?

A. In terms of introducing them at the same time, no.

Q. You have already told us that if a manufacturer introduces a price increase, as I understand it, you say you look at that independently to consider what the effect of that price increase is on your prices?

A. Yes.

Q. Am I also correct in understanding that the prices that you have recommended, we probably need to get this straight, are not, as it were, set in stone so that, as things develop, you change the prices that are being recommended according to factors which are relevant to you, Shell, as per your margin; is that right?

A. Yes.

Q. That's why, if we look through the price files that we have, for instance -- we can just illustrate it, if you go back to tab 10(a) and 11(a), I think, you can see

10(a), we saw the price of Hamlet 5s at 2.95, and at 11(a) they were £3.05. Do you see that?

A. Yes, I do.

Q. Interestingly, the Shell invoice cost has gone up between 15 June and 21 July; do you see that?

A. Yes.

Q. Whereas the Castella Classic 5s that we were looking at, the invoice cost of those remained the same; right?

A. Yes.

Q. So that indicates, does it not, that here is an instance where one manufacturer has put up his prices in some way, or it's become more expensive for you to purchase, but the other manufacturer hasn't changed the price of his product?

A. That's correct.

Q. So --

THE CHAIRMAN: Well, do we know that? Just because the Shell invoice cost has gone up, does that necessarily mean that the manufacturer has put the price up?

MR HOWARD: Let's ask the witness: why would the Hamlet cost be going up between 15 June and 21 July? What would account for the increase in the price of Hamlet 5s?

A. It can only have been an increase in the cost price to ourselves. We weren't in the habit of making changes outside of price increases, because there is a lot of work attached to doing that, not only from ourselves centrally, but it then meant 600 sites, 650 sites had to do something, and there were many other things that we needed to do from a category and business perspective. So if we were driven to increase prices because cost price had gone up, then we made the change. But otherwise we left things very much alone.

Q. So from this, is it fair for us to infer that just because here the price of Gallaher's product is going up, that of itself does not provoke a price increase in Imperial's product?

A. No.

Q. And the same obviously would be true vice versa if Imperial puts up its price, Gallaher doesn't, it doesn't cause the price of Gallaher to go up?

A. Yeah, that's correct.

MR HOWARD: Thank you.

THE CHAIRMAN: I think we will take a short break now before we have re-examination. We will come back at five to 4.

(3.45 pm)

(A short break)

(3.55 pm)

Re-examination by MS ROSE

THE CHAIRMAN: Yes, Ms Rose.

MS ROSE: Mr Conrad, you were asked some questions about the degree of control that Shell had over the pricing before the RBA came into effect.

A. Yes.

Q. You were asked those questions with reference to the Richmond probation in 2000 to 2001; do you remember that?

A. Yes.

Q. If we just go back, if you could take up annex 19 and go to tab 22 -- D19/22

DR SCOTT: Sorry, Ms Rose, can we be a bit clearer?

MS ROSE: Yes.

DR SCOTT: He distinguished between the control that he as a category manager had and the control that Shell had. These were all Shell employees, as we understand it, so what was going on was --

MS ROSE: Shell head office --

DR SCOTT: Within the control -- so Shell head office.

MS ROSE: -- over the individual sites, yes.

DR SCOTT: But the prices were all being controlled by Shell employees, as we understand it.

MS ROSE: Yes, but the question is whether there is a single standard retail price that's operating at each retail outlet, that's the issue.

So if we go to tab 22, this is an email that you looked at earlier from Mr Culham to yourself of

3 November 2000.

He says:

"You agreed to alter the selling out price from 28 September in the first instance £3.56. The move to the correct price, £3.55, from 10 October, was confirmed by you at our meeting on 9 October. I have attached a summary of data collected between 16 and 31 October. As you can see, out of a total of 227 sites visited, just 138 were stocking Richmond Kingsize and of those 115 are charging over £3.55."

So doing the math, as they say, only 23 sites were actually charging £3.55; is that correct?

A. That's correct in terms of the details in this email.

Q. Again, just a matter of simple calculation, he visited a total of 227 sites, 23 were selling the product at the Imperial target price, that's 10 per cent compliance, isn't it?

A. Yes.

Q. Then if we go on to tab 24, this is now 18 days later, it's 20 November. Well, we start on 19 November. Again, Mr Culham to you:

"Can you please confirm the correct price at your sites, issue instruction to update the price tickets", and then he complains about his visit where it seems the price ticket was different from the price he was actually charged and both of those prices were above the £3.55?

A. Yes.

Q. You apologise and you say will reconfirm it to the sites.

A. Yes.

Q. Then we go on to the next tab, the internal ITL document. They say there are still reports of the Shell Select price being above £3.55, that's 27 November, and the following tab we see the same point being made by them again on 4 December?

A. Yes.

Q. Then turn on in the bundle to tab 29. D19/29. This is now another month later, this is 23 January 2001, and Mr Culham is saying:

"Since the price was lower in September 2000 I offered to pay a [confidential figure] per outer retro allowance subject to your selling out price not being above £3.55."

Then he tells us his current data, and we have a percentage that he still says are charging above the agreed price. So that's as between October and January, and we can still see a very substantial level of non-compliance; is that right?

A. That's correct, yes.

Q. Now, if we go on to the situation after the trading agreement was entered into, so that's January 2001, and that's the document at tab 27, D19/27 can I ask you to repeat the dangerous exercise and extract tab 27 again, and then turn to tab 32(a). You will recall that tab 32(a), this was an extract from the Shell price file dated 1 April 2001, and it was asserted by Mr Lasok, when he was cross-examining you, that he had checked every single product parity and differential on this sheet and that with the one exception of Dorchester and Richmond, he said they were all in line with the parities and differentials in the business plan investment document. Do you recall those questions being asked?
A. I do.
Q. Let's just look at the business plan investment, and in particular do you see the heading "Drum"?
A. On page 14, yes.
Q. Yes:

"All packings at least no more than the price of the same Amber Leaf and Cutters Choice packing."

Do you see that?
A. Yes.
Q. So that's suggesting at least parity between Drum and Cutters Choice; yes?

A. Yes.

Q. Of course Mr Lasok's case is that these are absolute differentials, not maximum differentials. You understand that that was the case that was being put to you?

A. Yes.

Q. Now, let's look at page 290. Do you see Cutters Choice, 12.5 grams, about eight lines from the bottom?

A. Yes.

Q. Do you see the prices, the recommended price, £2.31, and the maximum, £2.35?

A. Yes.

Q. Immediately below it, do you see Drum?

A. Yes.

Q. Do you see there the recommended price, £2.26, and the maximum, £2.30?

A. Yes.

Q. That's not parity, is it?

A. No.

Q. Is this the complete master price file for Shell from 1 April 2001?

A. It would appear not to be because there seems to be a third page missing.

Q. Just looking at it, we can see that it does not include a significant number of tobacco products, can't we?

A. Yes.
Q. Indeed, it doesn't include a significant number of the parity and differential pairings that are on the back of this agreement. For example, if you look again at the agreement --
THE CHAIRMAN: Is it really useful to take this witness through it? Is this a matter that can be sorted out in a note or something? I don't know whether this witness is saying he remembers setting these prices.
MS ROSE: Madam, it's simply the way it was dealt with in cross-examination. It was put by Mr Lasok in very forceful terms to this witness that it was an astonishing coincidence that every single price parity and differential in this price file was the same as in the agreement. Now, we have already seen --
THE CHAIRMAN: He stuck to his evidence that any coincidences were parity. I don't see the value of taking this witness through line by line with this point, if there is a point that you are going to make that actually they are not --
MS ROSE: Madam, let me hand up the relevant document. If I can hand up a copy of the complete price file. (Handed).
Madam, you will see that this is a complete copy of the Shell products master file list for RBA sites

1 April 2001, you see that on the first page?
THE CHAIRMAN: Yes.
MS ROSE: If you turn on in the document to page 22, you see the beginning of the tobacco category, starting with B&H Superkings 20. In fact, if you turn the page to page 24, there are some price pairings that don't appear on the extract that's in the bundle. Can I just identify three in particular? If you look at the business plan investment, you will see that it says, in the middle of the page, "Golden Virginia all packings at least no more than the price of the same Old Holborn packing". Do you see that?
THE CHAIRMAN: Yes.
MS ROSE: If you look at this price file on page 24, about eight lines down do you see "Golden Virginia, 12.5 grams"?
THE CHAIRMAN: Mm.
MS ROSE: With an RRP £2.35 and an MRP £2.39. About another eight lines down, do you see Old Holborn 12.5 grams?
THE CHAIRMAN: Yes.
MS ROSE: And the RRP, £2.38, and the MRP £2.42. So not at parity.
Then going back to the price requirements --
THE CHAIRMAN: Well, as I said, Ms Rose, this is a matter of submission. We have Mr Conrad in the witness box, are

there any questions as to what he can properly give evidence about that you want to ask him?

MS ROSE: Madam, all I am doing is exactly the same exercise as was done in cross-examination by Mr Lasok with this witness, and either the whole matter should be dealt with by submission or --

THE CHAIRMAN: No, the evidence he was being asked to give was as to whether he complied with the differentials, and he said he didn't, and that if there were parities and differentials, that it was a matter of coincidence, and my recollection is that he maintained that position, despite the points that were put to him which you now say were bad points.

Now, to then say they are bad points, is your evidence the same, of course it is going to be the same.

MS ROSE: Madam, can I just tell you that in fact there are three more pairings, so that there are a total of four. No, I beg your pardon, five, if you include the Richmond and Dorchester, which are not equivalent from this.

THE CHAIRMAN: Well, is there any question that you want to then ask Mr Conrad about his recollection of these matters that arises from that?

MS ROSE: Does that accord with your recollection of the way in which you would set the prices for these products?

A. Yes. I go back to what I said before. The margin was the key driver. Then it was about price point and then, a distant third, any parities and differentials that may be in place.

Q. Now, if we can come back, if you would like to put the contract back in at tab 27, it may be that this matter has already been clarified, but just in order to be clear.

If we come back to your first witness statement, paragraph 7.23, you explain at 7.23 that you were responsible for:

" ... ensuring that alterations to duty or increase in manufacturers' prices were reflected in Shell's price files [though] ... these changes did not result in lower margins ... [you were] requesting confirmation as to the effect of duty", when you sent the price files.

And then:

"ITL would then communicate whether Shell had accurately accounted for these changes in its price files, as was the case in document 9 of annex 19 ... where ITL highlighted an error in Shell's post Budget prices for Classic cigars and that Classic cigars should be priced the same as Hamlet 5s. My attention has been brought to Shell's price files dated 15 June ... and 21 July ... Although Shell appears to have priced in accordance with ITL's price recommendation of £2.88 for

Classic cigars, parity with Hamlet 5s was not maintained in the June and July price files where prices for Hamlet 5s were increased to £2.95 on 15 June and £3.05 on 21 July."

Just going back to tab 9, we see the original letter of 11 June, error in the post Budget prices, Classic cigars should now be sold at £2.88, the same as Hamlet 5s.

So there are two points being made there by ITL: one, Classic cigars should be £2.88; two, they should be the same as Hamlet 5s; yes?

A. Yes.

Q. If you then go to 10(a), there is some argument about whether the Classics in question are the Castella Classic 5 or the Classic Small Cigars. But we can see the Classic Small Cigars are at 2.88 which would have been in accordance with ITL's recommendation.

A. Yes.

Q. But are not at parity with Hamlet 5s?

A. That's true.

Q. On the other hand, in June, the Castella Classic 5 are at 2.95, which is not in accordance with ITL's recommendation of 2.88, but are in parity with Hamlet 5s. Do you see that?

A. I do.

Q. By contrast, in July, at 11(a), we see that at this date the Classic Small Cigars remain at 2.88 but are not at parity with Hamlet 5s, and the Castella Classic 5 are now at 2.95 and are also not at parity with Hamlet 5s?
A. That's correct.
Q. Does that lead you to draw any conclusion about whether or not you accepted the recommendation in the letter of 11 June 2000?
A. The recommendation was around Classic cigars being at 2.88, and the file indicates that product was placed at that price, Hamlet cigars were moved into a different price, as the invoice cost has increased.
THE CHAIRMAN: Well, are you now saying, then, that you do think that the Classic cigars referred to at tab 9 was the Classic Small Cigars 10 rather than the Castella Classic 5? Is that your evidence, that you recollect that that was what he was referring to?
A. I don't recall going back to June 2000, and specifically this point, but the evidence suggests that that was the product that I was working with in terms of the suggestion from Imperial.
DR SCOTT: We don't know when you received the letter of 11 June 2000, but 10(a) appears to be 15 June 2000, so that appears to be the price file following the letter. Do I have that ...

MS ROSE: That would appear to be so chronologically, yes.
DR SCOTT: It is confusing, I must say.
MS ROSE: The point is that whichever products you take, they clearly didn't adopt the ITL recommendation, it doesn't matter which of the products you take.
DR SCOTT: We see parity but not at 2.88.
MS ROSE: But we don't see parity in July?
DR SCOTT: That's right, absolutely.
MS ROSE: We don't see £2.88 or parity in July.
THE CHAIRMAN: But what he agreed to do we don't know or he doesn't remember beyond what's written in the letter.
MS ROSE: No, but madam, what we clearly see from the chronology is that the recommendation that's in the June letter is not implemented.
DR SCOTT: We had the question about the figure I am not allowed to mention of the Shell invoice cost, and as a matter of fact do we -- you probably don't know, but does OFT know whether there is a relevant Gallaher document?
MR LASOK: I am terribly sorry, I missed that.
DR SCOTT: The question is this: is there a relevant Gallaher document between 15 June 2000 and ...
MR LASOK: Not in the relevant Gallaher file, which is annex 9, because that starts off with a document dated to something like August or September 2001, which was

the first letter between Gallaher and Shell kicking off the negotiations for the Gallaher trading agreement, or at least it's the first one that we have. I am afraid at this stage I don't know whether in the interstices of the OFT's files somewhere there might be a document relating to an earlier period.
DR SCOTT: Yes. So basically, so far as we are concerned in this room, we don't know the answer?
MR LASOK: We know that there was parity later in the year between Hamlet and the Classic 5s that I was referring to.
MS ROSE: Now, just to be clear about the supply chain, in the period before the RBA, Shell purchased the tobacco products from the manufacturers; is that right?
A. For the period before the RBA, but also for a period, a short period, when the RBA was being --
Q. Let's take it in stages.
A. Yes.
Q. Before the RBA, Shell purchased tobacco products from the manufacturers?
A. Yes.
Q. And would then invoice the sites the invoice cost for those products?
A. Yes.
Q. Then what was the position in the transitional period?

A. So from recollection, we sold our warehouse and the distribution around about the middle of 2001, and there was a period where all sites received product from our warehouse, and then we actually I believe sold the warehousing to Palmer & Harvey, who we then had an agreement with to distribute to all of our sites, and that was then at the invoice price which they delivered.
Q. After you got rid of your own distribution network, from whom did the retailers buy tobacco products?
A. From Palmer & Harvey.
Q. So would you have been involved from that date in pre-buying tobacco products if there was a manufacturer price increase?
A. No. No.
Q. So that's why the pre-buy agreements that we see date from the period 2000 or early 2001; is that right?
A. That's correct, yes.
Q. So from around March/April 2001 onwards, there were no such agreements; is that correct?
A. As far as I recall we wouldn't have pre-bought stock once the transition from our distribution had been made to Palmer & Harvey.
MS ROSE: I have no further questions.
THE CHAIRMAN: Thank you very much, Mr Conrad, that's been very helpful, and we can release you from the witness

box now.

A. Thank you very much, madam.

THE CHAIRMAN: And thank you for reorganising your diary so you could stay this afternoon.

A. I am glad I could. Thank you.

(The witness withdrew)

Discussion re timetable

THE CHAIRMAN: So tomorrow morning we start with Mr Culham; is that right?

MR HOWARD: Yes, madam, that is right.

THE CHAIRMAN: It may be worthwhile counsel having a discussion about whether documents that have already been put to one witness by way of challenge to that witness's evidence need to be put to a second witness, if that second witness says roughly the same thing about that document, in order for that to be a sufficient challenge for the OFT's purposes, or whether there is any other agreement to which you can come which might have the advantage of shortening the cross-examination by reducing the number of documents that need to be put. I am not sure what convention you are currently working to, or what discussions have taken place, but I just mention that in case there is anything useful that can be arrived at.

Mr Thompson, you rise to your feet.

MR THOMPSON: I'm not in any way complaining, but simply that the Tribunal will be aware that my first day in the sun I think was supposed to be today, and I have witnesses who are present who thought they were going to be finished by Monday, and I am becoming increasingly concerned that they may not be started by Monday, and one in particular needs to be out of the country after Tuesday night, and so it's simply -- I did hear that it's possible a Shell witness may come back in on Monday, and I am getting a bit concerned about timetabling. I suspect I am speaking on behalf of Morrisons and Asda as well, because the further we go in the track, the more difficult it's becoming to know when our witnesses will actually be required.

THE CHAIRMAN: Well, you must discuss this with your colleagues, there is a limit to what the Tribunal can do to control matters other than to make the gentle hints that I think I have been making.

MR THOMPSON: In terms of expectation, it obviously makes a difference whether witnesses are interposed, as it were, in other retailers' slots, and without knowing what has or hasn't been approved, I am not sure whether that's a matter for counsel or a matter for the Tribunal to direct when witnesses who haven't finished will be brought back in or whether the Tribunal simply wants the parties to speak among themselves.

THE CHAIRMAN: Well, I think in the first instance the parties should speak amongst themselves. If there is a clash which you are unable to resolve, then you may need to bring it to us for us to consider, bearing in mind the structure of the hearing that we agreed way back at the first or second CMC, it was intended to ensure that the evidence came out in some logical fashion, so that the interposition of witnesses out of sequence should be avoided so far as that's possible to take into account people's immovable arrangements.

MR THOMPSON: I suppose the simplest point is that tomorrow all my witnesses were supposed to be available but it now seems to be unlikely that any of them will be required, so if they can be released, obviously they may wish to go home. I think the next stop is Mr Goodall, after Mr Culham and Mr Howard's opening.

MR LASOK: If I may be of some assistance, I think the plan was that we would have Mr Culham, that would finish off the Shell case, and then -- well, it finishes off the Shell case with the exception of Ms Parker returning on Monday for re-examination.

As I understand it, what was going to happen next after Mr Culham was that Mr Howard would do his mini opening on the Co-op case and then we would have

Mr Goodall. The thing about Mr Goodall is that his evidence consists in part of material that relates to specifically the Co-op because at one point he was the Co-op's NAM. But he also gives more general evidence and he was originally scheduled to have given the more general evidence after Mr Batty. So the plan is, as I understand it, at any rate, to deal with Mr Goodall in relation to both aspects of his evidence after Mr Howard's mini opening on the Co-op.

Now, realistically that means that in all likelihood tomorrow is going to be spent dealing with Mr Culham, the short Co-op opening and then Mr Goodall. I doubt very, very much whether we will be able to turn to any other witnesses concerned with the Co-op aspect of the case on Friday, it will just be Mr Goodall for the rest of the day. Obviously I certainly have taken on board what the Tribunal has said and I am well aware of the exigencies of the timetable, but I'll try and keep my cross-examination to the absolute minimum, but I don't think that I have been cross-examining more than was appropriate.

THE CHAIRMAN: Yes. That seems to be in all likelihood that we will not get to the Co-op witnesses tomorrow, and, as you may or may not know at the beginning of the proceedings this morning the Tribunal indicated that we did not want witnesses sitting in the Tribunal when the opening was given or when other witnesses were being cross-examined, so it would be better for your witnesses not to attend tomorrow. Is that helpful, Mr Thompson?

MR THOMPSON: I am grateful and I suspect that they may be too. I am very grateful, thank you.

MR HOWARD: I am just looking at the timetable and essentially I think we are, as we have been for a little while, about a day behind. What appears to be the case is that once we get to the Morrisons case, we seem to have quite a generous amount of time for the evidence, and similarly on the Safeway case, and then we seem to have a day on Safeway without any evidence at all, so I am not quite sure what's supposed to happen that day, Tuesday 18 October, if Mr Lasok is looking at it. There doesn't seem to be any factual evidence being called that day.

THE CHAIRMAN: Why don't you discuss it amongst yourselves, if there is a revised timetable that could usefully be provided to the witnesses so they can rearrange their engagements so far as possible, then that would be helpful.

So tomorrow, what time are we starting? Shall we meet at 10 tomorrow in order to have a better chance of getting through Mr Culham and the Co-op opening and

Mr Goodall?

MR HOWARD: It's entirely a matter for the Tribunal.

THE CHAIRMAN: Well, we do have to finish very promptly tomorrow afternoon.

MR HOWARD: Yes, that would certainly be welcome on a Friday.

THE CHAIRMAN: Yes. If we could finish at 4 tomorrow afternoon, that would be good.

MR HOWARD: It certainly won't meet any resistance from this side.

THE CHAIRMAN: Well, ever the optimist, let's start at 10 tomorrow morning and hope we can make good progress.

MS ROSE: Madam, I should say I won't be here tomorrow but Mr Kennelly will be, but I wish you well in your fast.

THE CHAIRMAN: Thank you.

(4.35 pm)

(The court adjourned until 10.00 am on

Friday, 7 October 2011)

INDEX